MARCH 21, 2022 • 9 MIN READ

# SEC proposes sweeping changes to Schedule 13D and 13G beneficial ownership reporting requirements


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The Securities and Exchange Commission (SEC) has proposed amendments[1] to the rules governing beneficial ownership[2] reporting under the U.S. Securities and Exchange Act (Exchange Act).

Similar to the early warning reporting and alternative monthly reporting filings required to be made under Canadian securities laws, Schedule 13D and Schedule 13G filings provide transparency to the market that an investor, or group of investors, has accumulated or holds a significant stake in the voting equity securities of any domestic or foreign issuer that has securities listed on a U.S. national securities exchange or otherwise has a class of equity securities registered under section 12 of the Exchange Act[3] (a U.S. reporting company). Canadian reporting issuers that are also U.S. reporting companies, including Canadian companies relying on the multijurisdictional disclosure system (MJDS), are subject to both the Canadian and U.S. regimes and would be affected by the SEC's proposed amendments, if adopted.

## What you need to know

- The SEC is proposing to significantly shorten the Schedule 13D and 13G filing deadlines. For example, initial Schedule 13D filings would have to be made within five days (versus 10 days) and material amendments would have to be filed within one business day (versus "promptly").
- Initial Schedule 13G filings for certain investors would have to be made within five business days after the month in which the reporting obligation is triggered. In addition, institutional managers whose holdings exceed the 10% threshold would have file an amendment within five calendar days, and passive investors exceeding the 10% threshold would have to file within one business day.
- Investors in companies that are both reporting issuers in Canada and U.S. reporting companies need to be mindful of the reporting thresholds, deadlines and other requirements under both the Canadian and U.S. regimes. For example, under Canadian securities laws the initial early warning threshold typically is triggered at 10% (versus 5% under the current and proposed U.S. rules) and the purchaser must publicly disclose its holdings "promptly" and file an early warning report within two business days (versus five calendar days under the proposed U.S. rules).
- The SEC proposes to adopt a new rule deeming holders of certain cash-settled derivatives to be beneficial owners of the reference security if the instrument is held 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.
- The SEC is also proposing to clarify the circumstances under which a "group" is formed and becomes subject to these reporting obligations.

## Background

Schedule 13D is the U.S. equivalent of a Canadian early warning report. Currently, an initial Schedule 13D report must be filed within 10 calendar days of the acquisition of beneficial ownership of more than 5% of a class of a U.S. reporting company's voting equity securities by a person or group (a purchaser) that has or is deemed to have "control intent" in respect of the company. Schedule 13D must be amended "promptly" following any material change in share ownership, such as an increase or decrease in the purchaser's holdings of 1% or more of the company's outstanding shares.

Schedule 13G is a short-form filing that may be used in lieu of Schedule 13D by eligible institutional investors, passive investors and exempt investors (e.g., significant shareholders prior to the company going public) with no "control intent" to report ordinary course beneficial ownership of more than 5% of a U.S. reporting company's voting equity securities. Schedule 13G is the U.S. equivalent of the Canadian alternative monthly report that certain eligible institutional investors can file instead of an early warning report.

## Filing deadlines to be shortened

The SEC is proposing to shorten many of the filing deadlines for Schedules 13D and 13G, as follows.

- For Schedule 13D filers, the initial filing deadline would be shortened from 10 to five calendar days and amendments would have to be filed within one business day (versus the current requirement to file "promptly", a term that has been open to interpretation by market participants)[4].
- For qualified institutional investors and exempt investors, the filing deadline for their initial Schedule 13G would be shortened from 45 calendar days after year-end to five business days after the end of the month in which the investor beneficially owned more than 5% of the covered class. For passive investors, the initial Schedule 13G filing deadline would be shortened from 10 to five calendar days after crossing the 5% ownership threshold[5].
- The SEC is also proposing to require institutional managers with beneficial ownership exceeding 10% of a U.S. reporting company to file an initial Schedule 13G (or an amendment to their existing Schedule 13G, if previously over 5%) within five calendar days of crossing the 10% threshold (versus within 10 days of month-end under current rules).
- Passive investors would be required to file an initial Schedule 13G (or an amendment to their existing Schedule 13G, if previously over 5%) within one business day of crossing the 10% threshold (vs "promptly" under current rules).
- For all Schedule 13G filers, the filing deadline for all other amendments would be shortened from 45 calendar days after the year in which any change occurred to five business days after the month in which the material change occurred (or earlier, for institutional managers and passive investors crossing the 10% threshold as described above).
- The proposed amendments would extend the filing cut-off times for Schedules 13D and 13G from 5:30 pm to 10:00 pm Eastern time.

