June 27, 2023

Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Reopening of Comment Period for Modernization of Beneficial Ownership Reporting (File Number S7-06-22); 88 Fed. Reg. 28440 (May 4, 2023)

Dear Ms. Countryman:

Better Markets[1] appreciates the opportunity to provide additional comment on the proposal to modernize beneficial ownership reporting ("Proposal"), which was originally published in the Federal Register on March 10, 2022.[2] The Commission has now reopened the Proposal for comment in light of a memorandum issued by the staff of the Division of Economic and Risk Analysis on April 28, 2023 ("DERA Staff Memo").[3]

The Proposal has four main components. It would (1) accelerate the filing deadlines for initial and amended beneficial ownership reports filed on Schedules 13D and 13G; (2) expand the scope of beneficial ownership reporting to include certain cash-settled derivatives; (3) clarify when two or more persons have formed a group subject to beneficial ownership reporting obligations; and (4) require Schedules 13D and 13G to be filed using a structured, machine-readable data language. As we stated in our original letter in response to the Proposal,[4] which we fully incorporate herein by reference, we believe that the collective effect of these reforms would be to increase transparency, fairness, and systemic stability in our markets.

Nothing in the DERA Staff Memo alters our position. It confirms that moving from a 10-day deadline for filing a Schedule 13D to a 5-day filing deadline would strike an appropriate balance: It would mitigate the harm that shareholders suffer when they sell before the market becomes aware of an effort by some purchasers to accumulate shares, without stifling the ability of activist shareholders to accumulate shares in their effort to influence corporate policy.

---

1 Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system that protects and promotes Americans' jobs, savings, retirements, and more.

2 87 Fed. Reg. 13,846 (Mar. 10, 2022) ("Release").

3 Reopening of Comment Period for Modernization of Beneficial Ownership Reporting, 88 Fed. Reg. 28,440 (May 4, 2023).

4 Better Markets, Comment Letter to the SEC on Modernization of Beneficial Ownership Reporting (Apr. 11, 2022), https://www.sec.gov/comments/s7-06-22/s70622-20123233-279507.pdf.

BACKGROUND

The DERA Staff Memo focuses on the part of the Proposal that would accelerate the deadline for Schedule 13D filings. The Proposal would shorten the initial filing deadline for disclosing on Schedule 13D a person's acquisition of more than 5% of a covered class of equity securities from 10 days to 5 days and require that amendments be filed within 1 business day. The Proposal notes that economically significant price increases often occur in response to news about changes in corporate control, such as the initial filing of a Schedule 13D, which means that any delay between a person's acquisition of more than 5% of a covered class of equity securities and the filing of a Schedule 13D results in an information asymmetry between the Schedule 13D filer (and those with whom they share the information) and the rest of the market.[5] The current 10-day filing deadline thus allows shareholders who reach the 5% threshold to continue to acquire far more than 5% of shares at favorable prices during the 10-day window.[6] The Proposal notes that the current 10-day delay could therefore harm investors who happen to sell their shares during the 10-day window, and shortening the delay could reduce these harms.[7] Nonetheless, the Proposal also notes that shortening the deadline for filing the initial Schedule 13D could have the undesirable effect of deterring activists from acquiring shares to gain influence or control over an issuer. This concern arises because the earlier disclosure would increase the share price sooner, which could reduce the gains on which activists depend for their campaigns and also potentially reduce the number of shares activists could afford to acquire.[8]

The DERA Staff Memo involves an examination of the Schedule 13D filings between 2011 and 2021 that were most likely to be the result of activist campaigns.[9] In order to determine the appropriate sample, it excluded Schedule 13D filings that reflected the acquisition of beneficial ownership through corporate actions or other off-market transactions. The staff believed these acquisitions were unlikely to be the result of activist campaigns.[10] This left the staff with 3,067 Schedule 13D "non-corporate-action filings" that were likely the result of activist campaigns.[11]

The DERA Staff Memo then examined a subset of these filings in which filers used the full 10-day window to file and determined that there were significant additional abnormal returns after day five following the trigger date for filing a Schedule 13D (the date on which the investor

---

5 Release at 13,881.
6 *Id.* at 13,880-13,881.
7 *Id.* at 13,881; *see also id.* at 13,850 n.19 (discussing the notion that the gains that activists make in trading on asymmetrical information before the filing of a Schedule 13D come at the expense of selling shareholders).
8 *Id.* at 13,822; *see also id.* at 13,850 nn.17 & 19, 13,883 (discussing the notion that shortening the deadline for filing a Schedule 13D will reduce the returns for activist investors and thereby reduce the incidence of activists acquiring large blocks of shares in public companies and the size of those blocks).
9 Memorandum From the SEC Division of Economic and Risk Analysis Re: supplemental data and analysis on certain economic effects of proposed amendments regarding the reporting of beneficial ownership (Apr. 28, 2013) ("DERA Staff Memo"), https://www.sec.gov/comments/s7-06-22/s70622-20165251-334474.pdf.
10 DERA Staff Memo at 3.
11 *Id.* at 3-4.

