



Bill Targeting Activist Fund Tactics Introduced by Prominent Democratic Senators

Apr 5, 2016

Reading Time : **5 min**

By: Jason Daniel, William K. Wetmore

Accelerated Due Date

The Bill would accelerate the Schedule 13D due date from 10 calendar days to two business days following the date of the acquisition, tracking the Section 16 due date for changes in beneficial ownership to be reported on Form 4. According to the [press release](#) from the office of Sens. Baldwin and Merkley on March 17, 2016 (the "Press Release"), the shortened time frame is designed to stop activists from abusing "lax securities laws to gain large stakes in public companies."

It appears that the two-business-day deadline was incorporated from the Form 4 filing requirement originally adopted in the Sarbanes-Oxley Act of 2002. However, unlike the content of a Form 4, which consists wholly of trading information, a Schedule 13D includes narrative disclosure of investment intent and any agreements relating to the securities, and it frequently requires the filing of agreements. Given these requirements, filing persons would likely need to preplan their filings prior to crossing the 5 percent threshold to be able to satisfy the proposed deadline.

Economic Beneficial Ownership

The Bill would require the SEC to amend the definition of beneficial ownership under Section 13(d) within a year after enactment to include a pecuniary or indirect pecuniary interest in a security as a form of beneficial ownership. The revised definition would be very similar to the definition of beneficial ownership that comes into play under Section 16 once a person is subject to reporting. For example:

- The Bill would increase the scope of required reporting of derivative securities for Section 13(d) and for short interest reporting, as described below, to include any instrument with a value derived, in whole or in part, from the value of the equity security in addition to the reporting of options, warrants and convertible securities.¹
- Securities held by members of the filing person's immediate family that share the same household would be presumed to be beneficially owned by the filing person.
- The proportional interest or profit allocation of a general partner would be deemed to be a pecuniary interest.
- The performance-based fee of an investment adviser would be deemed to be a pecuniary interest, subject to similar carveouts to Section 16.

The Press Release states that part of the reason for the inclusion of derivative securities and pecuniary interests is that, "In some cases [derivatives] are used [by activists] to create a 'net short' that allows the activist to profit by secretly voting against the company's interests. Currently, derivatives and other synthetic instruments do not require disclosures despite the fact that they can have substantial impacts on the price of the security and its issuer."

This rationale is confusing in light of Item 6 of Schedule 13D, which currently requires any filing person that acquires beneficial ownership (i.e., voting and/or investment power) of more than 5 percent of an equity security to report any agreements, contracts or understandings with respect to the securities, which would require disclosure of the above net short relationship.

The Bill's inclusion of economic interests in Section 13(d)'s beneficial ownership definition would dramatically change the purpose of Section 13(d) from disclosure of who has, or can obtain, control over an issuer's voting securities to disclosure of any person that has any economic interest in the securities. This control purpose has motivated practitioners to incorporate Section 13(d) standards into change-of-control provisions in indentures and for the definition of "acquiring person" as the trigger for poison pills and protective charter provisions. In addition, the SEC incorporated Section 13(d) control standards into Section 16 for determining who has enough influence over an issuer as a 10 percent beneficial owner to be subject to public trade reporting and disgorgement for short-swing profits pursuant to Section 16. Expanding the scope of these provisions would have unexpected consequences beyond Section 13(d), and, hopefully, any implementing regulations would take these impacts into account.

Targeting Wolf Packs

The Bill would also expand the scope of “persons” that are required to file a Schedule 13D beyond the current requirement for “groups” of persons acting together for the purposes of “acquiring, holding, voting or disposing of equity securities of an issuer” together to also include two or more persons that are acting together (i) “seeking to control or influence the board, management or policies of an issuer”; (ii) “evading, or assisting others in evading the designation as a ‘person’”; or (iii) “working together to evade the requirements of Sections 13(d), 13(g) or 13(s)” of the Exchange Act. According to the Press Release, the Bill would include persons that are “loose associations of ‘wolf packs’ and engage in ‘tipping’ allies to the impending 13(d) disclosure.”

Wolf-pack behavior is very difficult to define, especially since a group of hedge funds may work together for purposes other than circumventing group disclosure. The proposed definition would likely discourage funds from speaking together, since the communication that would be prohibited by the Bill is vague. An overly broad definition may capture funds that happen to have a common goal as it relates to an issuer and could interfere with shareholders being able to exercise their rights as shareholders even when they are not acting together to “target” an issuer.

Short Disclosure

The Bill would add new Section 13(s) to the Exchange Act to require persons to disclose whether they have a gross short interest of more than 5 percent of the class of equity securities covered by Section 13(d) to file a statement that is similar to that required under Section 13(d). Similar to the above-described expansion of beneficial ownership, short interest would include any instrument that provides the ability to profit from the decrease in the value of the security and would include indirect pecuniary interests similar to those required to be reported under Section 16. It is unclear exactly what the disclosure would look like, since much of the disclosure of a Schedule 13D seems irrelevant to a short seller.

Conclusion

Even if the Bill is not adopted, the SEC may feel political pressure to exercise its discretion granted under the Dodd-Frank Act to accomplish some of the Bill’s goals, such as the inclusion of securities-based swaps in beneficial ownership or shortening the required filing date for a Schedule 13D. Given these new pressures, we recommend that issuers re-examine their change of control and poison pill trigger language to consider including the concepts

from the current version of Section 13(d) and related rules in change-of-control provisions instead of merely incorporating Section 13(d) and related rules by reference.

¹ For computing the pecuniary interest, the Bill would permit a person to use the notional of a swap, the number of contracts and multiplier for a security future or the number of cash equivalent shares in a swap, subject to delta adjustment. This delta-adjustment concept is not expressly addressed in Section 16 pecuniary interest tests, but a similar concept appears to be incorporated into the derivative matching regime of Rule 16b-6(c) under the Exchange Act.

Categories

Shareholder Activism

Compliance

© 2025 Akin Gump Strauss Hauer & Feld LLP. All rights reserved. Attorney advertising. This document is distributed for informational use only; it does not constitute legal advice and should not be used as such. Prior results do not guarantee a similar outcome. Akin is the practicing name of Akin Gump LLP, a New York limited liability partnership authorized and regulated by the Solicitors Regulation Authority under number 267321. A list of the partners is available for inspection at Eighth Floor, Ten Bishops Square, London E1 6EG. For more information about Akin Gump LLP, Akin Gump Strauss Hauer & Feld LLP and other associated entities under which the Akin Gump network operates worldwide, please see our Legal Notices page.