FENWICK

Securities Law Update

Securities Law Update—August 29

Welcome to the latest edition of Fenwick's Securities Law Update. This edition contains updates and reminders on:

- The federal court decision that struck down the FTC's noncompete ban, blocking it from taking effect nationwide on September 4
- New filing deadlines for Schedule 13G, which become effective on September 30
- New increases to SEC registration fees that become effective October 1
- A recent push by the Investor Coalition for Equal Votes (ICEV) discouraging private companies from having a dual-class structure when they go public

Rules and Regulations

- **New filing deadlines for Schedule 13G become effective on September 30.** In October 2023, the SEC adopted new rules governing beneficial ownership reporting, including accelerating the filing deadlines for Schedule 13G and extending the filing day deadline. See Fenwick's alert for more details on new SEC rules and deadlines for share ownership reporting.

  Note that amended 13G filings must be filed by *10 p.m. EST on Thursday, November 14* to report material changes since the filer's last 13G filing.

New Schedule 13G

Initial Filing Deadline	QIIs & Exempt Investors: 45 days after calendar quarter end in which beneficial ownership exceeds 5%. *Rules 13d-1(b) and (d)* QIIs: Five business days after month-end in which beneficial ownership exceeds 10%. *Rule 13d-1(b)* Passive Investors: Within five business days after acquiring beneficial ownership of more than 5%. *Rule 13d-1(c)*
Amendment Triggering Event	All Schedule 13G Filers: Material change in the information previously reported on Schedule 13G. *Rule 13d-2(b)* QIIs & Passive Investors: Same as current Schedule 13G—upon exceeding 10% beneficial ownership or a 5% increase or decrease in beneficial ownership. *Rules 13d-2(c) and (d)*

New Schedule 13G

Amendment Filing Deadline	All Schedule 13G Filers: 45 days after calendar quarter-end in which a material change occurred. *Rule 13d-2(b)* QIIs: Five business days after month-end in which beneficial ownership exceeds 10% or a 5% increase or decrease in beneficial ownership. *Rule 13d-2(c)* Passive Investors: Two business days after exceeding 10% beneficial ownership or a 5% increase or decrease in beneficial ownership. *Rule 13d-2(d)*
EDGAR Filing "Cut-Off" Time	All Schedule 13G Filers: 10 p.m. EST. *Rule 13(a)(4) of Regulation S-T*

A QII (Qualified Institutional Investor) files its Schedule 13G under Rule 13d-1(b).
An "Exempt Investor" files a Schedule 13G under Rule 13d-1(d).
A "Passive Investor" files a Schedule 13G under Rule 13d-1(c).

The SEC continues to closely monitor the implementation of the new beneficial ownership rule. The SEC has already issued several comment letters about the timing of Schedule 13D filings (for example, see here) and recently charged Carl Icahn for failing to file required amendments to his Schedule 13D.

Beyond technical compliance, legal counsel should also inform their management and investor relations team about these new deadlines. Public information about stockholders' holdings will now be available sooner. As result, investor relations may want to review these filings so they can track changes in the company's shareholder base and prepare for any questions, particularly before earnings. The accelerated deadlines can also help investor relations monitor which investors are increasing their ownership stake and target outreach efforts.

- **Effective October 1, the SEC will increase the registration fee rate from $147.60 per million dollars to $153.10 per million dollars.** Remember to use the new rate when calculating the fees for registration statement filing on or after October 1.

- **Form 4: Code J transactions under scrutiny.** The *Harvard Business Law Review* recently published an article entitled "Insider Trading by Other Means" by an influential research group, which asserts that using the "J" (other) code in a Form 4 is highly correlated with dispositions based on material non-public information (i.e., insider trading). The authors argue that "insiders conceal their suspicious trades by publicly reporting them (as they are required to do) in ways that confuse or discourage investigators," such as using code J for "other" transactions. The authors call on the SEC and investigators to prioritize the review of J-coded transactions over ordinary sales transactions in Form 4 filings.