acquired beneficial ownership of more than 5% of the security).[12] This indicated that there remained information that had not been fully incorporated into market prices as of that time.[13] This pattern of returns suggested to the staff that there was the potential for improvement in allocative efficiency and a reduction in information asymmetry under a shortened deadline with respect to non-corporate-action filings.[14] The staff also believed that these filers could be likely to be impacted by the proposed shortening of the filing deadline as any open-market accumulation of shares between the proposed deadline and their current filing date (days six through ten following the trigger date) could become more costly.[15]

Having determined that abnormal returns after day five following the trigger date existed for a subset of non-corporate-action filings, the DERA Staff Memo determined to use the non-corporate action filings to examine two principal issues. First, it used those filings to investigate the potential effects on activism that could result from the proposed shortening of the initial Schedule 13D filing deadline from 10 days to 5 days. Second, it used those filings to analyze the potential harms to certain selling shareholders under the existing 10-day filing deadline and the reduction in that harm that could be expected to result from establishing the shorter 5-day filing deadline.

COMMENTS

The DERA Staff Memo supports the Proposal's proposed shortening of the deadline for filing an initial Schedule 13D from 10 days to 5 days in two ways. First, the DERA Staff Memo indicates that shortening the deadline from 10 days to 5 days is unlikely to significantly curtail activism. Second, the DERA Staff Memo indicates that shortening the deadline will mitigate the harms to shareholders who sell their shares between the time of a Schedule 13D filer's acquisition of 5% beneficial ownership and the time of the Schedule 13D filing.

I. The DERA Staff Memo indicates that activists will still be able to benefit from the increase in stock price after the announcement of their presence under the shortened deadline.

The DERA Staff Memo first attempted to determine the impact that shortening the deadline for filing an initial Schedule 13D from 10 days to 5 days might have on activists.[16] The staff started with the sample of 3,067 non-corporate-action filings and then excluded late filers and filers with no beneficial ownership reported as of the filing date and adjusted for multiple filings on the same date. These refinements resulted in a sample size of 2,371 non-corporate-action filings.[17]

---

[12] *Id*. at 7.
[13] *Id*.
[14] *Id.* at 7-8.
[15] *Id.* at 8.
[16] *Id.* at 14.
[17] *Id*.

With respect to these 2,371 non-corporate-action filings, the staff extracted data from the Schedule 13D filings to examine filers' patterns of share purchases and determine the percentage of instances that had trading between the proposed deadline and the actual filing date.[18] In this way, the staff could examine whether shortening the deadline would affect the way in which activists acquire large blocks of shares before the filing deadline in order to profit from the price increase that usually occurs after a Schedule 13D filing.

The staff determined that two-thirds of the 2,371 non-corporate-action filings involved filers who completed acquiring their reported stake by the proposed deadline of 5 days after they reached the 5% beneficial ownership threshold.[19] The staff concluded that, for these filers, shortening the filing deadline as proposed would likely not impact their accumulation patterns.[20] This makes sense, because even under a 5-day deadline for filing a Schedule 13D these filers would not have had to change their behavior to accumulate their reported stake—they would have been able to acquire the block of shares they deemed necessary before the filing deadline even if they would have had to file the Schedule 13D earlier than under the existing deadline.

With respect to the remaining third of filers who did not complete acquiring their reported stake by the proposed deadline, the DERA staff memo determined that most had *substantially* completed acquiring their share block by that time. The staff determined that 92% of filers completed acquiring 90% of their reported stake by the proposed deadline and only 8% of filers continued to accumulate shares constituting 10% of more of their reported stake after the proposed deadline.[21] Similarly, the staff found that 98% of filers completed acquiring 75% of their reported stake by the proposed deadline and only 2% of filers continued to accumulate shares constituting 25% of more of their reported stake after the proposed deadline.[22]

These figures indicate that shortening the deadline should not significantly impede activist campaigns. The overwhelming majority of past filers have acquired at least 75% of their reported stake by the proposed 5-day reporting deadline. This means that a 5-day reporting deadline likely would still enable activists to profit from the information asymmetry that would exist during the 5-day period before disclosure triggers a stock price increase.

Indeed, the DERA Staff Memo estimated the average percentage of a filer's unrealized gains on their reported equity stake, as of the day after the filing date, attributable to shares accumulated after the proposed deadline. Obviously, for filers who acquired 100% of their reported stake by the proposed deadline, 0% of their unrealized gains were attributable to shares accumulated after the proposed deadline because there were no such shares. But for filers who

---

18 *Id.*
19 *Id.* at 15.
20 *Id.*
21 *Id.* at 17.
22 *Id.*

acquired less than 100% of their reported stake by the proposed deadline, only 6.8% of their unrealized gains on average were attributable to shares accumulated after the proposed deadline.[23]

These statistics support the points we made in our initial comment letter. There, we said that to the extent it is desirable to preserve a period of time in which activists may accumulate profits before public disclosure of their goals, enabling them to offset the costs of their activism, the 5-day reporting deadline under the Proposal would preserve that opportunity to a significant degree.[24] The DERA Staff Memo indicates that this is, in fact, the case.

