



ALERT

SEC Adopts Short Reporting Rule for Institutional Investment Managers With Global Scope

November 7, 2023



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On Oct. 13, 2023, the SEC adopted new rule 13f-2 (“Rule 13f-2”) of the Securities Exchange Act of 1934, as amended (“Exchange Act”).¹ Rule 13f-2 requires institutional investment managers to report equity security short positions to the SEC on new Form SHO. Since publishing the proposed rule changes in February 2022,² industry groups and market participants have raised concerns about the broad scope of the proposed rule, the operational expense of compliance and the risks to market quality that might follow, including the potential that proprietary information could be discovered by those who reverse engineer the statistics that the SEC plans to publish.

In spite of these concerns, which were all presented to the SEC, the SEC adopted a rule that imposes significant costs and risks on a broad swath of managers, including US managers with investment discretion over limited assets and foreign managers with limited US jurisdictional ties. Unlike Rule 13f-1, which only imposes a Form 13F filing obligation on institutional investment managers who exercise investment discretion over \$100 million or more in Section 13(f) securities, there is no exclusion under Rule 13f-2 for managers who exercise investment discretion over equity securities below a certain threshold. Additionally, while Section 13(f)(4) of the Exchange Act requires the SEC to make available to the public a list of Section 13(f) securities that can be relied upon by Form 13F filers, institutional investment managers will need to individually assess whether the securities over which they exercise investment discretion qualify as equity securities, as that term is defined under Section 3(a)(11) of the Exchange Act and Rule 3a11–1 thereunder.

To ensure compliance with Rule 13f-2, most institutional investment managers that engage in any form of short selling,³ regardless of whether they will ultimately be required to file Form SHO, will need to adopt procedures to assess whether they exceeded any of the applicable filing thresholds during the prior month. To conduct this assessment, institutional investment managers will first need to categorize their global equity securities positions into Reporting Company Issuers and Non-Reporting Company Issuers and then assess, on a security-by-security basis, whether they exceeded the relevant Rule 13f-2 filing threshold. For Reporting Company Issuers, the filing threshold is the exercise of investment discretion over a monthly average gross short position of \$10 million or more or which constituted 2.5 percent or more of the shares outstanding in the equity security. For Non-Reporting Company Issuers, the filing threshold is the exercise of investment discretion over a gross short position of \$500,000 or more at the close of regular trading hours on any settlement day during the preceding calendar month. Institutional

¹ Exchange Act Release No. 34-98738 (Oct. 13, 2023), available at <https://www.sec.gov/files/rules/final/2023/34-98738.pdf> (“Adopting Release”).

² “SEC Proposes Short Sale Disclosure Rule, Order Marking Requirement, and CAT Amendments,” SEC Press Release, Feb. 25, 2022, available at <https://www.sec.gov/news/press-release/2022-32>.

³ The term “gross short position” in Rule 13f-2 incorporates the definition of short sale under Rule 200(a) of Regulation SHO. Rule 200(a) of Regulation SHO defines a short sale as “any sale of a security which the seller does not own or any sale which is consummated by the delivery of a security borrowed by, or for the account of, the seller.” (emphasis added). As such, even where an institutional investment manager sells securities that they are deemed to own, they still may have a Rule 13f-2 filing obligation if those sales are consummated by the delivery of borrowed securities.



investment managers will have 14 calendar days after the end of a calendar month to perform the necessary computations and submit a Form SHO filing to the SEC. The SEC plans to publish aggregated short position information derived from Form SHO filings approximately 14 days after the filing deadline.

Rule 13f-2 will go into effect on Jan. 2, 2024.⁴ However, compliance with the Rule 13f-2 reporting requirements will not be required until 12 months later, January 2025, with the SEC commencing the publication of aggregated short position data collected under Rule 13f-2 three months later.

