HEALTHY MARKETS
TRANSPARENCY & TRUST

August 28, 2020

Via Electronic Mail

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

Re: Reporting Threshold for Institutional Investment Managers[1]

Dear Ms. Countryman:

The Healthy Markets Association[2] objects to the above-referenced proposal to reform the holdings reporting threshold for institutional investors.

The 13F Proposal is contrary to the law and public policy. Further, the Commission has failed to demonstrate that it has conducted the necessary analysis, or has otherwise engaged in an appropriate rulemaking process that is consistent with its statutory obligations.[3]

Because the 13F Proposal is fatally flawed, it should be rescinded.

Background

In July 1968, Congress directed the Commission to study the impact of institutional traders on the markets. In April 1971, the Commission sent its Institutional Investor Study Report to Congress.[4] That Report found "gaps in information about the purchase, sale and holdings of securities by major classes of institutional investors."[5] The Commission's report to Congress recommended that Congress revise the securities

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[1] *Reporting Threshold for Institutional Investment Managers*, SEC, Exch. Act Rel. No. 34-89290 (July 10, 2020), *available at* https://www.sec.gov/rules/proposed/2020/34-89290.pdf ("13F Proposal").

[2] The Healthy Markets Association is an investor-focused not-for-profit coalition working to educate market participants and promote data-driven reforms to market structure challenges. Our members, who range from a few billion to hundreds of billions of dollars in assets under management, have come together behind one basic principle: Informed investors and policymakers are essential for healthy capital markets. To learn more about Healthy Markets or our members, please see our website at http://healthymarkets.org.

[3] See, e.g., Administrative Procedure Act, 5 U.S.C. §551 et seq.

[4] INSTITUTIONAL INVESTOR STUDY REPORT OF THE SECURITIES AND EXCHANGE COMMISSION , House Doc. 92-64, 92nd Cong. (1971), *available at* http://3197d6d14b5f19f2f440-5e13d29c4c016cf96cbbfd197c579b45.r81.cf1.rackcdn.com/collection/papers/1970/1971_0310_SECInstitutionalInvestor_25.pdf ("1971 SEC Report").

[5] 1971 SEC Report, at X-XI.

laws to require continuous reports of holdings and transactions from "all types of institutional investors."[6] Those sentiments were generally echoed by the President's Commission on Financial Structure and Regulation and by the Senate Subcommittee on Securities in 1973.[7]

As part of the Securities Act Amendments of 1975, Congress adopted section 13(f) of the Exchange Act to provide for the "rapid dissemination of the institutional disclosure information to the public."[8] Section 13(f) expressly requires institutions that exercise discretion over $100 million or more of covered securities ("13(f) Securities") to provide detailed holdings information to investors and the public.[9]

Pursuant to that law, since 1978, the Commission has required institutional owners to file reports within 45 days of the end of the year in which a firm first hits the threshold, and within 45 days following the end of each subsequent quarter.[10] In the more than four decades since the rule was first implemented, the Commission has never adjusted the dollar threshold nor the time horizon for filing reports.

In 1999, the Commission mandated that the filings be made via the SEC's EDGAR system.[11] The data is submitted in a machine-readable (XML) format.[12]

In practice, each quarter, the American Bankers Association creates a list of qualifying securities, and the Commission then publishes that list as the definitive list of 13(f) Securities.[13] That list is not exhaustive. It "generally include[s] equity securities that are traded on an exchange or quoted on National Association of Securities Dealers Automated Quotations (NASDAQ), equity options and warrants, shares of closed-end

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[6] 1971 SEC Report, at XI; *see also, Filing and Reporting Requirements Relating to Institutional Investment Managers*, Sec. and Exch. Comm'n, 43 Fed. Reg. 26700, 26701 (June 22, 1978), *available at* https://tile.loc.gov/storage-services/service/ll/fedreg/fr043/fr043121/fr043121.pdf (Rule 13f-1 Release).

[7] Rule 13f-1 Release, at 26701 (citing to Report of the Senate Subcommittee on Securities, Committee on Banking, Housing. and Urban Affairs, 93rd Cong. (1973)).

[8] Report to Accompany S.249, Securities Act Amendments of 1975, Sen. Rep. No. 94-75, at 87, 94th Cong. 1975 ("Senate Report").

[9] 15 U.S.C. § 78m(f).

[10] Rule 13f-1 Release, at 26701.

