

To: Commission File No. S7-32-10

From: Division of Economic and Risk Analysis

Date: June 20, 2023

Re: Supplemental data and analysis regarding the proposed reporting thresholds in the equity security-based swap market

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## Introduction

The Securities and Exchange Commission (“Commission”) proposed a new rule (“proposed Rule 10B-1”), on December 15, 2021, that would require any person with a security-based swap position that exceeds a certain threshold to promptly file with the Commission a schedule disclosing certain information related to its security-based swap positions (the “Proposing Release”).<sup>1</sup> The most recent comment period closed on November 1, 2022.<sup>2</sup>

Several commenters focused on the potential use by the Commission of security-based swap data reported to registered Security-Based-Swap Data Repositories (“SBSDR”).<sup>3</sup> Since

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<sup>1</sup> See Prohibition Against Fraud, Manipulation, or Deception in Connection with Security-Based Swaps; Prohibition Against Undue Influence Over Chief Compliance Officers; Position Reporting of Large Security-Based Swap Position, Release No. 34-93784 (Dec. 15, 2021), 87 FR 6652 (Feb. 4, 2022) (“Proposing Release”). The Proposing Release also included re-proposed antifraud and anti-manipulation rules in connection with security-based swaps, and a rule aimed at protecting the independence and objectivity of a security-based swap dealer’s or major security-based swap participant’s chief compliance officer (“CCO”) by preventing the personnel of such an entity from taking actions to coerce, mislead, or otherwise interfere with the CCO. These additional rules are not addressed in this memorandum.

<sup>2</sup> Resubmission of Comments and Reopening of Comment Periods for Several Rulemaking Releases Due to a Technological Error in Receiving Certain Comments, Release No. 33-11117 (Oct. 7, 2022), 87 FR 63016 (Oct. 18, 2022). The initial comment period for the Proposing Release closed on March 21, 2022. The comment period was reopened on October 7, 2022, and this reopened comment period closed on November 21, 2022. The comment letters are available at <https://www.sec.gov/comments/s7-32-10/s73210.htm>.

<sup>3</sup> See, e.g., Letter from Richard B. Zabel, Elliott Investment Management L.P., dated March 21, 2022, at 5 (“Elliott Letter”) (arguing that “The Proposed Rule is Premature. The Proposed Rule’s restrictive regime is also premature and inappropriate in light of the Commission’s recently adopted SBS repository reporting regime, which was implemented to provide less intrusive, nonpublic disclosure of swap holdings in a given issuer that would enable the Commission to effectively monitor the SBS market.”); Letter from Jiri Król, Deputy CEO, Global Head of Government Affairs, Alternative Investment Management Association, dated March 21, 2022, at 9-10 (arguing that “The Commission fails to adequately consider that reporting under Regulation SBSR began only mere weeks ago. Even with this limited SBSDR data, the Commission focuses almost entirely on the CDS market in the Proposal, despite daily trading volume in equity-based SBSs vastly outnumbering single-name CDS volume. The Proposing Release even goes so far as to explain that the Commission “intends to consider this newly available data in determining thresholds . . . when adopting a final rule. Such a decision would require the Commission to re-issue the Proposal to allow market participants the opportunity to opine on these new thresholds, while also indicating that the Proposal’s thresholds are not grounded in appropriate data analysis. We believe the Commission was premature in issuing the Proposal until it, SBSDRs and market participants have had some experience with the reported data and public dissemination thereof.”); Letter from John L. Thornton and R. Glenn Hubbard Co-Chairs, and Hal S. Scott, President, Committee on Capital Markets Regulation, dated March 21, 2022, at 12 (arguing that “The SEC should allow SBSDR reporting to take full effect and study the related data

November 2021, the Commission has had access to security-based swap data reported to SBSDR pursuant to Regulation SBSR.<sup>4</sup> Only approximately one month of these data were available at the time of the Proposing Release, and therefore the data were not used in the Proposing Release.<sup>5</sup> The commenters generally stated that the Commission should analyze the security-based swap market using the SBSDR data.<sup>6</sup>

Several commenters also focused on the potential effects of proposed Rule 10B-1 on activist investors.<sup>7</sup> The commenters generally stated that activist investors deploy strategies to acquire minority stakes of shares in a target issuer, in an attempt to effect managerial or strategic change.<sup>8</sup>

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before imposing extensive reporting requirements that present a clear risk of negative impacts to security-based swap markets and to capital formation that depends on such markets to hedge risk.”).

<sup>4</sup> See 17 CFR 242.900-909.

<sup>5</sup> Proposing Release, 87 FR at 6671. The data reported to SBSDRs include all security-based swaps transactions that: (1) include a U.S. person as a direct or indirect counterparty; (2) are accepted for clearing by a clearing agency with a principal place of business in the U.S.; (3) are executed on a platform with a principal place in the U.S.; (4) are effected by or through a registered broker-dealer (including a registered security-based swap execution facility); or (5) are connected with a non-U.S. person's security-based swaps dealing activity and are arranged, negotiated, or executed by personnel of such non-U.S. person located in a U.S. branch or office, or by personnel of an agent of such non-U.S. person located in a U.S. branch or office.

<sup>6</sup> See, e.g., Elliott Letter (“The public release of SBS position data will prematurely reveal information about the value of a security that activist investors have developed through their own fundamental research. SBS allow activist investors to take an economic stake in a company without some of the costs and disclosure obligations of investing in other securities.”).

<sup>7</sup> See, e.g., *id.* at 4 (arguing that “activists’ strategies are of significant value, and the Proposed Rule [10B-1] would destroy that value by making it difficult or impossible to execute such strategies, despite their broad benefits to the market”); Letter from 85 Law and Finance Professors, dated Mar. 21, 2022, at 7 (arguing that incentives to activism would decrease because “[t]hese incentives arise from the expected gains in positions that shareholder activists can accumulate before engaging in actions to mitigate agency costs, reduce corporate malfeasance, and hold managers and directors accountable to shareholders”).

<sup>8</sup> See, e.g., Elliott Letter, ex. B, at 13 (“The public release of SBS position data will prematurely reveal information about the value of a security that activist investors have developed through their own fundamental research. SBS allow activist investors to take an economic stake in a company without some of the costs and disclosure obligations of investing in other securities.”); Letter from Robert E. Bishop and Frank Partnoy, International Institute of Law and Finance, dated March 20, 2022, at 7 letter (“To the extent investors take smaller positions, we expect less shareholder engagement with management, and likely higher agency costs and managerial entrenchment. As at least one other comment letter shows, there are significant benefits to such engagement, including for retail investors.”). There are also academic studies that look at the stock performance of the targeted firm. See, e.g., Lucian Bebchuk et al., *The Long-Term Effects of Hedge Fund Activism*, 115 COLUM. L. REV. 1085 (2015) (estimating an announcement return of about 6% to initial Schedule 13D filings by activist hedge funds from 1994 through 2007, with, on average, no reversal in returns over the following five years); Simi Kedia et al., *Institutional Investors and Hedge Fund Activism*, 10 REV. CORP. FIN. STUD. 1 (2021) (demonstrating, in Table IA2 of the Internet Appendix, no reversal over five years of the positive one-year buy-and-hold returns for different subsamples of initial Schedule 13D filings by activist hedge funds from 2004 through 2012, based on a variety of models of benchmark returns); Nicole Boyson & Pegaret Pichler, *Hostile Resistance to Hedge Fund Activism*, 32 REV. FIN. STUD. 771 (2019) (estimating a buy-and-hold return of about 12% over a holding period averaging 2.7 years to campaigns by hedge fund activists from 2001 through 2012); Martijn Cremers et al., *Hedge Fund Activism and Long-Term Firm Value* (Working Paper, Dec. 13, 2018), available at <https://ssrn.com/abstract=2693231> (estimating a return of about 6% around the start of activist hedge fund

After reviewing the comments provided relating to the new SBSDR data and shareholder activism, staff in the Division of Economic Research and Analysis prepared this memorandum to provide supplemental analysis related to the economic effects of proposed Rule 10B-1. Using equity security-based swap data reported to SBSDRs, we first examine whether certain Schedule 13D Lead Filers would have had to report equity security-based swap positions under the reporting thresholds in proposed Rule 10B-1. Second, we analyze whether equity security-based swap positions of certain activist investors would have been reportable under some of the thresholds in proposed Rule 10B-1. Lastly, we inform on whether equity security-based swap positions of market participants generally would have been reportable under the thresholds in proposed Rule 10B-1 and several others.