II. <u>The DERA Staff Memo indicates that shortening the deadline will mitigate harms to selling shareholders.</u>

The DERA Staff Memo also analyzed the potential harm, under current rules, to shareholders selling their shares between the time of a Schedule 13D filer's acquisition of 5% beneficial ownership and the time of the Schedule 13D filing.[25] The DERA Staff Memo focused on the harm that may accrue between the proposed filing deadline and the current filing deadline.[26] The DERA Staff Memo limited its analysis of the 2,371 filings to filings for which stock return data was available and for which filers used the full 10-day filing window to file.[27]

The DERA Staff Memo estimated the amount of appreciation forgone by trading prior to the filing becoming public information. The harm to a shareholder selling to a potentially informed, opportunistic trader would consist of the stock return between the day that they sell and the day after the filing date. The DERA Staff Memo determined that there were meaningful abnormal returns between the proposed filing deadline and the actual filing deadline, with greater such returns when the filer was still accumulating shares after day five.[28]

For filers who completed accumulating their shares by the proposed filing deadline, the DERA Staff Memo estimated that there was a 1.2% median abnormal return from the proposed deadline to the day after filing. For filers who were still accumulating their shares by the proposed filing deadline, the DERA Staff Memo estimated that there was a 2.2% median abnormal return from the proposed deadline to the day after filing. Using these estimates, the DERA Staff Memo further estimated that the aggregate harm to shareholders selling between the proposed filing deadline and the current filing deadline was $27 million per year with respect to filers who completed accumulating their shares by the proposed filing deadline. The aggregate harm was $66 million per year with respect to filers who had not completed accumulating their shares by the proposed filing deadline. The DERA Staff Memo concluded, based on these estimates, that the

---

23 *Id.* at 18.
24 Better Markets, supra note 4, at 5.
25 The DERA Staff Memo focused on sales in this time period to opportunistic traders who are not the filer.
26 DERA Staff Memo, supra note 9, at 23.
27 *Id.* at 23 & n.70.
28 *Id*. at 24-25.

aggregate estimate of potential harms that could be avoided by shortening the filing deadline to 5 calendar days if no filers abandoned their campaigns was about $93 million per year ($27 million per year plus $66 million per year).[29]

The DERA Staff Memo also considered the harms that could be avoided if some activists abandoned their campaigns under a 5-day filing deadline. The DERA Staff Memo estimated that, for filers who had not completed accumulating their stake as of the proposed filing deadline, the median abnormal return was 3.8% for filers who accumulated 10% or more of their stake after the proposed filing deadline and 6.9% for filers who accumulated 25% or more of their stake after the proposed filing deadline. The aggregate harm was $32 million per year for filers who accumulated 10% or more of their stake after the proposed filing deadline and $27 million per year for filers who accumulated 25% or more of their stake after the proposed filing deadline. The DERA Staff Memo concluded that if filers accumulating 25% or more of their stake after the proposed deadline completely abandoned their campaigns, the aggregate estimate of potential harms that could be avoided was therefore still about $66 million per year ($93 million minus $27 million). If filers accumulating 10% or more of their stake after the proposed deadline completely abandoned their campaigns, the aggregate estimate of potential harms that could be avoided would still be about $61 million per year ($93 million minus $32 million).[30]

Again, these statistics support the points we made in our initial comment letter. There, we said that during the current 10-day delay between the acquisition of a 5% beneficial ownership stake and the disclosure of that stake, those accumulating the beneficial ownership in the target company enjoy an informational advantage and an opportunity to profit at the expense of other investors in the market. As these activists accumulate additional shares that are likely if not bound to rise at a later point in time, they amass profits at the expense of shareholders not yet aware that the stock price will change. These "stealth" accumulations at artificially low market prices transfer value from countless public investors to those activists.[31] The DERA Staff Memo confirms that shortening the filing deadline to 5 calendar days could mitigate the harm to shareholders who sell before the disclosure of activists' 5% beneficial ownership.

---

29 *Id.* at 25.
30 *Id.*
31 Better Markets, supra note 4, at 4.

CONCLUSION

We hope these comments are helpful as the Commission finalizes the Proposal.

Sincerely,

Stephen Hall

Stephen W. Hall
Legal Director and Securities Specialist

Better Markets, Inc.
2000 Pennsylvania Avenue, NW
Suite 4008
Washington, DC 20006
(202) 618-6464

shall@bettermarkets.org
http://www.bettermarkets.org