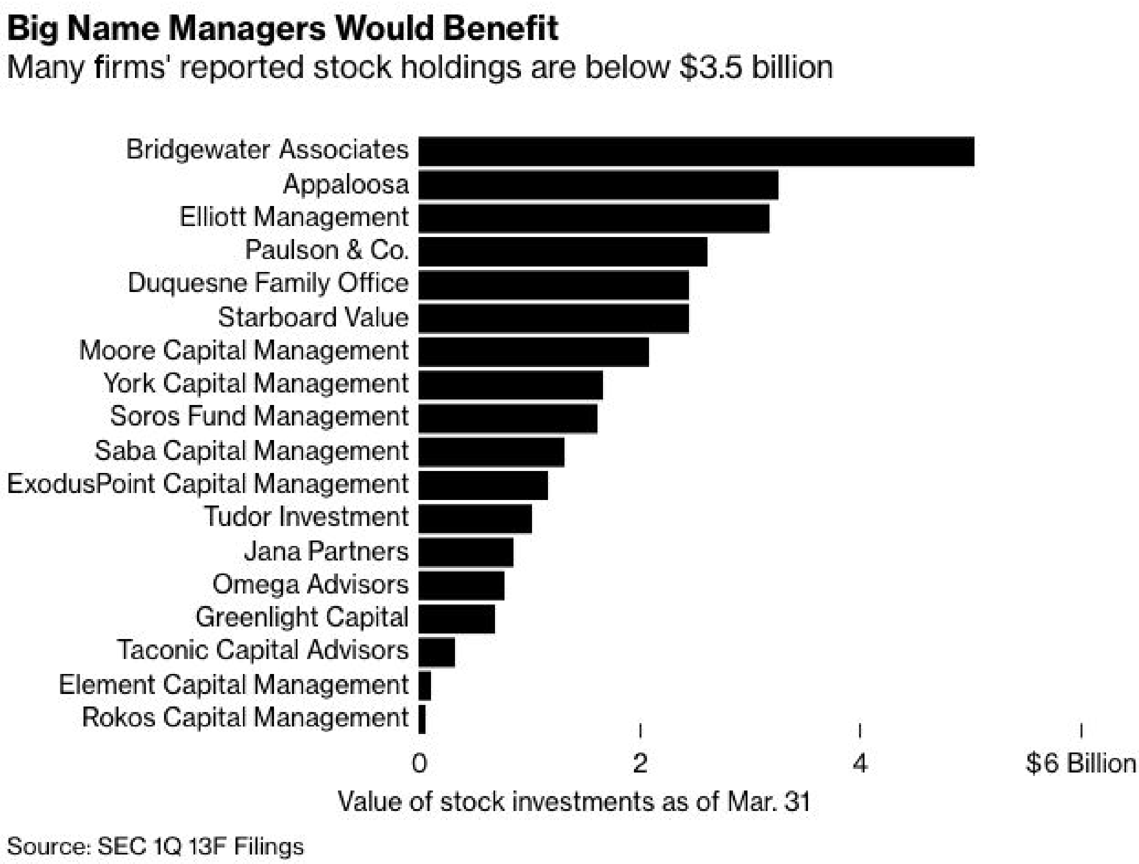
[11] *Rulemaking for EDGAR System*, Sec. and Exch. Comm'n, Exch. Act Rel. No. 34–40934, 64 Fed. Reg. 2843, 2845, (Jan 19, 1999), *available at* https://www.govinfo.gov/content/pkg/FR-1999-01-19/pdf/99-1043.pdf ("EDGAR Reform Adoption").

[12] See generally, EDGAR Form 13F XML Technical Specification (Version 1.3), Sec. and Exch. Comm'n, *available at* https://www.sec.gov/info/edgar/specifications/form13fxmltechspec.htm.

[13] *See, e.g.*, *List of Section 13F Securities, Second Quarter FY 2020*, Sec. and Exch. Comm'n, available at https://www.sec.gov/divisions/investment/13f/13flist2020q2.pdf (reflecting a copyright by the American Bankers Association). Notably, the Commission's Inspector General took issue with the preparation of the list by a third party and with a lack of Commission staff oversight of the process in 2010. See, i.e., SEC IG Report, at vi ("In addition, our review disclosed that a third party prepares the official list of Section 13(f) securities that the Commission is required to provide to the public, and has been doing so since 1981, based upon specifications received from the SEC in 1979. The official list prepared by the third party is posted to the Commission's website each quarter; however, no SEC division or office conducts any review of the list for accuracy and completeness before it is posted.").

investment companies, and some convertible debt securities."[14] It does not include, for example, selling put options, or other derivative equity positions.

