

## SECURITIES AND EXCHANGE COMMISSION

### 17 CFR Part 240, 242, and 249

[RELEASE NO. 34-94313; FILE NO. S7-08-22]

RIN 3235-AM34

### Short Position and Short Activity Reporting by Institutional Investment Managers

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Proposed rule.

**SUMMARY:** The Securities and Exchange Commission (the “Commission”) is proposing a new rule and related form pursuant to the Securities Exchange Act of 1934 (the “Exchange Act”), including Section 13(f)(2), which was added by Section 929X of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“DFA”). The proposed rule and related form are designed to provide greater transparency through the publication of short sale related data to investors and other market participants. Under the rule, institutional investment managers that meet or exceed a specified reporting threshold would be required to report, on a monthly basis using the proposed form, specified short position data and short activity data for equity securities. In addition, the Commission is proposing a new rule under the Exchange Act to prescribe a new “buy to cover” order marking requirement, and proposing to amend the national market system plan governing the consolidated audit trail (“CAT”) created pursuant to the Exchange Act to require the reporting of “buy to cover” order marking information and reliance on the bona fide market making exception in the Commission’s short sale rules. The Commission is publishing the text of the proposed amendments to the CAT NMS Plan in a separate notice.

**DATES:** Comments should be received on or before April 26, 2022.

**ADDRESSES:** Comments should be submitted by any of the following methods:

#### Electronic Comments:

- Use the Commission’s internet comment form (<https://www.sec.gov/rules/submitcomments.htm>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number S7-08-22 on the subject line.

#### Paper Comments:

- Send paper comments to: Vanessa A. Countryman, Secretary, Securities

and Exchange Commission, 100 F Street NE, Washington, DC 20549-1090.

All submissions should refer to File Number S7-08-22. This file number should be included on the subject line if email is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission’s internet website (<https://www.sec.gov/rules/proposed.shtml>). Comments are also available for website viewing and printing in the Commission’s Public Reference Room, 100 F Street NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Operating conditions may limit access to the Commission’s public reference room. All comments received will be posted without change. Persons submitting comments are cautioned that the Commission does not redact or edit personal identifying information from comment submissions. Commenters should submit only information that they wish to make available publicly.

Studies, memoranda, or other substantive items may be added by the Commission or staff to the comment file during this rulemaking. A notification of the inclusion in the comment file of any such materials will be made available on the Commission’s website. To ensure direct electronic receipt of such notifications, sign up through the “Stay Connected” option at <https://www.sec.gov/> to receive notifications by email.

#### FOR FURTHER INFORMATION CONTACT:

Timothy M. Riley, Branch Chief; Patrice M. Pitts, Special Counsel; James R. Curley, Special Counsel; Quinn Kane, Special Counsel; Jessica Kloss, Attorney Advisor; Brendan McLeod, Attorney Advisor; and Josephine J. Tao, Assistant Director, Office of Trading Practices, Division of Trading and Markets, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549, at (202) 551-5777.

**SUPPLEMENTARY INFORMATION:** The Commission today is proposing for comment new rule 13f-2 (“Proposed Rule 13f-2”) (17 CFR 240.13f-2) and related form (“Proposed Form SHO”) (17 CFR 249.333) under the Exchange Act. Proposed Rule 13f-2 would require certain institutional investment managers to report, on a monthly basis on new Proposed Form SHO, certain short position data and short activity data for certain equity securities as prescribed in Proposed Rule 13f-2.

The Commission is also proposing for comment a new rule prescribing a “buy to cover” order marking requirement

under Regulation SHO (“Proposed Rule 205”) (17 CFR 242.205), and amendments to the national market system plan governing the CAT, pursuant to Rules 608(a)(2) [17 CFR 242.608(a)(2)] and 608(b)(2) [17 CFR 242.608(b)(2)] of the Exchange Act (“Proposal to Amend CAT”) that enable the Commission to propose amendments to any effective national market system (“NMS”) plan. For the text of the proposed amendments to the CAT NMS Plan, please see the Notice of Proposed Amendments to the National Market System Plan Governing the Consolidated Audit Trail for Purposes of Short Sale-related Data Collection.<sup>1</sup>

Proposed Rule 13f-2, Proposed Form SHO, Proposed Rule 205, and the Proposal to Amend CAT are hereinafter collectively referred to as the “Proposals.”

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<sup>1</sup> See *Notice of the Text of the Proposed Amendments to the National Market System Plan Governing the Consolidated Audit Trail for Purposes of Short Sale-related Data Collection*, Exchange Act Release No. 34-94314 (Feb. 25, 2022).

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## I. Introduction

A short sale involves the sale of a security that the seller does not own, or a sale that is consummated by the delivery of a security borrowed by, or for the account of, the seller.<sup>2</sup> Short selling has long been used in financial markets as a means to profit from an expected downward price movement, to provide liquidity in response to unanticipated demand,<sup>3</sup> or to hedge the risk of a long position in the same security or a related security.<sup>4</sup> Short selling has also been shown to improve pricing efficiency by providing information to the market.<sup>5</sup> While short selling can serve useful market purposes, it also may be used to drive down the price of a security, to accelerate a declining market in a security, or to manipulate stock prices.<sup>6</sup>

<sup>2</sup> See 17 CFR 242.200(a).

<sup>3</sup> Market liquidity is generally provided through short selling by market professionals, such as market makers, who offset temporary imbalances in the buying and selling interest for securities. Short sales effected in the market add to the selling interest of stock available to purchasers and reduce the risk that the price paid by investors is artificially high because of a temporary contraction of selling interest. Short sellers covering their sales also may add to the buying interest of stock available to sellers. See *Amendments to Regulation SHO*, Exchange Act Release No. 61595 (Feb. 26, 2010), 75 FR 11232, 11235 (Mar. 10, 2010) (“Rule 201 Adopting Release”).

<sup>4</sup> See *Short Sales*, Exchange Act Release No. 50103 (July 28, 2004), 69 FR 48008 (Aug. 6, 2004) (“Regulation SHO Adopting Release”).

<sup>5</sup> See, e.g., Phil Mackintosh, *How Short Selling Makes Markets More Efficient*, NASDAQ (Oct. 1, 2020), available at <https://www.nasdaq.com/articles/how-short-selling-makes-markets-more-efficient-2020-10-01>. Efficient markets require that prices fully reflect all buy and sell interest. Market participants who believe a stock is overvalued may engage in short sales in an attempt to profit from a perceived divergence of prices from true economic values. Such short sellers add to stock pricing efficiency because their transactions inform the market of their evaluation of future stock price performance. This evaluation is reflected in the resulting market price of the security. See Rule 201 Adopting Release, 75 FR at 11235 n.29 and 30. See generally discussion *infra* Part VIII.D.2.

<sup>6</sup> See, e.g., Division of Economic and Risk Analysis, *Short Sale Position and Transaction Reporting 6–7* (June 5, 2014) (“DERA 417(a)(2) Study”), available at <https://www.sec.gov/files/short-sale-position-and-transaction-reporting%2C0.pdf>. (This is a study of the Staff of the U.S. Securities and Exchange Commission, which represents the views of Commission staff,

The Commission has plenary authority under Section 10(a) of the Exchange Act to regulate short sales of securities registered on a national securities exchange, as necessary or appropriate in the public interest or for the protection of investors. Current regulatory requirements applicable to short sales of equity securities are generally found in Regulation SHO, which became effective on January 3, 2005.<sup>7</sup> Regulation SHO imposes four general requirements with respect to short sales of equity securities. It requires broker-dealers to properly mark sale orders as “long,” “short,” or “short exempt;”<sup>8</sup> before effecting a short sale, to locate a source of shares that the seller reasonably believes can be timely delivered (commonly referred to as the “locate” requirement);<sup>9</sup> and to close out failures to deliver that result from long or short sales.<sup>10</sup> Further, Regulation SHO imposes a short sale price test circuit breaker.<sup>11</sup> In addition, the Commission adopted an antifraud provision, Rule 10b–21, to address failures to deliver in securities that have been associated with “naked” short

and is not a rule, regulation, or statement of the Commission. The Commission has neither approved nor disapproved the content of this study and, like all staff statements, it has no legal force or effect, does not alter or amend applicable law, and creates no new or additional obligations for any person.; Rule 201 Adopting Release, 75 FR at 11235 (describing a “bear raid” where an equity security is sold short in an effort to drive down the price of the security by creating an imbalance of sell-side interest, as an example of unrestricted short selling that could “exacerbate a declining market in a security by increasing pressure from the sell-side, eliminating bids, and causing a further reduction in the price of a security by creating an appearance that the security’s price is falling for fundamental reasons, when the decline, or the speed of the decline, is being driven by other factors”). See generally discussion *infra* Part VIII.D.1.

<sup>7</sup> See Regulation SHO Adopting Release, *supra* note 4.

<sup>8</sup> See 17 CFR 242.200(g). A broker or dealer must mark all sell orders of an equity security as “long,” “short,” or “short exempt.” A sell order may only be marked “long” if the seller is “deemed to own” the security being sold and either (i) the security to be delivered is in the physical possession or control of the broker or dealer; or (ii) it is reasonably expected that the security will be in the physical possession or control of the broker or dealer no later than the settlement of the transaction. See *id.* A person is deemed to own a security only to the extent that he has a net long position in such security. See 17 CFR 242.200(c). Once marked as long, short, or short-exempt, the order mark should not be changed regardless of any subsequent changes in the person’s net position. See OZ Mgmt., Exchange Act Release No. 75445 (July 14, 2015) (settled) (where OZ Management submitted short sale orders to its executing broker, but identified such sales as long sales to its prime broker, causing books and records of the prime broker to be inaccurate), available at <https://www.sec.gov/litigation/admin/2015/34-75445.pdf>.

<sup>9</sup> See 17 CFR 242.203(b)(1) through (2).

<sup>10</sup> See 17 CFR 242.204.

<sup>11</sup> See 17 CFR 242.201.

selling.<sup>12</sup> As discussed below, Proposed Rule 13f–2 would apply to equity securities that are subject to Regulation SHO in order to be consistent with those requirements.

DFA Section 929X added Section 13(f)(2) of the Exchange Act, titled “Reports by institutional investment managers,” which requires the Commission to prescribe rules to make certain short sale data publicly available no less frequently than monthly.<sup>13</sup> Specifically, Section 13(f)(2) provides that the Commission shall 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 Commission following the end of the reporting period. At a minimum, such public disclosure shall occur every month.<sup>14</sup>

Proposed Rule 13f–2 is designed to provide greater transparency through the publication of certain short sale related data to investors and other market participants by requiring certain institutional investment managers to report to the Commission, on a monthly basis on Proposed Form SHO, certain short position data and short activity data for certain equity securities. More information about the short sale activity and short positions of institutional investment managers (“Managers”)<sup>15</sup> may promote greater risk management among market participants, and may facilitate capital formation to the extent that greater transparency bolsters confidence in the markets.

Proposed Rule 205 would establish a new “buy to cover” order marking requirement for certain purchase orders effected by a broker-dealer for its own account or for the account of another person at the broker-dealer. The Proposal to Amend CAT would require CAT reporting firms to report short sale data not currently required that would enhance regulators’ understanding of the lifecycle of a trade—from order origination, including an order’s mark, through order execution and allocation.

<sup>12</sup> See Exchange Act Release No. 58774 (Oct. 14, 2008), 73 FR 61666 (Oct. 17, 2008).

<sup>13</sup> Public Law 111–203, 929X, 124 Stat. 1376, 1870 (July 21, 2010).

<sup>14</sup> 15 U.S.C. 78m(f)(2).

<sup>15</sup> As defined in Section 13(f)(6)(A) of the Exchange Act and for purposes of Proposed Rule 13f–2, “institutional investment manager” 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. As such, the term “institutional investment manager” typically can include investment advisers, banks, insurance companies, broker-dealers, pension funds and corporations. See also Instructions to Form 13F.

Proposed Rule 205 and the Proposal to Amend CAT are intended to supplement the short sale data made available to the Commission in Proposed Form SHO filings by requiring the reporting to CAT of (i) “buy to cover” order marking information and (ii) reliance on the bona fide market making exception in Regulation SHO. The Commission believes greater transparency of short sale activity and short position data would improve the Commission’s oversight of financial markets and compliance with existing regulations, as well as facilitate regulators’ ability to reconstruct significant market events, which may, in turn, improve the Commission’s ability to respond to similar events in the future.<sup>16</sup> This could, in turn, benefit the public and market participants by aiding the Commission in more effectively maintaining a fair and orderly market.

The Commission believes that the short sale related information that would be collected under the Proposals, particularly the required disclosures of Proposed Form SHO and the aggregated data published pursuant to Proposed Rule 13f–2, would fill an information gap for market participants and regulators by providing insights into the lifecycle of a short sale. In contrast to data related to short sales that is currently collected and published by FINRA and most exchanges, the aggregated information derived from information reported on Proposed Form SHO and published pursuant to Proposed Rule 13f–2 would reflect the timing of increases and decreases in the reported short positions.<sup>17</sup> Such aggregated information would help inform market participants regarding the overall short sale activity by reporting Managers. The information reported on Proposed Form SHO, along with the information gleaned through the operation of Proposed Rule 205 and the Proposal to Amend CAT would help the Commission and SROs to overcome current challenges in using data from CAT to estimate short positions and changes in short positions.<sup>18</sup>

The Commission acknowledges that the Proposals would entail costs to some

market participants—more specifically, compliance costs associated with determining whether the Manager is required to report on Proposed Form SHO and, if so, with filing Proposed Form SHO, pursuant to Proposed Rule 13f–2, and the costs associated with accommodating the additional order marks, pursuant to Proposed Rule 205 and the Proposal to Amend CAT. Implementing Proposed Rule 13f–2 and Proposed Form SHO could also reduce certain industry participants’ incentives to gather information about the marketplace and specific securities. For example, requiring disclosure of short positions could facilitate copycat trading that, in turn, could limit the profit an investor may earn using strategies developed in connection with its marketplace information gathering efforts.<sup>19</sup> In addition, requiring disclosure of large short positions, even in an aggregated format, could make holders of such short positions more susceptible to short squeezes. To the extent that these circumstances could reduce the value of marketplace information gathered to develop a short selling strategy, they could discourage investors from making an effort to gather marketplace information. A reduction in information collection could harm price efficiency, which could, in turn, affect capital allocations and managerial decisions. Aggregating short sale activity and short position information across all reporting Managers for each reported equity security prior to publication and publishing such data on a delay would likely mitigate—though not fully eliminate—the potential negative economic effects of the reporting requirements and associated information disclosure of Proposed Rule 13f–2 and Proposed Form SHO.

Proposed Rule 13f–2 and Proposed Form SHO are designed to address the requirements of Section 13(f)(2). In developing Proposed Rule 13f–2, the Commission recognizes the need to consider the important role short selling plays in the market as well as the benefits of providing more disclosure about short selling. For reasons discussed more fully below, the Commission believes Proposed Rule 13f–2 represents an appropriate balance by offering increased transparency into the short selling activities of certain Managers with large short positions through the dissemination of aggregated information reported on new, stand-alone, Proposed Form SHO. The information reported on Proposed Form

SHO would provide investors, market participants, and the Commission with short sale data that supplements what is currently available, free or on a fee basis, from FINRA and most exchanges.<sup>20</sup> Proposed Rule 13f–2 and Proposed Form SHO would improve the utility of information regularly available to the Commission, and made available as appropriate to self-regulatory organizations (“SROs”), that could be used to examine market behavior and recreate significant market events. It would also increase information available to market participants and could assist in their understanding of the level of negative sentiment and the actions of short sellers collectively. While the primary focus of Proposed Rule 13f–2 and Proposed Form SHO is transparency, the Commission’s regular access to the data reported on Proposed Form SHO would also bolster its oversight of short selling. In addition, Proposed Rule 205 and the Proposal to Amend CAT would enhance the information regularly available to the Commission and other regulators that could be used to oversee short selling and to reconstruct significant market events. In turn, the Commission’s more accurate and timely reconstruction and response to market events could contribute to overall investor protections, particularly in times of increased market volatility.<sup>21</sup>

## II. Background

### A. Enhancing Short Sale Transparency

In recent years, market volatility associated with short selling has brought heightened attention to the difference in long and short position reporting requirements, and, more generally, the lack of transparency into the circumstances surrounding short sale transactions.<sup>22</sup> The Commission has

<sup>20</sup> See *infra* Parts II.B and VIII.C.4 (discussing short sale data that is currently available and how that compares to the data to be reported on Proposed Form SHO).

<sup>21</sup> See *infra* Part VIII.D.1.

<sup>22</sup> See, e.g., Letter from Elizabeth King, Corporate Secretary, NYSE Group, and James M. Cudahy, President and CEO, National Investor Relations Institute (Oct. 7, 2015, Petition 4–689) (stating that rulemaking under 929X “provides an opportunity to implement meaningful public disclosure standards for short-sale activity, consistent with that currently required for institutional investment managers under Section 13(f) of the Exchange Act for long position reporting”), available at <https://www.sec.gov/rules/petitions/2015/petn4-689.pdf> [hereinafter “NYSE Petition”]; Letter from Edward S. Knight, Executive Vice President, General Counsel and Chief Regulatory Officer, NASDAQ (Dec. 7, 2015, Petition 4–691) (requesting that the Commission “take swift action to promulgate rules to require public disclosure by investors of short positions in parity with the disclosure regime applicable to long positions”), available at <https://www.sec.gov/rules/petitions/2015/petn4-691.pdf>

<sup>16</sup> See generally Part VIII.D.1 (discussing how the Commission could have used the data provided under the Proposals to address market events such as the recent market volatility associated with meme stocks, and how the data provided under the Proposals could have aided the Commission in examining that market event).

<sup>17</sup> See generally *infra* Part VIII.C.4 (discussing existing short selling data).

<sup>18</sup> See generally *infra* Parts VIII.B and VIII.C.4.iv (discussing challenges of extracting short sale information—e.g., to estimate positions and to track how those positions change over time—from CAT).

<sup>19</sup> See generally *infra* Parts VIII.C.5 and VIII.F (discussing the impact of copycat trading strategies on competition).

received requests to increase transparency into short sale related activity through the adoption of reporting requirements similar to those currently required by holders of long positions above certain thresholds.<sup>23</sup>

As noted above, Section 13(f)(2) requires the Commission to prescribe rules to make certain short sale data publicly available no less frequently than monthly. After carefully considering the possible economic effects of various approaches, the Commission believes that publication of aggregated gross short position data of certain Managers, and certain related activity data, as discussed in more detail below, would provide valuable transparency to market participants and regulators.<sup>24</sup> The Commission believes that the data resulting from Proposed Rule 13f-2 would help to provide valuable context to overall short position data currently available by distinguishing directional short selling of Managers from short sale activity effected pursuant to hedging as well as that of market makers and liquidity

[hereinafter “NASDAQ Petition”]. See also Letter from E. Carter Esham, Executive Vice President, Emerging Companies, Biotechnology Innovation Organization (BIO) (Mar. 11, 2016) (applauding reforms to the short disclosure framework proposed in the NASDAQ Petition and in the NYSE Petition and advocating for the promulgation of rules to ensure parity between public disclosures required of investors taking long and short positions), available at <https://www.sec.gov/comments/4-691/4691-5.pdf>; Letter from Andrew D. Demott, Jr., Chief Operating Officer, Superior Uniform Group (supporting NASDAQ Petition and advocating adoption of disclosure requirements for short sellers), available at <https://www.sec.gov/comments/4-691/4691-10.pdf>. Developments in the market with regard to “meme” stocks in early 2021, some of which were widely reported as involving large short sellers, also highlighted a need for more consistent and consolidated short sale information. See, e.g., Robert Smith, Laurence Fletcher, Madison Darbyshire, Eric Platt and Hannah Murphy, “Short squeeze spreads as day traders hunt next GameStop”, *Fin. Times* (Jan. 27, 2021), available at <https://www.ft.com/content/acc1dbfe-80a4-4b63-90dd-05f27f21ceb2>; Are “meme stocks” harmless fun, or a threat to the financial old guard?, *Economist* (July 6, 2021). See also Sharon Nunn and Adam Kulam, *Short-Selling Restrictions During Covid-19* (Jan. 12, 2021), available at <https://som.yale.edu/story/2021/short-selling-restrictions-during-covid-19> for a discussion of global short selling regulatory responses to the Covid-19 pandemic.

<sup>23</sup> See, e.g., NYSE Petition and NASDAQ Petition, *supra* note 22. See also Final Report of the 2021 SEC Government-Business Forum on Small Business Capital Formation (May 2021), available at [https://www.sec.gov/files/2021\\_OASB\\_Annual\\_Forum\\_Report\\_FINAL\\_508.pdf](https://www.sec.gov/files/2021_OASB_Annual_Forum_Report_FINAL_508.pdf) (requesting the Commission act to increase the transparency of short selling activities).

<sup>24</sup> See *infra* Part VIII.D (stating that Proposed Rule 13f-2, in conjunction with Proposed Rule 205 and the Proposal to Amend CAT, could help to advance the policy goal of investor protection by deterring market manipulation, and aid regulators in reconstructing significant market events and observing systemic risks).

providers.<sup>25</sup> In addition, the Commission believes that the data would provide regulators with a more complete picture of significant market events by shedding additional light on the potential role of short selling activity.<sup>26</sup>

In determining the proposed reporting requirements under Proposed Rule 13f-2 and Proposed Form SHO, the Commission is mindful of concerns that certain short selling activity can be carried out pursuant to potentially abusive or manipulative schemes. For instance, market manipulators may seek to spread false information about an issuer whose stock they sold short in order to profit from a resulting decline in the stock’s price.<sup>27</sup> The Commission has previously noted various other forms of manipulation that can be advanced by short sellers to illegally manipulate stock prices, such as “bear raids.”<sup>28</sup> As discussed below, greater transparency into the activities of Managers holding large short positions in a security could help regulators’ oversight of short selling and deter these and other types of manipulative short selling campaigns potentially by alerting regulators to suspicious activity.<sup>29</sup>

<sup>25</sup> See *infra* Part VIII.C, VIII.D.

<sup>26</sup> See *infra* Part VIII.D.1 (stating that “because short positions often take some time to create, the Commission could have attempted to quickly identify individual short sellers with large short positions in the various meme stocks in January 2021 based on the most recent reports; then the Commission could have used the enhanced CAT data to understand how these short sellers traded during the heightened volatility.”).

<sup>27</sup> See *infra* Part VIII.D.1 (stating that “[i]n ‘short and distort’ strategies, which are illegal, the goal of manipulators is to first short a stock and then engage in a campaign to spread unverified bad news about the stock with the objective of panicking other investors into selling their stock in order to drive the price down”; stating further that “[i]f successful, the scheme can drive down the price, allowing the manipulators to profit when they ‘buy-to-cover’ their short position at the reduced price.”). See also, John D. Finnerty, *Short Selling, Death Spiral Convertibles, and the Profitability of Stock Manipulation*, SSRN (2005) at n.8, available at <https://www.sec.gov/comments/s7-08-08/s70808-318.pdf> (stating that the posting of “false notices on electronic bulletin boards in internet chat rooms is an example of the type of manipulative behavior that is difficult for regulators to monitor”).

<sup>28</sup> *Proposed Rule: Short Sales*, Exchange Act Release No. 48709, (Oct. 28, 2003), 68 FR 62972 (Nov. 6, 2003), available at <https://www.sec.gov/rules/proposed/34-48709.htm> (stating that “[a]lthough short selling serves useful market purposes, it also may be used to illegally manipulate stock prices. One example is the ‘bear raid’ where an equity security is sold short in an effort to drive down the price of the security by creating an imbalance of sell-side interest. Further, unrestricted short selling can exacerbate a declining market in a security by increasing pressure from the sell-side, eliminating bids, and causing a further reduction in the price of a security by creating an appearance that the security price is falling for fundamental reasons.”).

<sup>29</sup> See Part VIII.D.1 (stating that “if a short and distort campaign is suspected, then detecting this

## B. Existing Short Sale Data

There are currently multiple sources of public and nonpublic data related to short sales.<sup>30</sup> FINRA and most exchanges collect and publish daily aggregate short sale volume data, and on a one month delayed basis publish information regarding short sale transactions.<sup>31</sup> However, the Commission understands that some exchanges only make certain data available for a fee. In addition, FINRA collects and aggregates short interest data<sup>32</sup> from broker-dealer member firms, by security, twice each month.<sup>33</sup>

behavior via the activity and positions data in Proposed Form SHO would be easier than it would be using current data. Short and distort campaigns are more likely to occur in stocks with lower market capitalizations with less public information. Consequently, among these stocks it may not, in dollar terms, take a very large short position to reach the 2.5% threshold in securities of smaller reporting issuers or the \$500,000 threshold in securities of non-reporting issuers to report on Proposed Form SHO. As a result, it is likely that an entity engaging in such a practice would be required to report Proposed Form SHO data. Consequently, if short and distort type behavior were to be suspected, then the Commission would be more likely to identify individuals with large short positions and could thus quickly focus any inquiries on entities in an economic position to potentially profit from manipulation.”).

<sup>30</sup> Additionally, the Commission publishes on its website fail to deliver data, which can result from both long and short sales, twice per month for all equity securities. Securities and Exchange Commission, *Fails-to-Deliver Data*, available at <https://www.sec.gov/data/foiadocsfailsdata.htm>. Further, the CAT created pursuant to Rule 613 of Regulation NMS gives regulators, including the Commission, access to comprehensive information regarding the lifecycle of a trade—from origination, including an order’s mark (*i.e.*, “long,” “short,” or “short exempt”), through execution and allocation. See Part VI. Notably, CAT is currently structured to collect information, but not to disseminate it.

<sup>31</sup> This data is transaction by transaction for each security without identification of the broker-dealer or short seller.

<sup>32</sup> See *Short Interest — What It Is, What It Is Not*, FINRA Inv’r Insights (Apr. 12, 2021), available at <https://www.finra.org/investors/insights/short-interest> (stating that “‘short interest’ is a snapshot of the total open short positions in a security existing on the books and records of brokerage firms on a given date. Short interest data is collected for all stocks—both those that are listed and traded on an exchange and those that are traded over-the-counter (OTC). FINRA and U.S. exchange rules require that brokerage firms report short interest data to FINRA on a per-security basis for all customer and proprietary firm accounts twice a month, around the middle of the month and again at the end of each month.”).

<sup>33</sup> See *infra* Part VIII.C.4.i. FINRA recently sought comment on a variety of potential enhancements to its short interest position program. See FINRA Regulatory Notice 21-19 (June 2021), available at <https://www.finra.org/rules-guidance/notices/21-19>. Any such changes to FINRA rules would be filed with the Commission and published for notice and public comment, pursuant to Exchange Act Section 19(b) and Rule 19b-4 thereunder. See also FINRA Rule 4560, *Short Interest Reporting*, available at <https://www.finra.org/rules-guidance/rulebooks/finra-rules/4560> (requiring FINRA member firms to maintain a record of total “short” positions in all

Continued

FINRA provides this aggregated short interest data to the appropriate listing exchange for publication, some of which charge a fee for access to the data. For over-the-counter (“OTC”) securities, which are not listed on an exchange, FINRA publishes the aggregated short interest data itself.<sup>34</sup> FINRA’s aggregation of the short interest data for each security does not disclose the identity of reporting market participants or the size of any individual short position.

### C. Prior Nonpublic Short Sale Reporting by Certain Institutional Investment Managers to the Commission

In October 2008, the Commission adopted interim temporary Rule 10a–3T, which required certain institutional investment managers to file weekly nonpublic reports with the Commission on Form SH regarding their short sales and positions in Section 13(f) securities, other than options.<sup>35</sup> Rule 10a–3T required reporting of short positions that were either greater than 0.25% of shares outstanding or \$10 million in fair market value. This temporary rule was adopted in the wake of the 2008 financial crisis in response to concerns about high levels of volatility associated with short selling and was specifically intended to provide the Commission with information to evaluate whether its short selling regulations were working

customer and proprietary firm accounts and to regularly report such information to FINRA).

<sup>34</sup> For stocks traded OTC, FINRA collects and publishes equity short interest information free on its Over-the-Counter Equities page, available at <https://otce.finra.org/otce/equityShortInterest>.

<sup>35</sup> *Disclosure of Short Sales and Short Positions by Institutional Investment Managers*, Exchange Act Release No. 58785 (Oct. 15, 2008), 73 FR 61678 (Oct. 17, 2008). The rule extended the reporting requirements established by the Commission’s Emergency Orders dated September 18, 2008, September 21, 2008, and October 2, 2008, with some modifications. See *Emergency Order Pursuant to Section 12(k)(2) of the Securities and Exchange Act of 1934 Taking Temporary Action to Respond to Market Developments*, Exchange Act Release No. 58591 (Sept. 18, 2008), 73 FR 55175 (Sept. 24, 2008); *Amendment to Emergency Order Pursuant to Section 12(k)(2) of the Securities Exchange Act of 1934 Taking Temporary Action to Respond to Market Developments*, Exchange Act Release No. 58591A (Sept. 21, 2008), 73 FR 55557 (Sept. 25, 2008) (amending the September 18, 2008 Emergency Order (“Order”) to clarify certain technical issues and when the information filed by the institutional investment managers on a nonpublic basis would be made public by the Commission on a delayed basis); *Amendment to Order and Order Extending Emergency Order Pursuant to Section 12(k)(2) of the Securities Exchange Act of 1934 Taking Temporary Action to Respond to Market Developments*, Exchange Act Release No. 58724 (Oct. 2, 2008), 73 FR 58987 (Oct. 8, 2008) (extending effectiveness of the Order through October 17, 2008, and stating that the Forms SH filed under the Order would remain nonpublic to the extent permitted by law).

as intended.<sup>36</sup> Rule 10a–3T remained in effect through July 2009, at which time the Commission stated that it and its staff were working with several SROs to make publicly available certain information related to short sale activity, such as short sale volume and transaction data.<sup>37</sup>

Forms SH were nonpublic filings. The Commission’s determination to maintain the confidentiality of the information disclosed on Form SH was based in part on the concern that requiring public disclosure may have had the unintended consequence of giving rise to imitative short selling, thereby exacerbating already extreme levels of market volatility observed during the 2008 financial crisis.<sup>38</sup> The Commission also stated that implementing a nonpublic, rather than public, disclosure requirement would help to prevent the potential for sudden and excessive fluctuations of securities prices and disruption in the functioning of the securities markets that could threaten fair and orderly markets.<sup>39</sup> Moreover, the Commission stated at the time that requiring nonpublic submission of the form may help prevent artificial volatility in securities as well as further downward swings that are caused by short selling while also providing the Commission with valuable information to combat market manipulation.<sup>40</sup> Just before interim temporary Rule 10a–3T was set to expire in August 2009, the Commission stated that it would continue to examine whether additional measures are needed to further enhance market quality and transparency, as well as address short selling abuses.<sup>41</sup>

### D. Petitions and Commentary Regarding Short Position Disclosure

NASDAQ, NYSE, and the National Investor Relations Institute, have previously petitioned the Commission requesting that, pursuant to DFA

<sup>36</sup> See *Disclosure of Short Sales and Short Positions by Institutional Investment Managers*, Exchange Act Release No. 58785 (Oct. 15, 2008), 73 FR 61678 (Oct. 17, 2008).

<sup>37</sup> Press Release, Securities and Exchange Commission, *SEC Takes Steps to Curtail Abusive Short Sales and Increase Market Transparency* (July 27, 2009), available at <https://www.sec.gov/news/press/2009/2009-172.htm> (stating that the Commission and its staff were working with several SROs to make certain short sale volume and transaction data available through SRO websites).

<sup>38</sup> *Amendment to Order and Order Extending Emergency Order Pursuant to Section 12(k)(2) of the Securities Exchange Act of 1934 Taking Temporary Action to Respond to Market Developments*, Exchange Act Release No. 58724 (Oct. 2, 2008), 73 FR 58987 (Oct. 8, 2008).

<sup>39</sup> *Id.* at 58987.

<sup>40</sup> *Id.*

<sup>41</sup> See *supra* note 37.

Section 929X, it require disclosure of individual short positions similar to the disclosures required under Section 13(f)(1) or Regulations 13D and 13G for long-position reporting.<sup>42</sup> The petitions also request that “short position” or “short interest” be interpreted broadly to capture not only traditional short sales but also derivative and other transactions having the same economic impact. Among these petitioners’ concerns is that the lack of public disclosure of individual short positions may facilitate accumulations of significant positions in an issuer’s securities and potentially compromise investors’ ability to accurately evaluate market movements in those securities.<sup>43</sup> They further argue that the benefits associated with requiring individual, public disclosure of short selling would include allowing investors to more accurately evaluate market movements and make more informed investment decisions, reducing manipulative conduct, increasing investor confidence, and improving issuers’ ability to engage with short sellers.

While some market participants have noted instances when public announcements by short sellers have aided the market in ultimately discovering the truth behind fraudulent activity,<sup>44</sup> critics of that position have countered with ways short sellers may unfairly harm issuers that are not engaged in fraudulent activity.<sup>45</sup> Other such critics of short selling have posited that issuers may be unduly harmed<sup>46</sup> even when short sellers suffer through normal market forces.<sup>47</sup>

In response to requests for comment on the short sale reporting study required by Section 417(a)(2) of DFA,<sup>48</sup>

<sup>42</sup> See *supra* note 22.

<sup>43</sup> *Id.*

<sup>44</sup> See, e.g., Jane Lewis, *Jim Chanos: the short-seller who called Enron*, MoneyWeek (Sept. 28, 2018), available at <https://moneyweek.com/495688/jim-chanos-the-short-seller-who-called-enronarticle>.

<sup>45</sup> See, e.g., Duncan Lamont, *GameStop: the ethics of short sellers*, Schroders (Jan. 29, 2021), available at <https://www.schroders.com/en/insights/economics/are-short-sellers-ethical/>; Ariel D. Multak, *The Big Patent Short: Hedge Fund Challenges to Pharmaceutical Patents and the Need for Financial Regulation*, 23 Fordham J. Corp. & Fin. L. 301 (2017), available at <https://news.law.fordham.edu/jcfl/wp-content/uploads/sites/5/2018/01/Multak-Note.pdf>.

<sup>46</sup> See, e.g., Tom Brennan, *How Short-Sellers Almost Destroyed U.S. Banking*, CNBC (Aug. 5, 2010), available at <https://www.cnbc.com/id/28239960>.

<sup>47</sup> See, e.g., Alex Rosenberg, *When shorting goes wrong: Zulily crushes the bears*, CNBC (Aug. 18, 2015), available at <https://www.cnbc.com/2015/08/17/when-shorting-goes-wrong-zulily-crushes-the-bears.html>.

<sup>48</sup> *Short Sale Reporting Study Required by Dodd-Frank Act Section 417(a)(2)*, Exchange Act Release No. 64383 (May 3, 2011), 76 FR 26787 (May 9, 2011). See also DERA 417(a)(2) Study, *supra* note

one commenter stated that identification of a market participant that has engaged in a short sale may have the unintended consequence of exposing investors to the risk of short squeezes.<sup>49</sup> This commenter also maintained that individual public disclosure could chill short selling and thereby deny the marketplace certain resulting benefits, such as market liquidity, and pricing efficiency.<sup>50</sup>

*Design of Proposals.* As discussed more fully throughout the release, the Commission believes that Proposed Rule 13f-2 appropriately balances these competing interests. Proposed Rule 13f-2 would result in the publication of certain short sale related data, which would provide additional transparency to market participants, but data would be aggregated across all reporting Managers for each reported equity security prior to publication. The Commission believes that publicly disclosing the identity of individual reporting Managers may not currently be necessary to advance the policy goal of increasing public transparency into short selling activity, and that aggregating across reporting Managers would help safeguard against the concerns noted above related to retaliation against short sellers, including short squeezes, and the potential chilling effect that such public disclosure may have on short selling. Further, by establishing minimum reporting thresholds, Proposed Rule 13f-2 would apply only to Managers with large gross short positions in a security, and would not generally apply to market participants that do not carry

large overnight gross short positions in equity securities.

Managers that meet a specified reporting threshold, as discussed below, would be required to file Proposed Form SHO with the Commission within 14 calendar days after the end of the calendar month. The Commission would then publish aggregated information derived from data reported on Proposed Form SHO. The Commission estimates that it will publish such aggregated information within one month after the end of the reporting calendar month —e.g., for data reported by Managers on Proposed Form SHO for the month of January, the Commission would expect to publish aggregated information derived from such data no later than the last day of February. This additional time prior to publication of data by the Commission following receipt of the monthly Proposed Form SHO reports would be used to aggregate the data received from the reporting Managers. At this time, the Commission does not intend to verify the accuracy of the data reported by Managers, but may consider doing so in the future after assessing whether such verification would be useful or necessary to enhance the integrity of the data.<sup>51</sup> The additional delay prior to publication of the aggregated data would also help to reduce the risk of imitative trading activity by market participants and help to protect reporting Managers' proprietary trading strategies.<sup>52</sup>

As discussed throughout this release, the Commission believes that, by limiting the reporting requirements to positions exceeding a reporting threshold and by publishing data on an aggregated and delayed basis, the structure of Proposed Rule 13f-2 and the information required to be reported on Proposed Form SHO would likely mitigate many potential negative effects on the market.

