

**Recent SEC Staff Interpretations Regarding
Schedule 13G And 13D Reporting Requirements**

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On September 14, 2009, the staff of the SEC's Division of Corporation Finance released compliance and disclosure interpretations (the "C&DIs") regarding Schedule 13G and 13D reporting under Exchange Act Sections 13(d) and 13(g) and Regulation 13D-G. They provide some new interpretations, revise existing ones and replace interpretations in the July 1997 Manual of Publicly Available Telephone Interpretations. This article highlights those C&DIs that are likely to be of the most interest to mutual funds.

1. Counting the 10-Day Filing Deadline. The C&DIs clarify that the requirement to file a Schedule 13D within 10 days after the transaction that causes beneficial ownership to exceed 5% is counted from the trade date rather than the settlement date, with the trade date counting as day one. The SEC has taken enforcement action against late Section 13 filers, so knowing which day to count from could be critical.

2. Re-establishing Schedule 13G Eligibility after Switching to Schedule 13D. If an initial report is filed on Schedule 13D, there can be no switch to Schedule 13G. Advisers to mutual funds typically file Schedule 13G as qualified institutional investors. If an adviser was originally eligible to file a Schedule 13G but switched to Schedule 13D because it held reportable securities with the purpose or effect of changing or influencing management, it may

switch back to Schedule 13G when it once again qualifies, if the securities are no longer held with control intent. The SEC makes clear that the key to the ability to switch back to Schedule 13G is the term "again." Therefore, if an adviser holds securities with control intent when it first crosses the 5% threshold and as a result initially files a Schedule 13D, it must remain a Schedule 13D filer until it files a final amendment to report beneficial ownership of 5% or below. Only afterwards, if the adviser's beneficial ownership of the securities again increases to above 5%, may the adviser qualify to file a Schedule 13G.

3. Involuntary Change in Circumstances. The C&DIs clarify a security holder's obligation to file a Schedule 13D or 13G when its beneficial ownership of Section 12 securities changes because of circumstances outside its control.

(a) Change in the Aggregate Number of Outstanding Securities. A Schedule 13D filer is required to amend to reflect any material change in the percentage of the class that that it beneficially owns as a result of a change in the aggregate number of outstanding securities in the class. This amendment requirement applies even if the filer did not cause the changes in reported ownership. Therefore, a Schedule 13D filer should monitor the number of outstanding shares of a class of Section 12 securities of which it beneficially owns more than 5% to determine whether any changes in the

outstanding may require it to amend. Schedule 13G filers do not have to file an amendment under the same circumstances.

(b) Investor that Beneficially Owns More than 5% of an Equity Security when It becomes Registered under Section 12. If an investor owns over 5% of a class of equity securities on the date that the class is registered under Section 12 (for example, as a result of an IPO) and the investor has not acquired any more securities since that date, it may report on Schedule 13G within 45 days after the end of the calendar year in which the class was registered. The investor is not required to certify that the shares were acquired or are held in the ordinary course or without the purpose or the effect of changing or influencing control of the issuer. A qualified institutional investor beneficially owning more than 10% of a class is not required to file a Schedule 13G within 10 days after the end of a month in this circumstance, unless it acquires more shares after the registration becomes effective. If the investor acquires more equity securities, it must report its entire holdings on Schedule 13D or evaluate whether it may continue to file Schedule 13G, if the most recent acquisition, and all other acquisitions of the same class during the immediately preceding 12 months (or the period since the issuer was privately held, if shorter) aggregate to more than 2% of the class.

(c) Investor in a Parent Company Receives More than 5% of a Class of Reportable Securities of the Parent's Subsidiary in a Spin-Off. If a security holder of a parent company receives more than 5% of a class of Section 12 securities of the parent's subsidiary in a spin-off that was not conditioned on the approval of the

parent's security holders, it may file a Schedule 13G within 45 days after the end of the calendar year in which the spin-off occurred, since the receipt of securities in a spin-off is not an acquisition. This exception from Schedule 13D filing obligations is not available to persons who influence or control the parent's decision to spin off the subsidiary.

4. Late Amendments. If a Schedule 13D filer has failed to timely file any required amendment, it should immediately amend its Schedule 13D to disclose the required information. If the filer failed to file multiple amendments, it may disclose that information by multiple filings or one combined filing. Regardless of the approach taken, the filer must include all of the information that it should have disclosed in each required amendment, including the dates and details of each event that required an amendment. The SEC staff reminds filers that any of these steps will not necessarily affect a filer's liability under the federal securities laws for failing to promptly file a required amendment to Schedule 13D. Although the C&DIs only addressed Schedule 13D amendments, we recommend that this analysis also be applied to Schedules 13G.

5. Determining Beneficial Ownership. The CD&Is clarified the following issues related to calculating beneficial ownership for Schedule 13D or 13G reporting purposes.

(a) Short Sales, Pledges and Writing Call Options. These transactions normally do not change beneficial ownership because they do not change the amount of shares over which the beneficial owner has voting or investment power.

