

**ABSTRACT.** For more than thirty years, one of the most prevalent strategies for insider trading has gone undetected and unaddressed. This Article uncovers the techniques by which executives and directors sell overvalued stock worth more than \$100 billion per year, shifting losses to ordinary investors. The basic idea is that insiders conceal their suspicious trades by publicly reporting them (as they are required to do) in ways that confuse or discourage investigators. We develop a taxonomy of concealment strategies, complete with suggestive examples. We then empirically test our taxonomy using a database of essentially all stock trades since 1992. We find that insiders who trade using the subterfuges we describe outperform the market by up to 20% on average. Worse yet, we find evidence that this simple subterfuge works. Essentially no one has ever been prosecuted for undertaking one of these suspicious trades. Nor do journalists or scholars seem to appreciate them. Accordingly, we call for scholars and prosecutors to cast a wider net in their studies and market surveillance, then discuss implications for the design of insider-trading reporting requirements and related legal rules.

## **INSIDER TRADING BY OTHER MEANS**

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*INSIDER TRADING BY OTHER MEANS*

Introduction ..... 2

I. Insider Trading ..... 6

II. Insider Trading Reports ..... 9

    A. Reporting Obligations ..... 10

    B. “Other” Opportunism ..... 18

    C. Lack of Scrutiny ..... 20

III. Insider Trading by “Other” Means ..... 22

    A. Miscoding ..... 23

    B. Transferring or Distributing Stock to Investors ..... 35

    C. Transactions with the Corporation ..... 39

IV. Empirical Results ..... 41

    A. Methodology ..... 42

    B. Empirical Findings ..... 46

V. Implications ..... 60

    A. Scholarship ..... 60

    B. Scrutiny ..... 62

    C. Systemization ..... 63

    D. Scope ..... 64

Conclusion ..... 65

## Introduction

In December 2000, Enron was the world’s seventh largest company. Within a year, the stock was worthless. In that intervening year, Enron directors and officers sold \$50 million worth of shares to outside investors who didn’t know about any problems. Like all stock-trades by insiders, these transactions were publicly reported. However, no Enron insider was ever prosecuted for these sales, even though they were almost certainly illegal insider trading.

To be sure, Enron’s leadership was prosecuted for many other violations, including other acts of insider trading. But *these* \$50 million transactions were never mentioned in any civil complaint

or criminal indictment.<sup>1</sup> Nor did journalists report on them.<sup>2</sup> This omission is curious, since these insider trades were visible in public filings – the very public filings that prosecutors and journalists used to successfully identify many other insider trades.

How were millions of dollars of insider trades hidden in plain sight, ignored by prosecutors and journalists alike? The simple answer is that securities law permits insiders to report trades in ways that investigators are likely to misunderstand or overlook.<sup>3</sup> If the public transaction report is confusing, prosecutors and journalist may not bother scrutinizing them. With their trades obscured, officers and directors needn't obey insider trading law.<sup>4</sup>

Should we be worried that insiders often violate federal law in plain sight? Only if three things are true. First, there would need to be some easy way for insiders to apparently satisfy their public reporting obligation, which nevertheless conceals the true nature of their trade. Second, this

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<sup>1</sup> See, e.g., Complaint ¶ 36, *Newby v. Enron Corp.*, No. 4:01-CV-03624 (S.D. Tex. filed Oct. 22, 2001) (accusing Enron CEO Kenneth Lay of insider trading 400,000 shares of Enron stock). The complaint fails to note an additional 264,382 shares Lay sold just a few days before the first one the complaint cites. *Enron Corp.*, Statement of Changes in Beneficial Ownership (Form 4) (Dec. 18, 2000). At the time, those shares were worth \$79.56 each, or about \$21 million. The complaint ultimately alleges \$100 million in insider trading. First Amended Complaint and Demand for Jury Trial at 40, *Newby v. Enron Corp.*, No. 4:01-CV-03624 (S.D. Tex. filed Apr. 1, 2002). So, this omission amounted to 20% of the allegation. The SEC's complaint against Lay likewise omits mention of this trade. Second Amended Complaint, *SEC v. Lay*, No. H-04-0284 (S.D. Tex. filed Jul. 8, 2004), <https://www.sec.gov/litigation/complaints/comp18776.pdf>.

<sup>2</sup> Mitchell Pacelle & Cassell Bryan-Low, *Belfer Family Is Big Loser in Collapse of Enron Stock*, WALL ST. J. (Dec. 5, 2001, 12:01 AM), <https://www.wsj.com/articles/SB1007504552303214600> (December 5 article reporting that Ruben had sold 148,902 shares). The trades discussed in this first paragraph here numbered 295,942. *Enron Corp.*, Statement of Changes in Beneficial Ownership (Form 4) (Dec. 20, 2000); *Enron Corp.*, Statement of Changes in Beneficial Ownership (Form 4) (Dec. 22, 2000); *Enron Corp.*, Statement of Changes in Beneficial Ownership (Form 4) (Jan. 8, 2001); *Enron Corp.*, Statement of Changes in Beneficial Ownership (Form 4) (Sep. 5, 2001); *Enron Corp.*, Statement of Changes in Beneficial Ownership (Form 4) (Nov. 1, 2001); *Enron Corp.*, Statement of Changes in Beneficial Ownership (Form 4) (Nov. 9, 2001); *Enron Corp.*, Statement of Changes in Beneficial Ownership (Form 4) (Nov. 30, 2001). The WSJ missed two thirds of Ruben's sales in the relevant period. The New York Times missed these transactions too. Leslie Wayne, *ENRON'S COLLAPSE; Before Debacle, Enron Insiders Cashed in \$1.1 Billion in Shares*, N.Y. TIMES (Jan. 13, 2002), <https://www.nytimes.com/2002/01/13/business/enron-s-collapse-before-debacle-enron-insiders-cashed-in-1.1-billion-in-shares.html>. It reported that "between early 1999 and July 2001," Enron CEO Kenneth Lay sold "sold as many as 100,000 shares" at a time. The Times appears to have missed his December 18, 2000, sale of 264,382 shares, worth \$21 million.

<sup>3</sup> This Article will use the word "investigator" to refer to anyone who has an interest in detecting insider trading. Thus, the term includes the Department of Justice and Securities and Exchange Commission, but also journalists, plaintiffs' lawyers, and scholars.

<sup>4</sup> PLATO, REPUBLIC, 360b-d ("If you could imagine any one obtaining this power of becoming invisible, and never doing any wrong or touching what was another's, he would be thought by the lookers-on to be a most wretched idiot").

concealment would need to actually fool investigators. Third, lots of insiders would need to have realized this strategy and put it to work. Then we would have a problem. Unfortunately, this Article demonstrates all three points are true, and so there is a large loophole in our insider trading enforcement system. Indeed, this loophole is so large it may represent the predominant form of insider trading.

Our first contribution is to catalogue the techniques by which insiders minimize the legibility of their suspicious trades. We call these techniques, “insider trading by ‘other’ means.”<sup>5</sup> This name refers to a component of many strategies. When insiders report their transactions, they are required to characterize the nature of the transaction using one of twenty transaction codes. Most trades fit into tidy boxes such as purchase (P) and sale (S). Insiders who disclose a “P” at a low price followed by an “S” at a high price will face scrutiny, because they appear to have purchased and then sold at a profit.

Traders who want to avoid scrutiny may prefer to dispose of their shares under code “J.” That designation is reserved for transactions that fit into none of the predetermined templates. Its meaning is “other.” Hence insider trading by “other” means. This Article explains how insiders report ordinary sales under a fig leaf of “other.” We identify and explain seven distinct techniques and, for each one, we provide suggestive examples drawn from insider filings from insiders at WorldCom, Peloton, Nikola and others.<sup>6</sup> In each of these cases, insiders disposed of vast quantities of corporate stock at princely prices, shortly before the company disclosed information material to its demise. And in each case, the insiders covered their sale under the label of “other.”

Second, we show that obfuscation succeeds. We look for signs that prosecutors, civil plaintiffs, journalists, or scholars are aware that some J-coded transactions may be illegal insider trading. Unfortunately, we find the opposite. Despite being a potential proxy for suspicious trading, J-coded transactions are mentioned in essentially no criminal indictments, civil complaints, news

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<sup>5</sup> In part, this label alludes to the protean quality of insider trading, where substitutes for insider trading exist and may enjoy different legal status. See Ian Ayres & Joe Bankman, *Substitutes for Insider Trading*, 54 STAN. L. REV. 235 (2001). Of course, the “by other means” idiom is a reference to Clausewitz. CARL VON CLAUSEWITZ, ON WAR (Michael Howard & Peter Paret trans., Princeton University Press 1984) (“War is a mere continuation of policy by other means.”).

<sup>6</sup> While suspicious, we acknowledge that any of the examples might be benign and lawful. These examples are meant to be illustrative rather than conclusory. Fortunately, our case does not rest on innuendo and anecdote.

articles, or scholarly papers.<sup>7</sup> To the contrary, many observers actively avoid considering J-coded transactions.<sup>8</sup> Insiders would be right to think that it is safe to insider trade by “other” means.

Third, we demonstrate that insiders have learned the forgoing lessons, such that a large volume of suspicious trading is now concealed as we have described. We conduct an empirical analysis of essentially all publicly reported trades. We find that the trades whose filings fit the patterns described above substantially outperform the market, suggesting that insiders opt to obfuscate their can’t-lose bets. The effect becomes stronger when we look at proxies for strategic use of the J code, such as a transaction that appears to lack any justification for invoking the J code. The scale of this practice is huge, with more than \$1.5 trillion transacted under “other” during our sample period.

The theoretical and normative implications of our findings are profound.

Theoretically, it appears that scholars know less about insider trading than we think we do. Insider trading is a vastly studied subject, with empirical work estimating the prevalence and nature of insider trading based on much of the public data. Yet without considering the rich seam of barely-hidden trades, the existing literature understates the extent of insider trading. Insider trading may have been rife just outside of the spotlight.

Normatively, investigators must update their search and audit patterns, recognizing that obscure transactions are more, not less, suspicious than their plain-vanilla peers. Relatedly, the SEC should consider issuing more guidance on J-code use and prosecuting miscoding. We also consider deeper reforms that go to the root of the problem.

Our Article proceeds as follows. Part I briefly introduces insider trading law and policy. Part II describes the related system of mandatory public reporting of insider trades. Part III illustrates abuses of the reporting system: mischaracterizing one’s trade, or changing the form of the trade in order to be able to characterize it differently. That Part offers suggestive examples to help concretize the explanation.

Those examples set the stage for our empirical analysis. In Part IV, we describe our method for identifying trades that are likely to have based on material, non-public information. We present our findings, which are that insider trades marked “other” greatly outperform the trades of

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<sup>7</sup> Accordingly, our article joins a rich literature of articles demonstrating loopholes in the reporting environment and failures of market observers to fully appreciate trade disclosures outside of the heartland of filings. *See, e.g.*, Alma Cohen, Robert J. Jackson, Jr. & Joshua Mitts, *The 8-K Trading Gap* (Columbia L. & Econ. Working Paper No. 524, 2015), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2657877](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2657877); Rober J. Jackson, Jr., Bradford Lynch-Levy, and Daniel J. Taylor, *Holding Foreign Issuers Accountable*, [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4072797](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4072797). *See also* SEHWA KIM & SEIL KIM, FRAGMENTED SECURITIES REGULATION, INFORMATION-PROCESSING COSTS, AND INSIDER TRADING (2022), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3416204](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3416204); Tom McGinty & Ben Foldy, *Signature Bank Insiders Sold \$100 Million in Stock During Crypto Surge*, WALL ST. J. (Apr. 4, 2023, 12:50 AM), <https://www.wsj.com/articles/signature-bank-insiders-sold-100-million-in-stock-during-crypto-surge-a9f77615>.

<sup>8</sup> *Infra* Parts II.C., V.A.

outsiders, particularly when proxies for miscoding are considered. In other words, insider trading by other means tends to be quite profitable.

Part V analyzes implications findings, both theoretical and normative. We then conclude.

