

February 17, 2022

## SEC Proposes Substantial Changes to Beneficial Ownership Reporting

On February 10, 2022, the Securities and Exchange Commission (the “SEC”) proposed substantial amendments to the reporting regime for beneficial owners of greater than 5% in public companies.<sup>1</sup> The SEC’s proposal would accelerate the filing deadlines for Schedule 13D and Schedule 13G and require more frequent amendments to Schedule 13G filings. The proposal would also change how some cash-settled derivatives are treated and when investors have formed a “group” and must aggregate their holdings.

### Background

Sections 13(d) and 13(g) of the Securities Exchange Act of 1934 (the “Exchange Act”) and the related rules require beneficial owners of more than 5% of an Exchange Act-registered class of voting equity securities to file a Schedule 13D or Schedule 13G to publicly report such ownership. Rule 13d-3 provides that a security is beneficially owned by anyone who has the right within 60 days to direct the voting or disposition of such security.<sup>2</sup> Beneficial owners of a security who act in concert with respect to an issuer may be deemed to have formed a “group.”<sup>3</sup> If a group is formed, the beneficial ownership of each member of the group is aggregated for purposes of determining reporting requirements.

Schedule 13D requires significant disclosure regarding, among other things, plans or proposals with respect to the issuer, transactions in securities of the issuer and agreements with respect to securities of the issuer, as well as the reporting person’s beneficial ownership of the relevant class. Schedule 13G requires substantially less disclosure, which is focused primarily on the reporting person’s beneficial ownership of the relevant class. Three classes of investors are eligible to file a Schedule 13G in lieu of the longer form Schedule 13D: Exempt Investors;<sup>4</sup> Qualified Institutional Investors;<sup>5</sup> and Passive Investors.<sup>6</sup> The filing deadlines and amendment requirements for each class of Schedule 13G filers are different – with Exempt Investors currently receiving the most favorable treatment and Passive Investors the least. If adopted, the proposed amendments would erode many of those differences.

<sup>1</sup> Release Nos. 33-11030; 34-94211 (Feb. 10, 2022) (the “Proposing Release”), *available at* <https://www.sec.gov/rules/proposed/2022/33-11030.pdf>.

<sup>2</sup> Exchange Act Rule 13d-3(d) also provides that a person who obtains such a right is immediately deemed to be the beneficial owner of the relevant securities, even if the right is not exercisable within 60 days, if it was acquired “with the purpose or effect of changing or influencing the control of the issuer, or in connection with or as a participant in any transaction having such purpose or effect.”

<sup>3</sup> Proposing Release at 77–81.

<sup>4</sup> Investors who beneficially own more than 5% of the relevant class but have not made an acquisition that is captured by Section 13(d). Common examples include pre-IPO investors and persons who exceed the 5% threshold due solely to a share repurchase. An investor who acquired or holds the securities with a control purpose may qualify as an Exempt Investor. *See* Exchange Act Section 13(d)(6); Exchange Act Rule 13d-1(d).

<sup>5</sup> Regulated institutions of a type listed in Rule 13d-1(b) (e.g., banks, registered investment companies, investment advisers and broker-dealers and certain employee benefit plans) who acquired and hold the securities in the ordinary course of business and “not with the purpose nor with the effect of changing or influencing the control of the issuer, nor in connection with or as a participant in any transaction having such purpose or effect.” *See* Exchange Act Rule 13d-1(b).

<sup>6</sup> Investors who beneficially own less than 20% of the relevant class and did not acquire and do not hold “the securities with any purpose, or with the effect, of changing or influencing the control of the issuer, or in connection with or as a participant in any transaction having that purpose or effect.” *See* Exchange Act Rule 13d-1(c).

## Proposed Amendments

The key amendments addressed in the Proposing Release are summarized below.

