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Via Electronic Mail: rule-comments@sec.gov

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

Re: Modernization of Beneficial Ownership Reporting, Release Nos. 33-11030; 34-94211; File No. S7-06-22

Dear Ms. Countryman:

Irenic Capital Management LP ("Irenic" or "we") appreciates the opportunity to provide comments to the United States Securities and Exchange Commission (the "SEC" or the "Commission") on the proposed changes to certain rules that govern beneficial ownership reporting (the "Proposed Rules"). We respectfully submit this letter in opposition to the Proposed Rules and, in particular, the contemplated shortening of the filing deadline for an initial Schedule 13D under Rule 13d-1(a) from ten days after the date on which a person acquires more than 5% of a covered class of equity securities to five days thereafter (the "Reporting Deadline Rule").

As to the Proposed Rules regarding Section 13(d) "group" formation and certain cash-settled derivatives being included in beneficial ownership calculations, Irenic opposes such rules, but does not directly address them herein. Separately, we understand that the Commission has proposed that parties to certain security-based swaps report their ownership on Schedule 10B by the next business day, if such ownership exceeds specified thresholds,[1] and Irenic similarly opposes such rule.[2] The Proposed Rules and proposed Rule 10B-1 (including Schedule 10B), considered together, introduce complicated and sweeping beneficial ownership reporting reforms that will likely lead to a stark regression in shareholder engagement, which the SEC has previously

[1] United States Securities and Exchange Commission, Prohibition Against Fraud, Manipulation, or Deception in Connection with Security-Based Swaps; Prohibition against Undue Influence over Chief Compliance Officers; Position Reporting of Large Security-Based Swap Positions, Release No. 34-93784; File No. S7-32-10 (2022).

[2] Irenic shares the views opposing new Rule 10B-1 set forth in the letters submitted to the Commission by Managed Funds Association and Elliott Investment Management L.P., each of which is dated March 21, 2022.

recognized as the "hallmark of our capital markets,"[3] acknowledged as one of the "key principles"[4] of our securities laws, and purposefully sought to bolster.[5]

Founded in 2021, Irenic is a private investment fund that intends to be an active shareholder of public companies. Through collaborative engagement with the leadership of our portfolio companies, we will seek to produce improvements in operating and financial performance that create value for companies and their shareholders. Irenic principally intends to invest in small-capitalization and mid-capitalization issuers, the very entities on which Schedule 13D filings are most frequently made[6] and also the kinds of companies that are more likely to employ harmful business, environmental, social, and governance practices that necessitate effective shareholder engagement and monitoring.

I. Introduction

In 1968, Congress established the Williams Act for the "sole purpose" of protecting investors who receive a cash tender offer for their shares of a publicly held company.[7] More specifically, as the United States Supreme Court has recognized, "[t]he purpose of the Williams Act is to insure that public shareholders who are confronted by a cash tender offer for their stock will not be required to respond without adequate information regarding the qualifications and intentions of the offering party."[8] Further, the objective of the beneficial ownership regime adopted as part of the Williams Act is to require certain disclosure from investors that "have acquired a substantial interest, or increased their interest in the equity securities of a company by a substantial amount, within a relatively short period of time."[9]

The Williams Act, at its core, was designed to enhance investor protection mechanisms under the federal securities laws through compelled disclosure by persons seeking to control a corporation, either by means of a cash tender offer or via open market or privately negotiated purchases of securities.[10] However, Senator Williams, in explaining the purposes of the Williams Act, emphasized that he took "extreme care . . . to protect the legitimate interests of the corporation, management, and shareholders" and sought to "avoid tipping the balance of regulatory burden" in favor of any party to a contest for corporate control.[11]

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[3] Former Chair Jay Clayton, *Statement Announcing SEC Staff Roundtable on the Proxy Process* (July 30, 2018), *available at* https://www.sec.gov/news/public-statement/statement-announcing-sec-staff-roundtable-proxy-process.

[4] Former Chair Jay Clayton, *Statement at Open Meeting on Proposals to Enhance the Accuracy, Transparency and Effectiveness of Our Proxy Voting System* (Nov. 5, 2019), *available at* https://www.sec.gov/news/public-statement/statement-clayton-2019-11-05-open-meeting.

[5] *See, e.g.*, United States Securities and Exchange Commission, "What We Are Doing to Enhance Shareholder Engagement," *available at* https://www.sec.gov/what-we-are-doing-improve-shareholder-engagement.

[6] According to Intelligize, between April 7, 2019 and April 7, 2022, only 22 initial Schedule 13D filings were made on S&P 500 companies, whereas 1,005 such filings were made on Russell 3000 companies.

[7] *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. 1, 35 (1977).

[8] *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 58 (1975).

[9] S. Rep. 90-550, at 7 (1967).

[10] 113 Cong. Rec. 854 (1967).

[11] *Id*.

We fear that the Proposed Rules undermine the balance that Senator Williams expressly sought to preserve and stand to harm investors, issuers, and corporate stakeholders alike. In doing so, the Proposed Rules seemingly do not serve the purpose of the Williams Act, but rather turn Section 13 into an expansive and onerous reporting regime aimed at providing information to market participants (*i.e.*, pre-disclosure sellers) that were not the subject of the enacted rules. Accordingly, this letter—respectfully submitted in opposition to the Proposed Rules—is in response to the Reporting Deadline Rule, which, in Irenic's view, would substantially burden institutional investment manager acquisition programs and have the perverse effect of reducing the accountability of corporate managers.

