

**MEMO# 24311**

May 21, 2010

## **SEC Proposes Large Trader Reporting Requirements**

[24311]

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TO: CLOSED-END INVESTMENT COMPANY COMMITTEE No. 9-10  
ETF (EXCHANGE-TRADED FUNDS) COMMITTEE No. 10-10  
ETF ADVISORY COMMITTEE No. 18-10  
EQUITY MARKETS ADVISORY COMMITTEE No. 16-10  
SEC RULES COMMITTEE No. 20-10 RE: SEC PROPOSES LARGE TRADER REPORTING REQUIREMENTS

The Securities and Exchange Commission has issued a proposal that would require: (1) certain large-volume, high-frequency traders (“large traders”) to self-identify to the SEC (i.e., register) and (2) broker-dealers that effect transactions for large trader customers to maintain and produce records of these customers’ trades to the SEC. [\[1\]](#) According to the Release, the proposal is intended to bolster the SEC’s regulatory and enforcement capabilities by increasing its ability to reliably identify large traders and their affiliates, obtain far more promptly trading data on the activity of large traders, including execution time, and aggregate and analyze trading data among affiliated large traders. Comments on the proposal are due to the SEC no later than June 22, 2010.

We will hold a conference call on Tuesday, May 25, at 3:00 p.m. Eastern time to discuss the Institute’s comments relating to the SEC’s proposal. If you plan to participate on the call, please contact Ruth Tadesse by email at [rtadesse@ici.org](mailto:rtadesse@ici.org) or by phone at 202-326-5836 to receive the dial-in information.

## **I. Large Trader**

Under the proposal, a large trader would be defined as any person [\[2\]](#) who, directly or indirectly (including through other persons controlled by such person), exercises investment discretion over one or more accounts and effects transactions in U.S. exchange-listed stocks and options for those accounts by or through one or more registered broker-dealers that, in the aggregate, exceed either (1) \$20 million or 2 million shares per day, or (2) \$200 million or 20 million shares per month. The value of purchases and sales of stocks and options [\[3\]](#) would be aggregated without netting or offsetting, although certain transactions would be exempt under the proposal. [\[4\]](#)

In complex organizations, parent companies would be deemed large traders if, in the aggregate, their subsidiaries meet the daily or monthly transaction thresholds – even if the parent company itself does not trade securities. In the Release, the SEC stated its intention to reduce the number of registrations by focusing on the parent company of the entities that employ or otherwise control the individuals that exercise investment discretion. Accordingly, a parent company generally would register on behalf of itself and each of its large trader subsidiaries. If each controlled person that is a large trader registered individually, however, the parent company would not need to register itself unless it is separately a large trader. [\[5\]](#) Mere ownership of accounts without investment discretion (e.g., trusts, custodians, or nominees) would not trigger large trader status.

Large traders would include advisers to funds, pension plans, insurance companies, and other institutional investors. In the case of a registered investment adviser that acts as the adviser to several registered funds, even if each fund is managed by one natural person that would meet the applicable large trader threshold, the proposal would require that the investment adviser register with the SEC as a large trader but not the individual fund manager. According to the Release, the investment company would not directly or indirectly exercise investment discretion over one or more accounts.

Traders whom broker-dealers believe to be large traders but who do not register with the SEC would be deemed Unidentified Large Traders.

## **II. Requirements for Large Traders**

Large traders would be required to identify themselves to the SEC by promptly filing Form 13H after first effecting transactions that reach the identifying activity level. [\[6\]](#) Thereafter, they would be required to update the Form 13H annually, within 45 days of the calendar year-end, and to amend the Form 13H promptly following the end of each calendar quarter if any information contained in the previously filed Form 13H had become inaccurate. Large traders also would be required to provide additional information to the SEC, upon request, to assist the SEC in further identifying the large trader and its accounts.

Upon registration with the SEC, a large trader would receive a unique Large Trader Identification Number ("LTID"). The large trader would be required to disclose its LTID to every registered broker-dealer that effects transactions on its behalf and identify each account held by that broker-dealer through which the large trader trades. The proposal also would require a large trader to disclose its LTID to others with whom it collectively exercises investment discretion.

A large trader could file for inactive or terminated status if its aggregate transactions during the previous full calendar year did not reach the identifying activity level or it had ceased operations.