### III. Proposed Rule 13f-2 and Proposed Form SHO

#### A. Proposed Form SHO Filing Requirement Through EDGAR

Proposed Rule 13f-2 is designed to provide greater transparency through the publication of certain short sale related data to investors and other market participants by requiring a Manager to file a report in a structured data language in two information tables on Proposed Form SHO, in accordance

with the form's instructions (attached below). Managers would file Proposed Form SHO with the Commission via the Commission's Electronic Data Gathering, Analysis, and Retrieval system ("EDGAR") in an eXtensible Markup Language ("XML") specific to Proposed Form SHO ("custom XML," here "Proposed Form SHO-specific XML"). Managers would have two ways to file Proposed Form SHO or any amended Proposed Form SHO with the Commission. A Manager could use a fillable web form the Commission would provide on EDGAR to input Proposed Form SHO disclosures, which EDGAR would convert to Proposed Form SHO-specific XML, or, alternatively, a Manager could use its own software tool to file Proposed Form SHO to EDGAR directly in Proposed Form SHO-specific XML.

A Manager would be required to file Proposed Form SHO with the Commission within 14 calendar days after the end of each calendar month with regard to each equity security over which the Manager and all accounts over which the Manager (or any person under the Manager's control) has investment discretion<sup>53</sup> collectively meet or exceed a quantitative reporting threshold. Specifically, a Manager must file a Proposed Form SHO report:

- With regard to any equity security of an issuer that is registered pursuant to section 12 of the Exchange Act<sup>54</sup> or for which the issuer is required to file reports pursuant to section 15(d) of the Exchange Act<sup>55</sup> (a "reporting company issuer") in which the Manager meets or exceeds either (1) a gross short position in the equity security with a US dollar value of \$10 million or more at the close of regular trading hours<sup>56</sup> on any settlement date during the calendar month, or (2) a monthly average gross short position<sup>57</sup> as a percentage of shares outstanding in the equity security of 2.5% or more ("Threshold A"); and
- with regard to any equity security of an issuer that is not a reporting company issuer as described above (a

6. The DERA 417(a)(2) Study was a study conducted by Commission staff in the Division of Economic and Risk Analysis analyzing the feasibility, costs, and benefits of *real-time* reporting of short positions in publicly listed securities.

<sup>49</sup> See Letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, Managed Funds Association (June 22, 2011) ("2011 MFA Letter"), available at <https://www.sec.gov/comments/4-627/4627-137.pdf>; see also Letter from Matthew Newell, Associate General Counsel, Managed Funds Association (Sept. 6, 2019), available at <https://www.sec.gov/comments/s7-26-18/s72618-6082119-191807.pdf>.

<sup>50</sup> In this regard, the commenter in the 2011 MFA Letter stated that individual public disclosure would cause potential short sellers to either refrain from or minimize engaging in short sale transactions, including hedging activity, to avoid triggering any threshold for requiring individual public disclosure. The commenter further stated that public disclosure of individual short positions could be misleading to investors (stating that investors frequently short a stock for portfolio risk management purposes) and could potentially enable market participants to reverse engineer a reporting firm's trading strategies. In addition, the commenter stated that individual public disclosure could expose market participants to the risk of a "short squeeze," which may deter investors from engaging in short selling more generally. 2011 MFA Letter, *supra* note 49.

<sup>51</sup> See *infra* Part III.B.4 for a discussion of how technical errors are to be addressed in filing Proposed Form SHO with the Commission.

<sup>52</sup> See generally *infra* Parts VIII.C.5 and VIII.F (discussing "copycat trading").

<sup>53</sup> For purposes of Proposed Rule 13f-2, the term "investment discretion" has the same meaning as in Rule 13f-1(b) under the Exchange Act. 17 CFR 240.13f-1(b). Proposed Rule 13f-2(b)(2).

<sup>54</sup> 15 U.S.C. 78l.

<sup>55</sup> 15 U.S.C. 78o(d).

<sup>56</sup> For purposes of Proposed Rule 13f-2 and Proposed Form SHO, the term "regular trading hours" would have the same meaning as in Rule 600(b)(77) under the Exchange Act. See, e.g., Proposed Rule 13f-2(b)(5).

<sup>57</sup> For purposes of Proposed Rule 13f-2, the term "gross short position" means the number of shares of the reportable equity security that are held short, without inclusion of any offsetting economic positions (including shares of the reportable equity security or derivatives of such security). Proposed Rule 13f-2(b)(4).

“non-reporting company issuer”) in which the Manager meets or exceeds 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 (“Threshold B”).

Threshold A and Threshold B are discussed further in Part III.D below and are referred to herein collectively as the “Reporting Thresholds” (each a “Reporting Threshold”). For each equity security for which a Manager meets or exceeds a Reporting Threshold, such Manager, identifying itself using its name and active Legal Entity Identifier (“LEI”), if available,<sup>58</sup> would be required to report information that is aggregated across accounts over which the Manager, or any person under the Manager’s control, has investment discretion. If a Manager does not have an active LEI, such Manager would file Proposed Form SHO using only its name as registered with the Commission to identify itself.

Managers that meet a Reporting Threshold would be required to file Proposed Form SHO with the Commission via EDGAR within 14 calendar days after the end of the calendar month. Section 13(f)(2) requires that public disclosure of certain short sale information at a minimum shall occur every month. The Commission believes that 14 calendar days after the end of each month provides sufficient time for Managers that meet a Reporting Threshold to assemble, review, and file the required information on Proposed Form SHO. Further, the Commission believes that providing Managers with a reasonable period of time to file complete and accurate short sale related information in the first instance would reduce the need for Managers to file amendments to Proposed Form SHO, as discussed below.

Consistent with Regulation SHO, Proposed Rule 13f–2 would apply to equity securities.<sup>59</sup> As such, the Commission believes that the short sale related data that would be published by the Commission under Proposed Rule 13f–2 would provide additional context to market participants regarding equity

securities that are subject to the requirements of Regulation SHO.

For purposes of Proposed Rule 13f–2, the term “investment discretion” has the same meaning as in Rule 13f–1(b) under the Exchange Act.<sup>60</sup> Rule 13f–1(b)’s definition is comprehensive in that it covers all accounts over which the Manager, or any person under the Manager’s control, has investment discretion. This same definition of investment discretion was used by the Commission in adopting interim temporary Rule 10a–3T in 2008, which required certain Managers to file weekly nonpublic reports with the Commission on Form SH regarding short sales and positions,<sup>61</sup> and is currently used for Form 13F “long” position reporting by certain Managers. Because Proposed Rule 13f–2 is designed to provide greater transparency to investors and other market participants through the publication of certain short sale related data, the Commission believes that using the same comprehensive definition of investment discretion for Manager reporting under Proposed Rule 13f–2 is likewise appropriate. In addition, Managers that would be filing reports on Proposed Form SHO are likely experienced with reporting on Form 13F using this same definition. As discussed above, Proposed Rule 13f–2 is designed to address the requirements of Section 13(f)(2) by offering increased transparency into the activities of certain Managers with large short positions. As such, information reported by a Manager should include all accounts over which such Manager has investment discretion.

Proposed Rule 13f–2 would require that a Manager calculate its “gross short position” in an equity security in determining whether it meets a Reporting Threshold. Under Proposed Rule 13f–2, “gross short position” would mean the number of shares of the equity security that are held short, without inclusion of any offsetting economic positions, including shares of the equity security or derivatives of such equity security. The Manager shall report its gross short position in an equity security without offsetting such gross short position with “long” shares of the equity security or economically equivalent long positions obtained through derivatives of the equity security. A Manager’s gross short position in a security is distinct from its net short position in such security, and

the Commission believes that gross short position information provides a more complete view of a Manager’s short exposure, especially if coupled with the hedging information that the Commission is proposing Managers report on Proposed Form SHO, as discussed below. Requiring reporting of gross short positions would also likely result in more consistent reporting among Managers. Specifically, the Commission is concerned that using net short positions could result in Managers using varying approaches in determining what “long” positions, including equivalent “long” positions through derivatives, are appropriate to offset against their gross short position in determining whether the Manager meets a Reporting Threshold in the first instance. Consequently, the Commission believes that using a net short position could result in different reporting results for otherwise similarly situated Managers in terms of a gross short position in the equity security.

The Commission is proposing required Manager disclosures that are significantly different from currently available data and that would be useful to both market participants and regulators, with a focus on addressing data limitations exposed by the market volatility in January 2021.

## B. Proposed Form SHO

### 1. Filing Proposed Form SHO Reports

Proposed Form SHO is entitled “Information required of institutional investment managers pursuant to Section 13(f)(2) of the Securities Exchange Act of 1934 and rules thereunder.” Managers would use Proposed Form SHO for reports to the Commission required by Proposed Rule 13f–2. A Manager would file a report on Proposed Form SHO with the Commission within 14 calendar days after the end of each calendar month with regard to each equity security in which the Manager meets or exceeds a Reporting Threshold.

Pursuant to Proposed Rule 13f–2 and Proposed Form SHO, to determine whether the dollar value threshold described in the first prong of Threshold A—a gross short position in an equity security of a reporting company issuer (as described above) with a US dollar value of \$10 million or more at the close of regular trading hours on any settlement date during the calendar month—is met, a Manager shall 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

<sup>58</sup> LEI is a unique global identifier for legal entities participating in financial transactions that is currently used in regulatory reporting to financial regulators, including the Commission.

<sup>59</sup> Regulation SHO applies to equity securities, both exchange-listed and over-the-counter, as defined in Section 3(a)(11) of the Exchange Act and Rule 3a11–1 thereunder. See Regulation SHO Adopting Release, *supra* note 4.

<sup>60</sup> 17 CFR 240.13f–1(b). Rule 13f–1 is entitled “Reporting by institutional investment managers of information with respect to accounts over which they exercise investment discretion.”

<sup>61</sup> See *supra* Part II.C.

closing price at the close of regular trading hours on the settlement date.

To determine whether the second prong of Threshold A—2.5% or higher monthly average gross short position as a percentage of shares outstanding in the equity security—is met, the Manager shall (a) identify its gross short position (as defined in Proposed Rule 13f-2) in the equity security at the close of each settlement date during the calendar month of the reporting period, and divide that figure by the number of shares outstanding in such security at the close of that settlement date, then (b) add together the daily percentages during the calendar month as determined in (a) and divide the resulting total by the number of settlement dates during the calendar month of the reporting period. The number of shares outstanding of the security for which information is being reported shall be determined by reference to an issuer's most recent annual or quarterly report, and any subsequent update thereto, filed with the Commission.

To determine whether the dollar value threshold described in Threshold B—a gross short position in an equity security of a non-reporting company issuer (as described above) 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—is met, a Manager shall 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. In circumstances where such closing price is not available, the Manager would be required to use the price at which it last purchased or sold any share of that security in determining whether Threshold B is met.

The rules to prevent duplicative reporting of Proposed Form SHO are modeled after those in Form 13F.<sup>62</sup> More specifically, if two or more Managers, each of which is required by Proposed Rule 13f-2 to file Proposed Form SHO for the reporting period, exercise investment discretion with respect to the same securities, only one such Manager must report the information in its report on Proposed Form SHO. If a Manager has information that is required to be reported on Proposed Form SHO and such information is reported by another Manager (or Managers), such Manager

<sup>62</sup> See “Rules to Prevent Duplicative Reporting” in the “General Instructions” of Form 13F, available at <https://www.sec.gov/pdf/form13f.pdf>.

must identify the Manager(s) reporting on its behalf in the manner described in Special Instruction 5 to the Proposed Form SHO instructions. Such information would be reported by Managers on the “Cover Page,” as discussed further below. Duplicative reporting could result in unnecessary costs to Managers, and could make the aggregated data published by the Commission less accurate.

The Commission believes that requiring Proposed Form SHO to be reported via EDGAR would enhance the accessibility, usability, and quality of the Proposed Form SHO disclosures for the Commission. Proposed Rule 13f-2 and Proposed Form SHO would improve the quality and scope of the information regularly available for the Commission's use in examining market behavior and recreating significant market events. In addition, Proposed Rule 13f-2 and Proposed Form SHO would expand the scope of information available to market participants and could thereby assist in their understanding of the level of negative sentiment and the actions of short sellers collectively. While the primary focus of Proposed Rule 13f-2 and Proposed Form SHO is transparency, the Commission's regular access to the data reported on Proposed Form SHO would also bolster its oversight of short selling. The Commission's ability to more accurately and timely reconstruct and respond to market events could enhance investor protections, particularly in times of increased market volatility.<sup>63</sup>

Reporting via EDGAR would allow the Commission to download the Proposed Form SHO disclosures directly, facilitating efficient access, organization, and evaluation of the reported information, thereby allowing the Commission to more effectively examine market behavior, recreate significant market events, and further bolster its oversight of short selling activity.

The Commission believes that requiring Proposed Form SHO to be filed in Proposed Form SHO-specific XML, a structured machine-readable data language, would facilitate more thorough review and analysis of the reported short sale disclosures by the Commission, increasing the efficiency and effectiveness of the Commission's understanding of short selling and systemic risk. Additionally, most Managers have experience filing EDGAR forms that use similar EDGAR Form-

<sup>63</sup> See *infra* Part VIII.D.1.

specific XML-based data languages, such as Form 13F.<sup>64</sup>

## 2. Confidential Treatment

The instructions to Proposed Form SHO expressly provide that all information that would reveal the identity of a Manager filing a Proposed Form SHO report with the Commission is deemed subject to a confidential treatment request under Rule 24b-2 (17 CFR 240.24b-2). The Commission currently plans to publish only aggregated data derived from information provided in Proposed Form SHO reports. Accordingly, Proposed Form SHO, by its terms, ensures that information reported on the form that could reveal the identity of the reporting Manager will be deemed subject to a confidential treatment request. Pursuant to Section 13(f) of the Exchange Act, the Commission may prevent or delay public disclosure of all other information reported on Proposed Form SHO in accordance with FOIA, Section 13(f)(4)-(5), Rule 24b-2(b) under the Exchange Act, and any other applicable law.<sup>65</sup> The Commission believes that, because the Commission currently plans to publish only aggregated data derived from information reported on Proposed Form SHO, it would be unlikely to grant requests for confidential treatment of the information from which the aggregated data is derived. While it is possible a person may be able to reverse engineer data in a situation where only one person was selling short, especially where the short seller has publicly disclosed that they have a short position in a specific security, the Commission anticipates that many potential negative effects on the market or that short seller would likely be mitigated by the delay in publication of the aggregated data. Further, the Commission believes that granting a request from a Manager that the data it provides on a Proposed Form SHO report be excluded from the aggregated data published by the Commission could affect the integrity of the data by limiting or possibly excluding relevant information. This likely would limit the usefulness of the information to the public. For these reasons, the Commission believes that, on balance, the public's need for the

<sup>64</sup> See Form 13F, available at <https://www.sec.gov/pdf/form13f.pdf>.

<sup>65</sup> Any requests for confidential treatment of the information reported on Proposed Form SHO should be made in accordance with Rule 24b-2 under the Exchange Act (17 CFR 240.24b-2), should be filed electronically in accordance with proposed Rule 24b-2(i) and Rule 101(d) of Regulation S-T (17 CFR 232.101(d)), and should provide enough factual support in the request to enable the Commission to make an informed judgment as to the merits of the request.



aggregated data the Commission would publish likely would justify any potential harm that disclosing such aggregated disclosure would impose on the Manager requesting confidential treatment.

### 3. Proposed Form SHO Contents

Proposed Form SHO consists of two parts: (1) The Cover Page, and (2) the Information Tables.

#### *On the Cover Page—*

- The Manager shall report certain basic information, including its name, mailing address, business telephone and facsimile numbers, as well as the name, title, business telephone and facsimile numbers of the Manager's contact employee for the Proposed Form SHO report; and the date the report is filed. The Manager will also provide its active LEI, if it has one. The Commission believes that this basic information should be included to identify the reporting Manager and the calendar month for which the Manager is reporting.

- The Manager shall identify the calendar month (using the last settlement date of the calendar month) for which the Manager is reporting. The date should name the month, and express the day and year in Arabic numerals, with the year being a four-digit numeral (e.g., 2022).

- The Manager filing the report will include the representation that "all information contained herein is true, correct and complete, and that it is understood that all required items, statements, schedules, lists, and tables, are considered integral parts of this form."

- The reporting Manager shall designate the report type for the Proposed Form SHO by checking the appropriate box in the "Report Type" section of the Cover Page, and include, where applicable, the name and active LEI of each other Manager reporting for this Manager. If the other Manager's active LEI is not available to the reporting Manager, the reporting Manager shall include only the name of the other Manager as registered with the Commission. This information will provide the Commission with a summary of the nature and scope of the information that the Manager is reporting for the calendar month, as well as identify other reporting Managers, if applicable.

- If all of the information that a Manager is required by Proposed Rule 13f-2 to report on Proposed Form SHO is reported by another Manager (or Managers), the Manager shall check the box for Report Type "FORM SHO NOTICE," include on the Cover Page the

name and active LEI (if available) of each of the Other Managers Reporting for this Manager and omit the Information Tables.

- If all of the information that a Manager is required by Proposed Rule 13f-2 to report on Proposed Form SHO is reported in the report filed by the Manager, the Manager shall check the box for Report Type "FORM SHO ENTRIES REPORT," omit from the Cover Page the name and active LEI of each other Manager reporting for this Manager, and include the Information Tables.

- If only a part of the information that a Manager is required by Proposed Rule 13f-2 to report on Proposed Form SHO is reported in the report filed by the Manager, the Manager shall check the box for Report Type "FORM SHO COMBINATION REPORT," include on the Cover Page the name and active LEI of each of the Other Managers reporting for this Manager, if available, and include the Information Tables.

- If the Manager is filing the Proposed Form SHO report as an amendment, then the Manager must check the "Amendment and Restatement" box on the Cover Page, and enter the Amendment and Restatement number.<sup>66</sup> Each amendment must include a complete Cover Page and Information Tables. Amendments must be filed sequentially. This information will provide the Commission with a summary of the nature and scope of the information that a Manager is reporting for the calendar month.

In reporting information required on Information Tables 1 and 2, as discussed below, a Manager also must account for and report a gross short position in an ETF, and activity that results in the acquisition or sale of shares of the ETF resulting from call options exercises or assignments; put options exercises or assignments; tendered conversions; secondary offering transactions; or other activity, as discussed further below. However, for purposes of Proposed Form SHO reporting, a Manager, in determining its gross short position in an equity security, would not be required to consider short positions that the ETF holds in individual underlying equity securities that are part of the ETF basket. Not requiring the Manager to consider these short positions in the underlying equity securities should limit the burden to reporting Managers in determining whether such Manager meets a Reporting Threshold in such underlying equity securities, while not materially affecting the reported gross short position and short activity data.

<sup>66</sup> See *infra* Part III.B.4.

*Information Table 1: "Manager's Gross Short Position Information"*—The information being reported will include gross short position information regarding transactions that have settled during the calendar month being reported.

- In Column 1, a Manager shall enter the last day of the calendar month being reported by the Manager on which a trade settles ("settlement date"). This information will identify the month being reported by the Manager.

- In Column 2, a Manager shall enter the name of the issuer to identify the issuer of the equity security for which information is being reported.

- In Column 3, a Manager shall enter the issuer's active LEI, if the issuer has an active LEI. The LEI provides standardized information that will enable the Commission and market participants to more precisely identify the issuer of each equity security for which information is being reported.

- In Column 4, consistent with Section 13(f)(2), a Manager shall enter the title of the class of the equity security for which information is being reported.

- In Column 5, consistent with Section 13(f)(2), a Manager shall enter the nine (9) digit CUSIP number of the equity security for which information is being reported, if applicable.

- In Column 6, a Manager shall enter the twelve (12) character, alphanumeric Financial Instrument Global Identifier ("FIGI")<sup>67</sup> of the equity security for which information is being reported, if a FIGI has been assigned. Like CUSIP, FIGI provides a methodology for identifying securities.

- In Column 7, a Manager shall enter the number of shares that represent the Manager's gross short position in the equity security for which information is being reported at the close of regular trading hours on the last settlement date of the calendar month of the reporting period. The term "gross short position" means the number of shares of the security for which information is being reported that are held short, without inclusion of any offsetting economic positions (including shares of the equity security for which information is being reported or derivatives of such security).

- In Column 8, a Manager shall enter the US dollar value of the shares reported in Column 7, rounded to the nearest dollar. A Manager shall report the corresponding dollar value of the

<sup>67</sup> FIGI is a randomly assigned 12 character, alphanumeric ID that provides a standardized unique unambiguous identification framework for financial instruments across all asset classes and jurisdictions. It is open sourced, freely available, and non-proprietary.

reported gross short position by multiplying the number of shares of the security for which information is being reported by the closing price at the close of regular trading hours on the last settlement date of the calendar month. In circumstances where such closing price is not available, the Manager shall use the price at which it last purchased or sold any share of that security. This additional information regarding the dollar value of the reported short position will provide additional transparency and context to market participants and regulators.

- In Column 9, a Manager shall indicate whether the identified gross short position in Column 7 is fully hedged (“F”), partially hedged (“P”), or not hedged (“O”) at the close of the last settlement date of the calendar month of the reporting period. A Manager shall indicate that a reported gross short position in an equity security is “fully hedged” if the Manager also holds an offsetting position that reduces the risk of price fluctuations for its entire position in that equity security, for example, through “delta” hedging<sup>68</sup> (in which the Manager’s reported gross short position is offset 1-for-1), or similar hedging strategies used by market participants. A Manager shall report that it is “partially hedged” if the Manager holds an offsetting position that is less than the identified price risk associated with the reported gross short position in that equity security. This additional hedging information would help to indicate whether the reported gross short position is directional or non-directional in nature. More specifically, a short position that is not hedged could be an indicator that the short seller has a negative view of the security, believes that the price of the equity security will decrease, and accepts the market risk related to its short position. A short position that is fully hedged could be an indicator that the short seller has a neutral or positive view of the security, and is engaged in hedging activity to protect against potential market risk. A short position that is partially hedged could be an indicator that the short seller has a negative, neutral, or positive view of the security. Whether the hedge itself is full, partial, or non-existent might provide further context to market participants regarding the short sellers’ view of the equity security. The Commission believes that hedging information also can assist with distinguishing position

trading, which typically has corresponding hedging activity, from other strategies such as arbitrage.

*Information Table 2: “Daily Activity Affecting Manager’s Gross Short Position During the Reporting Period”*—The Manager shall report the information required by the Proposed Form SHO instructions for each date during the reporting period on which a trade settles (settlement date) during the calendar month. The Commission believes that such daily activity information would provide market participants and regulators with additional context and transparency into whether, how, and when reported gross short positions in the reported equity security are being closed out (or alternatively, increased) as a result of the acquisition or sale of shares of the equity security resulting from call options exercises or assignments; put options exercises or assignments; tendered conversions; secondary offering transactions; and other activity. The Commission believes that such activity data would also assist the Commission in assessing systemic risk and in reconstructing unusual market events, including instances of extreme volatility.

- In Column 1, a Manager shall enter the date during the reporting period on which a trade settles for the activity reported. This will identify the settlement date activity being reported.

- In Column 2, a Manager shall enter the name of the issuer, consistent with Section 13(f)(2), to identify the issuer of the security for which information is being reported.

- In Column 3, a Manager shall enter the issuer’s active LEI, if the issuer has an active LEI. The LEI provides standardized information that will enable the Commission and market participants to more precisely identify the issuer of each equity security for which information is being reported.

- In Column 4, consistent with Section 13(f)(2), a Manager shall enter the title of the class of the security for which information is being reported.

- In Column 5, consistent with Section 13(f)(2), a Manager shall enter the nine (9) digit CUSIP number of the equity security for which information is being reported, if applicable.

- In Column 6, a Manager shall enter the twelve (12) character, alphanumeric FIGI of the equity security for which information is being reported, if a FIGI has been assigned. Like CUSIP, FIGI provides a methodology for identifying securities.

- In Column 7, for the settlement date set forth in Column 1, a Manager shall enter the number of shares of the equity

security for which information is being reported that resulted from short sales and settled on that date.

- In Column 8, for the settlement date set forth in Column 1, a Manager shall enter the number of shares of the security for which information is being reported that were purchased to cover, in whole or in part, an existing short position in that security and settled on that date. This activity information will allow the Commission and other regulators to more quickly identify a potential “short squeeze,” which can be evidenced by short sellers closing out short positions by purchasing shares in the open market. If it appears that a short squeeze may have occurred through potential manipulative behavior involving short selling, the Commission could perform further analysis regarding the squeeze. Increased risk of detection may deter some market participants seeking to orchestrate a short squeeze.<sup>69</sup>

- In Column 9, for the settlement date set forth in Column 1, a Manager shall enter the number of shares of the security for which information is being reported that are acquired in a call option exercise that reduces or closes a short position on that security and settled on that date. The exercise or assignment of an option position can reduce or close a short position in the underlying equity security.

- In Column 10, for the settlement date set forth in Column 1, a Manager shall enter the number of shares of the security for which information is being reported that are sold in a put option exercise that creates or increases a short position on that security and settled on that date. Options can be used to create economic short exposure such that an exercise or assignment of an option could create or increase a short position in the underlying equity security.

- In Column 11, for the settlement date set forth in Column 1, a Manager shall enter the number of shares of the security for which information is being reported that are sold in a call option assignment that creates or increases a short position on that security and settled on that date. Options can be used to create economic short exposure such that an exercise or assignment of an option could create or increase a short position in the underlying equity security.

- In Column 12, for the settlement date set forth in Column 1, a Manager shall enter the number of shares of the security for which information is being reported that are acquired in a put option assignment that reduces or closes a short position on that security and

<sup>68</sup> See Brandon Renfro, *What is Delta Hedging?*, The Balance (Nov. 4, 2021), available at <https://www.thebalance.com/what-is-delta-hedging-5207735>.

<sup>69</sup> See *infra* Part VIII.D.1.

settled on that date. The exercise or assignment of an option position can reduce or close a short position in the underlying equity security.

- In Column 13, for the settlement date set forth in Column 1, a Manager shall enter the number of shares of the security for which information is being reported that are acquired as a result of tendered conversions that reduce or close a short position on that security and settled on that date. Holders of convertible debt often hold short positions to hedge their convertible position. When the shares of the convertible debt are converted, they can reduce or close a short position in the equity security.

- In Column 14, for the settlement date set forth in Column 1, a Manager shall enter the number of shares of the security for which information is being reported that were obtained through a secondary offering transaction that reduces or closes a short position on that security and settled on that date.<sup>70</sup> A secondary offering transaction, sometimes referred to as a “seasoned” offering, occurs when a company sells newly created shares to the market, at a time subsequent to the company’s initial public offering, or “IPO.” Purchasing securities in a secondary offering can reduce or close a short position in the equity security.

- In Column 15, for the settlement date set forth in Column 1, a Manager shall enter the number of shares of the security for which information is being reported that resulted from other activity not previously reported in Information Table 2 that creates or increases a short position on that security and settled on that date. Other activity to be reported includes, but is not limited to, shares resulting from ETF creation or redemption activity.

- In Column 16, for the settlement date set forth in Column 1, a Manager shall enter the number of shares of the security for which information is being reported that resulted from other activity not previously reported on Information Table 2 that reduces or closes a short position on that security and settled on that date. Other activity to be reported includes, but is not limited to, shares resulting from ETF creation or redemption activity.

The Commission believes that the information in Columns 9, 12, 13, 14,

<sup>70</sup> Regulation M Rule 105 makes it unlawful, in connection with an offering of certain equity securities, for any person to sell short a security that is the subject of an offering and purchase the offered securities from an underwriter or broker or dealer participating in the offering if such short sale was effected during the Rule 105 restricted period. See 17 CFR 242.105(a).

and 16 is useful in providing the Commission additional context and transparency into how and when short positions in the reported equity security are being closed out or reduced.

The Commission believes that the information in Columns 10, 11, and 15 is useful in providing the Commission additional context and transparency into how and when short positions in the reported equity security are being created or increased.

#### 4. Procedures for Filing and Amending Proposed Form SHO

Managers will have two ways to file Proposed Form SHO or any amended Proposed Form SHO to the Commission. A Manager can use a fillable web form provided by EDGAR to input Proposed Form SHO disclosures that EDGAR will convert to Proposed Form SHO-specific XML or, alternatively, use its own software tool to file Proposed Form SHO to EDGAR directly in Proposed Form SHO-specific XML.<sup>71</sup> If a Manager uses the web-fillable Proposed Form SHO on EDGAR and encounters a technical error when filling out the form, such Manager will be required to correct the identified technical error before being permitted to file the Proposed Form SHO through EDGAR. If a Manager uses its own software tool to file a Proposed Form SHO filing to EDGAR directly in Proposed Form SHO-specific XML, and a technical error is identified by EDGAR after the filing is sent, such Manager will receive an error message that the filing has been suspended, and will be required to correct the identified technical error and re-file the Proposed Form SHO through EDGAR.<sup>72</sup>

A Manager that determines or is made aware that it has filed a Proposed Form SHO with errors that affect the accuracy of the information reported must file an amended Proposed Form SHO within ten (10) calendar days of discovery of

<sup>71</sup> The filing options described for Proposed Form SHO are consistent with other EDGAR filings that are filed in Form-specific XML-based languages. See, e.g., *Regulation of NMS Stock Alternative Trading Systems*, Exchange Act Release No. 83663, (July 18, 2018), 83 FR 38768 (Dec. 9, 2021) (requiring new EDGAR Form ATS-N to be filed in an XML-based language specific to that Form).

<sup>72</sup> The Commission’s XML schema (i.e., the set of technical rules associated with Proposed Form SHO-specific XML) for Proposed Form SHO would incorporate validations of each data field on Proposed Form SHO to help ensure consistent formatting and completeness. For example, letters instead of numbers in a field requiring only numbers, would be flagged by EDGAR as a “technical” error that would require correction by the reporting Manager in order to complete its Proposed Form SHO filing. Field validations act as an automated form completeness check when a Manager files Proposed Form SHO through EDGAR; they do not verify the accuracy of the information submitted in Proposed Form SHO filings.

the error. Filing an amended Proposed Form SHO within 10 calendar days of discovery of the error would provide Managers with a reasonable period of time to prepare the Proposed Form SHO amendment, while helping to ensure that accurate information is received by the Commission in a timely manner.

To facilitate the Commission’s process of aggregating the short sale related information reported on Proposed Form SHO for publication, amendments to Proposed Form SHO must restate the Proposed Form SHO in its entirety. To inform the Commission that the filing is an amendment of a previously filed Proposed Form SHO, a Manager must check the box on the Proposed Form SHO Cover Page to indicate that the filing is an “Amendment and Restatement.” On the Cover Page of each Amendment and Restatement filed, a Manager must provide a written description of the revision being made, explain the reason for the revision, and indicate whether data from any additional Proposed Form SHO reporting period(s) (up to the past 12 calendar months) is/are affected by the amendment. If other reporting periods have been affected, a Manager shall complete and file a separate Amendment and Restatement for each previous calendar month so affected, and provide a description of the revision being made and explain the reason for the revision. As discussed below, the Commission proposes to provide aggregated data on a rolling twelve-month basis, with prior months’ data updated as necessary to reflect data from Amendments and Restatements. The Commission proposes to limit the requirement to file amended Proposed Forms SHO to twelve months to reduce the burden and cost on Managers.

If a revision reported in an Amendment and Restatement changes a data point reported in the Proposed Form SHO that is being amended by twenty-five percent (25%) or more, the Manager must notify the Commission staff via the Office of Interpretation and Guidance of the Division of Trading and Markets (“TM OIG”) at [TradingAndMarkets@sec.gov](mailto:TradingAndMarkets@sec.gov) within two (2) business days after filing the Amendment and Restatement. The Commission believes that a change of 25% or greater reflects a significant change, particularly for securities with few Managers reporting Proposed Form SHO data, which, as discussed below, should be highlighted in the updated aggregated data that will be published.

Regardless of the scope of the revision being reported, if the data being reported in an Amendment and Restatement affects the data reported on

the Proposed Form SHO reports filed for multiple Proposed Form SHO reporting periods, the Manager, within two (2) business days after filing the Amendment and Restatement, must provide the Commission staff via TM OIG with notice of such occurrence, and provide an explanation of the reason for the revision. Reporting discrepancies could harm the integrity of the data being reported on Proposed Form SHO through EDGAR (and published by the Commission on an aggregated basis as discussed herein), particularly if such reporting discrepancies go uncorrected. The Commission believes that requiring a Manager to notify Commission staff when reporting discrepancies have occurred, with a description of the revision being made and the reason for the revision, would help Commission staff determine whether there may be an ongoing or continuing issue with the integrity of the data being reported by that Manager.

Each reporting period, the Commission plans to update prior months' aggregated Proposed Form SHO data on EDGAR to reflect information reported in Amendments and Restatements and will add an asterisk (*i.e.*, \*) or other mark for any updated data for which a Manager notified Commission staff that it filed an Amendment and Restatement to correct a data point of 25% or greater to highlight for market participants that the published aggregated data includes significantly revised data. The Commission will publish the aggregated Proposed Form SHO data for the latest reporting period along with aggregated Proposed Form SHO data for the prior twelve months on a rolling basis. The published aggregated Proposed Form SHO data will include a disclaimer that the Commission does not ensure the accuracy of the data being published.

### C. Publication of Information by the Commission

The Commission will publish through EDGAR aggregated information regarding each equity security reported by all Managers. The Commission estimates that it will publish such aggregated information within one month after the end of the reporting calendar month.<sup>73</sup> The Commission will use the time following receipt of the monthly forms to aggregate the data received from the reporting Managers. The Commission does not plan to verify the accuracy of data elements reported

by Managers, but may consider doing so in the future after assessing whether such verification would be beneficial. This delay prior to publication will also help protect reporting Managers' proprietary trading strategies, thereby reducing the risk of imitative trading activity by the market.<sup>74</sup>

Analysis of data filed under temporary Rule 10a-3T showed the mean duration that short positions were held after the end of the month ranged from nine (9) to thirteen (13) calendar days, increasing with higher threshold levels, and the median position was not held into the following month.<sup>75</sup> At a Reporting Threshold of \$10 million or 2.5% of shares outstanding, positions were held for a mean of 9.85 calendar days and a median of 0 calendar days. Therefore, the Commission believes Managers would close the majority of short positions prior to publication. Under Proposed Rule 13f-2, the requirement to file Proposed Form SHO within 14 calendar days after the end of each calendar month applies to Managers who meet or exceed either Reporting Threshold.

With regard to each individual equity security reported by Managers on Proposed Form SHO's Information Tables 1 and 2 (discussed above), the Commission will publish the issuer's name, and active LEI (if the issuer has an active LEI). The Commission will also publish the equity security's title of class, CUSIP, and FIGI (if a FIGI has been assigned). These data points will identify the equity security for which information is being reported.

With regard to Proposed Form SHO's Information Table 1, entitled "Manager's Gross Short Position Information" (discussed above), the Commission will publish, as an aggregated number of shares across all reporting Managers, the number of shares of the reported equity security that represent the Managers' gross short position at the close of the last settlement date of the calendar month, as well as the corresponding US dollar value of this reported gross short position. The Commission will also publish a summary of the Managers' reported hedging information with regard to the reported equity security. Specifically, the Commission will identify the percentage of the aggregate gross short position for a reported equity security that is reported as being fully hedged, partially hedged, or not hedged.

With regard to Proposed Form SHO's Information Table 2, entitled "Daily Activity Affecting Manager's Gross Short Position during the Reporting Period" (discussed above), for each reported equity security, for each individual settlement date during the calendar month, the Commission will publish the "net" activity in the reported equity security, as aggregated across all reporting Managers. The net activity will be expressed by a single identified number of shares of the reported equity security, and will be determined by offsetting the purchase and sale activity that is reported by Managers in Columns 7 through 16 of Information Table 2. A positive number of shares identified would indicate net purchase activity in the equity security on the specified settlement date, while a negative number of shares identified would indicate net sale activity.

The aggregated information published would provide market participants with additional information beyond what is currently publicly available, specifically information regarding the scope of activity during the calendar month by reporting Managers as a group. Furthermore, by providing the aggregated security-level information through EDGAR in a structured, machine-readable data language, the Commission would allow investors and other public data users to download the aggregated information directly. In each case, the data could then be analyzed using various tools and applications, thus potentially removing the need to pay a third-party vendor to search for, extract, and structure the published information.

### D. Reporting Thresholds

#### 1. Threshold Structure

Setting a reporting threshold level involves a tradeoff between the interests of gathering and disclosing data, such as short sale related data, and potential costs to reporting Managers.<sup>76</sup> A reporting threshold that is set too low could impose substantial compliance costs on Managers that tend to have small short positions or are low volume short sellers, and may only provide incrementally meaningful short sale related data. A reporting threshold that is set too high might limit the amount of data provided to regulators and industry participants, and incentivize Managers to develop trading strategies

<sup>76</sup> These costs to reporting Managers include, for example, compliance costs of reporting; costs associated with retaliation to short sellers, including an increased risk of short squeezes; and market participants reducing their short positions to avoid disclosure, which can have negative impacts on price discovery and market efficiency.

<sup>73</sup> The Commission notes that publication of the aggregated information may be delayed for an initial period following effectiveness of Proposed Rule 13f-2 and Proposed Form SHO.

<sup>74</sup> See generally *infra* Parts VIII.C.5 and VIII.F (discussing "copycat trading").