## Data

For purposes of this memorandum, all data are for the period from November 1, 2021, through November 25, 2022 (the “Sample Period”). The Sample Period is limited to this date range because of structural changes in the transaction data reported to SBSDRs after December 5, 2022.<sup>9</sup> The analysis incorporates equity security-based swap data reported to SBSDRs and information from Schedule 13D filings.

We first curate the SBSDR data.<sup>10</sup> In our curated dataset, there are 8,523 unique equity security-based swap market participants identified by Legal Entity Identifiers (“LEIs”)<sup>11</sup> that had

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campaigns from 1995 through 2011, with, on average, no reversal in returns over the following five years); Edward Swanson et al., *Are All Activists Created Equal? The Effect of Interventions by Hedge Funds and Other Private Activists on Long-Term Shareholder Value*, 72 J. CORP. FIN. 102144 (2022) (estimating returns of 5% to initial Schedule 13D filings in 1994 through 2014, with, on average, no reversal in returns over the following three years); Ed deHaan et al., *Long-Term Economic Consequences of Hedge Fund Activist Interventions*, 24 REV. ACC. STUD. 536 (2019) (estimating, on an equally weighted basis, returns of 5% to initial Schedule 13D filings by activist hedge funds from 1994 through 2011, with, on average, no reversal in returns over the following two years); Alon Brav et al., *Governance by Persuasion: Hedge Fund Activism and Market-Based Shareholder Influence*, OXFORD RSCH. ENCYCLOPEDIA OF ECON. AND FIN. (2022) (estimating an announcement return of about 5% to blockholdings by hedge fund activists from 1994 to 2018, with, on average, no reversal in returns over the following three years).

<sup>9</sup> See CFTC Letter No. 22-06 (June 10, 2022), available at <https://www.cftc.gov/csl/22-06/download>.

<sup>10</sup> The SBSDR data as submitted by security-based swap market participants has several data issues, *See* Report on Security-Based Swaps, Mar. 20, 2023, available at <https://www.sec.gov/files/report-security-based-swaps-032023.pdf>; Report on Security-Based Swaps, July 15, 2022 (“July 2022 Report on Security-Based Swaps”), available at <https://www.sec.gov/files/report-security-based-swaps-071522.pdf>. To adjust for and address these data issues, we develop a curated SBSDR dataset. The curating process involves: i) standardizing counterparty information such that all buyers and sellers are consistently identified, ii) converting all non-U.S. Dollar notional amounts to U.S. dollar notional amounts using end of day exchange rates, iii) standardizing all reference entity identifier types to a single consistent type, and iv) removing erroneous observations (*e.g.*, notional amount reported in non-existing currencies, notional amounts per report greater than \$1 trillion, etc.).

<sup>11</sup> The LEI is a 20-digit, alphanumeric code that connects to key reference information that enables clear and unique identification of companies participating in global financial markets. The LEI is based on the ISO 17442 standard developed by the International Organization for Standardization. Each LEI contains information about an entity’s ownership structure and thus answers the questions of “who is who” and “who owns whom.” *See* Global Legal Entity Identifier Foundation (“GLEIF”), Level 1 Data: Who is Who,

at least one reported equity security-based swap position over the Sample Period. Of these LEIs, we exclude the 45 that are security-based swap dealers (“SBSDs”)<sup>12</sup> because they are not likely to engage in activist activity.<sup>13</sup> The remaining 8,478 non-SBSD market participants (hereafter “market participants”) trade contracts on a total of 133,025 reference securities. We include the 72% of such reference securities that are standardized to a consistent and identifiable reference identifier in our Sample Period and exclude the remaining 28%.<sup>14</sup>

In the Schedule 13D filings data<sup>15</sup> for the Sample Period, there are 1,184 initial filings<sup>16</sup>, with 1,102 unique “Schedule 13D Lead Filers”<sup>17</sup> who reported 3,516 unique “Schedule 13D Reporting Persons.” Schedule 13D Reporting Persons are required to report their beneficial ownership of a class of securities under Exchange Act Section 13(d).<sup>18</sup> These Schedule 13D filings reference 883 unique securities, 813 of which are referenced by an equity security-based swap in our data.

### **Equity Security-Based Swap Positions, in Reference to Schedule 13D Filing Events**

In this Section, we examine the equity security-based swap positions and beneficial ownership positions across Schedule 13D Reporting Persons on a Schedule 13D filing (hereafter, positions “on a Schedule 13D filing” or “on the Schedule 13D Filing”), with objective to inform on whether the Schedule 13D Lead Filer would have had to report the equity security-based swap positions under the reporting thresholds in proposed Rule 10B-1.

For a given Schedule 13D filing, we identify the equity security-based swap positions that (1) are held by each Schedule 13D Reporting Person in that filing, and (2) reference the class of equity securities in that Schedule 13D filing. We consider equity security-based swap positions up to 30 reporting days before and after the filing date (for a total of 61 reporting days) of each Schedule 13D filing (the “Event Period”).

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available at <https://www.gleif.org/en/lei-data/access-and-use-lei-data/level-1-data-who-is-who>; GLEIF, Level 2 Data: Who Owns Whom, available at <https://www.gleif.org/en/lei-data/access-and-use-lei-data/level-2-data-who-owns-whom>. The publicly available LEI data pool can be regarded as a global directory, which greatly enhances transparency in the global marketplace. *See* GLEIF, Introducing the Legal Entity Identifier, available at <https://www.gleif.org/en/about-lei/introducing-the-legal-entity-identifier-lei>.

<sup>12</sup> A complete list of conditionally registered SBSDs is available at <https://www.sec.gov/tm/List-of-SBS-Dealers-and-Major-SBS-Participants>.

<sup>13</sup> *See, e.g.*, Letter from Institute of International Bankers, International Swaps and Derivatives Association, and Securities Industry and Financial Markets Association, dated Mar. 21, 2022 (“Persons taking a directional position for the purpose of influencing control over an issuer are required to report on a more frequent basis than dealers, which are not in the business of changing or influencing the control of an issuer.”).

<sup>14</sup> Contracts on these 28% of referenced securities represent an estimated 15.1% of the gross notional amount for the Sample Period.

<sup>15</sup> Initial Schedule 13D filings are programmatically collected from EDGAR. The estimates described in this section are based on staff analysis of EDGAR filings.

<sup>16</sup> Amendments to Schedule 13D filings are not used; we use only initial Schedule 13D filings.

<sup>17</sup> “Schedule 13D Lead Filer” indicates the filer that submits a Schedule 13D filing to the Commission, though the same filing may include information about additional Schedule 13D Reporting Persons.

<sup>18</sup> 17 CFR 240.13d-1.

In 11 Schedule 13D filings, we observe Schedule 13D Reporting Persons—18 Scheduling 13D Reporting Persons in total across the 11 filings—who entered into an equity security-based swap position that referenced the class of equity securities in the Schedule 13D filing.<sup>19</sup> These 18 Schedule 13D Reporting Persons represent only 0.5% of the 3,516 Schedule 13D Reporting Persons in our data.

For each of these 11 Schedule 13D filings, we collect the beneficial ownership position from the Schedule 13D filing and security-based swap positions as reported in the equity SBSDR data across the Schedule 13D Reporting Persons on that filing, to get aggregate positions on the Schedule 13D filing.<sup>20</sup> There are significant limitations to our ability to perfectly identify equity security-based swap positions associated with a Schedule 13D filing. Critically, to be included in our sample, the equity security-based swap position must be held directly by a Schedule 13D Reporting Person on the Schedule 13D filing. We are aware of cases, not included in our sample, in which a fund that is affiliated with the Schedule 13D Reporting Persons, but is not itself a Schedule 13D Reporting Person, held equity security-based swaps even when none of the Schedule 13D Reporting Persons on the filing directly held such exposure.<sup>21</sup> Further, because Schedule 13D filings and the SBSDR data do not use the same identifiers for reporting entities and reference securities for Schedule 13D issuers, we may not identify all holdings in the SBSDR data that are associated with Schedule 13D Reporting Persons. Lastly, in 3 of these 11 Schedule 13D filings, we observe duplicate reporting of the same interests as beneficial ownership in Schedule 13D and as equity security-based swaps in the equity SBSDR data.<sup>22</sup>

Figure 1 shows the average, maximum, and minimum aggregate gross equity security-based swap positions across the 11 Schedule 13D filings.<sup>23</sup> The average gross position on a Schedule 13D filing varies from \$70 to \$170 million over the Sample Period, and the maximum gross position exceeds \$300 million only on 1 day (day 11 in Figure 1).