Who is Required to File

Like Form 13F, the requirement to file Form SHO applies to institutional investment managers, which are broadly defined under Section 13(f)(6)(A) of the Exchange Act to cover “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.” In the Adopting Release, the SEC notes that the definition is intended to cover “investment advisers exercising investment discretion over client assets, including investment company assets such as mutual funds, ETFs, and closed-end funds; banks and bank trust corporations offering investment management services; pension fund managers; firms, including broker-dealers and insurance companies, managing corporate or employee investment assets; and individuals exercising investment discretion over the accounts of others.”⁵

Notably, the definition of institutional investment manager does not require prospective reporters to primarily operate in the US or impose any minimum standard on the size of the advisory business. Nearly any domestic person or entity investing (other than a natural person investing for their own account) would need to perform the threshold calculations under Rule 13f-2(a)(1) and (2) (detailed below) to determine if a Form SHO filing is required in a given month. For foreign institutional investment managers, the SEC’s jurisdictional analysis in the Adopting Release suggests that “operating in the US securities markets such that the investment manager is subject to filing reports with the Commission,”⁶ is sufficient to require compliance with Rule 13f-2 on the foreign institutional investment manager’s global operations. It is currently unclear whether the SEC intends to limit the application of Rule 13f-2 to just foreign institutional investment managers that are subject to Form 13F filing obligations (managers that exercise investment discretion over \$100 million or more in Section 13(f) securities) or more broadly to any SEC filing obligation. Accordingly, nearly any manager who has investment discretion over an account that may engage in short selling of an equity security — even if those sales occur outside of the US, are not subject to a long/short order marking requirement under SEC Regulation SHO, or typically occur at a de minimis level — will need to adopt an operational process to determine whether any of the monthly average or end-of-day reporting thresholds were triggered in the prior month.

What Securities are in Scope

Rule 13f-2 applies to equity securities, as defined in Section 3(a)(11) of the Exchange Act and Rule 3a11-1 thereunder.⁷ As a general matter, institutional investment managers will be required to perform

⁴ The effective date for Rule 13f-2 is 60 days after the date of publication in the Federal Register, which occurred on Nov. 1, 2023.

⁵ Adopting Release at 175.

⁶ Adopting Release at 36.

⁷ Rule 3a11-1 broadly defines equity security to include “any stock or similar security, certificate of interest or participation in any profit sharing agreement, preorganization certificate or subscription, transferable share, voting trust certificate or certificate of deposit for an equity security, limited partnership interest, interest in a joint venture, or certificate of interest in a business trust; any



the calculations under Rule 13f-2(a)(1) and (2) across any exchange-listed and over-the-counter stock, warrant, convertible debt, ADR and ETF positions. The definition of “equity security” is not limited to securities issued by US issuers or traded on US markets. As discussed in the Adopting Release, the SEC intends Rule 13f-2 to have an extra-territorial effect and require the disclosure of “short selling by Managers of securities of US and non-US issuers ... regardless of where those sales occur.”⁸

Listed options, swaps and certain other derivatives are generally not expected to be directly reportable under Rule 13f-2, however, the SEC notes that certain of these products may meet the definition of an “equity security” and therefore would be directly reportable under the rule. Given the potential confusion, we are optimistic that the SEC staff will provide additional guidance on the application of Rule 13f-2 to securities that may meet the technical definition of equity security under in Section 3(a)(11) of the Exchange Act and Rule 3a11-1 thereunder but are not typically subject to a Regulation SHO order marking requirement prior to the compliance date for the rule.

With respect to ETFs, the instructions to Form SHO are clear that while managers must report the gross short position in the ETF over which they exercise investment discretion on Form SHO, they should not consider short positions that the ETF holds in individual underlying equity securities that are part of the ETF basket when calculating a gross short position in each underlying equity security (that is, the manager’s short position in the ETF and its short positions in any underlying equity security should be considered and, where applicable, reported separately).

