Whitehorse Executive Center
1255 Whitehorse Mercerville Road
Building B, Suite 514
Trenton, NJ 08619
T 609-890-3185 F 609-581-8244

March 30, 2022

Vanessa A. Countryman, Esq.
Secretary
Securities and Exchange Commission
100 F Street NE
Washington DC 20549-1090

RE: Affirmative defense provisions of Rule 10b5-1; Proposed Rule (File Number S7-20-21)

Dear Ms. Countryman:

On behalf of BioNJ's 400 research-based life sciences companies, academic institutions, and other stakeholder Members, we thank you for the opportunity to comment on the Securities and Exchange Commission's proposed rule to amend Rule 10b5-1 under the Securities Exchange Act of 1934, published in the Federal Register on February 15th, 2022 (87 Fed. Reg. 8686).

BioNJ is New Jersey's largest life sciences trade association, representing our State's premier biopharmaceutical firms as well as emerging companies, patient advocacy organizations, academic research institutions, and those that support them. Discovering, developing, and delivering access to groundbreaking and lifesaving patient cures is the mission of our membership – Because Patients Can't Wait®. With its strong academic infrastructure and significant life science company presence, New Jersey has long served as a robust incubator of emerging biopharmaceutical companies. As a result, New Jersey is home to well over 3,000 life sciences establishments, and a significant percentage of all FDA-approved drugs in recent years were developed by biopharmaceutical companies with a footprint in New Jersey.

The path from academic lab to patients requires significant capital, prompting most successful emerging growth biopharmaceutical companies to enter the public markets before they are cash-flow positive or even have a commercial product on the market. These companies must manage the high costs of research and development while attracting top talent, and a primary component of this is equity compensation. When cash is constrained, our member companies use their equity to attract and retain the specialized workforce on which the life sciences industry depends. A key requirement for this approach is a well-defined framework that allows companies to provide meaningful equity compensation and at the same time allows employees reasonable opportunities to benefit from their efforts and realize the gains they have created in their company's stock price. While we generally support the Commission's efforts to clarify the conditions for the affirmative defense offered by Rule 10b5-1 plans, we wish to bring to your attention some important information about how 10b5-1 plans are used in practice by our members and to request you to consider amending the proposed rule to avoid potential unforeseen consequences of the rule as drafted.

Companies in the life sciences industry typically offer both stock options and restricted stock awards or units as part of their equity compensation programs, in each case vesting over time (annual vesting over a four-year period is common). Unlike stock options, restricted stock is taxable at the time of vesting, and state and federal taxes on any gain must be withheld by the employer and promptly paid to the government. Because the restricted stock vesting event by itself does not generate any free cash, another way must be found to fund the tax withholding obligation. Many emerging growth and early stage public companies rely on a "sell-to-cover" program. Under this program, the employee, at the time of the grant and as a condition of the grant, enters into a binding agreement with the company under which, upon a vesting event for the restricted shares, enough are sold to cover the appropriate withholding amounts. At the same time, the employee enters into an automatic sale instruction with a broker that authorizes both the sale of the appropriate amount of shares and the remittance of the proceeds to the employer to fund the withholding payment. Taken together, the binding contract with the employer and the written instruction to the broker are intended to create a trading arrangement consistent with the affirmative defense to liability under Rule 10b5-1(c). The form of the sell-to-cover instruction, which the employee signs as of their acceptance of the grant, typically includes an explicit reference to this fact.

Upon each vesting event, a broker (often under contract with the company to provide the overall infrastructure to manage equity grants to employees), on behalf of the employer and in accordance with the employer's calculations for each employee, sells the number of shares necessary to cover the withholding amount on the open market and remits the resulting funds to the employer for that purpose. Importantly, the employee has no involvement or discretion with respect to the calculation of the number of shares "sold to cover." An important benefit of this approach is that the affirmative defense under Rule 10b5-1(c) allows the sale-to-cover to proceed on the vesting date regardless of the employee's possession of material nonpublic information as of that date.