  In light of the SEC's recent focus on insider trading and data analytics, the agency may take note of this article and begin scrutinizing J-coded transactions more closely. Accordingly, companies should carefully review any Form 4 filings with code J transactions and ensure that the filings include the required explanatory footnotes about the transaction. Deficient filings are likely to raise red flags. See Insider Trading: Watch Your Form 4 Transaction Codes (*theCorporateCounsel.net*, August 2024) and There's Something Fishy About Insiders' 'Other' Trades (*Bloomberg*, August 2024, subscription required).

- **Nasdaq proposes to accelerate the delisting process for companies with "penny stocks."** Nasdaq has proposed changes to Listing Rules 5810 and 5815 to provide that a company will be suspended from trading if the company has been non-compliant with the $1.00 bid price requirement for more than 360 days. Further, under the proposed changes, Nasdaq would immediately send a Delisting Determination, without any compliance period, to any company that becomes non-compliant with the $1.00 minimum bid price requirement if the company effected a reverse stock split within the past year. See Nasdaq Has Hundreds of Penny Stocks. Now It's Trying to Purge Them (*the Wall Street Journal*, August 2024, subscription required).

- **The SEC approved several Public Company Accounting Oversight Board rule changes addressing auditors' general responsibilities in conducting an audit, the use of technology assisted data analysis in audits, and auditor liability.** See SEC Signs Off on PCAOB Rule Changes (*theCorporateCounsel.net*, August 2024).

  PCAOB and the SEC enforcement actions against auditors have also continued to increase. The agencies appear to be focusing on systems of quality control, independence, and ethics both in recent rulemaking and enforcement actions. See Heightened PCAOB and SEC Enforcement Against Auditors Continues in H1 2024, According to Brattle Report (*Morningstar*, August 2024).

Relevant Litigation and Enforcement Actions

- **A Texas federal district court struck down the FTC's noncompete ban on August 20,** blocking it from taking effect nationwide on September 4. While the court's decision is subject to appeal, it is unlikely that any appeal will be ruled upon before September 4. In the meantime, state law will continue to govern the enforceability of noncompetes. Learn more in our alert about the court setting aside the FTC's noncompete ban.

  In light of this decision, companies are no longer required to send notices of prohibited noncompetes to their workers by September 4.

- **The SEC filed its brief in support of its controversial climate disclosure rules on August 6.** In the SEC's brief, the agency argues it has express statutory authority from Congress to adopt the climate disclosure rules, that it acted reasonably in adopting such rules and satisfied the Administrative Procedures Act's procedural requirements, and that the First Amendment does not prohibit the climate disclosure rules. Get the details in Fenwick's client alert on the SEC's brief in support of climate rules.
  While the future of the SEC's climate rules remains uncertain, companies should prepare themselves for climate disclosure more generally.
- **The SEC and SolarWinds are in settlement negotiations after a New York federal court dismissed the majority of the SEC's fraud claims.** A New York federal court has dismissed most of the securities fraud claims brought by the SEC against SolarWinds and its chief information security officer regarding its cybersecurity risk disclosures reporting a large-scale cybersecurity hack. However, the court allowed the case to proceed against both SolarWinds and the CISO regarding a detailed statement SolarWinds about its cybersecurity practices posted on its website, with the court ruling it could be actionable under the securities laws even though it was directed at "customers" rather than investors as the statement remained available to the public post-IPO. See Fenwick's client alert for more on SEC v. Solarwinds and the dismissal. Since then, the SEC and SolarWinds have begun settlement negotiations over the remaining claim. See SEC, SolarWinds In Settlement Talks After Cyber Suit Trimmed (*Law360*, August 2024, subscription required).
- **The SEC announced charges against Carl Icahn and his publicly traded company, Icahn Enterprises L.P. (IEP), for failing to disclose Icahn's pledges of IEP securities as collateral for personal margin loans.** IEP allegedly failed to disclose Icahn's pledges of IEP securities as required by Item 403(b) and (c) of Regulation S-K. For his part, the SEC says Icahn failed to file amendments to Schedule 13D describing his personal margin loan agreements and amendments and failed to attach required agreements. IEP and Icahn agreed to pay $1.5 million and $500,000 in civil penalties, respectively, to settle the SEC's charges.
  In light of this enforcement action, companies should consider reviewing their controls and procedures for margin loans and pledges.
- ***Jarkesy* decision invoked against other agencies' administrative proceedings.** As you may recall, the U.S. Supreme Court held in *SEC v. Jarkesy* that defendants are entitled to jury trials when the SEC seeks civil penalties for securities fraud, limiting the SEC's use of administrative proceedings. Since then, defendants have begun invoking the *Jarkesy* decision to enjoin other agencies' administrative proceedings, including the U.S. Department of Labor, PCAOB and the Financial Industry Regulatory Authority (FINRA).