## I. Insider Trading

Insider trading law seeks to vindicate a number of policy goals. It seeks to cultivate loyal and productive managers.<sup>9</sup> It seeks to protect ordinary investors, from whom insiders' profits are

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<sup>9</sup> If insiders can trade, they may be distracted from their duties as they focus their attention on trading and acquiring information. James D. Cox, *Insider Trading and Contracting: A Critical Response to the "Chicago School"*, 1986 DUKE L.J. 628, 659 (1986) ("The prohibition against insider trading . . . stems from the shareholders' expectation that a manager is paid to look after the shareholders' welfare, not his own."). They may mismanage the firm in order to generate trading opportunities. Insiders can sabotage the firm in order to profit from a short position. Saul Levmore, *Securities and Secrets: Insider Trading and the Law of Contracts*, 68 VA. L. REV. 117, 149 (1982) ("[T]he temptation of profit might actually encourage an insider to act against the corporation's interest."). *But see* Dennis W. Carlton & Daniel R. Fischel, *The Regulation of Insider Trading*, 35 STAN. L. REV. 857, 875 (1983) ("[I]t seems likely that the critics of insider trading have exaggerated the magnitude of the perverse incentives associated with short selling."). Even without sabotage, insiders can increase risk taking, knowing that they will know before the public which risks have paid off and which flopped. Frank H. Easterbrook, *Insider Trading, Secret Agents, Evidentiary Privileges, and the Production of Information*, 1981 SUP. CT. REV. 309, 332 (1982) ("[Insider traders] may select riskier projects than the shareholders would prefer, because if the risk pays off they can capture a portion of the gains in insider trading and, if the project flops, the shareholders bear the loss."). They may sometimes delay public disclosure in order to preserve their informational advantages. Victor Brudney, *Insider, Outsiders, and Informational Advantages Under the Federal Securities Laws*, 93 HARV. L. REV. 322, 335 n.53 (1979) ("If the insider is allowed to use such information for his personal gain, he will be tempted to . . . [decide] to delay . . . the release of the information so as to serve his trading or borrowing needs . . ."). Other times, their trades may intentionally or unintentionally spill the beans on information that the corporation had a legitimate need to keep secret. *See* James D. Cox, *Seeking an Objective for Regulating Insider Trading Through Texas Gulf Sulphur*, 71 SMU L. REV. 697, 707 (2018). For example, when mining executives buy their company's shares en masse, it may hint to other prospectors where they should dig to find valuable minerals. Andrew Verstein, *Insider Trading in Commodities*, 107 VA. L. REV. 447, 490–91 (2016).

unfairly<sup>10</sup> derived.<sup>11</sup> It seeks to protect market as a whole from the demoralization and caution, which insider trading might otherwise spread.<sup>12</sup>

Yet other policy objectives caution against an overly broad restriction on insider trading. Harsh trading restrictions may discourage stock-based compensation.<sup>13</sup> Insider trading can also improve stock price efficiency.<sup>14</sup>

In service of the forgoing policies, the law prohibits many forms of trading. Some of these prohibitions are generally applicable, proscribing categories of trade regardless of the identity of the trader. It is illegal to trade based on information one obtained by conferring personal benefit onto someone to breach their duty of trust and confidence to the ultimate information source. Thus, it's a crime for anyone to bribe a corporate executive to learn and trade on a hot tip about the

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<sup>10</sup> See Alan Strudler & Eric W. Orts, *Moral Principle in the Law of Insider Trading*, 78 TEX. L. REV. 375 (1999) (arguing that “insider trading is wrong because it is a kind of fraud.”). Of course, fairness is a deeply contested context.

<sup>11</sup> Manne argued that no trader was victimized. HENRY G. MANNE, *INSIDER TRADING AND THE STOCK MARKET* 93–104 (1966). Wang showed this not true. See William K. S. Wang, *Trading on Material Non-Public Information on Impersonal Stock Markets: Who is Harmed, and Who Can Sure Whom Under SEC Rule 10b-5?*, 54 S. CAL. L. REV. 1217, 1234–40 (1981); William K. S. Wang, *Stock Market Insider Trading: Victims, Violators and Remedies, Including an Analogy to Fraud in the Sale of a Used Car with a Generic Defect*, 45 VILL. L. REV. 27 (2000). A more sophisticated account in Fox et al shows that non-insiders may not be harmed on an ex-ante basis, since they can discount the price of stock by their expected future trading losses. Merritt B. Fox, Lawrence R. Glosten & Gabriel V. Rauterberg, *Informed Trading and Its Regulation*, 43 J. CORP. L. 817, 850–51 (2018). Accordingly, unsophisticated investors may pass their trading losses onto initial issuers of stock and the entrepreneurs before them.

<sup>12</sup> The conventional explanation is that capital formation requires retail investor confidence, and that insider trading impedes this confidence. The empirical basis for this claim has been questioned. But there is little question that insider trading decreases stock market liquidity, as market makers seek to offset their trading costs. See Merritt B. Fox, Lawrence R. Glosten & Gabriel V. Rauterberg, *The New Stock Market: Sense and Nonsense*, 65 DUKE L.J. 191, 218–19 (2015). Either way, a vibrant market requires some boundary to informed trading.

<sup>13</sup> That is because stock-based compensation is only valuable insofar as insiders can practically sell it. If insiders are in legal jeopardy whenever they sell, or if they can only safely sell on a few designated days of the year, they will resist stock-based compensation. Yet stock-based compensation can be otherwise efficient: it lets cash-strapped startups hire and it aligns the incentives of managers with the shareholders they serve.

<sup>14</sup> When insiders know that their company is concealing problems, they are tempted to sell the stock short, in order to profit from the eventual revelation. If their sales can be observed (directly or indirectly) other market participants will infer bad news about the stock – leading to a decline in stock price and possible further investigations. Here, we focus on trading by insiders such as managers. The goal of improving price accuracy is also vindicated by substantially legalizing trading for non-insiders. Outsiders, such as hedge funds, may improve price accuracy by researching and combining information in service of their trading strategy. Zohar Goshen & Gideon Parchomovsky, *The Essential Role of Securities Regulation*, 55 DUKE L.J. 711, 723 (2006).

company.<sup>15</sup> It is illegal for anyone to trade based on information that a tender-offer is likely (and where your source can be traced back one of the companies' management teams or their advisors).<sup>16</sup> It is illegal to trade, having defrauded the source of their information.<sup>17</sup> It is illegal to selectively disclose corporate secrets to shareholders who are likely to trade.<sup>18</sup> Commonsense suggests that large shareholders who nevertheless receive such information will have implicitly agreed not to trade.<sup>19</sup>

The forgoing prohibitions apply even to individuals who are truly "outsiders" to the corporation, whose shares are traded. Nevertheless, the main focus of insider trading law is on "insiders," those officers, directors, and large shareholders whose position and power gives them special access to the corporation and its secrets.

In addition to the generally applicable rules above, two additional rules lay constraints upon insiders. First, the "classical theory" prohibits corporate fiduciaries from trading the corporation's stock based on material non-public information, even if the corporation grants them permission to trade.<sup>20</sup> Thus, insider trading restrictions become mandatory and expansive, rather than subject to modification and proviso. This theory, and all those listed before it, are subject to criminal prosecution,<sup>21</sup> civil enforcement,<sup>22</sup> and treble damages in private civil suits.<sup>23</sup>

Second, statutory insiders (officers, directors, and owners of greater than 10% of shares) are subject to the "short-swing profits" rule.<sup>24</sup> Under this rule any profits insiders make from trading

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<sup>15</sup> *Dirks v. SEC*, 463 U.S. 646, 660 (1983) ("[A] tippee assumes a fiduciary duty to the shareholders of a corporation not to trade on material non-public information only when the insider has breached his fiduciary duty to the shareholders by disclosing the information to the tippee and the tippee knows or should know that there has been a breach.").

<sup>16</sup> 17 C.F.R. § 240.14e-3 (2023).

<sup>17</sup> *United States v. O'Hagan*, 521 U.S. 642, 659 (1997). A duty of trust and confidence can arise formally, or informally. 17 C.F.R. § 240.10b5-2(b)(1), (2) (2023). The SEC presumes that such confidences exist whenever two people have a "history, pattern, or practice of sharing confidences." *Id.* § 240.10b5-2(b)(2). Thus, a psychiatrist may not trade based on corporate secrets, disclosed by a client seeking care. *See Complaint, SEC v. Gangavarupu*, No. 1:09-CV-231 (E.D. Tenn. filed Aug. 31, 2009), 2009 WL 3028066. An outside lawyer for a corporation must keep her client's confidences by not trading on the basis of them *O'Hagan*, 521 U.S. at 648. Such unprofessional behavior defrauds their clients who probably shared information because of an implicit assurance that it would not be used for trading.

<sup>18</sup> Regulation FD, 17 C.F.R. § 243.100 (2023).

<sup>19</sup> If shareholders receive such information from any insider, they will have implicitly assumed that insider's duty to all shareholders. Michael Guttentag, *Selective Disclosure and Insider Trading*, 69 FLA. L. REV. 519, 559 (2017).

<sup>20</sup> A.C. Pritchard, *United States v. O'Hagan: Agency Law and Justice Powell's Legacy for the Law of Insider Trading* 78 B.U. L. REV. 13, 17 n.19 (1998) ("[T]he misappropriation theory [of insider trading] is subject to contractual waiver by the owner of the information, while the classical theory is not.").

<sup>21</sup> 15 U.S.C. § 78ff(a) (allowing for up to 20 years of imprisonment).

<sup>22</sup> *Id.* § 78u.

<sup>23</sup> *Id.* § 78u-1(a)(2).

<sup>24</sup> *Id.* § 78p(b).



their company's stock in any given six-month window are redeemable back to the corporation. Thus, a trader who sells her company's stock on April 1 and buys it back on May 1 for a profit must disgorge the profit back to the corporation. This is true even if the insider traded "innocently," without any special information at all.

None of these prohibitions are self-enforcing. Each requires a proponent, such as a civil plaintiff or prosecutor, to detect and prove violations of the law. But lawbreaking can be challenging to observe and verify. Trading in our securities market is, at a first approximation, anonymous. Individuals trade through their brokers, who are not obliged to disclose their clients' names – nor could they practically do so, in today's light-speed electronic trading environment. Traders do not know against whom they trade, nor can they request live updates on whether company executives happen to be trading today. Prosecutors cannot see a live report from the stock exchange about which individuals have enjoyed trading profits today, nor can companies and their shareholders peer into the brokerage accounts of their directors. In a faceless market, no eyewitnesses can pick suspects out of a lineup.

Enforcement of insider trading law necessarily depends in part on systems of surveillance, but the most important precondition for law enforcement is Section 16 of the Securities Exchange Act, which requires timely public disclosure of all trades by insiders. With those trades public, it is feasible for violations to be detected and proven. It is to Section 16 that we now turn.

## II. Insider Trading Reports

Insider trading law has long been the subject of controversy. What no one disputes is that it is important to know accurate information about insider trading.<sup>25</sup> This public information is vital for scholars who wish to understand the extent and nature of insider trading – whether to praise or criticize it. It is helpful to prosecutors, seeking to spot violations of the law. Even proponents of deregulation, who think that companies ought to be allowed to opt out of insider trading law, tend to think that Section 16 is sensible. That is because everyone agrees that *some* forms of insider trading (such as short-selling by insiders or short-swing profits), are problematic, and shareholders benefit from a legible report on what exactly is happening at their company.

This Part discusses the law and policy of trade reporting, misreporting, and the coding decisions that can make the difference between them.

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<sup>25</sup> This broad acceptance stands in stark contrast to most other aspects of insider trading law – including other aspects of Section 16. See Steve Thel, *The Genius of Section 16: Regulating the Management of Publicly Held Companies*, 42 HASTINGS L.J. 391, 393 (1991) (“Section 16 of the Securities Exchange Act (Exchange Act) is probably the most criticized provision of the federal securities statutes”). Thel is, of course, referring to the non-disclosure parts of 16, which penalizes insiders who trade in proscribed ways.

## A. Reporting Obligations

### 1. Reporting law

Section 16(a) of the Securities Exchange Act of 1934 (the “Exchange Act”)<sup>26</sup> contains reporting requirements for persons considered “insiders” of public companies.<sup>27</sup> Such insiders include the individuals and entities which are the issuer’s directors, officers, or beneficial owners of more than ten percent of the shares (each, a “reporting person”).<sup>28</sup> If these individuals acquire or dispose of the company’s securities, they are required to provide timely public notice of that transaction.<sup>29</sup>

Reporting law contains several anti-evasion principles, intended to close “unforeseen ‘loopholes’ that seek to use form to evade substance or to comply with technicalities while violating the ‘spirit’ or intent of regulatory provisions.”<sup>30</sup> Thus, insiders must file in connection with shares she directly *or indirectly* owns, so an individual must file even in cases where the transfer is not a plain vanilla sale from her brokerage account. For example, an insider in XYZ Corp must report trades if she wholly owns a company, and that latter company sells XYZ Corp shares.<sup>31</sup> The reporting person must likewise report transactions of shares for which she is a *beneficial* owner, even if she is not a *legal* owner. For example, an investor must report transactions of securities she does not own outright, if the nominal owner has agreed that the investor gets to dictate how the shares are voted and whether they are ever sold.<sup>32</sup> Reporting by indirect and beneficial owners addresses simple subterfuge strategies, such as transferring shares to a non-insider friend (who sells the shares and returns the money to the insider), that might otherwise frustrate reporting law’s policy objectives.<sup>33</sup>

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<sup>26</sup> Securities Exchange Act of 1934 § 16, 15 U.S.C. § 78p.

<sup>27</sup> 17 C.F.R. § 240.16a-2 (2023) (requiring such disclosures for companies that have registered a class of equity securities under Section 12 of the Exchange Act).