We also examine the gross position on each of the 11 Schedule 13D filings.<sup>24</sup> The gross position on only one of these filings exceeds the \$300 million reporting threshold in proposed Rule 10B-1 after the Schedule 13D filing date, and the Schedule 13D Lead Filer would have had

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<sup>19</sup> We merge the list of Schedule 13D Reporting Persons by name string with the list of equity security-based swap market participants.

<sup>20</sup> Some Schedule 13D filings report cash settled security-based swaps as well, while not counting them as part of the beneficial ownership.

<sup>21</sup> Through manual searches, we found six additional Schedule 13D filings within our sample period in which an affiliate of the Reporting Person had equity security-based swap exposure on the Schedule 13D filing date. These are not included in the below analysis as we require the Reporting Person to have direct exposure to both the equity security-based swap and the beneficial ownership.

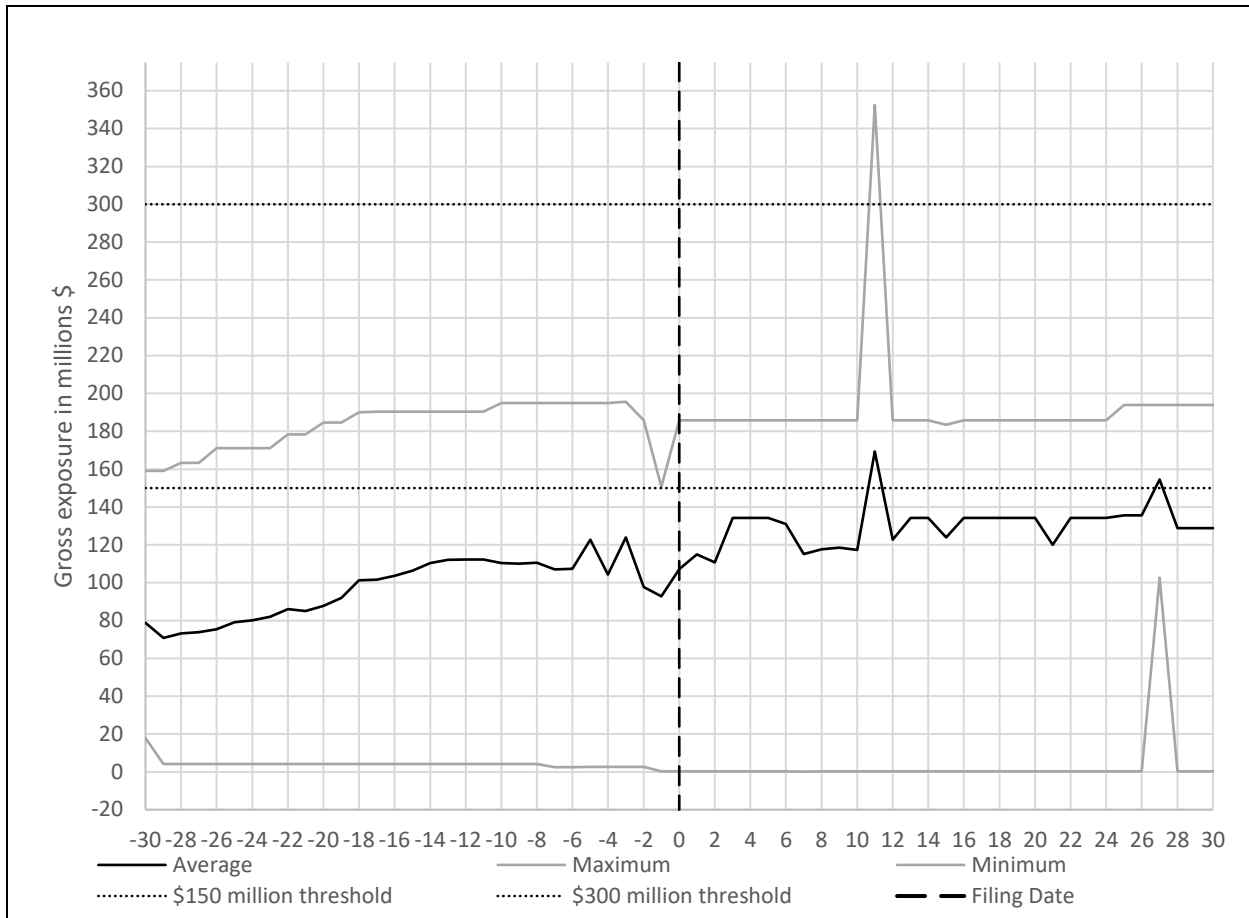
<sup>22</sup> Physically settled security-based swaps (as well as cash settled security-based swaps) are required to be reported under Regulation SBSR. In addition, the SBSDRs includes a classification for forward contracts, although that is not a Commission classification under Regulation SBSR. Some of the same physically settled security-based swaps and forward contracts positions are also reported in Schedule 13D filings, creating duplicate reports across the equity SBSDR data and Schedule 13D filings.

<sup>23</sup> The sample on any given day of aggregate gross equity security-based swap positions across the Schedule 13D filings used in calculating the average, maximum, and minimum can vary from a minimum of four observations to a maximum of eight observations with a median of seven observations per day.

<sup>24</sup> Figure 1 displays the average, maximum, and minimum to convey the distribution of the aggregate gross equity security-based swap positions in order to avoid disclosing to the public the equity security-based swap positions of Schedule 13D Reporting Persons on a given Schedule 13D filing.

to report the position. The gross position on each of the other 10 Schedule 13D filings is below that \$300 million threshold, and under that threshold the Schedule 13D Lead Filer would not have had to report. The gross position on four of these 10 Schedule 13D filings, while less than \$300 million, exceeds the other reporting dollar threshold in proposed Rule 10B-1 (specifically, the \$150 million threshold), and the Schedule 13D Lead Filer might have had to report depending on the extent of additional equity and derivative exposures on the Schedule 13D filing.

**Figure 1: Average, Maximum, and Minimum Aggregate Gross Equity Security-Based Swap Positions on a Schedule 13D Filing.**



In 11 Schedule 13D filings, Schedule 13D Reporting Persons on the filing entered into an equity security-based swap position that referenced the class of equity securities in the filing. Figure 1 shows the average, maximum, and minimum aggregate gross equity security-based swap positions at the level of the Schedule 13D filing across these 11 Schedule 13D filings.

Data gaps and quality observations on certain days reflect a lack of data in the SBSDR on those days.<sup>25</sup>

The two horizontal dotted lines represent the \$150 million and \$300 million thresholds.

In 9 of the 11 Schedule 13D filings considered, Schedule 13D Reporting Persons had equity security-based swap economic exposure in the 30-reporting day period prior to the Schedule 13D filing date.<sup>26</sup> For these 9 Schedule 13D filings, Figures 2A through 2D show the average, maximum, and minimum aggregate equity security-based swap exposure and beneficial

<sup>25</sup> See generally July 2022 Report on Security-Based Swaps, at 10 (discussing potential data quality issues in security-based transactions).

<sup>26</sup> On the other two Schedule 13D filings, all Schedule 13D Reporting Persons do not hold any equity security-based swaps before the Schedule 13D filing date; they hold such swaps only in the 30 days after the filing date.

ownership amounts<sup>27</sup> on a Schedule 13D filing, as a percentage of the market capitalization of the referenced class of equity securities in the filing, for each of the 30 reporting days prior to the Schedule 13D filing date. The data on beneficial ownership exposure prior to the filing date are derived from the Schedule 13D Reporting Persons' reported transaction history under Item 5(c) of Schedule 13D, which requires the Schedule 13D Reporting Person to disclose any transactions in the class of securities reported on that were effected during the 60 days preceding the initial Schedule 13D filing.<sup>28</sup> Accordingly, these data are available only for the period prior to the Schedule 13D filing data (represented by "event time zero" in Figure 2).<sup>29</sup>