Since FINRA has no private right of action under the federal securities laws, the agency can only litigate cases involving federal securities fraud in its own administrative proceedings. If a court applies the *Jarkesy* decision to FINRA, the agency will likely have to refer such cases to the SEC going forward, which would increase the SEC's caseload. See SEC and FINRA Face New Limits on Enforcement powers in Post-Chevron Landscape (*Reuters*, July 2024).

- **The SEC and DOJ are targeting "short-and-distort" schemes.** These schemes involve an investor shorting a public company's stock and then spreading misinformation about the company to drive down the company's stock price so the investor can realize a profit on the short. These schemes can impact a company's market value and reputation, even if the information is later proven false. As part of a broader effort, the SEC and DOJ recently charged an investor and his research company with securities fraud for allegedly spreading misinformation about companies on social media to manipulate the markets for his own profit. See Why The SEC Is Targeting Short-And-Distort Schemes (*Law360*, August 2024, subscription required).

Stockholder Activism

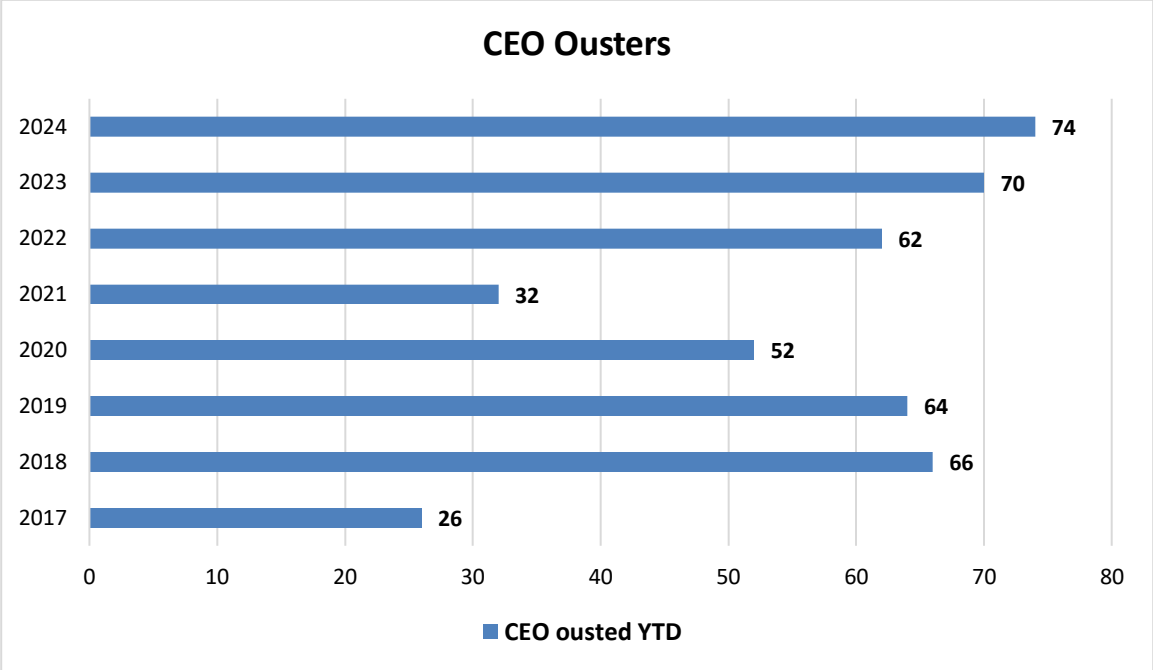
- **Investor Coalition for Equal Votes (ICEV) targets dual-class structures.** Recently, ICEV has been sending letters to private companies requesting a meeting to discuss dual-class voting structures and their impact on corporate governance. In the letter, ICEV discourages private companies from having a dual-class structure when they go public. However, if a company does go public with such structure, ICEV expects the company to have a time-based sunset provision of seven years or less. ICEV's outreach appears to target late-stage private companies broadly regardless of their current capital structure.
  According to the letter, ICEV members have approximately $3 trillion assets under management. Members appear to largely include the Council of Institutional Investors (CII) and its members, such as the California State Teachers Retirement System (CalSTRS), Office of the New York City Comptroller, and Washington State Investment Board.
- **CalSTRS votes against director for inadequate climate risk disclosure.** During the 2024 proxy season, CalSTRS voted against the boards of directors at a record 2,258 companies due to inadequate climate risk disclosure. The pension fund has emphasized that it expects all portfolio companies to provide Task Force on Climate-related Financial Disclosures-aligned and Scopes 1 and 2 GHG emissions disclosure. See CalSTRS Stresses Climate Disclosure with 2024 Proxy Season Votes (*CalSTRS*, August 2024).