While Irenic, of course, strongly supports the Commission's goal of protecting investors, we are deeply concerned that the Proposed Rules may stunt or disincentivize the kinds of beneficial changes public investors have recently enjoyed as a result of the significant intellectual and financial commitments undertaken by engaged shareholders that seek to improve issuer performance, including through environmental, social, and governance advancements that benefit all stakeholders of public companies. Accordingly, we hereby request that the SEC abandon the Reporting Deadline Rule, specifically, and the Proposed Rules, generally.

II. The Deleterious Reporting Deadline Rule

A. *The Reporting Deadline Rule Lacks A Compelling Justification*

The release containing the Proposed Rules (the "Proposing Release") provides two primary justifications for the contemplated implementation of the Reporting Deadline Rule. First, the Proposing Release indicates that the ten-day filing deadline has not been updated since it was enacted more than 50 years ago and that, in light of technological advancements since 1968, a reformation of the ten-day filing deadline is appropriate. Second, the Proposing Release summarily resolves that the passage of time and the associated technological advances, taken together with the current ten-day filing deadline under Rule 13d-1(a), have yielded a market reality in which information is not being timely disseminated to the public and that such delay is contributing to "information asymmetries that could harm investors."[12] The Proposing Release ultimately concludes that the Commission has determined that an amendment to Rule 13d-1(a) is needed to adequately support the regulatory objectives of Section 13(d).

As to the technological dissimilarities between today's markets and those of the period in which the Williams Act was refined, such dissimilarities should carry little weight when the Commission is engaging in the calculus of whether to implement the Reporting Deadline Rule. Advocates of the Reporting Deadline Rule have relied on conclusory statements without empirical evidence to suggest that the SEC should shorten the Rule 13d-1(a) reporting window due, in relevant part, to changes in technology.[13] In fact, a review of the legislative history underlying the Williams Act reveals that nothing therein was intended to address the technological limitations of the era in which the relevant rules were enacted. Further, the legislative history in respect of the

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[12] United States Securities and Exchange Commission, Modernization of Beneficial Ownership Reporting, Release Nos. 33-11030; 34-94211; File No. S7-06-22, at 14-16 (2022) ("Beneficial Ownership Reporting Release").

[13] *See*, *e.g.*, Letter from Wachtell, Lipton, Rosen & Katz to Ms. Elizabeth M. Murphy, Secretary, United States Securities and Exchange Commission, at 3 (Mar. 7, 2011).

Williams Act reflects a "congressional judgment, in balancing the relative merits, that open-market transactions should be unregulated prior to the acquisition of a 5% stake and during the ten-day period after such acquisition."[14] That is, the ten-day filing deadline was part of the total mix of factors utilized to ensure that "the balance of regulation" was not "tipp[ed]" in favor of management or the investor, and such balance should not be disturbed absent compelling, empirical justification, which the Reporting Deadline Rule is without.[15] To that end, Senator Williams explicitly noted that the compromised reached — including a ten-day disclosure window — was meant to prevent "upsetting the free and open auction market where buyer and seller normally do not disclose the extent of their interest and avoid[] prematurely disclosing the terms of privately negotiated transactions."[16]

With respect to the purported "information asymmetries" that result from the technological advancements and financial product innovations of the past 50 years and the related potential harm to investors, we, respectfully, find such justification for the Reporting Deadline Rule to be without grounding in either the letter or spirit of the Williams Act. To further this justification for the Reporting Deadline Rule, the Proposing Release cites to writings by shareholder activism defense advisors that suggest that activist shareholders unfairly realize gains at the expense of selling shareholders as a consequence of the ten-day period between the acquisition of a 5% stake and the filing of an initial Schedule 13D.[17] This theory of investor harm, invented by anti-activist actors and adopted by the Commission, effectively "posits that a shareholder who sells during the ten-day window would be harmed by not knowing that someone else had acquired a large stake in the company"[18] (*i.e.*, if the Schedule 13D had been filed earlier, the selling shareholder might have sold at a higher price or re-evaluated whether to sell at all). Nothing in the words of the Williams Act or its legislative history suggests that the relevant rules were designed to favor the interests of short-term sellers (*i.e.*, shareholders who elect to sell prior to the disclosure of an initial Schedule 13D) to the detriment of other shareholders and potential shareholders. Rather, as Senator Williams indicated, the principal objective of the Williams Act is, understandably, to protect investors and management who are in a *reactive* posture following the public commencement of a tender offer and who may be operating on the basis of inadequate information when determining whether to tender into such offer.[19]

The United States Supreme Court has explicitly endorsed the foregoing reading of the Williams Act and questioned the propriety of the theory of investor harm relied upon in the instant case. In *Rondeau v. Mosinee Paper Corporation*, which the Proposing Release does not address, the Court stated that "it is not at all clear" that the Williams Act is intended to safeguard "the interests of shareholders who have either sold their stock . . . at pre[-]disclosure prices or would not have invested had they known that a takeover bid was imminent."[20] The utilization of the Williams Act to solve the dilemma of shareholders that have elected to capture, or refrain from capturing, pre-disclosure value through the uncoerced sale or purchase of securities in the open

