

**MEMO# 34059**

March 5, 2022

# SEC Proposes Short Sale Disclosure Rule for Institutional Investment Managers

[34059]

March 4, 2022

TO: Equity Markets Advisory Committee

ETF (Exchange-Traded Funds) Committee RE: SEC Proposes Short Sale Disclosure Rule for Institutional Investment Managers

On February 25, the SEC proposed new Rule 13f-2 to require institutional investment managers<sup>[1]</sup> ("managers") to report certain gross short position and related activity data for equity securities on a monthly basis through a new confidential Form SHO.<sup>[2]</sup> The proposed rule is intended to implement Section 929X of the Dodd-Frank Act, which authorizes the SEC to prescribe rules for short sale disclosure on, at a minimum, a monthly basis.<sup>[3]</sup> As described further below, the SEC plans to publish only aggregated data for each equity security derived from the filings.

Comments are due on the later of 30 days after publication in the Federal Register or April 26. We will hold a Zoom member call on **Tuesday, March 15 at 3:00 p.m. ET** to discuss the proposal.

The SEC states that the information collected would supplement short sale data that is already reported and publicly available, with the specific goal of overcoming the data limitations exposed during the January 2021 market volatility.<sup>[4]</sup> In its view, additional transparency would benefit market participants by promoting greater risk management, market confidence, and capital formation. Importantly, the SEC also believes that the data would provide more insight into the lifecycle of a short sale and, thus, enhance its oversight over potential abusive or manipulative schemes. While the SEC recognizes that more transparency could erode the benefits of short selling, it believes that the proposal strikes an "appropriate balance" with adequate protections.

## Reporting Thresholds

Managers would be required to file a Form SHO report based on the following thresholds below. The SEC calculated these thresholds by using data that it received from Form SH data collected under Rule 10a-3T from October 2008 to July 2009 following the 2008 financial crisis, as well as from various rulemaking petitions and comment letters that it has received since the adoption of Section 929X.

- For any equity security of an issuer registered under Section 12 or subject to Section 15(d) of the Exchange Act (a "reporting company issuer"), a position that meets or exceeds either (i) a gross short position in the equity security with a US dollar value of \$10 million<sup>[5]</sup> or more at the close of regular trading hours on any settlement date during the calendar month; or (ii) a monthly average gross short position as a percentage of shares outstanding in the equity security of 2.5 percent<sup>[6]</sup> or more;<sup>[7]</sup> or
- For any equity security of an issuer that is not a reporting company issuer, a position that meets or exceeds a gross short position in the equity security with a value of \$500,000<sup>[8]</sup> or more at the close of trading hours on any settlement date during the calendar month.<sup>[9]</sup>

Given that Rule 13f-2 would apply to institutional investment managers as defined under Section 13(f) of the Exchange Act, the manager would be required to determine if it meets these thresholds and report a position that is aggregated across accounts over which the manager, or any person under the manager's control, has investment discretion.<sup>[10]</sup>

### **Form SHO Short Position and Daily Activity Information**

A manager would be required to report certain basic information that identifies the reporting manager and the applicable calendar month. To avoid duplicative reporting, the proposed rule adopts a similar approach to Form 13F reporting, such that only one manager must report the information if there are multiple managers that exercise investment discretion with respect to the same securities.<sup>[11]</sup> Managers would be required to file Form SHO with the SEC within 14 calendar days after the end of the calendar month that is the reporting period.<sup>[12]</sup>

A Form SHO filing must also include two categories of information: gross short position (Information Table 1) and daily activity that affects the gross short position during the reporting period (Information Table 2). With respect to the gross short position, the manager must identify the issuer and the security, the number of shares held short (without including any offsetting economic positions (including shares long of the equity security or derivative positions of the security)) at the close of the last settlement date of the calendar month of the reporting period; the US dollar value; and whether the position is fully hedged, partially hedged, or not hedged.<sup>[13]</sup>

With respect to daily activity, the manager must report information for each settlement date during the calendar month of the reporting period, including the number of shares of the security sold short and the number of shares purchased to cover an existing short position (in whole or in part).<sup>[14]</sup> Further, the manager must report information on whether, how, and when reported gross short positions are being reduced, closed out, created or increased due to the acquisition or sale of shares resulting from call option exercises or assignments; put option exercises or assignment; tendered conversations; secondary offering transactions; and other activity.