<sup>28</sup> *Id.* Officers include the executive officers identified pursuant to Item 401(b) of Regulation S-K and any other officer or person who performs a policy-making function for the issuer. *Id.* § 240.16a-1(f). A person is a beneficial owner subject to Section 16 reporting requirements if that person has or shares, directly or indirectly, voting power or investment power of greater than ten percent of the shares of the issuer. *Id.* § 240.16a-1(a)(1). Beneficial ownership means having a pecuniary interest, whether direct or indirect, to profit or share in the profits from a transaction in the securities. *Id.* § 240.16a-1(a)(2). Control over the security also amounts to beneficial ownership. *Id.* § 240.13d-3(b).

<sup>29</sup> See Statement of Changes of Beneficial Ownership of Securities (Form 4) General Instructions, SEC, <https://www.sec.gov/about/forms/form4data.pdf>.

<sup>30</sup> *CSX Corp. v. Children’s Inv. Fund Mgmt. (UK) LLP*, 654 F.3d 276, 302–03 (2d Cir. 2011) (Winter, J., concurring).

<sup>31</sup> *Bartel*, Exchange Act Release No. 97084, 2023 WL 2455410, at \*1 (Mar. 9, 2023).

<sup>32</sup> *Editek, Inc. v. Morgan Capital, L.L.C.*, 150 F.3d 830, 832–34 (8th Cir. 1998); *Huppe ex rel. WPCS Int’l Inv. v. Special Situations Fund III QP, L.P.*, 565 F. Supp. 2d 495, 499–500 (S.D.N.Y. 2008).

<sup>33</sup> Although indirect and beneficial ownership extend the reach of reporting law, it also nevertheless perforated with exceptions and imitations. For example, no reporting may be required if retirement plan securities are transferred in connection with a divorce. 17 C.F.R. § 240.16a-12

2. Reporting policy

Trade reporting law serves a number of important policies. First, and most obviously, it discourages insiders from trading on the basis of inside information.<sup>34</sup> Some insiders may be embarrassed to have their well-timed trades publicized.<sup>35</sup> More importantly, reporting increases the riskiness of illegal trades. Investigators can use reports to spot suspicious trades, in order to sue or prosecute the traders.<sup>36</sup> Shareholders who observe insider trading patterns may take account of these trades as they evaluate the merits of the company and its executives. Executives who trade a great deal may appear disloyal, distracted, opportunistic, or just overpaid.<sup>37</sup> Shareholders who observe insider trades can opt to sell their shares or vote for new management.<sup>38</sup>

Second, and relatedly, reporting may discourage other misbehavior apart from insider trading, such as market manipulation.<sup>39</sup>

Third, reporting may encourage officers and directors to hold large amounts of their company's stock.<sup>40</sup> It will do this by alerting shareholders to officers and directors who sell their stock, and rendering credible any managerial assertion of continuous ownership. Shareholders tend

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(2023) (“The acquisition or disposition of equity securities pursuant to a domestic relations order . . . shall be exempt from section 16 of the Act.”). Likewise, if an entity distributes securities to its investors, and those investors had previously reported their beneficial ownership in the underlying securities (by dint of their ownership of the entity), those investors need not report their direct acquisition of the securities. However, the entity must still disclose its disposition of the distributed securities. *Id.* § 240.16a-13 (“A transaction, *other than the exercise or conversion of a derivative security* or deposit into or withdrawal from a voting trust, that effects only a change in the form of beneficial ownership . . . shall be exempt from section 16 of the Act.”) (emphasis added); Division of Corporation Finance, *Exchange Act Section 16 and Related Rules and Forms* § 217.02, SEC (updated Oct. 7, 2022), <https://www.sec.gov/divisions/corpfin/guidance/sec16interp.htm> (“[T]he scope of Rule 16a-9(a) is limited to persons subject to Section 16 who experience an increase or decrease in the number of securities held as a result of a stock distribution or reverse stock split effected by the distributing party . . . .”); SEC Division of Corporation Finance, *Manual of Publicly Available Telephone Interpretations* § R, Question 9 (July 1997) (same); 1 ARNOLD S. JACOBS, SECTION 16 OF THE SECURITIES EXCHANGE ACT § 2:91, § 3:17 n.54.50 and accompanying text. (2d ed. 2023). *id.*

<sup>34</sup> Thel, *supra* note 25, at 419 n.77 and accompanying text (1991).

<sup>35</sup> *Id.* at 419–20.

<sup>36</sup> See Wang v. Cloopen Group Holding Ltd., No. 21-CV-10610, 2023 WL 2534599, at \*6 (S.D.N.Y. Mar. 16, 2023) (“When presented with a motion to dismiss a complaint, . . . [t]he Court can take judicial notice of public disclosures that must be filed with the SEC . . . .”); Fresno County Employees’ Retirement Ass’n v. comScore, Inc., 268 F. Supp. 3d 526 (2017).

<sup>37</sup> Carlton & Fischel, *supra* note 9, at 891 (determining compensation).

<sup>38</sup> *But see* Thel, *supra* note 25, at 420–21 nn.81–82 and accompanying text (arguing that shareholders will tend not to act against insider trading).

<sup>39</sup> See Andrew Verstein, *Benchmark Manipulation*, 56 B.C. L. REV. 215, 256 (2015) (describing how selective disclosure of trades can enable an actor to manipulate price benchmarks and, thereby, the market).

<sup>40</sup> Thel, *supra* note 25, at 422–24.

to benefit from manager ownership, since it aligns their interests and leads to more efficient pursuit of corporate objectives.<sup>41</sup>

Fourth, disclosure sends signals about company quality.<sup>42</sup> When insiders sell their shares – even if legally – it may hint at pessimism among those with the most knowledge. Stock prices are more efficient if the public can observe these informative trades.

### 3. Misreporting

Misreporting is illegal.<sup>43</sup> The Exchange Act authorizes the SEC to initiate enforcement proceedings to for violations of 16(a), including its transaction reporting requirements.<sup>44</sup> Possible remedies include an injunction,<sup>45</sup> a bar on future officer and director service,<sup>46</sup> disgorgement,<sup>47</sup> and civil monetary penalties.<sup>48</sup> The Department of Justice can bring criminal penalties for willful

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<sup>41</sup> Nitzan Shilon, *Replacing Executive Equity Compensation: The Case for Long-Term Performance*, 43 DEL. J. CORP. L. 1, 10 (2018) (“[B]y tying pay directly to the change in a firm’s stock price, it is expected to align the interests of managers with those of shareholders . . .”).

<sup>42</sup> Carlton & Fischel, *supra* note 9, at 892.

<sup>43</sup> Arguably, any trade misreported has not been reported. Some other (fictional) trade was reported. If that is correct, then the consequences for misreporting include all of the consequences for non-reporting. *See* SEC v. Ali, 454 F. Supp. 3d 1281, 1300 (N.D. Ga. 2020) (failed to file Form 4); SEC v. Blackburn, 431 F. Supp. 3d 774, 800, 816–17 (E.D. La. 2019) (same); S.E.C. v. Verdiramo, 890 F. Supp. 2d 257, 273 (S.D.N.Y. 2011) (same); SEC v. Sierra Brokerage Servs. Inc., 608 F. Supp. 2d 923, 974 (S.D. Ohio 2009) (same). And there are many consequences to delayed reporting. For example, the two-year limitations period provided in § 16(b) is tolled while § 16(a) reports are delinquent. *Whittaker v. Whittaker Corp.*, 639 F.2d 516, 530 (9th Cir. 1981); *see also* Thel, *supra* note 25, at 448 n.191 (suggesting that this sanction is neither effective nor onerous).

<sup>44</sup> Securities Exchange Act of 1934 § 21(c), 15 U.S.C. § 78u(c); *see, e.g.*, SEC v. Shattuck Denn Mining Corp., 297 F. Supp. 470, 477 (S.D.N.Y. 1968) (Defendant failed to disclose disposition of some of his stock on the appropriate Form 4, and was enjoined from further § 16(b) violations and ordered to file an accurate revision); Burns, Exchange Act Release No. 66738, 2012 WL 1119224, at \*1 (ALJ Apr. 4, 2012) (default order); Bartel, *supra* note 31, at \*5–6.

<sup>45</sup> Securities Exchange Act of 1934 § 21(d)(1), 15 U.S.C. § 78u(d)(1); *see, e.g.*, Burns, *supra* note 44, at \*1 (noting that the respondent “misrepresented his . . . stock holdings in proxy statements and Forms 4”, and was accordingly permanently enjoined from future violations of the Exchange Act, as well as ordered to pay disgorgement plus prejudgment interest and barred from acting as an officer or director of a public company).

<sup>46</sup> Burns, *supra* note 44, at \*1.

<sup>47</sup> Securities Exchange Act of 1934 § 21(d)(3)(A)(ii), 15 U.S.C. § 78u(d)(3)(A)(ii); *see, e.g.*, S.E.C. v. Teo, No. 2:04-CV-01815, 2010 WL 3184349, slip op. at \*11 (D.N.J. Aug. 10, 2010); Burns, *supra* note 44, at \*1.

<sup>48</sup> Securities Exchange Act of 1934 § 21(d)(3)(A)(i), 15 U.S.C. § 78u(d)(3)(A)(i); SEC v. Govil, No. 1:21-CV-6150, 2021 WL 3188325, slip op. at \*2 (S.D.N.Y. Jul. 28, 2021); S.E.C. v. Olins, 762 F. Supp. 2d 1193 (N.D. Cal. 2011); Bartel, *supra* note 31, at \*5–6 (ordering a civil monetary penalty of \$100,000 when the respondent filed a Form 4 that correctly disclosed a purchase but incorrectly stated his total beneficial ownership).

violations of the statute.<sup>49</sup> There is some uncertainty about whether private plaintiffs, such as those who sell shares in reliance on a false Form 4, can sue.<sup>50</sup>

A trader's misreporting can have consequences for the company whose securities are traded.<sup>51</sup> Regulation S-K Item 405 requires corporations to periodically report on their insiders' degree of reporting compliance.<sup>52</sup> This is one reason that many companies file reports on behalf of their insiders.<sup>53</sup> A false trade report could therefore lead to consequences for the issuer. If it is culpable in misfiling a trade report or in failing to accurately disclose the poor coding of their insiders' own filings, the issuer would run afoul Regulation S-K.

There are consequences for misreporting. However, the risks may be manageable, given the paucity of oversight and the weak sanctions for violations. "Relatively few cases substantively address Section 16(a), considering its importance."<sup>54</sup> There does not seem to be any serious appetite to audit transaction codes or test the accuracy of these filings. We discuss the risk of detection and prosecution *infra* Part II.F.

#### 4. Coding

The form used to report most transaction is called Form 4 (Statement of Changes of Beneficial Ownership of Securities).<sup>55</sup> **Error! Reference source not found.** An example of Form 4 is shown here:

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<sup>49</sup> Securities Exchange Act of 1934 § 32(a), 15 U.S.C. § 78ff(a) ("Any person who willfully violates any provisions of [the Act], or any [related] rule or regulation . . . shall upon conviction be fined . . ., or imprisoned . . ., or both . . .; but no person shall be subject to imprisonment under this section . . . if he proves that he had no knowledge of such rule or regulation."). *E.g.*, U. S. v. Guterma, 281 F.2d 742, 752 (2d Cir. 1960).

<sup>50</sup> 1 JACOBS, *supra* note 33, § 2:1 ("[I]t is unlikely that a Section 16(a) private right of action exists today . . . . If there is a Section 16(a) private right of action, it should redress a late filing, a false filing, or a failure to file at all.").

<sup>51</sup> Additionally, whomever controls the misfiler may be held liable. Securities Exchange Act of 1934 § 20, 15 U.S.C. § 78t; *cf.* SEC v. Markusen, 143 F. Supp. 3d 877, 892 (D. Minn. 2015) (holding that the controlling person of a beneficial owner was liable for the beneficial owner's failure to file required forms).

<sup>52</sup> Regulation S-K Item 405, 17 C.F.R. § 229.405 (2023). *See* Ownership Reports and Trading by Officers, Directors and Principal Security Holders, Exchange Act Release No. 28,869, 56 Fed. Reg. 7242, at § VI.B (Feb. 21, 1991) (adopting Item 405).

<sup>53</sup> THOMAS LEE HAZEN, 4 TREATISE ON THE LAW OF SECURITIES REGULATION § 13:3 (2023) ("[M]any companies try to assure their insiders' compliance with the section 16 reporting requirements by filing the Form 4 on the insider's behalf.").

<sup>54</sup> 1 JACOBS, *supra* note 33, § 2:1.

<sup>55</sup> Form 5 (Annual Statement of Beneficial Ownership of Securities) may be used to give notice of transactions for which timely filing on a Form 4 was not necessary. 17 C.F.R. § 240.16a-3(f) (2023); Statement of Changes of Beneficial Ownership of Securities (Form 4) General Instructions, *supra* note 29. For example, certain acquisitions of less than \$10,000 aggregate market value in the last six months need not be timely filed in a Form 4, but if not otherwise filed,

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need to be noted in a Form 5. SEC v. [Nutra Pharma Corp.](#), 2022 U.S. Dist. LEXIS 157474, \*39 (E.D. N.Y. 2022).

