



Forensic Focus on COVID-19

Insider trading risk in the wake of COVID-19: An alert to boards and audit committees

Deloitte's Forensic series around COVID-19 business impacts and steps you can proactively take to help respond to and recover from the outbreak and mitigate potential fraud and financial crime risks.

Recent accusations of “stock dumping” raise questions about whether those made privy to nonpublic material information during times of crisis have placed their personal financial interests ahead of those of the investing public or their companies, potentially violating insider trading laws.

The Securities and Exchange Commission (SEC) requires that any director, officer, or beneficial owner of a registered company file a Form 4 (Statement of Changes in Beneficial Ownership) with the SEC at any time a transaction resulting in a change in beneficial ownership has been executed.¹ The filings documenting execution of these transactions are easily accessible by the general public via the SEC's online Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system.²

The Market Abuse Regulation (MAR)³, in Europe, with the Commission Implementing Regulation (EU) 2016/347 of 10 March 2016, and in France,

the « Code Monétaire et Financier »⁵ along with the Autorité des Marchés Financiers (AMF)⁶ set guidelines, regulate and enforce sanctions on insider trading. In France, the filings of changes of beneficial ownership are available via the AMF database: Base des décisions et informations financières (BDIF)⁷.

The Wall Street Journal recently examined more than 4,000 public company SEC filings and reported that top executives of SEC registered companies sold approximately \$9.2 billion worth of shares in their own companies from February 1, 2020, through March 19, 2020, resulting in approximately \$1.9 billion in savings.⁸ This activity apparently drew the SEC's attention, where in early March 2020, it issued a press release stating that “where a company

has become aware of a risk related to the coronavirus that would be material to its investors, it should refrain from engaging in securities transactions

with the public and to take steps to prevent directors and officers (and other corporate insiders who are aware of these matters) from initiating such transactions until investors have been appropriately informed about the risk.”⁹

The SEC's Division of Enforcement weighed in as well in a March 23, 2020, release in which it emphasized that corporate insiders privy to new material nonpublic information on the outbreak “should be mindful of their obligations to keep this information confidential and comply with the prohibitions on illegal securities trading.” The release further referenced the Division of Enforcement's commitment to “ensuring that our Main Street Investors are not victims of fraud or illegal practices in these unprecedented market and economic conditions.”¹⁰

While the legal analysis as to whether specific trading violated securities laws is often complex, factual questions regarding the timing of trades, whether and to what extent

nonpublic material information was available and disseminated prior to trading and to whom, the potential impact of such information to a company's financial condition and share price, and consistencies or inconsistencies between internal and public communications prior to and after trading activity—as well as other issues—will need to be resolved prior to legal determinations on the propriety of the trades.

In light of publicly disclosed trading activity and the recent SEC releases, boards of directors and audit committees, as well as legal and compliance departments of companies impacted by COVID-19, should assess whether trades made by insiders require additional scrutiny and/or investigation. Potential “red-flag” transactions will require prompt attention to determine the propriety of the trades, as such transaction may well give rise to regulatory inquiries and potential shareholder litigation.

Deloitte Forensic possesses the experience and capabilities to assist attorneys and companies in conducting proactive and reactive investigations into such matters, including utilizing digital forensics to electronically collect, preserve, and analyze structured data (such as financial and accounting data) and unstructured data (such as emails and texts). Our digital capability also enables us to initiate or continue performing key investigative tasks remotely in an efficient and cost-effective manner. While the investigative requirements will differ for each investigation, the following tasks should be considered when conducting insider trading reviews or investigations:

1. Identification of key personnel:

Identify all directors, officers, and beneficial owners required to file the form with the regulator (SEC, AMF..) any time a transaction resulting in a change in beneficial ownership is executed.

2. Timeline and market analysis:

Establish a COVID-19 timeline of events, including general market conditions and events (for example, imposition of travel bans, timing of the first cases reported in specific countries, and specific stock market drop dates), as well as conditions and

events specific to the company (such as internal and external discussions around closure of certain operations, announcement of layoffs, and impact of COVID-19 on business operations). The analysis should take into account the information being shared and discussed internally, with that of public statements made by the company on social media, in press releases, and in regulatory filings.

3. Review of company documents:

Obtain and review relevant company documentation, including (but not limited to) meeting minutes, policies and procedures, and preestablished stock sales plans to identify additional events that should potentially be considered and included in the timeline and market analysis.

Such a review could result in identification of (i) disclosure of nonpublic material information in meeting minutes, (ii) preestablished insider “blackout periods” documented in insider trading policies, and (iii) preestablished executive stock sales plans.

4. Transactional review and analyses:

Obtain and aggregate historical buying and selling data from Form 4 issued with the SEC for the last two to three years for directors, officers, and beneficial owners. Employ advanced analytics to establish historical asset acquisition and/or disposal trends. Compare such trends to the COVID-19 timeline relevant to the organization.

5. E-discovery collections and review:

Réaliser des collectes d'email ciblées ePerform focused email collection and review procedures based on the identification of potential red-flag indicators to assess whether executives may have based their trades on certain confidential information not known to the public. The investigation should also assess whether such information may have also been communicated to relatives and close friends of the executives, since this will also likely be an area of focus to the regulators.

6. Investigative interviews:

Conduct investigative interviews with key personnel, including those potentially implicated by the transactions in question, following the

collection and analyses of the relevant documents and data described above.

Deloitte brings the right people, processes, and technologies to assist the board, audit committee, and legal and compliance executives with important and sensitive investigations.

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Endnotes

1. Règlement (UE) n°596/2014 du Parlement européen et du Conseil du 16 avril 2014
<https://eur-lex.europa.eu/legal-content/FR/TXT/HTML/?uri=CELEX:32014R0596&from=FR> et <https://www.amf-france.org/fr/actualites-publications/dossiers-thematiques/abus-de-marche-mar>
2. <https://eur-lex.europa.eu/legal-content/FR/TXT/HTML/?uri=CELEX:32016R0347&from=FR>
3. Code monétaire et financier, article L465-1 modifié par LOI n° 2016 819 du 21 juin 2016 - art. 1.
<https://www.legifrance.gouv.fr/affichCodeArticle.do?idArticle=LEGIARTI000006654281&cidTexte=LEGITEXT000006072026&dateTexte=20100211&oldAction=rechCodeArticle>
4. Règlement général de l'Autorité des marchés Financiers, article 622-2.
<https://reglement-general.amf-france.org/eli/fr/aai/amf/rg/622-2/article/20041125/fr.html>
5. <https://www.sec.gov/about/forms/form4data.pdf>.
6. <https://www.sec.gov/edgar/searchedgar/companysearch.html>.
7. https://bdif.amf-france.org/Recherche-avancee?formId=BDIF&DOC_TYPE=BDIF&LANGUAGE=fr&subFormId=dd&DATE_PUBLICATION=&DATE_OBSOLESCENCE=&isSearch=true
8. <https://www.wsj.com/articles/bezos-other-corporate-executives-sold-shares-just-in-time-11585042204>.
9. <https://www.sec.gov/news/press-release/2020-53>.
10. <https://www.sec.gov/news/public-statement/statement-enforcement-co-directors-market-integrity>.