### **Form SHO Information on ETFs and Diversified Portfolio Products**

The SEC emphasizes that the required information to be reported in Form SHO on gross short positions and daily activity also applies to ETFs.<sup>[15]</sup> However, for purposes of calculating gross short positions for individual equity securities, a manager would not be required to consider short positions that an ETF holds in those individual underlying equity securities that are part of the ETF basket. The SEC further asks whether there are other diversified portfolio products in addition to ETFs that should be included, and whether a manager should be required to consider short positions in individual underlying securities of

the product's basket of assets.[\[16\]](#)

## **SEC Publication of Aggregated Data**

The SEC would publish aggregated information derived from Form SHO filings for each reported equity security (including the issuer's name and related identifiers) across all reporting managers; it estimates that it would do so within one month after the end of the reporting calendar month.

Specifically with respect to gross short positions, the SEC would publish (i) the aggregated number of total shares at the close of the last settlement date of the calendar month and the corresponding US dollar value; and (ii) a summary of the managers' reported hedging information, i.e., the percentages of the aggregate gross short position that is reported as being fully hedged, partially hedged, or not hedged.

With respect to daily activity, the SEC would publish the "net" activity in the equity security aggregated across all reporting managers for each individual settlement date within a reporting period calendar month, which would be determined by offsetting the purchase and sale activity reported in Form SHO.[\[17\]](#)

However, the SEC seeks comment on an alternative approach to reporting aggregated information. Under the alternative approach, the information on Form SHO would not be aggregated with information from other managers. Rather, the information would be published as reported on Form SHO, albeit without any information that would identify the reporting manager.

## **Amendments to Form SHO**

Amendments to a Form SHO to correct errors would need to be filed within 10 calendar days of discovery of the error and restate the form in its entirety, with a written description of the revision being made, the reason for the revision, and an indication of whether data from any additional prior reporting periods up to the past 12 calendar months are affected by the amendment. If there are other affected reporting calendar months, then the manager would need to complete and file a separate filing for each affected month.

If a revision represents a data point that is being amended by 25% or more, then the manager would need to notify SEC staff in the Division of Trading and Markets within 2 business days after submitting the updated filing. The SEC views this as a significant change, particularly for securities with few managers reporting short data.[\[18\]](#) Further, if the data being reported leads to multiple prior filings, then the manager would need to notify SEC staff and provide an explanation for the revision. The SEC believes that doing so would help staff determine if there is a data integrity issue with that manager.

## **"Buy to Cover" Order Marking Requirement**

The SEC is also proposing new Rule 205 under Regulation SHO to establish a new "buy to cover" order marking requirement for certain purchase orders effected by a broker-dealer for its own account or the account of another person at the broker-dealer. This marking would be required if, at the time of order entry, the purchaser has a gross short position in such equity security in the specific account for which the purchase is being made at the broker-dealer.[\[19\]](#)

## **Amendments to CAT**

The proposed rule would also require amendments to the CAT NMS Plan to require broker-dealers to report whether a buy order for an equity security is a "buy to cover" order

pursuant to proposed Rule 205(a) of Regulation SHO. Reporting broker-dealers would be required to identify "buy to cover" orders in order receipt and order origination reports submitted to the CAT Central Repository. According to the SEC, this proposed requirement is similar to but narrower than the originally proposed requirement under the CAT rules that reporting parties report an "open/close indicator" as a "Material Term" on all orders.<sup>[20]</sup>

The proposed rule would also require CAT reporting firms that are reporting short sales to indicate whether the reporting firm is asserting use of the bona fide market making exception under Regulation SHO for the locate requirement in Rule 203 for reported short sales.

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#### endnotes

<sup>[1]</sup> The proposed rule would rely on the definition of "institutional investment manager" under Exchange Act Section 13(f)(6)(A), which includes 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. Rule 13f-1(b) specifies that "investment discretion" is defined under Section 3(a)(35) of the Exchange Act and further specifies that an institutional investment manager also exercises "investment discretion" with respect to all accounts over which any person under its control exercises investment discretion.