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14 *Hyde Park P'rs, LP v. Connolly*, 839 F.2d 837, 851-52 (1st Cir. 1988).
15 S. Rep. 90-550, at 3 (1967).
16 113 Cong. Rec. 856 (1967).
17 Beneficial Ownership Reporting Release, at 16, n.19.
18 Commissioner Hester M. Peirce, *Dissenting Statement on Proposed Modernization of Beneficial Ownership Reporting* (Feb. 10, 2022).
19 *See* 113 Cong. Rec. 854-55 (1967); S. Rep. 90-550, at 3 (1967).
20 *Rondeau*, 422 U.S. at 59-60.

market is a distortion of what the legislation is intended to shield against (*i.e.*, post-disclosure coercion and information asymmetries).[21] To be sure, it is not readily apparent that a short-term seller that transacts in the securities of an issuer in a pre-disclosure environment has an entitlement to the rise in share price attributable to another investor's intellectual property or is somehow unfairly harmed by not possessing the independently developed and closely-held investment thesis of a third party. Generally, "[a] shareholder's decision to sell results either from liquidity needs or the shareholder's reservation price for the security in question. Any asymmetry of information involved in the transaction arises from the activist's private information about its own intentions, which may include a forecast as to the likely target firm response."[22]

Moreover, our securities markets fundamentally rely on one investor's belief that pre-disclosure pricing of subject securities represents an attractive investment opportunity relative to another investor's determination that such pricing represents an attractive liquidation opportunity (*i.e.*, markets operate properly when two parties engage in a transaction at a mutually beneficial price on the basis of the same issuer-provided information).[23] As Commissioner Peirce recognized in her written dissent to the Proposed Rules, "information asymmetries in this sense—where investors have equal access to disclosure from the issuer and insiders, but come to different conclusions about the long term prospects of a company based on their respective due diligence—are a feature, not a bug, of our capital markets."[24]

Respectfully, the Reporting Deadline Rule lacks a compelling justification. Those set forth in the Proposing Release—technological advancements and potential pre-disclosure information asymmetries—fail to rise to the level of necessitating a disturbance of the "balance" that Congress carefully curated when drafting the Williams Act. Newfound word processing efficiencies and information asymmetries that result from the independent efforts (including on the basis of the same issuer-provided information) of the ultimate Schedule 13D filer do not suggest to us that the purpose of Section 13 is no longer being properly served by Rule 13d-1(a).

B. *The Reporting Deadline Rule Unduly Deters Shareholder Engagement and Monitoring Activities to the Detriment of Corporate Stakeholders*

As the legislative history of the Williams Act reflects, and as noted above, Rule 13d-1(a)'s filing deadline is intended to "avoid[] upsetting the free and open auction market where buyer and seller normally do not disclose the extent of their interest and avoid[] prematurely disclosing the terms of privately negotiated transactions."[25] If implemented as contemplated, the Reporting Deadline Rule will drastically shorten the amount of time that a shareholder has to build an ownership stake in an issuer before the market learns of such interest, thereby disincentivizing critical shareholder engagement and monitoring activities at underperforming public companies. In other words, as further described below, by reducing the period during which a shareholder may

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21 *See* S. Rep. 90-550, at 10 ("This subsection would give shareholders who tender their shares immediately *after the offer is made* a short period within which to reconsider." (emphasis added)) (1967).

22 Ronald J. Gilson and Jeffrey N. Gordon, *The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights*, 113 COLUM. L. REV. 863, 907-09 (2013).

23 *See* Commissioner Hester M. Peirce, *Dissenting Statement on Proposed Modernization of Beneficial Ownership Reporting* (Feb. 10, 2022) (stating that "information disparities make markets function").

24 *Id*.

25 113 Cong. Rec. 856 (1967).

accumulate an ownership stake "before mandatory disclosure of its holding drives up the price of the target company's stock," [26] the Reporting Deadline Rule effectively undercuts the likelihood that an engaged shareholder can achieve a favorable return on its investment and, consequently, discourages shareholders from undertaking beneficial corporate engagement initiatives in the first instance.[27]

Prior to making a significant investment in a public company, engaged shareholders typically participate in substantial, costly, and time-consuming due diligence activities involving, in some instances, legal advisors, accountants, financial advisors, proxy solicitation firms, public relations firms, ESG consultants, and executive search firms. In conjunction with their advisors, shareholders work to identify value creation opportunities in the capital markets through an examination of a given issuer's financial performance, environmental and social impact, and governance structure. The cost of many of these diligence activities are fixed and the overall expense of diligence is particularly burdensome for smaller engaged shareholders who must justify the investment against both a smaller capital base and smaller position size in the target company. Increasingly, the efforts undertaken by engaged shareholders have yielded more than wealth creation for the investing public, as such shareholders have driven corporations to account for how their businesses and operations impact corporate stakeholders and society more broadly. However, an engaged shareholder "needs to anticipate recovering [its] costs and earning a favorable risk-adjusted return before it will enter the business in the first place and engage with identified companies."[28]

Engaged shareholders expect to recoup a fraction of their investment costs due to, and are often incentivized by, their "ability to purchase shares at prices that do not yet fully reflect the expected value of [their] future monitoring and engagement activities."[29] But, a shareholder's ability to realize the financial value of its engagement with a given issuer is typically lessened upon such shareholder's ownership interest becoming public.[30] That is, "empirical evidence shows that [a] target's stock price immediately appreciates upon disclosure of [an] activist's block,"[31] as the market adjusts to a pricing level that reflects the anticipated benefit of the engaged shareholder's involvement at the company,[32] making stake-building activities less economically efficient. Indeed, the theory of investor harm adopted by the Commission for purposes of the Reporting Deadline Rule recognizes the foregoing as fact (*i.e.*, the Proposing Release acknowledges that "[i]f an initial Schedule 13D were required to be filed more promptly, . . .

