

April 11, 2022

Vanessa Countryman  
Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-0609

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

Dear Ms. Countryman,

We are professors who write, teach, and study business law and securities regulation, including issues with respect to investor communications and activism. We write regarding the proposed rules relating to the “Modernization of Beneficial Ownership Reporting presented in Release Nos. 33-1103; 34-94211 (the “Release,” or “Proposed Rules”).<sup>1</sup> Specifically, we are focused on proposed amendments to Rules 13d-5 and 13d-6 and the discussion in the Release of the circumstances under which persons will be deemed to have formed a “group” that would be subject to beneficial ownership reporting obligations.<sup>2</sup> These amendments, as the Release recognizes, raise concerns among investors as to whether their communications or other activities would constitute formation of a group.<sup>3</sup>

Our concern is one the Commission highlights in the Release: discouraging communicative action among shareholders engaged in shareholder governance.<sup>4</sup> Investor communications regarding corporate policy issues with broad societal impact have been increasing in recent

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<sup>1</sup> An early draft of this comment letter was drafted by staff of the International Institute of Law and Finance, a non-profit, non-partisan corporation.

<sup>2</sup> The Release states that “[t]hese amendments would 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.” Release, at 78.

<sup>3</sup> “We recognize that our proposal to amend Rule 13d-5, as discussed above, may raise concerns among investors as to whether their communications and other activities with other investors would constitute the formation of a group. We also recognize the possibility that additional exemptions may be warranted to address situations in which beneficial ownership reporting under Section 13(d) or 13(g) by a group would be unnecessary from an investor protection standpoint or even contrary to the public interest. Specifically, we are aware that activity exists among shareholders, investors, holders of derivatives and other market participants that may, absent an exemption, implicate Sections 13(d)(3) and 13(g)(3). For example, institutional investors or shareholder proponents may wish to communicate and consult with one another regarding an issuer’s performance or certain corporate policy matters involving one or more issuers. Subsequently, those investors and proponents may take similar action with respect to the issuer or its securities, such as engaging directly with the issuer’s management or coordinating their voting of shares at the issuer’s annual meeting with respect to one or more company or shareholder proposals.” Release, at 90.

<sup>4</sup> See *id.*

years, and expressive conduct surrounding these issues is increasingly frequently associated with shareholder activists and their activities.<sup>5</sup> Engine No. 1’s campaign against ExxonMobil is a prominent example of how investors increasingly are siding with shareholder activists on significant social policies. Though investor activism on significant social policy issues is on the rise in the twenty-first century, it has deep historical roots. For example, new research shows that, as far back as the Progressive Era, investors engaged in expressive activity and shareholder activism to raise issues with a broad societal impact regarding labor practices.<sup>6</sup>

We urge the Commission to consider the extent to which ambiguity in the Proposed Rules could deter investors from communicating about these important social issues and engaging in shareholder governance activities, such as identifying and discussing significant social policy issues, sponsoring shareholder proposals, communicating about proposals, and negotiating proposals with corporate management. The Release does not cite data or academic literature that identifies flaws in the current, common-law-style approach to determining when investors are acting for the purpose of acquiring, holding, or disposing of securities (and therefore are part of a “group”). A change to the rules that upends the existing approach could deter important and socially valuable shareholder communication that has long been considered essential to shareholder governance.

We are especially troubled by the vague language in the SEC’s proposed exemption from the “group” definition. We imagine an investor considering communicating with a shareholder activist about an important social issue who reads the Commission’s warning about chilling communications, and then seeks refuge in the safe harbor described below. We imagine this investor pausing at words such as “solely,” “only,” “indirectly,” “purpose,” “effect,” or “contemplated” in the following sentences from the Release, and worrying about whether this language would protect them from a future government official’s inquiry:

We recognize the potential risk of chilling such communications. We therefore are also proposing amendments to Rule 13d-6 to exempt certain actions taken by two or more persons from the scope of Sections 13(d)(3) and 13(g)(3). In addition to proposed Rule 13d-6(d), which we discussed in Section III.C.2.b above, proposed Rule 13d-6(c) would provide that two or more persons will not be deemed to have acquired beneficial ownership of, or otherwise beneficially own, an issuer’s equity securities as a group solely because of their concerted actions related to an issuer or its equity securities, including engagement with one another or the issuer. This exemption would only be available if such persons, when taking such concerted actions, are not directly or indirectly obligated to take such actions and communications among or between such persons are not undertaken with the purpose or the effect of changing or influencing

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<sup>5</sup> See, e.g., Geeyoung Min & Hye Young You, *Active Firms and Active Shareholders: Corporate Political Activity and Shareholder Proposals*, 48 J. LEG. STUD. 81, 85-88 (2019) (describing the growth in use and the expressive nature of the shareholder proposal).

