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SEC Adopts Significant Amendments to Beneficial Ownership Reporting Requirements and Provides Guidance on Derivatives Reporting and Group Formation Matters

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On October 10, 2023, the Securities and Exchange Commission (the "Commission" or "SEC") adopted final rules (the "Final Amendments"), significantly amending the beneficial ownership reporting requirements under Regulation 13D-G as promulgated pursuant to Sections 13(d) and 13(g) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). The Final Amendments are based on the Commission's February 10, 2022 proposed amendments (the "Proposed Amendments"), and primarily impact Schedule 13D and 13G ("13D/G") filing deadlines, while issuing guidance on topics such as the reporting obligations related to certain derivatives and the scenarios for potential group formation.

Specifically, the Final Amendments:

- Accelerate the 13D/G filing deadlines as detailed below
- Extend the 13D/G filing cut-off *times* from 5:30 p.m. to 10 p.m. EST
- Require disclosure of cash-settled derivative securities under Item 6 of Schedule 13D
- Impute group member acquisitions to the group once a group has been formed (excluding intragroup transfers of securities)
- Require the use of a structured, machine-readable data language (XBRL) for 13D/G filings

In addition, instead of adopting certain of the Proposed Amendments, the SEC provided guidance with respect to (i) the reporting obligations related to cash-settled derivatives and (ii) the types of situations where a Section 13(d) group may or may not be deemed to have formed.

The tables below summarize the more substantive changes to the Schedule 13D/G beneficial ownership reporting requirements.

Initial 13D Due Date (under Rule 13d-1(a))	Within 10 days of acquiring more than 5% beneficial ownership	Within **5 business days** of acquiring more than 5% beneficial ownership
Initial 13D Due Date	Within 10 calendar days after the event that	Within **5 business days** of losing

Related People

Ed Batts

David Korvin

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(Following Loss of 13G Eligibility under Rules 13d-1(e), (f), and (g))	causes ineligibility	eligibility to file on Schedule 13G
13D/A Trigger	"Material" change	"Material" change
13D/A Due Date	"Promptly"	Within **two business days** after the triggering event
Schedule 13G filed by Qualified Institutional Investors ("QIIs")	**Current**	**Revised (starting Sept. 30, 2024)**
Initial 13G Due Date	45 days after year-end in which beneficial ownership exceeds 5%	**45 days after quarter-end** in which beneficial ownership exceeds 5%
Periodic 13G/A Due Date and Trigger	Annual amendments: due 45 days after year-end if any change (not including changes due to fluctuations in number of shares outstanding)	Quarterly amendments: due **45 days after quarter-end if a material change** (not including changes due to fluctuations in number of shares outstanding)
Ownership Change 13G/A Due Date	10 business days after month-end if beneficial ownership exceeds 10% or there is a 5% decrease in beneficial ownership Thereafter, upon deviation by more than 5% of a covered class of equity securities	**Five business** days after month-end if beneficial ownership exceeds 10% Thereafter, upon deviation by more than 5% of a covered class of equity securities
Schedule 13G filed by "Passive" Investors (Rule 13d-1(c))	**Current**	**Revised (starting Sept. 30, 2024)**
Initial 13G Due Date	Within 10 days of acquiring more than 5% beneficial ownership	Within **5 business days** of acquiring more than 5% beneficial ownership
Periodic 13G/A Due Date and Trigger	Annual amendments: due 45 days after year-end if any change (not including changes due to changes in shares outstanding)	Quarterly amendments: due **45 days after quarter-end if a material change** (not including changes due to changes in shares outstanding)
Ownership Change 13G/A Due Date	"Promptly" upon acquiring more than 10% beneficial ownership Thereafter, upon deviation by more than 5% of a covered class of equity securities	Within **2 business days** of acquiring more than 10% beneficial ownership Thereafter, upon deviation by more than 5% of a covered class of equity securities
Schedule 13G filed by "Exempt" Investors (Rule 13d-1(d))	**Current**	**Revised (starting Sept. 30, 2024)**
Initial 13G Due Date	45 days after year-end in which beneficial ownership exceeds 5%	**45 days after quarter-end** in which beneficial ownership exceeds 5%
Periodic 13G/A Due Date and Trigger	Annual amendments: due 45 days after year-end in which any change occurred (other than change in percentage solely due to change in shares outstanding)	Quarterly amendments: due **45 days after quarter-end if material change occurred**

Cash-Settled Derivatives

The Commission declined to adopt proposed Rule 13d-3(e), which would have caused holders of certain cash-settled derivative securities, excluding security-based swaps ("SBS"), to be considered beneficial owners of the reference equity security. Instead, the Commission issued guidance on the circumstances under which a holder of a cash-settled derivative security, excluding SBS, may be deemed the beneficial owner of the reference equity security under Rule 13d?3.