- Schedule 13D filing deadlines.
  - *Initial Filing.* The deadline for filing a Schedule 13D would be accelerated from 10 calendar days after the triggering event to five calendar days.
  - *Amendments.* Amendments would continue to be required whenever there is a material change to the information reported. However, the proposed rules would change the deadline for amendments from “promptly” (which is undefined) following the triggering event to one business day.
- Schedule 13G filing deadlines and amendment triggers. The proposed changes to filing deadlines and amendment triggers for Schedule 13G are more extensive and vary depending on the type of filer.
  - **Exempt Investors.**
    - *Initial Filing.* The deadline for filing a Schedule 13G would be accelerated from February 14 of the year that follows occurrence of the triggering event to five business days after the end of the month in which the triggering event occurred.
    - *Amendments.* Amendments would be triggered by any material<sup>7</sup> change in the information reported in the Schedule 13G and would be due five business days after the end of the month in which the triggering event occurred.

Currently, amendments are only due annually on February 14, reporting changes that occurred during the previous year.

- **Qualified Institutional Investors.**

- *Initial Filing.* As with Exempt Investors, the deadline for filing a Schedule 13G would be accelerated to five business days after the end of the month in which the triggering event occurred.

Currently, Qualified Institutional Investors who beneficially own up to 10% of the relevant class are only required to file a Schedule 13G by February 14 of the year that follows the triggering event. If, as of the end of any month, a Qualified Institutional Investor’s beneficial ownership exceeds 10%, it is required to file within 10 calendar days of the end of such month.

- *Amendments.* Qualified Institutional Investors would be subject to the same requirements as Exempt Investors to file an amendment whenever there is a material change in the information reported. Additionally, Qualified Institutional Investors would be required to file an amendment five calendar days after exceeding 10% beneficial ownership and thereafter within five calendar days of an increase or decrease in beneficial ownership of more than 5% (e.g., within five calendar days of that percentage changing from 12% to 6.9%).

Currently, amendments are due annually, on February 14, reporting changes that occurred during the previous year and within 10 calendar days after the month end at which beneficial ownership exceeded 10% of the relevant class or at which subsequent 5% changes occurred.

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<sup>7</sup> While this standard is similar to the amendment standard that applies to Schedule 13D, the SEC did not propose to deem an acquisition or disposition of more than one percent of the class of securities to be material for this purpose. Rule 13d-2(a) provides that such a change is deemed to be material in the context of a Schedule 13D.

○ **Passive Investors**

- *Initial Filing.* Consistent with Schedule 13D filers, the deadline would be accelerated from 10 calendar days after the triggering event to five calendar days.
- *Amendments.* Passive Investors would be subject to the same amendment triggers as Qualified Institutional Investors. However, Passive Investors would be required to file such amendments within one business day after exceeding the 10% threshold and for subsequent 5% changes. As with Qualified Institutional Investors and Exempt Investors, amendments required because of a material change in the information reported would be due five business days after the end of the month in which the triggering event occurred.

Currently, amendments are due annually, on February 14, reporting changes that occurred during the previous year and “promptly” if beneficial ownership exceeds 10% of the relevant class or if subsequent 5% changes occur.

- Treatment of Cash-Settled Derivatives. The SEC proposed treating holders of cash-settled derivatives as beneficial owners of the referenced securities (adjusted for any differences between the derivative and the referenced securities, where applicable). “Derivatives” would be broadly defined for this purpose.<sup>8</sup> However, the SEC’s proposal includes two significant limitations that would significantly reduce the number of affected instruments.

- *Control purpose.* Cash-settled derivatives would only confer beneficial ownership of the underlying reference securities if they are “held with the purpose or effect of changing or influencing the control of the issuer of such class of equity securities, or in connection with or as a participant in any transaction having such purpose or effect.”<sup>9</sup>
- *Exclusion of security-based swaps.* Cash-settled security-based swaps (as defined in Section 3(a)(68) of the Exchange Act) are excluded from the SEC’s proposal, limiting the universe of cash-settled derivatives that would confer beneficial ownership of the underlying reference securities.

