

Practice Update

DOJ Indicts CEO for Allegedly Using Trading Plans to Commit Insider Trading

March 16, 2023

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Critics have repeatedly alleged that executives routinely take advantage of the many loopholes that exist regarding Rule 10b5-1 trading plans to engage in improper conduct. These criticisms finally seem to have been heard by both the Department of Justice (DOJ) and the Securities and Exchange Commission (SEC).

On March 1, 2023, the DOJ indicted Terran Peizer, founder and CEO of Ontrak, Inc., on securities fraud charges for allegedly engaging in insider trading to avoid stock market losses through the use of his 10b5-1 trading plans. The indictment alleges that Peizer refused to engage in any “cooling-off” period after he adopted his 10b5-1 trading plan despite warnings from two brokers and instead began selling shares the day after establishing a new 10b5-1 trading plan. The indictment also alleges that just six days after Peizer’s most recent 10b5-1 trading plan was adopted, Ontrak announced that one of Ontrak’s key customer contracts had been terminated, causing Ontrak’s stock price to decline by more than 44 percent.

In its press release announcing the charges, the DOJ noted that—consistent with recent shifts in SEC and DOJ enforcement policy—this was the first time DOJ had brought insider trading charges based exclusively on an executive’s use of Rule 10b5-1

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trading plans. The DOJ noted that the charges are part of a “data-driven initiative” led by DOJ’s Fraud Section to identify any illegal insider trading schemes, which is also in line with both the SEC’s and DOJ’s publicly and recently stated intent of relying more heavily on modern data tools and technology to identify illegal insider trading. Indeed, just recently in a keynote address at the American Bar Association’s Annual National Institute on White Collar Crime, Assistant Attorney General Kenneth A. Polite stated: “By assessing trading data and SEC filings, our experts detected company insiders who greatly outperformed the market when trading pursuant to 10b5-1 plans, which allow insiders who are not in possession of material, non-public information to set up pre-planned stock transactions.”

At the end of 2022, the SEC adopted amendments to SEC Rule 10b5-1 regarding public company stock trading plans and new disclosure requirements that institute stricter legal requirements for corporate insiders who wish to buy or sell stock pursuant to their company’s predetermined Rule 10b5-1 stock trading plans (see SEC press release).

Those amendments generally limit the scope of insider trading defenses available to corporate insiders who buy and sell company stock pursuant to the company’s Rule 10b5-1 trading plan. They also, among other things, require corporate insiders to abide by a cooling-off period after the 10b5-1 plan is adopted before a corporate insider can buy or sell stock pursuant to the company’s 10b5-1 trading plan. With respect to directors and officers, the cooling-off period is the later of (i) 90 days after the adoption of the trading plan or (ii) two business days following the filing of the Form 10-Q or Form 10-K for the fiscal quarter in which the plan was adopted. The cooling-off period, however, does not exceed 120 days following adoption of the company’s 10b5-1 plan (see <https://www.sec.gov/rules/final/2022/33-11138.pdf> at 27-28). For persons other than stock issuers, directors, or officers, the cooling-off period is 30

days after the adoption of the company's 10b5-1 trading plan (*Id.* at 34).

While the indictment may have caused a stir, it shouldn't have in light of reports in December 2022 that the DOJ and SEC were investigating whether executives had been using 10b5-1 trading plans to hide impermissible trading. These reports noted that the government was using computer algorithms in a sweeping examination of preplanned equity sales by company executives. Further, in October, Sientra Inc. disclosed that it had received subpoenas from both the Justice Department and the SEC, including one from a grand jury, seeking materials concerning the trading activities of a former chief executive officer in 2019 and 2020 (Sientra, Inc. Oct. 11, 2022, Form 8-k at 2, Item 8.01).

The real questions are: (1) when will the next set of indictments as well as SEC actions drop given the government's use of a "data-driven initiative" to ferret out impermissible trading;^[1] and (2) was Deputy Attorney General Lisa Monaco's proclamation that "the Department's first priority in corporate criminal matters is to hold accountable the individuals who commit and profit from corporate crime"^[2] a warning that the DOJ is looking at corporate crime in a way that it hasn't before?

For more information regarding DOJ and SEC enforcement priorities, please contact the authors of this article.

[1]AAG Polite commented, regarding the Peizer indictment, to "take note . . . other such cases will follow." See <https://www.justice.gov/opa/speech/assistant-attorney-general-kenneth-polite-jr-delivers-keynote-aba-s-38th-annual-national> (last visited March 14, 2023).

[2]Deputy Attorney General Lisa Monaco's September 15, 2022 *Remarks on Corporate Criminal*

Enforcement,

<https://www.justice.gov/opa/speech/deputy-attorney-general-lisa-o-monaco-delivers-remarks-corporate-criminal-enforcement> (last visited March 13, 2023).

See also Lisa Monaco, Further Revisions to Corporate Criminal Enforcement Policies Following Discussions with Corporate Crime Advisory Group Memorandum,

<https://www.justice.gov/opa/speech/file/1535301/download> (last visited March 13, 2023).

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