



Equity Gifts Under the Microscope

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Executive Summary

- Bona fide gifts of equity securities by Exchange Act (Section 16) reporting persons are now required to be publicly reported no more than two business days after the gift.
- In making the change, the U.S. Securities and Exchange Commission (SEC) stated a desire to evaluate the context in which such gifts are made and noted that certain gifts may raise the same concerns as more common forms of insider trading.
- Given SEC Chair Gary Gensler's statement that charitable gifts of securities are subject to insider trading laws, we expect company insiders to focus more carefully on the timing of any such gifts and companies to add/refine restrictions around gifting in their insider trading policies.
- It may become common practice for donors to make gifts of securities during an open trading window and when the donor is comfortable, they do not have material, non-public information (MNPI).

Context and Applicability

Gifting securities may be part of an estate planning strategy for executives. Their estate plan may call for gifting equity to a trust, family members, charities or their own charitable foundation. We frequently see such gifts made in the last few weeks of the year, as part of year-end tax planning. In 2022, Section 16 reporting persons made over 4,500 gifts of stock, valued at more than \$32.5 billion. While gifts were made throughout the year, over 21% of those gifts were made during December.¹

Notes:

¹ Data represents SEC Form 4 filings reflecting gift dispositions, with a transaction date in 2022. Used with permission from The Washington Service, 301-913-5100, www.washingtonservice.com.

Changes to Gift Reporting and Comments by the SEC

Executives that have in the past made last-minute gifts of securities in December intending to reap benefits for the current tax year might get an unexpected surprise in the new year – public scrutiny. Last year, the SEC adopted rule changes relating to insider trading arrangements and related disclosures² which included significant changes to Rule 10b5-1 as well as changes to reporting requirements for gifts of equity securities by Section 16 reporting persons. While summaries of the changes relating to Rule 10b5-1 abound, we have seen much less reporting of the remarks by the SEC that compare gifts to sales of stock and that may signal a future area of regulatory focus.

The swath of changes to insider trading rules were headlined by new requirements under Rule 10b5-1 (a rule that provides for an affirmative defense to a claim of insider trading where a plan to sell securities was entered into in accordance with the conditions of the rule) but also included enhancements to reporting and disclosure requirements for both Section 16 reporting persons and issuers. With an eye toward increasing transparency of insider transactions, the SEC introduced new disclosure requirements for 10b5-1 plans, company policies around insider transactions, and an accelerated timeframe for reporting bona fide gifts by Section 16 reporting persons.

In adopting the amendments relating to gifting, the SEC cited a study published in the Duke Law Journal³, which investigated “problematic practices” around making gifts of securities. The study found that insiders’ charitable gifts were “unusually well timed” and suggested that executives may have possessed MNPI at the time or backdated of the gifts. As a result of the changes,

Section 16 reporting persons are now required to report bona fide gifts of equity on a Form 4, due no more than two business days after the gift. Previously, gifts could be reported as late as 45 days after the fiscal year end. According to the SEC, this acceleration in reporting is intended to help investors, other market participants, and the SEC “better evaluate the actions of these Section 16 reporting persons and the context in which equity gifts are being made.”⁴

	PREVIOUS REQUIREMENT	NEW REQUIREMENT
Form Required	Form 5	Form 4
Due Date	45 days after fiscal year end	2nd business day after gift

The SEC also disagreed with certain concerns raised by public commenters, saying that a gift followed closely by a sale “may raise the same policy concerns as more common forms of insider trading” and that “a gift made with the knowledge that the donee will soon sell can be seen as in effect a sale for cash followed by gift of the cash.”⁵

Given these recent rule changes and SEC Chair Gary Gensler’s statement that charitable gifts of securities are subject to insider trading laws, we expect company insiders to focus more carefully on the timing of any such gifts. In our experience, companies will close their trading windows for the last two weeks or more of each fiscal quarter, given the potential for exposure to MNPI at that time. We expect insiders whose trading windows are closed for part or all of December to consider gifting earlier, in an open window.

We also expect issuers to take action around their own policies. All SEC registrants will be required to attach a copy of their insider trading policies and procedures to their 10-K/20-F starting in 2024 or 2025, depending on the fiscal year of the company.⁶ If a registrant has not adopted such policies and procedures, it must explain why it has not done so. In our experience, while most companies have these policies, many do not include restrictions on when gifts may be made. Since the stated goal of this new requirement is to allow investors to “evaluate the extent to

Notes:

² Securities and Exchange Commission, Release Nos. 33-11138, 34-96492 (“SEC Adopting Release”).

³ S. Burcu Avci et al., Insider Giving, 71 Duke L.J. 619–700 (2021).

⁴ SEC Adopting Release, page 80391.

⁵ SEC Adopting Release, page 80392.

⁶ SEC Adopting Release, part II.B.2

which those policies and procedures protect investors from the misuse of [MNPI],”⁷ we expect companies will review and revise their policies to attempt to meet investor expectations in a number of areas, including gifts.

The Effect on Estate and Philanthropy Vehicles

As an estate planning matter, gifts of stock may allow an executive to transfer wealth without drawing on their cash. While such transfers can be subject to federal gift or estate taxes, there are annual or lifetime gifting exemptions that may be available to the gift maker to reduce or eliminate tax consequences. The gifted stock could be sold immediately after receipt or at a time of the executive’s choosing, depending on who is receiving the gift (e.g. an individual vs a trust).

Some trust and estate strategies may allow for reduction or elimination of federal gift and estate taxes when transferring property to family members. For instance, transferring shares to a properly drafted Grantor Retained Annuity Trust (GRAT) can, under certain circumstances, reduce potential transfer tax liability entirely. Going forward, sales of shares in these GRATs should be carefully considered in light of the remarks by SEC Chair Gary Gensler.

Spousal Lifetime Access Trusts (SLATs), a type of grantor trust, offer an opportunity to take advantage of the federal gift and estate tax exemption by structuring gifts between spouses. Sales by family members, going forward, may raise the same concerns as direct sales by the executive.

Gifts for philanthropic purposes could also receive scrutiny. Donations of stock with a low-cost basis, e.g., those acquired early in the company’s life when its valuation was low, have historically offered the donor income tax deductions that may be used to offset gains in other areas. While direct donations of stock to a charity or a Donor Advised Fund (DAF) are popular, some executives also set up private foundations, charitable trusts, or contribute to other long-term vehicles in order to support their favorite causes and leave a philanthropic legacy.

A charity or a DAF generally does not hold shares of donated stock. Rather, shares are generally sold and proceeds are applied to their efforts as soon as possible. An executive may be able to control the timing of sales for donations to a Charitable Remainder Trust or Charitable Lead Trust, if they serve as trustee. This would also be true if they control their own private foundation, although this may also be considered self-dealing and result in taxes or penalties. In all cases, the grantor should be cognizant of the new rules. Charitable trusts and private foundations typically take significant time to set up, and executives should seek the help of legal and tax advisors when considering these vehicles or when choosing an appropriate trust and estate strategy.

Next Steps & Considerations

It is uncertain whether the SEC will make gifts of securities an area of investigation or enforcement. However, the SEC’s commentary and Chair Gary Gensler’s statements underscore the need to consider the timing of these gifts, in particular if the donor knows or has reason to believe that the gifted shares may be sold prior to the disclosure of any MNPI the donor may have had at the time of the gift. Executives should therefore consider making gifts at a time when they would be allowed to sell – during an open trading window when they have no MNPI.

Notes:

⁷ SEC Adopting Release, page 80384.

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