Form 13H would require a large trader to disclose the following information:

- Information about its business and organization;
- Whether any of its affiliates file forms with the SEC and if so, which forms;
- Whether it or its affiliates are registered, as traders or otherwise, under the Commodities Exchange Act, or are a bank holding company, bank, savings bank or association, credit union, foreign bank, or insurance company;
- The names and LTID of any affiliates that are large traders;
- The names of any general partners or limited partners that own more than 10 percent of the accounts of the large trader;
- The names of any officers, directors or trustees of the large trader;
- The jurisdiction(s) in which the large trader is organized and maintains its principal place of business; and
- For each account over which the large trader exercises investment discretion
  - The name of broker-dealer that holds the account;
  - The account number;
  - The name of the account; and
  - The identification number of any other large trader that exercise discretion over the account.

### **III. Requirements for Registered Broker-Dealers**

The proposal would impose recordkeeping and reporting requirements on registered broker-dealers for transactions effected for large traders and Unidentified Large Traders. Specifically, broker-dealers would be required to maintain the following records for any transaction in excess of 100 shares of exchange-listed securities or options effected directly or indirectly through a large trader or Unidentified Large Trader's account:

- The transaction date and price;
- Account number;
- Identifying symbol of the security (i.e., ticker symbol);
- Number of shares or options contracts traded and type of transaction;
- Clearing house number;
- Whether the transaction was proprietary or agency;
- Name of exchange or market where transaction was effected;
- Execution time;

- LTIDs associated with the account;
- Prime broker identifier, if any;
- Average price account identifier, if any; and
- Identification assigned by depository institution, if applicable.

Broker-dealers would be required to have records available the day after a transaction is effected. [7] Upon request from the SEC, a registered broker-dealer would have to provide information to the SEC by the close of business on the same day as the request.

Under the proposal, broker-dealers also would be tasked with maintaining systems and procedures to assure compliance with the identification requirements in the proposal. However, the proposal would include a safe harbor from the recordkeeping and reporting obligations with respect to Unidentified Large Traders if a broker-dealer (1) does not have actual knowledge that an entity is a large trader, and (2) has established policies and procedures reasonably designed to detect and identify Unidentified Large Traders. If a broker-dealer's safe harbor policies and procedures detect an Unidentified Large Trader, the broker-dealer would be required to inform the trader of its obligation to register as a large trader with the SEC.

#### *Foreign Entities*

Foreign entities that trade on U.S. exchanges would be classified as large traders if they meet the applicable daily or monthly thresholds in the proposal. Registered broker-dealers, therefore, would be obligated to monitor foreign customer transactions for qualification as large traders and also maintain records for foreign entities that either self-report as large traders or are Unidentified Large Traders.

#### **IV. Confidentially**

According to the Release, the information provided to the SEC by large traders and broker-dealers under the proposal would be required to be treated confidentially and would be exempt from disclosure under the Freedom of Information Act.

#### **V. Implementation**

The large trader self-identification requirements would become effective three months after adoption of a final rule by the SEC. The broker-dealer recordkeeping and reporting requirements would become effective after six months.

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## endnotes

[1] See SEC Release No. 61908 (April 14, 2010), 75 FR 21456 (April 23, 2010) (“Release”), available at <http://www.sec.gov/rules/proposed/2010/34-61908.pdf>.

[2] Under the proposal, “person” would include, among other things, two or more persons acting together for the purpose of trading, acquiring, holding, or disposing of exchange-listed stocks and options. The term also would include any person that directly or indirectly has the right to vote or direct the vote of 25 percent or more of a class of voting securities of an entity or has the power to sell or direct the sale of 25 percent or more of a class of voting securities of such entity, or in the case of a partnership, has the right to receive, upon dissolution, or has contributed, 25 percent or more of the capital.

[3] With respect to options, only purchases and sales, and not exercises, would be counted.

[4] Exempt transactions would include: bookkeeping entries memorializing the settlement of transactions; offerings by or on behalf of an issuer; gifts; distributions of estates; transactions ordered by a court; rollover of a retirement plan; and transactions pursuant to an issuer benefit plan.

[5] The SEC noted in the Release that it would design the large trader reporting system to accommodate those large traders that wish to voluntarily identify with more granularity the subsidiary, trading desk, or other unit that is directly exercising investment discretion over the account.

[6] The proposal would prohibit a person from disaggregating accounts and splitting activity among multiple broker-dealers or transactions in an attempt to evade the proposed self-identification and other large trader requirements.

[7] Broker-dealers would be required to retain the records for three years.