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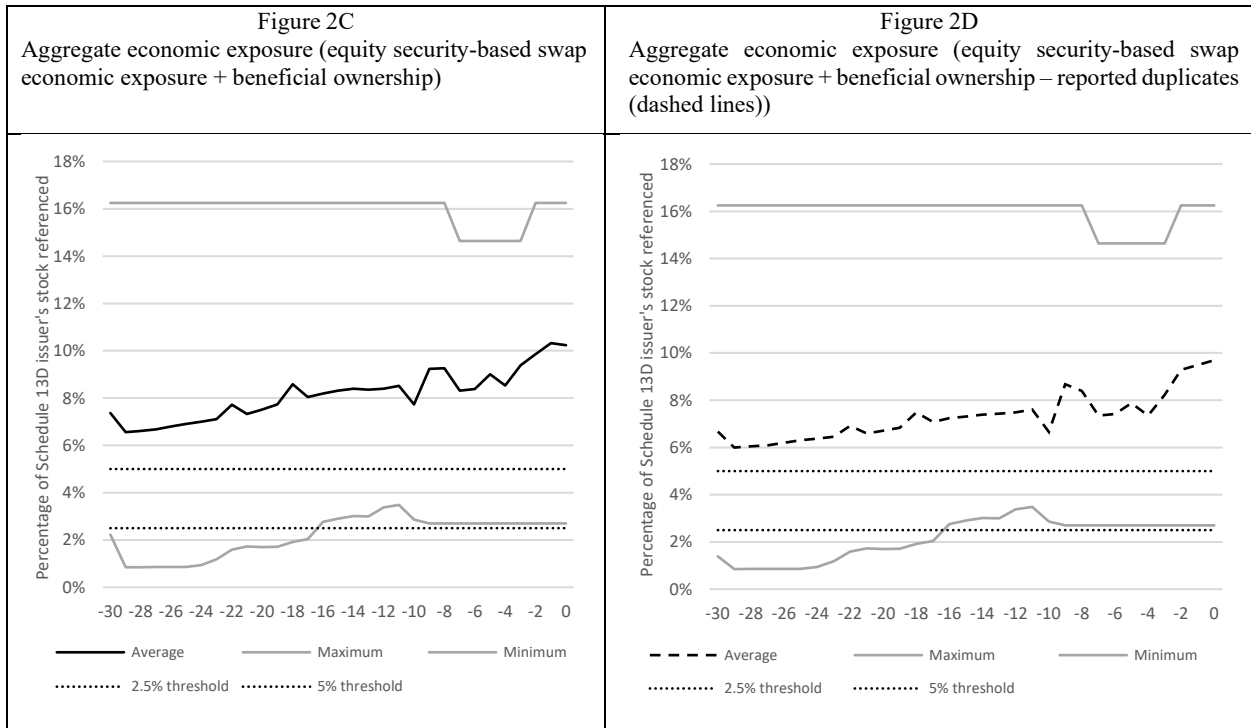
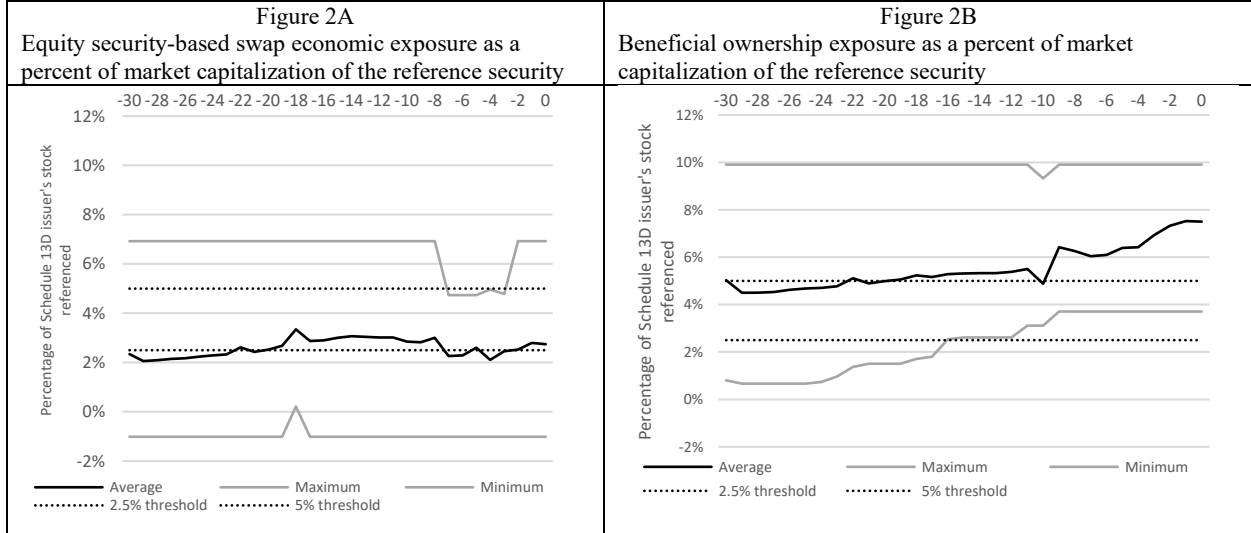
<sup>27</sup> Equity security-based swap economic exposure is aggregated across Schedule 13D Reporting Persons, while the beneficial ownership exposure is retrieved directly from the Schedule 13D filing.

<sup>28</sup> 17 CFR 240.13d-101.

<sup>29</sup> The analysis is limited to the Event Period of 30 reporting days before and after the Schedule 13D filing date as empirically observed changes in equity security-based swap positions occur closer to the Schedule 13D filing date.



**Figures 2A-2D. Average, Maximum, and Minimum Aggregate Equity Security-Based Swap Positions and Beneficial Ownership Positions on a Schedule 13D filing, as a percentage of the market capitalization of the referenced class of equity securities in the filing.<sup>30</sup>**



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Figure 2A uses only equity security-based swap data, while Figures 2B, 2C, and 2D use both equity security-based swap data and beneficial ownership data. Beneficial ownership data is limited to the period prior to the Schedule 13D filing, hence all the charts in Figure 2 are limited to the time period prior to the Schedule 13D filing up to and including the filing date.

Each chart displays the security-based swap reporting percent thresholds of more than 2.5% and more than 5%. Data gaps on certain days reflect a lack of data in the SBSDR on those days.<sup>31</sup>

The event period is 30 reporting days prior to the Schedule 13D filing date. The Schedule 13D filing date is time zero. Two Schedule 13D filings from Figure 1 are not plotted as the Schedule 13D Reporting Persons on these filings do not hold any equity security-based swaps before the filing date (event time zero); they only hold such swaps in the 30 days after the filing date.

In Figure 2D the dashed average line adjusts for three Schedule 13D filings that had duplicate, in part or in entirety, equity security-based swap positions data reported in both the Schedule 13D and the SBSDR data.

Figure 2A: Average, maximum, and minimum equity security-based swap economic exposures aggregated across Reporting Persons across Schedule 13D filings for which Reporting Persons reported equity security-based swap positions referencing class of equity securities in the Schedule 13D filing in the SBSDR data on the Schedule 13D filing date.

Figure 2B: Average, maximum, and minimum beneficial ownership exposure for each of the filings as stated in Item 5 of Schedule 13D.

Figure 2C: Average, maximum, and minimum aggregate economic exposure that is captured through equity security-based swap and beneficial ownership, *not adjusting* for double reports in the two databases. Due to double reports not being adjusted, this aggregate exposure can be thought of as upper bounds in terms of overall economic exposure.

Figure 2D: Average, maximum, and minimum aggregate economic exposure that is captured through equity security-based swap and beneficial ownership *while adjusting* for double reports in the two databases. Equity security-based swaps that are reported in both Schedule 13D and the SBSDR data are removed once from the aggregate numbers to provide a precise percentage of the aggregate economic exposure. This occurs in three Schedule 13D filings.

Figure 2A shows the average, maximum, and minimum equity security-based swap positions on a Schedule 13D filing, as a percentage of the market capitalization of the reported beneficial ownership with respect to the class of equity securities in the filing. In four of the nine filings, the equity security-based swap exposure is less than the 2.5% reporting threshold in proposed Rule 10B-1, and the Schedule 13D Lead Filer would not have had to report. In two filings, the swap exposure exceeds the 5% reporting threshold in proposed Rule 10B-1, and these two Schedule 13D Lead Filers would have had to report, likely prior to the Schedule 13D filing. In the remaining three filings, the equity security-based swap exposure is over 2.5% but less than 5%, in which instance the Schedule 13D Lead Filer would have had to report under proposed Rule 10B-1 only if the combined beneficial ownership exposure and equity security-based swap exposure on the Schedule 13D filing were more than 5%.

Figure 2B shows the average, maximum, and minimum beneficial ownership amount on a Schedule 13D filing, as a percentage of the market capitalization of the referenced class of equity securities in the filing. In two out of the nine filings, the initial Schedule 13D filing was made after the Schedule 13D Lead Filer had previously reported on Schedule 13G without changing the amount of beneficial ownership. This explains why, in Figure 2B, the maximum beneficial ownership, across the nine Schedule 13D filings, is higher than 5% over 10 days before the filing date.