As a result, several very large investment firms have only fractions of their total assets counting toward the threshold today.[15] The following chart was prepared by Bloomberg.



Form 13F reports are often filed by "investment advisers, banks, insurance companies, broker-dealers, pension funds and corporations."[16] To assist filers, the Commission maintains a Frequently Asked Questions page on its website containing answers to more than sixty questions.[17] Perhaps because of the relative ease of avoiding the

[14] SEC IG Report, at v.

[15] See, e.g., Miles Weiss, Benjamin Bain, and Hema Parmar, *Tepper, Einhorn, Soros Stock Holdings Would Go Dark in SEC Plan*, Bloomberg, July 14, 2020, *available at* https://www.bloomberg.com/news/articles/2020-07-14/tepper-einhorn-soros-stock-holdings-would-go-dark-in-sec-plan (noting that "Bridgewater Associates, the world's biggest hedge fund manager with $138 billion of assets, is in striking distance of the SEC's suggested limit because the firm holds just $5 billion of stocks.").

[16] Review of the SEC's Section 13f Reporting Requirement, Inspector General of the Sec. and Exch. Comm'n, Rep. 480, at iv, Sept. 27, 2010, *available at* https://www.sec.gov/files/480.pdf ("SEC IG Report").

[17] *Frequently Asked Questions About Form 13F*, Sec. and Exch. Comm'n, *available at* https://www.sec.gov/divisions/investment/13ffaq.htm (updated Feb. 24, 2020).

thresholds or the ease in making the reports, there has been essentially no significant effort to materially ease the filing burdens on institutional investors.

However, for years, corporate issuers and their advocates have expressed concerns to the Commission and Congress that activist funds were able to escape the reporting requirements by acquiring financial exposures that weren't on the list of 13(f) Securities, but were nevertheless equivalent to equity interests.

As discussed below, some fund investors have been able to acquire significant interests in companies without having to file Forms 13F and alerting the company, other market participants, or regulators. Further, the rules don't expressly prohibit "wolf pack" behavior, where different investors may work together to establish significant holdings in a company, again, without alerting the company, other market participants, or regulators. Congress and the SEC have, in the past, explored efforts to revise the requirements to address these perceived loopholes.

At the same time, market participants and their advocates have asked the Commission to shorten the reporting period significantly from the existing 45 days. For example, in 2013, NYSE Euronext, the Society of Corporate Secretaries and Governance Professionals and the National Investor Relations Institute jointly filed a rulemaking petition to the Commission asking for the agency to cut the 45 day reporting period down to two days.[18]

13F Proposal

The 13F Proposal would, by rule, purport to raise the statutory threshold of $100 million to $3.5 billion, thus exempting approximately 90% of the current form 13F filers from having to make the submissions. The 13F Proposal does not address the timing of the reports nor what counts towards the threshold.

The 13F Proposal Is Inconsistent with the Federal Securities Laws and the Provision's Legislative History

The 13F Proposal ignores the law, the legislative history, and the clear purpose for the law itself.

The statute itself declares that "every" manager holding 13(f) Securities whose "aggregate fair market value on the last trading day in any of the preceding twelve months [was] at least $100,000,000 ***or such lesser amount*** (but in no case less than $10,000,000) as the Commission, by rule, may determine, shall file reports."[19]

The statute itself does not contemplate the Commission raising the reporting threshold

[18] Letter from Janet McGinness, NYSE Euronext, et. al. to Elizabeth M. Murphy, Sec. and Exch. Comm'n, Feb. 1, 2013, available at https://www.sec.gov/rules/petitions/2013/petn4-659.pdf.

[19] 15 U.S.C. § 78m(f) (emphasis added).

beyond $100 million. However, the statute expressly contemplates lowering the reporting threshold, but then limits the Commission's authority to set the threshold below $10 million. Put simply, the statute establishes a range within which the threshold is to be set: $10-$100 million.

The legislative record similarly contemplates lowering the threshold, but not raising it beyond $100 million.[20] The Senate Report repeatedly references the $100 million threshold as the "initial" level, and suggests that the Commission would subsequently lower that threshold.[21] The express purpose of starting at $100 million was to capture the largest institutional investors first, which Congress opined could be done relatively quickly and efficiently, and then expand the requirement to smaller managers thereafter.[22]

The 13F Proposal ignores the statutory language, the legislative history of the provision, and the reason Congress established the institutional holdings reporting requirement. The Commission can't do that.

