Proskauer

SEC Adopts New Short Sale Disclosure Rule

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Applies Broadly to A Wide Range of Equities

Compliance Delayed One Year to Permit Fund Systems Updates

On October 13, 2023, the Securities and Exchange Commission adopted new Rule 13f-2 to require monthly reporting of short sale positions and activity data on new Form SHO by institutional investment managers. The new rules require monthly reporting on new Form SHO of activity related to a broad spectrum of "equity securities." An investment manager must report on activity and positions where it has investment discretion, subject to thresholds described below. The SEC also amended the CAT NMS Plan to supplement the reporting requirements for covered firms.

What investment managers are covered by Rule 13f-2?

The "institutional investment managers" to which the new rules apply is the same group as are subject to Form 13F, without the additional element for purposes of Form 13F that the manager have $100 million or more under management. The term is defined under the Exchange Act to mean any person, other than a natural person, investing in or buying and selling securities for its own account and any person exercising investment discretion with respect to the account of any other person.

Because Rule 13f-2 and new Form SHO are not limited by the $100 million threshold that triggers Form 13F filing obligations, they will pick up many new investment managers that have not traditionally been required to report their short or long positions with the SEC, including many based outside of the U.S.

What securities are covered by Rule 13f-2?

The scope of “equity securities” to which the new rules apply is broad and generally tracks the applicability to Regulation SHO, covering securities as well as convertible instruments, ADRs and ETFs. By contrast, while Form 13F focuses on “equity securities,” the scope of reportable securities is limited to those on the “13F List,” which the SEC updates quarterly. The new rule also applies to both exchange-listed and other securities issued by public companies, as well as to equity securities issued by non-public companies, such as those that might be traded over-the-counter.

What are the reporting thresholds under Rule 13f-2 and new Form SHO?

A covered investment manager will be required to report on Form SHO all short activity related to public company equity securities if the manager has a monthly average gross short position in such stock at the close of regular trading hours equal to or greater than $10 million, or, as a percentage of shares outstanding, equal to or greater than 2.5%. For private company equity securities, the threshold is a gross short position with a dollar value of $500,000 or more at the close of regular trading hours on any settlement date during the month. Economic short positions created through the use of swaps or other derivatives do not need to be included when calculating the reporting thresholds.

What information is required in Form SHO?

For each reported equity security, a covered investment manager will report all Form SHO information, including the following:

- The investment manager’s end-of-month gross short position in the equity security at the close of regular trading hours on the last settlement date of the calendar month; and
- For each individual settlement date during the month, the manager’s “net” activity in the reported equity security.

Will the information in Form SHO become public?

Form SHO will be filed with the SEC within 14 calendar days of each month end, but the information in individually-filed forms will not be available to the public, except perhaps pursuant to a FOIA request. However, the SEC will publish aggregated data for each equity security. The SEC expects that it will make public aggregated information derived from data reported on Form SHO within one month after the end of the reporting calendar month.

The Amendment to the CAT NMS Plan

The SEC also amended the CAT NMS Plan to require CAT reporting firms (broker-dealers) to report for short sales whether they are relying on the *bona fide* market making exception in Rule 203(b)(2)(iii) of Regulation SHO.

What were the changes from the proposing release?

The SEC made several key changes to the final rules from what had been proposed in response to comments received. In particular, the SEC did not adopt proposed Rule 205 which would have required broker-dealers to mark purchase orders as "buy to cover" when purchasing to cover short positions, removed the proposed requirements for Form SHO to report positions as "fully hedged," "partially hedged," or "not hedged," and did not adopt the proposed requirement for investment managers to separately notify the SEC when certain information required an amendment to their Form SHO.

Compliance Dates

The new rules relating to Form SHO and the amendment to the CAT NMS Plan will be effective 60 days after publication in the Federal Register, although the obligation to comply with new Rule 13f-2 and file the new Form SHO will be delayed for 12 months following the effective date. The SEC will begin to publish aggregated short sale data three months following the delayed compliance date. The amendment to the CAT NME Plan has a compliance date of 18 months following the effective date of the rules.

What Affected Firms Should Do Now

Although compliance is delayed for more than 12 months from the date of the SEC's adoption release, firms should begin now to ensure that their systems are up-to-date to compile the required information within the required timeframes in a manner that minimizes the burden of reporting monthly and to monitor on a daily basis whether their "gross short position" exceeds the identified thresholds. Firms should also think about how the SEC's publication of aggregated short sale data may impact their investment strategies in either a positive or negative manner, or may impact general market behavior. Please feel free to contact us for more information.

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