Figure 2C shows the average, maximum, and minimum aggregate economic exposure that is gained by combining both equity security-based swap positions and beneficial ownership

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<sup>31</sup> See *supra* note 25.

on a Schedule 13D filing. Three Schedule 13D filings included equity security-based swap positions that matched positions also reported in the equity SBSDR data. In other words, their beneficial ownership reports already contained a portion of the reported equity security-based swap position in the equity SBSDR data. This overlap amounts to 0.2% on average and 1.18% at most. Removing the duplication decreases the aggregate positions on these three filings, and Figure 2D shows the average, maximum, and minimum aggregate economic exposure after adjusting for the duplication in three of the Schedule 13D filings.

Based on the data in Figure 2D, in all three Schedule 13D filings in Figure 2A for which the equity security-based swap exposure is over 2.5% but less than 5%, the combined beneficial ownership amount and equity security-based swap exposure is more than 5% (over 10 days before the Schedule 13D filing date). Accordingly, in each of these three Schedule 13D filings, the Schedule 13D Lead Filer would have had to report under proposed Rule 10B-1, prior to the date at which the Schedule 13D was filed.

In summary, under the reporting thresholds in proposed Rule 10B-1, the Schedule 13D Lead Filer in five of the nine Schedule 13D filings considered would have had to report under proposed Rule 10B-1.

### **Equity Security-Based Swap Positions, Generally Across Activist Investors**

In this Section, we inform on the extent to which the equity security-based swap positions of certain individual market participants may be reportable under some of the thresholds in proposed Rule 10B-1. We consider all Schedule 13D Reporting Persons who reported equity security-based swap activity over the Sample Period. We supplement this list of Schedule 13D Reporting Persons with a list of equity market participants who have engaged in activist activity, as reported in FactSet data.<sup>32</sup> Overall, the analysis may provide insight into the use of equity security-based swaps by “activist investors” even when these swap positions are not associated directly with a Schedule 13D filing.

There are 114 Schedule 13D Reporting Persons (identified by their LEIs), supplemented with another 62 GLEIF intra-affiliate entities,<sup>33</sup> who reported equity security-based swap activity in the SBSDR data over the Sample Period. These 114 Schedule 13D Reporting Persons

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<sup>32</sup> The list of “activist investors” we obtain from FactSet is comprised of “known activist” investors, or in general (i) equity market participants that are in FactSet’s SharkWatch 50 (top 50 “activist investors”) and (ii) additional equity market participants that have been designated by FactSet as “known activists” in its SharkRepellent database, where most “known activists” have been involved in at least five campaigns. This list includes 349 globally known investors that participate in activist activities, of which 289 are U.S. persons, 51 are non-U.S. persons, and nine have an unreported jurisdiction. We manually identified the LEIs of the parent entities of these 349 activist investors, using the (“GLEIF”) database, available at <https://www.gleif.org/en>. Not all of these 349 FactSet “activist investor” parent entities reported a LEI, decreasing the sample to 182 FactSet “activist investors” of which 149 in the U.S. persons and 33 are non-U.S. persons.

<sup>33</sup> See, e.g., GLEIF, Level 2 Data: Who Owns Whom, *supra* note 11 (“The business card information available with the LEI reference data; e.g. the official name of a legal entity and its registered address, is referred to as ‘Level 1’ data. It provides the answer to the question of ‘who is who.’ In addition, the LEI data pool includes the ‘Level 2’ data that answers the question of ‘who owns whom.’ Specifically, legal entities that have or acquire an LEI report their ‘direct accounting consolidating parent’ as well as their ‘ultimate accounting consolidating parent.’”).

represent only 3.2% of the 3,516 Schedule 13D Reporting Persons in our data. In the FactSet data, 49 activists, supplemented with another 36 GLEIF intra-affiliate entities, reported equity security-based swap activity in the SBSDR data over the Sample Period. These 49 activists represent 14% of the 349 global activists in the FactSet data.<sup>34</sup> In total, accounting for overlap between the list of Schedule 13D Reporting Persons and FactSet data, we have a list of 244 potential activist investors<sup>35</sup> (including GLEIF intra-affiliate entities) who reported equity security-based swap activity in the SBSDR data.

Our analysis is subject to significant limitations in our ability to identify equity security-based swap positions associated with an activist investor. Critically, to be included in our sample, the equity security-based swap position must be held by the GLEIF intra-affiliate entities, whose LEI we obtain and search for in the SBSDR database. However, many activist investors are associated with many different funds or other entities, any of which may be party to an equity security-based swap. We are aware of many cases in which an activist investor has equity security-based swap exposure through an entity other than the parent or child entity.

We consider gross positions for equity security-based swaps that reference U.S. listed securities over the Sample Period.<sup>36</sup> We define gross position as the aggregate of both long and short equity security-based swap holdings for the same referenced security.<sup>37</sup> For the purpose of calculating gross positions, we aggregate positions across sub-products in equity security-based swaps (*e.g.*, contracts for difference, total return swaps, forwards,<sup>38</sup> etc.) for the same referenced security and activist investor. These data on positions do not account for direct equity holdings due to data constraints. Data regarding equity holdings, although potentially available in a smaller number of cases, have yet to be successfully merged broadly with equity security-based swap data positions because of differences in underlying reference data identifiers. Hence, the analysis may undercount the number of activist investors who might need to file Schedule 10B when aggregating both beneficial ownership and equity security-based swap positions.

In our data, on a given day, an activist investor held, on average, equity security-based swap gross positions on 55 different referenced securities, and an activist investor's gross position in a referenced security was \$8.41 million. This average gross position comprised an average long position of \$3.47 million and an average short position of \$4.94 million. In total,

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<sup>34</sup> Number of known activist investors' LEIs from FactSet that reported equity SBS positions (49 in total, 43 are US, and 6 are non-US), divided by total number of activist investors in FactSet (349 in total, 289 are US, 51 are non-US, and nine did not have a valid country code),  $49/349=14\%$ ,  $43/289=14\%$ , or  $6/51=11\%$  if limited to non-US investors.

<sup>35</sup> When it comes to activism, this list of Schedule 13D filers may be over-inclusive in that some small portion of Schedule 13D filers may not be involved in activist investor strategies.

<sup>36</sup> These reference securities are limited to U.S. entities that are listed on the following exchanges: NYSE, NASDAQ, Direct Edge Holdings, Investors Exchange, OTC Bulletin Board, OTC (Finra), Intl Sec Exch – Equities, Third Market Stock, OPRA NBBO Options, Chicago Options, Philadelphia Options, BATS Trading for Nasdaq, and Long-Term SE.

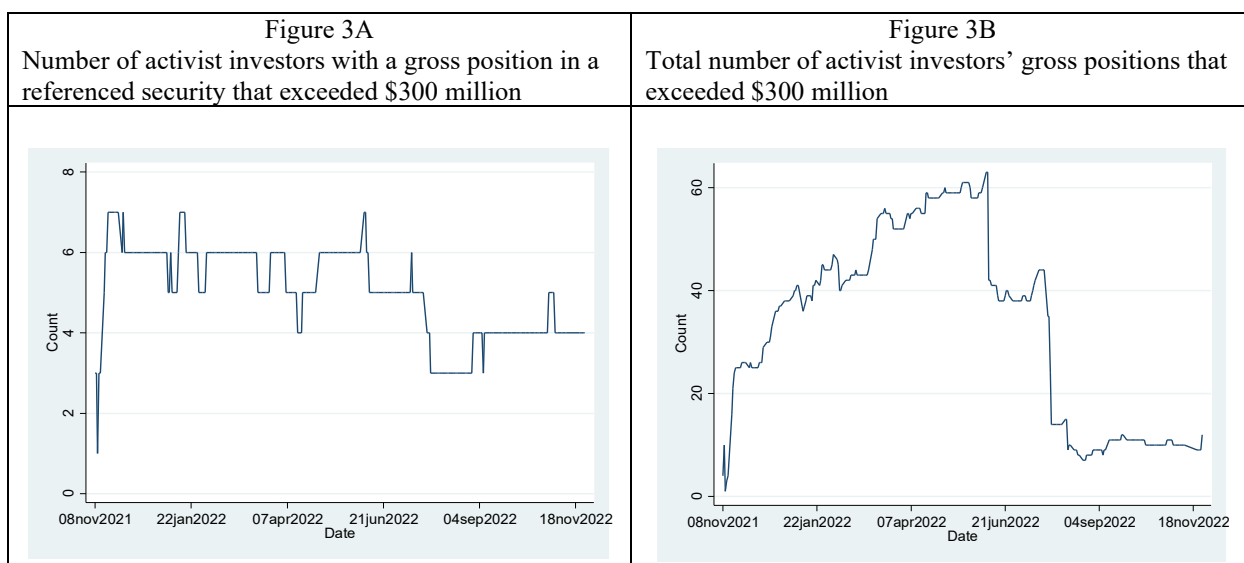
<sup>37</sup> The Proposing Release uses the term "gross" to mean the sum of the absolute values of notional amounts outstanding of all of the security-based swaps included in a security-based swap position. For example, if a person has a \$75 million long CDS position and a \$75 million short CDS position on the same reference entity or security, the person will have a gross security-based swap position of \$150 million. *See* Proposing Release, 87 FR at 6669.