<sup>75</sup> See *infra* Parts III.D.2 and VIII.C.3.v for additional discussion of analysis of temporary Rule 10a-3T data.

designed to avoid having to report their short sale related data altogether.<sup>77</sup>

The Reporting Thresholds are designed to require the filing of Proposed Form SHO by Managers with substantial gross short positions. The Reporting Thresholds are structured to make it more difficult for Managers with substantial gross short positions to avoid disclosure by trading below a Reporting Threshold, particularly with lower market capitalization securities. The Reporting Thresholds are based on a Manager's gross short position in the equity security itself, and do not include the calculation of derivative positions or long positions in the equity security. While the proposed rule does not include derivatives as part of the threshold calculation, the Commission is proposing to require Managers to report certain changes in their gross equity short positions derived from acquiring or selling the equity in connection with derivative activity, such as exercising an option. The Commission believes this proposed approach balances Managers' reporting costs with the utility such data provides to regulators.

*Threshold A.* The Commission is proposing a two-pronged reporting threshold structure with regard to any equity security of an issuer that is registered pursuant to section 12 of the Exchange Act or for which the issuer is required to file reports pursuant to section 15(d) of the Exchange Act (a reporting company issuer). Specifically, Threshold A, identified in Proposed Rule 13f-2(a), is focused on Managers that, with regard to each equity security of a reporting company issuer in which the Manager and all accounts over which the Manager or any person under the Manager's control has investment discretion, collectively have either (1) a gross short position in the equity security with a US dollar value of \$10 million or more at the close of regular trading hours on any settlement date during the calendar month, or (2) a 2.5% or higher monthly average gross short position as a percentage of shares outstanding in the equity security.

This two-pronged approach measures the size of the short position in question relative to both a monetary dollar amount and the number of shares

outstanding. This approach is designed to ensure that a substantial short position in either a small capitalization security or a large capitalization security could potentially trigger a reporting obligation under Threshold A. As noted above, the Reporting Thresholds are based on a Manager's gross short position in the equity security itself, and do not include the calculation of derivative positions or long positions in the equity security. The Commission believes that this is a simple and straight forward approach for Managers to determine whether they meet Threshold A that avoids any additional cost and complexity of including derivative or long positions.

The Commission believes that requiring reporting of short positions with a US dollar value of \$10 million or more would capture Managers with substantial short positions, even if such positions are relatively small compared to the market capitalization of the issuer. To determine whether this dollar threshold is met, a Manager will be required to determine its end of day gross short position 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 relevant settlement date.

The Commission believes that using end of day gross short position, rather than an intraday high gross short position, for example, would help to prevent Managers engaged in intraday market making strategies (who do not typically carry large overnight short positions) from triggering this \$10 million threshold.<sup>78</sup> The use of the end of day position on any settlement date as opposed to the last settlement date of the month is designed to prevent a scenario where, for example, a Manager engages in trading activity on the last day of the month to avoid reporting altogether.

In addition, the Commission believes that requiring the reporting of short positions with a 2.5% or higher monthly average gross short position would capture Managers with gross short positions that are large relative to the size of the issuer, and could therefore have a significant impact on the issuer. Using a monthly average gross short position, rather than an end of month gross short position, is also designed to prevent the scenario where a Manager engages in trading activity on the last day of the month in order to avoid reporting. To determine whether this percentage threshold is met, a Manager

shall (a) identify its gross short position in the equity security at the close of each settlement date during the calendar month, and divide that figure by the number of shares outstanding in such security at the close of that settlement date, and (b) add up the daily percentages during the calendar month as determined in (a) and divide that total by the number of settlement dates during the calendar month of the reporting period. The number of shares outstanding of the equity security shall be determined by reference to an issuer's most recent annual or quarterly report, and any subsequent update thereto, filed with the Commission.

*Threshold B.* The Commission is separately proposing a single-pronged reporting threshold structure with regard to any equity security of a non-reporting company issuer. Specifically, Threshold B, identified in Proposed Rule 13f-2(a), is focused on Managers that, with regard to each equity security of a non-reporting company issuer in which the Manager and all accounts over which the Manager or any person under the Manager's control has investment discretion, collectively have a gross short position in the 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.

With regard to an equity security of a non-reporting company issuer, the Commission understands that the number of total shares outstanding may not be readily and consistently accessible to Managers. As such, the Commission has determined that a single-pronged reporting threshold based on a set dollar value is appropriate for equity securities of non-reporting company issuers. The Commission believes that this approach is an efficient way for Managers to determine whether they meet Threshold B that avoids the potential additional cost and complexity of locating total number of shares outstanding for a non-reporting company issuer that might be difficult, or impossible, to locate.

Like Threshold A, Threshold B is based on a Manager's gross short position in the equity security itself, and does not include the calculation of derivative positions or long positions in the equity security. As noted above, the Commission believes that this is a simple and straight forward approach for Managers to determine whether they meet Threshold B that avoids any additional cost and complexity of including derivative or long positions.

The Commission believes that requiring reporting of short positions with a US dollar value of \$500,000 or

<sup>77</sup> With regard to reporting thresholds, research has shown that some short sellers in Europe, for example, avoid crossing the stated percentage reporting threshold of 0.5% of shares outstanding by keeping their short positions just under such reporting threshold. See Eur. Sec. and Mkts. Auth., ESMA Report on Trends, Risks and Vulnerabilities No. 1, 62–63 (2018), available at [https://www.esma.europa.eu/sites/default/files/library/esma50-165-538\\_report\\_on\\_trends\\_risks\\_and\\_vulnerabilities\\_no.1\\_2018.pdf](https://www.esma.europa.eu/sites/default/files/library/esma50-165-538_report_on_trends_risks_and_vulnerabilities_no.1_2018.pdf).

<sup>78</sup> See, e.g., Albert J. Menkveld, *High frequency trading and the new market makers*, 16 J. Fin. Mkts., 712, 712–740 (2013).

more would capture Managers with substantial short positions in an equity security of a non-reporting company issuer, even if such positions are relatively small compared to the market capitalization of the issuer. To determine whether this dollar threshold is met, a Manager will be required to determine its end of day gross short position 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 relevant settlement date. In circumstances where such closing price is not available, a Manager would be required to use the price at which it last purchased or sold any share of that security, which would be readily available to the Manager, in determining whether Threshold B is met.

The Commission believes that using end of day gross short position, rather than an intraday high gross short position, for example, would help to

prevent market participants engaged in intraday market making strategies (who do not typically carry large overnight short positions) from triggering this \$500,000 threshold. The use of the end of day position on any settlement date as opposed to the last settlement date of the month is designed to prevent a scenario where, for example, a Manager engages in trading activity on the last day of the month to avoid reporting altogether.

## 2. Determination of Reporting Threshold

As discussed in this section, the Reporting Thresholds are based on comment letters and analysis of Form SH data collected under Rule 10a-3T. Rule 10a-3T required reporting of short positions that were either greater than 0.25% of shares outstanding or \$10 million in fair market value. Comment letters to Rule 10a-3T generally concurred with the dollar reporting obligation but expressed concerns that

the percentage obligation was too low. Suggestions for a percentage reporting obligation ranged from 1% to 5% of shares outstanding.<sup>79</sup>

*Threshold A.* Based on analysis of Form SH data,<sup>80</sup> the Commission believes that a two-pronged threshold of \$10 million or 2.5% of shares outstanding would provide significant coverage of the dollar value of positions, while limiting the reporting burden on Managers. Panel A of Table I shows the Reporting Threshold would have captured 89% of the dollar value of the positions reported by Managers who were required to report Form SH; Panel B shows that it would have captured 346 Managers.<sup>81</sup> The reporting burden would not significantly increase compared to slightly higher threshold levels, while the value of the positions potentially collected would drop significantly for higher dollar threshold levels.

TABLE I—VARIOUS THRESHOLD LEVELS FOR MONTHLY AVERAGE POSITIONS AND MONTHLY MAXIMUM DOLLAR VALUE

Greater than (%)	Greater than								
	\$0	\$1M	\$5M	\$10M	\$15M	\$20M	\$25M	\$50M	\$100M
<b>Panel A: Percentage of Position Dollar Value</b>									
0.0 .....	100	100	100	100	100	100	100	100	100
0.25 .....	100	100	100	100	98	96	94	88	82
0.5 .....	100	100	98	95	92	88	85	76	68
1.0 .....	100	100	96	91	85	81	77	65	54
1.5 .....	100	100	96	90	83	78	74	60	48
2.0 .....	100	100	95	90	83	77	72	58	45
2.5 .....	100	100	95	89	82	77	72	56	43
3.0 .....	100	100	95	89	82	76	71	55	42
4.0 .....	100	100	95	89	82	76	71	54	40
5.0 .....	100	100	95	89	82	76	71	54	39
<b>Panel B: Number of Managers by Position Percentage or Position Dollar Value</b>									
0.0 .....	442	442	442	442	442	442	442	442	442
0.25 .....	442	442	442	442	435	429	425	421	419
0.5 .....	442	435	406	402	388	380	373	360	355
1.0 .....	442	433	384	373	348	335	320	294	281
1.5 .....	442	432	377	362	333	314	293	255	232

<sup>79</sup> See, e.g., Seward & Kissel LLP, available at <https://www.sec.gov/comments/s7-31-08/s73108-43.pdf>, Investment Adviser Association, available at <https://www.sec.gov/comments/s7-31-08/s73108-38.pdf>, and Securities Industry and Financial Markets Association, available at <https://www.sec.gov/comments/s7-31-08/s73108-52.pdf>.

<sup>80</sup> To perform this analysis, Form SH data on daily short positions for November 2008 through February 2009 were filtered to remove duplicate and missing observations, weekend or holiday observations, and positions below the *de minimis* reporting threshold. They were matched to Center for Research in Security Prices, LLC for daily closing prices and Compustat for daily shares outstanding. The Commission recognizes that the results of an analysis of Form SH data may not fully reflect the status quo but that the analysis uses appropriate data currently available to the Commission for this use. The Form SH data covered a limited time period, may not be comparable because of subsequent market changes, and did not

represent “normal” market conditions as the trading took place during and after the 2008 financial crisis. Additionally, Managers that exercise investment discretion with respect to accounts holding Section 13(f) securities having an aggregate fair market value of less than \$100 million were not required to report. Further, we believe that many aggregated short positions that we calculated using Form SH data likely overestimate the actual number of shares that were short. This is because in many instances the size of a short position calculated using Form SH data was greater than 100% of FINRA short interest for the same stock on the same date. This difference could potentially be explained if arranged financing, which is not included in the definition of FINRA short interest, was a large fraction of aggregated Form SH short positions. According to FINRA, “arranged financing programs (sometimes called ‘enhanced lending’ or ‘short arranging products’) [describe an arrangement in] which a customer [ ] borrow[s] shares from [its broker’s] domestic or foreign affiliate and [then] use[s] those shares to close out a short position in

the customer’s account.” See FINRA Notice 21-19 available at <https://www.finra.org/sites/default/files/2021-06/Regulatory-Notice-21-19.pdf>. In addition, this difference could also be explained if affiliated Managers reported the same short positions on multiple Form SH filings. Despite the potential overestimate, the Commission believes that the analysis provides information informative for selecting the Reporting Threshold because it involves the same type of entities (Managers) and the same activity (short positions). Intraday short selling activity could not be examined because the data field for “Number of Securities Sold Short” was populated in only 7% of observations after filters were applied, likely because most short selling volumes were below the threshold.

<sup>81</sup> Although they were not required to, some Managers submitted data for positions below the 10a-3T reporting threshold. These were excluded from the analysis. See Part VIII.C.3.v for additional discussion. See also *infra* notes 365-66 and accompanying text.

TABLE I—VARIOUS THRESHOLD LEVELS FOR MONTHLY AVERAGE POSITIONS AND MONTHLY MAXIMUM DOLLAR VALUE—Continued

Greater than (%)	Greater than								
	\$0	\$1M	\$5M	\$10M	\$15M	\$20M	\$25M	\$50M	\$100M
2.0 .....	442	432	374	350	319	297	275	229	202
2.5 .....	442	432	373	346	312	286	261	210	178
3.0 .....	442	432	373	345	310	282	255	200	165
4.0 .....	442	432	372	344	306	277	247	184	142
5.0 .....	442	432	372	343	303	274	243	174	127

This table reports the coverage of Managers reporting at different threshold levels. Data are from Form SH filings for a 4 month period from 2008 to 2009. The “Greater than” levels are cumulative. Entries are calculated as a percentage of Manager/stock observations for the row or column criteria. Rows are monthly average positions as a percentage of shares outstanding and columns are monthly maximum unscaled dollar value of positions as determined by the daily closing price in Center for Research in Security Prices, LLC (CRSP). Values in Panel A are average percentages of total position dollar value. Values in Panel B are the average number of Managers reporting.

*Threshold B.* Based on analysis of OTC Markets data,<sup>82</sup> the Commission believes that a threshold of \$500,000 would provide significant coverage of the dollar value of positions, while limiting the reporting burden on Managers. The \$500,000 threshold is also similar to the median dollar value of 2.5% of the market capitalization of OTC stocks for which we were able to obtain total shares outstanding. The

median for this set of stocks was approximately \$460,000. The proposed threshold of \$500,000 is the rounded median and is likely greater than 2.5% of the market capitalization of the equity securities of non-reporting company issuers, assuming such equities have lower market capitalization than that of reporting company issuers. The Commission believes that this level provides a reasonable estimate in the

absence of data on the market capitalization for equity securities of non-reporting company issuers. Table II shows Threshold B would have captured over 99% of the dollar value of short positions and 15% to 24% of Managers, assuming 1 to 3 Managers had equivalently-sized short positions in each stock.

TABLE II—VARIOUS THRESHOLD LEVELS FOR OTC STOCKS

Greater than	% of \$ Short Interest	% of Short Positions (1 Manager per stock)	% of Short Positions (3 Managers per stock)
\$50K .....	99.91	48.08	35.47
\$100K .....	99.82	40.38	27.56
\$250K .....	99.52	29.70	21.58
\$500K .....	99.17	23.72	15.60
\$1M .....	98.65	19.66	13.03
\$5M .....	95.30	10.90	6.84
\$10M .....	92.66	8.76	3.63

This table reports the coverage of the short interest in the equities in non-reporting company issuers at different threshold levels. Data are from OTC Markets Group for September 30, 2020. The “Greater than” levels are cumulative. “% of \$ Short Interest” is the percentage of total dollar value of short interest. “% of Short Positions” is the percentage of short positions, assuming 1 or 3 Managers have short positions in each stock.

*E. Supplementing Current Short Sale Data Available From FINRA and the Exchanges*

As noted above, certain short sale data is publicly disseminated currently by FINRA and most of the exchanges. Notably, however, FINRA or the exchanges, at their discretion, could modify, or eliminate, their collection or publication of such short sale data. Moreover, the Commission understands that some of the exchanges require payment of a fee to access the data, which may make it difficult for some investors to access. The Commission believes that the short sale data

provided pursuant to Proposed Rule 13f-2 and Proposed Form SHO would supplement the short sale information that is currently publicly available from FINRA and the exchanges, with the benefit of having certain of the short sale data provided consolidated in a readily accessible location (*i.e.*, EDGAR), with aggregated data free to all investors and other market participants. The short sale data collected pursuant to Proposed Rule 13f-2 and Proposed Form SHO, for example, would include certain activity related data that is not currently available from FINRA or the exchanges, including activity in related

options. While FINRA’s existing short interest data reports aggregate short positions on a bi-monthly basis,<sup>83</sup> they do not reflect the timing with which short positions increase or decrease in the two week period between the two reporting dates. The short sale data collected pursuant to Proposed Rule 13f-2 and Proposed Form SHO would help to fill that gap. The Commission believes that publication of this additional information, aggregated as discussed above, could help to further inform market participants regarding overall short sale activity by reporting

<sup>82</sup> This analysis was performed using data from OTC Markets Group Inc. available through Wharton Research Data Services, <https://wrds-www.wharton.upenn.edu/pages/about/data-vendors/otc-markets-group/>. The data were filtered to only include equities that had a closing price and short interest on September 30, 2020.

Approximately 13% of the data did not have total shares outstanding available, representing approximately 14% of the dollar value of short interest. We use these data without shares outstanding as a proxy for non-reporting issuers. The Commission used September 2020 because that is the most recent date in which a dataset

containing total shares outstanding for a broad set of OTC equities was available.

<sup>83</sup> The short interest data reported reflects aggregate short positions as of the specified reporting dates.

Managers with substantial short positions.

#### F. Request for Comments

While the Commission welcomes any public input on Proposed Rule 13f-2 and Proposed Form SHO, the Commission asks commenters to consider the following questions.

• **Q1: EDGAR:** Managers that meet a Reporting Threshold would be required to report prescribed short sale related data on Proposed Form SHO through EDGAR.

○ Are there are other reporting mechanisms for reporting Managers that would be more appropriate, including more efficient, than reporting through EDGAR? If so, please identify the alternative reporting mechanism, and provide the reasons why such alternative reporting mechanism would be more appropriate.

• **Q2: Managers:** Under Proposed Rule 13f-2, the Commission is proposing that the information reported by Managers be aggregated across all reporting Managers prior to publication.

○ Please discuss any views on the reporting requirements of Proposed Rule 13f-2 and Proposed Form SHO.

○ Please discuss any views regarding the Commission's proposed approach to aggregate the reported information across all reporting Managers prior to publication and address the pros and cons, as applicable, of the Commission's proposed approach.

○ Proposed Rule 13f-2 would require that a Manager provide identifying information including its active LEI (if it has one) when filing Proposed Form SHO. If a Manager does not have an active LEI, should such Manager be required to obtain an LEI?

• **Q3: Hedging Information:** When reporting on Proposed Form SHO, Managers would be required to identify whether the gross short position reported is fully hedged, partially hedged, or not hedged.

○ Please describe any views regarding the reporting of hedging information as proposed by the Commission and address the pros and cons, as applicable.

○ Do Managers generally know whether a position is fully hedged or partially hedged?

○ Is there a common understanding among Managers regarding what fully hedged or partially hedged means? Are those understandings different than the Commission's proposed instructions and discussion above? If there is a common understanding or definition, please describe it.

○ Is the Commission's description of "fully hedged" or "partially hedged"

appropriate for purposes of reporting under Proposed Rule 13f-2? If so, describe why. If not, please describe what would be an appropriate definition of these terms for purposes of Manager reporting under Proposed Rule 13f-2.

○ Would the required hedging information provide important information to assist in interpreting the reported gross short position information?

▪ If not, what other information might help to inform on the economic exposure of the reported gross short position?

• **Q4: Publication of "Activity"**

#### Information by the Commission:

○ Please discuss any views regarding the Commission's proposed approach with regard to the publication of aggregated "net" activity, as described above, and address the pros and cons, as applicable.

○ Would aggregated "net" activity be more useful and informative if it was published by "category" of activity identified in Information Table 2, rather than consolidated across all "categories" of activity identified in Information Table 2?

○ Is there another manner in which aggregated "activity" information could be published that would be more useful and informative than is proposed by the Commission? If so, please describe.

• **Q5: Reporting Thresholds:** Under Proposed Rule 13f-2, only Managers that meet a stated Reporting Threshold would be required to report on Proposed Form SHO through EDGAR. This approach is intended to focus reporting by Managers with substantial gross short positions.

○ Are the proposed Reporting Thresholds appropriate? If so, explain why. If not, explain why not and how the Reporting Thresholds should be modified.

○ Do you believe that Managers would try to avoid triggering the proposed Reporting Thresholds? If so, please explain.

○ In determining whether the dollar value threshold in Threshold A (U.S. dollar value of \$10 million or more) is met, the Commission proposes that a Manager utilize the closing price at the close of regular trading hours on the settlement date. Should Managers be required to use a specific source of information in determining the closing price of the equity security? If yes, explain why, and describe the source(s) of information. Could there be circumstances in which a closing price is not available for equity securities subject to Threshold A? If yes, please describe those circumstances. In such circumstances, should a Manager be

required to use a specific source of information in determining the closing price of the equity security?

○ To determine whether the percentage threshold in Threshold A (2.5% or more) is met, the Commission proposes that a Manager utilize the number of outstanding shares of the security for which information is being reported as determined by reference to an issuer's most recent annual or quarterly report, and any subsequent update thereto, filed with the Commission. Are there circumstances in which Managers should not reference these reports filed with the Commission to determine the number of outstanding shares? If yes, please describe those circumstances. Should Managers be required or permitted to use a different source of information in determining the number of shares outstanding of the equity security? If yes, please explain why, and describe the source(s) of information.

○ In determining whether the dollar value threshold in Threshold B (U.S. dollar value of \$500,000 or more) is met, the Commission proposes that a Manager utilize the closing price at the close of regular trading hours on the settlement date. The Commission further proposes that in circumstances where such closing price is not available, a Manager would be required to utilize the price at which it last purchased or sold any share of that equity security in determining whether Threshold B is met. Should Managers be required to use a specific source of information in determining the closing price of such an equity security—for example, the closing price provided on an interdealer quotation system ("IDQS")<sup>84</sup> or an alternative trading system ("ATS")<sup>85</sup>? Or alternatively, last available sale price of such equity security? If yes, explain why, and describe the source(s) of information.

○ Managers would be required to report their gross short positions in equity securities without offsetting such gross short positions with long shares of the equity security or with an equivalent long position through derivatives of the equity security. Are there any pros and cons of such a proposed approach, especially when compared to using a "net" short interest position calculation? If so, explain why, and describe any associated costs and benefits.

• **Q6: Securities Covered:** Under Proposed Rule 13f-2, Managers would be required to report to the Commission certain short sale related data, as

<sup>84</sup> See 17 CFR 240.15c2-11(e)(3).

<sup>85</sup> See 17 CFR 242.300(a).



described above, for equity securities consistent with the Commission's short sale regulations (*i.e.*, Regulation SHO).

- Should reporting Managers be required to report short sale related data for a different universe of securities than equity securities consistent with Regulation SHO? If so, please explain why and describe the universe of securities that would be more appropriate.

- Should fixed income securities be included under Proposed Rule 13f-2? If yes, explain why and describe what costs and benefits might be associated with such reporting.

- Should other securities be included under Proposed Rule 13f-2? If yes, identify such securities, explain why, and describe what costs and benefits might be associated with such reporting.

- Should certain securities be excluded from Proposed Rule 13f-2 reporting? If yes, identify the securities in question, and explain why.

- ETFs would be included under Proposed Rule 13f-2. Should ETFs be excluded from Proposed Rule 13f-2? If yes, describe why. If no, explain why not.

- **Q7: Economic Short Positions:** Proposed Rule 13f-2 requires that a Manager calculate its gross short position in the equity security in determining whether it meets the Reporting Thresholds.

- Should a Manager also be required to include short positions resulting from derivatives in determining whether it meets the Reporting Thresholds? If so, explain why, and describe any associated costs and benefits to doing so. If not, explain why not.

- Should only certain derivative positions be included? If so, which ones and why?

- Should certain derivative positions not be included? If so, which ones and why?

- Does excluding derivative positions create opportunities to avoid triggering the Reporting Thresholds through other economically equivalent instruments? If so, please explain.

- **Q8: Short Position Information:** Under Proposed Rule 13f-2, Managers that meet a Reporting Threshold are required to report their end of month gross short position in the equity security.

- Should a Manager also be required to separately report its end of month gross short position in derivatives, including, for example, options? Please explain.

- If yes, should only certain derivatives be reported? Please explain.

- If yes, should certain derivatives not be reported? Please explain.

- Please describe any views related to the pros or cons associated with reporting end of month gross short positions in derivatives.

- Proposed Form SHO requires Managers to report CUSIP and if assigned, FIGI, for a security for which information is being reported in both Instruction Tables 1 and 2. If a FIGI has been assigned, should a Manager be required to report CUSIP as well?

- Please describe any views related to the position data that a Manager would be required to report as described in Information Table 1 of Proposed Form SHO.

- **Q9: Short Sale "Activity" Information Reported by Managers:** Under Proposed Rule 13f-2, Managers would be required to report on Proposed Form SHO all activity in the equity security on each settlement date during the calendar month.

- Please describe any views related to the "categories" of activity data that a Manager would be required to report as described in Information Table 2 of Proposed Form SHO.

- With regard to the reporting of "other" activity, are there certain types of "other" activity that should be reported? If yes, describe the other activity and describe why it should be reported.

- ETF creations and redemptions would be included under Proposed Rule 13f-2. Should ETF creations and redemptions be excluded from Proposed Rule 13f-2? If yes, describe why. If no, explain why not.

- Should other activity be included or excluded from Proposed Rule 13f-2? If yes, describe the other activity and describe why it should be included or excluded.

- **Q10: Indirect Short Positions or Short Activities:** Managers meeting a Reporting Threshold would be required to report a gross short position in an ETF, but would not be required to consider short positions that the ETF holds in individual underlying equity securities that are part of the ETF basket in determining whether the Manager meets a Reporting Threshold for such underlying equity securities that are part of the ETF basket.

- Should Managers be required to consider short positions that the ETF holds in individual underlying equity securities that are part of the ETF basket in determining whether the Manager meets a Reporting Threshold for such underlying equity securities that are part of the ETF basket? If yes, explain why. If no, explain why not.

- Are there other diversified portfolio products in addition to ETFs that should be included? If yes, describe the

product. Describe why, or why not, a Manager should be required to consider short positions in individual underlying equity securities of the product's basket of assets.

- **Q11: Frequency of Reporting:** Under Proposed Rule 13f-2, a Manager that meets a Reporting Threshold must file Proposed Form SHO with the Commission within 14 calendar days after the end of each calendar month.

- Is monthly reporting by Managers appropriate? If so, explain why. If no, explain why not and describe an alternative frequency of reporting that is more appropriate.

- Does reporting within 14 calendar days of the end of the calendar month provide reporting Managers sufficient time to accurately report the short sale related information as described in Proposed Rule 13f-2? If no, please explain why not and describe any suggested alternative timeline(s). Alternatively, is the 14 calendar days after the end of the calendar month reporting period for Managers too much time? If so, please explain why and describe any suggested alternative.

- **Q12: Multiple Managers with Investment Discretion.** As noted above, as is the case for Form 13F filers, under Proposed Rule 13f-2, to prevent duplicative reporting of Proposed Form SHO if two or more Managers, each of which is required by Proposed Rule 13f-2 to file Proposed Form SHO for the reporting period, exercise investment discretion with respect to the same securities, only one such Manager must report the information in its report on Proposed Form SHO.

- Please describe any views related to the pros or cons associated with the Commission's proposed approach as described above.

- Will a Manager always be aware of instances in which there is another Manager(s) with investment discretion with respect to the same securities? If yes, how will that Manager be aware of the other Manager(s)? If yes, if there is more than one Manager that has investment discretion with respect to the same securities, how would each manager determine which Manager shall report short position and short position activity pursuant to Proposed Form SHO in order to avoid duplicative reporting?

- Should there be a mechanism that requires Managers to coordinate with one another to avoid duplicative reporting? If yes, please describe. In addition, please describe any alternative approach designed to prevent duplicative reporting by Managers.

- **Q13: Amendments to Proposed Form SHO:** A Manager that determines

that it has filed a Proposed Form SHO that includes inaccurate information must file an amended Proposed Form SHO within 10 calendar days of discovery of the error. Amendments to Proposed Form SHO must restate the Proposed Form SHO in its entirety and provide on the Proposed Form SHO Cover Page prescribed information about the revision being made—including the impact on prior Proposed Form SHO reporting periods. In prescribed circumstances, Managers must notify the Commission staff of the filing of an amended Proposed Form SHO.

○ Please discuss any views regarding the Commission's proposed approach regarding filing amendments to Proposed Form SHO and address the pros and cons, as applicable, of the Commission's proposed approach. In particular:

▪ Should the Commission provide updated data on a rolling basis for more (or less than) 12 consecutive months?

▪ Should Managers notify Commission staff of errors for any data point of greater than, or less than, 25%? Should the Commission flag, with an asterisk or other indicator, updates to published data that are less than 25% of prior published data? Should the Commission use other types of indicators (e.g., asterisk for an update of 25% or greater, or other indicator for update of less than 25%, etc.)?

▪ In filing an amended Proposed Form SHO, should Managers be required to re-file the entire Proposed Form SHO, or should Managers have the opportunity to re-file only the data that is being corrected?

▪ The Commission is proposing to require Managers to notify Commission staff about multiple consecutive Amendments and Restatements to help Commission staff determine if there is a continuing issue with the integrity of that Manager's filings. Should Managers be required to notify Commission staff only if there are a specified number of months of consecutive Amendments and Restatements, e.g., three, four, or five consecutive months?

▪ The Commission is proposing that if a revision reported in an Amendment and Restatement changes a data point reported in the Proposed Form SHO by twenty-five percent (25%) or more, the Manager must notify the Commission staff via email within two (2) business days after filing the Amendment and Restatement. Does two (2) business days provide a Manager with sufficient time to notify the Commission? If no, please explain why not and describe any suggested alternative timeline(s).

▪ The Commission is proposing that, regardless of the scope of the revision being reported, if the data being reported in an Amendment and Restatement affects the data reported on the Proposed Form SHO reports filed for multiple Proposed Form SHO reporting periods, the Manager, within two (2) business days after filing the Amendment and Restatement, must provide the Commission staff via email with notice of such occurrence, and provide an explanation of the reason for the revision. Does two (2) business days provide a Manager with sufficient time to notify the Commission? If no, please explain why not and describe any suggested alternative timeline(s).

On November 18, 2021, the Commission proposed rule 10c-1 under the Exchange Act<sup>86</sup>—a rule designed to increase the transparency and efficiency of the securities lending market by requiring lenders of securities to provide the material terms of securities lending transactions to a registered national securities association, such as FINRA. On [insert date of vote], the Commission reopened the comment period for proposed Rule 10c-1.<sup>87</sup> We encourage commenters to review the Reporting of Securities Loans Proposing Release to determine whether it might affect their comments on this proposing release and Proposed Rule 13f-2 and Proposed Form SHO.

#### **IV. Potential Alternative Approach to Proposed Rule 13f-2 Regarding How the Information Reported on Proposed Form SHO Is Published by the Commission**

As noted above, the Commission's Proposed Rule 13f-2 would require that a Manager provide identifying information including its name and active LEI, if the Manager has an active LEI, when filing Proposed Form SHO through EDGAR. The Commission would collect information from all reporting Managers and publish aggregated information across all Managers reporting in a particular equity security. The Commission, however, seeks comment on the following alternative approach regarding how the information reported on Proposed Form SHO by reporting Managers would be published by the Commission. Under this alternative approach, the Commission would not alter the proposed Reporting Thresholds or the information that would be

reported by a reporting Manager on Proposed Form SHO, as described herein. However, under this alternative, the information reported by a Manager on Proposed Form SHO would be published as it is reported to the Commission, and would not be aggregated with information reported by other Managers. Reported information would therefore be published at the individual Manager level, rather than aggregated across all reporting Managers prior to publication. The reporting Manager's identifying information, including its name and active LEI, if the Manager has an active LEI, would be removed in an effort to anonymize the information published. In anonymizing the reporting Manager's information prior to publication, the Commission would be seeking to balance the above noted calls for additional short sale transparency with, among other things, the above noted concerns regarding potential issuer and investor retaliation against identified short sellers. The Commission remains concerned that such retaliation could result in a reduction in short selling, along with a reduction in the corresponding liquidity and price transparency benefits. The Commission further understands that despite measures designed to help anonymize published information, it may still be possible for market participants to identify certain reporting Managers. For example, it is not uncommon for there to be only one large short seller in an equity security, and under such circumstances, sophisticated traders may be able to link individual short sellers to their short positions reported on Proposed Form SHO through public statements, social media posts, or even rumors.<sup>88</sup> Using Threshold A as described above, the Commission estimates that 32% of reportable equity securities would have only one reporting Manager.

• *Q14: Managers and the Potential Alternative Approach:* Under the potential alternative approach presented, the reported information by a Manager would be published at the Manager level, without aggregation with other reporting Managers, with the reporting Manager's identifying information, including any active LEI, being removed prior to publication.

○ Please discuss the Commission's potential alternative approach, and address the pros and cons, as applicable.

<sup>86</sup> *Reporting of Securities Loans*, Exchange Act Release No. 93613 (Nov. 18, 2021) ("Reporting of Securities Loans Proposing Release").

<sup>87</sup> *Reopening of Comment Period for Reporting of Securities Loans*, Exchange Act Release No. 34-94315 (Feb. 25, 2022).

<sup>88</sup> See generally *infra* Part VIII.D.2.

## V. Proposed Amendment to Regulation SHO To Aid Short Sale Data Collection

The Commission is proposing new Rule 205 of Regulation SHO to facilitate its collection of more comprehensive data on the lifecycle of short sales. Proposed Rule 205 would 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. Specifically, a broker-dealer would be required to mark a purchase order as “buy to cover” if, at the time of order entry, the purchaser (*i.e.*, either the broker-dealer or another person) has a gross short position in such security in the specific account for which the purchase is being made at such broker-dealer. A broker-dealer would be required to mark a purchase order as “buy to cover,” regardless of the size of such purchase order in relation to the size of the purchaser’s gross short position in such security in the account, and regardless of whether the gross short position is offset by a long position held in the purchaser’s account at the time of order entry.<sup>89</sup> If, for example, the purchaser has a gross short position of 100 shares in security ABC in account number 123 at broker-dealer X, then purchases 50 shares of ABC through broker-dealer X in account number 123 (a purchase amount less than the purchaser’s gross short position in the account at broker-dealer X), broker-dealer X would be required to mark the purchase order as “buy to cover.” If the purchase order was instead for 150 shares of ABC in account number 123 (a purchase amount greater than the purchaser’s gross short position in account number 123 at broker-dealer X), broker-dealer X would likewise be required to mark the purchase order as “buy to cover.” The proposed “buy to cover” marking requirement would not impact compliance with, or the operation of, other rules under Regulation SHO, including a broker-dealer’s determination of whether to mark a sale order as “long,” “short,” or “short exempt” pursuant to Rule 200.

There is presently no “buy to cover” order marking requirement, so the Commission does not currently have

regular access to “buy to cover” order marking information. The Commission believes that having “buy to cover” order marking information would provide additional context to the Commission and other regulators regarding the lifecycle of short sales by identifying the timing of purchases that close out, in whole or in part, open short positions in a security. The Commission believes this information would assist in reconstructing market events, and would be useful in identifying and investigating any potentially abusive trading practices including any potential manipulative short squeezes.<sup>90</sup>

To reduce potential burdens and costs to broker-dealers, the proposed rule would require the broker-dealer to determine only whether a purchase is being made for an account at the broker-dealer that has a gross short position in that equity security in that account at the time of the purchase. The Commission believes that this simplified approach would help minimize costs to broker-dealers by allowing short positions held in any accounts other than the purchasing account, as well as offsetting long positions held by the purchaser in the purchasing account or any other account, to be excluded for purposes of the broker-dealer’s “buy to cover” order marking determination. The Commission believes that the resulting data would provide the Commission with an indication of which purchases are potentially associated with a “short squeeze,” where short sellers are pressured to cover their open short positions by purchasing shares as a result of increases in the price of a stock or borrowing costs. Having access to “buy to cover” information would help the Commission identify instances in which an increase in “buy to cover” orders in a particular equity security coincides with an increase in price and/or borrowing costs in the same equity security, and thus identify where “short squeezes” may be occurring. As discussed further below, this data would aid the Commission in reconstructing significant market events related to short selling.

The Commission alternatively considered proposing to require the broker-dealer to look across multiple accounts held by the customer within the broker-dealer itself, if applicable, and/or to its customer’s account(s) held at other firms, if applicable, but

determined that the costs and burdens to the broker-dealer would likely increase significantly under such an approach. With regard to other accounts held by the customer within the broker-dealer itself, the broker-dealer would incur additional costs and burdens in conducting such review. With regard to its customer’s accounts held at other firms, the Commission understands that this information is not typically available to the broker-dealer and might be challenging to obtain. As a result, after considering the potential costs and burdens to broker-dealers, Proposed Rule 205 would require the broker-dealer to determine only whether a purchase is being made for an account at the broker-dealer that has an open short position in that equity security in that account.

The proposed “buy to cover” requirement would likely create one-time programming costs to broker-dealers as well as ongoing costs associated with order marking. The proposed “buy to cover” order mark determination would be distinct from that made by broker-dealers’ existing order marking systems and processes designed to ensure compliance with Rule 200 of Regulation SHO. Thus, broker-dealers would be required to update their respective systems and processes to account for compliance with Proposed Rule 205 (*i.e.*, broker-dealers would likely need to program systems to add an additional field for the “buy to cover” order mark).

While the Commission welcomes any public input on Proposed Rule 205, the Commission asks commenters to consider the following questions.

- Q15: Should Proposed Rule 205 also require the broker-dealer to mark a purchase as “buy to cover” if the person is purchasing in an account that does not have a gross short position, but the person may have gross short positions in other accounts at the same and/or other broker-dealers? Would a purchase in a different account than an account with a gross short position in that security also be reflective of a person’s intent to buy to cover a gross short position in that security? To what extent do short sellers buy to cover short positions by purchasing securities through accounts other than the account holding the short position? Would persons buy to cover securities at accounts at different broker-dealers? How often might such buy to cover orders occur in different accounts or at different broker-dealers? What would be the additional burdens or costs of such an additional requirement?

- Q16: Are there likely to be costs, other than those described in the

<sup>89</sup> Unlike the netting requirements under Rule 200 of Regulation SHO, the “buy to cover” order marking determination under Proposed Rule 205 will be made on a “gross” basis. The Commission believes that this approach would help minimize costs to broker-dealers because it would require them to determine only whether any short position is held by the account on whose behalf the purchase is being effected regardless of whether such short position is offset by any long position in the same security held by the purchaser in the same or any other account.