Reporting Thresholds

Unlike Rule 13f-1 for Form 13F filers, there is no exclusion under Rule 13f-2 for managers who exercise investment discretion over equity securities below a certain threshold. Each institutional investment manager must determine if it has a reporting obligation on an individual equity security basis by aggregating its gross short exposure in that security and comparing it to the thresholds defined in Rule 13f-2(a)(1) and (2) (“Filing Thresholds”). The term “gross short position” means the number of shares of the equity security that are held short as a result of short sales defined under Rule 200(a) of Regulation SHO, without the inclusion of any offsetting positions. For purposes of the calculations under Rule 13f-2(a)(1) and (2), the institutional investment manager’s calculation is on the basis of the aggregate gross position of the institutional investment manager and all accounts over which the institutional investment manager (or any person under the institutional investment manager’s control) has investment discretion.

Reporting Company Issuers

The Filing Thresholds for reporting gross short positions of an equity security of a reporting company issuer is the lesser of:

- a *monthly average* gross short position at the close of regular trading hours in the equity security with a US dollar value of \$10 million or more, or;

security future on any such security; or any security convertible, with or without consideration into such a security, or carrying any warrant or right to subscribe to or purchase such a security; or any such warrant or right; or any put, call, straddle, or other option or privilege of buying such a security from or selling such a security to another without being bound to do so.”

⁸ Adopting Release at 36.



- a *monthly average* gross short position at the close of regular trading hours as a percentage of shares outstanding in the equity security of 2.5 percent or more.⁹

Non-Reporting Company Issuers

The Filing Thresholds for reporting gross short positions of an equity security of a non-reporting company issuer is:

- a gross short position in the equity security with a US dollar value of \$500,000 or more at the close of regular trading hours *on any settlement date during the calendar month*.

The reporting company issuer Filing Thresholds apply to an equity security: 1) if the class of security is registered pursuant to Section 12 of the Exchange Act; or 2) to any equity security of the issuer if the issuer is required to file reports pursuant to Section 15(d) of the Exchange Act. As a general matter, any security listed on a US stock exchange or any security of an issuer that files periodic reports (e.g., 10-Q, 10-K, 8-K, etc.) would be subject to the reporting company issuer Filing Thresholds. Certain equity securities traded over-the-counter in the US, as well as certain securities of large foreign issuers, may also qualify for the reporting company issuer Filing Thresholds.

Any equity security that is not registered pursuant to Section 12 of the Exchange Act or issued by an issuer subject to the filing requirements under Section 15(d) of the Exchange Act must be treated as a non-reporting company issuer subject to a reporting obligation if the institutional investment manager maintains gross short exposure in the security in excess of \$500,000 at the close of regular trading on any settlement date during the month. Given the extraterritorial effect of Rule 13f-2, this may have significant unintended consequences for institutional investment managers who exercise investment discretion over foreign equity securities or for managers that exercise investment discretion over more complex products or in special situations.

Publication of Aggregate Information

While Form SHO filings will be treated as confidential,¹⁰ the SEC plans to publish aggregated data derived from Form SHO submissions within a month (currently targeted at 28 days) of the end of each reporting period. With regard to Table 1 information (further detailed below), this will be the aggregated gross short position calculated as the number of shares and US dollar notional value reported by all managers for each class of equity security. With regard to Table 2 information (further detailed below), the SEC will publish the aggregate of the net activity reported by all reporting managers for each equity security. In addition to the statistics reflecting the prior month's activity, each month the SEC also plans to publish similar aggregated Form SHO data for the prior 12 months that reflect updated information that accounts for any changes that result from amendments and restatements to Form SHO filings.

⁹ The number of shares outstanding of a security shall be determined by reference to an issuer's most recent annual or quarterly report, and any subsequent update thereto.

¹⁰ The instructions to Form SHO include a notation that all information included in a Form SHO report is deemed subject to a confidential treatment request under 17 CFR 200.83. Based on the Adopting Release, it does not appear that an institutional investment manager would be required to take any additional action to avail itself of the protections under FOIA, section 13(f)(4) through (5), SEC Rule 83, and any other applicable law against disclosure.