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[26] Gilson and Gordon, *supra* note 22, at 902.

[27] Lucian A. Bebchuk and Robert J. Jackson Jr., *The Law and Economics of Blockholder Disclosure*, 2 HARV. BUS. L. REV. 39, 49 (2012) ("It is well understood that the incidence and size of outside blocks, and the investments in value-enhancing activities made by outside blockholders, depend on the ability of outside blockholders to obtain returns that cover their costs.")

[28] Gilson and Gordon, *supra* note 22, at 902.

[29] Bebchuk and Jackson Jr., *supra* note 27, at 50.

[30] *See* Lucian A. Bebchuk, Robert J. Jackson Jr., and Wei Jiang, *Pre-Disclosure Accumulations by Activist Investors: Evidence and Policy*, 39 J. CORP. L. 1, 17 (2013) (explaining that tightening the SEC's rules under Section 13(d) would likely deter investors from accumulating large ownership blocks in public companies because "[r]educing the amount of time that investors have before they are required to disclose their position will likely reduce their profits—and, thus, their incentives to accumulate large blocks of public-company stock").

[31] Gilson and Gordon, *supra* note 22, at 902.

[32] Bebchuk and Jackson Jr., *supra* note 27, at 50.

investors might be able to sell their shares at a higher price, or they may re-evaluate their investment decisions").[33]

The Commission has, in other contexts, recognized the import of the stock price appreciation that occurs upon the publication of a shareholder acquiring a significant ownership interest in an issuer and the harm that results to the shareholder's investment program. Specifically, the Commission's Division of Investment Management grants, in certain instances, confidential treatment of information filed on Form 13F, including where the information would reveal an investor's ongoing program of acquisition or disposition of a reportable security. In a staff letter, the Commission took note that the legislative history of Section 13(f) emphasized that "generally it is in the public interest to grant confidential treatment to an ongoing investment strategy of an investment manager. Disclosure of such strategy would impede competition and could cause increased volatility in the market place."[34] The same concern is present here in a different form: "Reducing the size of the toeholds that activists can accumulate before disclosure reduces their returns"[35] and, consequently, their incentive and ability to advocate for change at target companies.

The harm created by the Reporting Deadline Rule is, thus, two-fold. First, if active shareholders are unable to establish an economically efficient pre-disclosure ownership stake, public company shareholders (and the economy more broadly) will be less likely to benefit from the improved stock price performance that often attends the monitoring and engagement activities pursued by engaged shareholders,[36] given that such shareholders would have difficulty justifying certain engagements with issuers. The consequence of a reduction in the ability of engaged shareholders to acquire a sufficient ownership stake at an economically rational price may be fewer campaigns at issuers and, accordingly, less corporate innovation and more market stagnation.[37]

Second, if engaged investors are less incentivized to enter the market, shareholders of all sizes (and regardless of their investment timeline) would be deprived of the benefits that result from the strategic, environmental, social, and governance enhancements identified through the diligence and resources of large blockholders that wield sufficient influence to drive corporate managers to assess potential areas of improvement. That is, "investors can also expect to lose some gains associated with the mere *possibility* that an activist will emerge to reduce agency costs and managerial slack because the probability that such investor will emerge will be reduced by the tightening of the rules under Section 13(d)."[38] The unintended effect of the Reporting Deadline Rule, in other words, will likely be to reduce managerial and corporate accountability to public company stakeholders both before and after an engaged shareholder emerges, as such shareholders

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33 Beneficial Ownership Reporting Release, at 129.

34 United States Securities and Exchange Commission, *Section 13(f) Confidential Treatment Requests* (June 17, 1998), *available at* https://www.sec.gov/divisions/investment/guidance/13fpt2.htm (quoting Report of Senate Comm. on Banking, Housing and Urban Affairs, S. Rep. No. 75, 94th Cong., 1st Sess. 87 (1975)).

35 Gilson and Gordon, *supra* note 22, at 904.

36 *See* Bebchuk, Jackson Jr., and Jiang, *supra* note 30, at 17-18.

37 *See* Gilson and Gordon, *supra* note 22, at 904 (2013) (". . . reducing the size of the toeholds that activists can accumulate before disclosure reduces their returns. The likely outcome would be that the activist sector would shrink, fewer firms would be identified as targets for strategic initiatives, and the activists would reduce costly campaign efforts.").

38 Bebchuk, Jackson Jr., and Jiang, *supra* note 30, at 18.

may be less likely to engage in any instance and, when they do, it may be without the necessary voting or economic influence to drive change, yielding a scenario where public shareholders remain invested in underperforming issuers.[39]

The harms articulated above will be most pronounced at micro-, small-, and mid-capitalization issuers (the "Subject Companies"), where the majority of active shareholder engagement occurs.[40] The ten days of permitted stake-building pre-disclosure is particularly important for engaged shareholders investing in smaller issuers with lower average trading volumes, as such a window allows for the ability to build a sufficient dollar stake to justify engagement. Additionally, the Subject Companies are statistically more likely to benefit from effective shareholder engagement and monitoring.[41] As the Commission has stated, issuers with smaller market capitalizations already have fewer third parties examining their businesses and strategies.[42] For example, (i) passive institutional shareholders rationally tend to allocate their efforts towards larger companies that comprise a larger percentage of their portfolios,[43] and (ii) media, private enforcement mechanisms (such as shareholder lawsuits), and public regulatory

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[39] Shareholder engagement is a scarce social resource. Few investors have the financial and political ability to attract and hold management's attention and effectively engage with a company for the benefit of all shareholders. *See* Edward B. Rock, *The Logic and (Uncertain) Significance of Institutional Shareholder Activism*, 79 GEO. L. J. 445, 455 (1991) ("Thus, shareholders of a corporation with at least one shareholder whose individual stake is large enough to justify the costs of disciplining management will be a privileged group, while shareholders of a corporation in which the dispersion of shareholding is such that no single shareholder has an incentive to discipline management will form a latent group.").

