HudsonWest LLC

March 31, 2022

Ms. Vanessa A. Countryman, Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Rule 10b5-1 and Insider Trading; File No: S7-20-21

Dear Ms. Countryman:

HudsonWest LLC ("**HudsonWest**") appreciates the opportunity to comment on the above-referenced proposed amendments to Rule 10b5-1 under the Exchange Act (the "**Proposal**")[1]. HudsonWest is a registered broker-dealer that advises corporate issuers on equity-linked solutions, including structured share repurchases such as accelerated share repurchases ("**ASRs**"). HudsonWest appreciates the detail the Securities and Exchange Commission (the "**Commission**") has given to the Proposal regarding 10b5-1 plans entered into by officers and directors but would like to comment specifically on the impact these amendments would have on repurchases of stock by issuers, in particular with respect to ASRs.

An ASR is a contract that an issuer enters into opposite one or more financial institutions (or "**dealers**") that allows the issuer to repurchase and retire its shares on an "accelerated" basis. Typically, at inception of the ASR, (1) the issuer will prepay the full notional amount of the contract (i.e., the full value of shares the issuer is targeting to repurchase) to the dealer, and (2) the dealer will deliver a number of shares to the issuer with a notional value slightly less than the prepayment amount (typically, 70-90%). The dealer gets these shares by borrowing them from third parties, thus creating an open short position.

Over time, the dealer will purchase shares in the open market to cover its short position – though, as ASRs are principal trades and not agency trades, it is under no contractual obligation to do so. At maturity, the parties will determine the true underlying number of shares by reference to the volume-weighted average price of the stock over the life of the ASR (less a pre-agreed discount) and will then determine the final number of shares to be settled by the parties.

Typically, but not always, the dealer can elect a maturity date between a pre-agreed minimum maturity and maximum maturity. That election provides the dealer with the economic equivalent of owning a put option with a floating strike price. The dealer "pays for" that option by offering the issuer a lower price for its purchases – which is where much of the pre-agreed discount is derived from. As with any option, the higher the underlying stock's volatility, the higher the value of the option, and therefore the higher the pre-agreed ASR discount.

The Proposal indicates that, based on a recent study[2], a small minority of share repurchase activity is done via an ASR – just 12% as of 2014.[3] While the Commission's referenced study indicates that the full scale of issuer repurchases and ASRs are difficult to quantify[4], ASRs are an important tool used by corporates to manage their share repurchase operations[5]. And while the Bonaimé et al. study did indicate that just 12% of share repurchases

[1] Rule 10b5-1 and Insider Trading, 87 Fed. Reg. 8686 (Feb. 15, 2022).
[2] Alice Bonaimé, Jarrad Harford, and David Moore, Payout Policy Trade-Offs and the Rise of 10b5-1 Preset Repurchase Plans, 66(6) Management Science, 2762-2786 (2020).
[3] Proposal, note 170, at 8710.
[4] *Id.* at 8705. HudsonWest appreciates the Commission's goals in data collection and disclosure of share repurchases and believes that such proposals, generally, will be helpful in evaluating the overall size of the repurchase market.
[5] In 2022 alone, for example, several firms have publicly announced ASRs with notional amounts in the billions of dollars each. *See*, *e.g.*, https://www.sec.gov/ix?doc=/Archives/edgar/data/64040/000006404022000061/spgi-20220302.htm (S&P Global - $7 billion ASR), https://www.businesswire.com/news/home/20220209005341/en (Bristol Myers Squibb - $5 billion ASR), https://www.prnewswire.com/news-releases/stanley-black--decker-announces-2-0-billion-accelerated-share-repurchase-program-301494495.html (Stanley Black & Decker - $2 billion ASR) and https://www.prnewswire.com/news-releases/twitter-inc-announces-2-billion-accelerated-share-repurchase-agreements-301480607.html (Twitter - $2 billion ASR).

in 2014 included an ASR component based on their data, the relative size of the ASRs studied show the importance of ASRs: In their sample, the researchers noted the studied ASRs had a mean size of $602 million, over ten times the mean size of pure 10b5-1 plans ($56 million). Therefore, while the number of ASRs was smaller, the dollar volume repurchased under ASRs was much higher. More recent data published highlights the growing importance of ASRs.[6]

We believe that several aspects of the Proposal would have unintended negative consequences on the ASR market and would not address the Commission's concerns about "abuse of the rule to opportunistically trade securities on the basis of material nonpublic information in ways that harm investors and undermine the integrity of the securities markets,"[7] "traders [taking] advantage of the liability protections provided by the rule to opportunistically trade securities on the basis of material nonpublic information"[8] or issuers entering into "trading arrangements that are terminated shortly after adoption."[9]

We respond to the Commission's request for comments from the standpoint of the ASR market exclusively.