<sup>38</sup> Equity security-based swaps are reported to the SBSDR under these sub-classifications; these are not our classifications.

activist investors took an aggregate daily average gross position of \$57.426 billion, which amounted to 1.19% of the total gross market outstanding, which was \$4.806 trillion on average during this Sample Period. Activist investors may engage in significant activities outside of activism, so some of this equity securities-based swap exposure may represent general investing or hedging activities unrelated to activist campaigns.

Figures 3 and 4 below report on large gross positions in equity security-based swaps held by activist investors.

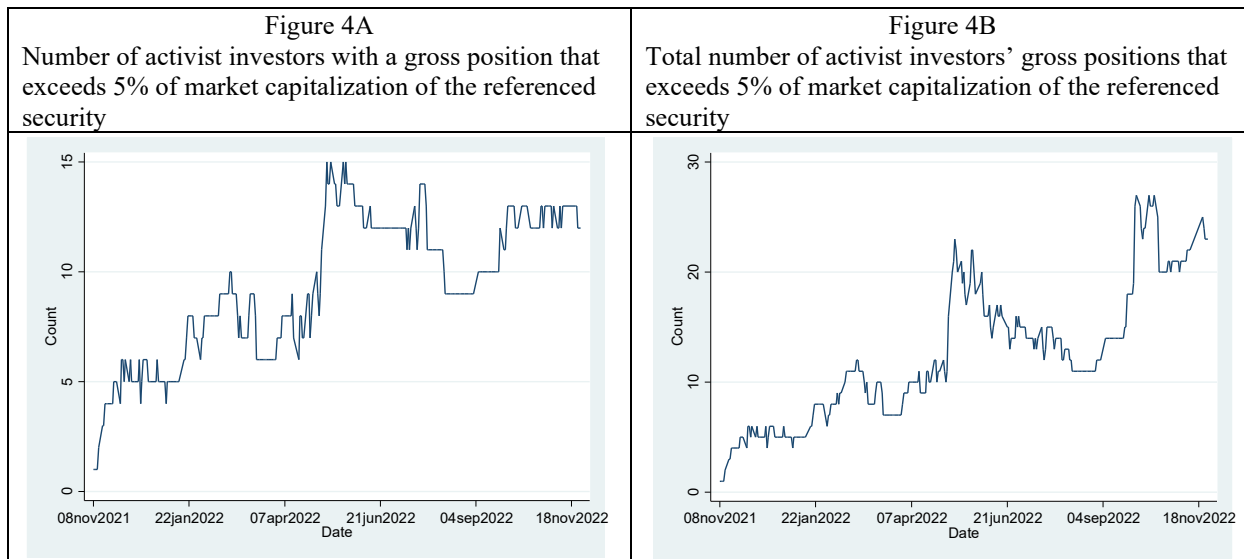
**Figure 3: Activist Investors with Gross Positions Exceeding \$300 Million (listed in the U.S.)**



Figures 3A and 3B pertain to activist investors' gross positions in referenced securities that exceed \$300 million. Figure 3A shows the number of activist investors who held at least one such large gross position. There are at most seven such activist investors on any given day during the Sample Period. Figure 3B shows the total number of large gross positions held by the activist investors shown in Figure 3A. On any given day, the number of large gross positions in referenced securities can be greater than the number of activist investors, if any activist investor holds more than one such large gross position.<sup>39</sup> Figure 3B shows that activist investors held fewer than 63 large gross positions on any given day during the Sample Period.

<sup>39</sup> Similarly, the number of large gross positions in referenced securities could also be greater than the number of referenced securities on any given day, if multiple activist investors hold a large gross position in the same referenced security.

**Figure 4: Activist Investors with Gross Positions Exceeding 5% of Market Capitalization in a Referenced Security (listed in the U.S.)**



Figures 4A and 4B pertain to activist investors' gross positions in referenced securities such that each gross position exceeds 5% of the referenced security's market capitalization. Figure 4A shows the daily number of activist investors who held at least one such large gross position. There are at most 15 such activist investors on a given day during the Sample Period. Figure 4B shows the total number of large gross positions held by the activist investors shown in Figure 4A. On any given day, the number of large gross positions in referenced securities can be greater than the number of activist investors, if any activist investor holds more than one such large gross position.<sup>40</sup> Figure 4B shows that activist investors held fewer than 30 large gross positions on any given day during the Sample Period.

### Equity Security-Based Swap Positions, Generally Across Market Participants

In this Section, we inform on the extent to which market participants may have equity security-based swap gross positions that would be reportable under the thresholds in proposed Rule 10B-1 and several others.

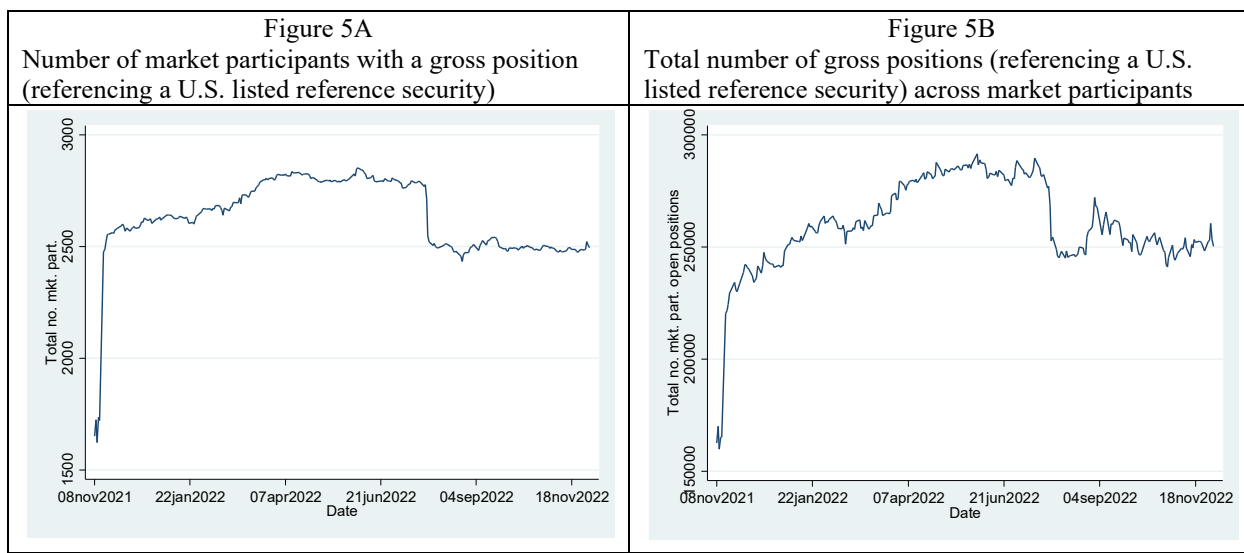
The analysis is again limited to equity security-based swaps that reference U.S. listed securities, and it is subject to the same limitations we previously identified in our analysis of equity security-based swap positions associated with activist investors. We also continue to use the same definition of gross positions for equity security-based swaps that reference U.S. listed securities over the Sample Period. This analysis uses all market participants, both SBSs and non-SBSs.

For each day during the Sample Period, Figure 5 shows the number of market participants who reported an open equity security-based swap position referencing a U.S. listed

<sup>40</sup> *Id.*

reference security and the total number of such positions across market participants. Specifically, Figure 5A shows the number of market participants. There are, on average on a daily basis, 2,628 market participants, and the largest number of market participants on any given day is 2,852. Figure 5B shows the total number of positions. Market participants had, on average on a daily basis, 259,733 positions, and the largest number of positions on any given day is 291,587.