[40] According to FactSet, between April 7, 2019 and April 7, 2022, there were 1,346 campaigns launched at Russell 3000 companies, relative to 501 campaigns at S&P 500 companies during the same time period.

[41] For example, according to Deal Point Data, as of April 7, 2022, (i) 42.4% of all U.S.-incorporated Russell 3000 companies have a classified board and only 12.7% of all U.S.-incorporated S&P 500 companies have a classified board, (ii) 23.1% of all U.S.-incorporated Russell 3000 companies afford shareholders proxy access rights, while 83.1% of all U.S.-incorporated S&P 500 companies afford shareholders proxy access rights, (iii) 45.9% of all U.S.-incorporated Russell 3000 companies permit shareholders to call special meetings, whereas 68.4% of U.S.-incorporated S&P 500 companies permit shareholders to call special meetings, (iv) no U.S.-incorporated S&P 500 company has an active poison pill (exclusive of tax asset protection pills), but 22 U.S.-incorporated Russell 3000 companies have anti-activist pills (*i.e.*, non-tax asset protection pills) in effect, and (v) of the U.S.-incorporated Russell 3000 companies with an active poison pill (exclusive of tax asset protection pills), 54.5% use a trigger threshold of 10.0% or less and 77.3% use a trigger threshold of 15.0% or less.

[42] United States Securities and Exchange Commission, Staff Report on the Issues Affecting the Provision of and Reliance Upon Investment Research Into Small Issuers, at 7 (2021) (". . . [S]mall issuers are less likely than large issuers to be covered by research coverage. Specifically, the availability of research coverage and the number of analysts covering an issuer correlate with market capitalization. In recent years, approximately 60% of small issuers have received research coverage while approximately 90% of large issuers have received coverage. Furthermore, small issuers received coverage by approximately two analyst firms on average while large issuers received coverage by approximately nine analyst firms on average." (internal citations omitted)).

[43] *See* Kobi Kastiel and Yaron Nili, *The Corporate Governance Gap*, 131 YALE L. J. 782, 805 (2022) ("As studies show, in order to keep their fees low, investors, especially index funds, with limited resources and incentives to invest in engaging with public firms must prioritize their targets and resources. . . . When [index] investors do engage with portfolio companies, they tend to prefer large-capitalization companies, rather than small ones. In the case of small firms, the costs of engagement are somewhat the same, but the potential benefits from such activities are reduced, given that they represent a smaller fraction of the portfolio of institutional investors. For this reason, institutional investors do not have adequate incentives to invest resources in engaging with and changing the governance structure of small companies." (internal citations omitted)).

bodies similarly exhibit an enhanced focus on larger firms.[44] Reducing the probability that an engaged shareholder will provide effective corporate oversight further narrows the pool of external auditors at companies that more frequently engage in troublesome business,[45] environmental, social, and governance practices.[46] Thus, the rule change will most discourage engagement at the very companies who are statistically most likely to benefit from engagement—a double blow for the shareholders of these firms.

The Reporting Deadline Rule does not serve the balance that Senator Williams sought to strike when advancing the beneficial ownership regime adopted as part of the Williams Act. Rather, it overturns such balance and upsets the market dynamics that the legislative history of the Williams Act indicates Congress sought to preserve. Ultimately, a significant reduction in Rule 13d-1(a)'s filing window may exacerbate any principal-agent problem that exists between corporate managers and shareholders, given that an engaged shareholder will be less capable of ensuring that managers are advancing shareholder interests and not their own.

C. *Technology-Based Reasons Are Not Sufficient To Justify Material Changes To Rule 13d-1(a)'s Ten-Day Deadline*

The Proposing Release states that the primary purposes of Section 13(d) are "to provide information to the public and the subject issuer about accumulations of a covered class by persons who ha[ve] the potential to change or influence control of such issuer and to regulate rapid accumulations of beneficial ownership that occur[] within a short period of time. . . ."[47] As explained above, in our view, the Commission and other proponents of the Proposed Rules have not demonstrated a compelling justification for the Reporting Deadline Rule. Nor have the Commission and the other proponents of the Proposed Rules exhibited why an amendment to Rule

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44 *Id.* at 815-20 (finding that smaller companies are less likely than larger companies to be covered by analysts, media, and public and private enforcers).

45 *See*, *e.g.*, *id.* at 818 ("Public enforcement is also a critical disciplining mechanism. This type of enforcement is significantly more crucial to small firms, as these firms are associated with a high incidence of fraud." (citations omitted)).