Form 5 is due 45 days after the end of an entity's fiscal year, such that some transactions reported on a Form 5 are quite stale. 17 C.F.R. § 240.16a-3(f)(1) (2023). An exempt transaction on January 1, 2023, concerning an entity with Fiscal year ending on December 31, 2023, would not have to be disclosed until February 15, 2024.



*INSIDER TRADING BY OTHER MEANS*

SEC Form 4  
**FORM 4**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

OMB APPROVAL	
OMB Number:	3235-0287
Estimated average burden hours per response:	0.5

Check this box if no longer subject to Section 18, Form 4 or Form 5 obligations may continue. See Instruction 1(b).

**STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP**

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934 or Section 30(h) of the Investment Company Act of 1940

1. Name and Address of Reporting Person <u>DOMENECH CARLOS</u>  (Last) (First) (Middle) <u>12500 BALTIMORE AVENUE</u>  (Street) <u>BELTSVILLE MD 20705</u>  (City) (State) (Zip)			2. Issuer Name and Ticker or Trading Symbol <u>TerraForm Power, Inc. [ TERP ]</u>		5. Relationship of Reporting Person(s) to Issuer (Check all applicable) <input checked="" type="checkbox"/> Director 10% Owner <input checked="" type="checkbox"/> Officer (give title below) Other (specify below)  <u>See Remarks</u>	
			3. Date of Earliest Transaction (Month/Day/Year) <u>07/23/2014</u>			
			4. If Amendment, Date of Original Filed (Month/Day/Year)		6. Individual or Joint/Group Filing (Check Applicable Line) <input checked="" type="checkbox"/> Form filed by One Reporting Person Form filed by More than One Reporting Person	

**Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned**

1. Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed Of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Class A common stock	07/23/2014		J		476,732	A <sup>(1)</sup>	(1)	476,732	D	
Class A common stock	07/23/2014		J		1,212,228	A <sup>(2)</sup>	(2)	1,688,860	D	
Class A common stock	07/23/2014		P		10,000	A	\$25	1,698,860	D	
Class A common stock	07/23/2014		P		10,000	A	\$25	10,000	I	By son.
Class A common stock	07/23/2014		P		10,000	A	\$25	10,000	I	By daughter.
Class A common stock	07/23/2014		P		10,000	A	\$25	10,000	I	By daughter.

**Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned (e.g., puts, calls, warrants, options, convertible securities)**

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)		5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)	6. Date Exercisable and Expiration Date (Month/Day/Year)		7. Title and Amount of Securities Underlying Derivative Security (Instr. 3 and 4)	8. Price of Derivative Security (Instr. 5)	9. Number of derivative Securities Beneficially Owned Following Reported Transaction(s) (Instr. 4)	10. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	11. Nature of Indirect Beneficial Ownership (Instr. 4)
				Code	V		Date Exercisable	Expiration Date					

**Explanation of Responses:**

- TerraForm Power, Inc. (the "Company") effected a 127.1624-for-1 stock split of its outstanding Class A common stock immediately prior to the completion of the Company's initial public offering, resulting in the reporting person's ownership of additional shares of Class A common stock.
- Effective immediately after the stock split referenced in footnote (1), the outstanding shares of Class C common stock of the Company automatically converted into shares of the Company's Class A common stock on an 85.8661-for-one basis, resulting in the reporting person's ownership of additional shares of Class A common stock.

**Remarks:**

President and Chief Executive Officer

/s/ Sebastian Deschler, by 07/23/2014  
power of attorney

\*\* Signature of Reporting Person Date

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

\* If the form is filed by more than one reporting person, see Instruction 4 (b)(v).

\*\* Intentional misstatements or omissions of facts constitute Federal Criminal Violations See 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, see Instruction 6 for procedure.

Persons who respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB Number.

As this figure indicates, Form 4 has separate tables for disclosing transactions in non-derivative securities (such as ordinary common stock) and derivative securities (such as call

*INSIDER TRADING BY OTHER MEANS*

options).<sup>56</sup> Insiders must disclose their name and address, the name of the company that issued the security being traded (as well as their ticker or trading symbol), the date of the earliest transaction, the relationship of the reporting person to the issuer, and an indicator for whether the form is being filed individually or jointly.<sup>57</sup> For each transaction, the reporting person must provide information about the number and price for the shares. The reporting person must mark (A) if the transaction was an acquisition (increasing the investor's ownership) or (D) for a disposition (reducing ownership).<sup>58</sup>

Most central to our purposes, the reporting person must also mark an identifying code for each transaction, from the options below.<sup>59</sup>

P	Open market or private purchase of non-derivative or derivative security
S	Open market or private sale of non-derivative or derivative security
V	Transaction voluntarily reported earlier than required
A	Grant, award or other acquisition pursuant to Rule 16b-3(d)
D	Disposition to the issuer of issuer equity securities pursuant to Rule 16b-3(e)
F	Payment of exercise price or tax liability by delivering or withholding securities incident to the receipt, exercise or vesting of a security issued in accordance with Rule 16b-3
I	Discretionary transaction in accordance with Rule 16b-3(f) resulting in acquisition or disposition of issuer securities
M	Exercise or conversion of derivative security exempted pursuant to Rule 16b-3
C	Conversion of derivative security
E	Expiration of short derivative position
H	Expiration (or cancellation) of long derivative position with value received
O	Exercise of out-of-the-money derivative security
X	Exercise of in-the-money or at-the-money derivative security
G	Bona fide gift
L	Small acquisition under Rule 16a-6
W	Acquisition or disposition by will or the laws of descent and distribution
Z	Deposit into or withdrawal from voting trust
K	Transaction in equity swap or instrument with similar characteristics
U	Disposition pursuant to a tender of shares in a change of control transaction
J	Other acquisition or disposition (describe transaction)

<sup>56</sup> Statement of Changes of Beneficial Ownership of Securities (Form 4), SEC, <https://www.sec.gov/files/form4.pdf>.

<sup>57</sup> *Id.*

<sup>58</sup> This is in section 4, the central column for table I.

<sup>59</sup> Statement of Changes of Beneficial Ownership of Securities (Form 4) General Instructions, *supra* note 29. This table below includes verbatim quotations of the transaction codes, but headings have been omitted and codes reordered.



The most familiar transaction codes are P, indicating a purchase of stock, and S, an ordinary sale of stock. At the very bottom of this list is “J,” a transaction code representing some transaction “other” than the nineteen types preceding it.

The SEC instructs individuals to “indicate. . . the character of the transaction reported. Use the code that most appropriately describes the transaction. If the transaction is not specifically listed, use transaction Code ‘J; and describe the nature of the transaction in the space for explanation of responses.”<sup>60</sup> Thus, if one code fits best, that is the one that is required. And if no code fits, the answer is J.

The SEC provides more guidance on the interpretation of these codes,<sup>61</sup> and a substantial secondary literature has emerged to guide lawyers and their clients on reporting best practices. Romeo and Dye’s two-volume handbook offers more than 1000 pages of practical guidance, focused just on the details of how to fill out the one-page Form-4 and its peers. Romeo and Dye also publish a treatise on Section 16 law, more generally. Nor are their handbooks and treatises the only ones.<sup>62</sup> Section 16 filings appear to be an area of law where the law abides partially in the craft wisdom about what is commonplace and acceptable, supervening on a framework of rules that cover the easy cases.

What does that lore indicate about the proper use of the “other” code? Many strange transactions fit the bill.<sup>63</sup> A few examples:

- Shares acquired or disposed in a stock split or reverse split.<sup>64</sup>
- Cancellation of shares, spinoffs, some mergers, and some corporate transactions requiring a corporate name change.<sup>65</sup>
- Securities paid as consideration to redeem a poison pill.<sup>66</sup>

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<sup>60</sup> *Id.*

<sup>61</sup> For example, the SEC has issued no-action letters to clarify the filing requirements for various forms of arguable beneficiary ownership. *E.g.*, Prudential-Bache Sec., Inc., SEC Staff No-Action Letter, 1985 WL 55643 (Dec. 2, 1985) (clarifying that purchases and sales made by broker-dealers for the purpose of market-making need not be disclosed).

<sup>62</sup> HAZEN, *supra* note 53; LAWRENCE D. LEVIN & ADAM R. KLEIN, 2014 HANDBOOK FOR PREPARING SEC ANNUAL REPORTS AND PROXY STATEMENTS (2013); SECURITIES AND EXCHANGE COMMISSION, A PLAIN ENGLISH HANDBOOK: HOW TO CREATE CLEAR SEC DISCLOSURE DOCUMENTS (1999).

<sup>63</sup> We reviewed the two leading handbooks on Section 16 filings. Both Jacobs and Romeo & Dye identify 24 instances in which Code J is proper and one in which it may not be inferior but some other transaction code is a better fit. Romeo and Dye additionally identify two instances where J and K should *both* be selected, and five cases where either J or P are both equally proper. *See* 1 JACOBS *supra* note 33; ROMEO & DYE, *infra* note 68.

<sup>64</sup> 1 JACOBS, *supra* note 33, § 8:25. Also see the footnotes for J-coded acquisitions on Form 4 for \$TERP, *supra*.

<sup>65</sup> For instance, on November 3, 2021, IBM distributed 179M or 80.1% of the newly spun-off division, Kyndryl Holding, Inc. (KD) as a J-coded trade. *See*, [https://www.sec.gov/Archives/edgar/data/1867072/000095014221003574/xslF345X03/es210199109\\_4-ibm.xml](https://www.sec.gov/Archives/edgar/data/1867072/000095014221003574/xslF345X03/es210199109_4-ibm.xml)

<sup>66</sup> 1 JACOBS, *supra* note 33, § 8:29.

- The insider had previously acquired exchange-traded call options on the company's stock, but the options are now gone, because they expired unused.<sup>67</sup>
- Shares previously granted to a Grantor Retained Annuity Trust that are returned in substitution for other assets.<sup>68</sup>
- The execution of an equity swap agreement.<sup>69</sup>
- Shares received because of the rescission of a transaction.<sup>70</sup>

As the forgoing litany indicates, code J is not used for everyday sales and purchases. It is properly limited to special cases as we will discuss.

Yet hundreds of thousands of trades end up coded as J, and our findings in Part IV indicate that they are (on average) highly profitable. How might “other” transactions gain such prominence? Part III lays out some case studies in how some traders found J-codes to be convenient. But the following section (III.D) introduces the notion that codes are, at least in part, discretionary.

## B. “Other” Opportunism

### 1. Opportunistic Coding

Opportunistic trade reporting means reporting trades in a manner that reduces the risk of scrutiny. One such form of opportunism involves selecting transaction codes that are subject to less examination. At a high level, opportunistic reporting exists on a spectrum of legality. At one extreme are highly fraudulent codings, where the insider selects a transaction code without any legal basis. For example, a brazen miscoder might just apply a G code (indicating a gift) to conceal a sale. We can call this approach “miscoding.”

At the other extreme, the insider may have a strong legal basis for the coding selection, but the coding remains opportunistic because the insider intentionally structured her affairs in order to qualify for the preferred coding. For example, a trader who wishes to sell shares might instead gift the shares to a child or investment partner, who then sells the shares. Such an indirect transaction may sometimes properly incur a code other than S (sale) for the insider, even though the economic substance is similar to an outright sale. Largely lawful coding strategies, which are nevertheless selected in part to conceal, can be called “trade laundering.”

In between are cases where there is some legal basis for the selection, perhaps because the trader structured their affairs to create such a basis, but where the best application of the law to the facts would still call for some other code.<sup>71</sup> There are transactions about which reasonable doubt

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<sup>67</sup> *Id.* § 8:60.

<sup>68</sup> 1 PETER J. ROMEO & ALAN L. DYE, SECTION 16 FORMS & FILINGS HANDBOOK, Model Form 47 (9th ed. 2021).

<sup>69</sup> 2 *id.* Model Form 201, Reporting Principle 5. Note that here, the authors recommend using “‘J/K’ (‘J’ accompanied by ‘K’),” rather than just J.

<sup>70</sup> 2 *id.* Model Form 234, Reporting Principle 3.

<sup>71</sup> For example, imagine a stock-for-stock merger in which employees of one company will lose their stock options but be given cash equal to what the employee would have received if they had exercised those stock options and then sold the stock. One could code it as X or O (representing an exercise of an option) followed by S (for a sale), because this transaction is economically

may exist as to the best filing, such as when it is not clear whether a transaction has occurred yet.<sup>72</sup> Any transaction that could be coded S (sale), but which has peculiar features might be better characterized as J or S/J; a trader can introduce unusual features in order to plausibly depart from S. Indeed, there are even cases where the leading treatises disagree on the appropriateness of the J code.<sup>73</sup> A coding can have some legal basis (thus, not pure miscoding) but that basis is weak (thus, not pure trade laundering).