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The SEC originally proposed Rule 13d-3(e) in response to concerns that holders of certain cash-settled derivatives were excluded from the definition of "beneficial owner" but could still exert influence over an issuer by, among other methods, pressuring a counterparty to the derivative transaction to make certain decisions regarding the voting and disposition of the issuer's securities. In response to public comments, the Commission determined that issuing guidance on the topic would be sufficient.

The SEC's guidance makes reference to its Security-Based Swaps Release which outlines three characteristics of a derivative position that may lead to the imputation of beneficial ownership: (i) the derivative security confers voting and/or investment power (or a person otherwise acquires such power based on the purchase or sale of a derivative security); (ii) the derivative security is used with the purpose or effect of divesting or preventing the vesting of beneficial ownership as part of a plan or scheme to evade the reporting requirements; or (iii) the derivative security grants a right to acquire an equity security. The Commission clarified that this guidance applies to non-SBS cash-settled derivatives, indicating that holders of a wide range of cash-settled derivatives could be considered beneficial owners when these circumstances exist.

The Commission also amended Item 6 of Schedule 13D to explicitly remove any implication that a person is not required to disclose interests in all derivative securities that use a covered class of security as a reference security. The new Item 6 expressly states that derivative contracts, arrangements, understandings, and relationships with respect to an issuer's securities, including cash-settled SBS and other derivatives which are settled exclusively in cash, must be disclosed. The SEC believes that investors will benefit from this more complete picture of Schedule 13D filers' economic interests in the relevant issuer.

Group Formation

In addition, the SEC declined to adopt certain of the Proposed Amendments relating to Rule 13d-5 that would have broadly expanded the type of investor activities giving rise to group formation. Instead, the Commission chose to issue guidance directly in the adopting release to the Final Amendments (the "Adopting Release") on the scope of activities that could give rise to group formation.

In doing so, the Commission acknowledged that neither the relevant statute nor SEC rules define "group." Instead, the Commission reiterated that the relevant standard for determining the existence of a "group" is found in Sections 13(d)(3) and 13(g)(3) of the Exchange Act. The Commission stated that the determination of whether two or more persons are acting as a group "depends on an analysis of all the relevant facts and circumstances and not solely on the presence or absence of an express agreement, as two or more persons may take concerted action or agree informally."

The guidance on activities that may or may not give rise to formation of a group is presented in question and answer format. In a helpful manner, the Commission described the following situations where a Section 13(d) group would not arise:

- Communications between two or more shareholders concerning a particular issuer, including topics relating to the improvement of the issuer's long-term performance, changes in issuer practices, submissions or solicitations in support of a non-binding shareholder proposal, a joint engagement strategy (that is not control-related), or a "vote no" campaign against individual directors in uncontested elections.
- Two or more shareholders engaging in joint communications with an issuer's management.
- Two or more shareholders making recommendations regarding the structure of the board of directors (so long as no discussion of individual directors or board expansion occurs and no commitments, agreements, or understandings are made

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among shareholders regarding their voting for director candidates).

- Two or more shareholders jointly submitting a non-binding shareholder proposal.
- A shareholder and an activist investor communicating regarding the activist's proposals, (so long as the shareholder does not make a commitment to a particular course of action).

However, in the Commission's view a group is likely to form where a beneficial owner of a substantial block of shares (one that is or will be required to file a Schedule 13D) intentionally communicates to other market participants (including investors) that such a filing will be made (to the extent this information is not yet public) with the purpose of causing such persons to make purchases, and one or more of the other market participants makes purchases in the same covered class of securities as a direct result of that communication. The concept of such "tipping" was discussed in the Proposing Release and is used in the Adopting Release as an example of where, in the Commission's view, a group would likely result.

Effective Dates

The Final Amendments were published in the Federal Register on November 7, 2023 and will become effective on February 5, 2024. Compliance with the revised Schedule 13G filing deadlines will be required beginning on September 30, 2024. Compliance with the structured data requirement for Schedules 13D and 13G will be required on December 18, 2024. Compliance with the other rule amendments will be required upon their effectiveness. In determining whether to file a Schedule 13G/A for year-end 2023, on or before February 14, 2024, we recommend holders file if there is any change (other than changes due to a fluctuation in the number of shares outstanding) consistent with most filers' traditional approach to reporting their ownership as of December 31.