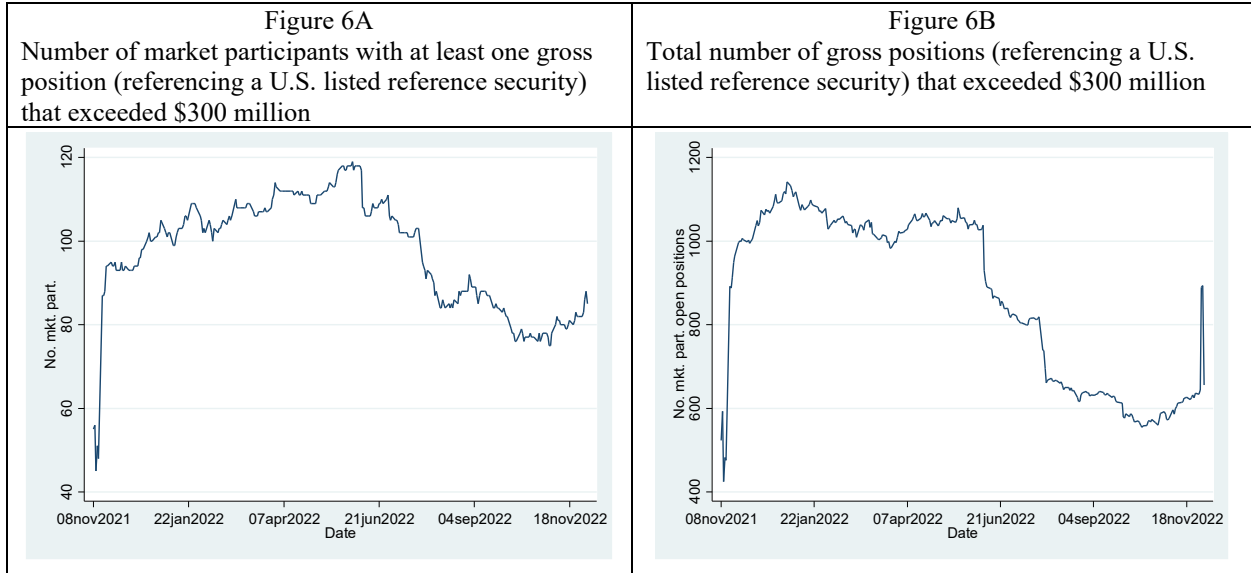
**Figure 5: Number of Market Participants with a Gross Position and Total Number of Gross Positions**



For each day during the Sample Period, Figure 6 shows the number of market participants with at least one gross position exceeding the \$300 million threshold under proposed Rule 10B-1 and the total number of such large positions across market participants. Figure 6A shows the number of market participants with at least one gross position exceeding \$300 million. There are, on average on a daily basis, 97 such market participants, and the largest number of market participants on any given day is 119. Figure 6B shows the daily total number of gross positions exceeding \$300 million. On any given day, the number of such large gross positions can be greater than the number of market participants if any market participant holds more than one large gross position.<sup>41</sup> Figure 6B shows that market participants had, on average on a daily basis, 868 large gross positions, and the largest number of gross positions on any given day is 1,142.

<sup>41</sup> *Id.*

**Figure 6: Number of Market Participants with a Gross Position Exceeding \$300 Million and Total Number of Gross Positions Exceeding \$300 Million**

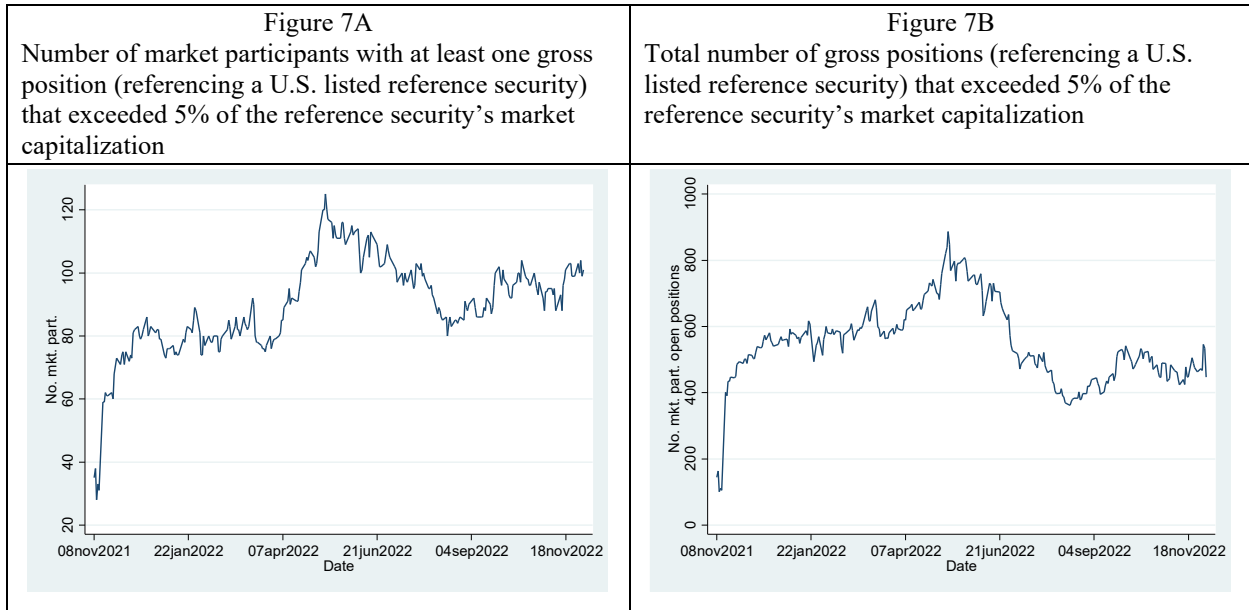


For each day during the Sample Period, Figure 7 pertains to market participants’ gross positions in referenced securities such that each gross position exceeds 5% of the referenced security’s market capitalization. Figure 7A shows the number of market participants with at least one gross equity security-based swap position exceeding 5% of the referenced security’s market capitalization. On a daily basis, there are, on average, 90 such market participants, and the largest number of market participants on any given day is 125. Figure 7B shows, for U.S. listed reference securities, the daily total number of gross positions exceeding 5% of the reference security’s market capitalization. On any given day, the number of such large gross positions can be greater than the number of market participants if any market participant holds more than one large gross position.<sup>42</sup> Figure 7B shows that market participants have, on average on a daily basis, 545 large gross positions, and the largest number of gross positions on any given day is 887.

<sup>42</sup> *Id.*



**Figure 7: Number of Market Participants with a Gross Position Exceeding 5% of the Reference Security’s Market Capitalization and Total Number of Gross Positions Exceeding 5% of the Reference Security’s Market Capitalization**

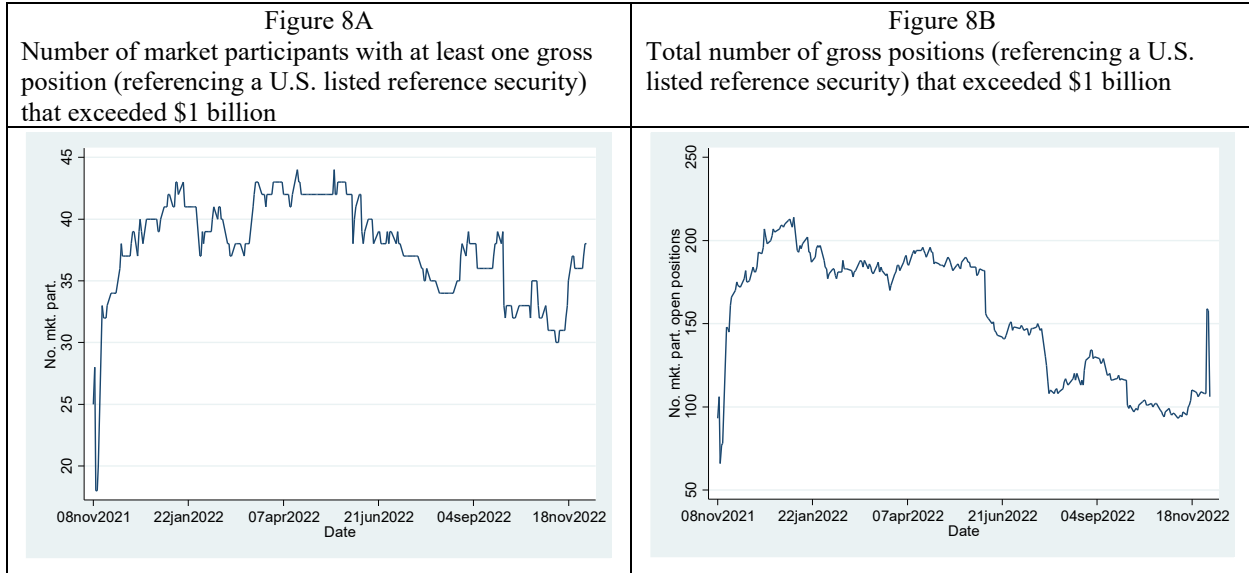


For each day during the Sample Period, Figure 8 shows the number of market participants with at least one gross position exceeding a \$1 billion threshold and the total number of such large positions across market participants. Figure 8A shows the number of market participants with at least one gross position exceeding \$1 billion. There are, on average on a daily basis, 38 such market participants, and the largest number of market participants on any given day is 43. Figure 8B shows the daily total number of gross positions exceeding \$1 billion. On any given day, the number of such large gross positions can be greater than the number of market participants if any market participant holds more than one large gross position.<sup>43</sup> Figure 8B shows that market participants had, on average on a daily basis, 154 large gross positions that exceed \$1 billion, and the largest number of gross positions on any given day is 210.