Whether form of opportunistic coding is considered, traders are likely to succeed more easily and safely because of the transaction code “J,” which represents “other.” The next Section explains why.

## 2. The Power of “Other.”

Opportunistic coding may help conceal the nature of a potentially suspicious or objectionable insider trade. When insiders code opportunistically, they may exhibit a preference for the J-code, representing “other.” This is because the subjective and vague nature of the “other” categorization lends itself to both opacity and plausible deniability.

In theory, any coding can serve as a substitute for the highly suspicious S (sale) and P (purchase codings. But most codings can be quickly understood by investigators. A trader who sells in the open market can simply omit the S code and punch in G, thereby asserting (falsely, and with no basis) that it is a bona fide gift. But investigators can easily audit such a transaction, asking for a gift receipt or questioning why the “gift” led to trading profits. And such a miscodings would be so implausible that a prosecutor could easily establish that the miscoding was intentional or willful.<sup>74</sup>

A J selection may be preferable because prosecutors cannot easily understand the transaction and its proper coding. J is at the penumbra of every transaction, so it is imaginable that one might complicate a transaction to obtain J characterization. And a trader who incorrectly codes their transaction as J may be wrong, but how can prosecutors establish that the miscoding was willful or even negligent? Absent some smoking gun emails (containing bragging or confessions), a trader

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equivalent to an exercise and sale. But the transaction was not actually an exercise and sale. So J is the better coding. 1 JACOBS, *supra* note 33, § 8:66.

<sup>72</sup> Someone who thinks the transaction has occurred would report it, someone who doesn’t might not report it. Reporting it under J can itself be an arguable accommodation to uncertainty. PETER J. ROMEO & ALAN L. DYE, SECTION 16 DESKBOOK 354 (2022) [hereinafter ROMEO & DYE DESKBOOK] (when there is reasonable doubt as to whether a purchase or sale occurred, “the insider should not report a transaction using transaction code ‘P’ (‘Open market or private purchase or non-derivative or derivative security’) or ‘S’ (‘Open market or private sale of non-derivative or derivative security’), but instead should use transaction code ‘J’ (‘Other acquisition or disposition’) and explain the nature of the transaction in a footnote.”); *see* 1 PETER J. ROMEO & ALAN L. DYE, SECTION 16 TREATISE AND REPORTING GUIDE 633 (2019) [hereinafter ROMEO & DYE TREATISE AND REPORTING GUIDE].

<sup>73</sup> *See, e.g.*, 1 JACOBS, *supra* note 33, § 8:52 (noting a disagreement regarding whether a J code or an X code is more appropriate in the case of a former director settles her phantom stock within six months of the termination of her directorship).

<sup>74</sup> Intentional wrongdoing establishes scienter for civil securities litigation. Willful establishes criminal liability.

may risk detection without risking the most serious consequences.<sup>75</sup> Prosecutors know the challenges they face and may be discouraged from expending the effort. Moreover, prosecutors might just trust that the transaction is benign. Many transactions properly coded “J” are both confusing and useless for insider trading. For example, J is proper when there is a stock split. A stock split is a decision by the company to double the number of shares (and halve their per-share value). Such a transaction poses no risk of insider trading, so prosecutors may implicitly trust a J-coded transaction as likely to be anodyne.

Not only might investigators give J coded transactions a pass, but we have strong evidence that they do so. As we discuss in the following Section, investigators do not catch and prosecute transactions erroneously coded as J.

### C. Lack of Scrutiny

Investigators do not spot and interrogate the underlying J-coded transactions. Use of a J code seems to occlude any oversight of otherwise suspicious trades. We scoured the public record and can find no case, enforcement action, or other investigatory material addressing transaction code J.<sup>76</sup>

We examined the public record for evidence that the Department of Justice<sup>77</sup> or the SEC had prosecuted insiders for trades undertaken with the J code.<sup>78</sup> We found none. This was true even

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<sup>75</sup> All of this is different for miscoding without J. A trader who wrongly asserts that an open market sale (S) was a bona fide gift (G) will usually have no justification for their selection and will, therefore, appear to have acted willfully and with scienter.

<sup>76</sup> The closest we found was a motion in which a filer apologized for *not* using code J. Defendant David H. Smith's Memorandum of Law in Support of His Cross-Motion for Summary Judgment and in Opposition to Plaintiff's Motion for Summary Judgment at 8, *Morales v. Quintiles Transnational Corp.*, 25 F. Supp. 2d 369 (1998), 1997 WL 3471487 (“In the SEC filings, Dr. Smith's counsel mistakenly entered the transaction code ‘P’ to refer to the October 19, 1995 substitution transaction when they should have entered the transaction code ‘J’ and an explanatory description of the transaction. This was a clerical error; the substitution transaction was not actually a purchase of Quintiles securities within the meaning of Section 16 because Dr. Smith was already the sole beneficial owner of the Quintiles securities held by the Smith Family Trusts before the transaction, as had been reported on previously filed Form 4s.”) (citations omitted).

<sup>77</sup> We read every DOJ information, plea agreement, complaint, and indictment going back to mid-2017. We found these by searching Bloomberg Law, with the keywords “insider trading”; “insider trading” AND “10b-5.” In the “Federal NOS” section in the column, we clicked the checkbox for “criminal.” We compiled to a similar list from Lexis Courtlink. We searched for “insider trading,” and then read each information, etc. This approach yielded 50 matters. For each one, we downloaded all Form 4s filed by defendants in the case. We read the Form 4s to see if any contained J coded transactions. Almost none did. Where we did, we still didn’t see the DOJ refer to these J-coded transactions as possible insider trading.

<sup>78</sup> From June 14, 2017 to June 30, 2023, the Securities and Exchange Commission (“SEC”) has litigated 177 insider trading suits. In none of these cases did the suspect transaction involve a J-code. We read every complaint and opinion from an SEC insider trading suit from June 14, 2017 to June 30, 2023. We found these by searching Bloomberg Law, with the keywords “insider trading”; “insider trading” AND “10b5-1.” In the “Federal NOS” section in the column, we clicked

where insiders were prosecuted for securities fraud<sup>79</sup> or insider trading and where suspicious J coded transactions had occurred.<sup>80</sup> Prosecutors focused on the S trades and left the J codes to the side.

We checked whether plaintiffs bringing individual and class actions cited suspicious J coded trades in their complaints.<sup>81</sup> They do not, even in cases where the plaintiffs otherwise build their case around suspicious trades, and even where suspicious J coded transactions existed and could have been cited.<sup>82</sup>

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the checkbox for “Statutes: Securities / Commodities.” Then, for each docket, we read the complaint to determine whether the SEC alleged insider trading had occurred. We followed a similar methodology to find court opinions on SEC-litigated insider trading suits. We searched “insider trading” on Lexis+, limiting the search to Civil cases from U.S. District Courts. After having sorted the results by date, we read through all results to determine if insider trading was alleged; occasionally, if the opinion discussed the details of the case in a cursory manner, we opened the “Filings” to read the complaint. If the SEC alleged insider trading, we determined whether the complaint or opinion mentioned that a company insider was alleged to have done the trading themselves. If the complaint or opinion did mention this, then we read the Form 4s containing the alleged insider trading transactions to determine whether they contained J-coded transactions. Almost none did. In the few cases where the defendant did make a J-coded transaction, the SEC’s complaint or court’s opinion did not mention these trades.

<sup>79</sup> Trevor Milton filed J-Coded transactions when he swapped stock options for real estate, a transaction for which he was prosecuted. But the prosecution was for fraud, not for insider trading. Chris Dolmetsch, *Nikola Founder Bought Utah Ranch with ‘Worthless’ Options*, BLOOMBERG (Sep. 29, 2022, 1:15 PM), <https://www.bloomberg.com/news/articles/2022-09-28/nikola-founder-bought-utah-ranch-with-worthless-stock-options>.

<sup>80</sup> When the SEC and DOJ prosecuted Nikola insiders for fraud, they did not accuse them of insider trading in connection with the J-coded transactions. *See* Complaint, SEC v. Milton, No. 1:21-CV-6445 (S.D.N.Y. filed Jul. 29, 2021), <https://www.sec.gov/litigation/complaints/2021/comp-pr2021-141.pdf>; Jack Ewing, *Trial Begins for Truck Maker Accused of Duping Investors*, N.Y. TIMES (Sep. 12, 2022), <https://www.nytimes.com/2022/09/12/business/trevor-milton-nikola-trial.html>. This is true even though there are suspicious J coded transactions as we describe in the paper.

<sup>81</sup> Again, we obtained the Form 4s corresponding to all insider trading defendants. From August 23, 2022 to June 30, 2023, shareholders have filed 46 lawsuits that allege that company executives, while in possession of material non-public information or while perpetrating a fraudulent scheme, traded company securities.

<sup>82</sup> For example, a shareholder class action accused Nikola executives of insider trading. *See* Public Version of the Verified Stockholder Derivative Complaint, *In re* Nikola Corp. Derivative Litig., No. 2022-0023 (Del. Ch. filed Jan. 12, 2022), 2022 WL 144305. It mentions several S-trades, such as when Jeffrey Ubben (whose venture capital fund distributed Nikola stock at the best of all moments) had allegedly offloaded 1,400,000 shares on August 11, 2020, in violation of his lock-up agreement, a few weeks before the company’s fraud was disclosed. *Id.* at 29. But despite its various accusations, this complaint does not consider J-coded transactions. Nikola Corp., Statement of Changes in Beneficial Ownership (Form 4) (Aug. 13, 2020),

We likewise checked whether journalists had spotlighted suspicious J coded transactions. None had. To the contrary, respected newspapers frequently accused insiders of suspicious trading, but did not include the J coded transactions in their tallies. We mention Enron insiders in the introduction, but they are far from alone. Consider Enron's rival in perfidy, Worldcom. Bernie Ebbers was CEO of Worldcom at the time it crashed as the nation's largest financial fraud. The New York Times reported on July 3, 2002 that Ebbers hadn't sold Worldcom stock since 1996.<sup>83</sup>

The implication of such coverage was that "Bernie Ebbers was unlike the other corporate titans whose reputations have crashed in the past 18 months. He alone kept faith with the company he ran, holding on to WorldCom shares right to the end. He was a baron of bankruptcy who never bailed out."<sup>84</sup> But Ebbers was no such tragic hero. Just a few months earlier, on March 28, Ebbers had sold 3 million Worldcom shares for \$70 million dollars.<sup>85</sup> While the Times had many nasty things to say about Ebbers, this large insider trade escaped scrutiny for years – probably in large part because it was coded J.<sup>86</sup>

We likewise checked whether scholarly articles examine the profitability of J-coded transactions. We believe this Article is the first to do so, so insiders were (until now) also evading scholarly notice.

Prosecutors, plaintiffs, journalists, and scholars all overlook J-coded transactions. Almost no transaction marked "other" has ever led to adverse consequences, nor has anyone ever been punished for wrongly using the J code. These facts suggest that insiders would be wise to conceal their trades with J codes – to insider trade by other means. So is it plausible that insiders might do so? What would that look like? Those are the questions that drive the next few parts of the paper.

### III. Insider Trading by "Other" Means.

Insiders may try to conceal suspicious trades as "other" in order to avoid scrutiny. What would that look like, and is there any reason to think they actually do this? Surely, there is bound to be great variety. Yet, some patterns may emerge. This Part acquaints readers with four patterns of

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<https://www.sec.gov/Archives/edgar/data/1731289/000090266420003008/xslF345X03/ownershi p.xml>. Nevertheless, we did find one case in which the plaintiff refers to J-coded transactions. Amended Complaint at ¶¶ 178, 181, *Ng v. Berkeley Lights, Inc.*, No. 4:21-CV-09497 (N.D. Cal. filed Jul. 25, 2022), 2022 WL 4234694. It cites two investment funds distribution of stock as evidence of scienter for fraud, but even that complaint fails to address suspicious "other" filings. *Id.* at ¶181 (citing March 16 Form 4 but not March 11 Form 4).

<sup>83</sup> David Leonhardt, *WorldCom Officer Sold Almost All His Shares*, N.Y. TIMES (Jul. 3, 2002), <https://www.nytimes.com/2002/07/03/business/worldcom-officer-sold-almost-all-his-shares.html>.

<sup>84</sup> Thomas Catan & Stephanie Kirchgaessner, *How WorldCom's "Big Fraud" Began*, NAT'L POST (Canada) (Dec. 24, 2002), 2002 WLNR 8223914 (Westlaw NewsRoom).

<sup>85</sup> DENNIS R. BERESFORD, NICHOLAS DEB. KATZENBACH & C.B. ROGERS, JR., REPORT OF INVESTIGATION BY THE SPECIAL INVESTIGATIVE COMMITTEE OF THE BOARD OF DIRECTORS OF WORLDCOM, INC. 315–22 (2003), [sec.gov/Archives/edgar/data/723527/000093176303001862/dex991.htm#ex991902\\_89](https://www.sec.gov/Archives/edgar/data/723527/000093176303001862/dex991.htm#ex991902_89).

