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VIA OVERNIGHT MAIL

July 5, 2011

Ms. Elizabeth M. Murphy
Secretary, Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: "Petition for Rulemaking Under Section 13 of the Securities Exchange Act of 1934" filed by Wachtell, Lipton, Rosen & Katz on March 7, 2011

Dear Ms. Murphy:

The undersigned submit this letter in connection with the "Petition for Rulemaking Under Section 13 of the Securities Exchange Act of 1934" that Wachtell, Lipton, Rosen & Katz ("Wachtell") sent you on March 7, 2011 pursuant to Rule 192(a) of the Rules of Practice and Rules on Fair Fund and Disgorgement Plans of the Securities and Exchange Commission.

Alon Brav is professor of finance at the Fuqua School of Business, Duke University. J.B. Heaton is a partner with Bartlit Beck Herman Palenchar & Scott LLP in Chicago.¹ Wei Jiang is professor of finance and economics at Columbia Business School.

We respectfully request that the Secretary transmit this letter to the Commission for consideration along with the Wachtell petition.

Wachtell proposes that the Commission shorten the time for disclosing ownership under Section 13(d) of the Exchange Act from ten days to one day because, Wachtell asserts, the current ten day period facilitates "market manipulation and abusive tactics."² Wachtell asserts:

¹ J.B. Heaton's views are his own and do not necessarily represent the views of Bartlit Beck Herman Palenchar & Scott LLP or its clients.

² Available at <http://www.sec.gov/rules/petitions/2011/petn4-624.pdf> (last accessed on July 5, 2011). Section 13(d) provides that the Commission may shorten the time for reporting from within ten days to "within such shorter time as the Commission may establish by rule." 15 U.S.C. § 78m.

³ *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 60 (1975).

² Available at <http://www.sec.gov/rules/petitions/2011/petn4-624.pdf> (last accessed on July 5, 2011). Section 13(d) provides that the Commission may shorten the time for reporting from within ten days to "within such shorter time as the Commission may establish by rule." 15 U.S.C. § 78m.

[T]he ten-day reporting lag leaves a substantial gap after the reporting threshold has been crossed during which the market is deprived of material information, and creates incentives for abusive tactics on the part of aggressive investors prior to making a filing. Such investors may – and frequently do – secretly continue to accumulate shares during this period, acquiring substantial influence and potential control over an issuer without other shareholders (or the issuer) having any information about the acquirer or its plans and purposes at the time stockholders sell their shares.

We disagree with certain aspects of Wachtell’s proposals.

First, in a comprehensive dataset of hedge fund activism during 2001 to 2007, we find that more than 50 percent of hedge fund activists file their initial Schedule 13D *before* day ten, with more than 30 percent filing before day *six*. While Wachtell cites two examples where the same hedge fund activist (Pershing Square) increased its stake significantly during the ten-day window, our research finds that this is not typical. In fact, the relationship between days to report and ownership stake is statistically significantly *negative*, with *shorter* days to report (often *zero* days or *one* day, *i.e.*, reporting on the same day the 5% threshold is crossed, or the day after) associated with *higher* initial disclosed ownership. At the same time, we do find that an increasing number of days to report is associated with higher abnormal volume that is not due to the hedge fund's own share accumulation. Whether, arguably consistent with Wachtell’s premise, this reflects indirect share accumulation by the activist’s allies, or whether, inconsistent with Wachtell’s premise, this reflects the spread of information even absent required disclosure, is a topic we are investigating in current research.

Second, Wachtell’s claim that the current reporting regime facilitates “market manipulation” is based on a false concept of market manipulation. Manipulators mislead investors into believing “that prices at which they purchase and sell securities are determined by the natural interplay of supply and demand” when in fact they are “rigged by manipulators.” *ATSI Communications, Inc. v. The Shaar Fund, Ltd.*, 493 F.3d 87, 100 (2d Cir. 2007). But there is no sense in which a hedge fund activist’s purchases are outside the “natural interplay of supply and demand.” Hedge fund activists make actual purchases from third parties at the market price in open markets. Therefore, those purchases are not manipulative.

Third, while Wachtell appeals to legislative history to support its position, that appeal is misdirected. Congress added Section 13(d) to the Exchange Act as part of the Williams Act of 1968 “to solve the dilemma of shareholders desiring to respond to a cash tender offer.”³ Prior to the pervasive use of cash tender offers in the 1960s, “corporate takeover attempts had typically involved either proxy solicitations ... or exchange offers of securities” both of which were subject to federal disclosure requirements.⁴ But cash tender offers were not. In part, the Williams Act subjected cash tender offers to disclosure requirements by using the acquisition of beneficial ownership of equity securities as the trigger for disclosure.⁵ Congress directed Section 13(d) to improving disclosure before cash tender offers that had become pervasive by late 1960s, and most case law arising under Section 13(d) concerns tender offers and mergers and acquisitions.