<sup>43</sup>

*Id.*

**Figure 8: Number of Market Participants with a Gross Position Exceeding \$1 Billion and Total Number of Gross Positions Exceeding \$1 Billion**

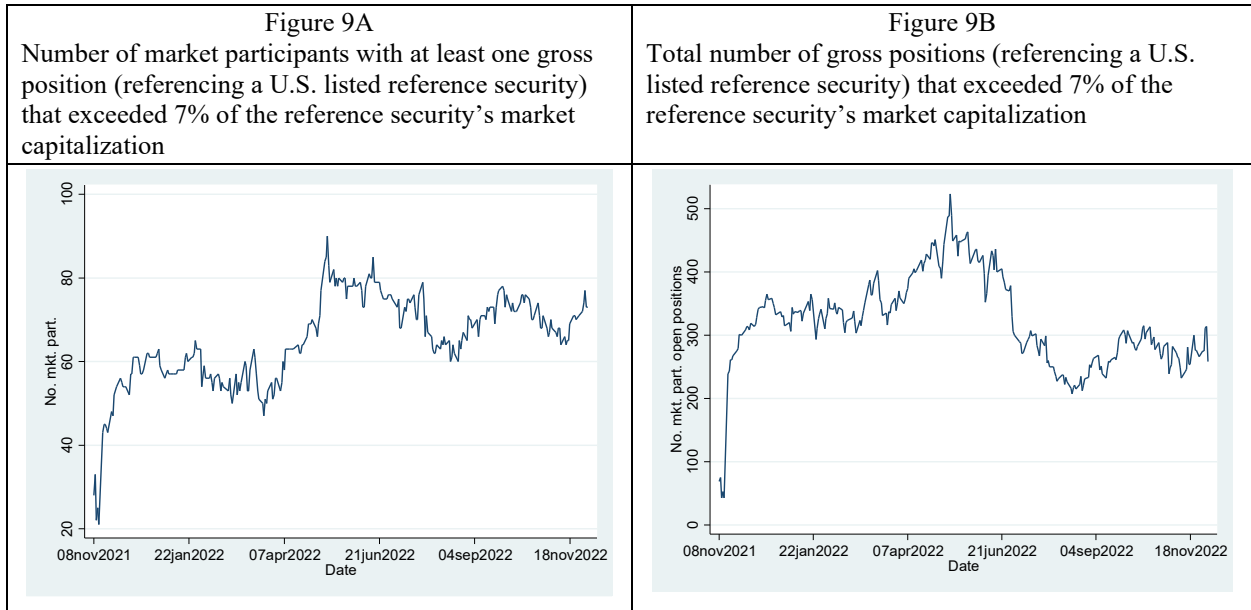


Finally, for each day during the Sample Period, Figure 9 and Figure 10 pertain to market participants’ gross positions in referenced securities such that each gross position exceeds 7% and 10% of the referenced security’s market capitalization, respectively. Figure 9A shows the number of market participants with at least one gross equity security-based swap position exceeding 7% of the referenced security’s market capitalization. Figure 10A shows the number of market participants with at least one gross equity security-based swap position exceeding 10% of the referenced security’s market capitalization. On a daily basis, there are on average 65 market participants that exceed the 7% threshold, and 46 market participants that exceed the 10% threshold. The largest number of market participants that exceed the 7% threshold on any given day is 90, while the largest number of market participants that exceed the 10% threshold on any given day is 60.

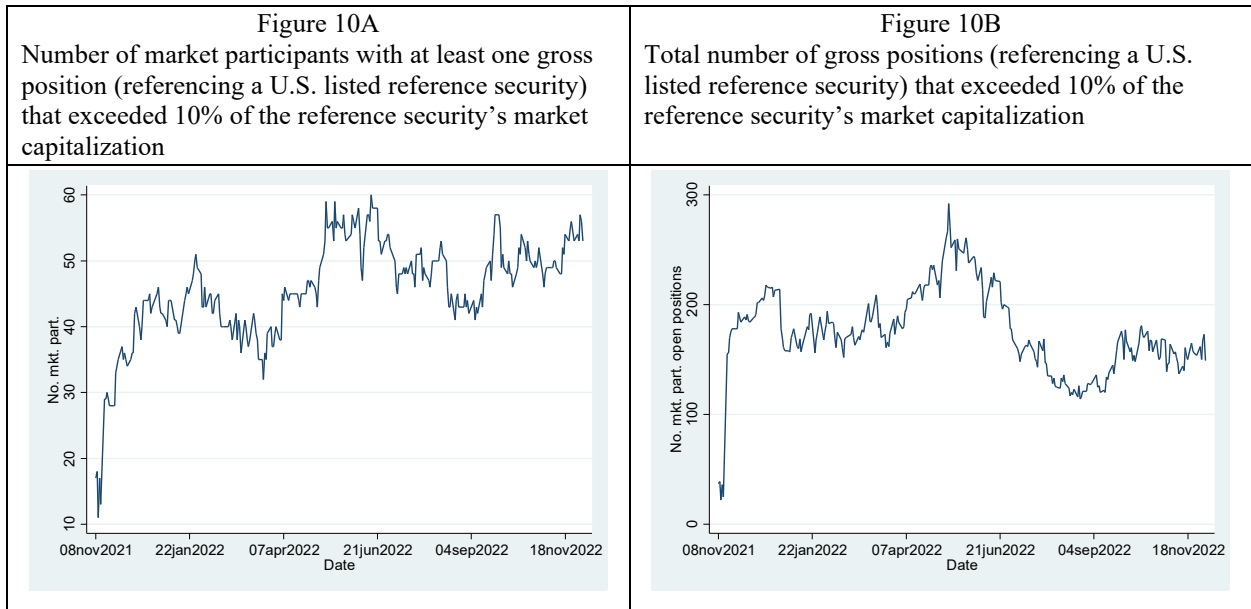
Figures 9B and 10B shows, for U.S. listed reference securities, the daily total number of gross positions exceeding 7% and 10% of the reference security’s market capitalization, respectively. On any given day, the number of such large gross positions can be greater than the number of market participants if any market participant holds more than one large gross position.<sup>44</sup> Figure 9B shows that market participants have, on average on a daily basis, 319 gross positions that exceed the 7% threshold, and the largest number of such gross positions on any given day is 523. Figure 10B shows that market participants have, on average on a daily basis, 174 gross positions that exceed the 10% threshold, and the largest number of such gross positions on any given day is 292.

<sup>44</sup> *Id.*

**Figure 9: Number of Market Participants with a Gross Position Exceeding 7% of the Reference Security’s Market Capitalization and Total Number of Gross Positions Exceeding 7% of the Reference Security’s Market Capitalization**



**Figure 10: Number of Market Participants with a Gross Position Exceeding 10% of the Reference Security’s Market Capitalization and Total Number of Gross Positions Exceeding 10% of the Reference Security’s Market Capitalization**



For Figures 6B, 7B, 8B, 9B, and 10B, the number of large gross positions on a given day would not represent the number of expected reports that would potentially have to be reported

because (1) market participants would report a position only the first time that they exceed the threshold (initial report); (2) positions are typically held for longer than a day, and there is no daily reporting requirement of positions; and (3) market participants would file amendments should they change their position by 10% (*i.e.*, increasing exposure by \$30 million if the initial position was \$300 million).