<sup>86</sup> Of course, the other challenge is that the 2002 transfer was reported in 2000, at the time that the cash was delivered.



opportunistic coding. In Part III.A., we consider transactions that are arguably miscoded. We identify widespread patterns of coding that seem to violate the best practices for coding. We surmise that insiders may not be making random filing errors – they may decide to pick a code with less legal justification that nevertheless provides superior cover against investigations.

In the next two parts, we turn away from probable miscoding to trade laundering. In II.B. we consider how insiders may distribute stock to their own upstream investors; these later investors can sell the stock without any public oversight, since they are not subject to reporting requirements. In III.C, we consider how insiders may use their influence to cause the corporation to sell them stock (or buy it back) at the moments insiders know will be the most advantageous. Finally, in III.D, we discuss how forced, or mandatory sales, classified as other, are from an economic perspective almost identical to open market sales and may involve informed trading.

For each type, we describe how the opportunistic coding works and provide an anecdotal example of the strategy in action. We do not select these examples in order to accuse the filers of misconduct.<sup>87</sup> Our goal is to help make tangible the plausibility of opportunistic coding so that the statistical proofs in the following sections do not seem abstract or implausible.

#### A. Miscoding

It is reasonable to suppose that transactions that apply an incorrect or deceptive transaction code might be more likely to exhibit other suspicious signs, such as exceptionally good timing. In this part, we consider five such coding scenarios, with suggestive examples illustrating each.

##### 1. 10b5-1 Plans

10b5-1 plans are plans that permit traders to trade, despite having acquired material, non-public information, so long as the trader has committed to the trade (or series of trades) in good faith and at a time when the trader has no such information. These plans are obviously suspicious.<sup>88</sup> An insider could trade illegally, but then concoct a fictional trading plan, after the fact, for cover. Or a trader could draft a trading plan in advance of the trade, but at a time the trader actually knows inside information. Or a trader could make numerous trading plans but cancel any trading plan that appears to be unprofitable in light of subsequently acquired non-public information. These possible abuses seem widespread and have attracted substantial scholarly and regulatory interest in recent years.

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<sup>87</sup> It is possible in each case that facts outside of the filing serve to justify the filing. Even where the filing is miscoded, it may be that the miscoding was in good faith – based on a reasonable disagreement about the law’s obligations. Even where miscoding was unreasonable, it may not have been a willful effort to subvert the law. And even where knowing misfiling occurred, it may not have been in order to conceal insider trading.

<sup>88</sup> Alan D. Jagolinzer, *SEC Rule 10b5-1 and Insiders’ Strategic Trade*, 55 MGMT. SCI. 224, 235 (2009) (noting that insiders’ trades pursuant to 10b5-1 plans, “on average, generate abnormal trade returns”). Accordingly, the SEC recently acted to constrain abusive deployment of these plans. *SEC Adopts Amendments to Modernize Rule 10b5-1 Insider Trading Plans and Related Disclosures*, SEC Press Release 2022-222 (Dec. 14, 2022), <https://www.sec.gov/news/press-release/2022-222>.

With that in mind, let us consider the 10b5-1 trading plan of Mel R. Brashears, Chairman of the Board at Irvine Sensors.<sup>89</sup> He sold 40,000 shares on April 13, 2004.<sup>90</sup> The footnote explained that this transaction was “pursuant to Rule 10b5-1 Trading Plan effectuated February 27, 2004.”<sup>91</sup> Consistent with the forgoing, Brashears trading was well-timed.<sup>92</sup> The day after his trade, the stock dropped 11%.<sup>93</sup> Three months later, the stock price had almost halved.<sup>94</sup> The cause of the drops may have been a bad mid-year results (including a 24% drop in revenues) and a dilutive equity issuance<sup>95</sup> – both of which a chairman would have known about before they were made public. Brashears earned an extra \$69,046 by selling his shares on April 13, 2004 rather than three months later.<sup>96</sup> Although it was allegedly pursuant to a plan of trading, no obvious pattern of planned trading exists for his trades.<sup>97</sup> This transaction is suspicious.

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<sup>89</sup> *Brashears, Kelly Join Irvine Sensors Board*, L.A. TIMES (Jan. 7, 2001), <https://www.latimes.com/archives/la-xpm-2001-jan-07-fi-9367-story.html>.

<sup>90</sup> Irvine Sensors Corp., Statement of Changes in Beneficial Ownership (Form 4) (Apr. 13, 2004), <https://www.sec.gov/Archives/edgar/data/357108/000118143104020464/xslF345X03/rrd39408.xml>.

<sup>91</sup> *Id.*

<sup>92</sup> *Id.*

<sup>93</sup> The price of Irvine Sensor’s stock, IRSN, at the open of trading on April 14, 2004 was \$4.34, and at the close, it was \$3.82. The stock has since been delisted from the NASDAQ, but historical prices of IRSN are available from the Center for Research in Security Prices (“CRSP”). The CRSP database is a subscription-only database that comes with a subscription to the Wharton Research Database. See *Wharton Research Data Services*, WHARTON SCH. UNIV. OF PA., <https://wrds-www.wharton.upenn.edu> (last visited Jul. 18, 2023) [<https://perma.cc/E85T-TNDX>].

<sup>94</sup> *Id.*

<sup>95</sup> *Irvine Sensors Releases Mid-Year Results*, PR NEWswire, May 7, 2004, Factiva, Doc. No. PRN0000020040507e0570073n; *Irvine Sensors Closes Private Placement Common Stock and Warrant Financing of Approximately \$2.75M*, PR NEWswire, Jun. 23, 2004, Factiva, Doc. No. PRN0000020040623e06n00501; *Final Court Approval of Irvine Sensors Class Action Settlement*, PR NEWswire, Jun. 7, 2004, Factiva, Doc. No. PRN0000020040607e06700d71. Insider trading with respect to the equity issuance was alleged by the SEC—though not with respect to Brashears.

<sup>96</sup> Brashears sold his shares for a total of \$160,246 on April 13, 2004. Irvine Sensors Corp., Statement of Changes in Beneficial Ownership (Form 4) (Apr. 13, 2004), <https://www.sec.gov/Archives/edgar/data/1195205/000118143104020464/xslF345X02/rrd39408.xml>. If he had sold them three months later on July 13, 2004, his shares would have been worth a total of \$91,200. *Wharton Research Data Services*, *supra* note 93.

<sup>97</sup> He sold 3,750 shares on February 24, 2004, which was roughly two months before the transaction in question Irvine Sensors Corp., Statement of Changes in Beneficial Ownership (Form 4) (Feb. 24, 2004), <https://www.sec.gov/Archives/edgar/data/357108/000118143104011718/xslF345X03/rrd34500.xml>. He then sold the 40,000 shares on April 13, 2004, which is the suspected insider trading. Irvine Sensors Corp., Statement of Changes in Beneficial Ownership (Form 4) (Apr. 13, 2004), <https://www.sec.gov/Archives/edgar/data/1195205/000118143104020464/xslF345X02/rrd39408.xml>. The next time that he sells any shares is on August 20, 2007. Irvine Sensors Corp., Statement of Changes in Beneficial Ownership (Form 4) (Aug. 21, 2007),



It is also miscoded. Sales pursuant to these plans are plainly reportable under S, not J.<sup>98</sup> Traders were not required to make reference to 10b5-1 plans in their trade reports until a few months ago.<sup>99</sup> They were permitted to do so, and leading commentators urged their inclusion.<sup>100</sup> The SEC considers disclosure of the 10b5-1 plan in a filing to be evidence of good faith in connection with the plan.<sup>101</sup> But a trader who wants to disclose this 10b5-1 plan information is permitted to do so on under code S, and leading commentators assert that this is the correct choice.<sup>102</sup> That is true even if the trade was somehow more complicated, like that it was executed by a broker given discretionary authority to cause the trade.<sup>103</sup> Traders accordingly miscode when they report an 10b5-1 trading plan transaction under code J.

In some cases, this miscoding may be simple error, despite the uniformity of guidance mentioned above. In other cases, it may be intentional miscoding. If a trader wishes to avoid risk for insider trading, asserting that the trade is under a 10b5-1 trading plan may help. But the trade is still a highly profitable “S” transaction, so it is going to be flagged as a suspicious sale. Applying the “other” label could help the trader avoid automatic detection as a well-timed S-trade.<sup>104</sup>

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<https://www.sec.gov/Archives/edgar/data/1195205/000118143107053352/xslF345X03/rrd170143.xml>. He has a number of transactions for stock options, but they also don’t seem to conform to a pattern.

<sup>98</sup> 1 ROMEO & DYE, *supra* note 68, at Model Form 66, Reporting Principle 16. The explanatory footnote attached to the S code in Romeo and Dye’s model form states “[t]he sales reported in this Form 4 were effected pursuant to a Rule 10b5-1 trading plan adopted by the reporting person on January 27, 2020.” *Id.*

<sup>99</sup> 1 ROMEO & DYE TREATISE AND REPORTING GUIDE, *supra* note 72, at 652. Insider Trading Arrangements and Related Disclosures, 87 Fed. Reg. 80,362, 80,409 (Dec. 29, 2022) (to be codified at 17 C.F.R. pts. 229, 232, 240, 249), 2022 WL 17981318 (requiring insiders indicate by “checkbox . . . that a reported transaction was intended to satisfy . . . Rule 10b5-1(c)(1)” and to disclose “the date and adoption of the trading plan.”). However, it remains inappropriate to code J where S (even with a footnote) will suffice. *Id.* at 80,431.

<sup>100</sup> 1 ROMEO & DYE TREATISE AND REPORTING GUIDE, *supra* note 72, at 652.

<sup>101</sup> *Id.* However, there is a division of enforcement policy as to how a 10b5-1 plan ought to be weighed in determining whether an insider acted with scienter. *Compare In re Nutrisystem, Inc. Deriv. Litig.*, 666 F. Supp. 2d 501, 518 (E.D. Penn. 2009) (stating that a defendant’s 10b5-1 plan, with which the allegedly illegal trades were in accordance, “counter[ed] any inference that the trades were made on the basis of insider knowledge.”) *with* *Indiana Public Retirement System v. Pluralsight, Inc.*, 45 F.4th 1236, 1265–66 (10th Cir. 2022) (“[T]he text and history of Rule 10b5-1 shows that such plans can be manipulated easily for personal financial gain and thus cannot rebut the inference that personal financial gain was a motive for Defendants’ material misrepresentations.”).

<sup>102</sup> 1 ROMEO & DYE, *supra* note 68, at Model Form 66, Reporting Principle 16.

<sup>103</sup> *Id.*

<sup>104</sup> As another example, Oxford Industries director Reese Lanier Sr. sold 2,500 shares on November 21, 2005 pursuant to a Rule 10b5-1 plan through an S-code. Oxford Industries, Inc., Statement of Changes in Beneficial Ownership (Form 4) (Nov. 23, 2005), <https://www.sec.gov/Archives/edgar/data/1216102/000120919105059545/xslF345X03/doc4.xml>

2. Other Trades that need an explanation.

In keeping with the previous example, a grab-bag of trades may end up in the J-code with no excuse other than that they require some explanation. Whether willful or negligent, this reasoning is plainly erroneous. Although J codes require an explanation, explanations do not require J codes. Yet J-coding may provide the trader with some strategic benefits, as an example at Nikola goes to show.