<sup>90</sup> See *infra* Part VIII.D.1 for a discussion of how the Commission could have used this data to enhance our understanding and recreation of the ‘meme stock’ phenomenon of January 2021.

release, to broker-dealers resulting from the proposed “buy to cover” order marking requirement?

- Q17: Should Proposed Rule 205 require broker-dealers to make the “buy to cover” order marking determination based on the purchaser’s net short position instead of gross short position? What are the costs and benefits associated with each approach?

## VI. Proposal To Amend CAT

In July 2012, the Commission adopted Rule 613 of Regulation NMS, which required national securities exchanges and national securities associations (the “Participants”)<sup>91</sup> to jointly develop and submit to the Commission a national market system plan to create, implement, and maintain a consolidated audit trail (the “CAT”).<sup>92</sup> The goal of Rule 613 was to create a modernized audit trail system that would provide regulators with more timely access to a sufficiently comprehensive set of trading data, thus enabling regulators to more efficiently and effectively reconstruct market events, oversee market behavior, and investigate misconduct. On November 15, 2016, the Commission approved the national market system plan required by the CAT NMS Plan.<sup>93</sup>

Section 6.4(d) of the CAT NMS Plan provides that each Participant, through

<sup>91</sup> The Participants include: BOX Exchange LLC; Cboe BYX Exchange, Inc.; Cboe BZX Exchange, Inc.; Cboe C2 Exchange, Inc.; Cboe EDGA Exchange, Inc.; Cboe EDGX Exchange, Inc.; Cboe Exchange, Inc.; Financial Industry Regulatory Authority, Inc.; Investors’ Exchange LLC; Long-Term Stock Exchange, Inc.; MEMX LLC; Miami International Securities Exchange LLC; MIAX Emerald, LLC; MIAX PEARL, LLC; Nasdaq BX, Inc.; Nasdaq GEMX, LLC; Nasdaq ISE, LLC; Nasdaq MRX, LLC; Nasdaq PHLX LLC; The Nasdaq Stock Market LLC; New York Stock Exchange LLC; NYSE American LLC; NYSE Arca, Inc.; NYSE Chicago, Inc.; and NYSE National, Inc.

<sup>92</sup> See Exchange Act Release No. 67457 (July 18, 2012), 77 FR 45722 (Aug. 1, 2012) (“Rule 613 Adopting Release”).

<sup>93</sup> Exchange Act Release No. 79318 (Nov. 15, 2016), 81 FR 84696, (Nov. 23, 2016) (“CAT NMS Plan Approval Order”). The CAT NMS Plan is Exhibit A to the CAT NMS Plan Approval Order. See CAT NMS Plan Approval Order, 81 FR at 84943–85034. The CAT NMS Plan functions as the limited liability company agreement of the jointly owned limited liability company formed under Delaware state law through which the Participants conduct the activities of the CAT (the “Company”). Each Participant is a member of the Company and jointly owns the Company on an equal basis. The Participants submitted to the Commission a proposed amendment to the CAT NMS Plan on August 29, 2019, which they designated as effective on filing. Under the amendment, the limited liability company agreement of a new limited liability company named Consolidated Audit Trail, LLC serves as the CAT NMS Plan, replacing in its entirety the CAT NMS Plan. See Exchange Act Release No. 87149 (Sept. 27, 2019), 84 FR 52905 (Oct. 3, 2019).

its Compliance Rule,<sup>94</sup> must require Industry Members<sup>95</sup> to record and electronically report certain information to the CAT Central Repository, which means that any broker-dealer that is a member of a national securities exchange or a member of a national securities association must report the lifecycle of an order from original receipt or origination, modification, cancellation, routing, execution (in whole or in part) and allocation of an order, and receipt of a routed order to the CAT.<sup>96</sup> This provides regulators, including the Commission, access to comprehensive information regarding the lifecycle of orders, from origination to execution, as well as the post-execution allocation of shares.

Broker-dealers, through the Compliance Rule adopted pursuant to the CAT NMS Plan, are required to report some short sale order data, including for sell orders, whether an order is long, short, or short exempt,<sup>97</sup> but not other short sale order data, including when a buy order is designed to close out an existing short position, or whether a market participant is relying on the bona fide market making exception of the Regulation SHO locate requirement in Rule 203. To supplement the short sale related data that would be reported by Managers to the Commission pursuant to Proposed Rule 13f–2 and on Proposed Form SHO, the Commission now believes it is appropriate to amend the CAT NMS Plan to require the Participants to require CAT reporting firms to report certain additional short sale related data to the CAT, as discussed below.

### A. “Buy to Cover” Information

First, the Commission proposes that Industry Members be required to report to the CAT “buy to cover” information, which would be collected pursuant to Regulation SHO through Proposed Rule 205 as discussed in Part IV above. Specifically, the Commission proposes to amend Section 6.4(d)(ii) of the CAT NMS Plan by adding new subparagraph 6.4(d)(ii)(D) which would require the

<sup>94</sup> “Compliance Rule” means, with respect to a Participant, the rule(s) promulgated by such Participant as contemplated by Section 3.11 of the CAT NMS Plan. See CAT NMS Plan, Section 1.1.

<sup>95</sup> An “Industry Member” means a member of a national securities exchange or a member of a national securities association. See CAT NMS Plan, Section 1.1.

<sup>96</sup> “Central Repository” means a repository responsible for the receipt, consolidation, and retention of all information reported to the CAT pursuant to Rule 613 of Regulation NMS and the CAT NMS Plan. See CAT NMS Plan, Section 1.1.

<sup>97</sup> Section 1.1 of CAT NMS Plan defines “Material Terms of the Order,” which includes, for sell orders, “whether the order is long, short, [or] short exempt[.]”

Participants to update their Compliance Rules to require Industry Members to report for the original receipt or origination of an order to buy an equity security, whether such buy order is for an equity security that is a “buy to cover” order as defined by Rule 205(a) of Regulation SHO (17 CFR 242.205(a)).<sup>98</sup> This provision would require Industry Members to identify “buy to cover” equity orders received or originated by Industry Members and Customers<sup>99</sup> as “buy to cover” orders in order receipt and order origination reports submitted to the CAT Central Repository.

The originally proposed CAT NMS Plan would have required all CAT Reporters (*i.e.*, Participants and Industry Members) to report an “open/close indicator” as a “Material Term” on all orders, as required by Rule 613.<sup>100</sup> This open/close indicator could have been used to identify “buy to cover” equities orders, because it would have provided information on whether an order is to open or close an existing position in a security. However, when the Commission approved the CAT NMS Plan, it determined that it was appropriate to remove the proposed requirement that an open/close indicator be reported as part of the Material Terms of the Order for equities and Options Market Maker quotations.<sup>101</sup> At the time, three commenters objected to the requirement that CAT Reporters report an open/close indicator for equities transactions. Among other things, commenters noted that an “open/close indicator” is not used for equities, and believed that an additional or separate cost-benefit analysis should be done before it be required for equities.<sup>102</sup> One of these commenters stated that including an “open/close indicator” for equities would require “significant process changes and involve parties other than CAT Reporters, such as buy-side clients, OMS/EMS vendors, and others.”<sup>103</sup> Ultimately, the Commission decided that limiting the open/close indicator to

<sup>98</sup> See Proposed Section 6.4(d)(ii)(D) of the CAT NMS Plan; Proposed Rule 205(a) of Regulation SHO, 17 CFR 242.205(a).

<sup>99</sup> Section 1.1 of the CAT NMS Plan defines the term “Customer” as (a) the account holder(s) of the account at a registered broker-dealer originating the order; and (b) any person from whom the broker-dealer is authorized to accept trading instructions for such account, if different from the account holder(s). See also, 17 CFR 242.613(j)(3).

<sup>100</sup> See 17 CFR 242.613(j)(7) (defining “Material Terms of the Order” to include “open/close indicator”); Exchange Act Release No. 77724 (Apr. 27, 2016); 81 FR 30614, 30680 (May 17, 2016).

<sup>101</sup> See CAT NMS Plan Approval Order, 81 FR at 84747.

<sup>102</sup> See *id.*

<sup>103</sup> See *id.*

listed options was “reasonable,” acknowledging concerns in other areas, “including the lack of a clear definition of the term for equities transactions.”<sup>104</sup>

The Commission believes it is now appropriate to require “buy to cover” CAT reporting by Industry Members. Unlike the “open/close indicator” requirement in Rule 613, which was included in the definition Material Terms of the Order, the Commission is proposing to only require reporting by Industry Members on a subset of CAT reports related to equity buy orders; specifically, order receipt and order origination reports. Pursuant to the CAT NMS Plan, Material Terms of the Order are required to be reported to the CAT for numerous other events in an order’s lifecycle, including routing of an order, receipt of an order that has been routed, order modifications, order cancellations, and executions of orders, in whole or in part.<sup>105</sup> In addition, the proposed provisions only require “one-sided” CAT reporting—that is, except in circumstances where an Industry Member originates a “buy to cover” order and submits it to another Industry Member as a Customer (requiring both Industry Members to report “buy to cover” information as part of order origination and order receipt reports, respectively), only one CAT Reporter is required to report that an order is a “buy to cover” order to the CAT. In addition, the “buy to cover” information does not have the same definitional issues as an “open/close indicator” because “buy to cover” is being added to Regulation SHO, as discussed in Part IV above. “Buy to cover” is also a more narrow concept than an “open/close indicator” and would require only a change to CAT reporting for a subset of equity buy orders, and thus would not affect CAT reporting for a majority of equity orders, and would not change CAT reporting relating to options trading at all. Because of this, the costs associated with the reporting of “buy to cover” information to the CAT should be

<sup>104</sup> See *id.* The Commission believes that the proposed reporting requirements here do not have the same issue regarding the lack of a clear definition because, unlike simply requiring an “open/close indicator,” the proposed reporting requirements more clearly define when a “buy to cover” indicator would be required to be reported.

<sup>105</sup> See Section 6.3(d) and 6.4(d) of the CAT NMS Plan. Because “buy to cover” information will only be available on order receipt and order origination reports, Commission staff and regulators will have to do more analysis to identify certain CAT records (*e.g.*, order routes, modifications, cancellations, and executions) as associated with a “buy to cover” order since Industry Members would not be required to report “buy to cover” information on these CAT reports, but the Commission believes this inefficiency is justified by the reduction in burden of reporting for Industry Members.

substantially less than the costs of reporting an “open/close indicator” would have been.

The Commission believes that requiring proposed reporting of “buy to cover” information to the CAT would provide valuable information for the Commission and other regulators in investigations and reconstruction of market events. The Commission and regulators currently do not have ready access to “buy to cover” information because they do not regularly receive Industry Member and customer position information, and it is only possible to identify “buy to cover” orders if the Commission or regulators independently obtain position information, such as by obtaining trade data and blotters from Industry Members. Even then, it is difficult to identify and track equity orders that are “buy to cover.” Ready access to “buy to cover” information in the CAT would allow regulators to more easily determine whether a purchase of an equity security increases the equity exposure of an Industry Member or Customer and whether the buy covers a short position. Ready access to information used to determine whether an order adds to an existing position or covers an existing short position would assist in detecting and investigating portfolio pumping, short selling abuses, short squeezes marking the close, potential manipulation, insider trading, or other rule violations, such as violations of Rule 105 of Regulation M, which generally governs when short sellers can participate in a follow-on offering.<sup>106</sup> This information would also enhance the Commission staff’s and regulators’ analysis and interpretations of the impact short selling and “buys to cover” have on the market, by more accurately lining up trading activity data available in the CAT with security price changes to examine and study the impact of “short squeezes” on equity prices.

#### *B. Reliance on Bona Fide Market Making Exception*

The Commission also proposes to require CAT reporting firms that are reporting short sales to indicate whether such reporting firm is asserting use of the bona fide market making exception under Regulation SHO for the locate requirement in Rule 203 for the reported short sales. Specifically, the Commission proposes to amend Section 6.4(d)(ii) of the CAT NMS Plan to add a new subparagraph (E) which would require Participants to update their Compliance Rules to require Industry

<sup>106</sup> 17 CFR 242.105.

Members to report to the CAT, for the original receipt or origination of an order to sell an equity security, whether the order is a short sale effected by a market maker in connection with bona-fide market making activities in the security for which the exception in Rule 203(b)(2)(iii) of Regulation SHO is claimed.<sup>107</sup> The Commission believes that this information would provide valuable data to both the Commission and other regulators regarding the use of this exception by market participants, an exception which allows a broker-dealer (and consequently, a short seller) to avoid or delay certain requirements of Regulation SHO, including the locate and close out requirements.

Rule 203(b)(1) of Regulation SHO generally prohibits a broker-dealer from accepting a short sale order in an equity security from another person, or effecting a short sale in an equity security for its own account, unless the broker-dealer (i) has borrowed the security, (ii) has entered into a bona-fide arrangement to borrow the security, or (iii) has reasonable grounds to believe that the security can be borrowed so that it can be delivered on the date delivery is due.<sup>108</sup> This is generally referred to as the locate requirement. Rule 203(b)(2) of Regulation SHO provides an exception to the locate requirement for short sales effected by a market maker in connection with “bona fide” market making activities.<sup>109</sup> To qualify for the bona fide market making exception, however, a firm must be engaged in bona fide market making at the time of the short sale in question.<sup>110</sup> The Commission adopted this narrow exception to Regulation SHO’s locate requirement for market makers that may need to facilitate customer orders in a fast moving market without possible

<sup>107</sup> See proposed Section 6.4(d)(ii)(E) of the CAT NMS Plan.

<sup>108</sup> 17 CFR 242.203(b)(1).

<sup>109</sup> 17 CFR 242.203(b)(2). The Commission has provided guidance on indicia of bona fide market making activities eligible for the locate exception. See Regulation SHO Adopting Release, *supra* note 4 (setting forth examples of activities that would not be considered to be bona fide market making activities); see also, Exchange Act Release No. 58775 (Oct. 14, 2008), 73 FR 61690, 61698–99 (Oct. 17, 2004) (adopting amendments to Regulation SHO and providing additional guidance on what constitutes bona fide market making). Whether activity is considered bona fide market making activity for purposes of Regulation SHO will “depend on the facts and circumstances of the particular activity” in question, and only market makers engaged in bona fide market making activity in the security at the time they effect a short sale are eligible for the locate exception. See *id.* at 61699.

<sup>110</sup> See *id.* at 61699.

delays associated with complying with such a requirement.<sup>111</sup>

The Commission previously proposed to require a locate identifier for short sales to be reported to the CAT in Rule 613, but removed this requirement, among others, from the adopted rule text.<sup>112</sup> At the time, the Commission believed that the CAT would still achieve significant benefits without requiring the routine recording and reporting of these specific data elements to the CAT, that the Commission could obtain information from a broker-dealer in a follow-up request if necessary, and that the benefits of having these specific data elements in the CAT would be minimal.<sup>113</sup> However, with greater experience and access to CAT Data, the Commission now believes that it is important for regulatory and surveillance purposes to capture information regarding the use of the narrow bona fide market making exception to Regulation SHO and no longer believes that the benefits of having this specific data element in the CAT would be minimal. The Commission also believes that requiring this reporting would impact substantially fewer CAT Reporters than the original Rule 613 proposal, which would have required locate identifiers for all short sales.

There are a number of settled enforcement actions against firms in connection with their use of the exception.<sup>114</sup> Firms are not permitted to use the bona fide market making exception for, among other things, speculative selling strategies or investment purposes of the broker-dealer that are disproportionate to the usual market making patterns or practices of the broker-dealer in that security.<sup>115</sup> Firms that do not need to obtain a locate prior to effecting a short sale, on the basis of the bona fide market making exception, have a competitive advantage over firms that are required to

obtain a locate because these firms can trade more quickly and more easily adjust to or take advantage of changing market conditions. Currently, the Commission must request information from a broker-dealer to determine which orders have been submitted pursuant to the bona fide market making exception. The Commission believes that requiring Industry Members to identify short sales for which they are claiming the bona fide market making exception would provide the Commission and other regulators an additional tool to determine whether such activity qualifies for the exception, or instead could be indicative of, for example, proprietary trading instead of bona fide market making.<sup>116</sup>

While Regulation SHO does not require market maker firms to record whether they are relying upon the exception in Rule 203(b)(2)(iii) of Regulation SHO for bona fide market making activity, the Commission believes that market maker firms that engage in equity trading should be able to identify what trading activity qualifies for the exception so a firm can demonstrate its eligibility for the asserted exception. Thus, the Commission believes that this information should be easily reportable to the CAT by Industry Members that do rely upon this exception. As noted above, there is a narrow exception to Regulation SHO's locate requirement for bona fide market making in Rule 203(b)(2)(iii), and a firm should know at the time that it submits a sell short order without performing a locate pursuant to the bona fide market making exception

<sup>116</sup> Depending on the circumstances, the proposed requirement to report the use of the bona fide market making exception to Regulation SHO at order initiation could either reduce or increase compliance costs to market participants. In some cases, for example, examiners identifying market participants for examination of prolonged fails to deliver would be able to readily determine that such fails were due to bona fide market making activity, obviating the need to examine the particular market participant based on such fails alone. In other circumstances, by contrast, an indication of reliance on the bona fide market maker exception could be flagged for examination if it appears that the market participant is unlikely to be engaging in bona fide market making activities to the extent of the fails to deliver that have occurred—for instance, a market participant that does not post any quotes in the security for which the fails are occurring that has indicated it is relying on the bona fide market making exception in Regulation SHO. The Commission does not believe requiring the indicator will have a chilling effect on market making generally. Rather, the indicator will be used to identify whether a short sale for which a market participant is asserting the bona fide market making exception has been effected in connection with bona fide market making activities such that the narrow exception to a narrow exception to the locate requirement of Regulation SHO applies.

whether or not it qualifies for the exception.

### C. Request for Comments

While the Commission welcomes any public input on the Proposal to Amend CAT, the Commission asks commenters to consider the following questions.

- Q18: *Proposal to Amend CAT:* Under the Proposal to Amend CAT, Industry Members would be required to report certain additional short sale related data to the CAT, as described above.

- Are the proposed reporting requirements related to “buy to cover” and the bona fide market making exception sufficiently clear and understandable to allow Industry Members to collect and report the necessary information? Are the proposed requirements sufficiently clear for the Participants to implement the necessary changes to their Compliance Rules? Are the proposed requirements sufficiently clear for the CAT Plan Processor to implement necessary systems and technical changes and implement revised technical or other specifications required to facilitate and allow for the reporting of these new CAT data elements?

- Please describe any technical challenges or concerns relating to the reporting, capture and processing of the proposed new information.

- Are there concerns relating to the collection of “buy to cover” information by executing brokers to report to the CAT? What difficulties would Industry Members face in reporting their own proprietary “buy to cover” orders? Customer “buy to cover” orders? Are there other concerns relating to the reporting of “buy to cover” information to the CAT? If so, please describe those concerns and the specific issues or other burdens that should be considered by the Commission.

- Are there concerns relating to the collection of or reporting reliance on the bona fide market making exception of Regulation SHO to the CAT? Would it be difficult for market making firms to identify what orders are originated pursuant to the bona fide market making exception? If so, please describe those concerns and the specific issues or other burdens that should be considered by the Commission.

- The proposal would require broker-dealers to identify, at order origination, whether they are asserting use of the bona fide market making exception to the locate requirement. Should the Commission also require identification of purchases by broker-dealers to close out fails to deliver resulting from bona fide market making under Rule 204 of

<sup>111</sup> See Regulation SHO Adopting Release, *supra* note 4, at 48015 n.67.

<sup>112</sup> See Rule 613 Adopting Release, 77 FR at 45751.

<sup>113</sup> See *id.*

<sup>114</sup> See, e.g., In the Matter of Wilson-Davis & Company, Inc., Respondent, Order Making Findings and Imposing Remedial Sanctions and a Cease-and-Desist Order Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934, Release No. 80533 (April 26, 2017) (settled matter); In the Matter of Jeffrey A. Wolfson, Robert A. Wolfson, and Golden Anchor Trading II, LLC (n/k/a Barabino Trading, LLC), Respondents, Order Making Findings and Imposing Remedial Sanctions and Cease-and-Desist Order Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934 as to Robert A. Wolfson and Golden Anchor Trading II, LLC (n/k/a Barabino Trading, LLC), Release No. 67450 (July 17, 2012) (settled matter).

<sup>115</sup> See Regulation SHO Adopting Release, *supra* note 4, at 48015.

Regulation SHO?<sup>117</sup> If so, please describe the costs and benefits of such an approach.

○ Is there any other short sale related data that should be reported to the CAT? If so, please describe the costs and benefits of reporting that data.

• Q19: *Cost of Reporting*: Under the Proposal to Amend CAT, Industry Members would be required to report certain additional short sale related data to the CAT, as described above.

○ Please describe any views related to the anticipated costs or other burdens, as well as benefits, associated with reporting under the Proposal to Amend CAT, and identify the specific costs or other burdens that should be considered by the Commission.

## VII. Paperwork Reduction Act Analysis

### A. Background

Certain provisions of Proposed Rule 13f-2, Proposed Form SHO, Proposed Rule 205, and the Proposal to Amend CAT contain new “collection of information” requirements within the meaning of the Paperwork Reduction Act of 1995 (“PRA”).<sup>118</sup> The Commission is submitting the proposed collection of information to the Office of Management and Budget (“OMB”) for review in accordance with the PRA.<sup>119</sup> The title for the collection of information is: “Proposal to Enhance Short Sale Data.” OMB has not yet assigned a control number to the collection of information. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number. The requirements of this collection of information are mandatory for Managers under Proposed Rule 13f-2 and Proposed Form SHO, for broker-dealers under Proposed Rule 205, and Plan Participants and CAT reporting firms under the Proposal to Amend CAT.

As discussed above,<sup>120</sup> Proposed Rule 13f-2 and related Proposed Form SHO are designed to provide greater

<sup>117</sup> Rule 204 requires a participant of a registered clearing agency to deliver securities to a registered clearing agency for clearance and settlement on a long or short sale transaction in any equity security by settlement date, or to immediately close out a failure to deliver by borrowing or purchasing securities of like kind and quantity by the applicable close out date. For a short sale, a participant must close out a failure to deliver by no later than the beginning of regular trading hours on T+3. For a long sale, or for activity that is attributable to “bona fide” market making activities, a participant must close out a failure to deliver by no later than the beginning of regular trading hours on T+5.

<sup>118</sup> 44 U.S.C. 3501 *et seq.*

<sup>119</sup> 44 U.S.C. 3507(d) and 5 CFR 1320.11.

<sup>120</sup> See *supra* Part III.A.

transparency of short sale related data to regulators, investors and other market participants by requiring certain Managers to file monthly on Proposed Form SHO, through EDGAR in Proposed Form SHO-specific XML, certain short position and activity data. Under Proposed Rule 13f-2 and Proposed Form SHO, only those Managers that meet a specified Reporting Threshold for an equity security would be required to file Proposed Form SHO.

Proposed Rule 205 would establish a new “buy to cover” order marking requirement for purchase orders effected by a broker-dealer that applies if, at the time of order entry, the account for which the purchase order is placed has a gross short position in the security being purchased.<sup>121</sup> Such information would provide additional context to the Commission and other regulators regarding the lifecycle of short sales, would assist in reconstructing market events, and would be useful in identifying and investigating potentially abusive short selling practices. The Commission believes that many broker-dealers will have existing order marking systems and processes, and will be familiar with how to adapt and update them to accommodate new order marks.

The Proposal to Amend CAT is intended to supplement the short sale related data that would be reported by certain Managers to the Commission pursuant to Proposed Rule 13f-2 and Proposed Form SHO. As discussed above, the Commission proposes that CAT reporting firms be required to report “buy-to-cover” information to the CAT and believes that this information would allow Commission and SRO staff to review the life of a short sale, from creation to termination, which would assist in reconstructing unusual market events such as the market volatility in early 2021.<sup>122</sup> In addition, the Commission proposes to require CAT reporting firms that are reporting short sales to indicate whether such reporting firm is asserting use of the bona fide market making exception for the “locate” requirement in Rule 203 under Regulation SHO for the reported short sales. The Commission believes that this information would provide valuable data to both the Commission and other regulators regarding the use of the bona fide market making exception by market participants. The Proposal to Amend CAT could potentially affect all CAT reporting firms, but the Commission believes that the proposal will primarily affect those CAT reporting firms that engage in short sale activity with

<sup>121</sup> See *supra* Part V.

<sup>122</sup> See *supra* Part VI.A.

subsequent purchases to cover such short positions.

Given the differences in the information collections applicable to these parties, the burdens applicable to Managers, broker-dealers and CAT reporting firms are separated in the analysis below.

### B. Burdens for Managers Under Proposed Rule 13f-2 and the Related Proposed Form SHO

#### 1. Applicable Respondents

As discussed above, Proposed Rule 13f-2 and Proposed Form SHO would require Managers that trigger a Reporting Threshold to file monthly via EDGAR, on Proposed Form SHO, certain short position and activity data. Under Section 13(f)(6)(A) of the Exchange Act and for purposes of Proposed Rule 13f-2, Managers would include any person, other than a natural person, investing in or buying and selling securities for its own account, and any person (including a natural person) exercising investment discretion with respect to the account of any other person.<sup>123</sup> Thus, the requirements of Proposed Rule 13f-2 could apply, for example, to investment advisers that exercise investment discretion over client assets, including investment company assets; broker-dealers; insurance companies; banks and bank trust departments; and pension fund managers or corporations that manage corporate investments or employee retirement assets. Of those, the Commission estimates that, each month, approximately 1,000 Managers would trigger a Reporting Threshold for at least one security, and therefore be required to file a Proposed Form SHO.<sup>124</sup>

#### 2. Burdens and Costs

The Commission believes that the burden associated with Proposed Rule

<sup>123</sup> See also Instructions to Form 13F.

<sup>124</sup> This estimate is similar to the estimate provided in the *Disclosure of Short Sales and Short Positions by Institutional Investment Managers*, 73 FR at 61686. However, the number of estimated Proposed Form SHO filers represents a monthly, as opposed to weekly, filing, and therefore the Commission estimates fewer overall filings per month. Additionally, the estimate accounts for the estimate by the Commission staff that 346 Form SH filers would have been required to file had a threshold of 2.5% of shares outstanding or \$10 million position dollar value been imposed during the analyzed time period. The estimate of 1,000 is higher than the 346 estimated Form SH filers to account for: (1) Managers with discretion over less than \$100 million, which were not required to file Form SH; (2) the fact that Form SH was only required to be filed for 13(f) securities as opposed to all equity securities of both reporting and non-reporting issuers; and (3) the fact that Form SH did not include a second, lower threshold (Threshold B) for short positions in securities of non-reporting issuers.

13f-2 and the related Proposed Form SHO reporting in EDGAR would be similar to a Manager's reporting requirements for former Form SH. In October 2008, the Commission adopted interim temporary Rule 10a-3T, which required institutional investment managers that exercise investment discretion with respect to accounts holding Section 13(f) securities having an aggregate fair market value of at least \$100 million to file Form SH with the Commission following a calendar week in which it effected a short sale in a Section 13(f) security, with some exceptions. Form SH included information on short sales and positions of Section 13(f) securities, other than options.<sup>125</sup> With respect to each applicable Section 13(f) security, the Form SH filing identified the issuer and CUSIP number of the relevant security and required the Manager's start of day short position, the number and value of securities sold short during the day, the end of day short position, the largest intraday short position, and the time of the largest intraday short position.<sup>126</sup> In adopting interim temporary Rule 10a-3T, which required certain Managers to file weekly nonpublic reports via Form SH, the Commission believed that Managers would spend an estimated 20 hours to prepare and file each Form SH.<sup>127</sup>

While recognizing that the information required under former Form SH differs from that required under Proposed Form SHO, the Commission believes that both forms require the reporting of short sale related data of similar depth and complexity.<sup>128</sup> However, Proposed Rule 13f-2 would require monthly reporting if certain conditions are met, as opposed to the weekly reporting required by Form SH for Managers that effected short sales within the preceding week,<sup>129</sup> which is anticipated to decrease the overall volume of reports required to be filed by

Managers. Accordingly, the Commission believes that the burden associated with preparing and filing Proposed Form SHO in EDGAR would be approximately 20 hours per filing, consistent with that of former Form SH. The Commission further estimates that Managers would collectively spend approximately 240,000 hours per year to comply with the reporting requirements of Proposed Rule 13f-2.<sup>130</sup> The Commission estimates that the hourly cost of internal expertise required for each filing would be \$217.55, which includes a blended calculation of the estimated hourly rate for a compliance attorney, senior programmer, and in-house compliance clerk.<sup>131</sup> Taken together the estimated burden hours and hourly rate for the filing of Proposed Form SHO result in an estimated annual cost to the industry of \$52,212,000.<sup>132</sup> The Commission, however, recognizes that advances in technology over time could result in Managers spending less time preparing and filing Proposed Form SHO than is estimated above.<sup>133</sup>

The Commission also anticipates that most Managers will file Proposed Form SHO directly in the structured XML-

based data language for Proposed Form SHO,<sup>134</sup> rather than using the fillable web form provided by EDGAR, resulting in some limited additional costs for each filing.<sup>135</sup> The Commission believes that Managers that file Proposed Form SHO using a structured XML-based data language could incur an additional burden of 2 hours of work by a programmer,<sup>136</sup> at an estimated cost of \$540.<sup>137</sup> The Commission further estimates that Managers would collectively spend up to approximately 24,000 hours and \$6,480,000 per year to file Proposed Form SHO directly in a structured XML-based data language.<sup>138</sup> The Commission also estimates that a similar, additional burden of 2 hours of work by a programmer per filing would apply to Managers filing an amended Form SHO directly in a structured XML-based data language.

The Commission estimates that approximately 3.5% of the Managers that file Proposed Form SHO each month would also file an amended Proposed Form SHO, resulting in an

<sup>130</sup> 20 hours per filing × 1,000 filings by Managers each month × 12 months = 240,000 hours.

<sup>131</sup> The \$217.55 wage rate reflects current estimates of the blended hourly rate for an in-house compliance attorney (\$368), a senior programmer (\$334) and in-house compliance clerk (\$71). \$217.55 is based on the following calculation:  $((\$368) + ((\$334 + \$71) \div 2) \times 10) \div 11 = \$217.55$ . The estimated proportion of compliance attorney (1/11th) to senior programmer and in-house compliance clerk (10/11ths) time burden is based on commenter input and computation of the estimated burden for the filing of Form 13F-HR. See *Electronic Submission of Applications for Orders*, Exchange Act Release No. 93518 (Nov. 4, 2021), 86 FR 64839 (Nov. 19, 2021) at 64860-61 ("Electronic Submission of Applications for Orders"). The \$368 per hour and \$334 per hour figures for a compliance attorney and a senior programmer, respectively, are based on salary information for the securities industry compiled by the Securities Industry and Financial Markets Association's Office Salaries in the Securities Industry 2013 ("SIFMA Report"), modified by Commission staff to account for an 1800-hour work year and inflation, and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead. The \$71 per hour figure for a compliance clerk is based on salary information from the SIFMA Report, modified by Commission staff to account for an 1800-hour work-year and inflation, and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead. See Exchange Act Release No. 89290 (July 10, 2020), 85 FR 46016 (July 31, 2020) ("Proposed Reporting Threshold for Institutional Investment Managers").

<sup>132</sup> 20 hours per filing × 1,000 filings by Managers each month × 12 months × \$217.55 per hour = \$52,212,000.

<sup>133</sup> See *Electronic Submission of Applications for Orders*, 86 FR at 64859 (stating that "[c]ommenters stated that the advances in technology have made the process of completing and filing Form 13F highly automated, reducing the time and external costs to managers in complying with this requirement.").

<sup>134</sup> The Commission believes most Managers would be familiar with other EDGAR Form-specific XML data languages, the use of which is required for the filing (by Managers that exercise investment discretion with respect to accounts holding 13(f) Securities having an aggregate fair market value on the last trading day of any month of any calendar year of at least \$100 million) of Form 13F. See *Frequently Asked Questions About 13F*, available at <https://www.sec.gov/divisions/investment/13ffaq.htm>. In order to achieve a conservative estimate of industry costs, the Commission estimates that all of the 1,000 Managers estimated to file Proposed Form SHO each month will do so directly using the structured XML-based data language rather than the fillable web form provided by EDGAR.

<sup>135</sup> See Investment Company Act Release No. 34441 (Dec. 15, 2021) (proposing release) at 123-125, available at <https://www.sec.gov/rules/proposed/2021/ic-34441.pdf> (stating that, in the context of money market funds filing Form N-CR, the use of the XML-based data language for that Form may result in "some additional reporting costs related to adjusting their systems to a different data language" but that such changes "may reduce costs and introduce additional efficiencies for money market funds already accustomed to reporting using structured data and may reduce overall reporting costs in the longer term.").

<sup>136</sup> The 2 hour estimated burden is consistent with similar estimates for the use of structured XML data formats for the filing of Form N-CR and Form 24F-2. See Investment Company Act Release No. 34441 (Dec. 15, 2021) at 282 Table 10. See also, Exchange Act Release No. 88606 (Apr. 8, 2020), 85 FR 33290, 33329 n.439 (June 1, 2020) (stating that "[w]e assume that the burden of tagging Form 24F-2 in a structured XML format would be 2 hours for each filing.").

<sup>137</sup> Based on industry sources, Commission staff previously estimated that the average hourly rate for technology services in the securities industry (outside senior programmer or systems programmer) is \$270. See Exchange Act Release No. 83062 (Apr. 18, 2018), 83 FR 21574, 21653 n.493 (May 9, 2018) ("Regulation Best Interest Proposing Release").

<sup>138</sup> 2 hours per filing × \$270 per hour × 1,000 filings each month × 12 months = \$6,480,000.

<sup>125</sup> See *supra* note 35.

<sup>126</sup> Form SH was adopted in the wake of the 2008 financial crisis, and remained in effect until July 2009.

<sup>127</sup> See *Disclosure of Short Sales and Short Positions by Institutional Investment Managers*, 73 FR at 61686 (Stating that, "[t]he 20 hour per filing estimate is based on data received from a small sample of actual filers and a random sample of filings conducted by our Office of Economic Analysis.").

<sup>128</sup> Under Form SH, Managers who met the applicable threshold and effected a short sale in a Section 13(f) security in the preceding week were required to file a report identifying the opening short position, closing short position, largest intraday short position, and the time of the largest intraday short position, for that security during each calendar day of the prior week. Exchange Act Release No. 58591 (Sept. 18, 2008), 73 FR 55175, 55176 (Sept. 24, 2008).

<sup>129</sup> See *id.*



additional burden and cost for an estimated 35 Managers each month.<sup>139</sup> The additional burden could take up to the original 20 hours to process and file, as it would require the filing of an entirely new Proposed Form SHO.<sup>140</sup>

The associated wage rate would also be consistent with the cost of expertise required to complete the original Proposed Form SHO, estimated to be \$217.55 per hour.<sup>141</sup> The Commission also estimates that each amended

Proposed Form SHO would be filed directly using a structured XML-based data language, resulting in a corresponding additional burden of 2 hours of work by a programmer per amended Proposed Form SHO filing.

PRA TABLE 1—ESTIMATED MANAGER BURDEN AND COSTS ASSOCIATED WITH PROPOSED FORM SHO REPORTING

	Managers (monthly)	Proposed Form SHO reports processed and filed (annual)	Hours needed to process and file Proposed Form SHO (avg.)	Total industry burden hours to process and file Proposed Form SHO (annual)	Wage rate (Avg.)	Total industry cost burden (annual)
Proposed Form SHO Filings .....	1,000	12,000	20	240,000	\$217.55	\$52,212,000
Use of Structured XML-Based Data Language .....	1,000	12,000	2	24,000	270	6,480,000
Amended Proposed Form SHO Filings .....	35	420	20	8,400	217.55	1,827,420
Use of Structured XML-Based Data Language .....	35	420	2	840	270	226,800
<b>Total .....</b>				<b>273,240</b>		<b>60,746,220</b>

In addition to the costs associated with the reporting burden, the Commission believes that Managers could incur an initial technology-related burden of 325 hours, at an hourly estimated wage rate of \$320.30,<sup>142</sup> for an estimated total cost of \$104,097.50 per Manager,<sup>143</sup> to update their current systems to capture the required information, and automate and facilitate the completion and filing of Proposed Form SHO. The Commission generally believes that the type of Managers that

would trigger a Reporting Threshold would likely have sophisticated technologies and would be able to implement systems to help automate the reporting requirements of Proposed Rule 13f-2. In particular, the estimate of 325 initial technology-related burden hours for Managers filing Proposed Form SHO is based on the estimated initial filing burden (325 hours) for large hedge fund advisers<sup>144</sup> to fulfill proposed amendments to the reporting requirements for Form PF,<sup>145</sup> and is

similar to the initial technological infrastructure-related burden (355 hours) for the proposed security-based swap position reporting requirements of proposed Rule 10B-1(a).<sup>146</sup> While Managers most likely have other existing reporting obligations, the Commission recognizes that Managers may need to update their systems to ensure timely and accurate filing of the specific information required under Proposed Form SHO.