To make it easier for investors and markets to use the information disclosed on Schedules 13D and 13G, the proposed rules require these filings to use a structured, machine-readable data language. This requirement would apply to all information disclosed on Schedules 13D and 13G.

## Treatment of cash-settled derivatives

### Current rules

Currently, cash-settled equity derivatives generally are not included in the calculation of "beneficial ownership" for section 13 reporting purposes because such securities do not give the holder thereof the "right to acquire" any voting equity securities of a U.S. reporting company. Under existing case law, however, shareholders that are otherwise required to file a Schedule 13D in respect of a U.S. reporting company are required to disclose the existence of cash-settled equity derivatives for such U.S. reporting company, even if such derivatives are not counted toward the shareholder's beneficial ownership percentage[6].

### SEC proposal

The SEC is proposing to adopt new Rule 13d-3(e), which would deem holders of certain cash-settled derivative securities in the context of changing or influencing control of the issuer of the reference security to be beneficial owners of the reference covered class of securities. In connection with the proposed amendments, the SEC noted that some market commentators have raised concerns that an investor in a cash-settled derivative may influence or control an issuer by influencing a counterparty to make certain decisions regarding the voting or disposition of substantial blocks of securities. According to the SEC, an investor in a cash-settled derivative may be positioned, by virtue of its relationship with a counterparty to acquire any reference securities that the counterparty may acquire to hedge the economic risk of the transaction. Also, immobilized hedge positions, if not voted, could magnify the voting power that an investor acquires through its non-synthetic holdings of relevant securities.

Proposed new Rule 13d-3(e) would not apply to security-based swaps. However, disclosure of large positions in security-based swaps would be addressed by the SEC's proposed amendments to Rule 10B-1, which were announced in December 2021 but have not been adopted yet.

## Regulation of groups under the proposed amendments

### Proof of agreement not required for persons to be acting as a group

**SEC's current approach and proposed amendments:** Sections 13(d)(3) and (g)(3) of the Exchange Act provide that when two or more persons act as a group "for the purpose of acquiring, holding, or disposing of securities of an issuer", the group is treated as a single person for purposes of calculating beneficial ownership of the relevant securities. Among other things, this means that the group members' holdings and transactions in the issuer's securities are aggregated for purposes of determining when and how the reporting thresholds apply. There is no definition of "group" in the SEC rules and the determination of whether coordinated efforts among two or more persons constitutes a group subject to regulation as a single person is a question of fact that, historically, has been resolved through case law.

The SEC is proposing to amend certain rules to align the language with the Exchange Act and thereby remove the potential implication that express or implied agreement among purported group members is a necessary precondition to the formation of a group. The proposed rule amendments would also specify that a group would be formed in certain circumstances if a person shared non-public information about an upcoming Schedule 13D filing with another person who subsequently purchased the issuer's securities based on that information, to the extent such information was shared for the purpose of causing the other person to acquire equity securities of the same class for which the Schedule 13D is being filed.

### Proposed new exemptions relating to "groups"

**SEC proposal:** The SEC is proposing to introduce additional exemptions from the group formation rules to ensure that the proposed amendments described above do not have a chilling effect on shareholder communications or impair financial institutions' capacity to execute commercial transactions in the ordinary course of business.

- New Rule 13d-6(c) would specify that if two or more persons communicate and consult with each other and engage with an issuer without the purpose or effect of changing or influencing control of the issuer, they would not be subject to regulation as a group, provided that they acted independently in making their investment decisions and were not directly or indirectly obligated to do so pursuant to a cooperation, joint voting or similar agreement.

- New Rule 13d-6(d) would specify that a group will not be formed solely by virtue of a *bona fide* purchase and sale agreement governing the terms of a derivative security entered into in the ordinary course of business and without the purpose or effect of changing or influencing control of the issuer.

The comment period on the proposed rules expires on April 11, 2022.

**FOOTNOTES**

*To discuss these issues, please contact the author(s).*