Nikola Corporation is the electric truck startup that briefly impressed the world with videos of its zooming electric truck<sup>105</sup> – surreptitiously filmed on a hill, so the inoperative truck could roll.<sup>106</sup> Nikola’s stock skyrocketed to \$28.77 billion in June 2020, based on promises of a fully functional hydrogen powered truck.<sup>107</sup>

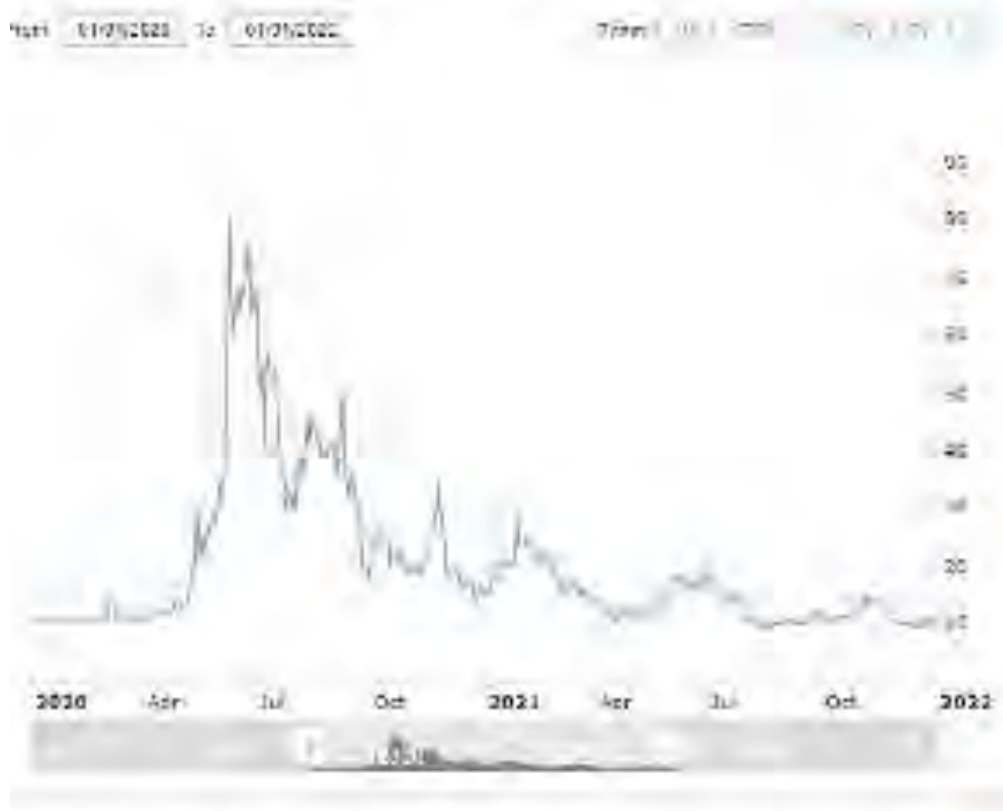
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. One and a half weeks later, Lanier made an identical transaction with an identical justification, but with the J-code. Oxford Industries, Inc., Statement of Changes in Beneficial Ownership (Form 4) (Dec. 5, 2005), <https://www.sec.gov/Archives/edgar/data/1216102/000120919105061141/xslF345X03/doc4.xml>. This inconsistent treatment suggests an error, and the migration toward the J-code suggests some sense that this code provides slightly more cover.

<sup>105</sup> For a re-upload of such a video, see Авторынок-News, *Nikola One in Motion*, YOUTUBE (Jan. 29, 2018), <https://www.youtube.com/watch?v=b5TPIjiCd5c>.

<sup>106</sup> Timothy B. Lee, *Nikola Admits Prototype Was Rolling Downhill in Promotional Video*, ARS TECHNICA (Sep. 14, 2020, 10:58 AM), <https://arstechnica.com/cars/2020/09/nikola-admits-prototype-was-rolling-downhill-in-promotional-video>.

<sup>107</sup> Ewing, *supra* note 80; *Nikola Corporation (NKLA) Interactive Stock Chart*, YAHOO FINANCE!, <https://finance.yahoo.com/quote/NKLA/chart> (last visited Jul. 8, 2023).



However, on September 10, 2020, Hindenburg Research released a report accusing Nikola of fabricating claims about its capabilities.<sup>108</sup> This report catalyzed a precipitous plummet in stock price.<sup>109</sup> By September 15, 2020, both the SEC and DOJ had begun an investigation into these claims, and Trevor Milton (founder and executive chairman) resigned from the board on September 21.<sup>110</sup> In November 2020, GM backtracked on a partnership with Nikola, and, in late July 2021, a US federal grand jury returned an indictment against Milton, saying he had lied about nearly all aspects of the business.<sup>111</sup> The closing price for Nikola’s stock on September 8, 2020

<sup>108</sup> *Nikola: How to Parlay an Ocean of Lies into a Partnership with the Largest Auto OEM in America*, HINDENBURG RESEARCH (Sep. 20, 2020), <https://hindenburesearch.com/nikola>.

<sup>109</sup> Akanksha Rana & Munsif Vegattil, *Nikola Threatens Hindenburg with Litigation, Short-Seller ‘Welcomes It’*, REUTERS, Sep. 11, 2020, <https://www.reuters.com/article/us-nikola-hindenburg-idUSKBN2621WR>.

<sup>110</sup> Matt Robinson & Edward Ludlow, *SEC Examining Nikola over Short Seller’s Fraud Allegation*, BLOOMBERG (Sep. 14, 2020, 5:26 PM), <https://www.bloomberg.com/news/articles/2020-09-14/sec-said-to-examine-nikola-over-short-seller-s-fraud-allegations>; Claire Bushey et al., *US Justice Department Inquires into Nikola Fraud Claims*, FIN. TIMES (Sep. 15, 2020), <https://www.ft.com/content/a45a6638-167b-4e27-a9fd-576e7229f959>; Charles Riley & Peter Valdes-Dapena, *Nikola Founder Trevor Milton Steps Down as Chairman in Battle with Short Seller*, CNN BUS. (Sep. 21, 2020, 3:00 PM), <https://www.cnn.com/2020/09/21/investing/nikola-trevor-milton/index.html>.

<sup>111</sup> Ben Foldy & Mike Colias, *General Motors Will No Longer Take a Stake in Nikola*, WALL ST. J. (Nov. 30, 2020, 5:20 PM), <https://www.wsj.com/articles/gm-nikola-agree-to-scaled-down->

was \$54.56; by the end of the year, on December 30, 2020, the closing price was \$15.98.<sup>112</sup> One year after Hindenburg's report, the closing price was \$9.95.<sup>113</sup>

With such a precipitous drop in stock price, anyone who knew about the company's problems would have known to sell at almost any point in the landslide. Some insiders did sell.<sup>114</sup> And some of these sales were J-coded, without any sufficient justification.

On December 3, 2020, Milton filed a Form 4 with the SEC, disposing of 2,744,543 shares in a J-coded transaction.<sup>115</sup> The footnotes explain that both of these transactions distributed shares as consideration for a previously negotiated transaction for the purchase of real estate.<sup>116</sup> The federal criminal trial of Milton shed more light on this transaction. Trevor Milton contacted Peter Hicks in March 2020 with an offer to purchase real estate.<sup>117</sup> Hicks eventually accepted Milton's offer of \$7.5 million in cash and \$7.5 million in Nikola stock call options, impressed by Milton's account of the company's growth and capabilities.<sup>118</sup> The deal closed in August 2020, when the shares were worth roughly \$40 apiece, but Hicks could not exercise the stock options until December, when the shares were worth around \$13.51 apiece.<sup>119</sup> Since the shares were worth less than the strike price of \$16.50, these shares were worthless.<sup>120</sup> Milton's late 2020 J-coded transaction is, presumably, the distribution of these shares in accordance with this real estate agreement.

Instead of simply realizing the value of the inflated shares by selling them, as would be typical with most insider trades, Milton exchanged stock options for real estate. This J-coded transaction allowed Milton to realize the value of the shares before their stock price plummeted while avoiding the scrutiny of the SEC and DOJ. However, neither the criminal prosecution of Milton nor the SEC's complaint for fraud accused him of insider trading.<sup>121</sup>

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supply-agreement-11606742652; Michael Wayland, *Grand Jury Indicts Trevor Milton, Founder of Electric Carmaker Nikola, on Three Counts of Fraud*, CNBC (Jul. 29, 2021, 4:16 PM), <https://www.cnbc.com/2021/07/29/us-prosecutors-charge-trevor-milton-founder-of-electric-carmaker-nikola-with-three-counts-of-fraud.html>.

<sup>112</sup> *Nikola Corporation (NKLA) Interactive Stock Chart*, *supra* note 107.

<sup>113</sup> *Id.*

<sup>114</sup> Jeffrey Ubben, a director mentioned in the Introduction to this Article, for example, was able to precede this drop in stock price by offloading 1,400,000 shares on August 11, 2020, in violation of his lock-up agreement. Public Version of the Verified Stockholder Derivative Complaint, *supra* note 82, at 29.

<sup>115</sup> Nikola Corp., Statement of Changes in Beneficial Ownership (Form 4) (Dec. 7, 2020), <https://www.sec.gov/Archives/edgar/data/1731289/000114036120027541/xslF345X03/form4.xml>.

<sup>116</sup> *Id.*

<sup>117</sup> Dolmetsch, *supra* note 79.

<sup>118</sup> *Id.*

<sup>119</sup> *Id.*

<sup>120</sup> *Id.*

<sup>121</sup> See Complaint, *supra* note 80; Matthew Goldstein & Niraj Chokshi, *Nikola Founder Is Charged with Fraud in Rebuke to Wall Street*, N.Y. TIMES (Jul. 29, 2021), <https://www.nytimes.com/2021/07/29/business/nikola-trevor-milton-fraud.html>.

The transaction's J-code likely helped Milton avoid scrutiny for insider trading. It was also miscoding. Milton had sold stock and should have used an ordinary S code. The fact that he may have wished to add a footnote is immaterial. One can affix footnotes to any transaction code. Milton knew this, since he affixed footnotes to other transactions on the very same Form 4, including transaction codes that do not specifically require footnoted explanations. The fact that he sold the stock for real estate is immaterial. S is the proper code for a sale of stock, regardless of the consideration one receives in return. The SEC's instructions clearly address sales for non-cash consideration – they call for the use of an explanatory footnote, but there is no hint that the J-code is appropriate.<sup>122</sup>

### 3. Gifts

There are two ways to miscode with J in gift-related contexts. First, one can use J when a G (“gift”) code is more appropriate. In general, bona fide gifts should be reported under G, rather than J. J is only appropriate for very unusual gift transactions, such as re-acquisition of stock previously “given” to a grantor retained annuity trust or charitable remainder trust.<sup>123</sup> But in general, a trader who selects “other” but then describes a gift has misfiled.

A second form of miscoding involves the use of J and a *purported* gift in order to conceal an ordinary sale. A trader willing to simply mischaracterize a sale as a gift can use the G code, but doing so is quite risky. It will often be easy to establish that no gift occurred. If the transaction is a gift, where is the gift receipt? The name for the G code is not just “gift” but “bona fide gift.” That suggests a trader is at fault for selecting G for borderline gifts. An *arguable* gift may have been a gift, but it is a *bona fide* gift? An erroneous coding of “gift” might be mere negligence, but erroneously calling a sale a bona fide gift sounds positively willful. A trader who wished to hide behind the mantle of a gift might prefer to soften the vehemence of the excuse.

Perhaps a little more wiggle room is retained when the characterization is J. A Form 4 reporting a gift by way of J-code asserts that there was a gift, but it does not claim that it was a *bona fide* gift, and there may be some suggestion that the transaction was unusual (and, hence, not obviously and willfully misfiled).

Would anyone ever misfile in these ways? Consider Escalade, Inc., a manufacturer of archery bows, trampolines, and other leisure or sporting accessories. From October 2003 to June 2004, Escalade stock price doubled from \$5.72 per share up to \$12.46 per share.<sup>124</sup> During that

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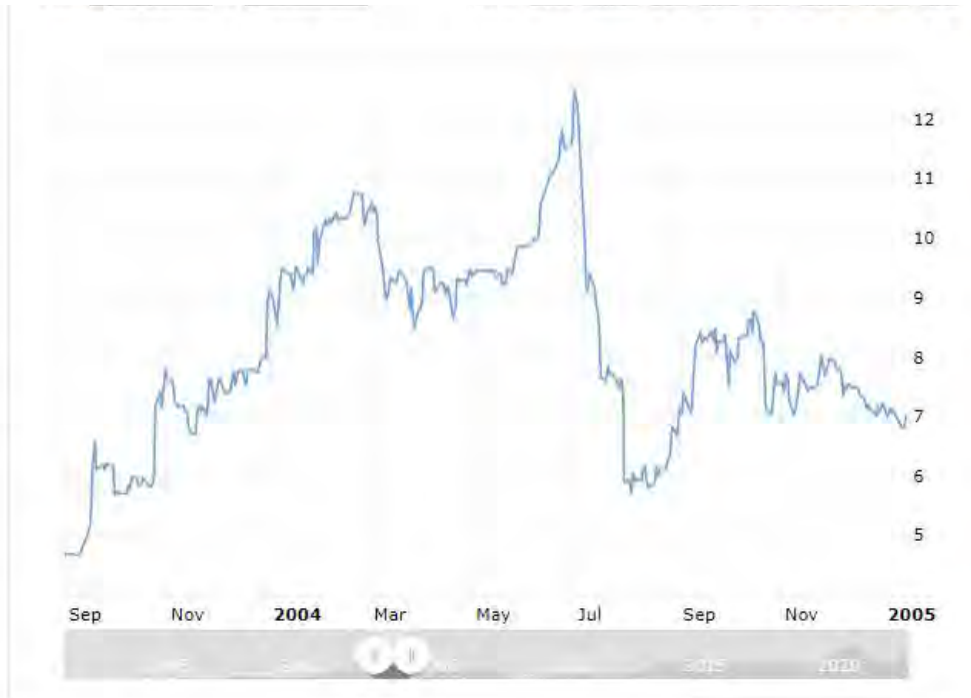
<sup>122</sup> See Statement of Changes of Beneficial Ownership of Securities (Form 4) General Instructions, *supra* note 29, at 4–5.