46 According to Glass Lewis, "[p]rogress on overall board gender parity remains slow and incremental." Glass Lewis, *Proxy Season Review 2021: United States*, at 19 (2021). The gender imbalance is such that women hold only 25.4% of the directorships at Russell 3000 companies, a figure that lags behind the S&P 500 by nearly 6%. Glass Lewis, *Proxy Season Review 2021: United States*, at 20 (2021); EY Center for Board Matters, *Corporate Governance by the Numbers* (as of December 31, 2021). Further, at Russell 3000 companies, Glass Lewis recommended, during the 2021 proxy season, director "against" or "withhold" votes at (i) 103 issuers due to an affiliate or insider having committee representation (compared to 13 companies in the S&P 500), (ii) 14 issuers due to board attendance (compared to one company in the S&P 500), (iii) 21 issuers due to auditors not being up for ratification (compared to one company in the S&P 500), (iv) 41 issuers due to a lack of board gender diversity (compared to zero companies in the S&P 500), (v) 42 issuers due to the chief financial officer serving as a director (compared to three companies in the S&P 500), (vi) 81 issuers due to insufficient board independence (compared to two companies in the S&P 500), (vii) 24 issuers due to a material weakness in financial reporting (compared to zero companies in the S&P 500), (viii) 106 issuers due to there being no lead director (compared to nine companies in the S&P 500), (ix) 43 issuers due to ongoing compensation concerns (compared to 11 companies in the S&P 500), (x) 78 issuers due to director overboarding (compared to 19 companies in the S&P 500), (xi) 58 issuers due to related party transactions (compared to three companies in the S&P 500), and (xii) 49 issuers due to holding virtual-only shareholder meetings that limited shareholder participation (compared to one company in the S&P 500). Glass Lewis, *Proxy Season Review 2021: United States*, at 58 (2021).

47 Beneficial Ownership Reporting Release, at 17.

13d-1(a) is needed to adequately support the regulatory objectives of Section 13(d). Assuming, however, for purposes of this letter, that a persuasive reason to dramatically reduce the amount of time that a person who acquires more than 5% of a covered class of equity securities has to file an initial Schedule 13D did exist, the Reporting Deadline Rule would still be unnecessary for purposes of Section 13(d), in light of the governance mechanisms and informational tools currently available to issuers and the public.

Like the technological landscape, the legal landscape has evolved since the passage of the Williams Act. During the period since 1968, the majority of states have adopted antitakeover statutes that shield against unwanted changes in corporate control and that otherwise help to entrench management.[48] State takeover statutes, in their various formulations and numerous varieties, have had their intended effect of making takeovers by outside blockholders more difficult.[49] Further, the advent of the poison pill effected a seismic shift in the balance of power between corporations and shareholders seeking to acquire large blocks of securities,[50] as the Proposing Release recognizes.[51] Today, and as further illustrated below, using publicly available information, issuers are able to preempt the filing of an initial Schedule 13D with the adoption of a poison pill and prevent additional share accumulations within Rule 13d-1(a)'s ten-day filing window.

In addition to the above protections provided by state law, after the enactment of the Williams Act, Congress passed Section 13(f) of the Securities Exchange Act of 1934 to increase the public availability of information regarding securities ownership of institutional investors.[52] Since the final rules related to the filing and reporting requirements of institutional investment managers were announced in 1979, issuers and their advisors have used Form 13F as a key tool to identify, monitor, and prepare for engagement with shareholders. In that light, Form 13F has buttressed Schedule 13D by providing information to the public and issuers about ownership interests in covered securities, facilitating the identification of persons that might have the potential

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[48] *See* Lucian A. Bebchuk and Allen Ferrell, *Federalism and Corporate Law: The Race to Protect Managers from Takeovers*, 99 COLUM. L. REV. 1168, 1177-78 (1999).

[49] *See* Bebchuk and Jackson Jr., *supra* note 27, at 56 ("To begin, those who might consider buying an outside block as a 'toehold' prior to acquiring a control block—the case that the drafters of the Williams Act devoted much attention to—now face formidable impediments that did not exist when the Williams Act was passed. In particular, state law now allows boards to use poison pills to block hostile tender offers. Because of the substantial legal impediments to hostile takeover bids, the incidence of such bids is low. Today, active outside blockholders filing a Schedule 13D are commonly not expected to seek to acquire control, but rather to monitor and engage with management and fellow shareholders.").

[50] According to Deal Point Data, there was one hostile tender offer launched in 2021.

[51] Beneficial Ownership Reporting Release, at 113-14 ("In addition, the legal landscape has evolved since the passage of the Williams Act. Hostile tender offers, once a prominent hallmark of the takeover wave in the 1980s, have become comparatively rare since the development and widespread adoption of the 'poison pill' shareholder rights plan in the 1980s as an anti-takeover device." (citing Marcel Kahan and Edward Rock, *Anti-Activist Poison Pills*, 99 B.U. L. REV. 915, 922-23 (2019) ("In effect, the poison pill moved the decision on the success of a hostile bid from shareholders voting with their feet (by tendering their shares in a tender offer) to shareholders voting by ballot (by replacing a majority of the board). . . . To get a rough sense of the current prevalence of toeholds, we collected data from Thompson Reuters on proposed takeovers that were classified as hostile. There were twenty-four such proposals between 2010 and 2015."))).

[52] *See* U.S. Securities and Exchange Commission, Office of Inspector General, Office of Audits, *Review of the SEC's Section 13(f) Reporting Requirements*, Report No. 480, at iv (Sept. 27, 2010).

to influence the control of an issuer or otherwise have an interest in accumulating a significant beneficial ownership position.