Takeaways

The SEC appears not to appreciate the operational complexity and costs associated with the requirements it adopted under Rule 13f-2. By failing to adopt a requirement that the SEC create a list of equity securities subject to the rule, institutional investment managers likely will need to develop complex systems to evaluate their global securities positions across the Filing Thresholds. As there are no current readily available data sources linking individual securities in the US, let alone globally, to the Reporting Company Issuer Filing Thresholds, less sophisticated institutional investment managers may need to evaluate all positions under the Filing Threshold applicable to Non-Reporting Company Issuers and then to determine if the relevant security qualifies as an equity security as defined in Section 3(a)(11) of the Exchange Act (and Rule 3a11-1 thereunder), or if one of the higher Reporting Company Issuer Filing Thresholds applies.

Similar to FINRA's short interest reporting regime, aggregation of securities positions that trade across markets is likely to be challenging (i.e., systematically identifying and aggregating positions in securities that trade in different jurisdictions under different symbols, such as dual-listed securities and the securities of foreign listed companies that trade over-the-counter in the US). For foreign securities that do not trade in the US, determining whether the security meets the definition of an equity security, whether the sale meets the definition of a short sale under Regulation SHO, or whether the security should be evaluated under the Reporting Company Issuer or Non-Reporting Company Issuer thresholds may also be difficult. This issue is compounded by the fact that Regulation SHO, which is incorporated by reference into the definition of "gross short position," is a requirement of US broker-dealers, not institutional investment managers, and largely limited to equity securities traded in the US¹¹

In addition to operational cost and complexity, by incorporating the definition of Regulation SHO into a filing requirement applicable to institutional investment managers, the SEC has an additional tool to impose liability on managers for inadvertent order marking mistakes.¹²

Lastly, while aggregation may limit the risks of market participants being able to reverse engineer and identify the institutional investment managers underlying a publicly disclosed short position, managers are rightly concerned about the risks. In the Adopting Release, the SEC acknowledges that an estimated 39 percent of the stocks reported on Form SHO would only have one manager above the Filing Thresholds for Reporting Company Issuers. Coupled with the near real-time and granular disclosure requirements of security lending information adopted pursuant to newly adopted Rule 10c-1a, the new rule may provide opportunities for third-parties to reverse engineer and engage in targeted manipulative trading activity against short sellers.

Outside of the US, the significantly lower Filing Threshold applicable to Non-Reporting Company Issuers and asymmetrical application to only US institutional investment managers or foreign institutional investment managers that are subject to other SEC filing obligations will likely have unintended consequences.

¹¹ While Regulation SHO has extraterritorial effect, the limitation that it only applies to orders placed with a US broker-dealer largely limits its application to foreign securities.

¹² Section 10(b) of the Exchange Act and SEC Rules 10b-5 and 10b-21 thereunder impose liability on any person for deceiving a broker-dealer, registered clearing agency, or purchaser about its ability or intent to deliver securities. The SEC has also charged managers for causing a violation of a broker-dealer's books and records violation.



Reporting Mechanics

Form SHO Requirements

Once an institutional investment manager determines that it has a filing obligation under one of the Filing Thresholds, it will need to complete and submit Form SHO to the SEC through EDGAR (although the form will not be publicly available on EDGAR) within 14 days of the conclusion of the month.

Cover Page

Each institutional investment manager required to report under Rule 13f-2 must complete a cover page and two informational tables. The cover page contains basic biographical information about the institutional investment manager, including its name, address, contact information, an employee contact for the filing and a non-lapsed Legal Entity Identifier (“LEI”), if they have one. Currently, the SEC is not requiring institutional investment managers to obtain or maintain an LEI solely as a result of a Rule 13f-2 filing requirement, however, the adopting release notes that “[t]he Commission may consider this issue in the future.”

Table 1 (Summary Information)

For each equity security that an institutional investment manager is required to report on Form SHO,¹³ the manager must complete an entry on Table 1 of Form SHO. For each reportable security, Table 1 requires the institutional investment manager to identify the settlement date for the position (i.e., the last settlement day of the calendar month of the relevant reporting period), the name of the issuer, the LEI of the issuer (if the issuer has one), and the title of the class of securities being reported (reasonable abbreviations are permitted).