The Commission Fails to Collect and Analyze Relevant Data, Including the Impacts on Market Participants, the Public, and the Commission Itself

The limited analysis provided in the 13F Proposal is an embarrassment to the Commission, and insufficient to withstand legal challenge.

When invalidating another recent Commission action, the DC Circuit explained that

> To satisfy the "arbitrary and capricious" standard, "the agency must examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made.'[23]

The Commission has not done that.

The 13F Proposal doesn't examine the purpose of the statute, who uses the filings, why, and to what benefits. It doesn't examine the consequences of the 13F Proposal on

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[20] Report to Accompany S.249, Securities Act Amendments of 1975, Sen. Rep. No. 94-75, at 87, 94th Cong. 1975 ("Senate Report"). But see Senate Report, at 107. We recognize that one sentence in the record suggests that the Commission could raise the threshold, we believe that this authority was intended to adjust the threshold over time within the dollar range created by the statutory language itself ($10-$100 million).

[21] Senate Report, at 86 (noting that the Commission could lower the threshold down to as low as $10 million).

[22] Senate Report, at 86 (noting that by ""limiting initially the impact of the reporting provisions to the largest institutional investment managers, the institutional disclosure program could be implemented rapidly with the least amount of unnecessary costs and burdens.").

[23] *Susquehanna Int'l Group LLP, et al, v. SEC*, 866 F.3d 442, 445 (D.C. Cir. 2017) (internal citations omitted).

the markets, market participants, or itself. Instead, the 13F Proposal essentially relies on four disparate assertions:

- Congress explicitly focused on larger asset managers in 1975, out of sensitivity to the "burdens" of making the filings on smaller firms;
- Since 1975, the market capitalization of the public markets has grown approximately 35 times;[24]
- Since 1975, the number of firms subject to the filing requirement has grown approximately 17 times; and[25]
- Seventeen years ago someone sent the Commission a letter and ten years ago the SEC's Inspector General wrote a report suggesting that the threshold be raised to reflect inflation since 1975.[26]

The Commission's assertions are materially misleading. As described above, Congress "initially" set the filing threshold at $100 million with a clear expectation that the Commission would later lower the threshold. It was never meant to apply to only the very largest firms. Similarly, the clear interest by market participants has been to enhance the reporting requirements, not reduce them.

But perhaps most importantly, the 13F Proposal seems to ignore the reasons Congress established the filing requirement in the first instance. Congress established Section 13(f) for both public and regulatory purposes. According to the Senate Report:

[24] 13F Proposal, at 11.
[25] 13F Proposal, at 11.
[26] 13F Proposal, at 12-13.

B. USES FOR THE INFORMATION

1. Public Use

> Perhaps the most important justification for the information collection program which this bill would authorize is the need to collect and disseminate to individual investors data about institutional investment managers. Many people believe that it is not possible to make informed investment decisions on a security without information related to the likely market activity and the degree of institutional concentration in the security. Institutional concentration may suggest a number of things to a variety of investors. For example, to some it may be a good sign because it may suggest that sophisticated investors believe the security is a good investment. To others, it may be a danger sign indicating a potential depressing "overhang," market illiquidity, or high price volatility. That different investors may draw different conclusions from the data is not important; rather, what is important is that information about the securities holdings and certain transactions of institutional investment managers be available to all investors—both institutional and individual—so that they can all have it, whatever its relative usefulness in making their independent judgments. Thus, with the dissemination of data about institutional investment managers, an institutional disclosure program should stimulate a higher degree of confidence among all investors in the integrity of our securities markets. [27]

As anticipated, the filings are used today by academics and market participants. As the Commission has its explicitly acknowledged

> investors would find the information contained in Form 13F filings useful in tracking institutional investor holdings in their investments and that issuers, too, would find detail as to institutional investor holdings useful because much of their shareholder list may reflect holdings in ''street name'' rather than beneficial ownership.[28]

Today, the filings are used by companies. For example, in its joint rulemaking petition to the Commission in 2013, NYSE Euronext explicitly noted that issuers use the disclosures to engage with their owners, and that more timely disclosures would help issuers better communicate with their large shareholders, particularly for proxy considerations. The 13F Proposal ignores that information.

The filings are used by academics. For example, the filings have been used by academics to study the value and impacts of activist hedge fund strategies.[29] The 13F Proposal also essentially ignores that information.