<sup>[2]</sup> Short Position and Short Activity Reporting by Institutional Investment Managers ("Short Sale Disclosure Proposal") (Feb. 25, 2022), available at <https://www.sec.gov/rules/proposed/2022/34-94313.pdf>.

<sup>[3]</sup> Section 929X amends Section 13(f) of the Exchange Act to authorize the SEC to "prescribe rules providing for the public disclosure of the name of the issuer and the title, class, CUSIP number, aggregate amount of the number of short sales of each security, and any additional information determined by the [SEC] following the end of the reporting period," providing that "[a]t a minimum, such public disclosure shall occur every month."

<sup>[4]</sup> The SEC notes that currently there are different sources of public and non-public data on short sales from FINRA and registered exchanges. For example, FINRA and some exchanges publish daily aggregate short sale volume data and publish information on transactions with a one-month lag. See FINRA, Daily Short Sale Volume Files, <https://www.finra.org/finra-data/browse-catalog/short-sale-volume-data/daily-short-sale-volume-files>. FINRA also collects and aggregates short interest data for each security twice a month, which is provided to relevant listing exchanges to make available for a fee. For non-listed OTC securities, FINRA publishes aggregated short interest data on its own. Further, the Consolidated Audit Trail provides the SEC with comprehensive information on the lifecycle of a trade (origination, execution, allocation).

<sup>[5]</sup> The SEC expressed the view that the \$10 million threshold would capture managers with substantial short positions, even if such positions are relatively small compared the issuer's market capitalization.

<sup>[6]</sup> The SEC states that this percentage threshold would capture managers with gross short

positions that are large relative to the issuer's size and could therefore have a significant impact on the issuer.

[7] To determine if this threshold is met, a manager would (i) determine its gross short position in the equity security at the close of each settlement date during the calendar month of the reporting period; (ii) divide that figure by the number of shares outstanding of that security at the close of that settlement date; (iii) add up the daily percentages as determined in (ii) and divide that total by the number of settlement dates during the calendar month of the reporting period. The number of shares outstanding would be referenced from an issuer's most recent annual or quarterly report.

[8] The SEC states that a straightforward dollar value would avoid the cost and complexity of locating the total number of shares for a non-reporting company issuer. This dollar figure would capture managers with substantial short positions in a non-reporting company issuer, even if such positions are small relative to the issuer's market capitalization.

[9] To determine if this threshold is met, a manager would determine its end of day gross short position in the equity security on each settlement date during the calendar month and multiply that figure by the closing price at the close of regular trading hours on the settlement date. Where the closing price is not available, the manager would use the price at which it last purchased or sold any share of that security.

[10] See *supra* note 1.

[11] If a manager has information that is subject to reporting and that information is reported by another manager(s), then that manager may designate its Form SHO filing as a notice filing but must identify those other reporting managers. See Special Instruction 5 to Form SHO.

[12] A manager would be able to file Form SHO either through either a fillable web form provided on EDGAR or use its own software to file the form to EDGAR directly.

[13] For a "fully hedged" position, the manager also holds an offsetting position that reduces the risk of price fluctuations for its entire position, e.g., through delta hedging or similar hedging strategies. For a "partially hedged" position, the manager holds an offsetting position that is less than the identified price risk associated with the reported gross short position.

[14] See Information Table 2, Column 8. The SEC states that this information will allow it to quickly identify a short squeeze that reflects market manipulation.

[15] Short Sale Disclosure Proposal at 29.

[16] Short Sale Disclosure Proposal at 54 (Request for Comment #10).

[17] See Form SHO, Information Table 2, Columns 7 through 16.

[18] The SEC would update prior months' aggregated Form SHO data and highlight any updated data that reflects a data point of 25% or greater.

[19] The mark would need to be applied regardless of the size of the purchase order in relation to the size of the gross short position and regardless of whether the gross short position is offset by a long position held in the purchaser's account.

[\[20\]](#) The SEC noted that several commenters objected to this original proposal; one commenter stated that an "open/close indicator" for equities would require significant process changes and involve non-reporting parties, including buy-side participants, OMS/EMS vendors, and others.

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