Table 1 of Form SHO also requires the institutional investment manager to report the Committee on Uniform Securities Identification Procedures (“CUSIP”) and Financial Instrument Global Identifier (“FIGI”) for each security being reported, if applicable. While FIGIs are available in the public domain and available for free, the use of CUSIPs by institutional investment managers may involve significant licensing costs.¹⁴

For each entry in Table 1, the institutional investment manager must identify the gross short position over which it exercised investment discretion in the relevant security at the close of regular trading hours on the last settlement date of the calendar month of the reporting period. Similar to the calculation of the Reporting Thresholds detailed above, this calculation is done without the inclusion of any offsetting economic positions — including long positions of the reportable equity security or derivatives of that security. Further, as noted below, short positions reported by another manager should be excluded under the Anti-Duplication instructions, and short positions of an equity security held within an ETF should not be considered when calculating a short position in an underlying security (a short position in the ETF itself, however, may be separately reportable).

Gross short positions must be identified both in terms of the number of shares of the security for which information is being provided and as a US dollar amount. Calculation of the US dollar value of an equity

¹³ Unless another manager also has investment discretion over that security, the institutional investment manager has noted this on the cover page to their Form SHO, and another manager has reported on Form SHO.

¹⁴ See Comment Letter on File No. S7-08-22, available at <https://www.sec.gov/comments/s7-08-22/s70822-20126773-287490.pdf>.



security is based upon the closing price at the close of regular trading hours on the last settlement date of the calendar month or, if a closing price is not available, the price at which the institutional investment manager last purchased or sold any share of that security.

Minimal information is currently available on how to interpret these requirements outside of the standard US context. Regular trading hours are defined by reference to Regulation NMS, Rule 600(b)(77), which sets the conclusion of regular trading hours at 4:00 P.M. Eastern Time. How this timing requirement will be applied more broadly to the full universe of securities covered by Rule 13f-2 is unclear. Similarly, there is currently no guidance as to how the notional value of equity securities that do not trade or get reported in US dollars should be reported or how share equivalents should be calculated for equity securities that do not trade as shares.

Table 2 (Detailed Information)

For each equity security included in Table 1, the institutional investment manager must also complete a Table 2 entry reflecting daily activity that affected the manager's short positions during the reporting period. For each such entry, the institutional investment would identify the settlement date on which a trade settles, similar biographical information about the issuer and security as required in Table 1, and a single number reflecting the net change in the short position as a number of shares on the relevant settlement date.

The detailed net change in short position information required in Table 2 should reflect how the gross short position reported in Table 1 was closed out or increased as a result of the acquisition or sale of shares of the equity security on each settlement date during the month. This includes:

1. Short sales of the security that settled on that date,
2. Shares of the security that were purchased to cover, in whole or in part, an existing short position and settled on that date,
3. Shares of the security that were acquired in a call option exercise that reduces or closes a short position on that security and settled on that date,
4. Shares of the security that were sold in a put option exercise that creates or increases a short position on that security and settled on that date,
5. Shares of the security that were sold in a call option assignment that creates or increases a short position on that security and settled on that date,
6. Shares of the security that were acquired in a put option assignment that reduces or closes a short position on that security and settled on that date
7. Shares of the security for which information is being reported that were acquired as a result of the tendered conversions that reduces or closes a short position on that security and settled on that date,



8. Shares of the security that were obtained through a secondary offering transaction that reduces or closes a short position on that security and settled on that date,¹⁵
9. Shares of the security that resulted from other activity not previously reported on this form that creates or increases a short position on that security and settled on that date, or that reduces or closes a short position on that security and settled on that date,
10. Activity other than (1) through (9) above that creates or increases, or reduces or closes, a short position on that security, including, but not limited to, shares resulting from ETF creation or redemption activity.

Any activity that results in the reduction of a short position must be netted against activity that increases a short position for purposes of Table 2 (unless the underlying position is excluded on Table 1 as a result of the Anti-Duplication instructions). By way of example, the purchase of shares of an equity security that are delivered to an account and reduce a short position over which the institutional investment manager exercises investment discretion is reportable in Table 2. Similar purchases of shares that do not result in the reduction of short positions, however, are not reportable even if they result in an increase in the net position of the accounts over which an institutional investment manager exercises investment discretion (e.g., purchases that are not used to close a boxed short position or are delivered to a prime broker that does not maintain a short position on behalf of the underlying account are not included in the Table 2 net change calculation).