PRA TABLE 2—ESTIMATED MANAGER BURDEN AND COSTS ASSOCIATED WITH PROPOSED FORM SHO INITIAL TECHNOLOGY PROJECTS

	Managers with proposed Form SHO reportable short interest positions	Number of hours needed for initial technology projects (avg.)	Industry burden hours for initial technology projects	Wage rate (avg.)	Total industry cost burden
Proposed Form SHO Initial Technology Projects .....	1,000	325	325,000	\$320.30	\$104,097,500

In making its estimates for the population of Managers that may be required to file a Proposed Form SHO, the Commission notes that its estimate

may be over-inclusive of the number of Managers that can reasonably be expected to be covered. This is highlighted by the estimate that only

346 Form SH filers would have had to file a report if one of the proposed Reporting Thresholds for Proposed Form SHO—\$10 million or 2.5% of

<sup>139</sup> The estimate of 3.5% of Regulation SHO filers that are anticipated to file an amended Proposed Form SHO is based on the frequency of recent filings of amended Form 13F. See Exchange Act Release No. 93518 (Nov. 4, 2021), 86 FR 64839, 64860-61 Table 5 Notes 7, 8, and 10 (Nov. 19, 2021) (estimating a total of 5,466 Form 13F-HR filings, 1,535 Form 13F-NT filings, and 244 Form 13F amendment filings (244 ÷ 7,001 = 3.5%) and noting that “[t]his estimate is based on the number of Form 13F amendments filed as of December 2019.”).

<sup>140</sup> See Form SHO, Special Instructions at 4.

<sup>141</sup> See *supra* note 131.

<sup>142</sup> The Commission estimates that, of a total estimated burden of 325 hours, approximately 195 hours will most likely be performed by compliance

professionals and 130 hours will most likely be performed by programmers working on system configuration and reporting automation. Of the work performed by compliance professionals, we anticipate that it will be performed equally by a compliance manager at a cost of \$316 per hour and a senior risk management specialist at a cost of \$365 per hour. Of the work performed by programmers, we anticipate that it will be performed equally by a senior programmer at a cost of \$334 per hour and a programmer analyst at a cost of \$246 per hour. ((((\$316 per hour × 0.5) + (\$365 per hour × 0.5)) × 195 hours) + ((((\$334 per hour × 0.5) + (\$246 per hour × 0.5)) × 130 hours) + 325 = \$320.30.

<sup>143</sup> 325 initial technology-related burden hours × \$320.30 per hour = \$104,097.50.

<sup>144</sup> See *Amendments to Form PF to Require Current Reporting and Amend Reporting Requirements for Large Private Equity Advisers and Large Liquidity Fund Advisers*, Investment Act Release No. 5950 (Jan. 26, 2022), 87 FR 9106 (Feb. 17, 2022) (The Commission recognizes that Proposed Rule 13f-2 would cover persons other than large hedge fund advisers, and that large hedge fund advisers may generally be more accustomed to existing Commission reporting requirements than some other persons that would be covered by Proposed Rule 13f-2.).

<sup>145</sup> See *id.* at 9140 Table 2.

<sup>146</sup> See Exchange Act Release No. 93784 (Dec. 15, 2021), 87 FR 6652, 6678 (Feb. 4, 2022).

outstanding shares—were to be applied.<sup>147</sup> However, Form SH represented a narrower population of potential filers (e.g., only those that exercise investment discretion with respect to accounts holding Section 13(f) securities having an aggregate fair market value of at least \$100 million) than prospective Proposed Form SHO filers. Form SH also applied to a narrower population of securities, 13(f) securities, than Proposed Form SHO, which is proposed to apply more broadly to all equity securities.<sup>148</sup> Additionally, Proposed Rule 13f–2 will include a second Reporting Threshold (Threshold B) that applies to short positions in non-reporting company issuers, which could result in additional Managers having to file a Proposed Form SHO. The number of Managers with accounts containing short positions big enough to trigger either of the proposed threshold prongs for Proposed Form SHO may have increased in the thirteen years since Form SH was implemented, particularly if overall shorting activity has increased. The Commission also recognizes that technological innovation and automation can change quickly, providing for new opportunities to streamline processes and reduce both initial and ongoing burdens and costs. Thus, the Commission seeks specific comment as to whether the proposed burden estimates are appropriate or whether such estimates should be increased or reduced. The Commission invites comment on the estimated number of Managers anticipated to be required to file a Proposed Form SHO each month (1,000), the estimated time

burden (20 hours) of preparing and filing each required Proposed Form SHO, and the estimated initial time burden (325 hours) for Managers to update their systems and technology to facilitate the filing of Proposed Form SHO. The Commission also invites comment on the estimated number of Managers that will file Proposed Form SHO each month directly in Proposed Form SHO-specific XML (1,000), the estimated associated additional burden (2 hours of work by a programmer) for each filing, and whether the burden is more accurately categorized as an ongoing per filing burden or an initial, one-time technological systems update burden. If those estimates or any other element of Proposed Rule 13f–2 and Proposed Form SHO burdens or costs should be increased or decreased, please address by how much and why.

### C. Burdens for Broker-Dealers Under Proposed Rule 205

#### 1. Applicable Respondents

As discussed above, Proposed Rule 205 would add a new “buy to cover” marking requirement for a broker-dealer effecting a purchase order for its own account or on behalf of another person, wherein the account has a gross short position in the security being purchased. Proposed Rule 205 would require that, regardless of the size of such purchase for such account, the broker-dealer mark the purchase “buy to cover.” All broker-dealers whose accounts or whose customers’ accounts at the broker-dealer could hold a short position are potentially subject to the requirements of Proposed Rule 205. As of December 31, 2020, there were 3,551

broker-dealers registered with the Commission.<sup>149</sup> The Commission estimates that of the 3,551 registered broker-dealers, 1,218 place orders that would require a “buy to cover” order mark.<sup>150</sup>

#### 2. Burdens and Costs

For purposes of the PRA, the Commission staff estimates that a total of approximately 62.25 billion “buy to cover” orders would be entered annually.<sup>151</sup> This would make for an average of approximately 51.1 million annual “buy to cover” order marks by each broker-dealer anticipated to require a “buy to cover” order mark.<sup>152</sup> Each instance of marking an order “buy to cover” is estimated to take between approximately .00001158 and .000139 hours (.042 and .5 seconds) to complete.<sup>153</sup> This estimate is based on a number of factors, including: previously estimated burdens for the current marking requirements of Rule 200(g) of Regulation SHO requiring broker-dealers to mark sell orders “long,” “short,” or “short exempt”; broker-dealers should already have the necessary mechanisms and procedures in place and already be familiar with processes and procedures to comply with the marking requirements of Rule 200(g) of Regulation SHO; broker-dealers should be able to continue to use the same or similar mechanisms, processes and procedures to comply with Proposed Rule 205; and that computing speeds have significantly improved since the initial order marking burdens of Rule 200(g) of Regulation SHO were initially estimated.

PRA TABLE 3—ESTIMATED BROKER-DEALER BURDEN ASSOCIATED WITH “BUY TO COVER” ORDER MARKING

	Broker-Dealers that may “buy to cover”	Annual “buy to cover” orders	Burden hours per “buy to cover” order	Total annual industry burden hours	Annual burden per broker-dealer
“Buy to Cover” Order Marking ..	1,218	62.25 billion .....	.00001158 (.042 seconds) to .000139 (.5 seconds).	721,000 to 8,652,750 .....	592 to 7,104.

<sup>147</sup> See *supra* Part III.D.2 Table I, Panel B.

<sup>148</sup> See *supra* Part III.A discussing equity securities subject to requirements of Regulation SHO.

<sup>149</sup> This estimate is derived from broker-dealer FOCUS filings as of December 31, 2020.

<sup>150</sup> This estimate is derived from an analysis conducted by Commission staff of CAT data indicating that 1,218 broker-dealers would have been required to mark an order “buy to cover” in November 2021. The Commission further estimates that a month-long period is likely to capture all broker-dealers to which the marking requirement of Proposed Rule 205 would apply.

<sup>151</sup> Our estimate of 62.25 billion annual “buy to cover” orders was calculated based on a staff review of short sale trades, comprised of trades marked

“short” and “short exempt” during the five years from 2016 through 2020. Based on a review of Rule 605 reports from the three largest market centers during August 2008, we have previously estimated a ratio of 14.4 orders to each completed trade. We gross up our 4.3 billion estimate of average annual short sale trades from 2016 to 2020 by 14.4, which yields 62.25 billion average annual short sale orders. A similar review of Rule 605 reports from large market centers has not been performed since the August 2008 period. The ratio of short sale orders to completed trades may have increased or decreased since that time.

<sup>152</sup> This figure was calculated as follows: 62.25 billion “buy to cover” orders divided by 1,218 broker-dealers anticipated to place orders requiring the “buy to cover” order mark.

<sup>153</sup> The upper end of this estimate—.5 seconds—is based on the same time estimate for marking sell orders “long” or “short” under Rule 200(g) of Regulation SHO. See Regulation SHO Adopting Release, *supra* note 4, at 48023. See also, Exchange Act Release No. 48709 (Oct. 28, 2003) 68 FR 62972, 63000 n. 232 (Nov. 6, 2003); Exchange Act Release No. 59748 (Apr. 10, 2009), 74 FR 18042, 18089 (Apr. 20, 2009) (providing the same estimate—.5 seconds—for marking sell orders “short exempt” under Rule 200(g) of Regulation SHO). The lower end of this estimate—.042 seconds—is based on a Commission estimate that computing speeds are twelve times faster today than they were in 2007. See *infra* note 312.

In addition to the burden and costs associated with the marking of individual “buy to cover” orders, the Commission believes that broker-dealers required to mark “buy to cover” will incur initial, one-time technology project costs to update their existing order marking systems. The Commission believes that the

implementation cost of the “buy to cover” marking requirement will likely be similar to the implementation cost of the “short exempt” order marking requirements of Rule 200(g) of Regulation SHO.<sup>154</sup> The initial implementation cost of the “short exempt” order marking requirement was estimated to be approximately \$115,000

to \$145,000 per broker-dealer. Taking the average of that range and updating it for inflation results in an approximate one-time cost of \$170,000 per broker-dealer,<sup>155</sup> and a total initial combined implementation cost of approximately \$207,060,000 for all broker-dealers that are estimated to “buy to cover.”<sup>156</sup>

**PRA TABLE 4—ESTIMATED BROKER-DEALER COSTS ASSOCIATED WITH INITIAL “BUY TO COVER” ORDER MARKING SYSTEM UPDATES**

	Broker-dealers that may “buy to cover”	Estimated initial technology cost to update order marking systems	Total initial costs to all broker-dealers
“Buy to Cover” Initial System Updates .....	1,218	\$170,000	\$207,060,000

In making its estimate of annual “buy to cover” orders, the Commission notes that its estimate may be over-inclusive of the total number of purchase orders that can be reasonably expected to be covered by Proposed Rule 205. As noted above, the estimate is based on the average annual orders marked “short” and “short exempt” over a five year period—2016 through 2020. Such data was used based on the assumption that, over the course of a year, for every short position created by a “short” or “short exempt” sale order, there will be an equal and opposite number of “buy to cover” purchase orders placed in order to cover, and ultimately close out, those short positions. However, the Commission recognizes that industry practices may differ in terms of how order marks are applied (e.g., whether orders marked “short” are defaulted to in some instances where the seller may in fact be net long) and/or how short positions are created (e.g., potentially with multiple, smaller orders over time) and covered (e.g., potentially with fewer, larger orders). The Commission also requests comment on the 14.4 ratio of orders to trades used to calculate the total number of anticipated “buy to cover” orders. The Commission recognizes that the number of orders that result in a transaction may have materially changed since the August 2008 estimate based on a review of Rule 605 reports.<sup>157</sup> The Commission also requests comment on the estimated range of .042 to .5 seconds (.00001158 to .000139 hours) that it takes for a broker-dealer to properly mark a

purchase order for an account that holds a gross short position in the security being purchased as “buy to cover.” The Commission also requests comment on the estimated cost of \$170,000 per broker-dealer of initially adding the “buy to cover” mark to existing order marking systems, including whether having existing order marking systems, potentially having previously updated such systems to include a “short exempt” order mark, and significant advances in technology and automation may have reduced the estimated costs from those described in 2003 and 2004.<sup>158</sup> Thus, the Commission seeks specific comment as to whether the proposed burden estimates are appropriate or whether such estimates should be increased or reduced. Among the other factors of these estimates, the Commission invites comments on the estimated number of “buy to cover” orders anticipated to be placed by broker-dealers each year (62.25 billion), the estimated ratio of orders per trade (14.4:1), the time required to accurately mark a purchase order “buy to cover” (between .042 and .5 seconds), and the cost of updating existing order marking systems to accommodate the “buy to cover” order mark (\$170,000). If those estimates or any other element of the estimated Proposed Rule 205 burdens should be increased or decreased, please address by how much and why.

*D. Burdens and Costs Associated With the Proposal To Amend CAT*

1. Summary of Collections of Information

The Proposal to Amend CAT would amend the CAT NMS Plan to require Participants to update their Compliance Rules to require reporting by Industry Members of the following information: (i) For the original receipt or origination of an order to buy an equity security, whether such buy order is for an equity security that is a “buy to cover” order as defined by Rule 205(a) of Regulation SHO (17 CFR 242.205(a)); and (ii) for the original receipt or origination of an order to sell an equity security, whether the order is a short sale effected by a market maker in connection with bona-fide market making activities in the security for which exception Rule 203(b)(2)(iii) of Regulation SHO is claimed.<sup>159</sup>

2. Proposed Use of Information

The Commission believes that requiring proposed reporting of certain short sale information to the CAT would provide valuable information for the Commission and other regulators in investigations and reconstruction of market events. Ready access to “buy to cover” information in the CAT would allow regulators to determine whether a purchase or sale of an equity security increases or decreases equity exposure of an Industry Member or Customer, and whether the buy covers a short position. The ability to determine whether an order adds to an existing position or covers an existing short position would

<sup>154</sup> See Exchange Act Release No. 61595 (Feb. 26, 2010), 75 FR 11232, 11287 (Mar. 10, 2010), basing its cost estimates for the implementation of “short exempt” order marking on the estimates contained in Regulation SHO Adopting Release, *supra* note 4, at 48023, which based its cost estimates on input from industry sources.

<sup>155</sup> The adjustment for inflation was calculated using information in the Consumer Price Index, U.S. Department of Labor, Bureau of Labor Statistics for February 2010 and November 2021.

<sup>156</sup> This figure was calculated as follows: \$170,000 implementation cost × 1,218 broker-

dealers anticipated to mark “buy to cover” = \$207,060,000 industry-wide implementation cost.

<sup>157</sup> See *supra* note 151.

<sup>158</sup> See *supra* note 154 and accompanying text.

<sup>159</sup> See *supra* Part VI; see also proposed CAT NMS Plan Sections 6.4(d)(ii)(D) and 6.4(d)(ii)(E).

be useful in detecting and investigating portfolio pumping, short selling abuses, short squeezes marking the close, potential manipulation, insider trading, or other rule violations. It would also assist Commission staff and regulatory staff analysis of the impact of “buys to cover” on equity prices and price volatility, and determine the impact of “short squeezes.” The Commission believes that requiring Industry Members to identify short sales for which they are claiming the bona fide market making exception would provide the Commission staff and other regulators an additional tool to determine whether such activity qualifies for the exception, or instead is indicative of, for example, proprietary trading instead of bona fide market making.

### 3. Respondents

#### a. National Securities Exchanges and National Securities Associations

The respondents to certain proposed collections of information for the Proposal to Amend CAT would be the 25 Plan Participants (the 24 national securities exchanges and one national securities association (FINRA)).<sup>160</sup>

#### b. Members of National Securities Exchanges and National Securities Associations

The respondents for certain information collection for the Proposal to Amend CAT are the Participants’ broker-dealer members, that is, Industry Members. The Commission understands that there are currently 3,551 broker-dealers;<sup>161</sup> however, not all broker-dealers are expected to have new CAT reporting obligations under the Proposal to Amend CAT.<sup>162</sup> Based on an analysis of CAT data from November 2021, conducted by Commission staff, the Commission estimates that approximately 1,218 broker-dealers will be affected by the Proposal to Amend CAT, including 1,218 broker-dealers that would be required to report “buy-to-cover” information on buy orders for equity securities and 104 broker-dealers

<sup>160</sup> The Participants are: BOX Options Exchange LLC; Cboe BZX Exchange, Inc.; Cboe BYX Exchange, Inc.; Cboe C2 Exchange, Inc.; Cboe EDGA Exchange, Inc.; Cboe EDGX, Inc.; Cboe Exchange, Inc.; Financial Industry Regulatory Authority, Inc.; Investors Exchange Inc.; Long-Term Stock Exchange, Inc.; MEMX, LLC; Miami International Securities Exchange LLC; MIAx PEARL, LLC; MIAx Emerald, LLC; NASDAQ BX, Inc.; NASDAQ GEMX, LLC; NASDAQ ISE, LLC; NASDAQ MRX, LLC; NASDAQ PHLX LLC; The NASDAQ Stock Market LLC; New York Stock Exchange LLC; NYSE MKT LLC; and NYSE Arca, Inc., NYSE Chicago Stock Exchange, Inc., NYSE National, Inc.

<sup>161</sup> See *supra* note 149.

<sup>162</sup> See also *supra* Part VI.B.2.

that would be required to report for the original receipt or origination of an order to sell an equity security whether the order is a short sale effected by a market maker in connection with bona-fide market making activities in the security for which the exception in Rule 203(b)(2)(iii) of Regulation SHO is claimed.

#### 4. Total Initial and Annual Reporting and Recordkeeping Burdens

The Commission’s total burden estimates in this Paperwork Reduction Act section reflect the total burden on all Participants and Industry Members. The burden estimates per Participant or Industry Member are intended to reflect the average paperwork burden for each Participant or Industry Member, but some Participants or Industry Members may experience more burden than the Commission’s estimates, while others may experience less. The burden figures set forth in this section are the based on a variety of sources, including Commission staff’s experience with the development of the CAT and estimated burdens for other rulemakings. Because the CAT NMS Plan applies to and obligates the Participants and not the Plan Processor, the Commission believes it is appropriate to estimate the Participants’ external cost burden based on the estimated Plan Processor staff hours required to comply with the proposed obligations.<sup>163</sup> Put another way, pursuant to the proposed amendments to the CAT NMS Plan the Participants will be obligated to make changes to the CAT, but the CAT is managed by the Plan Processor pursuant to contractual agreement, and so the Participants will be required to engage the Plan Processor to make any required changes.

##### a. Participant Burdens

The Proposal to Amend CAT would require the Participants to engage the Plan Processor to modify the Central Repository to accept and process the new short sale data elements on order receipt and origination reports. The Commission estimates that the Participants would incur an initial, one-time burden of 130 hours, or 5 hours per

<sup>163</sup> The Commission derives estimated costs associated with Plan Processor and Industry Member staff time based on per hour figures from SIFMA’s *Management & Professional Earnings in the Securities Industry 2013*, modified by Commission staff to account for an 1800-hour work-year, and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead, and adjusted for inflation based on Bureau of Labor Statistics data on CPI-U between January 2013 and January 2020 (a factor of 1.12). For example, the 2020 inflation-adjusted effective hourly wage rate for attorneys is estimated at \$426 (\$380 × 1.12).

Participant, of staff time required to supervise and implement the changes necessary for the Plan Processor to accept and process the new data elements, and an external cost of \$101,520, or a per Participant expense of approximately \$4,060.80 to compensate the Plan Processor for staff time required to make the initial necessary programming and systems changes to accept and process the new data elements, based on a preliminary estimate that it would take 300 hours of Plan Processor staff time to implement these changes.<sup>164</sup>

The Commission believes that other Paperwork Reduction Act burdens that would apply to the Participants, including ongoing burdens and external expenses for the Plan Processor’s acceptance and processing of the new data elements, are already accounted for in the existing Paperwork Reduction Act estimate that applies for Rule 613 and the CAT NMS Plan Approval Order, submitted under OMB number 3235–0671.<sup>165</sup> The Commission believes that the prior Paperwork Reduction Act analysis incorporates any other potential Paperwork Reduction Act burdens for the Participants because the existing Paperwork Reduction Act analysis accounts for initial and ongoing costs for, among other things, operating and maintaining the Central Repository, including the cost of systems and connectivity upgrades or changes necessary to receive and consolidate the reported order and execution information from Participants and their members, the cost to store data and make it available to regulators, the cost of monitoring the required validation parameters, and management of the Central Repository.<sup>166</sup> In addition, the Commission anticipates that each exchange and national securities association would file one Form 19b–4 filing to implement updated Compliance Rules. While such filings may impose certain costs on the exchanges, those burdens are already accounted for in the comprehensive

<sup>164</sup> The estimated 300 hours of Plan Processor staff time include 200 hours by a Senior Programmer, 40 hours by a Senior Database Administrator, 40 hours for a Senior Business Analyst and 20 hours for an Attorney. The Commission estimates that the initial, one-time external expense for Participants will be \$101,520 = (Senior Programmer for 200 hours at \$339 an hour = \$67,800) + (Senior Database Administrator for 40 hours at \$349 an hour = \$13,960) + (Senior Business Analyst for 40 hours at \$281 an hour = \$11,240) + (Attorney for 20 hours at \$426 an hour = \$8,520).

<sup>165</sup> See CAT NMS Plan Approval Order, 81 FR at 84911–43. See also OMB Control No. 3235–0671, 85 FR 37721 (June 23, 2020) (notice of submission of request for approval of extension).

<sup>166</sup> See CAT NMS Plan Approval Order, 81 FR at 84918.

Paperwork Reduction Act Information Collection submission for Form 19b–4.<sup>167</sup> The Commission does not expect the baseline number of 19b–4 filings to increase as a result of the Proposal to Amend CAT, nor does it believe that the incremental costs exceed those costs used to arrive at the average costs and/or burdens reflected in the Form 19b–4 PRA submission.

#### b. Broker-Dealer Burdens

The Commission believes that certain Industry Members will have initial, one-time burdens and costs relating to the Proposal to Amend CAT, to update systems and processes as necessary to capture and report the proposed data elements to CAT. The Commission has estimated these initial burdens and costs below.

The Commission also believes that the Proposal to Amend CAT would impose an ongoing annual burden relating to, among other things, personnel time to monitor each broker-dealer's reporting of the required data and the maintenance of the systems to report the required data, and implementing changes to trading systems that might result in additional reports to the Central Repository. However, the Commission believes that the ongoing burden imposed by the Proposal to Amend CAT related to reporting to the CAT is already accounted for in the existing information collections burdens associated with Rule 613 and the CAT NMS Plan Approval Order submitted under OMB number 3235–0671.<sup>168</sup> Specifically, the CAT NMS Plan Approval Order takes into account requirements on broker-dealer members to comply with the CAT NMS Plan, including the requirement to maintain the systems necessary to collect and transmit information to the Central Repository,<sup>169</sup> provides aggregate burden hour and external cost estimates for the broker-dealer data collection and reporting requirement of Rule 613, and did not quantify the burden hours or external cost estimates for each individual component comprising the broker-dealer's data collection and reporting responsibility.<sup>170</sup> The Proposal to Amend CAT would not require any Industry Member to submit new reports to the CAT, but to add

limited additional information to existing reports in certain circumstances for certain Industry Members. The Commission does not believe that this would alter the estimates of ongoing burden and external costs in the existing Paperwork Reduction Act Analysis and the ongoing burden associated with these new collection requirements are accounted for in the existing Paperwork Reduction Act Analysis.

#### Buy to Cover Information on Orders

With regard to the obligation to report “buy to cover” information on orders to the CAT, the Commission believes that it is appropriate to divide the 1,218 Industry Members that would be required to report buy to cover information to the CAT for the original receipt or origination of orders into two categories: (i) Industry Members that report directly to the CAT (“insourcing Industry Members”); and (ii) Industry Members that use third-party reporting agents such as service bureaus for CAT reporting (“outsourcing Industry Members”). For purposes of this Paperwork Reduction Act analysis, the Commission estimates that of the 1,218 Industry Members that would be required to report buy to cover information to the CAT for the original receipt or origination of orders, 126 would be insourcing Industry Members, and 1,092 would be outsourcing Industry Members. This is based on the CAT NMS Approval Order, which based on an analysis of specific data provided by FINRA on how firms report OATS data estimated that there were 126 large OATS<sup>171</sup> reporting broker-dealers, with all other broker-dealers either not reporting to CAT at the time or reporting to OATS through service bureaus.<sup>172</sup> The Commission believes it is reasonable to estimate for purposes of this Paperwork Reduction Act analysis that the same number of broker-dealers that reported directly to OATS report directly to CAT, and that it is unlikely that previously outsourcing broker-dealers and broker-dealers without an obligation to report to OATS developed the infrastructure necessary to report to the CAT.

The Commission estimates that the 126 insourcing Industry Members will incur an initial, aggregate, one-time

burden of 32,760 hours, or that each of these insourcing Industry Members would incur an initial, average one-time burden of 260 hours, and that these 126 insourcing Industry Members will incur an initial, aggregate, one-time external expense of approximately \$1,890,000 for software and hardware to facilitate reporting of the new data elements to CAT, or that each insourcing Industry Member would incur an initial, average one-time external expense of approximately \$15,000 for hardware and software to facilitate reporting of the new data elements to CAT.<sup>173</sup>

The Commission estimates that the 1,092 outsourcing Industry Members will incur an initial, aggregate, one-time burden of 10,920 hours, or that each of these outsourcing Industry Members would incur an initial, one-time burden of 10 hours on average, and that together these 1,092 outsourcing Industry Members will incur an initial, aggregate, one-time external expense of approximately \$1,092,000 for software and hardware to facilitate reporting of the new data elements to CAT and for external expenses relating to fees paid to CAT reporting agents to update their systems or coding as necessary, or that each outsourcing Industry Member would incur an initial, average one-time external expense of approximately \$1,000.<sup>174</sup>

<sup>173</sup> The Commission is basing this figure on the estimated internal burden for a broker-dealer that handles orders subject to customer specific disclosures required by Rule 606(b)(3) to both update its data capture systems in-house and format the report required by Rule 606. See Exchange Act Release No. 84528 (November 2, 2018), 83 FR 58338, 58383 (November 19, 2018) (“Rule 606 Adopting Release”). The Commission believes that this is a reasonable proxy for a preliminary estimation for the burdens and costs associated with updating data capture systems for reporting purposes here because in both rulemakings broker-dealers were required to update in-house data reported for pre-existing reporting obligations, and, as discussed above, the Paperwork Reduction Act analysis for Rule 613 and the CAT NMS Plan did not attempt to quantify the burden hours or external cost estimates for each individual component comprising the broker-dealer's data collection and reporting responsibility. See *supra* note 169.

<sup>174</sup> The Commission believes that the preliminary estimated burden and external costs for outsourcing Industry Members is reasonable because the burden on individual Industry Members should be significantly lower than insourcing Industry Members because of the difference in how these firms report to the CAT. Outsourcing Industry Members will not be required to change internal CAT reporting systems, but instead would have to be responsible for making any updates necessary for CAT reporting agents to report this information to the CAT. The outsourcing Industry Members will have external costs associated with paying CAT reporting agents for any additional fees relating to the change, but because CAT reporting agents can report on behalf of numerous outsourcing Industry Members at the same time, the costs of any updates to their systems can be distributed amongst outsourcing Industry Members.

<sup>167</sup> See OMB Control No. 3235–0045 (August 19, 2016), 81 FR 57946 (August 24, 2016) (Request to OMB for Extension of Rule 19b–4 and Form 19b–4 PRA).

<sup>168</sup> See CAT NMS Plan Approval Order, 81 FR at 84911–43.

<sup>169</sup> See, e.g., CAT NMS Plan Approval Order, 81 FR at 84930.

<sup>170</sup> See CAT NMS Plan Approval Order, 81 FR at 84930.

<sup>171</sup> OATS was FINRA's Order Audit Trail System, which existed prior to the creation of the CAT and was an order audit trail system maintained by FINRA, was retired on September 1, 2021 because FINRA determined that the accuracy and reliability of the CAT met certain standards and thus OATS was duplicative in light of the implementation of CAT. See Exchange Act Notice No. 92239 (June 23, 2021), 86 FR 34293 (June 29, 2021).

<sup>172</sup> See CAT NMS Plan Approval Order, 81 FR at 84860.

As discussed above, the Commission does not believe that these CAT Reporters would have an ongoing PRA burden or external costs related to the reporting of the new information to CAT because the ongoing burden and external costs are already accounted for in the existing information collections burdens associated with Rule 613 and the CAT NMS Plan Approval Order submitted under OMB number 3235–0671.<sup>175</sup>

#### Bona Fide Market Making Exception Information

The Commission believes that this aspect of the Proposal to Amend CAT will only impose additional burdens on Industry Members that trade equity securities and rely upon or plan to rely upon the bona fide market making exception. Based on an analysis of data reported to the CAT in November 2021, and specifically the identification of all unique CAT Reporters that were identified as equity market makers (including different classes of market makers such as “designated” or “lead” market makers, and secondary liquidity providers), the Commission believes that approximately 104 CAT Reporters will be subject to the new reporting obligation. The Commission believes that some broker-dealers that rely upon this exception may retain records regarding their eligibility for this exception for specific orders or for orders originated by specific desks or units of their business, and thus for some broker-dealers this information could be more easily reportable than information not currently available to Industry Members, such as the “buy to

cover” identification of equity buy orders.

With regard to the obligation to report regarding bona fide market making exception information to the CAT, the Commission believes that it is appropriate to divide the 104 Industry Members that would be required to report this information into two categories: (i) Industry Members that report directly to the CAT; and (ii) Industry Members that use third-party reporting agents for CAT reporting. For purposes of this Paperwork Reduction Act analysis, the Commission estimates that of the 104 Industry Members that would be required to this information, 60 Industry Members would be reporting this information directly to the CAT, and 44 Industry Members would be reporting this information through third-party reporting agents. The Commission believes this is a reasonable estimation because it believes that the majority of Industry Members that are identified as market makers in the CAT are large enough to have developed their own systems and technology to report directly to the CAT.

The Commission estimates that the 60 insourcing Industry Members that report directly to the CAT will incur an initial, aggregate, one-time burden of 15,600 hours, or that each of these CAT Reporters would incur an initial, average one-time burden of 260 hours, and that each of these 60 insourcing Industry Members will incur an initial, aggregate, one-time external expense of approximately \$900,000 for software and hardware to facilitate reporting of the new data elements to CAT, or that each insourcing Industry Member

would incur an initial, average one-time external expense of approximately \$15,000.<sup>176</sup>

The Commission estimates that the 44 outsourcing Industry Members that use third-party reporting agents to report to the CAT will incur an initial, aggregate, one-time burden of 440 hours, or that each of these outsourcing Industry Members would incur an initial, one-time burden of 10 hours on average, and that these 44 outsourcing Industry Members will incur an initial, aggregate, one-time external expense of approximately \$44,000 for software and hardware to facilitate reporting of the new data elements to CAT, or that each outsourcing Industry Member would incur an initial, average one-time external expense of approximately \$1,000.<sup>177</sup>

As discussed above, the Commission believes that the ongoing burden associated with reporting to the CAT is already accounted for in the existing information collections burdens associated with Rule 613 and the CAT NMS Plan Approval Order submitted under OMB number 3235–0671.<sup>178</sup> Because this information is already collected and maintained by market makers that engage in equity trading and claim the exception pursuant to Rule 17a–3 of the Exchange Act, the Commission believes there is no new ongoing burden associated with collecting or recording the information necessary to effectuate CAT reporting of this new element.

#### c. Summary of Initial One-Time Burdens Relating to Proposal To Amend CAT

Name of information collection	Type of burden	Number of entities impacted	Initial one-time hourly burden	Aggregate one-time hourly burden	Initial one-time cost	Aggregate one-time cost
CAT: Central Repository—Short Sale Data.	Recordkeeping ....	25	5	130	\$4,060.80	\$101,520
CAT: Reporting of Buy to cover Information for Orders—Insourcers.	Third Party Disclosure.	126	260	32,760	15,000	1,890,000
CAT: Reporting of Buy to cover Information for Orders—Outsourcers.	Third Party Disclosure.	1,092	10	10,920	1,000	1,092,000
CAT: Reporting of Bona Fide Market Making Exception—Insourcers.	Third Party Disclosure.	60	260	15,600	15,000	900,000
CAT: Reporting of Bona Fide Market Making Exception—Outsourcers.	Third Party Disclosure.	44	10	440	1,000	44,000

<sup>175</sup> See *supra* note 165.

<sup>176</sup> The Commission is basing this figure on the estimated burden and external costs for a broker-dealer that handles orders subject to customer specific disclosures required by Rule 606(b)(3) to update their systems to capture the data and produce a report to comply with Rule 606. See Rule 606 Adopting Release, 83 FR at 58383. The Commission believes that this is a reasonable proxy for a preliminary estimation for the burdens and costs associated with updating data capture systems for reporting purposes here because in both

rulemakings broker-dealers were required to update in-house data reported for pre-existing reporting obligations.

<sup>177</sup> The Commission believes that the preliminary estimated burden and external costs for outsourcing Industry Members is reasonable because the burden on individual Industry Members should be significantly lower than insourcing Industry Members because of the difference in how these firms report to the CAT. Outsourcing Industry Members will not be required to change internal CAT reporting systems, but instead would have to

be responsible for making any updates necessary for CAT reporting agents to report this information to the CAT. The outsourcing Industry Members will have external costs associated with paying CAT reporting agents for any additional fees relating to the change, but because CAT reporting agents can report on behalf of numerous outsourcing Industry Members at the same time, the costs of any updates to their systems can be distributed amongst outsourcing Industry Members.

<sup>178</sup> See *supra* note 165.

### *E. Collection of Information Is Mandatory*

The proposed information collections are required under Proposed Rule 13f-2 and Proposed Form SHO for Managers that meet one of the Reporting Thresholds, Proposed Rule 205 for broker-dealers that effect purchase orders for accounts with open short positions in the equity securities being purchased, and the Proposal to Amend CAT for Plan Participants to collect and process new CAT reportable information and for CAT Industry Members that engage in certain short sale activity.

### *F. Confidentiality*

As discussed above, Proposed Rule 13f-2 would require certain Managers to file monthly in EDGAR, on Proposed Form SHO, certain short sale volume data and short interest position data. However, the Commission is proposing that the information reported by Managers on Proposed Form SHO be aggregated prior to publication so as to protect the identity of reporting Managers.

The Commission would not typically receive confidential information as a result of Proposed Rule 205. To the extent that the Commission receives—through its examination and oversight program, through an investigation, or by some other means—records or disclosures from a broker-dealer that relate to or arise from Proposed Rule 205 that are not publicly available, such information would be kept confidential, subject to the provisions of applicable law.

With respect to the Proposal to Amend CAT, Rule 613 and the CAT NMS Plan requires that the information to be collected and electronically provided to the Central Repository would only be available to the national securities exchanges, national securities association, and the Commission. Further, the CAT NMS Plan includes policies and procedures designed to ensure the security and confidentiality of all information submitted to the Central Repository, and to ensure that all SROs and their employees, as well as all employees of the Central Repository, shall use appropriate safeguards to ensure the confidentiality of such data. The Commission would receive confidential information pursuant to this collection of information, and such information will be kept confidential, subject to the provisions of applicable law.

### *G. Request for Comments*

The Commission requests comment on whether the estimates for burden

hours and costs are reasonable. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comments to (1) evaluate whether the proposed collections of information are necessary for the proper performance of the functions of the Commission, including whether the information would have practical utility; (2) evaluate the accuracy of the Commission's estimate of the burden of the proposed collections of information; (3) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and (4) determine whether there are ways to minimize the burden of the collections of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

While the Commission welcomes any public input on this topic, the Commission asks commenters to consider the following questions:

- *Q20:* Has the Commission accurately estimated the paperwork burdens and costs to Managers associated with fulfilling the reporting requirements of Proposed Rule 13f-2?
- *Q21:* Has the Commission accurately estimated the number of Managers (1,000) anticipated to be required to file Proposed Form SHO each month? If the estimate should be increased or decreased, please address by how much and why.
- *Q22:* Has the Commission accurately estimated the amount of time (325 hours) needed for Managers to complete initial technology projects to facilitate fulfillment of the reporting requirements of Proposed Rule 13f-2? If the estimate should be increased or decreased, please address by how much and why.
- *Q23:* Has the Commission accurately estimated the number of Managers each month (1,000) that will use a structured XML data language methodology, as opposed to the web-fillable Proposed Form SHO directly on EDGAR, to file Proposed Form SHO? Has the Commission accurately estimated the number for Managers each month (35) that will use a structured XML data language methodology to file an amended Proposed Form SHO?
- *Q24:* Has the Commission accurately estimated the additional paperwork burden (2 hours of work by a programmer) for Managers to file a Proposed Form SHO via the structured XML data language methodology? Is the additional burden (2 hours of work by a programmer) more accurately categorized as an ongoing per filing burden or an initial, one-time technological systems update burden?

- *Q25:* Has the Commission accurately estimated that approximately 3.5% of Proposed Form SHO filers would also file an amended Proposed Form SHO, resulting in additional burdens and costs for an estimated 35 Managers each month?

- *Q26:* Has the Commission accurately estimated the paperwork burdens and costs to broker-dealers associated with fulfilling the order marking requirements of Proposed Rule 205? Has the Commission accurately estimated the number of broker-dealers (1,218) that will be required to update their order marking systems to incorporate the “buy to cover” order mark?

- *Q27:* Has the Commission accurately estimated the total number of orders marked “buy to cover” by broker-dealers each year (62.25 billion)? If the estimate should be increased or decreased, please address by how much and why.