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[27] Senate Report, at 82.
[28] EDGAR Reform Adoption, at 2845.
[29] See, e.g., Lucian Bebchuck, Alon Brav, Wei Jiang, *Long-Term Effects of Hedge Fund Activism*, NBER Working Paper No. 21227, 2015, *available at* https://www.nber.org/papers/w21227.

The Senate Report expects regulators to use the collected data.

> *2. Use by Regulatory Agencies*
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> Moreover, the SEC, bank regulatory agencies, and other agencies (both federal and state) could be expected to make extensive use of the institutional disclosure data in fulfilling their responsibilities to consider and develop standards designed to protect the public interest within a consistent and coordinated regulatory framework. It would be expected that the SEC might use the institutional disclosure data in two generally different ways: to analyze the characteristics of institutional investment managers, and to analyze the impact of institutional investment managers on the securities markets.[30]

The Commission does not even acknowledge, much less contemplate how those actual and potential uses of information would be impacted by the 13F Proposal. It must.

While the Commission has failed to offer any meaningful justification or analysis of the impact of the 13F Proposal, market research and data firm IHS Markit has prepared a detailed analysis of the impact of the 13F Proposal.[31] That analysis is devastating.

- **The Proposal would exempt approximately 90% of current filers.** According to the IHS Markit Analysis, the new requirement would exempt about 90% of current filers. In drafting Section 13f, Congress explicitly stated that the purpose of the requirement was to "facilitate consideration of the influence and impact of institutional investment managers on the securities markets and the public policy implications of that influence." How is that purpose furthered by exempting so many investors?

  The Commission does not address these basic inconsistencies between the clear intent and language of the statute and the 13F Proposal. It must

- **Holders of a huge swath of companies would disappear.** Specifically, on average, 55% of an issuer's shareholders would stop filing Form 13Fs. As a result, issuers, market participants, and regulators would have a much narrower view of the holders of any particular issuer. Again, how can the "influence" of institutional investors be studied when the majority of a company's shareholders (and over two-thirds of its hedge fund shareholders) would be exempted?

  The Commission again does not address these basic inconsistencies between the clear intent and language of the statute and the 13F Proposal. It must.

- **The Proposal would disproportionately hurt transparency into smaller companies.** The percentage of holdings that would be excluded would be relatively small for mega cap (4.4%) and large cap (5.5%) companies, but would be significantly larger for small cap (14.6%) and micro cap (17.1%) companies.

[30] Senate Report, at 83.

[31] *SEC's 13F Proposal – Issuer and Investor Analysis*, IHS Markit-Ipreo, Aug. 7, 2020, *available at* https://ipreo.com/blog/secs-13f-proposal-issuer-and-investor-analysis/.

We find this shocking loss of transparency into smaller companies deeply concerning for both the issuers and investors in these companies. It is also impossible to reconcile with the rhetorical support often proffered by the political leaders at the Commission for "small and emerging companies."

The Commission offers no analysis related to this disparate impact on issuers of different sizes. It must.

- **The Proposal would have disparate impacts across different industries.** According to the IHS Markit analysis, the Energy (16.5%), Healthcare (14.9%), and Technology (12.8%) sectors would be severely impacted, as there would be a significant loss into transparency of those companies. However, there would not be a significant loss to the transparency of holdings in Utilities (6.0%).

  The Commission offers no analysis related to this disparate impact on issuers of different sizes. It must.

- **The Proposal would generally not impact index funds, but would dramatically reduce filings by active funds.** According to the IHS Markit analysis, "[s]pecialty investors (20.4%) and alternative investors (32.9%) are the clear outliers as they would dramatically file for less dollars."

  The Commission offers no analysis related to this disparate impact on investors using different strategies. It must.

- **The Proposal punishes long term investors, but rewards high-turnover investors.** According to the IHS Markit analysis, "[v]ery high turnover firms would not have to file for 11 times more of their share value than low turnover investors." In fact, 86% of "activist" investors would no longer have to file Form 13Fs.

  Again, the Commission offers no analysis related to this disparate impact on investors using different dime horizons. It must. And even further, this disparate impact seems directly contrary to the Commission's previously stated interest in promoting long-term investment and capital formation.

While the 13F Proposal explicitly acknowledges that it would "take dark" holdings of more than 4,500 institutional investors managing more than $2.3 trillion in assets, it offers no reasoned analysis as to why they are taking this action and the practical impacts on issuers, investors, other market participants, and regulators. As the IHS Markit analysis confirms, this impact on transparency will be profound.