Implications

As long anticipated in light of prior comments by Chair Gensler as well as the previously proposed changes, these final amendments in theory seek to modernize the reporting timing for Schedules 13D and 13G given the modern computer age and instant nature of disclosure dissemination. That said, as a practical matter, the new rules are likely to materially impact equity accumulation strategies for activist investor hedge funds in three respects:

- The reduction from 10 calendar days to 5 business days for an initial Schedule 13D filing will shave down the period that activists have to purchase equity securities more gradually to mitigate upward price pressure and optimize their basis. Commentators have differing opinions on how material the time deadline reduction will be – but it is likely to be non-trivial.
- Second, it is clear that the Commission will be looking closely at synthetic alternatives to actual equity ownership of a reportable class. Derivatives – particularly cash-settled equity swaps - have become popular instruments for activist hedge funds to lever the financial impact of their positions without having to actually purchase securities (or arguably, in the past having had to disclose all such positions).
- Finally, while the Commission's guidance regarding group formation in and of itself does not represent a paradigm shift, the attention placed on this area by the Commission makes it clear that interactions between activist funds – sometimes in practice performed intentionally casually by such funds – can still trigger group formation. The Commission is poised to scrutinize 'wolf packs' of multiple activists who can suddenly take near-concurrent positions in a given company while denying purported coordination that would in turn require formal recognition of the formation of a group.

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Separate from ‘pure play’ activist hedge funds, the changes could also alter the landscape for potential acquirers who use a minority stake as a foothold in an acquisition strategy – albeit a complex strategy with the interplay of shareholder rights plans and other factors. Such investors may start as a ‘passive investor’ who must flip from Schedule 13G to Schedule 13D if they develop ‘control intent’ with respect to a given company. Investors who hold equity stakes from 5%-19.9% qualify for the ‘short form’ Schedule 13G so long as they are ‘passive’ and do not have ‘control intent’ through actions such as advocating for board changes or a change of control process/acquisition intent. If a ‘passive investor’ develops ‘control intent’ and seeks to consummate an acquisition transaction with the company – the new timeline reduces the amount of time to proceed from developing control intent to inking an acquisition contract before required public disclosure of intent on a Schedule 13D.

The following Gibson Dunn attorneys assisted in preparing this update: James J. Moloney, Ed Batts, Jeffrey L. Steiner, David Korvin, Lexi Hart, Chris Connelly, and Nicholas Whetstone.

Gibson Dunn lawyers are available to assist in addressing any questions you may have about these developments. To learn more about these issues, please contact the Gibson Dunn lawyer with whom you usually work, the authors, or any of the following leaders and members of the firm’s Securities Regulation and Corporate Governance, Capital Markets, Derivatives, or Mergers and Acquisitions practice groups:

Securities Regulation and Corporate Governance Group: Elizabeth Ising – Washington, D.C. (+1 202-955-8287, eising@gibsondunn.com) James J. Moloney – Orange County (+1 949-451-4343, jmoloney@gibsondunn.com) Lori Zyskowski – New York (+1 212-351-2309, lzyskowski@gibsondunn.com) Brian J. Lane – Washington, D.C. (+1 202-887-3646, blane@gibsondunn.com) Ronald O. Mueller – Washington, D.C. (+1 202-955-8671, rmueller@gibsondunn.com) Thomas J. Kim – Washington, D.C. (+1 202-887-3550, tkim@gibsondunn.com) Michael A. Titera – Orange County (+1 949-451-4365, mtitera@gibsondunn.com) Aaron Briggs – San Francisco (+1 415-393-8297, abriggs@gibsondunn.com) Julia Lapitskaya – New York (+1 212-351-2354, jlapitskaya@gibsondunn.com)

Capital Markets Group: Andrew L. Fabens – New York (+1 212-351-4034, afabens@gibsondunn.com) Hillary H. Holmes – Houston (+1 346-718-6602, hholmes@gibsondunn.com) Stewart L. McDowell – San Francisco (+1 415-393-8322, smcdowell@gibsondunn.com) Peter W. Wardle – Los Angeles (+1 213-229-7242, pwardle@gibsondunn.com)

Derivatives Group: Jeffrey L. Steiner – Washington, D.C. (+1 202-887-3632, jsteiner@gibsondunn.com) Darius Mehraban – New York (+1 212-351-2428, dmehraban@gibsondunn.com) Adam Lapidus – New York (+1 212-351-3869, alapidus@gibsondunn.com)

Mergers and Acquisitions Group: Ed Batts – Palo Alto (+1 650-849-5392, ebatts@gibsondunn.com) Robert B. Little – Dallas (+1 214-698-3260, rlittle@gibsondunn.com) Saee Muzumdar – New York (+1 212-351-3966, smuzumdar@gibsondunn.com)

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