1. Is the proposed cooling-off period an appropriate condition to the Rule 10b5-1(c)(1) affirmative defense for contracts, instructions and written plans? Would a cooling-off period effectively reduce the potential to abuse the rule, such as from selective termination of trades?

We do not believe that a cooling-off period is an appropriate condition to the Rule 10b5-1(c)(1) affirmative defense for ASRs. The Commission should exclude from the cooling-off period rule repurchases of shares by issuers not on an agency basis (or should reference ASRs specifically). For one, ASRs are always executed in open trading windows when the issuer does not have any material non-public information ("**MNPI**") about itself or its shares, and issuers are uniformly required to give a "no MNPI" representation to the dealer. Issuers are unable to abuse the affirmative defense at the time of entry into an ASR, as issuers have no material knowledge of any MNPI at the time they are entering into a contract to repurchase their shares.

A cooling-off period similarly would not reduce any abuse of the rule from selective termination of an ASR, as ASRs are almost never cancelled, owing to the fact that a termination of an ASR is an incredibly costly decision by an issuer. This termination cost would be high because the dealer would need to unwind its hedge positions with respect to the ASR, and because the issuer would be subject to a termination amount of the contract calculated by the dealer (most often using a pricing methodology favorable to the dealer and at the discretion of the dealer).

An ASR is typically structured such that the dealer's trading (or the presumption of trading, as the dealer is not required to engage in any trading per the contract) happens immediately following signing of the contract. This feature is integral to the ASR for two reasons.

First, ASRs are typically priced by dealers by referring to an issuer's share price volatility. The higher the volatility, the more valuable the contract is to the dealer (who has effectively purchased a floating-strike put option in the ASR). As dealers price ASRs by bidding a volatility level as of the trade date of the ASR, freezing dealers out of the market for 30 days (or any period of time) following execution of the ASR will require that dealers transact based on their best guess of volatility 30 days (or such relevant period of time) in the future. Because volatilities in the market and with respect to a particular issuer can change rapidly over days and weeks[10], dealers will be inclined to bid conservative (lower) volatilities, as they will (rightfully) want to protect themselves against a trading loss: Dealers in the ASR business are not in the business generally of taking risks; they generally mostly or fully hedge their exposures under ASRs and manage trading risks through sophisticated algorithms that attempt to minimize any potential losses as a result of the dealer offering the shares at a discount to the volume-weighted

[6] *See* US companies buy back shares in record volumes. "[In 2022, C]ompanies have publicly announced more than $33bn of so-called accelerated share repurchases." https://www.ft.com/content/e27975fc-a4f6-4e71-9ac8-af8a2418caca.
[7] *Id.* at 8686.
[8] *Id.* at 8688.
[9] *Id*. at 8689.
[10] For example, volatilities greatly increased in the market following Russia's recent invasion of Ukraine.

average price. These lower volatilities will result in smaller discounts for issuers, less efficient transactions for issuers' shareholders and more profits for dealers' trading desks[11].

Second, as the dealer must borrow a large number of shares of stock at inception for purposes of hedging its risk under the transaction and making the initial delivery of shares to the issuer, and as the stock borrow markets are real-time markets, starting the ASR immediately is important for efficient pricing and execution, so that the issuer has relative certainty that the initial delivery of the shares is going to be made, and so that the issuer can analyze whether the stock borrow markets for that issuer's shares are liquid and available at a low cost. Issuers are generally required under ASRs to shoulder the cost of any increased costs of the dealer's stock borrowing; if issuers do not have accurate real-time information as to their stock borrow costs on the date on which the initial shares under the ASR are delivered, they will have less certainty as to the overall costs and benefits of the contract.

If, in fact, the cooling-off period applies to ASRs, we could see situations in which ASRs are more likely cancelled than under the current regime, as the "forward starting" nature of these ASRs would allow issuers a lower-cost cancellation option during the cooling-off period because trading activity by the dealers would not have yet started and the breakage costs would be minimal. An issuer could effectively bet on its volatility declining from the execution date of an ASR to the first trading date of the ASR – if its volatility increased during the cooling-off period, it could cancel its ASR, at it would be beneficial to attempt to transact at the new, higher volatility; if its volatility decreased during the cooling-off period, it could allow its ASR to run as planned, as the issuer would be able to capture the benefit of the artificially better pricing received. Given this, we would further expect dealers to price their ASR discounts more conservatively – and, conceivably, some dealers would exit the ASR market entirely.