As previously stated, the 13F Proposal is contrary to the statute, unsupported by substantial evidence, and a clear abuse of the Commission's discretion.[32]

[32] See, *Susquehanna Int'l Group LLP, et al, v. SEC*, 866 F.3d 442, 445 (D.C. Cir. 2017).

The Commission Fails to Examine the Definition of 13(f) Securities

The Commission has effectively outsourced its job of defining "equity securities" under the statute to a third party. And that list does not capture all financial products that can give rise to an economic equivalent of an equity interest or position. The proliferation of complex financial products and strategies has resulted in significant gaps in the existing reporting framework.

The 13F Proposal fails to examine how the definition of 13(f) Securities has impacted filers and users of the disclosures over the decades. For example, has the proliferation of new and complex financial products allowed some types of investors to avoid making these filing requirements?

These are not theoretical concerns. For example, in September 2019, activist investor Elliott Management Corporation publicly released a letter to the Board of Directors AT&T in which the company claimed that it "owns $3.2 billion of the common stock and economic equivalents of AT&T Inc."[33] At the same time, the firm's 13F filings did not appear to reflect nearly that amount. One possibility for the discrepancy could be the use of synthetic long positions that may not have to be disclosed. The strategy of activist funds seeking to avoid public and regulatory holdings disclosures is not unique to the United States. In fact, just a few months ago, Elliott Management was fined €20 million by the French financial regulator, Autorité des Marchés Financiers, for failing to timely file accurate holdings reports related to the firm's holdings in Norbert Dentressangle, a French logistics firm that was the subject of a takeover dispute.[34]

In summary, the definition of 13(f) Securities clearly warrants Commission review and consideration for potential revisions.[35] The Commission has been asked to undertake that review. Yet, the 13F Proposal roundly ignores that information.

The Commission Fails to Examine the Timeliness of Reports

The 13F Proposal ignores recent requests by market participants to improve the timeliness of reporting. Under the existing filing framework, an investor could take a significant position on the first trading day of the year and not have to disclose it until mid-May.

[33] Letter from Jesse Cohn and Mark Steinberg, Elliott Management Corp., to Board of Directors of AT&T, Inc., Sept. 9, 2019, *available at* https://www.busin€esswire.com/news/home/20190909005482/en/Elliott-Management-Sends-Letter-Board-Directors-ATT.

[34] David Keohane, *French markets regulator fines hedge fund Elliott €20m*, Financial Times, Apr. 22, 2020, *available at* https://www.ft.com/content/976d1e30-e0cf-473f-a743-a6def0c3f21d.

[35] We also question whether the American Bankers Association is the apparent preparation agent for the list, and whether alternatives may better support the intended purpose of the requirement. Similarly, we question whether there may be better alternatives to relying on licensed intellectual property.

Today, investors are able to know and assess the associated risks of their holdings in time increments measured in seconds, minutes, and hours. We find it exceedingly difficult to argue that 45 days following the end of a quarter is a "rapid" disclosure of holdings in today's world.

One cannot credibly suggest five decades of computerized innovation haven't made the gathering of the data, preparation of the filings, and process for submitting the filings significantly easier for reporting firms.

The Commission has been asked to update the rules to match the intent of the law. It hasn't. Instead, the 13F Proposal ignores that information.

Concerns with Propriety and Origins of the 13F Proposal

Finally, the extraordinarily disparate impacts on investors using different strategies, combined with its lack of statutory, evidentiary, or public support, raise significant questions regarding the origins and intent of the 13F Proposal. Put bluntly, the 13F proposal looks and smells like a political favor that is intended to benefit one or more of a small handful of specific activist shareholders or special interests. We urge the Commission to refer the matter to the Inspector General for further inquiry to ensure the propriety of the Commission's regulatory agenda and processes.

Conclusion

We encourage the Commission to study the disclosure of fund holdings, and offer suggested improvements, but those improvements should be focused on promoting transparency and accountability, not obfuscation.

The 13F Proposal is contrary to the law, unsupported by the evidence, and unsupported by reasoned analysis. Accordingly, it should be rescinded.

Thank you for your consideration. Should you have any questions or would like to discuss our letter or exhibit further, please contact me at (202) 909-6138.

Sincerely,

Ty Gellasch

Tyler Gellasch
Executive Director