further oversight by the investment adviser, can undermine the adviser's provision of services and compliance with the Federal securities laws, and can directly harm clients." *Id*. at 13-14.

SEC/SRO UPDATE: SEC BRINGS ENFORCEMENT ACTION FOR UNDISCLOSED CEO PERKS; DOJ AND SEC CHARGE EXECUTIVE WITH INSIDER TRADING AND MISUSE OF 10b5-1 TRADING PLAN; SEC PROPOSES CHANGES TO REGULATION S-P TO ENHANCE PROTECTION OF CUSTOMER INFORMATION

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SEC Brings Enforcement Action for Undisclosed CEO Perks

On March 2, 2023, the SEC announced that it had settled charges against transportation supply company The Greenbrier Companies Inc. and its founder and former CEO William Furman for failing to disclose perks provided to Furman and other executives of the company and certain related party transactions involving Furman.[1] The company agreed to pay $1 million, and Furman agreed to pay $100,000, in civil penalties to settle the charges.

According to the SEC's orders, in Greenbrier's proxy statements from 2017 to 2020, it failed to disclose approximately $179,000 in perks to Furman for travel-related expenses for his spouse and for personal security, and approximately $142,000 in similar perks for other company executives.[2] In addition, Furman owned a private airplane, which he leased to a management company, which in turn chartered the plane to Greenbrier for business travel. The existence of this arrangement was disclosed in Greenbrier's proxy statement, as was the fact that Greenbrier paid the management company $3 million to charter the plane over the relevant period. However, the SEC alleged that this disclosure was inadequate in that it failed to include the fact that Furman received $1.6 million of the $3 million total pursuant to his arrangement with the management company.

The SEC also alleged that Furman provided incorrect information about his perks and the airplane to Greenbrier. Like most public companies, Greenbrier provided its directors and officers with a questionnaire to elicit information about those persons it was required to include in its proxy statements and other public filings. The questionnaire included questions about perks and related party transactions, but Furman did not provide any information about his spousal travel or security perks, and, in response to the related party question, merely referred to the "Furman aircraft."

This action is another example of the SEC's current aggressive enforcement posture. In particular, while the related party transaction in disclosure Greenbrier's proxy statements failed to include the share of the $3 million aircraft payments that Furman received personally, the materiality of this omission is debatable in light of the fact that it would have been clear to a reader that Furman had a personal interest in the transactions and had received some portion of those payments. Further, Furman's disclosure about the arrangement in his questionnaire, while brief, would be considered by most to be sufficient to raise the issue for analysis by the company's reporting personnel. In light of the current enforcement environment, public companies and their executives would be wise to exercise increased vigilance with respect to disclosures regarding perks and related party transactions.

DOJ and SEC Charge Executive With Insider Trading and Misuse of 10b5-1 Trading Plan

On March 1, 2023, the DOJ and the SEC announced insider trading charges against Terren Peizer, the executive chairman of healthcare company Ontrak Inc.[3] The action is noteworthy in that it represents the first charges brought by either agency for insider trading where the trades in question were purportedly effected pursuant to a trading plan under Rule 10b5-1. That rule provides that an insider may trade in a company's stock even while in possession of material non-public information about the company if the trade is made pursuant to a plan that satisfies the requirements of the rule. In particular, a plan under the rule must have been adopted at a time when the trading person was not in possession of material non-public information. The SEC has long had concerns that the conditions imposed by the rule are not sufficiently strict, and has recently adopted amendments to the rule that impose greater restrictions on the use of 10b5-1 plans.[4] This case illustrates the SEC's concerns about plans under the rule as it existed prior to the amendments.

According to the SEC's complaint, Ontrak was heavily dependent on four major customers. When the company disclosed in March 2021 that one of those customers was terminating its contract with the company, the company's stock fell 46% in a single day, causing the value of Peizer's position in Ontrak stock to decrease by over $265 million.[5] The company planned to make up for the loss by growing its revenues from one of its remaining major customers, "Customer A" (identified in the DOJ indictment as Cigna).[6] However, Peizer learned late in the same month that Customer A was considering terminating its contract as well. Peizer established a 10b5-1 trading plan in early May [2021], a time when he was in frequent communication with Ontrak's CEO about the uncertain status of the relationship with Customer A. He established the plan with a broker that did not require a 10b5-1 plan to have a "cooling-off" period—*i.e.*, a minimum period between establishment of the plan and the first trade under the plan—after first contacting a broker that did require a cooling-off period.