Given these outcomes, we believe that with the cooling-off period in effect, ASRs would no longer be attractive repurchase options for certain issuers[12]. An issuer's decision on whether to execute an ASR (whether in place of, or alongside, a standard open-market repurchase program or 10b5-1-based plan) would be materially altered by the Proposal – not in a way that would "support the integrity of the securities markets," but rather through unintended consequences of the Commission's rulemaking proposals chiefly focused on insider sales of securities.

5. Is the proposed 30-day cooling off period appropriate for issuers? Would a different period be more appropriate? For example, would a 60-day, 90-day, or 180-day cooling off period be more appropriate for issuers relying on the 10b5-1(c)(1) affirmative defense? If issuers were subject to the proposed requirements, how would their use of Rule 10b5-1(c)(1) trading arrangements to conduct share repurchases be affected? Would the proposed cooling-off period affect existing practices regarding when a repurchase window is "open" or "closed"?

Please refer to our response to question 1 above.

13. Are there legitimate uses of multiple, overlapping Rule 10b5-1 trade arrangements? If so, what are they? Is it appropriate to exclude from the affirmative defense multiple concurrent trading arrangements for open market purchases or sales of the same class of securities as proposed? Would the proposal create incentives for corporate insiders to own different classes of stock? Are there alternative approaches to addressing the concerns with multiple trading arrangements discussed above?

There are entirely legitimate uses of multiple, overlapping Rule 10b5-1 trade arrangements in the context of issuers repurchasing their shares through (1) multiple ASRs transacted simultaneously with multiple dealers, (2) multiple "tranched" ASRs transacted simultaneously with a single dealer and (3) one or more ASRs transacted simultaneously with one or more Rule 10b5-1-based open-market repurchase plans.

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[11] As with any uncertain situation, we would expect that dealers would not only bid more conservatively due to uncertainty in future volatilities, but that they would also build in an extra "uncertainty cushion," so as properly manage risks, receive internal trading and risk approvals and account for potential costs of hedging volatilities during the cooling-off period.

[12] However, should the Commission's proposal on share repurchase disclosure (Share Repurchase Disclosure Modernization, 87 Fed. Reg. 8443 (Feb. 15, 2022). HudsonWest has also prepared a separate comment letter on these proposals) result in onerous disclosure environments for issuers for non-ASR repurchase activities, HudsonWest believes that the relative benefits of an ASR from an administrative perspective could, in fact, outweigh the worsened economics of an ASR, leading to an increase in ASR activity relative to other types of share repurchases.

Multiple ASRs transacted with multiple dealers is a strategy used extensively by issuers, often to increase competition and efficiency in counterparty pricing and to diversify counterparty risk[13]. These ASRs are structured carefully with counsel to ensure that only one dealer is in the market purchasing shares under the ASR in connection with the ASR execution, and they otherwise behave like traditional ASRs entered into with a single dealer counterparty. We see no reason why these types of arrangements should be prohibited by the Commission, as they are not a source of market abuse and merely seek to afford issuers the opportunity to divide their ASR between multiple counterparties.

"Tranched" ASR structures offer benefits to certain issuers who wish to improve pricing[14] on their ASRs by offering to transact with a dealer on several alternating-day ASRs as opposed to a single every-day ASR. In practice, these transactions would be prohibited by the Proposal, even though they, like the multiple ASRs referenced in the paragraph above, are essentially equivalent to a vanilla ASR and do not result in any market abuse.

Finally, we routinely advise issuers on the benefits and drawbacks of ASRs as compared to various other share repurchase strategies, including traditional 10b5-1 plans. Often, issuers like certain features of ASRs:

- the ability to receive an up-front initial share delivery;
- the ability to repurchase shares at a discount; and
- the ability to commit to a fixed-dollar amount of shares to repurchase over a period,

but do not like other features of ASRs:

- the inflexibility of the ASR as compared to traditional Rule 10b5-1 plans or other open-market repurchases;
- the fact that issuers may have been better off with another repurchase strategy if volatilities increase during the ASR; and
- the fact that issuers may be unable to continue share repurchases if their ASR is called early by the dealer and they are not in an open trading window to put on a new repurchase plan.