- *Q28:* Is the Commission's estimation that, over the course of a year, for every short position created by a “short” or “short exempt” sale order, there will be an equal and opposite number of “buy to cover” purchase orders placed in order to cover, and ultimately close out, those short positions, an accurate projection of how frequently “buy to cover” order marks will be used? If there is a more accurate means of estimating the volume of anticipated annual “buy to cover” order marks, please describe its structure and why it is more accurate.

- *Q29:* Has the Commission accurately estimated the ratio of orders to trades (14.4:1) used to calculate the total number of anticipated “buy to cover” orders? If the estimate should be increased or decreased, please address by how much and why.

- *Q30:* Has the Commission accurately estimated the time it takes (between .042 and .5 seconds) for a broker-dealer to properly mark a purchase order as “buy to cover” for an account that holds a gross short position in the security being purchased? If the estimate should be increased or decreased, or the range narrowed, please address by how much and why.

- *Q31:* Has the Commission accurately estimated the cost to broker-dealers (\$170,000) to update their order marking systems, or is such a cost likely to have decreased for reasons including technological advances? If the estimate should be increased or decreased, please address by how much and why.

- *Q32:* Has the Commission accurately captured the market participants who would be subject to

the burdens and costs under the Proposal to Amend CAT?

- *Q33*: Has the Commission accurately estimated the number of Industry Members anticipated to be required to report new information to the CAT under the Proposal to Amend CAT?

- *Q34*: Has the Commission accurately estimated the paperwork burdens and costs to market participants associated with the Proposal to Amend CAT?

Persons wishing to submit comments on the collection of information requirements should direct the comments to the Office of Management and Budget, Attention: Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, DC 20503, and send a copy to Vanessa Countryman, Secretary, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549-1090, with reference to File No. S7-08-22. OMB is required to make a decision concerning the collection of information between 30 and 60 days after publication of this release. Consequently, a comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication. Requests for materials submitted to OMB by the Commission with regard to these collections of information should be in writing, refer to File No. S7-08-22, and be submitted to the Securities and Exchange Commission, Office of FOIA Services, 100 F Street NE, Washington, DC 20549-2736.

## VIII. Economic Analysis

### A. Introduction

The Commission is proposing new reporting requirements in connection with short sales. The Commission is mindful of the economic effects that may result from the proposed requirements, including the benefits, costs, and the effects on efficiency, competition, and capital formation.<sup>179</sup> The Commission believes that, if adopted, Proposed Rule 13f-2 and

<sup>179</sup> Exchange Act Section 3(f) requires the Commission, when it is engaged in rulemaking pursuant to the Exchange Act and is required to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action would promote efficiency, competition, and capital formation. See 15 U.S.C. 78c(f). In addition, Exchange Act Section 23(a)(2) requires the Commission, when making rules pursuant to the Exchange Act, to consider among other matters the impact that any such rule would have on competition and not to adopt any rule that would impose a burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act. See 15 U.S.C. 78w(a)(2).

Proposed Form SHO, Proposed Rule 205, and the Proposal to Amend CAT would result in improved regulatory oversight, as the data that would become available to regulators would close informational gaps in the currently available data, which would in turn benefit market participants and help foster fair and orderly markets. More specifically, the Proposals would increase transparency and improve regulators' examination of market behavior and recreation of significant market events. These improvements may, in turn, discourage abusive short selling.<sup>180</sup> Proposed Rule 13f-2 would also increase transparency for market participants about short selling, which could help refine market participants' understanding of the level of negative sentiment and the actions of short sellers.

The Proposals may also lead to tradeoffs in market quality. A reduction in abusive short selling and improved regulatory oversight may have a positive impact on market quality. Furthermore, the Proposals would provide market participants improved transparency into short selling which could also improve price efficiency. However, Proposed Rule 13f-2 and Proposed Form SHO could chill short selling by increasing the costs and risks of implementing large short positions, which could reduce the positive effects of short selling on market quality. Furthermore, public disclosure of information resulting from Proposed Rule 13f-2 and Proposed Form SHO could facilitate short squeezes, which could reduce market quality for all.<sup>181</sup>

In addition to the indirect costs to market quality, Proposed Rule 13f-2, Proposed Form SHO, Proposed Rule 205, and the Proposal to Amend CAT could impose significant compliance costs on market participants. The proposal to require Managers to report large positions and activity would likely impose significant initial and ongoing costs on Managers. Proposed Rule 205 and the Proposal to Amend CAT could impose large initial costs and ongoing compliance costs on broker-dealers.

<sup>180</sup> See *infra* Part VIII.D.1 (for additional discussion on potential abusive short selling practices).

<sup>181</sup> See *infra* Part VIII.D.1. The Commission expects that for many securities, a limited number of Manager positions may surpass the reporting requirement thresholds. Given the eventual public release of the aggregate position sizes, there is a risk that other market participants will be able to potentially identify the Managers with large short positions and orchestrate short squeeze efforts against them (should they seem vulnerable against a short squeeze). Nevertheless, the Commission maintains the ability of identifying such behavior using CAT data, which could mitigate initiation of such behavior.

The Commission has considered the economic effects of the Proposals and wherever possible, the Commission has quantified the likely economic effects of the Proposals. The Commission is providing both a qualitative assessment and quantified estimates of the potential economic effects of the Proposals where feasible. The Commission has incorporated data and other information to assist it in the analysis of the economic effects of the Proposals. However, as explained in more detail below, because the Commission does not have, and in certain cases does not believe it can reasonably obtain, data that may inform the Commission on certain economic effects, the Commission is unable to quantify certain economic effects. Further, even in cases where the Commission has some data, quantification is not practicable due to the number and type of assumptions necessary to quantify certain economic effects, which render any such quantification unreliable. Our inability to quantify certain costs, benefits, and effects does not imply that the Commission believes such costs, benefits, or effects are less significant. The Commission requests that commenters provide relevant data and information to assist the Commission in quantifying the economic consequences of Proposed Rule 13f-2, Proposed Form SHO, Proposed Rule 205, and Proposal to Amend CAT.

### B. Economic Justification

The Commission is proposing the required Manager reporting and disclosures, in part, to implement the specific statutory mandate of Section 929X of the Dodd-Frank Act. Accordingly, many of the costs and benefits of Proposed Rule 13f-2 and Proposed Form SHO stem from the Commission's response to the statutory mandate. In addition, the Commission is exercising discretion in its design and implementation of Proposed Rule 13f-2 and Proposed Form SHO, and recognizes that this discretion has economic effects. Specifically, the Commission is using this discretion to ensure that the proposed disclosures are additive to currently available data and would be useful to both market participants and regulators, with a focus on addressing data limitations exposed by the market volatility in January 2021. Finally, Proposed Rule 205 and Proposal to Amend CAT address such data limitations outside of the context of the statutory mandate of Section 929X.

CAT data, as well as other currently available data, can be used by regulators for surveillance, examinations, investigations, and other enforcement



functions, for the analysis and reconstruction of market events, and for more general market analysis and research. At times, these activities would benefit from information on customer or market participant positions and how those positions change over time. CAT was not designed to track such positions, and Staff experience in reconstructing the events of January 2021 provided insights into the challenges of using existing CAT data for this purpose. Other existing data sources, including public data sources, are also limited for these purposes and also for informing members of the public and market participants. Specifically, current data (1) fails to distinguish economic short exposure from hedged positions or intraday trading, (2) fails to distinguish the type of trader short selling or identify individual short positions, even for regulatory use, and (3) fails to capture the various ways that short positions can change and the various ways to acquire short exposure. The Proposals are designed to address these data limitations.

Existing data sources fail to accurately represent the economic short exposures of Managers due to several limitations. While existing data report aggregate short positions on a bi-monthly basis, they do not reflect the timing with which short positions expand or shrink in the two-week period between the two reporting dates.<sup>182</sup> Some data sources report daily short sale volume<sup>183</sup> without distinguishing short sale transactions that affect economic short exposures from those meant for purposes such as liquidity provision or hedging of long positions. As such, the existing short volume data may not be combined with the bi-monthly short interest data to construct aggregate daily short positions. Existing securities lending data that may be considered indirect measures of short interest are expensive, incomprehensive, and

<sup>182</sup> FINRA requires all members to report settled short positions in equities of all customer and proprietary accounts twice per month. According to the schedule it has adopted, FINRA publishes the short sale data about a week after each reporting due date. See, e.g., Short Interest Reporting, available at <https://www.finra.org/filing-reporting/regulatory-filing-systems/short-interest>.

<sup>183</sup> FINRA reports daily off-exchange short sale volume data that aggregate, for each exchange-listed security, short sale transactions reported to a FINRA TRF or ADF. See *Short Sale Volume Data*, FINRA, available at <https://www.finra.org/finra-data/browse-catalog/short-sale-volume-data>. Registered exchanges also report daily short sale volume aggregated at the security level, often charging a fee. See, e.g., *TAQ Group Short Sales & Short Volume*, New York Stock Exchange, available at <https://www.nyse.com/market-data/historical/taq-nyse-group-short-sales>.

biased—in particular, security loans may serve purposes other than covering short positions, e.g., cover failure to deliver or borrowing cash by the lender. No existing data identify short positions by individual traders. Even though some regulatory data identify short transactions of individual traders, they may not be utilized to reconstruct short positions because economic short exposure may change in the absence of any short sale transactions.

These data limitations inhibit regulators from performing functions such as market surveillance and market reconstruction. For example, the Commission would not have regular access to information about Managers who hold large short positions even if those positions are held for a long period of time. If the positions are sufficiently large and prices move against the positions, the Commission cannot currently efficiently assess the risk that the positions impose on the market more broadly. Additionally, with existing data the Commission may have difficulty reconstructing significant market events—inhibiting the Commission in quickly understanding market events and providing efficient market oversight.

The data limitations also prevent the market from more fulsome interpretations of existing short selling information. For example, existing data can show a short interest level, but little is known about how much of that short interest level is directional or hedged and the extent to which short positions change between short interest disclosures.

### C. Baseline

#### 1. Institutional Investment Managers

The potential universe of persons who meet the definition of Manager is expansive. Exchange Act Section 13(f)(6)(A) defines the term “institutional investment manager” as “includ[ing] 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.”<sup>184</sup> Exchange Act Section 3(a)(9) states that “[t]he term ‘person’ means a natural person, company, government, or political subdivision, agency, or instrumental subdivision of a government.” “‘Company’ means a corporation, a partnership, an association, a joint-stock company, a trust, a fund, or any organized group of persons whether

<sup>184</sup> See also Exchange Act Section 3(a)(35) defining when a person exercises “investment discretion” with respect to an account.

incorporated or not; or any receiver, trustee in a case under title 11 of the United States Code or similar official or any liquidating agent for any of the foregoing, in his capacity as such.”<sup>185</sup> As a result, Managers exercising discretion over the accounts of others could include but are not limited to investment advisors 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; corporations, including broker-dealers and insurance companies, managing corporate or employee investment assets; and individuals exercising investment discretion over the accounts of others. Also as a result of the definition of Manager, the set of Managers excludes natural persons buying and selling securities only for their own account but does include natural persons exercising discretion over the account of another person.<sup>186</sup>

Notwithstanding the broad statutory definition of Manager, it is the Commission’s understanding that only a fraction of Managers are believed to engage in short selling and fewer still engage in any significant short selling. Market makers, for example, engage in short selling but, with the exception of option market makers, generally do not hold large positions overnight. We are also aware, for example, that advisers to both hedge funds and registered investment companies engage in short selling to varying degrees. However, with the exception of hedge funds, institutional investors are viewed as “largely absent” from the short selling portion of the financial markets.<sup>187</sup>

<sup>185</sup> See Section 2(a)(8) of the Investment Company Act. The term “company” in the Exchange Act “ha[s] the same meaning[] as in the Investment Company Act of 1940.” Exchange Act Section 3(a)(19).

<sup>186</sup> To the extent that a natural person exercising discretion over the account of another person has a short position exceeding the proposed thresholds, that natural person would be subject to the costs associated with Proposed Rule 13f-2 and the Proposed Form SHO. We expect such a natural person would likely use the fillable web form provided by EDGAR to input Proposed Form SHO disclosures. The Commission believes that few Managers that are natural persons would be likely to have short positions large enough to exceed the threshold. See *infra* Section VIII.D.7 for more information on Managers’ costs.

<sup>187</sup> Peter Molk and Frank Partnoy, *Institutional Investors as Short Sellers?*, 99 B.U. L. Rev. 837, 839 (2019), available at <https://scholarship.law.ufl.edu/cgi/viewcontent.cgi?article=1980&context=facultypub>. Molk and Partnoy’s paper “identif[ies] the regulatory and other barriers that keep key categories of institutions[, specifically, mutual funds, insurance companies, banks, sovereign

Using actual investment strategies employed by registered investment companies<sup>188</sup> as a proxy for the number of Managers in the public fund markets engaged in short selling, the number of such Managers is likely to be relatively small. A Division of Economic and Risk Analysis White Paper survey of all mutual fund Form N-SAR filings in 2014 found that “[w]hile 64% of all funds were allowed to engage in short selling, only 5% of all funds actually did so.”<sup>189</sup> As of September 2021, there were 7,043 registered investment companies with total equity positions valued at approximately \$17 trillion. Of those, 152 funds had short positions with a total short position value of approximately \$17.5 billion. Of the funds with short positions of approximately \$17.5 billion, only 37 funds held positions equal to or greater than \$10 million.<sup>190</sup> Additionally, according to an analysis of publicly available Form PF data, a substantial minority of single-strategy hedge funds employ strategies involving short selling.<sup>191</sup>

wealth funds, endowments, and foundations,] from acquiring significant short positions.” *Id.* at 843.

<sup>188</sup> As of July 2021, there were 10,223 mutual funds (excluding money market funds) with approximately \$18,588 billion in total net assets, 2,320 ETFs organized as an open-end fund or as a share-class of an open-end fund with approximately \$6,447 billion in total net assets, 736 registered closed-end funds with approximately \$314 billion in total net assets, 722 unit investment trusts with approximately \$2,456 billion in total net assets, and 13 variable annuity separate accounts registered as management investment companies on Form N-3 with \$218 billion in total net assets. Estimates of the number of registered investment companies and their total net assets are based on an analysis of Form N-CEN filings as of July 31, 2021. For open-end management funds, closed-end funds, and management company separate accounts, total net assets equals the sum of monthly average net assets across all funds in the sample during the reporting period. See Item C.19.a (Form N-CEN). For UITs, we use the total assets as of the end of the reporting period, and for UITs with missing total assets information, we use the aggregated contract value for the reporting period instead. See Item F.11 and F.14.c in Form N-CEN.

<sup>189</sup> Daniel Deli *et al.*, Use Of Derivatives By Registered Investment Companies at 8, *DERA White Paper* (2015), available at <https://www.sec.gov/files/derivatives12-2015.pdf>.

<sup>190</sup> This is based on an analysis of data provided by registered investment companies to the Commission on Form N-PORT.

<sup>191</sup> As of 2021 Q2, there are 1,124 hedge funds out of 6,083 Single-Strategy hedge funds (excluding fund-of-funds hedge funds) that employ short selling in an Equity Long/Short strategy (1,062), Equity Short-Biased strategy (18), or Fixed Income Convertible Arbitrage strategy (44). Assets under management (AUM) in these types of hedge funds total approximately \$1.165 trillion. 2021 Q2 Private Fund Statistics, Division of Investment

While information about Managers’ investments other than from funds managed by investment advisers is limited, the Commission understands that such other Managers, other than options market makers due to their routine use of hedging transactions, do not frequently establish short positions that would be large enough to be subject to the proposed rule’s reporting requirement.<sup>192</sup> The Commission believes one possible proxy for the number of Managers that could potentially have a reporting obligation is a fraction of the number of Managers reporting positions on Form 13F because such persons by definition manage accounts holding Section 13(f) securities having an aggregate fair market value of at least \$100 million, making such Managers more likely to have the resources to engage in short selling over the proposed rule’s thresholds. As of March 31, 2021, 7,550 Managers with investment discretion over approximately \$39.79 trillion reported holdings on Form 13F in Section 13(f) securities.<sup>193</sup> The Commission also believes that registered

Management Analytics Office, available at <https://www.sec.gov/divisions/investment/private-funds-statistics.shtml>. Data includes both U.S. and non-U.S. domicile hedge funds managed by SEC-registered investment advisers with at least \$150 million in private fund assets under management. The data does not include hedge funds that were classified as multi-strategy on Form PF. These hedge funds could employ short selling as part of their multi-strategy. Data for non-U.S. domicile hedge funds with an equity short-bias strategy is not publicly available for 2021 Q2. In this case the last publicly available values were used (7 funds with a total AUM of \$1 billion) from 2019 Q3. As of the end of 2021, hedge fund assets totaled approximately \$4 trillion. Global Hedge Fund Industry Assets Top \$4 Trillion for the First Time, Reuters (Jan. 20, 2022), available at <https://www.reuters.com/business/finance/global-hedge-fund-industry-assets-top-4-trillion-first-time-2022-01-20/>.

<sup>192</sup> For example, according to Molk and Partnoy “insurance companies generally are not active short sellers. Short selling by insurance companies is used almost exclusively to hedge positions, and generally is not used with respect to equity positions at all.” *Supra* note 187 at 850. See also Molk and Partnoy discussion about banks and trusts. “Trust administrators . . . have a history of adopting conservative investment strategies. Although shorting can be used to reduce risk when matched with similar long positions, using short selling as an income generation tool is not consistent with the overall conservative investment tradition.” *Id.* at 854.

<sup>193</sup> See Enhanced Reporting of Proxy Votes by Registered Management Investment Companies; Reporting of Executive Compensation Votes by Institutional Investment Managers, Exchange Act Rel. No. 93169, (Oct. 15, 2021) available at <https://www.govinfo.gov/content/pkg/FR-2021-10-15/pdf/2021-21549.pdf>.

investment advisers, particularly those managing hedge funds, are the primary Managers likely to be affected by the Proposed Rule. Though the Commission lacks data to quantify the number affected parties, the Commission estimates that the total number of Managers with reporting obligations will be between 346 and 1,000.<sup>194</sup>

## 2. Short Selling

Short selling is a widely used market practice, which allows investors to profit if an asset declines in value or to hedge risks. Market participants can build an economic short positions using traditional means (*i.e.*, borrowing shares and selling them into the market to buy back later) or they can gain short exposure using derivatives. This section provides an overview of the current state of obtaining short exposure to equities and the different means of short selling—*i.e.*, traditional means and using derivatives. This information is based on the current state of research using existing data.

### i. Short Selling Equities

A short sale is the sale of a security that the seller does not own or any sale that is consummated by the delivery of a security borrowed by, or for the account of, the seller.<sup>195</sup> In general, short selling is used to profit from an expected downward price movement, to provide liquidity in response to unanticipated demand, or to hedge the risk of an economic long position in the same security or in a related security. To short sell a stock, the short seller borrows shares of a stock from a lender—typically a long-term investor such as a mutual fund or pension fund—and sells those shares into the market. Later, the short seller purchases the same number of shares and returns them to the lender. The profit on the transaction for the short seller is the difference between the price at which the shares were initially sold and the price at which the investor re-purchased the shares—less any fees such as securities lending fees. If the price of the stock goes down then this difference will be positive and the investor will make money.

<sup>194</sup> See *supra* section VII.B.2. for more information on the estimates of how many managers would have reporting obligations.

<sup>195</sup> See Rule 200(a) of Regulation SHO, 17 CFR 242.200(a). See also Regulation SHO Adopting Release, *supra* note 4.

In addition to short selling based on negative sentiment, market participants also short sell to hedge existing positions. Hedging is a particularly potent motive to short sell a stock for options market makers who can hedge the risk of writing a call option by short selling the underlying stock in the stock market. Other investors use short selling to hedge out an unwanted component of a stock's return. For example, an investor who wants to buy a particular stock to trade on stock specific information but does not want to expose itself to industry risk can hedge industry risk by short selling an industry index ETF while purchasing the underlying security. Market makers also use short selling extensively to maintain two sided quotes in the temporary absence of inventory. Lastly, traders may use short selling as part of algorithmic trading strategies attempting to detect temporary pricing anomalies. While short selling to trade on information or to hedge generally results in short positions that are held for some time, market makers and algorithmic technical traders generally close their positions by the end of the day and thus their short positions generally do not show up in existing measures of short interest.<sup>196</sup>

Short selling generally entails more risk than holding a long position. At worst, a buyer of a long position can lose its entire investment. This is not true for a short seller. If the stock price increases from the short sale price, the investor loses money and since prices could potentially rise indefinitely, the short seller could lose more than the value of its original investment. Additionally, margin requirements for short selling are typically 150%—including the proceeds of the short sale plus an additional 50% of the value of the short position.<sup>197</sup> If the stock price

<sup>196</sup> See *infra* Part VIII.C.4.i (for a discussion of existing short interest data).

<sup>197</sup> Regulation T specifies that in most situations margin requirements for equity short sales must be

goes up, the investor may receive a margin call, which would require the investor to commit additional assets to meet margin requirements. To protect itself from losses, if an investor is unable to meet margin requirements, the broker-dealer may close the short position at a significant loss to the short seller. These dynamics can make it difficult for investors to maintain short positions in highly volatile stocks.

Short selling is facilitated by the securities lending market. Borrowing shares generally occurs two days after the short sale is executed. This is because stock market transactions normally settle two business days after the transaction occurs, while securities lending transactions settle on the same day.<sup>198</sup> Consequently, a short seller (or their broker-dealer) will gauge the ability to borrow shares prior to executing the short sale, referred to as obtaining a “locate,” but would actually borrow the share on the day that they are required to deliver the share to settle the stock market transaction.

Short selling is prevalent in equity markets in general. A common ratio used to capture the amount of short selling is the short interest ratio, which measures the fraction of shares sold short at a given point in time divided by the total shares outstanding for that security. Figure 1 below presents the time series average for short interest outstanding for equities with different characteristics. This Figure shows that

150%. See 12 CFR 220.12 (1998), available at <https://www.ecfr.gov/current/title-12/chapter-II/subchapter-A/part-220/section-220.12>.

<sup>198</sup> There have been recent efforts by industry members to shorten the settlement cycle to one business day. Furthermore, the Commission has proposed to shorten the settlement cycle. Shortening the Securities Transaction Settlement Cycle, Exch. Act Rel. No. 94196 (Feb. 9, 2022) available at <https://www.sec.gov/rules/proposed/2022/34-94196.pdf>. See also SIFMA, ICI, DTCC and Deloitte, *Accelerating the U.S. Securities Settlement Cycle to T+1* (Ver. 1.0) (Dec. 1, 2021), available at <https://www.sifma.org/wp-content/uploads/2021/12/Accelerating-the-U.S.-Securities-Settlement-Cycle-to-T1-December-1-2021.pdf>.

short interest tends to be higher for small-cap stocks than for mid- or large-cap stocks.

Another way to measure the prevalence of short selling in financial markets is by analyzing the fraction of transactions that involve a short seller. Short sellers are involved in nearly 50% of trading volume, while only about 2% of shares outstanding are held short in the U.S. equity markets.<sup>199</sup> This average volume of short selling tends to be much higher than the typical changes in short interest,<sup>200</sup> suggesting that a significant fraction of short selling volume is reversed very quickly. Such short selling may be more indicative of the fact that short selling is a key component of modern market making strategies and technical algorithmic trading.<sup>201</sup>

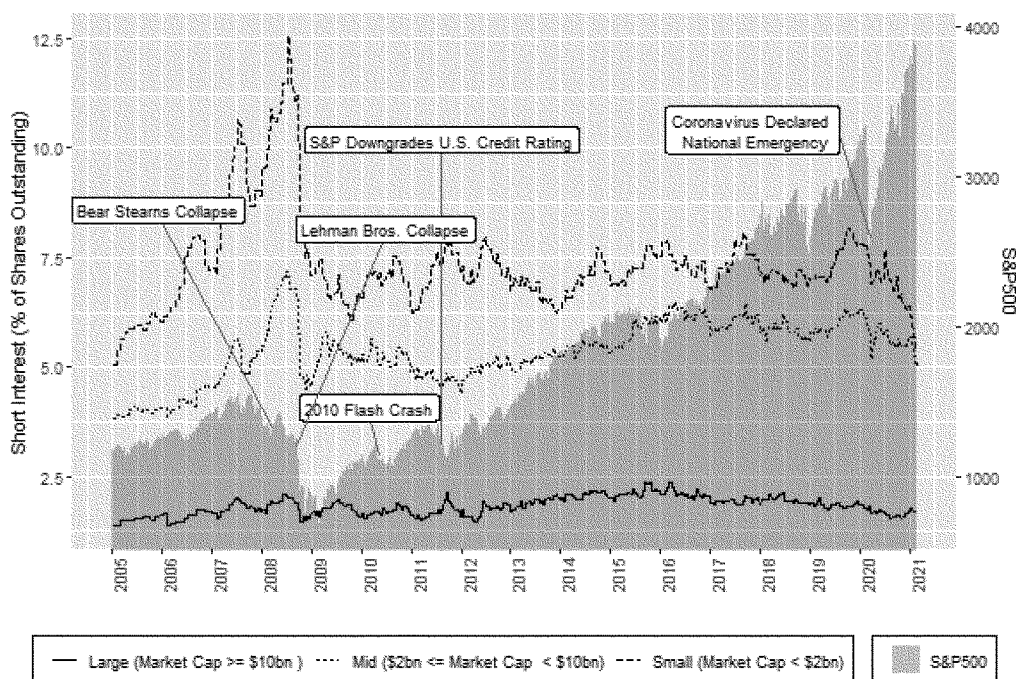
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<sup>199</sup> See *supra* note 6, Figure F.1 in the DERA 417(a)(2) Study (showing that the level of short selling as a percentage of trading volume grew from 2007 to 2013 to about 50%). See also D. Rapach, M.C. Ringgenberg, and G. Zhou, *Short Interest and Aggregate Stock Returns*, J. of Fin. Econ. 46–65 (2016).

<sup>200</sup> The Commission analyzed trading volume for common shares during the year 2019. This analysis revealed that the average common share during this period traded approximately five percent of shares outstanding each week, with approximately half of all trades involving short sellers. Consequently, total short selling volume amounts to approximately five percent of shares outstanding every two weeks for a typical stock. In contrast, from 2015–2019, absolute changes in short interest approximately every two weeks have equaled about a half of a percent of shares outstanding. Thus the total amount of short selling volume occurring is an order of magnitude larger than the changes in short interest over the same time period. These statistics suggest that the majority of short selling transactions likely do not involve long term traders building short positions. Additionally, the correlation coefficient for bi-monthly changes in short interest and short selling volume in 2019 is only about 0.018. This low correlation suggests that the economic forces driving total short selling volume and changes in short interest are likely different.

<sup>201</sup> See *infra* Part V.4.iii (for a more detailed discussion of short selling and liquidity provision).

Figure 1: Short Interest Ratio for Non-Financial Common Stocks, Jan. 2005 – Feb. 2021



This figure plots the weighted average short interest ratio for three groups of stocks based on market capitalization on a bi-weekly basis from for January 2005 to February 2021. Large cap stocks are defined as having a market capitalization of greater than \$10 billion, mid cap as \$2 billion to less than \$10 billion, and small cap as less than \$2 billion. We estimate the short interest ratio for each stock as the number of shares in short interest reported by the exchanges on a bi-weekly basis and obtained from the Compustat North America Supplemental Short Interest File (for NYSE- and Nasdaq-listed stocks), divided by shares outstanding obtained from the Center for Research in Security Prices, LLC (CRSP) daily stock files. Since short interest is reported as of the settlement date, we match short interest to the trading date two days prior to the short interest report date. The sample includes non-financial (i.e., excluding stocks with SIC code between 6000 and 6999) and common stocks (i.e., CRSP share code of 10 or 11). Following Blocher & Ringgenberg (2019), we discard stocks whose short interest ratio and adjusted short interest ratio (where the adjusted short ratio is adjusted for stock splits, buybacks, etc.) differ by more than 10%, in order to exclude potential asynchronous adjustments for stock splits in the shares outstanding and short interest datasets. Furthermore, stock-date observations for which a stock has multiple *gvkey*'s (Compustat identifier) or *permno*'s (CRSP identifier) per date are removed. We then take the value-weighted average short interest ratio within a group, using market capitalization as weights. Market capitalization is calculated as shares outstanding multiplied by the closing price (obtained from the CRSP daily stock files) two days prior to the short interest record date. S&P 500 values are obtained from the CRSP Index file. See Jesse Blocher, Matthew C. Ringgenberg, et al., *When Do Short Sellers Exit Their Positions?*, SSRN (Aug. 27, 2018), available at <https://ssrn.com/abstract=2634579>

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## ii. Taking Short Positions via Derivatives

Trading in derivatives affects short selling in two key ways. First, derivatives offer investors an alternative means to express negative sentiment rather than short selling the stock. For instance, an investor wishing to profit from the decline of a security's value can also trade in various derivative contracts, including options and security-based swaps. Confirming this

alternative means of short selling, academic research shows that investors do indeed use options as an alternative means to obtain short-like economic exposure when standard short selling is restricted.<sup>202</sup>

<sup>202</sup> See Robert Battalio and Paul Schultz, *Regulatory Uncertainty and Market Liquidity: The 2008 Short Sale Ban's Impact on Equity Option Markets*, 66 J. of Fin. 2013–2053 (2011); B.D. Grundy, B. Lim, and P. Verwijmeren, *Do Option Markets Undo Restrictions on Short Sales? Evidence from the 2008 Short-Sale Ban*, 106 J. of Fin. Econ. 331–348 (2012). See also G.J. Jiang, Y. Shimizu, and C. Strong, *Back to the Futures: When Short Selling*

Among the most popular derivative contracts are options, specifically put and call options. Call options give the owner of the option the right but not the obligation to purchase a stock at a specific price on a future date. Put options are similar, but give the owner

*is Banned* (2019), available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3420275](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3420275).

of the option the right but not the obligation to sell a stock at a specific price at a future date. In a put option the seller of the option is taking a long position in the underlying security while the purchaser of the put is taking a short position. The opposite is true for a call option.

In addition to options, convertible securities (in which the security can be converted into an equity security) and security-based swaps can be used to create the same economic exposure as a short position.<sup>203</sup> Security-based swaps include total-return swaps in which two counterparties agree to exchange or “swap” payment with each other as a result of changes in a security characteristic, such as the its price.<sup>204</sup> As with options, in each of these derivative contracts one party is inherently long and the other party is inherently short. These derivatives, and other more exotic derivatives, tend not to be as standardized as options, and are traded over-the-counter. Security-based swap transactions are reported to and publicly disseminated by security-based swap data repositories.<sup>205</sup>

In addition to providing an alternative means of expressing a bearish sentiment, trading in derivatives frequently leads to related trading in the stock market as derivatives’ counterparties seek to hedge their risk. For example, an options market maker who sells a put has taken on long

<sup>203</sup> On September 19, 2019 the Commission approved the “Recordkeeping and Reporting Requirements for Security-Based Swap Dealers, Major Security-based Swap Participants, and Broker-Dealers” which established a regulatory regime for security-based swaps under Title VII of the Dodd-Frank Act. See *Recordkeeping and Reporting Requirements for Security-Based Swap Dealers, Major Security-Based Swap Participants, and Broker-Dealers*, Exchange Act Release No. 87005 (Sept. 19, 2019), 84 FR 68550 (Dec. 16, 2019), available at <https://www.sec.gov/rules/final/2019/34-87005.pdf>.

<sup>204</sup> On July 9, 2012, the Commission approved rules and definitions of Security based swaps. See 17 CFR 230, 240–241; *Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”*; *Mixed Swaps; Security-Based Swap Agreement Recordkeeping*, Commodity Futures Trading Commission and Securities and Exchange Commission, available at <https://www.sec.gov/rules/final/2012/33-9338.pdf>.

<sup>205</sup> See, e.g., *Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information*, Exchange Act Release No. 74244 (Feb. 11, 2015), 80 FR 14563 (Mar. 19, 2015) (“2015 Regulation SBSR Adopting Release”); *Security-Based Swap Data Repository Registration, Duties, and Core Principles*, Exchange Act Release No. 74246 (Feb. 11, 2015), 80 FR 14437 (Mar. 19, 2015); *Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information*, Exchange Act Release No. 78321 (July 14, 2016), 81 FR 53545 (Aug. 12, 2016) (“2016 Regulation SBSR Adopting Release”). See also *Order Approving Application for Registration as a Security-Based Swap Data Repository*, available at <https://www.sec.gov/rules/other/2021/34-91798.pdf>.

exposure to the underlying security and may hedge this position by opening a short position in the underlying security. Thus, option market makers who sell large quantities of put options may amass large short positions in the underlying equities to hedge their options exposure.

### 3. Current Short Selling Regulations

Compliance with Regulation SHO began on January 3, 2005.<sup>206</sup> The Commission adopted Regulation SHO to update short sale regulation in light of numerous market developments since short sale regulation was first adopted in 1938 and to address concerns regarding persistent failures to deliver and potentially abusive “naked” short selling.<sup>207</sup>

In adopting Regulation SHO, the Commission recognized that short sales can provide important pricing information<sup>208</sup> and liquidity to the market.<sup>209</sup> However, the Commission was also concerned with the negative effect that failures to deliver may have on shareholders and the markets. For example, large and persistent failures to deliver may deprive shareholders of the benefits of ownership, such as voting and lending, and sellers that fail to deliver securities on settlement date may attempt to use their failures to engage in trading activities to improperly depress the price of a security.

Due to continued concerns regarding failures to deliver, and to promote

<sup>206</sup> See Regulation SHO Adopting Release, *supra* note 3.

<sup>207</sup> In a “naked” short sale, the seller does not borrow or arrange to borrow the securities in time to make delivery to the buyer within the standard two-day settlement cycle. As a result, the seller fails to deliver securities to the buyer when delivery is due (also known as a “failure to deliver”).

<sup>208</sup> Efficient markets require that prices fully reflect all buy and sell interest. Market participants who believe a stock is overvalued may engage in short sales in an attempt to profit from a perceived divergence of prices from true economic values. Such short sellers add to stock pricing efficiency because their transactions inform the market of their evaluation of future stock price performance. This evaluation is reflected in the resulting market price of the security. See Exchange Act Release No. 48709 (October 28, 2003), 68 FR 62972 (November 6, 2003), available at [https://www.sec.gov/rules/proposed/34-48709.htm#P179\\_15857](https://www.sec.gov/rules/proposed/34-48709.htm#P179_15857).

<sup>209</sup> Market liquidity is generally provided through short selling by market professionals, such as market makers, who offset temporary imbalances in the buying and selling interest for securities. Short sales effected in the market add to the selling interest of stock available to purchasers, and reduce the risk that the price paid by investors is artificially high due to a temporary contraction of selling interest. Short sellers covering their sales also may add to the buying interest of stock available to sellers. See Exchange Act Release No. 48709 (October 28, 2003), 68 FR 62972 (November 6, 2003), available at [https://www.sec.gov/rules/proposed/34-48709.htm#P179\\_15857](https://www.sec.gov/rules/proposed/34-48709.htm#P179_15857).

market stability and preserve investor confidence, the Commission has amended Regulation SHO on several occasions. For example, the Commission eliminated certain original exceptions to Regulation SHO’s close-out requirements,<sup>210</sup> strengthened those same close-out requirements by adopting Rule 204,<sup>211</sup> and reintroduced a short sale price test restriction by adopting Rule 201.<sup>212</sup> In addition, the Commission adopted a targeted antifraud rule, Rule 10b–21, to further address failures to deliver in securities that have been associated with “naked” short selling.<sup>213</sup>

<sup>210</sup> As initially adopted, Regulation SHO included two major exceptions to its then existing close out requirements: The “grandfather” provision and the “options market maker” exception. Due to continued concerns regarding failures to deliver, and the fact that the Commission continued to observe certain securities with failures to deliver that were not being closed out consistent with its then existing close out requirements, the Commission eliminated the “grandfather” provision in 2007 and the “options market maker” exception in 2008. See Exchange Act Release No. 56212 (Aug. 7, 2007), 72 FR 45544 (Aug. 14, 2007) (eliminating the “grandfather” provision to Regulation SHO’s close out requirement), available at <https://www.sec.gov/rules/final/2007/34-56212fr.pdf>; Exchange Act Release No. 58775 (Oct. 14, 2008), 73 FR 61690 (Oct. 17, 2008) (eliminating the “options market maker” exception to Regulation SHO’s close out requirement), available at <https://www.sec.gov/rules/final/2008/34-58775fr.pdf>.

<sup>211</sup> In 2008, the Commission adopted temporary Rule 204T, and in 2009 adopted Rule 204. Rule 204 further strengthens Regulation SHO’s close out requirements by making those requirements applicable to failing to deliver results from sales of all equity securities, while reducing the time-frame within which failures to deliver must be closed out. See Exchange Act Release No. 60388 (July 27, 2009), 74 FR 38266 (July 31, 2009), available at <https://www.sec.gov/rules/final/2009/34-60388fr.pdf>.

<sup>212</sup> In 2004, the Commission initiated a year-long pilot to study the removal of short sale price tests for approximately one-third of the largest stocks. After review of the pilot’s data, the Commission proposed the elimination of all short sale price tests. In June 2007, the Commission adopted a rule that eliminated all short sale price tests, including Rule 10a–1, a predecessor to Regulation SHO. The rule became effective in July 2007. In 2010, the Commission reinstated a short sale price test restriction by adopting Rule 201. See Exchange Act Release No. 61595 (Feb. 26, 2010), 75 FR 11232 (Mar. 10, 2010), available at <https://www.sec.gov/rules/final/2010/34-61595fr.pdf>.

