

# COURT REJECTS SHORT-SWING PROFITS CLAIM RELATING TO SHARE WITHHOLDING TO SATISFY TAXES

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**Practices & Industries**

Employee Benefits

On January 26, 2018, the United States District Court for the Northern District of Oklahoma granted summary judgment to WPX Energy, Inc. (the “Company”) and its CEO and general counsel in relation to a plaintiff’s claim that the Company’s satisfaction of its tax withholding obligations by withholding shares having a fair market value equal to the withholding obligation violated Section 16(b) of the Securities Exchange Act of 1934. As discussed in our June 2017 newsletter, the Southern District of Texas reached a similar conclusion in *Jordan v. Flexton*. See <http://www.hodgsonruss.com/newsroom-publications-9795.html>. However, the opinion from the Northern District of Oklahoma provides a much more comprehensive analysis than the *Jordan* opinion.

Section 16(b) requires that officers, directors, and beneficial owners of more than 10% of any class of an issuer’s equity securities disgorge any profits realized from any purchase and sale (or sale and purchase) of the issuer’s equity securities made within a six-month period. Section 16(b) authorizes the SEC to issue exemptions from Section 16(b)’s rules. In furtherance of this statutory authorization, the SEC issued Rule 16b-3, which exempts certain transactions from the “short-swing profit” rules under Section 16(b). Importantly in the WPX case, Rule 16b-3(e) generally exempts certain transactions involving the disposition of issuer equity securities to the issuer, if the terms of the disposition are approved in advance by a committee of the board of directors that is composed solely of two or more non-employee directors (i.e., the Compensation Committee of the Board). The SEC provided this exemption because, in an exempt transaction under Rule 16b-3(e), both the issuer and the insider have access to the same information, and there is no informational imbalance between the parties.

WPX had established an equity incentive plan in 2013. The plan provided that the plan was to be administered by the Board, except that an independent committee would administer the plan with respect to any awards made to executive officers. The independent committee was expressly created for the purpose of complying with Rule 16b-3 (along with Section 162(m) of the Internal Revenue Code). In regard to the satisfaction of any tax withholding obligations, the plan provided that an award recipient is required to “remit an amount in cash, or in the Company’s discretion, in

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Shares, valued at their Fair Market Value on the date the withholding obligation arises, sufficient to satisfy the employer’s federal, state, and local tax withholding requirements related thereto.”

The Company’s CEO and general counsel were each awarded restricted stock units (“RSUs”) under the Company’s equity incentive plan. The RSU award agreements mandated that a number of Company shares having a fair market value equal to the Company’s withholding obligation be withheld at the time the RSU was settled through the issuance of Company shares to the CEO and general counsel. When the RSUs vested and were settled, the Company withheld shares in satisfaction of the tax withholding obligation. The plaintiff alleged that this disposition by the CEO and general counsel occurred within six months of the date each executive made purchases of the Company’s stock and, therefore, violated Section 16(b).

In dismissing the plaintiff’s claim, the district court pointed to the second sentence in Note 3 to Rule 16b-3, which provides that “where the terms of a subsequent transaction (such as the exercise price of an option, or the provision of an exercise or tax withholding right) are provided for in a transaction as initially approved pursuant to [Rule 16b-3(e)], such subsequent transaction shall not require further specific approval.” In this regard, since the RSU award agreement that was approved by the independent committee expressly mandated that share withholding occur to satisfy any tax withholding obligation, the court found no further approval was required by the committee and the disposition squarely came within the exemption to Section 16(b) provided by Rule 16b-3(e). *Olaques v. Muncrief* (N.D. Okla. 2017).