However, any of these transactions may trigger a Schedule 13D amendment if it materially changes the disclosure in the Schedule 13D. For example, it may represent a change in the source of funds (Item 3), a possible shift in purpose (Item 4) (particularly if a plan or proposal to dispose of the issuer's securities was not disclosed previously), a transaction in the subject security (Item 5), a contract, agreement, understanding or relationship with respect to securities of the issuer (Item 6) or require that an exhibit be filed (Item 7).

(b) Delegation of Voting and Investment Authority to an Investment Adviser. An investor that owns more than 5% of a class of Section 12 securities and has delegated all authority to vote and dispose of the securities to an investment adviser still must continue to report beneficial ownership of the securities if it retains the right under the investment advisory contract to rescind the investment adviser's authority and regain investment or voting power over the shares within 60 days.

(c) ADRs. ADRs are not considered a separate class of equity security for purposes of calculating beneficial ownership. Therefore, a person who beneficially owns ADRs registered under Section 12 must file Schedule 13D or 13G if the equity securities represented by the ADRs plus any underlying securities that the person beneficially owns outside the ADR constitute more than 5% of the underlying class.

6. Determining Number of Shares Outstanding. Shares held by or for the account of the issuer or its subsidiary are excluded from outstanding shares. Therefore, shares that an issuer repurchased

to fund a stock option plan are not included in the number of shares of the class outstanding, even if the issuer did not retire the shares or account for them as treasury stock.

7. Convertible Securities. The CD&Is addressed the following issues related to convertible securities:

(a) Variable-Rate Convertible Notes. If a Schedule 13D filer owns variable-rate convertible notes convertible within the next 60 days into a number of common shares that varies daily with the price of the underlying common, the filer must promptly amend whenever a change in the conversion rate would result in a 1% or more change in ownership of the underlying shares. The C&DIs only addressed Schedule 13D amendment requirements, but we believe that the same analysis would apply if a conversion rate change caused a Schedule 13G filer's beneficial ownership to cross a Schedule 13G amendment threshold.

(b) Conversion Conditioned on the Effectiveness of a Registration Statement. An investor that receives a right to acquire more than 5% of a class of Section 12 securities (i) without the purpose or effect of changing or influencing control of the issuer, (ii) that is exercisable within 60 days and (iii) conditioned on the effectiveness of a related registration statement is not required to file a Schedule 13D or Schedule 13G until the condition is removed. The right becomes exercisable within 60 days from that date. Convertible securities often have provisions permitting the holder to exercise on 61 days' notice so that it is not deemed to beneficially own the underlying securities until after it has given that notice. Convertible securities often are

issued in circumstances in which investors seek an effective registration statement for the underlying shares. In those cases, this interpretation provides an alternative on which a holder of convertible securities may rely to not be deemed to beneficially own the underlying shares if there is no 61-day notice requirement for conversion.

(c) Terms of Convertible Security Prohibit Conversion if it would Cause Investor to Beneficially Own over 5%. Although an investor generally is deemed to beneficially own any securities that it has the right to acquire within 60 days, binding and valid conversion provisions limiting a holder's beneficial ownership of a class of underlying securities effectively eliminate the holder's right to acquire those shares and relieve it of a filing obligation. It appears to be increasingly common for issuers to use these provisions to limit the conversion rights of convertible securities to an amount of underlying shares that causes the holder's beneficial ownership to not exceed 4.9% of the class.

8. Schedule 13D Disclosure.

The C&DIs clarified the following issues related to Schedule 13D disclosures.

(a) Disclosure Should Be as of the Filing Date. The disclosure in an initial or amended Schedule 13D should be current through the filing date rather than the event date, including ownership totals on each cover page. Similarly, transactions disclosed in Item 5(c) should be those effected within the 60 days before the filing date rather than the event date.

(b) Reporting Multiple Transactions on the Same Day. Broker-

dealers may execute trade orders in small increments at prices that may be as little as a fraction of a penny apart and provide their clients with average, instead of per share, prices. Therefore, a Schedule 13D filer who, through an order executed by a broker-dealer, effects multiple open market trades on the same day at different prices may report in item 5(c) all trades within a one dollar price range at the weighted average price. The filer must then specify, in a footnote or otherwise, the range of prices for each of those trades and undertake to provide on the SEC staff's request, information about the number of shares purchased or sold at each separate price.

(c) Change in Plans or Proposals Regarding Issuer's Securities. Generic disclosure reserving the right to engage in any of the transactions listed in Items 4(a)-(j) of Schedule 13D must be amended when the filer formulates a specific intent regarding a matter that must be disclosed (for example, engaging an investment banker to take the issuer private) even if the filer has not approached management about the plan or taken other steps to implement it.

(d) Proxy Rules and Commentary in Items 4 or 6. A Schedule 13D filer may not include commentary in Items 4 or 6 or attach an exhibit that opposes management, its initiatives and/or a pending transaction in an effort to influence votes related to such matters without also considering whether the proxy rules apply. Schedule 13D does not create an exception to the proxy rules. If the proxy rules apply, the filer must comply with them and file the Schedule 13D disclosure under cover of Schedule 14A to indicate that it is a proxy solicitation.

9. Conclusion: Although some of the interpretations in the C&DIs restate existing interpretations, many are new and revised. Investment advisers to mutual funds should

consider them carefully when preparing, filing and amending Schedules 13G and 13D.

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