



COVID-19 Update

April 2020

Shareholder Activist Filings in Light of the COVID-19 Pandemic

As funds and other activist shareholders build positions through the open market, by participating in company securities offerings, or by otherwise taking advantage of buying opportunities in light of reduced company market caps and market volatility generated by the COVID-19 pandemic, below are some filing triggers to keep in mind in order to avoid regulatory violations. Although references below are to “funds,” the same filing triggers apply to family offices, activist directors, and other individuals and groups exceeding specified thresholds. With reduced market caps, investors should pay special attention to filing thresholds.

Reporting Investments on Schedules 13D/G

When an investment exceeds 5% of a voting class of a public company’s equity securities, a Schedule 13D or 13G is required to be filed with the Securities and Exchange Commission (SEC) within 10 days of crossing the 5% threshold. Warrants, stock options, convertible preferred stock, convertible notes, and any other securities that are exercisable or convertible into equity within 60 days are included in determining if 5% is exceeded. Although a Schedule 13G is a shorter, simpler form, if an investment is made with a “control” intent, such as when a fund intends to seek board representation and/or plans to propose changes at the company, a Schedule 13D is required. If a fund crosses the 5% threshold and intends to engage in discussions with a company, a Schedule 13D is almost always advisable. In addition, when an investment changes by 1% of the company’s outstanding equity securities, an activism campaign develops, or other material changes occur, an amendment to Schedule 13D is required to be filed “promptly.” The SEC’s recently announced relief that could be utilized to extend filing deadlines in light of the

COVID-19 pandemic is not applicable to Schedule 13D filings.

Reporting Trades on Forms 3/4

When an equity investment exceeds 10% of a public company’s outstanding equity securities or when a fund obtains board representation, a fund becomes subject to Section 16 of the Securities Exchange Act. By obtaining board representation, the fund itself can become subject to Section 16 filings under the “director by deputization” theory. Although in some cases safeguards can be implemented to separate a board representative’s decisions and Section 16 obligations from those of the fund itself, in other cases these safeguards are impracticable, particularly when the board representative oversees capital allocation and makes voting and investing decisions at the fund. Section 16 requires the filing of beneficial ownership reports, including the filing of an initial report within 10 calendar days after crossing the 10% ownership threshold or the appointment of a representative to the board of directors, and the filing of subsequent reports on Form 4 within two business days after an acquisition or disposition of securities. The SEC’s COVID-19 relief does not apply to deadlines for Section 16 filings.

Section 16 “Short Swing” Profits, Profit Disgorgement, and Insider Trading

Section 16 also imposes strict profit disgorgement for any purchases and sales occurring within six months of one another, with “profits” calculated by matching the highest sales price with the lowest purchase price within a six-month period and disgorgement potentially occurring even

when actual losses – rather than profits – are realized. It is advisable to carefully structure transactions when entering or exiting a 10% ownership position to avoid Section 16 “short swing” profit disgorgement. If consistent with a fund’s strategic plans for the company, a 9.99% beneficial ownership “blocker” may be included when participating in company securities offerings to eliminate potential Section 16 issues. Some states have little-known profit disgorgement statutes that are similar to Section 16 restrictions.

When board representation is obtained, Section 16 obligations may continue for up to six months after a fund’s representative steps down from the board even if the fund’s holdings are below 10% at that time. Board representation may also require compliance with the company’s insider trading policy and the company’s trading blackouts imposed upon insiders. Plaintiff firms monitor public company trades and act quickly when there is a potential match for profit disgorgement. The SEC also brings enforcement actions for insider trading violations as well as for reporting violations, especially when there is a historical pattern of missing or delinquent Schedule 13D and Section 16 filings.

13F, “Large Trader,” and HSR Filings

Institutional investment managers with at least \$100 million in equity assets under management are required to file a Form 13F, listing their holdings of 13F securities. The filing is due within 45 days of each quarter-end.

If trades are sufficiently large, “large trader” filings and filings under the Hart-Scott-Rodino Antitrust Improvements Act (HSR Act) may also be triggered. A trade that equals or exceeds two million shares or \$20 million worth of shares in a day, or 20 million shares or \$200 million worth of shares in a month, could trigger a “large trader” filing on Form 13H. In such case, the initial filing is required to be made “promptly,” which generally means within 10 days after the transaction for the purposes of this filing, with annual filings to follow. “Large trader” filings are not publicly accessible.

The size-of-transaction test under the HSR Act is generally triggered if, following an acquisition of securities, a fund will hold in the aggregate voting securities of a company valued

at more than \$94 million (with the dollar threshold adjusted annually). HSR filings are required in advance of the transaction and impose a 30-day waiting period. Penalties for non-compliance can be significant. For example, in 2016, ValueAct entered into a \$11 million settlement with the Department of Justice, which alleged that ValueAct violated the HSR Act by improperly relying on filings exemptions.

Analysis of the filing triggers noted above and potential exemptions is highly dependent on the specific facts and circumstances and should be analyzed in connection with each investment.

FOR MORE INFORMATION

For more information, please contact:

Jurgita Ashley

216.566.8928

Jurgita.Ashley@ThompsonHine.com

or any member of our [Corporate Transactions & Securities](#) practice’s Takeovers and Shareholder Activism subgroup.

ADDITIONAL RESOURCES

We have assembled a firmwide multidisciplinary task force to address clients’ business and legal concerns and needs related to the COVID-19 pandemic. Please see our [COVID-19 Task Force web page](#) for additional information and resources.

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