- **New York State Common Retirement Fund calls on companies to make corporate political spending disclosure.** After negotiating with the fund, Caesars Entertainment Inc., DoorDash Inc., and SoFi Technologies agreed to publicly disclose their political spending. During the 2024 proxy season, the fund's political spending proposals at Charter Communications Inc., Airbnb Inc., and DraftKings also won significant support from shareholders.
  According to the Office of the New York Comptroller, "the fund has filed 185 political spending and lobbying disclosure shareholder proposals, securing 64 agreements, achieving 108 votes, and withdrawing 13 proposals for other reasons since 2011." See State Comptroller DiNapoli Details Progress on Corporate Political Spending Disclosure (*Office of the New York State Comptroller*, August 2024).

- **Elliot Investment Management seeks to supplant Southwest Airlines' board of directors and executive leadership.** Elliot has nominated 10 director candidates for the company's 15-member board and called for replacing the current CEO and board chair. In response to Elliot, Southwest has adopted a poison pill to discourage Elliot from increasing its 8.2% ownership in the company. See Southwest Backs CEO as Activist Elliot Seeks Board Overhaul (*Bloomberg Law*, August 2024, subscription).

- **Record number of CEO ousters in 2024.** According to Exechange, 74 chief executive officers have been fired or forced out this year, which is the highest number since 2017. "CEOs who do not perform well in the rapidly changing market environment are now apparently being replaced very rigorously," Exechange founder Daniel Schauber recently told *Bloomberg Law*

(subscription required). For example, the CEO of Starbucks recently resigned after two quarters of declining sales and mounting pressure from activist investors Elliott Investment Management and Starboard Value.

CEO transitions are a decisive moment for companies. As companies prepare for annual board evaluations this year, they may want to consider whether the board is effectively addressing CEO succession planning. The CEO succession planning process should address not only expected transitions, such as retirement, but also unexpected events, such as death, illness, or an untimely departure.



Data as of August 13 of each year *Source: exechange.com, Bloomberg Law*

Notable Resources and News

- Audit Committee Oversight in the Age of Generative AI (*CAQ*, July 2024)
- The Chief AI Officer (*MyLogIQ*, July 2024)
- Recent Trends in Securities Class Action Litigation: 2024 H1 Update (*NERA*, August 2024)