<sup>213</sup> Rule 10b–21 is an antifraud provision intended to supplement existing antifraud rules, including Rule 10b–5, and to further evidence the liability of short sellers. This includes broker-dealers acting for their own accounts, who deceive specified persons about their intention or ability to deliver securities in time for settlement, while failing to deliver securities by settlement date. Among other things, the rule highlights the specific liability of short sellers who deceive their broker-dealers about their source of borrowable shares for purposes of complying with Regulation SHO’s “locate” requirement, or who misrepresent to their broker-dealers that they own the shares being sold and subsequently fail to deliver shares. See *supra* note 12, Exchange Act Release No. 58774, available at <https://www.sec.gov/rules/final/2008/34-58774.pdf>.

Regulation SHO requires broker-dealers to properly mark sale orders as “long,” “short,” or “short exempt,” to locate a source of shares prior to effecting a short sale (also known as the “locate” requirement), and to close out failures to deliver that result from long or short sales. In addition, if the price of an equity security has experienced significant downward price pressure, Regulation SHO temporarily restricts the price at which short sales may be effected.

Regulation SHO’s four general requirements are summarized below:

- **Rule 200—Marking Requirement.** Rule 200(g) requires that a broker-dealer mark all sell orders of any equity security as “long,” “short,” or “short exempt.” A sell order may only be marked “long” if the seller is “deemed to own” the security being sold and either (i) the security to be delivered is in the physical possession or control of the broker or dealer; or (ii) it is reasonably expected that the security would be in the physical possession or control of the broker or dealer no later than the settlement of the transaction. The “short exempt” marking requirement applies only with respect to the Rule 201 short sale price test circuit breaker noted below.

- **Rule 203(b)(1) and (2)—“Locate” Requirement.** Rule 203(b)(1) generally prohibits a broker-dealer from accepting a short sale order in an equity security from another person, or effecting a short sale in an equity security for its own account, unless the broker-dealer has borrowed the security, entered into a bona-fide arrangement to borrow the security, or has reasonable grounds to believe that the security can be borrowed so that it can be delivered on the date delivery is due. Rule 203(b)(2) provides an exception to the locate requirement for short sales effected by a market maker in connection with “bona-fide” market making activities.

- **Rule 204—Close out Requirement.** Rule 204 requires a participant of a registered clearing agency (*i.e.*, a clearing member) to deliver securities to a registered clearing agency for clearance and settlement on a long or short sale transaction in any equity security by settlement date, or to immediately close out a failure to deliver by borrowing or purchasing securities of like kind and quantity by the applicable close out date. For a short sale, a participant must close out a failure to deliver by no later than the beginning of regular trading hours on T+3. For a long sale, or for activity that is attributable to “bona-fide” market making activities, a participant must close out a failure to deliver by no later

than the beginning of regular trading hours on T+5.

- **Rule 201—Short Sale Price Test Circuit Breaker.** Rule 201 generally prevents short selling, including potentially manipulative or abusive short selling, from driving down further the price of a security that has already experienced a significant intraday price decline, and facilitates the ability of long sellers to sell first upon such a decline. Rule 201 contains a short sale circuit breaker that, when triggered by a price decline of 10% or more from a covered security’s prior closing price, imposes a restriction on the price at which the covered security may be sold short (*i.e.*, must be above the current national best bid). Once triggered, the price restriction would apply to short sale orders in that security for the remainder of the day and the following day, unless an exception applies.

In addition, Rule 105 of Regulation M generally prohibits participation in secondary offerings by persons who have sold short during the restricted period before the offering.

Regulation SHO imposes certain recordkeeping obligations on broker-dealers. However, the Commission does not have any information on how often the bona fide market making exception is used. Furthermore, bona fide market making information is not reported on a regular basis, instead the Commission must request bona fide market making records on a broker-dealer by broker-dealer basis.<sup>214</sup>

In addition, regulations currently do not require market participants to record, report, or track when short sellers buy-to-cover their short sales. This makes it difficult for regulators to assess compliance with Rule 105 and with close out requirements in Rule 204.

#### 4. Existing Short Selling Data

There are several sources of short selling data that are available both publicly and for regulatory purposes. In general, these data sources lack information about levels of and the timing of changes in economic short exposure for specific managers in specific securities. Some sources report aggregate short positions at the security level, but their content is not granular enough to further the understanding of short selling strategies. Other sources provide granular short volume information, but they are unable to distinguish short transactions that impact short positions from those that

<sup>214</sup> See *supra* Part VI.B (Reliance on Bona Fide Market Making Exception, for more information on the inefficiencies of not having a systematic way of capturing bona fide market making activities).

do not and do not contain all activity that can change short positions. Some regulatory data sources report short transactions at the individual investor level, but estimating short positions using these data would be significantly inaccurate and inefficient.

#### i. Bi-Monthly Short Interest Data

One of the primary data sources for aggregate short selling data is the bi-monthly short interest data collected by FINRA.<sup>215</sup> FINRA collects aggregate short interest information in individual securities on a bi-monthly basis as the total number of shares sold short in a given stock as of the middle and end of each month. Then the exchange that lists the given stock, or FINRA itself in the case of OTC stocks, distributes the collected data.<sup>216</sup> FINRA computes short interest using information it receives from its broker-dealer members pursuant to FINRA Rule 4560 reflecting all trades cleared through clearing broker-dealers.<sup>217</sup> FINRA Rule 4560 requires generally that broker-dealers that are FINRA members report “short positions” in customer and proprietary firm accounts in all equity securities twice a month through FINRA’s web-based Regulation Filing Applications (RFA) system.<sup>218</sup> FINRA defines “short positions” for this purpose simply as those resulting from “short sales” as defined in Rule 200(a) of Regulation SHO under the Exchange Act.<sup>219</sup> Member firms must report their short positions to FINRA regardless of position size.<sup>220</sup> The process of gathering and validating short interest data takes approximately two weeks.<sup>221</sup> Thus the data is available with approximately a two week lag.

These short interest data are widely available and are used by academics and

<sup>215</sup> See *supra* note 6, DERA 417(a)(2) Study at 17–18.

<sup>216</sup> See *Short Interest—What It Is, What It Is Not*, FINRA Inv’r Insights (Apr. 12, 2021), available at <https://www.finra.org/investors/insights/short-interest>.

<sup>217</sup> *Id.* (Short interest for a listed security at any date reported by FINRA is “a snapshot of the total open short positions in a security existing on the books and records of brokerage firms on a given date.”).

<sup>218</sup> FINRA Rule 4560 excludes short sales in “restricted equity securities,” as defined in Securities Act Rule 144, from the reporting requirement.

<sup>219</sup> See FINRA Rule 4560(b)(1).

<sup>220</sup> See FINRA Market Regulation Department, *General for Short Interest Reporting Instructions*, (Dec. 18, 2008) (reporting instructions to FINRA member firms), available at <https://www.finra.org/Industry/Compliance/RegulatoryFilings/ShortInterestReporting/P037072>.

<sup>221</sup> See *supra* note 6, DERA 417(a)(2) Study at 17–18.

other market participants.<sup>222</sup> These short interest data are found to predict future stock and market returns over the monthly and annual horizons, suggesting that the bi-monthly short interest data capture the economic short selling based on fundamental research.<sup>223</sup> However, these data face two major limitations.<sup>224</sup> First, the information content does not provide insight into the timing with which short positions are established or covered over the two-week reporting period. This precludes the possibility of understanding the behavior of aggregate economic short selling in the two weeks leading up to the reporting date of the positions. Second, given that short interest is aggregated at the security-level, the aggregation prevents the Commission and the public from understanding certain aspects of the underlying short selling activity. For example, the data cannot inform on whether short sentiment is broadly or narrowly held or the extent to which existing short interest is hedging in nature or based on short sentiment.

#### ii. Short Selling Volume and Transactions From SROs

Since 2009, many SROs have been publishing two short selling data sets, including same day publication of daily aggregated short sale volume in individual securities<sup>225</sup> and publication of short sale transaction information on no more than a two-month delay.<sup>226</sup>

<sup>222</sup> See *supra* note 182 (FINRA and the listing exchanges make these data publicly available with bi-weekly updates).

<sup>223</sup> See, e.g., Peter N. Dixon and Eric K. Kelley, *Business Cycle Variation in Short Selling Strategies: Picking During Expansions and Timing During Recessions*, J. of Fin. and Quantitative Analysis (Forthcoming); see also Ekkehart Boehmer, Zsuzsa R. Huszar, and Bradford D. Jordan, *The Good News in Short Interest*, 96 (1) *Journal of Financial Economics* 80–97 (2010); Stephen Figlewski, *The Informational Effects of Restrictions on Short Sales: Some Empirical Evidence*, 16 (4) J. of Fin. and Quantitative Analysis 463–476 (1981).

<sup>224</sup> See *supra* note 33.

<sup>225</sup> See *Short Sale Volume and Transaction Data*, available at <https://www.sec.gov/answers/shortsalevolume.htm>; (showing hyperlinks to the websites where SROs publish this data). See also *supra* note 183. See, e.g., *FINRA's Daily Short Sale Volume Files* (which provide aggregated volume by security on all short sale trades executed and reported to a FINRA reporting facility during normal market hours). See FINRA Information Notice, *Publication of Daily and Monthly Short Sale Reports* (Sept. 29, 2009), available at <https://www.finra.org/sites/default/files/NoticeDocument/p120044.pdf>.

<sup>226</sup> See *FINRA's Monthly Short Sale Transaction Files* (which provide detailed trade activity of all short sale trades reported to a consolidated tape. See *supra* note 183; See also *Short Sale Volume and Transaction Data*, available at <https://www.sec.gov/answers/shortsalevolume.htm>. Additional transaction data has been available at various times, including transaction data from the Regulation SHO

Some SROs make the historical daily short volume data available to market participants for a fee.<sup>227</sup> The fact that market participants and academic users pay these subscription fees indicate that these data are utilized. In addition to these daily short volume data, FINRA provides intraday short sale transaction information for the orders that execute and information from FINRA's Trade Reporting Facility ("TRF") and Alternative Display Facility ("ADF")<sup>228</sup> (the TRF and ADF are together referred to herein as "FINRA's Reporting Facilities"). Overall, these different sources of daily and intraday short volume data provide greater, though different, levels of granularity relative to the bi-monthly short interest observations discussed earlier.

Despite offering higher granularity, these existing short volume data provided by the SROs and FINRA have a number of limitations. First, the data does not provide insight into the activities of either individual traders, or different trader types. Consequently, it is not possible with existing short selling data provided by the SROs and FINRA to separate trading volume associated with market makers, algorithmic traders, investment managers, or other trader types.

Additionally, the data does not provide insight into activities that may reduce short exposure, thus using these data to estimate investor sentiment is fraught. For example, these data provide information only on short sales, whereas short positions could also change

Pilot, which has been discontinued by most exchanges in July 2007 when the uptick rule was removed. See Exchange Act Release No. 55970 (Jun. 28, 2007), 72 FR 36348 (July 3, 2007), available at <https://www.sec.gov/rules/final/2007/34-55970.pdf>. The Pilot data comprised short selling records available from each of nine markets: American Stock Exchange, Archipelago Exchange, Boston Stock Exchange, Chicago Stock Exchange, NASD, Nasdaq Stock Market, New York Stock Exchange, National Stock Exchange, and the Philadelphia Stock Exchange. See SEC Division of Trading and Markets, *Regulation SHO Pilot Data FAQ*, available at <https://www.sec.gov/spotlight/shopilot.htm#pilotfaq>.

<sup>227</sup> See, e.g., *TAQ Group Short Sale & Short Volume, New York Stock Exchange*, available at <https://www.nyse.com/market-data/historical/taq-nyse-group-short-sales> (for short sale data relating to all NYSE owned exchanges). See *Short Sale Volume and Transaction Reports from Nasdaq Trader*, available at <https://nasdaqtrader.com/Trader.aspx?id=shortsale> (for short sale data for Nasdaq exchanges); see also *Short Sale Daily Reports, Chicago Board Options Exchange*, (for Cboe exchanges) available at [https://www.cboe.com/us/equities/market\\_statistics/short-sale/](https://www.cboe.com/us/equities/market_statistics/short-sale/).

<sup>228</sup> Each TRF provides FINRA members with a mechanism for the public reporting of transactions effected otherwise than on an exchange. See FINRA, *Market Transparency Trade Reporting Facility*, available at <https://www.finra.org/Industry/Compliance/MarketTransparency/TRF/>.

because investors can increase or decrease their positions in ways other than short selling the stock. For example, investors can increase their short positions by exercising put options and delivering borrowed shares or by delivering borrowed shares when they are assigned call options. Investors can reduce their short positions in an equity when they, for example, buy to cover their positions, purchase shares in a secondary offering, convert bonds to stock, or redeem ETF shares containing the equity. As a result of this, the short selling volume and transactions data cannot easily explain changes in short interest, exposing a gap between these two types of existing data.

Aggregate short selling statistics and short selling transactions data have different lags with which they are available. Aggregate short selling volume statistics are usually put out by the SROs by the end of the following business day. For the transactions data, the lag can be much longer, and in some cases the data is released with a one month lag—implying that some short selling transactions data are not available for two months.

There is also a concern that these data may over-represent the total volume of short sales occurring in the market. This is because Regulation SHO provides specific criteria regarding what is a long sale.<sup>229</sup> If a market participant is unclear whether their trade would meet all the requirements at settlement to be marked a long sale, then they may choose to mark the trade as short to not run afoul of Regulation SHO requirements, even if the trade is likely an economic long sale.<sup>230</sup>

#### iii. Securities Lending

Securities lending data provides information on stock loan volume, lending costs, and the percentage of available stock out on loan, which some market participants use as measures of short selling.<sup>231</sup> The securities lending

<sup>229</sup> See Rule 200(g) of Regulation SHO specifies when an order can be marked as long. See also Part III.B; note 4 Regulation SHO Adopting Release.

<sup>230</sup> See 2009 letter from Securities Industry and Financial Markets Association ("SIFMA") commenting on an alternative short sale price test, expressing concern that compliance with Regulation SHO short selling marking requirements "will result in a substantial over-marking of orders as "short" in situations where firms are, in fact, "long" the securities being sold." Letter from Securities Industry and Financial Markets Association ("SIFMA Letter"), available at <https://www.sec.gov/comments/s7-08-09/s70809-4654.pdf>.

<sup>231</sup> Several commercial entities sell data on securities lending to clients. See, e.g., 2011 Letter from Data Explorers ("Data Explorers Letter") (in response to the request for comment relating to the proposed study of the cost and benefits of short selling required by Dodd Frank Act Section

industry appears to use securities lending data widely, though it is generally available only by subscription.<sup>232</sup>

The use of security lending data as proxy for economic short interest is associated with at least two major setbacks. First, commercial vendors of the securities lending data often impose access restrictions via high nominal subscription fees or give-to-get models. In this setting, the entities contributing data are mindful of whether other entities can access to the data. As such, participation rates in data sharing reflects strategic considerations that may lower the extent of data shared by each entity, reducing the information content of the pool of the data collected by each vendor. The market for these data is dominated by three major vendors, making it difficult for a given market participants to obtain access to comprehensive security lending information from one source. To this end, the existing data accessible by an individual market participant may not accurately proxy short selling activity. Second, while securities lending may be correlated with short selling, it is not a perfect measure of short selling. In practice, securities lending may be used for purposes other than short sales such as to cover failure to deliver or to borrow cash. In addition, short selling that is covered within the trading day does not require any loans, and vendors of commercial securities lending data do not have complete information. For example, they have less than 100% of the negotiated loans and no information on borrowing from margin accounts.<sup>233</sup>

417(a)(2)), available at <https://www.sec.gov/comments/4-627/4627-152.pdf>. As some commenters have noted, stock lending facilitates short selling. See, e.g., *Speech by Chester Spatt, former Chief Economist of the SEC* (April 20, 2007), available at <https://www.sec.gov/news/speech/2007/spch042007css.htm>. The information sold by vendors may include volume of loans, lending costs, and the percentage of available stock out on loan. This data offers indirect evidence of short selling, and some research has used stock lending data as a proxy for actual short sales. See, e.g., Oliver Wyman, *The Effects of Short Selling Public Disclosure of Individual Positions on Equity Markets*, Alternative Investment Management Association (Feb. 2011), available at <https://www.oliverwyman.com/our-expertise/insights/2010/feb/the-effects-of-short-selling-public-disclosure-regimes-on-equity.html>.

<sup>232</sup> See *supra* note 6, DERA 417(a)(2) Study at 22–23.

<sup>233</sup> See *supra* note 6, DERA 417(a)(2) Study at 23. The Commission has recently proposed a new rule, Rule 10c–1, and if adopted as proposed, the Commission and market participants would have access to comprehensive securities lending data market data that would significantly improve current securities lending based short selling estimates. See *Reporting of Securities Loans*, Exchange Act Release No. 93613, available at <https://www.sec.gov/rules/proposed/2021/34-93613.pdf>.

#### iv. CAT Data

Regulators can also extract short sale information from CAT data, which provides order lifecycle information for stocks and options.<sup>234</sup> The data contain an order mark that is a part of the “material terms of the trade” that indicates whether an order is a short sale. This order mark allows regulators to identify traders who are short selling and to see the order entry and execution times of these short sales. However, CAT was not designed to track traders’ positions or changes in those positions, but rather collects information to analyze trading and order lifecycles. As such, using CAT data to estimate positions and changes in those positions can be challenging.

Theoretically, one could use the order execution information in CAT data to estimate trader positions and track how those positions change over time. However, such estimates could be inaccurate in several circumstances. First, CAT data do not include information on the long or short positions held in each account at the time that Industry Members started reporting, so CAT does not provide an appropriate starting point for building short positions using investor-specific transaction information. Second, some investors may establish or cover short positions via other means that are not CAT reportable events, for example: Secondary offering transactions; option assignments; option exercises; conversions; or ETF creations and redemptions. Additionally, until the Customer Account Information System (CAIS) system goes live, which is expected in July 2022, there is no easy way to match Firm Designated ID (FDIDs) in CAT to individual Managers. Thus it is not currently feasible to identify the subset of CAT data pertaining to Managers. However, once the CAIS system goes live it would be possible for regulators to identify individuals in CAT, even if those individuals use multiple broker-dealers.

CAT is not designed to track positions. However, when focused on one or few accounts, estimating positions, though potentially inaccurate, can be manageable. Using transaction information to track positions across a broad set of positions is inefficient. Even in situations in which the above limitations do not apply, the use of CAT data to estimate short positions and changes in those positions for all or a large set of accounts is inefficient and would require a tremendous amount of processing power, which would take

<sup>234</sup> It is important to note that only regulators have access to CAT data.

time and reduce the processing power available for other CAT queries. This hinders the Commission’s estimation of short positions in a timely fashion.

Other than the inefficient means of estimating positions described above, CAT does not distinguish buy orders that establish a long position from those that cover, and therefore reduce, a short position. While Commission staff were able to identify some short covering activity during the volatile period in January 2021, due to the difficulties described above, the staff analyzing the volatility associated with meme stocks could not easily identify short covering activity using CAT data alone and was thus hindered in their reconstruction of key events.

Finally, even though CAT data identifies short selling by market makers, the data do not provide information as to whether a broker-dealer is claiming use of the Regulation SHO exceptions for bona fide market making.

There are 24 national securities exchanges and one national securities association (FINRA) that are CAT Plan Participants. There are also 3,734 broker-dealers who have reporting obligations to CAT, as Industry Members. These Industry Members often use third-party reporting agents such as service bureaus for CAT reporting.

#### v. Exchange Act Form SH

For a ten-month period in 2008 and 2009,<sup>235</sup> the Commission required certain institutional investment managers to submit confidential weekly reports of their short positions in Section 13(f) securities, other than options, on Exchange Act Form SH, through Temporary Rule 10a3–T.<sup>236</sup> *De minimis* short positions of less than 0.25% of the class of shares with a fair market value of less than \$10 million were not required to be reported.<sup>237</sup> Additionally, only Managers that

<sup>235</sup> See *supra* note 6, DERA 417(a)(2) Study at 18.

<sup>236</sup> With respect to each applicable Section 13(f) security, the Form SH filing was required to identify the issuer and CUSIP number of the relevant security and reflect the manager’s start of day short position, the number and value of securities sold short during the day, the end of day short position, the largest intraday short position, and the time of the largest intraday short position. The reporting requirement was implemented via a series of emergency orders followed by an interim final temporary rule, Rule 10a3–T. Exchange Act Release No. 58591 (Sept. 18, 2008), 73 FR 55175 (Sept. 24, 2008); Exchange Act Release No. 58591A (Sept. 21, 2008), 73 FR 58987 (Sept. 25, 2008); Exchange Act Release No. 58724 (Oct. 2, 2008), 73 FR 58987 (Oct. 8, 2008); Exchange Act Release No. 58785 (Oct. 15, 2008), 73 FR 61678 (Oct. 17, 2008).

<sup>237</sup> See Exchange Act Release No. 58591 (Sept. 18, 2008), 73 FR 55175 (Sept. 24, 2008).



exercise investment discretion with respect to accounts holding Section 13(f) securities having an aggregate fair market value of at least \$100 million were required to report. The investment manager was required to report short positions to the Commission on Form SH on a nonpublic basis on the last business day of each calendar week immediately following any calendar week in which it effected short sales,<sup>238</sup> a more frequent disclosure interval than the quarterly public reporting of long positions required on Exchange Act Form 13F.<sup>239</sup>

In addition to the limited and temporary time period during which disclosure of short positions was required to be reported on Exchange Act Form SH, even at the regulatory level, the reporting requirements and data had several drawbacks and limitations. One drawback was that only Managers who exercised investment discretion with respect to accounts holding Section 13(f) securities having an aggregate fair market value of at least \$100 million were required to file Form SH, which excluded short-only funds and other large short sellers who did not file Form 13F. Additionally, the report was costly as Managers filing Form SH had a weekly reporting requirement. Additionally, data fields in Form SH including start of day short position, gross number of securities sold short during the day, and end of day short position were each subject to the *de minimis* reporting threshold, which resulted in unreported data points when only a subset of the fields exceeded the *de minimis* threshold. Furthermore, Form SH data were not validated for errors such as duplicate entries, missing fields, or positions that were below the *de minimis* threshold and therefore did not need to be reported, which make the data difficult to work with.<sup>240</sup>

## 5. Competition

Many Managers operate in the investment management industry.<sup>241</sup> In broad terms, investment management is a highly competitive industry. Investment managers compete for investors and investor funds. Among the bases on which Managers compete are returns, fees and costs, trading strategies, risk management, and the ability to gather information. It is costly for investment managers to do market research to gain an informational advantage. Investment managers who

own a security have an advantage over those who don't in that a security owner can more cheaply trade on negative information by simply selling whereas investment managers not owning the same security must establish some form of short exposure, such as selling a security short, to capitalize on any negative information that they've uncovered. Academic research suggests that when the cost of short selling increases, a security owner's advantage in terms of being able to profitably trade on gathered information increases, leading investors not owning a security to engage in less fundamental research.<sup>242</sup>

Investment managers, like other investors that could be subject to Proposed Rule 13f-2, also compete by using proprietary trading strategies. They typically seek to trade in ways that would not expose their strategies because, if their strategies became known to others, the strategies could lose value and such Managers could also suffer higher trading costs. More specifically, other traders could use copycat trading strategies try to mimic the Managers' strategy, potentially competing away the profitability of the strategy or other traders could anticipate when the Managers might trade, which could result in higher trading costs for the Manager. Some Managers also compete for returns by engaging in securities lending whereby assets are lent to other investors, often short sellers, for a fee. These fees in aggregate can be substantial.<sup>243</sup>

Additionally, there are 3,734 broker-dealers. These broker-dealers also compete with each other for order flow. The broker-dealer industry is a highly competitive industry with reasonably low barriers to entry. Most trading activity is concentrated among a small number of large broker-dealers, with thousands of small broker-dealers competing for niche or regional segments of the market. To limit costs and make business more viable, the small broker-dealers often contract with bigger broker-dealers to handle certain functions, such as clearing and

execution, or to update technology. Larger broker-dealers often enjoy economies of scale over smaller broker-dealers and compete with each other to service the smaller broker-dealers who are both their competitors and customers.<sup>244</sup> Broker-dealers compete in multiple ways: reputation, convenience, and fees. Broker-dealers typically pass operating costs down to their customers in the form of fees.

## D. Economic Effects<sup>245</sup>

### 1. Investor Protection and Market Manipulation

The Proposals could lead to better investor protection by improving regulators' reconstruction of significant market events. They may also assist regulators in identifying manipulative short selling strategies. Improved identification of manipulative short selling strategies may also serve as a deterrent to would be manipulators and thus may help prevent manipulation. They would also improve the Commission's observation of systemic risk. However, to the extent that Managers may still be holding their short positions when the data becomes public, the Commission believes that Proposed Rule 13f-2 and Proposed Form SHO also could in some cases facilitate potentially manipulative strategies, such as certain short squeezes. The Commission also believes that Proposed Rule 205 and the Proposal to Amend CAT would improve regulators' oversight of markets.

The Commission believes that the Proposals would enhance the Commission's and SRO's reconstruction of significant market events by providing a clearer view into the role that short selling plays in market events of interest. Specifically, the Commission could have used the buy to cover information that would be provided by Proposed Rule 205 and data from Proposed Form SHO to reconstruct market events and better understand the link between short sellers exiting their positions and contemporaneous price volatility during the recent volatility associated with meme stocks. For example, while short sellers as a whole were exiting their positions during the

<sup>238</sup> See Exchange Act Release No. 58785, 73 FR at 61678.

<sup>239</sup> *Id.*

<sup>240</sup> See *supra* note 80 (information on the methodology and caveats of using Form SH data).

<sup>241</sup> See *supra* Part VIII.C.1.

<sup>242</sup> This occurs because if an investor not owning the asset engages in fundamental research and discovers evidence that a stock may be overpriced, then it is costly for that investor to act on that information. This is not true for investors who own the asset as they can simply sell the shares that they own. See, e.g., Peter N. Dixon, *Why Do Short Selling Bans Increase Adverse Selection and Decrease Price Efficiency?*, 11 (1) *The Rev. of Asset Pricing Studies* 122–168 (2021).

<sup>243</sup> The securities lending market is large and complex. See Part VI.B. (the proposing release for proposed Rule 10c-1 for a more detailed description of this market and players), available at <https://www.sec.gov/rules/proposed/2021/34-93613.pdf>.

<sup>244</sup> See CAT proposing release Part VII.A, available at <https://www.sec.gov/rules/proposed/2010/34-62174.pdf>.

<sup>245</sup> In preparing this economic analysis, the Commission accounted for the various types of Managers that could be subject to the reporting requirements. In general, the Commission believes that the economic effects of the rule are more influenced by the Managers' investment strategy and motivation for short selling rather than by the type of Manager that is reporting. Any exceptions are noted in the analysis. See *supra* Section VIII.C.1.

period of heightened volatility it may have been the case that large short sellers were acting differently.

The data that would be provided in Proposed Form SHO would have provided information the Commission could have used after the fact to examine separately short selling behavior of large short sellers. Additionally, because short positions often take some time to create, the Commission could have attempted to quickly identify individual short sellers with large short positions in the various meme stocks in January 2021 based on the most recent reports; then the Commission could have used the enhanced CAT data to understand how these short sellers traded during the heightened volatility.<sup>246</sup>

Additionally, the activity data provided in Proposed Form SHO would allow the Commission to observe how large short sellers responded to the heightened volatility, albeit with a time lag due to the filing deadline. Specifically, the Commission would be able to observe more precisely which days reporting short sellers were most actively increasing or decreasing their short positions and correlate that activity to market conditions on those days. The “activity categories” reported in Proposed Form SHO would allow regulators to identify the specific means by which large short sellers alter their economic short exposure on high volatility days. For example, economic short exposure may increase due to increased number of shares sold, issuing call options, exercising put options, as well as other activities that could raise the Manager’s short position.

<sup>246</sup> It is currently not straightforward to map CAT transactions to individual traders as the Firm Designated ID (FDID) assigned to each account are broker-dealer specific. Thus to map a trade reported in CAT to an individual trader would require requesting the specific FDID for a given trader. This lack in functionality is expected to change when the CAIS becomes operational. This system would allow regulators to map individual traders to their FDID’s and thus pull CAT information specifically for individual traders. Thus, while technically feasible, pulling data from CAT for specific traders is difficult, but will become much less so when the CAIS system becomes operational. The CAIS system is expected to go live in July 2022. See *Timeline, Consolidated Audit Trail*, available at <https://www.catnmsplan.com/timeline>. Additionally, some academics have critiqued the Commission Staff’s GameStop report, the Report on Equity and Options Market Structure Conditions in Early 2021, available at <https://www.sec.gov/files/staff-report-equity-options-market-structure-conditions-early-2021.pdf>, and some of its methods, which were driven by data availability. See Joshua Mitts, Robert Battalio, Jonathan Brogaard, Matthew Cain, Lawrence Glosten, and Brent Kochuba, *A Report by the Ad Hoc Academic Committee on Equity and Options Market Structure Conditions in Early 2021* (working paper) (2022), available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4030179](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4030179).

In contrast, economic short exposure may decrease due to purchase of shares to cover short positions, exercising call options, issuing put options, obtaining shares through secondary offerings or tendered conversions, and other activities that reduce short exposure. Receiving data about each of these categories separately would facilitate more efficient oversight by regulators.

Analysis of the data during periods of high volatility could help the Commission maintain fair and orderly markets by highlighting key economic channels and mechanisms through which short selling could affect periods of volatility or how periods of volatility affect short selling. This information can, in turn, allow the Commission to more specifically tailor responses to similar or related events in the future. While the CAT data provided by Proposed Rule 205 and the CAT amendment data would be provided relatively quickly, the Proposed Form SHO data would not be available for up to a one-month lag. Consequently, while the Proposed Form SHO data would be useful in recreating a significant market event after the fact, it would not provide the Commission tools to examine an immediate crisis.

The “bona fide market making” information from the Proposal to Amend CAT would facilitate regulatory analysis of the use of the bona fide market making exceptions to Regulation SHO.<sup>247</sup> The bona fide market making information from the Proposal to Amend CAT would provide regulators investigating potential Regulation SHO violations with more regular access to clearer evidence of whether a market maker was relying on a bona fide market making exception. This could save a significant amount of time during an investigation. Having regular access to these data would provide the Commission with insight into whether the exceptions for bona fide market making in Regulation SHO Rules 203 and 204 are being used appropriately, which should assist in assessing

<sup>247</sup> Two Regulation SHO rules include exceptions for bona fide market making. Rule 203(b)(2)(iii) exempts market makers selling short in connection with bona fide market making activities from the requirement that a short seller must either borrow or have reasonable grounds to believe he can borrow a security in time for delivery prior to effecting a short sale. See 17 CFR 242.203(b)(2)(iii). Rule 204(a)(3) provides that a failure to deliver positions attributable to bona fide market making activities by registered market makers, options market makers, or other market makers obligated to quote in the over-the-counter markets, must be closed out by no later than the beginning of regular trading hours on the third consecutive settlement day following the settlement date (T+5), rather than the settlement day following the settlement date (T+2). See 17 CFR 242.204(a)(3).

compliance with, and thus the benefits of, Regulation SHO.

The “bona fide market making” information and hedge information could improve regulators’ ability to interpret certain information in market reconstructions. Market reconstructions can sometimes benefit from regulators knowing when certain activity is either directional or market neutral because the motives and profitability of such trading types are different. The ‘bona fide market making’ information would help regulators separate short selling that represents market makers’ liquidity provision to facilitate investor demand from other short selling, including other market maker short selling. Because such short selling is more likely to be in response to customer demand, the shorts are less likely to signify that the short seller anticipates a price decline than if the short seller was trading directionally. Likewise, the hedging information on Proposed Form SHO would provide information on whether a Manager’s position is fully or partially hedged at the end of the month. From this, regulators could assess, for example, that the activity reported on Proposed Form SHO during the month was likely not related to hedging activity if the end of month position is not hedged, particularly if the previous month’s position was not hedged.

Additionally, the data provided by Proposed Rule 13f–2 and Proposal to Amend CAT would allow the Commission to detect certain types of fraud in a timelier manner. The data provided by Proposed Rule 13f–2 would improve the timeliness of fraud detection because the Proposed Form SHO data would provide the Commission quick flags that may signal potential fraud. Additionally, the enhanced CAT data would provide the Commission with regular access to improved information with which to examine potential instances of fraud without needing to ask broker-dealers for information.

Improved detection of fraud may also help deter fraud, improving price efficiency and market quality. Some market participants and academics have raised concerns that short selling may in some instances offer the potential for stock price manipulation, including “short and distort” campaigns.<sup>248</sup> In

<sup>248</sup> See, e.g., Comment letters submitted with regards to Short Sale Reporting Study Required by Dodd-Frank Act Section 417(a)(2); See letters from Naphtali M. Hamlet (May 6, 2011); Jan Sargent (May 6, 2011); Lee R. Donais, President and CEO, L.R. Donais Company (May 8, 2011); Joseph A. Scilla (May 9, 2011); Jane M. Reichold (May 17, 2011); John Gensen (May 18, 2011); Victor Y. Wong (May

“short and distort” strategies, which are illegal, the goal of manipulators is to first short a stock and then engage in a campaign to spread unverified bad news about the stock with the objective of panicking other investors into selling their stock in order to drive the price down.<sup>249</sup> If a “short and distort” campaign is suspected, then detecting this behavior via the activity and positions data in Proposed Form SHO would be easier than it would be using current data. Short and distort campaigns are more likely to occur in stocks with lower market capitalizations with less public information.<sup>250</sup> Consequently, among these stocks it may not, in dollar terms, take a very large short position to reach the 2.5% threshold in securities of smaller reporting issuers or the \$500,000 threshold in securities of non-reporting issuers to report Proposed Form SHO.<sup>251</sup> As a result, it is likely that an entity engaging in such a practice would be required to report Proposed Form SHO data. Consequently, if “short and distort” type behavior were to be suspected, then the Commission would be more likely to identify individuals with large short positions and could thus quickly focus any inquiries on entities in an economic position to potentially profit from manipulation. Then regulators could match buy to cover trading on individual days to statements or other actions of the

20, 2011); Kevin Rentzsch (May 24, 2011); Lynn C. Jasper (May 27, 2011); Donald L. Eddy (May 28, 2011); Al S. (Jun. 10, 2011); Jeffrey D. Morgan, President and CEO, National Investor Relations Institute, at 3 (Jun. 21, 2011) (“NIRI”); Professor James J. Angel, at 2 (June 24, 2011); and Dennis Nixon, CEO and Chairman, International Bancshares Corporation, at 1 (July 18, 2011). See all letters are available at <https://www.sec.gov/comments/4-627/4-627.shtml>.

<sup>249</sup> If successful, the scheme can drive down the price, allowing the manipulators to profit when they “buy-to-cover” their short position at the reduced price. Short sellers could also engage in price manipulations by systematically taking short positions in one firm while taking long positions in the competitor. See Bodie Zvi, Alex Kane, and Alan J. Marcus, *Investments and Portfolio Management*, McGraw Hill Education (2011). See also Rafael Matta, Sergio H. Rocha, and Paulo Vaz, *Predatory Stock Price Manipulation*, available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3551282](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3551282).

<sup>250</sup> See, e.g., Y. T. F. Wong and W. Zhao, *Post-Apocalyptic: The Real Consequences of Activist Short-Selling*, (Working Paper) (2017), available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2941015](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2941015).

<sup>251</sup> Academic research has found that the average short interest in stocks targeted by activist short sellers is about ten percent, while it is only four percent for non-targeted firms. Consistent with high information asymmetries, targeted firms also appear to have wider bid-ask spreads and higher disagreement among analysts. See W. Zhao, *Activist Short-Selling and Corporate Opacity* (Working Paper) (2020), available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2852041](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2852041).

investor which may indicate that the investor was engaging in such behavior. Regulators could then use CAT data to investigate further the trading activity of the alleged manipulator.

There are other manipulations, which the data from the Proposals would help regulators identify. For example, one theoretical study suggests that if managers’ decision-making is influenced by shifts in stock prices, then short sellers could potentially negatively affect managerial decisions by depressing stock prices when profitable projects are announced, which may lead managers to believe that their project is not good and to abandon it.<sup>252</sup> Doing so may lead to worse managerial decision making and lower stock prices. Another theoretical study argues that due to high levels of leverage and interconnectedness in the finance industry, if short sellers are successful at causing even small declines in stock price, then this can ripple through the financial system with large effects.<sup>253</sup> While the Commission notes that there is currently no empirical evidence that these types of manipulation occur or are widespread, should they be suspected, these types of manipulation could better be identified with the positions and activity data. The positions data would allow the Commission to quickly identify individuals with large short positions and then use the activity and CAT data to investigate their trading behavior to look for signs of manipulation. Improved detection capacity may also lead to decreased fraud as would be

manipulators choose not to engage in manipulative behavior due to increased fear of detection.<sup>254</sup>

Publicly releasing aggregated information about large short positions may, in some instances, increase the risk of trading behavior harmful to short sellers, namely short squeezes, though the Commission’s improved detection of

<sup>252</sup> See I. Goldstein and A. Guembel, *Manipulation and the Allocational Role of Prices*, 75 (1) *The Rev. of Econ. Studies* 133–164 (2008).