Additionally, while the acquisition of shares acquired or sold as a result of option exercises or assignments, warrant exercises, ETF creations or redemptions, tenders and other transactions involving the conversion, creation, redemption of a related or derivative instrument that creates or reduces ones short position in an equity security are reportable, the existence of the related or derivative instrument is itself not reportable unless that instrument is also an equity security that meets one of the Filing Thresholds.

Finally, while the preface to the instructions for calculating the net change in a short position expressly limits the calculation to transactions that “result ... in the acquisition or sale of shares of that equity security,” the SEC may require changes in a gross short position that result from operational movements (e.g., collapsing a box by delivering shares that a manager previously owned or allocating positions across prime brokers that results in the increase or reduction of a short position) to trigger a Table 2 disclosure obligation under item 9(g)(10) of the instructions to Form SHO.

Filing Deadlines

An institutional investment manager that exceeds any of the Filing Thresholds in the prior month must submit Form SHO to the SEC via an EDGAR filing within 14 days of the conclusion of the month.

Obligation to Amend and Restate

To the extent that an institutional investment manager identifies an inaccuracy on a previously filed Form SHO, it is required to submit an amended and restated Form SHO for the impacted period within *10 calendar days* of discovering the error. To submit an amendment and restatement, an institutional

¹⁵ For shares of a security obtained through a secondary offering subject to Regulation M, Rule 105, the instructions to Form SHO remind institutional investment managers that any such shares received must be reported regardless of whether they were used to close out a position acquired outside of the Rule 105 Restricted Period.



investment manager must restate the original version of the Form SHO in its entirety and note on the cover page that the submission is an amendment and restatement, provide a description of the revision being made, explain the reason for the revision, and indicate whether any data from any additional Form SHO reports within the prior 12 calendar months were impacted (and if so, file amendment and restatements for each such impacted report).¹⁶

Importantly, the SEC declined to include *any materiality threshold* in the requirement that an institutional investment manager amend any previously identified Form SHO reports. Additionally, while the Adopting Release states that the purpose of the amendment and restatement process is to facilitate the SEC's publication of updated aggregated Form SHO data for a rolling 12-month period after initial publication and that the amendment and restatement process is limited to errors impacting Form SHO data in the prior 12 months, neither Rule 13f-2 nor Form SHO explicitly limit the amendment and restatement process to errors that impacted filings in the prior 12 calendar months (the instructions just limit the requirement to identify "additional" impacted Form SHO reporting periods impacted during the prior twelve months).

Anti-Duplication

To prevent duplicative reporting, if two or more managers, each of which would be required by Rule 13f-2 to file Form SHO, exercise investment discretion with respect to the same security for the same period, only one such manager would be required to report information regarding that security on Form SHO in the relevant informational tables. This relief, however, does not extend to filing the cover page of Form SHO, which must identify whether any information for the reporting institutional investment manager is reported on Form SHO by other manager(s), and if so, identify the name and LEI of the relevant manager(s).

Form of Filing

The Form SHO filing must be made in a custom eXtensible Markup Language ("XML") specific to Form SHO. We expect that the SEC will update the EDGAR Filer Manual and publish additional technical specifications regarding this custom XML format and electronic filing process for Form SHO in advance of the compliance date for Rule 13f-2.

While not anticipated to be used by larger institutional investment managers, the SEC will also permit Form SHO to be submitted using a fillable web form prepared by the SEC that will render data submitted by a manager into Form SHO-specific XML in EDGAR.

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If you have any questions concerning this *Alert*, please contact your attorney at Schulte Roth & Zabel or one of the authors.

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¹⁶ Rule 13f-2 and the instructions to Form SHO leave it ambiguous as to whether the 12-month limitation is intended to limit the amendment of additional months impacted by an issue or whether it also applies to the initial identification of an inaccuracy.



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