While it is undeniable that Section 13(d) on its face applies to share accumulations by hedge fund activists, it is not true that the legislative history of Section 13(d) anticipated the unique concerns that hedge fund activism raises, especially since hedge fund activists rarely seek control of their targets. Only in 4.6% of events in our sample did the hedge funds intend to take over the target company. The median ownership stake at the highest point of each activism event is 9.5%; and the 95th percentile is 26.7%. Hedge fund activism is quite a different phenomenon from the cash tender offers that were Congress’s concern in the 1960s. Under the guise of legislative history, Wachtell in fact advocates a broad expansion of Section 13(d)’s historical motivation.

Fourth, Wachtell’s call for an “issuer” remedy for violations of Section 13(d) threatens to tip too far in management’s favor the balance between the interests of hedge fund activists and management. As the Supreme Court has stated, “There is no question that in imposing these [Section 13(d)] requirements, Congress intended to protect investors. But it is also crystal clear that a major aspect of the effort to

³ *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 60 (1975).

⁴ *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. 1, 22 (1977). As Professor Colombo states in an excellent recent article on Section 13(d): “[A]s of 1968, not all efforts at seizing corporate control were covered by the securities acts’ disclosure requirements. Importantly, a simple cash tender offer was not subject to reporting obligations under either the Securities Act of 1933 or the Securities Exchange Act of 1934. Similarly, disclosure was not required of those who would simply purchase large quantities of a company’s stock via privately negotiated cash transactions or open-market cash sales of stock. Compounding the problem, these undertakings could be, and often were, pursued quite effectively together.” Ronald J. Colombo, *Effectuating Disclosure Under the Williams Act*, 60 CATH. U. L. REV. 311, 315 (2011).

⁵ *Id.*

protect the investor was to avoid favoring either management or the takeover bidder.” *Edgar v. MITE Corp.*, 457 U.S. 624, 633 (1982) (citations omitted). Already, targets resist hedge fund activism with corporate funds, while hedge fund activists must use their own funds. Wachtell’s suggestion of an issuer remedy is inconsistent with Supreme Court precedent and would too significantly tip the balance in favor of management.

Finally, Wachtell fails to address the benefits of hedge fund activism. Prior research demonstrates that hedge fund activism is, on average, associated with higher stock returns and operational improvements. *See, e.g.*, A. Brav, W. Jiang, F. Partnoy, and R. Thomas, *Hedge fund activism, corporate governance, and firm performance*, 63 J. FIN., 1729 (2008). Wachtell asserts that “[t]here is no valid policy-based or pragmatic reason that purchasers of significant ownership stakes in public companies should be permitted to hide their actions from other shareholders, the investment community and the issuer,”⁶ but the benefits of hedge fund activism suggest otherwise. If the ten-day period is necessary, in some cases at least, for hedge fund activists to acquire a significant enough share to warrant their expensive efforts, and if those cases also are associated with positive stock returns and operational improvements, then Wachtell’s proposed rulemaking may harm shareholders and companies alike. Especially where the legislative history of Section 13(d) plainly demonstrates concern with a different type of phenomenon than that reflected in shareholder activism, it is important for the Commission to balance the costs of nondisclosure with the benefits of hedge fund activism.

Not surprisingly, hedge fund activism is unpopular in many quarters, particularly among firms that become or may become its targets. Activism is often acrimonious and sometimes leads to litigation.⁷ Corporate targets have an interest in shaping the debate over hedge fund activism. However, we caution the Commission to consider carefully the empirical evidence on hedge fund activism before limiting the ability of hedge fund activist to deliver benefits to investors and companies alike.

⁶ *Id.* at 2.

⁷ *See, e.g.*, *CSX Corp. v. Children's Inv. Fund Mgmt. (UK) LLP*, 562 F. Supp. 2d 511, 519 (S.D.N.Y. 2008) *aff'd*, 292 F. App'x. 133 (2d Cir. 2008). In *CSX Corp.*, an activist firm – The Children’s Investment Fund – was found liable for violating Section 13(d) in connection with its activist targeting of CSX Corp. *See* J.B. Heaton, *CSX Corporation v. The Children's Investment Fund: Total Return Swaps as Evasions of Section 13(d) Reporting*, *Sec. Lit. J.*, Summer 2009, 16-18, available at <http://www.bartlit-beck.com/assets/attachments/csx.pdf>