Further, to the extent that advancements in information technology factor into the Commission's calculus regarding the desirability and propriety of the Reporting Deadline Rule, such advancements should be considered in the context of how they impact the securities markets generally. The Proposing Release notes that, "given advances in the information technologies used by market professionals today, less time is needed to compile the necessary data and prepare and transmit the Schedule 13D to the Commission than was required in 1968."[53] The Proposing Release continues by asserting that Rule 13d-1(a)'s ten-day filing window "raises concerns that material information about potential change of control transactions is not being disseminated to the public in a manner that would be considered timely in today's financial markets."[54] However, the Proposing Release seemingly does not confront the issuer-specific advancements in information technology that provide public companies with the benefit of nearly-contemporaneous insight into their shareholder base. Specifically, sophisticated issuers engage stock watch firms that provide regular updates on transactions in the company's securities, and such firms (or the issuer's proxy solicitation firm) are frequently able to identify, utilizing information with respect to the custodians executing the relevant trades, the transacting shareholder and a range of how many shares such shareholder owns at a given moment in time. This technological advancement in shareholder monitoring, as it relates to the issuer, renders irrelevant any purported delay in reporting material information. To be certain, information technologies provided by stock watch firms counterbalance (if not outweigh) new word processing efficiencies and any perceived information asymmetries used to justify the Reporting Deadline Rule.

In an effort to contextualize the foregoing, Irenic respectfully refers the Commission to Engaged Capital, LLC's ("Engaged Capital") 2018 investment in Del Frisco's Restaurant Group, Inc. ("DFRG"). There, over the course of approximately two months, Engaged Capital accumulated an ownership interest in DFRG requiring a filing under Section 13.[55] According to the Schedule 13D filed by Engaged Capital, the shareholder crossed the 5% ownership threshold on November 26, 2018.[56] On December 5, 2018, DFRG issued a press release stating that the company had "recently observed unusual and substantial activity in [DFRG's] shares."[57] Based on DFRG's disclosure, the company apparently used information technology of the kind that was unavailable when the Williams Act was enacted to "observe[]" transactions in its securities by a then-unidentified shareholder that rose to the level of needing to implement a poison pill in advance of any Schedule 13D filing confirming that an individual shareholder had crossed the 5% threshold. On the morning of December 6, 2018, prior to market open, DFRG filed a Form 8-K with the Commission divulging that it had implemented a poison pill with a 10% trigger

[53] Beneficial Ownership Reporting Release, at 16.
[54] *Id.*
[55] Engaged Capital, LLC, Schedule 13D, filed December 6, 2018, *available at* https://www.sec.gov/Archives/edgar/data/1415301/000092189518003208/sc13d09455033_12062018.htm.
[56] *Id.*
[57] Del Frisco's Restaurant Group, Inc., Press Release, *Del Frisco's Restaurant Group Adopts Short-Term Shareholder Rights Plan* (Dec. 5, 2018), *available at* https://www.sec.gov/Archives/edgar/data/1415301/000119312518342873/d669807dex991.htm.

threshold.[58] Later on December 6, 2018, Engaged Capital filed its initial Schedule 13D, disclosing a 9.99% stake in DFRG. In sum, with the benefit of issuer-specific advancements in information technology, DFRG was able to identify real-time transactions in its securities by a single shareholder and preempt a Schedule 13D filing with a poison pill utilizing a trigger threshold 0.01% higher than the position accumulated by Engaged Capital.

We respectfully submit that the technology-based reasons for the Reporting Deadline Rule are neither compelling nor sufficient to justify material changes to Rule 13d-1(a). Nonetheless, if the Commission is persuaded by such justifications, we urge the SEC, in connection with its final rulemaking processes, to further consider and analyze how information technologies have evolved in a manner that serves the primary purposes of Section 13(d), including how such technologies provide contemporaneous ownership information to issuers.

D. *Rule 13d-1(a)'s Ten-Day Deadline Still Serves The Primary Purposes of Section 13(d)*

Irenic welcomes the Commission's efforts to protect investors and ensure a fair and efficient marketplace, but does not believe that the Proposed Rules effectively achieve those ends. From our perspective, the efforts to modernize beneficial ownership reporting in the manner contemplated by the Proposed Rules—and the Reporting Deadline Rule in particular—may have the opposite effect, as described herein. Moreover, our concerns are deepened by the absence of a cogent need for the Reporting Deadline Rule relative to the purposes of the Williams Act.

As the Proposing Release recognizes, present day corporate control contests are meaningfully different than those which existed at the time that the Williams Act was implemented and immediately thereafter. "Today's market for corporate control features activist investors, particularly activist hedge funds, who seek to influence governance through accumulation of strict minority equity stakes instead of full control."[59] However, the aforementioned "sole purpose"[60] of the Williams Act is to protect investors from coercive tender offers, not from other shareholders who accumulate minority stakes through open market purchases that afford neither control nor negative control of an issuer.[61] Rule 13d-1(a)'s ten-day deadline still serves such purpose and activist hedge funds that most commonly hold ownership stakes below 10% of an issuer's outstanding voting shares, which typically seek ESG-related reforms by means of a shareholder vote or through negotiations with an issuer, and that are fundamentally different in both their methods and purposes than "corporate raiders" do not jeopardize the objectives of the Williams Act.