<sup>123</sup> 1 ROMEO & DYE, *supra* note 68, at Model Form 46, Reporting Principle 8, . Model Form 58.

<sup>124</sup> *Escalade – 31 Year Stock Price History*, MACROTRENDS, <https://www.macrotrends.net/stocks/charts/ESCA/escalade/stock-price-history> (last visited Jul. 8, 2023). This figure accounts for stock splits. Actually, the apparent price of the shares was much higher at the start of this period, but only due to an economically insignificant doubling of the number of shares on May 26, 2004. *Escalade – 31 Year Stock Split History*, MACROTRENDS, <https://www.macrotrends.net/stocks/charts/ESCA/escalade/stock-splits> (last visited Jul. 8, 2023).

window, Robert E. Griffin (an officer and director) made four J-coded dispositions of stock.<sup>125</sup> For each, the explanation offered was merely “charitable contribution.”

The stock lost its luster in July, when its quarterly earnings reported a substantial decline in net profits.<sup>126</sup>



The transactions were well-timed, and one might suspect that Griffin knew on June 3 something about the problems that the July 30 earnings report would contain.<sup>127</sup> But what kind of well-timed, suspicious transaction was it?

This might have been a genuine, if well-timed, gift. In that case, it was misfiled. Griffin offers no excuse for using the J-code instead of the proper G code. Perhaps Griffin erred. Or

<sup>125</sup> Robert E. Griffin’s J-coded transactions were reported on Oct. 3 and Dec. 12 of 2003 and Jan. 20 and Jun. 24 of 2004. *EDGAR Full Text Search*, SEC, <https://www.sec.gov/edgar/search/#/dateRange=custom&category=form-cat2&entityName=0000033488&startdt=2003-10-01&enddt=2004-06-30> (last visited Jul 14, 2023) (each Form 4 referenced above can be herein identified by the filer’s name and date of filing).

<sup>126</sup> Dune Lawrence, *Escalade, Janus, Netgear, Opnet, Suntron, U.S. Equity Movers*, BLOOMBERG LAW, Jul. 30, 2004, <https://www.bloomberglaw.com/product/blaw/document/I1O5Q01A74E9>; *Escalade Announces Third Quarter Results*, PR NEWswire (Oct. 22, 2004, 10:55), <https://www.bloomberglaw.com/product/blaw/document/I5ZQTA3TCF0H>. The prices dropped prior to the disclosure, which may suggest some leakage of information.

<sup>127</sup> The quarter ended on July 10, meaning that Griffin would have already observed about 60% of the quarterly results. Escalade, Inc., Quarterly Report Pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934 (Form 10-Q) (Jul. 30, 2004), [https://www.sec.gov/Archives/edgar/data/33488/000101905604001006/escalade\\_q.txt](https://www.sec.gov/Archives/edgar/data/33488/000101905604001006/escalade_q.txt).

perhaps he thought that G codes faced a slightly higher chance of discovery than J codes. Journalists and scholars do *sometimes* take a look at suspicious G-coded transactions.<sup>128</sup>

But it could be more interesting than that. Griffin's Forms 4s indicated non-zero disposition prices. Indeed, he seems to have received the prevailing market price in return for his gift. That is obviously atypical for a gift. Gifts typically report a disposition price of zero, because one received no consideration in return for the gift.<sup>129</sup> It is possible that this was a deeply miscoded gift, erroneously stating that he received consideration when he did not. Or perhaps the transaction was a sale, masked as an "other" transaction.

#### 4. Empty Footnotes

The simplest way to miscode is to take an ordinary sale and apply a J code instead of an S code, without any explanation or pretense justify the atypical coding. J-coded transactions are required to have such an explanation, and this requirement is one of the main constraints on J-code use. A trader can make easier recourse to this transaction code if they ignore that requirement. Perhaps surprisingly, they often do. Consider an example involving one of the world's most prominent venture capital firms.

Align Technology Inc. is a company that manufactures products to fix misaligned teeth without the use of wires or brackets.<sup>130</sup> In 2003 to 2004, more than 10% of its shares were held by Kleiner Perkins Caufield & Byers VIII LP.<sup>131</sup> Throughout these years, Kleiner Perkins disposed of many shares under the J-code without footnotes to explain their purpose. For example, on May 28, 2004, Kleiner Perkins made disposed of 1,085,816 shares in Align for \$19.06 per share using the J-code; Kleiner Perkins did not include a footnote explaining the transaction or the use of the J-code.<sup>132</sup>

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<sup>128</sup> E.g., S. Burcu Avci, Cindy A. Schipani, H. Nejat Seyhun & Andrew Verstein, *Insider Giving*, 71 DUKE L.J. 619 (2021); S. Burcu Avci, Cindy A. Schipani & H. Nejat Seyhun, *Manipulative Games of Gifts by Corporate Executives*, 18 U. PENN. J. BUS. L. 1131 (2016).

<sup>129</sup> More than half the J-coded transactions (about 63%) in our survey likewise list zero for the price or list no price at all.

<sup>130</sup> *Align Technology Files Lawsuit*, PR NEWSWIRE, Feb. 2, 2005, <https://www.bloomberglaw.com/product/blaw/document/IBBA2Z3TCF0H>.

<sup>131</sup> Align Tech. Inc., Statement of Changes in Beneficial Ownership (Form 4) (Nov. 4, 2003), <https://www.sec.gov/Archives/edgar/data/1032458/000117911003009992/xsIF345X03/edgar.xml>.

<sup>132</sup> Align Tech. Inc., Statement of Changes in Beneficial Ownership (Form 4) (June 1, 2004), <https://www.sec.gov/Archives/edgar/data/1032458/000117911004011888/xsIF345X03/edgar.xml>.



*INSIDER TRADING BY OTHER MEANS*

SEC Form 4

**FORM 4**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP**

OMB APPROVAL	
OMB Number:	3235-0287
Estimated average burden hours per response:	0.5

Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. See Instruction 1(b).

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934 or Section 30(h) of the Investment Company Act of 1940

1. Name and Address of Reporting Person <u>KLEINER PERKINS CAUFIELD &amp; BYERS</u> <u>VIII LP</u>			2. Issuer Name and Ticker or Trading Symbol <u>ALIGN TECHNOLOGY INC [ ALGN ]</u>			5. Relationship of Reporting Person(s) to Issuer (Check all applicable) Director <input checked="" type="checkbox"/> 10% Owner Officer (give title below) _____ Other (specify below) _____		
(Last)	(First)	(Middle)	3. Date of Earliest Transaction (Month/Day/Year) 05/28/2004			6. Individual or Joint/Group Filing (Check Applicable Line) <input checked="" type="checkbox"/> Form filed by One Reporting Person <input type="checkbox"/> Form filed by More than One Reporting Person		
2750 SAND HILL ROAD			4. If Amendment, Date of Original Filed (Month/Day/Year)					
(Street)	(City)	(State)	(Zip)	MENLO PARK CA 94025				

**Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned**

1. Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed Of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Common Stock	05/28/2004		J		1,085,816	D	\$19.06	2,760,260	D	

**Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned (e.g., puts, calls, warrants, options, convertible securities)**

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)		5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)		6. Date Exercisable and Expiration Date (Month/Day/Year)		7. Title and Amount of Securities Underlying Derivative Security (Instr. 3 and 4)	8. Price of Derivative Security (Instr. 5)	9. Number of derivative Securities Beneficially Owned Following Reported Transaction(s) (Instr. 4)	10. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	11. Nature of Indirect Beneficial Ownership (Instr. 4)
				Code	V	(A)	(D)	Date Exercisable	Expiration Date					

Explanation of Responses:

Susan Biglieri, Attorney-in-Fact 06/01/2004

\*\* Signature of Reporting Person Date

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

\* If the form is filed by more than one reporting person, see Instruction 4.(b)(v).

\*\* Intentional misstatements or omissions of facts constitute Federal Criminal Violations See 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

Note: File three copies of this Form, one of which must be manually signed, if space is insufficient, see Instruction 6 for procedure.

Persons who respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB Number.

This transaction was particularly well-timed. On October 21, 2004, Align announced its 3rd quarter results, reporting that its revenue and profit per share had fallen short of analysts' estimates.<sup>133</sup> Align's stock price plummeted 33% on this date, from \$14.82 to \$9.90.<sup>134</sup> By selling its shares on May 28, 2004, Kleiner Perkins made \$20,695,653. If it had waited until October 21, 2004, it would have only earned \$10,749,578.40 from this transaction. Therefore, Kleiner Perkins saved \$9,946,074.60 by selling these shares when he did.<sup>135</sup>

<sup>133</sup> Danny King, *Align Shares Fall on 3rd-Qtr Profit, 2004 Forecast, Dow Says*, BLOOMBERG (Oct. 21, 2004, 16:48) <https://www.bloomberglaw.com/product/blaw/document/I5YCGX1A74E9>.

<sup>134</sup> *Id.*

<sup>135</sup> This is not the only instance of Kleiner Perkins selling under a J-code, without any explanation, at Align. On November 10, 2004, Kleiner Perkins made a disposal of 1,267,839 shares in Align for \$11.12 per share using the J-code. Align Tech. Inc., Statement of Changes in Beneficial Ownership (Form 4) (Nov. 11, 2004),



Why omit an explanation? Perhaps because Kleiner Perkins lacked any justification and feared that a true explanation (that there is no explanation) would increase the risk of detection and prosecution for misfiling and insider trading. The insider might have fabricated an explanation, but any untrue explanation might later be falsified by prosecutors, in such a way as to generate proof of willful fraud.

Yet, filers are required to explain their use of the J-code. The official name of the J code selection is “Other acquisition or disposition (describe transaction).” A trader plainly must describe the transaction. And SEC guidance repeatedly concurs with this commonsense observation. The law provides no justification for blank footnotes, nor do any secondary sources advise the absence of explanation.<sup>136</sup> Anyone who selects “J” without providing an explanation has misfiled, in that their J-filing was not handled properly, and many such filers may have been improper in selecting

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<https://www.sec.gov/Archives/edgar/data/1032458/000117911004021188/xslF345X03/edgar.xml>

1. On January 26, 2005, Align announced its 4th quarter results. *Align Technology, Inc. Reports Revenues of \$43.7M for Q4 2004*, PR NEWswire, Feb. 2, 2005, [https://www.bloomberglaw.com/product/blaw/document/IXDHB3TCF0J?criteria\\_id=9b520fb2f894438c94909d3c367e347b&searchGuid=ef5c7b37-18df-4713-b8a9-ca8173e1fce7](https://www.bloomberglaw.com/product/blaw/document/IXDHB3TCF0J?criteria_id=9b520fb2f894438c94909d3c367e347b&searchGuid=ef5c7b37-18df-4713-b8a9-ca8173e1fce7). They were poor, showing lower sales than the previous year. *Id.* These results coincided with a drop in stock price, with the stock opening at \$10.26 on January 24, 2005 and closing at \$7.99 on January 31, 2005. *Align Technology, Inc. (ALGN) Interactive Stock Chart*, YAHOO FINANCE!, <https://finance.yahoo.com/quote/ALGN/chart> (last visited July 24, 2023). More significantly, on February 3, 2005, news broke that OrthoClear Holdings Inc., a competitor of Align, had poached 10% of Align’s sale force. Laure Edwards, *Amazon.com, FEI, Fluor, Labor Ready, Maytag: U.S. Equity Movers*, BLOOMBERG (Feb. 3, 2005, 15:00), <https://www.bloomberglaw.com/product/blaw/document/IBCQ8C1A74E9>. Contemporaneously, Align also filed a lawsuit against OrthoClear alleging that it had stolen Align’s trade secrets and intellectual property. *Id.* On this news, Align’s stock fell 71 cents to \$7.99. *Id.* Kleiner Perkins earned \$14,098,369.70 from its transaction. On the other hand, if it had sold its shares on February 3, 2005, it would have only earned \$10,130,033.60. Therefore, Kleiner Perkins saved \$3,968,336.10 by selling its shares when it did.

<sup>136</sup> Interestingly, among the hundreds of fictional examples of filings printed in practitioner guides, we were able to discover exactly four instances in which a J code was reported without any explanation. See 1 JACOBS, *supra* note 33, § 8:15; 1 *id.* § 8:41; ROMEO & DYE DESKBOOK, *supra* note 72, at 353; 2 ROMEO & DYE, *supra* note 68, at Model Form 100. However, it is not natural to infer that these sources endorse a blank form in these cases. For one thing, such an endorsement is plainly incompatible with nearby writings. For example, with respect to one of these explanation-lacking forms, the authors write, “... the insider could use transaction code ‘J’ (‘Other acquisition or disposition,’ *with a footnote explanation*) to report the option grant. [The Insider] has reported her option grant using transaction code ‘J’ and has explained the transaction in a footnote.” *Id.* (emphasis added). It seems plausible that the authors omitted the explanation because they wished to focus the reader on some other aspect of the form that they were highlighting. It is perhaps equally likely that the explanations were omitted erroneously.