However, the SEC recently proposed adopting a new rule, Exchange Act Rule 10B-1, which would establish a reporting regime, separate from Sections 13(d) and 13(g) of the Exchange Act, for public disclosure of security-based swaps.<sup>10</sup> That regime is in many ways broader than the beneficial ownership reporting regime under Sections 13(d) and 13(g) of the Exchange Act.<sup>11</sup> One of the proposed triggers for reporting under Exchange Act Rule 10B-1 is holding a Security-Based Swap Equivalent Position (as defined in the Swaps Reporting Proposal) in equity securities equal to more than 5% of the relevant class.

- Definition of “Groups.” The SEC proposed significant amendments to Rule 13d-5 and the adoption of new Rule 13d-6 regarding groups. The proposed amendments would both expand the definition of group in Rule 13d-5 and create important new exclusions to that definition, which may make it easier for passive investors to communicate.

<sup>8</sup> The SEC proposed using the definition of “derivative securities” from Rule 16a-1 for this purpose.

<sup>9</sup> Proposed Rule 13d-3(e)(1)(ii).

<sup>10</sup> See Release No. 34-93784 (Dec. 15, 2021), available at <https://www.sec.gov/rules/proposed/2021/34-93784.pdf> (the “Swaps Reporting Proposal”).

<sup>11</sup> For example, the Swaps Reporting Proposal would also require reporting of security-based swaps referencing instruments not captured by Sections 13(d) and 13(g) of the Exchange Act. It also proposes disclosure triggers based on notional amounts.

○ **Expansions.**

- *Clarifying that acting in concert is sufficient, even absent an agreement.* The SEC proposed amending Rule 13d-5 to “make clear that the determination as to whether two or more persons are acting as a group does not depend solely on the presence of an express agreement and that, depending on the particular facts and circumstances, concerted actions by two or more persons for the purpose of acquiring, holding or disposing of securities of an issuer are sufficient to constitute the formation of a group.”<sup>12</sup>
- *Tipper-Tippee relationships.* The SEC also proposed amending Rule 13d-5 to provide that a person who gives advance notice of a Schedule 13D filing to another market participant will be deemed to be a group with such other market participant “to the extent such information was shared with the purpose of causing such other person or persons to acquire equity securities of the same class for which the Schedule 13D will be filed.”<sup>13</sup>

The proposed exclusions discussed below would provide important relief from these provisions.

○ **Exclusions.**

- *Control purpose.* Rule 13d-6(c) would provide an important exclusion from the definition of a group – providing that persons will not be deemed to form a group if communications between them “are not undertaken with the purpose or the effect of changing or influencing control of the issuer, and are not made in connection with or as a participant in any transaction having such purpose or effect” and such persons “are not directly or indirectly obligated” to take actions in concert.<sup>14</sup> If adopted, this provision may mitigate or eliminate group concerns in several contexts, including with respect to certain ESG-related advocacy.
- *Discussions with derivative counterparties.* Rule 13d-6(d) would provide that persons entering into derivatives in the ordinary course of their business would not be deemed to form a group so long as the relevant agreement was not entered into “with the purpose or effect of changing or influencing control of the issuer, or in connection with or as a participant in any transaction having such purpose or effect.”<sup>15</sup>

Comments on the SEC’s proposal will be due on the later of April 11, 2022 and 30 days after the proposal is published in the Federal Register.

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If you would like to follow up regarding any of the matters covered by this Alert, please contact your usual Ropes & Gray attorney.

<sup>12</sup> Proposing Release at 82.

<sup>13</sup> Proposed Rule 13d-5(b)(1)(ii). It is unclear when a group formed under this provision would be terminated.

<sup>14</sup> Proposed Rule 13d-6(c).

<sup>15</sup> Proposed Rule 13d-6(d).