One of the Commission's proposed new conditions to the rules for 10b5-1 plans would restrict multiple overlapping Rule 10b5-1 plans, and another would limit the use of single-trade plans. However, under the proposed amendment, sell-to-cover trading arrangements could be viewed as overlapping plans, and even single-trade plans, and therefore not be entitled to the Rule 10b5-1 plan affirmative defense. This is because given an annual vesting cycle and standard four year vest, there will typically be four or more sell-to-cover orders in place for many employees at any given time, each representing a distinct vesting event for a specific grant. This, of course, is over and above any 10b5-1 plan the employee may have for personal diversification purposes. The Commission's proposed amendments could be read to limit and perhaps even eliminate the use of the sell-to-cover approach for tax withholding because of the prohibition on multiple simultaneous plans and because each sell-to-cover order could be viewed as a single-trade plan. There is little justification for this outcome. These programs do not present the opportunity for insider trading because the vesting dates, and therefore the sell-to-cover dates, are established at the time of the grant by the company, typically at least a year in advance of the first vesting date, and there is no employee discretion as to the sale itself or the number of shares sold.

We urge the Commission to consider creating an explicit exception in the final rule to allow for sell-to-cover programs for restricted stock grants. This exception could include language specifically exempting mandatory sell-to-cover trading arrangements from the counting of overlapping plans, and to the extent applicable from the definition of single-trade plans. The exemption could be drafted to require that any sell-to-cover trading arrangements be formally adopted as a "binding contract" by the employee in connection with acceptance of the grant and require that the company (not the employee) calculate the amount of the applicable tax withholding (and therefore the number of shares to be sold by the broker).

It is worth noting that there are other cases where use of multiple overlapping or single-trade plans is legitimate. For example, a sell-to-cover approach is sometimes used where companies require executives to exercise stock options and hold the resulting shares to meet ownership requirements. In this case, the exercise itself may also generate an immediate tax withholding obligation, and a sell-to-cover approach with an automatic sale instruction for a portion of the shares from the exercise is often required by companies to generate the necessary cash. This type of trading arrangement might well be a contained in a separate document from a 10b5-1 plan for personal diversification purposes, causing the employee to run afoul of the limitation on overlapping plans in the proposed amendments. Another example is the case of employee stock purchase plans, where employees often wish to purchase shares through the ESPP and immediately sell them to lock in the discount from the public price that these ESPPs provide. While this might be viewed as a single-trade plan, it clearly does not present the issues that have been raised generally with respect to such plans. The Commission may wish to consider drafting any exemption to the multiple overlapping plan and single-trade plan conditions to cover these other circumstances.

In the absence of an explicit exception, the proposed amendment to Rule 10b5-1(c) would restrict or eliminate the ability for companies to have sell-to-cover programs. These companies would then need to fund the tax withholding obligations that become due upon vesting of restricted stock (or the other circumstances we described above) with their own cash, whether by netting off shares from the vesting event or grossing up the employee. This is because in most cases, particularly in a successful startup company where significant stock price appreciation has occurred, the employee will not have the liquidity to cover the withholding obligation. The company's ability to arrange for any extension of credit to an executive employee to cover the withholding obligation is severely limited by the Sarbanes-Oxley Act of 2002 and, even if in some carefully engineered scenarios theoretically allowable, involves both administrative complexities and market risk. Sell-to-cover programs are intended to conserve a startup or early-stage public company's cash and taking away this type of program will cost these companies funds and other resources that could be put to better use.

Finally, we also urge the Commission to explicitly provide for a transition process for existing Rule 10b5-1 plans (whether under sell-to-cover programs or for personal diversification purposes) that exist as of the effective date of the proposed amendments. Without clarity on whether and to what extent existing plans are grandfathered, employees and companies will be forced to make difficult decisions about early plan termination and (for sell-to-cover plans) tax and withholding issues that cannot easily be addressed. The unusually short comment period for the proposed rulemaking also mitigates in favor of clear guidance for companies and their employees on the treatment of Rule 10b5-1 plans that are currently in effect.

BioNJ appreciates the Commission's consideration of our comments. We encourage the Commission to modify the proposed rule to avoid the potential unforeseen consequences we have described above with respect to use of Rule 10b5-1 plans by our members and their employees.

Thank you again, Secretary Countryman, for the opportunity to comment on the Commission's proposed rule. Please do not hesitate to contact me at DHart@BioNJ.org or 609.890.3185 should you have any questions. In addition, we are prepared to make available representatives of our membership to discuss specifics of the potential impact of the proposed rule on them and their employees.

Sincerely,

Debbie Hart
President and CEO