If, despite the positions set forth herein and in other comment letters in opposition to the Reporting Deadline Rule, the Commission nonetheless believes that the primary purposes of

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58 Del Frisco's Restaurant Group, Inc., Form 8-K, filed December 6, 2018, *available at* https://www.sec.gov/Archives/edgar/data/0001415301/000119312518342873/d669807d8k.htm.

59 Beneficial Ownership Reporting Release, at 107-08 (citations omitted).

60 *Piper*, 430 U.S. at 35.

61 *See* 113 Cong. Rec. 855 (1967) (". . . anyone acquiring securities which would give him more than 10 percent of a class of an equity security registered under the Securities Exchange Act would be required to file this information with the SEC. This is the only way that corporations, their shareholders and others can adequately evaluate a tender offer or the possible effects of a change in substantial shareholdings.").

Section 13(d) are no longer being served by Rule 13d-1(a) "in light of advances in technology and developments in the financial markets,"[62] we urge the SEC to consider implementing reforms to Rule 13d-1(a) through the so-called "tiered approach,"[63] without any limitation on acquisitions during the period between the time that the investor acquires more than 5% of a covered class of equity securities and the time that the initial Schedule 13D is filed. Specifically, a tiered approach designed to vary the reporting deadline for an initial Schedule 13D based on the issuer's market capitalization (the "Issuer Metric") would be less problematic than the Reporting Deadline Rule, although still undesirable relative to the status quo.

With respect to the Issuer Metric, we believe that Rule 13d-1(a)'s ten-day reporting deadline should be preserved for the Subject Companies. Due to lower average trading volumes at the Subject Companies,[64] economically and temporally efficient stake-building is more challenging for shareholders relative to investments in large- and mega-capitalization issuers. Maintaining the existing reporting requirements at the Subject Companies will meaningfully curtail the potential harms stemming from the Reporting Deadline Rule and, by definition, affect fewer filers and issuers, lowering the costs of the Proposed Rules. That is, using the Issuer Metric to determine the time at which an initial Schedule 13D filing need be made may serve to limit the impact that reforms to Rule 13d-1(a) have on shareholder engagement and monitoring, particularly at the Subject Companies, where, as established, such effective engagement and monitoring is most necessary.[65]

III. Conclusion

Engaged shareholders perform vital engagement and monitoring functions within the public company ecosystem, but, if the Reporting Deadline Rule is implemented, fewer will expend the labor, time, and expense necessary to catalyze superior share price performance at underachieving companies. This is particularly true in the case of smaller engaged shareholders with less deployable capital, fewer resources, and a more inflexible portfolio company base than larger active shareholders with greater capital reserves. The Reporting Deadline Rule, and the attendant restrictions on efficient stake-building activities, introduce a potentially significant roadblock for smaller investors with narrower margin for investment program error, potentially yielding fewer investments that facilitate capital formation and growth for issuers, especially those with smaller market capitalizations. Further, while the Proposed Rules directly impact only a small subset of institutional investors,[66] their repercussions will be more widespread, depriving the

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62 Beneficial Ownership Reporting Release, at 18.

63 *See* Beneficial Ownership Reporting Release, at 24, 152-53.

64 Kastiel and Nili, *supra* note 43, at 809 (noting that "[t]here are also disadvantages of engaging with small firms," including that "small firms have relatively less liquid stock than large firms do, which creates hurdles to accumulating a large nonmajority position and then selling it once the hedge fund is willing to exit").

65 Academics have called for regulators to consider the particular governance challenges of the Subject Companies when engaging in rulemaking, including in light of the shallower external auditor pool. *Id.* at 855-56 ("Regulators, too, need to acknowledge the governance gap and the underlying disparity in investor attention and activism that could contribute to change. . . . There are many avenues to address both approaches, but here we highlight two. First, regulators may need to creatively promote practices that make it easier for governance debates to take place in small-cap corporations. . . . A second possible solution is to ease the regulatory environment under which current activist shareholders operate, enhancing their ability to engage with small companies and initiate governance changes through the submission of proposals.").

66 According to Insightia, activist shareholders had $244 billion in assets under management during 2021.

public of the short- and long-term wealth generation that attends the investment of an engaged shareholder, increasing the vulnerability of public investors to managerial slack, and impeding crucial environmental, social, and governance advancements that have profound societal benefits.

The Proposed Rules materially jeopardize the status quo, and they do so without a compelling justification and in a manner that will likely lead to a reduction in managerial accountability, corporate innovation, and evolution in the capital markets. Irenic respectfully requests that the Commission abandon the Proposed Rules, which further tip the balance in favor of issuers and corporate executives. We unequivocally agree that investor protection is essential to the functioning of our free and open markets, but we fear that the Reporting Deadline Rule will have the opposite effect by precipitating investor harm, leaving issuers without effective checks and balances, and dramatically reducing shareholder-driven campaigns aimed at strategic, environmental, social, and governance enhancements.

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Irenic appreciates the opportunity to provide comments on the Proposed Rules. We would be happy to provide you with further information to the extent that you would find it useful.

Respectfully submitted,

/s/ Adam Katz

Adam Katz
Co-Founder and Chief Investment Officer
Irenic Capital Management LP

cc: The Honorable Gary Gensler, Chair
The Honorable Hester M. Peirce, Commissioner
The Honorable Allison Herren Lee, Commissioner
The Honorable Caroline A. Crenshaw, Commissioner
Nicholas Panos, Division of Corporate Finance
Valian Ashfar, Division of Corporate Finance