A way for issuers to mitigate those risks is to diversify their share repurchase strategies and enter into a "side-by-side" 10b5-1 plan under which the issuer repurchases shares during the ASR period but is not subject to the same consideration as an ASR. These plans, together with the ASR, are thought through carefully with counsel to ensure that purchases of shares are made by a single dealer on a single day. In addition, dealers will require that the ASR size and tenor, which are in practice guided by Rule 10b-18 volume limitations, take into account the potential open-market activity and be adjusted with Rule 10b-18 in mind. Again, we see no reason why these arrangements should be prohibited by the Commission – they are legitimate, risk-mitigating contracts entered into by issuers and are in no way an attempt to harm investors, undermine the integrity of the securities markets or opportunistically trade on the basis of MNPI.

14. Is the proposed amendment sufficiently clear as to what types of overlapping trading arrangements a trader can maintain, while still preserving the availability of the 10b5-1(c)(1) affirmative defense? If not, how could additional clarity be provided? In particular, how would the proposed exclusion affect current practices with respect to tax qualified retirement savings plans, and tax withholding transactions with respect to equity compensation arrangements, such as stock options and restricted stock units?

Please refer to our response to question 13 above.

15. Is it appropriate to limit the availability of the Rule 10b5-1(c)(1) affirmative defense for single-trade plans as proposed? If not, are there alternative approaches to addressing concerns about the potential abuse of single-trade plans? Would the proposed cooling-off periods sufficiently mitigate the potential to misuse single-trade plans to execute trades based on material nonpublic information? Alternatively, would the limited availability of the Rule 10b5-1(c)(1) affirmative defense for single-trade plans as proposed still allow for potential abuse? Should we consider prohibiting the use of single-trade plans entirely?

[13] As ASRs are prepaid contracts, issuers take credit risk with respect to their dealer counterparty.
[14] This improved pricing is achieved through improved optionality on the dealer's end – essentially, the dealer's ability to call the ASR early is enhanced through these "tranched" structures.

Under an ASR, which is a principal trade by the dealer, there is no actual required trading activity by the dealer. We therefore do not believe that an ASR would qualify as a "single-trade plan." However, we would ask the Commission to clarify that ASRs would not fall under the proposed definition.

21. Would the disclosures in proposed Item 408(a) provide useful information to investors and the markets? Does the proposed disclosure requirement specify all of the information that should be disclosed as to registrants' trading arrangements? Does the proposed disclosure requirement specify all of the information that should be disclosed as to trading arrangements of officers and directors? Are there other disclosures that we should require that would provide more transparency into the use of Rule 10b5-1 and non-Rule 10b5-1 trading arrangements? Is there any information that we have proposed to require be disclosed that we should not require? We are proposing disclosure about trading arrangements both for registrants and for officers and directors. Should we instead require disclosure about only one of those categories of traders? Should we consider requiring disclosure of trading arrangements of insiders who are not officers or directors? If so, at what level of specificity?

If the Commission requires the "material terms" disclosure to include pricing parameters of ASRs, bad actors would have information necessary to front-run dealers' activities under ASRs, which would lead to an undermining of the integrity of the securities markets and inefficient and worse pricing for issuers in their ASRs. We would request that the Commission clarify that these disclosures, if adopted, would not require issuers to disclose any pricing information in ASRs (including, but not limited to, the discount and the minimum and maximum maturity dates).[15]

22. Would a description of the material terms of a trading arrangement encourage front-running of trades under the trading arrangement? Should the required disclosures be limited to particular terms of a trading arrangement?

Please refer to our response to question 22 above. However, yes, we believe front-running of ASRs would be a widespread and destructive feature of these disclosures.

We very much appreciate the opportunity to comment on the Commission's Proposal. Members of HudsonWest would be happy to discuss any of our comments with the Commission in further detail. Any inquiries can be directed to barry.gewolb@hudson-west.com.

Yours truly,

HudsonWest LLC

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[15] We would note that the public disclosure of ASRs is generally fulsome, typically indicating: (1) the total notional amount of the ASR, (2) the number of shares the issuer expects to receive as an initial delivery, (3) the maximum maturity of the ASR and (4) that the final price at which the issuer repurchases shares under the ASR will be calculated over an averaging period and will equal the arithmetic average of the volume-weighted average prices of the shares over the averaging period, less a discount. Other repurchase plans do not carry the same level of disclosure (and are not typically publicly announced at their execution). Moreover, the ASR contract is often filed by an issuer with the Commission on Form 8-K, whereas the same cannot be said for typical agency repurchase plans.