<sup>6</sup> See, e.g., Sarah C. Haan, *Corporate Governance and the Feminization of Capital*, 74 STAN. L. REV. 515, 541-42 (2022) (describing Progressive Era shareholder activism to reform labor practices at major companies).

control of the issuer. This exemption would, therefore, exclude activity that is not contemplated within the purpose of Section 13(d).<sup>7</sup>

Unfortunately, the Release does not specifically discuss the types of communications or activities that might be covered, or not covered, by any new rules, or the extent to which language in the proposed exemption from the new “group” definition might protect particular types of communications or activities.<sup>8</sup> Instead, the Release recognizes the potential for chilling communications or activities, and attempts to provide comfort as follows:

Additionally, by removing any potential misimpression that an agreement must exist for determining whether a group is formed, the proposed amendments could potentially chill shareholder communications in general, as shareholders may be uncertain whether their coordination constitutes “acting as” a group. As discussed in Section II.D.1., shareholders may choose to communicate with one another regarding an issuer’s performance or a certain policy matter, and they may take similar action with respect to the issuer or its securities, such as aligning their voting of shares at the issuer’s annual meeting with respect to one or more proposals. We recognize the potential risk of chilling such communications. We therefore are also proposing amendments to Rule 13d-6 to exempt certain actions taken by two or more persons from the scope of Sections 13(d)(3) and 13(g)(3). In addition to proposed Rule 13d-6(d), which we discussed in Section III.C.2.b above, proposed Rule 13d-6(c) would provide that two or more persons will not be deemed to have acquired beneficial ownership of, or otherwise beneficially own, an issuer’s equity securities as a group solely because of their concerted actions related to an issuer or its equity securities, including engagement with one another or the issuer. This exemption would only be available if such persons, when taking such concerted actions, are not directly or indirectly obligated to take such actions and communications among or between such persons are not undertaken with the purpose or the effect of changing or influencing control of the issuer. This exemption would, therefore, exclude activity that is not contemplated within the purpose of Section 13(d).<sup>9</sup>

The Release then further asks: “Are there actions taken among shareholders other than the ones that we have proposed to exempt that the Commission should consider exempting?”<sup>10</sup>

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<sup>7</sup> Release, at 147.

<sup>8</sup> The Release states that “the beneficial ownership reporting system is not intended to impede communications among shareholders or between proponents and issuers that are not undertaken with the purpose or effect of changing or influencing control of an issuer,” Release at 90. As examples of the types of shareholder activity that are not deemed to be undertaken to change or influence control of the issuer, the Release refers to “institutional investors or shareholder proponents communicat[ing] and consult[ing] with one another regarding an issuer’s performance or certain corporate policy matters involving one or more issuers,” Release at 95.

<sup>9</sup> Release, at 147.

<sup>10</sup> Release, at 94.

The answer to this question is yes: the Commission should consider the circumstances under which investors advocating for specific changes (e.g., board composition or diversity) might later be subjected to an inquiry about whether their communications or activities were protected by the exemptions. Given the interpretive questions surrounding much of the above language, as well as the concerns expressed in the Release, the implications for this group of investors are potentially serious. Investors might justifiably be concerned about the degree of protection that would be offered by an exemption given the use of terms such as “solely,” “only,” “indirectly,” “purpose,” “effect,” and “contemplated.”

Moreover, the Commission should consider the costs imposed on investors who might seek protection from this exemption, even given its ambiguity. At minimum, they would need to obtain legal advice regarding the application of Rule 13d-6(c), and then become sufficiently comfortable that they would not be deemed to have acquired beneficial ownership of, or otherwise beneficially own, an issuer’s equity securities as a group. The additional costs and risks associated with obtaining such assurances and related compliance could deter investors from engaging in communications and activities that otherwise would have been helpful in promoting greater awareness about important social concerns. The Release does not address these potential costs and risks.

The kinds of communications we describe here are protected expression, and thus restraints on these communications may lead to claims that the Proposed Rules burden investors’ First Amendment rights. The SEC should take care to minimize any burdens on investors’ expression and thereby to avoid First Amendment claims by investors. Even if the Proposed Rules survived a challenge on free speech grounds, the litigation itself could result in new law imposing rigorous First Amendment review on securities regulations. The litigation itself would also likely discourage investors from engaging in important expressive conduct.

Many investors who are active on social issues lack the resources to file a Schedule 13D or implement compliance systems to monitor issues related to the requirement to file a Schedule 13D. Most social activists are not Schedule 13D filers, and are unlikely to want to take on the risk of an after-the-fact prosecution for failure to file a Schedule 13D. For all of these reasons, we are concerned that investors would shy from communications when a shareholder activist has purchased a significant block of shares (or has a significant swaps position) in a targeted company.

In sum, various investors have begun advocating on significant social policy issues in ways that future Commission officials under the Proposed Rules might later deem to have been part of a “group.” Increasingly, investors are focused on corporate issues of broad societal impact, including various aspects of environmental, social, and governance issues. The proposed new definition of “group” could deter investors from engaging in socially valuable activism, and could lead to claims that the Proposed Rules violate investors’ First Amendment rights. Careful

drafting is imperative, both to advance efficient and socially-beneficial shareholder governance, and to avoid costly, time-consuming litigation that may subject securities regulation to more stringent First Amendment review than historically has applied.

Thank you for your consideration.

Respectfully,

- Benjamin Edwards, *Associate Professor of Law, University of Nevada, Las Vegas, William S. Boyd School of Law*
- Sarah C. Haan, *Professor of Law, Washington and Lee University School of Law*
- Geeyoung Min, *Assistant Professor of Law, Michigan State University College of Law*
- Cary Martin Shelby, *Professor of Law, Washington and Lee University School of Law*
- Faith Stevelman, *Professor of Law, New York Law School*