Sales began under the plan on May 11, one day after it was established, and sales under the plan from that date until July 20 totaled approximately $19 million. On May 18, Customer A notified Ontrak of its intention to terminate its contract. In August, Peizer established a second 10b5-1 plan and trading under that plan also began immediately afterwards. Later that month, Ontrak disclosed that Customer A had formally terminated its contract, leading to a 44% fall in the trading price of Ontrak's stock on the day of the announcement.

According to the complaint, Peizer was in possession of material non-public information about Customer A when he established both of his 10b5-1 plans, and the plans were therefore ineffective in protecting him from insider trading liability. In the accompanying press release, SEC Chair Gary Gensler stated "[w]e allege that Mr. Peizer violated Rule 10b5-1 as it has existed for two decades by establishing and executing trading plans while aware of non-public information. Today's action comes the week that updated amendments to Rule 10b5-1 become effective. These reforms to Rule 10b5-1 will further help prevent unlawful trading by executives on the basis of non-public information and help build greater confidence in the market." Under current Rule 10b5-1, a 10b5-1 plan adopted by an officer or director must have a cooling-off period of at least 90 days. As Gensler's statement indicates, the SEC believes that cases like this one vindicate its decision to impose additional restrictions on the use of 10b5-1 plans.

SEC Proposes Changes to Regulation S-P to Enhance Protection of Customer Information

On March 15, 2023, the SEC proposed amendments to Regulation S-P that would require broker-dealers, investment companies, registered investment advisers, and transfer agents (collectively, "covered institutions") to provide notice to individuals affected by certain kinds of data breached that may put them at risk for identity theft or other harm.[7]

Regulation S-P, adopted in 2000, includes a "safeguards rule" that requires brokers, dealers, investment companies, and RIAs registered with the SEC to adopt written policies and procedures that address administra-

tive, technical, and physical safeguards for the protection of customer records and information.[8] Transfer agents are not covered by the safeguards rule, but transfer agents registered with the SEC are covered by a "disposal rule" under Regulation S-P, which requires proper disposal of records about an individual, whether in paper, electronic, or other form, that is a consumer report or is derived from a consumer report.[9] While the safeguards rule currently addresses protecting customer information, it does not require notification to affected individuals when a data breach occurs.[10]

The proposed amendments would require covered institutions to adopt reasonably designed incident response programs that would include policies and procedures for the assessment, control and containment, and customer notification.[11] Subject to limited exceptions, the customer notification component would require covered institutions to notify individuals in the event their sensitive customer information was, or is reasonably likely to have been, accessed or used without authorization.[12] Such notification would be required to be provided to an affected individual as soon as practicable, but within 30 days of the covered institution becoming aware that unauthorized access or use of a customer's information occurred or is reasonably likely to have occurred.[13]

Noting that transfer agents also obtain, share, and maintain personal information of securityholders that hold securities in registered form, the proposed amendments would extend the safeguards rule to cover transfer agents.[14] Both the safeguards rule and the disposal rules would also be extended under the proposed amendments to apply to customer information that a covered institution receives from other financial institutions.[15]

Comments on the proposed amendments are due 60 days after the date of publication in the Federal Register.

ENDNOTES:

[1]*See* https://www.sec.gov/news/press-release/2023-43.

[2]*See* https://www.sec.gov/litigation/admin/2023/33-11162.pdf and https://www.sec.gov/litigation/admin/2023/33-11161.pdf.

[3]*See* https://www.sec.gov/news/press-release/2023-42.

[4]*See* https://www.sec.gov/rules/final/2022/33-11138.pdf.

[5]*See* https://www.sec.gov/litigation/complaints/2023/comp-pr2023-42.pdf.

[6]*See* https://www.justice.gov/opa/press-release/file/1570711/download.

[7]*See* https://www.sec.gov/news/press-release/2023-51.

[8]*See* 17 CFR 248.30(a).

[9]*See* 17 CFR 248.30(b); and https://www.sec.gov/rules/proposed/2023/34-97141.pdf.

[10]*See* https://www.sec.gov/rules/proposed/2023/34-97141.pdf.

[11]*See* https://www.sec.gov/rules/proposed/2023/34-97141.pdf.

[12]*See* https://www.sec.gov/rules/proposed/2023/34-97141.pdf.

[13]*See* https://www.sec.gov/news/press-release/2023-51.

[14]*See* https://www.sec.gov/rules/proposed/2023/34-97141.pdf.

[15]*See* https://www.sec.gov/rules/proposed/2023/34-97141.pdf.