<sup>253</sup> See Markus K. Brunnermeier and Martin Oehmke, *Predatory Short Selling*, 18 (6) *Rev. of Fin. 2153–2195* (2014). Similarly, some have also asserted that short sellers may have played a role in the stock market crash at the beginning of the Great Depression. See, e.g., Jonathan R. Macey, Mark Mitchell, and Jeffrey Netter, *Restrictions on Short Sales: An Analysis of the Uptick Rule and its Role in View of the October 1987 Stock Market Crash*, 74 *Cornell L. Rev.* 799, 801–802 (1989) (collecting reports of such allegations).

<sup>254</sup> See letters from Christine Lambrechts (hereafter “Lambrechts Letter”), available at <https://www.sec.gov/comments/4-627/4627-14.htm>; see also International Association of Small Broker Dealers and Advisor, available at <https://www.sec.gov/comments/4-627/4627-109.pdf>. See NIRI Letter, available at <https://www.sec.gov/comments/4-627/4627-134.pdf>.

such potential manipulation could help deter it. The Commission estimates that 32% of stocks reported on Proposed Form SHO would only have one Manager above the reporting Threshold A.<sup>255</sup> If market participants can ascertain which positions belong to only one Manager,<sup>256</sup> then market participants may seek to orchestrate a short squeeze targeting that particular manager. Mitigating this risk is the fact that the data provided by Proposed Rule 13f–2, Proposed Form SHO and the Proposal to Amend CAT, particularly the activity data provided in Proposed Form SHO may allow the Commission to more quickly determine if a short squeeze occurred. The Commission could correlate buy-to-cover activity in Proposed Form SHO with price increases to look for signs of a squeeze. If it appears that a short squeeze may have occurred, the Commission could perform further analysis using the information in the Proposal to Amend CAT to attempt to determine the market participants involved in the squeeze.<sup>257</sup> Increased risk of detection may deter some market participants from seeking to orchestrate a short squeeze. The Reporting Threshold, aggregating the data by security prior to releasing it to the public, and the delay in releasing the data to the public are all designed to help mitigate this effect. Only Managers whose positions surpass the threshold would be required to report—limiting the number of Managers whose information would be aggregated and made public.

Despite not releasing Managers’ identities to the public, the nature and the position size thresholds that underlie publicly released information may lead to the risk of Managers being identified by the public. Focusing on stocks in which market participants can ascertain that only one Manager filed, combined with a Manager’s posts on social media, or other means, such as information discovered by a private investigator, market participants may be able to identify which Manager holds

<sup>255</sup> Based on analysis of Form SH data. See *supra* note 80 (for information on the methodology and caveats of using Form SH data).

<sup>256</sup> In many cases identifying which publicly released reports had only one Manager reporting may not be difficult. For example, if the total short positions reported in security with a market capitalization greater than \$400 Million (where the \$10 Million dollar threshold is hit before the percent of shares outstanding threshold) are less than \$20 million then market participants may be able to reasonably presume that there is only one Manager reporting a position.

<sup>257</sup> Identifying the market participants involved in fraud solely from CAT data is currently difficult, but would become less so when the CAIS system becomes fully operational.

the short position.<sup>258</sup> As such, the limited number of reporters potentially risks shining a spotlight on the few managers with large short positions. However, the delay before publicly releasing the data means that the information would not be as fresh and thus may not as accurately reflect current short positions.<sup>259</sup> Thus, if market participants sought to orchestrate a short squeeze based on the aggregated information made public based on the Proposed Form SHO data that the squeeze could fail if the short positions that are the target of the squeeze no longer exist. This may reduce the likelihood that market participants seek to orchestrate squeezes based on the publicly released Proposed Form SHO data which may help protect short sellers who maintain short positions for a longer horizon and thus may still hold the positions reported on the aggregated Proposed Form SHO data. Based on analysis using Form SH data, the Commission expects that most, but not all, of the short positions leading to reporting on Proposed Form SHO would be closed by the time that the aggregated Proposed Form SHO data is released.<sup>260</sup>

Having detailed information about which Managers currently hold large and unhedged short positions may also help the Commission observe potential systemic risk concerns regarding short selling. Large and concentrated short positions have the potential to increase systemic risk. As discussed previously, unlike a long transaction, short selling places an investor at risk of losing significantly more than their initial investment should the value of the

underlying asset increase significantly. Even temporary spikes in asset value can lead to significant losses—by triggering margin calls or even position liquidations if capital requirements cannot be met.<sup>261</sup> If the value of an underlying asset increases, a short seller may be required to post additional collateral to meet margin requirements. If the investor is unable to do so, then the investor's broker-dealer may liquidate the investor's position with existing collateral leading to steep losses for the short seller. Consequently, it may be more difficult for a short seller to ride out periods of turbulence than a long seller.

Manager level short position data of individuals with large short positions could allow the Commission to better observe these positions and more appropriately respond to any market events that arise. For example, in the context of the meme stock phenomenon in January 2021, if the Commission had the Proposed Form SHO data at the time then it would have had a clearer view as to which Managers held large short positions prior to the volatility event and thus which Managers were at greatest risk of suffering significant harm from a short squeeze.

All the effects, positive and negative, associated with the data collected by Proposed Rule 13f-2 discussed in this section would be limited by several factors. First, upon filing Proposed Form SHO would be checked for technical errors but not for the accuracy of the position and activity data in the Form. If Managers make mistakes in their calculations, such mistakes would reduce the utility of the data. However, the amendment process would require Managers to amend filings when they discover errors, thus promoting the accuracy of the information. The Commission also recognizes that there are limitations to Proposed Rule 205. For example, broker-dealers would be required to mark transactions as buy to cover based only on information that they currently have access to and they would not be required to net such activity across the same customer's accounts at that broker-dealer. This may miss some buy to cover trades that may occur if a Manager uses a broker to

execute transactions and a prime broker (or prime brokers) to manage positions. In this case, the broker-dealer managing the purchase of shares would not necessarily know that the buy is actually a buy to cover and would thus not mark the trade as such. The current proposal may also miss transactions that may occur if a Manager uses multiple accounts at the same broker-dealer to trade.

## 2. Effects on Stock Price Efficiency

The Commission believes that the Proposals may have uncertain effects on stock price efficiency.<sup>262</sup> The uncertain effects on price efficiency come because increased transparency generally increases efficiency whereas increased transparency could also discourage investors from gathering information—which harms price efficiency. This section discusses both the concept of price efficiency and the positive and negative impacts that the Proposals may have on price efficiency.

The publicly released aggregated data from Proposed Form SHO would provide new information to market participants about the aggregate activities of some short sellers—with a planned lag of approximately fourteen days from the end of the filing deadline.<sup>263</sup> Existing short selling data, such as the FINRA short interest data, is timelier than the potential data from the Proposed Rule 13f-2 and Proposed Form SHO, and it includes short interest for all short sales known to clearing broker-dealers but does not provide the Commission or the public daily information about short sellers' activities.

There is likely significant overlap between the information about stock fundamentals contained in FINRA short interest data and in the data that would be aggregated from Proposed Form SHO filings. However, the information in Proposed Form SHO filings focuses on Managers and indicates whether positions are fully or partially hedged, and provides daily net changes in positions. Thus, the Proposed Rule 13f-2 and Proposed Form SHO would increase the information available to investors about bearish sentiment in the market. For example, the information on the proportion of short interest made up of Managers with substantial positions, how much of those positions are fully or partially hedged, and the activity information would allow market

<sup>258</sup> For example, one issuer, upon learning that short sellers had taken a large short position in the issuer, reportedly sent a letter to all shareholders urging them to request physical custody of their shares from their broker-dealers in an apparent attempt to disrupt securities lending which supports short selling. This strategy appeared to work initially as the share price increased by nearly 50% in the subsequent three weeks. The issuer also hired private investigators to determine who was behind the short selling and filed suit against a well-known short seller. The issuer, however, entered bankruptcy less than a year later. The bankruptcy courts ruled that the issuer defrauded investors. *See* G. Weiss, *The Secret World of Short-Sellers*, *Business Week*, 62a (August 5, 1996). *See also* Owen A. Lamont, *Go Down Fighting: Short Sellers vs. Firms*, 2 (1) *The Rev. of Asset Pricing Studies* 1–30 (2012).

<sup>259</sup> Analysis of Form SH data found that short positions were held at or above the \$10 million or 2.5% thresholds only for an average of 9.85 days after the end of each month. *See* note 80 (for information on the methodology and caveats of using Form SH data).

<sup>260</sup> *See infra* note 265 (for a discussion on the Commission's estimates on how long Managers hold short positions). *See also infra* note 269 (for more information on short sellers that do hold their positions for long periods of time).

<sup>261</sup> Due to imperfect information and market frictions, a short seller who "does not have access to additional capital when security prices diverge . . . may be forced to prematurely unwind the position and incur a loss[.]" *See, e.g.*, Mark Mitchell, Todd Pulvino, and Erik Stafford, *Limited Arbitrage in Equity Markets*, 57 (2) *The J. of Fin.* 551–584 (2002). *See also, e.g.*, Andrei Shleifer and Robert W. Vishny, *The Limits of Arbitrage*, 52 (1) *The J. of Fin.* 35–55 (1997) and Denis Gromb and Dimitri Vayanos, *Limits of Arbitrage*, 2 (1) *Annu. Rev. Fin. Econ.* 251–275 (2010) (citations therein).

<sup>262</sup> *See infra* Part VIII.E.1 (for additional discussion of the effect of the Proposals on efficiency).

<sup>263</sup> *See supra* Part III.C (for more information on the delay of public dissemination of Proposed Form SHO data).

participants an enhanced view of short interest and provide insight on changes in short interest between short interest reports. Further, the use of the last settlement day of the month as the reference month for the Proposed Form SHO reports would allow for a direct comparison of the Proposed Form SHO data to the FINRA short interest data. With FINRA short interest as a reference point, the activity data may then provide insight to market participants about changes in total short interest from FINRA short interest report to FINRA short interest report. For example, market participants could potentially use the data on positions' changes to correlate periods of significant increases or decreases in short positions with corporate events or announcements to gather a more precise view of how the market views corporate actions or events and which events contributed to the final short interest tally at the end of the month.

Increased information may increase price efficiency. As such, the proposed publication of the aggregated Proposed Form SHO data represents new information that market participants could use to value stocks—increasing stock price efficiency. Price efficiency (also known as market efficiency) refers to how accurately prices reflect available information relevant to the value of the asset.<sup>264</sup> For example, this information may allow market participants to more effectively make trading decisions and manage risk—increasing price efficiency. Although, the majority of Managers' short positions would be closed by the time the aggregated data from Proposed Form SHO would be made public due to the lag in reporting and public dissemination, a portion of the short positions would still be open.<sup>265</sup> While the market reacts to unexpected short interest changes,<sup>266</sup> the ability to understand short interest and short interest changes should be additive information that would be reflected in prices upon publication. However, the increase in price efficiency from the publication of aggregated Proposed

Form SHO data is likely to be limited due to the delay in publication.

The Proposals may also improve price efficiency if they mitigate fraud as discussed in Part VIII.D.1. Fraud is inherently non-efficient trading and harms price efficiency because a fraudster's motive is to create a deviation of a firm's value from fundamentals and to profit from this deviation. Thus, to the extent that fraudulent trading, such as short and distort campaigns, are limited by regulator's access to the data provided by Proposed Form SHO, the Proposed Rule 13f-2 would result in improved price efficiency.

On the other hand, Proposed Rule 13f-2 may harm price efficiency by increasing the cost of short selling. Academic studies, both theoretical and empirical, have shown that when short selling becomes more costly, stock prices are less reflective of fundamental information both because costly short selling makes trading on information difficult, and because costly short selling dissuades investors from collecting information in the first place.<sup>267</sup>

Proposed Rule 13f-2 affects the value of short selling in four ways: Compliance costs, revealing short sellers' information, potentially revealing short sellers trading strategies, and increasing the threat of retaliation. First, the compliance costs associated with reporting large short positions are a direct increase in the cost of short selling.<sup>268</sup> As many Managers have underlying investors, these costs would likely be passed on to end consumers in the form of lower returns due to limiting the strategies that Managers could profitably employ.

Second, publicly releasing the aggregated Proposed Form SHO data has the potential to reveal some of the information that short sellers may have acquired through fundamental research. Revealing this information to the market may cause prices to adjust to the information that the short seller uncovered before the short seller is able to acquire their full desired position—decreasing the profits to acquiring the information and providing less incentive to produce fundamental research. Thus, the publication of Proposed Form SHO data represents an

additional cost to short selling in the form of potentially lower profitability for trading on negative information. That the data is aggregated and released on a lag mitigates this cost somewhat but does not eliminate it. To avoid price impacts, a short seller seeking to build a sizeable position in a firm generally does so by building up small positions over time until the desired position is accumulated.<sup>269</sup> Because short positions can take a long time to accumulate even with a lag the information motivating the trades being reported may not be stale. While aggregation limits the precision with which markets can estimate an individual short seller's motivation, it does not eliminate it.<sup>270</sup> Additionally, the threshold may protect short sellers with smaller short positions from having the information in their trades revealed. In contrast, the Proposed Rule 13f-2 may highlight very large positions potentially increasing the likelihood that some of the information contained in the trades of large short sellers would be acted on by other market participants before the short seller could acquire their optimal position. Thus, the Commission expects that publication of aggregated Proposed Form SHO data would still represent a cost to short selling.<sup>271</sup> Relatedly, Managers who build short positions that exceed the threshold may choose to

<sup>269</sup> See Albert S. Kyle, *Continuous Auctions and Insider Trading*, *Econometrica*: J. of the Econometric Society 1315–1335 (1985). See Kirilenko, Andrei, Albert S. Kyle, Mehrdad Samadi, and Tugkan Tuzun, *The Flash Crash: High-Frequency Trading in an Electronic Market*, 72 (3) *The J. of Fin.* 967–998 (2017) (for a discussion of this type of trading); Amir E. Khandani and Andrew W. Lo., *What Happened to the Quants in August 2007? Evidence from Factors and Transactions Data*, 14 (1) *J. of Fin. Markets*, 1–46 (2011) (for a discussion of what happens when investors build large positions without properly smoothing their trading). Well-known short seller Gabe Plotkin testified that his firm had built and maintained a short position in GameStop for over 5 years prior to the significant volatility experienced in January 2021. See *Game Stopped? Who Wins and Loses When Short Sellers, Social Media, and Retail Investors Collide* (Hearing), *U.S. House of Representatives Committee Repository* ("Game Stopped Hearing"), available at <https://docs.house.gov/Committee/Calendar/ByEvent.aspx?EventID=111207>; See also Juliet Chung and Melvin Capital Says It Was Short GameStop Since 2014, *Wall Street Journal* (Feb 17, 2021). In the Form SH data, 25% of positions were held above the proposed Threshold A for at least a month. See *supra* note 80.

<sup>270</sup> See *supra* Part VIII.D.1 (for a discussion of how market participants may be able to uncover individual identities).

<sup>271</sup> Consistent with this expectation, research on similar regulations in Europe has documented a similar effect there. See *Market Impact of Short Sale Position Disclosures*, *Copenhagen Economics: Office of Global Research and Markets at the MFA*, available at <https://www.copenhagoneconomics.com/publications/publication/market-impact-of-short-sale-position-disclosures>.

<sup>264</sup> See, e.g., Eugene Fama, *Efficient Capital Markets II*, 46(5) *J. Fin.* 1575–1617 (1991).

<sup>265</sup> The Commission estimates that the median number of days that the short position is held above the threshold after the end of the month is 0, while the average number of days that a short position is held above the threshold is 9.85 (suggesting that the majority of positions will be closed. Some are held longer than the delay in reporting).

<sup>266</sup> See, e.g., A. Senchack and L. Starks, *Short-Sale Restrictions and Market Reaction to Short-Interest Announcements*, *J. of Fin. and Quantitative Analysis* 177–194 (1993).

<sup>267</sup> See, e.g., *supra* note 242. See Dixon (2021). See Edward Miller, *Risk, Uncertainty, and Divergence of Opinion*, 32 (4) *The J. of Fin.* (1977). See Robert F. Stambaugh, Jianfeng Yu, and Yu Yuan, *The Short of It: Investor Sentiment and Anomalies*, 104 (2) *J. of Fin. Econ.* 288–302 (2012).

<sup>268</sup> See *infra* Part VIII.E.2 (for a discussion of how these direct costs may affect investors in funds that employ short selling).

execute the positions that are beyond the threshold at a pace that is faster than what they would have done otherwise to attempt to build their optimal position before information is disclosed and copy-cat investors are able to trade based on the reported data. Executing transactions at a faster speed than would be optimal imposes increased transaction costs on Managers than they would have incurred otherwise.<sup>272</sup> Additionally, trading faster than is optimal may harm price efficiency by leading prices to over-react to the aggressive trading.<sup>273</sup>

Third, the Proposed Form SHO data may provide information about the specific trading strategies of certain short sellers. For example, in the case where there is only one filer and market participants know this, then market participants could attempt to use the activity data to extract information about the specific trading strategies that short sellers use to implement their trades. Market participants could then try to identify similar patterns in the live data and alter their trading strategies to attempt to profit from any predictability in the short seller's trading strategy. This behavior would further limit the benefit to short selling as it may allow other market participants to game the short seller's trading behavior—increasing the cost of implementing short selling trading strategies. While the Commission acknowledges this risk, it believes that the proposed design of the published activity data would significantly limit this risk. In particular, the proposed netting of short selling activity across increases and decreases in short position along with showing only one number per day per security would mask much of the trading behavior of individual short sellers while still providing information about changes in bearish sentiment in the market. For example, Managers may build or reduce a short position using complex trading strategies potentially involving transactions on both sides of the market. By netting trading activity and aggregating across Form SHO filers, market participants viewing the publicly reported Form SHO data would still get a view of changes in bearish sentiment while keeping Manager specific trading strategies hidden.

The public disclosure requirements may also expose Managers to retaliation

by other market participants.<sup>274</sup> Although aggregating the data before releasing it to the public on a delay would provide some protection to Managers from having their identities uncovered, in certain cases motivated market participants may still be able to identify individual investors. For instance, in the case that the aggregated short position reported to the public is just above the threshold, one could reasonably assume that only one Manager has a short position large enough to report, which may facilitate identifying who that manager is. The Commission believes that even if the probability of identifying individual short sellers is low, the threat of this additional exposure to retaliation may disincentivize short selling. However, the Commission believes that on balance aggregating the data prior to publishing it provides appropriate protection of short sellers' identities and trading strategies.

If specific Managers are identified, issuers might take retaliatory action against individual short sellers through lawsuits and by forwarding information to regulators in attempts to precipitate regulatory investigations, through claims in the media, or by applying pressure on the shorting firm through business relationships that may exist outside of trading.<sup>275</sup> There is also evidence that when short sellers' positions become public, market participants strive to orchestrate short squeezes and are successful a significant fraction of the time.<sup>276</sup> Short sellers often face lawsuits when they take their information public or their identities otherwise become known—regardless of whether the information the short sellers brought forth was legitimate.<sup>277</sup> Some issuers have even been known to hire private investigators in an attempt to uncover the identities of individuals short selling their stock.<sup>278</sup> Some short sellers have also expressed that they have experienced threats to their

personal safety after their short positions were revealed.<sup>279</sup>

Lastly, even if the identities of the individuals reporting short selling data remain unknown, publicly disclosing that Managers have amassed large aggregate short positions may expose the Managers to increased risk of being the target of predatory strategies such as short squeezes. The risk of short squeeze increases if market participants are able to identify the individuals with large short positions as discussed in Part VIII.D.1. In this case they may be able to better estimate the capital constraints of the short seller to identify the likelihood of a squeeze being successful.

Because reporting information on Proposed Form SHO increases the costs of short selling, it is possible that short sellers may strategically select short positions to have an average short position just below the threshold that requires reporting. However, the risk of this is mitigated by the way in which the threshold is constructed, which could make trading around the threshold more costly. For example, because the threshold is not based on the position at the end of the month, Managers would not be able to simply reduce their positions at the end of the month to avoid reporting. Instead, Managers would need to maintain a position below the Reporting Thresholds throughout the month to avoid reporting. The size of a short position is often related to the expected magnitude of the short seller's negative information with revelations of larger negative information being associated with larger short positions.<sup>280</sup> Consequently, to the extent that Managers may choose to select otherwise sub-optimal short positions to avoid reaching the reporting threshold, Proposed Rule 13f-2 and Proposed Form SHO could result in a sub-optimal allocation of capital and may harm price efficiency. To this end some have argued that stock prices can be viewed as a weighted average of investor sentiment, if short sellers limit their positions to avoid disclosure requirements, then stock prices may skew towards being overvalued.<sup>281</sup>

<sup>279</sup> See Lamont (2012) *supra* note 258; Game Stopped Hearing, *supra* note 269 (CEO of Melvin Capital LP stated that after his short positions were made known, Reddit users made posts and sent personal text messages that were laced with anti-Semitic slurs and threats of physical harm to him and others.).

<sup>280</sup> See, e.g., *supra* note 269; Kyle (1985).

<sup>281</sup> See, e.g., *supra* note 267, Miller (1977); Letters on the Short Sale Reporting Study Required by Dodd-Frank Act Section 417(a)(2) from Investment Company Institute (hereafter "ICI Letter") available at <https://www.sec.gov/comments/4-627/4627->

<sup>272</sup> See *supra* note 269; see also Kyle (1985).

<sup>273</sup> See, e.g., Albert S. Kyle and Anna A. Obizhaeva, Large Bets and Stock Market Crashes (March 22, 2019), available at <https://ssrn.com/abstract=2023776> or <https://dx.doi.org/10.2139/ssrn.2023776>.

<sup>274</sup> See 2011 MFA Letter, *supra* note 49; Owen A. Lamont, *Go Down Fighting: Short Sellers vs. Firms*, 2(1) *The Rev. of Asset Pricing Studies* 1–30 (2012); Lorian Stice-Lawrence, Yu Ting Wong, Yu Ting Forester Wong, and Wuyang Zhao, *Short Squeezes After Short-Selling Attacks* (November 2021), available at <https://ssrn.com/abstract=3849581> or <http://dx.doi.org/10.2139/ssrn.3849581>.

<sup>275</sup> See 2011 letter from Security Traders Association of New York on the Short Sale Reporting Study Required by Dodd-Frank Act Section 417(a)(2), available at <https://www.sec.gov/comments/4-627/4627-155.pdf>.

<sup>276</sup> See *supra* note 274, Stice-Lawrence, Wong, and Zhao (2021) and Lamont (2021).

<sup>277</sup> See Owen A. Lamont, *Go Down Fighting: Short Sellers vs. Firms*, 2 (1) *The Rev. of Asset Pricing Studies* 1–30 (2012).

<sup>278</sup> *Id.*

For these reasons, the Commission believes that the Proposals may increase the costs of short selling and potentially dissuade investors from engaging in fundamental research and the total amount of short selling may decrease, though the Commission has designed the Proposals to mitigate these risks. To the extent that fundamental research decreases, price efficiency could be harmed as prices would not necessarily reflect all available relevant information, only that portion that had been discovered by investors performing fundamental research. Additionally, Proposed Rule 13f-2 could dissuade options market makers from holding large short positions and providing liquidity in options markets and, thus, could harm price efficiency in equity markets.<sup>282</sup>

As with the discussion in Part VIII.D.1, many of the economic effects articulated in this section relating to the reporting of Proposed Form SHO could be limited to the extent that the data reported in Proposed Form SHO contains factual errors. The EDGAR system would check the data for technical errors, however the accuracy of the data is dependent on accurate and

141.pdf; Data Explorers Letter; SIFMA Letter available at <https://www.sec.gov/comments/4-627/4627-143.pdf> (about transaction marking leading to less short selling). In contrast, some argue that short selling itself increases the value of assets as it provides demand for securities lending and allows owners to collect securities lending fees. From this perspective, restricting short selling may decrease stock prices by restricting the demand for securities loans. See Darrell Duffie, Nicolae Garleanu, and Lasse Heje Pedersen, *Securities Lending, Shorting, and Pricing*, 66 (2-3) J. of Fin. Econ. 307-339 (2002). The Commission does not believe that this effect is the predominate effect of short selling on asset prices, because the average fee earned from securities lending is usually very small relative to the average long term stock returns. Thus, it appears that other economic effects tend to dominate the relationship between short selling and stock prices and that on net short selling restrictions lead to stock overvaluation. See also OTC Markets, Provable Markets, SIFMA, and Chester Spatt letters (responding to FINRA's regulatory notice 21-19 arguing that short selling is vital to price efficiency), available at <https://www.finra.org/rules-guidance/notices/21-19#>. In contrast, others have argued that absent disagreement, costly short selling can help correct over-pricing by preventing the uninformed (but not informed traders) from transacting. This skews the distribution of traders in the market towards being more informed meaning that markets learn more from each trade and prices adjust more quickly when uninformed traders do not trade. See Douglas Diamond and Robert E. Verrecchia, *Constraints On Short-Selling And Asset Price Adjustment To Private Information*, 18 (2) J. of Fin. Econ. 277-311 (1987).

<sup>282</sup> See *infra* Part VIII.D.3. Research has found a that options play an important informational role in stock price discovery, therefore reductions in liquidity in the options market can reduce the price efficiency in the equity market. See also David Easley, Maureen O'hara, and Pulle Subrahmanya Srinivas, *Option Volume and Stock Prices: Evidence on Where Informed Traders Trade*, 52 (2), THE JOURNAL OF FINANCE 431-465 (1998).

complete data entry by filers. Thus, the data reported in Proposed Form SHO could contain errors. To the extent that these errors exist and meaningfully affect the usability of the data, the value of the data and the economic benefits and costs associated with collecting the data would be limited. Additionally, the benefits and costs are lessened by the proposed delay in the publication of the data. Furthermore, the proposed data would only be available for those securities with Managers who have short positions over the threshold, which in some cases may not be representative of all short positions, and the number of reporting Managers may change from month to month.

### 3. Effect on Market Liquidity

The effect of the Proposals on liquidity is uncertain. Part V.4.ii, discusses the possibility that Proposed Rule 13f-2 and Proposed Form SHO may harm price efficiency by dissuading investors from pursuing fundamental research and that Proposed Rule 13f-2 and Proposed Form SHO along with Proposed Rule 205 and the Proposal to Amend CAT may help price efficiency by increasing transparency with respect to the actions of large short sellers. To the extent that the Proposals improve price efficiency, this could also indirectly improve liquidity because market makers would be subject to less mispricing risk. However to the extent that Proposed Rule 13f-2 and Proposed Form SHO harm price efficiency, the opposite may be true. Mispricing risk leads to lower liquidity because market makers must be compensated, in the form of wider bid ask spreads, for the potential that there is information relevant to the firm that has not yet been discovered and may affect prices. Thus if the rule harms price efficiency it may also harm liquidity. The opposite is also true. To the extent that the Proposals enhance market efficiency they may also enhance liquidity by mitigating mispricing risk.

Additionally, in the event that an options market maker might have a short position close to the Reporting Thresholds, the Proposed Rule 13f-2 could dissuade the option market maker from increasing their short position, which may harm their willingness to provide liquidity in options markets. Alternatively, Proposed Rule 13f-2 might not result in option market makers who exceed the Reporting Thresholds changing their positions, in which case the costs of filing Form 13f-2 (and other compliance costs) could result in wider spreads if the compliance costs are large enough.

### 4. Effect on Corporate Decision Making

The Commission believes that Proposed Rule 13f-2 and Proposed Form SHO could have mixed effects on corporate decision making. On the one hand, research suggests that corporate managers learn from market reactions to announcements.<sup>283</sup> Consequently, Proposed Rule 13f-2 and Proposed Form SHO may provide corporate managers with additional feedback on their decisions. For instance, projects often take some time to design and implement after announcement, consequently, even with the lag in the reporting time for the Proposed Form SHO data, a corporate manager could review the data around significant announcements to better understand how the market may view a particular project or announcement. If large short positions are built shortly after a corporate announcement, then this may give the signal to corporate management that the market views that announcement negatively which may help a manager modify or reverse poor decisions. From this perspective the Proposals may enhance corporate manager decision making.

In contrast, short sellers, and particularly large short sellers with the resources to perform fundamental research, serve as valuable external monitors of management. If a corporate manager knows that short sellers are monitoring their actions and financial statements and are willing to expose wrong-doing, then they are less likely to engage in fraud or do other things that may hurt the value of the company. Historically, short sellers have, through doing research, uncovered fraudulent behavior.<sup>284</sup> Academic research has also shown that even the threat of short

<sup>283</sup> See, e.g., James B. Kau, James S. Linck, and Paul H. Rubin, *Do Managers Listen to the Market?*, 14 (4) J. of Corporate Fin. 347-362 (2008).

<sup>284</sup> See, e.g., A. Dyck, A. Morse, and L. Zingales, *Who Blows the Whistle on Corporate Fraud?*, 65(6) The J. of Fin. 2213-2253 (2010) (using a large sample of fraud cases between 1996 and 2004, the authors find that short sellers uncovered the fraud in nearly 15% of cases.). See also Cassell Bryan-Low and Suzanne McGee, *Enron Short Seller Detected Red Flags in Regulatory Filings*, The Wall Street J. (Nov. 5, 2001) (discussing an Enron short seller that detected red flags reviewing, among other things, the company's SEC filings), available at <https://www.wsj.com/articles/SB1004916006978550640>, retrieved from Factiva database. Cf. Nessim Mezrahi, Stephen Sigris, and Carolina Doherty, *More Securities Class Actions May Rely on Short-Seller Data*, Portfolio Media (January 10, 2022) (authors' "analysis of 131 Rule 10b-5 securities class actions indicates that plaintiffs continue to rely on short-seller research to substantiate fraud-on-the-market claims."), available at <https://www.law360.com/articles/1453499/more-securities-class-actions-may-rely-on-short-seller-data>.

selling serves to discipline managers.<sup>285</sup> As discussed in Parts V.4.i and V.4.ii, Proposed Rule 13f–2 may discourage Managers from performing fundamental research. If less fundamental research is performed by short sellers, then their role as monitors of the firm diminishes. Less monitoring could lead to higher incidences of fraud as managers feel that the likelihood of being caught goes down.<sup>286</sup> Thus, to the extent that Proposed Rule 13f–2 and Proposed Form SHO discourage fundamental research it may lead to both an increase in the total amount of corporate fraud in the economy as well as decrease the fraction of frauds that are discovered by investors.

#### 5. Effect of Certain Electronic Filing and Dissemination Requirements

Proposed Rule 13f–2 and Proposed Form SHO would require the short position and activity disclosures to be filed on the Commission’s EDGAR system using a structured, machine-readable data language. In particular, the rule and Form would require Proposed Form SHO to be filed on EDGAR in a custom XML-based data language specific to that Form (“custom XML,” here “Proposed Form SHO-specific XML”). The XML Schema for Proposed Form SHO-specific XML would incorporate validations of certain data fields on the Form to help ensure consistent formatting and completeness.<sup>287</sup> While the field validations would act as an automated form completeness check when a Manager files a Proposed Form SHO, the field validations would not be designed to verify the accuracy of the information filed in Proposed Form SHO filings. EDGAR would subsequently aggregate the reported information at the equity security level and release the aggregated

data to the public, either on EDGAR or on the Commission’s website.

The Commission believes these requirements would incrementally augment the various effects of the short position and activity disclosures discussed herein by enhancing the accessibility, usability, and quality of the Proposed Form SHO disclosures (for use by the Commission) and the aggregate security-level disclosures (for use by the public). By requiring a structured machine-readable data language and a centralized filing location (EDGAR) for the disclosures on Proposed Form SHO, the Commission would be able to access and download large volumes of Proposed Form SHO disclosures in an efficient manner.

Similarly, the provision of the aggregated security-level information at a centralized, publicly accessible location in a structured, machine-readable data language, would enable investors and other public data users to download the aggregated information directly, and the data could then be analyzed using various tools and applications. If the security-level information were not available at a centralized location in a structured, machine-readable language, data users seeking to analyze the information using tools and applications would need to search for, extract, and structure the security-level short position and activity information, or pay a third-party vendor to do so.

The Commission believes requiring the short position and activity disclosures to be filed in Proposed Form SHO-specific XML would facilitate more thorough review and analysis of the reported short sale disclosures by the Commission, which would increase the efficiency and effectiveness with which the Commission could identify manipulative short selling strategies—which may also serve as a deterrent to would be manipulators and thus may help prevent manipulation—and observe systemic risk. The Commission believes that this outcome would benefit investors by facilitating the Commission’s observation of short selling and would thus help protect investors and ensure the sufficiency of information related to short selling in the market.

The proposed requirement for short sale disclosures to be filed on EDGAR in Proposed Form SHO-specific XML would result in additional incremental compliance costs on filing Managers. These direct compliance costs are detailed in a subsequent section.<sup>288</sup> Moreover, to the extent these

incremental compliance costs further chill the incidence of short-selling, the EDGAR and Proposed Form SHO-specific XML requirements would increase the likelihood of the indirect costs that are discussed elsewhere in this section.

#### 6. Effect on the Securities Lending Market

As discussed in parts V.4.i and V.4.ii, the Proposals would increase the cost of short selling, particularly large short positions—potentially leading to less overall short selling. As discussed in Part V.3.i, short sellers must borrow shares to open a short position. When investors borrow shares they pay a borrowing fee to the owner of the share. These fees can represent a significant source of revenue for pension funds, mutual funds, and others who engage in securities lending.<sup>289</sup> Consequently, to the extent that the Proposals discourage short selling they may also lower overall portfolio returns, including for institutional investors that engage in securities lending.<sup>290</sup>

#### 7. Direct Compliance Costs

The Commission believes that there would be direct costs associated with Proposed Rule 13f–2, Proposed Form SHO, Proposed Rule 205, and the Proposal to Amend CAT. These costs include: Managers reporting position and activity data; broker-dealers updating CAT reporting processes; amendments to Regulation SHO; and the Commission processing and releasing the Manager reports through EDGAR.

The Commission’s estimates for Managers’ collective direct compliance costs to capture and report the information required for Proposed Form SHO range from \$54,083,087 to \$156,309,500. This range reflects estimates for the number of managers that would be subject to the rule’s reporting requirement, their data capture costs, and their reporting costs. The Commission estimates that between 346 and 1,000 managers would be required to file Proposed Form SHO. We based our lower estimate on the number of Form SH filers above Threshold A. The actual number of reporting Managers would likely be higher than

<sup>285</sup> See, e.g., Massimo Massa, Bohui Zhang and Hong Zhang, *The Invisible Hand of Short Selling: Does Short Selling Discipline Earnings Management?* 28 (6) *The Rev. of Fin. Studies* 1701–1736 (2015).

<sup>286</sup> See, e.g., Paul Povel, Rajdeep Singh, and Andrew Winton, *Booms, Busts, and Fraud*, 20 (4) *The Rev. of Fin. Studies* 1219–1254 (2007) (linking variations in monitoring intensity to the incidence rate of financial fraud.).

<sup>287</sup> See *supra* Part III.B.4. Field validations are restrictions placed on each data element which would not allow a filer to file a form if there are certain technical errors in critical fields. If a Proposed Form SHO were to include, for example, letters instead of numbers in a field requiring only numbers, it would be flagged as a technical error, at which point the filer would either be unable to file the Form (if completed using the fillable web form provided by EDGAR) or the filing would be rejected (if directly filed in EDGAR in Proposed Form SHO-specific XML). To complete the filing, the filer would need to correct the error and re-file.

<sup>288</sup> See *infra* Part VIII.D.7.

<sup>289</sup> See *supra* note 232.

<sup>290</sup> Commenters on the Short Sale Reporting Study Required by Dodd-Frank Act Section 417(a)(2) argue that increased public short selling disclosure may result in reduced short selling, thereby lowering revenues to institutions that maintain long positions in equities for extended periods (such as pension funds). See, e.g., 2011 Letter from Alternative Investment Management Association, available at <https://www.sec.gov/comments/4-627/4627-138.pdf>.



our low estimate, because Managers that exercise investment discretion with respect to accounts holding Section 13(f) securities having an aggregate fair market value of less than \$100 million were not required to file Form SH,<sup>291</sup> and lower than our high estimate.<sup>292</sup> Based on this estimated range, the Commission estimates that the collective cost for updating systems to capture the required information would be between \$36,017,735 and \$104,097,500<sup>293</sup> and the annual total cost for reporting managers would be between \$18,065,352 and \$52,212,000.<sup>294</sup> Costs could be underestimated to the extent that wages are higher than those used in the estimation. The initial costs are likely higher than the lower bound estimates as Managers who may not file Proposed Form SHO on a monthly basis would still incur the initial costs. Furthermore, because Manager short positions are fluid, some Managers would not be required to file a report every month when they fall below the reporting threshold. As a result of this fluidity, ongoing costs could be lower than our estimates. Moreover, to the extent that the number of reportable short positions varies across Managers, the costs to track and report those positions would also vary by Manager. And initial costs could also be higher for some Managers who do not currently report to EDGAR.

The Commission believes that there could be costs in addition to the previously stated costs. The Commission estimates that filing amendments to Proposed Form SHO may take as long to file as the initial filing, therefore Managers could also incur additional costs up to \$4,351 to file amendments to Proposed Form SHO.<sup>295</sup> These costs may be more

<sup>291</sup> See Table I. See also note 80 (for more information on the methodology and caveats of using Form SH data).

<sup>292</sup> *Disclosure of Short Sales and Short Positions by Institutional Investment Managers*, 73 FR at 61686. (This estimate is similar to the estimate provided). Proposed Form SHO filers filed weekly reports. As a result, each reporting manager would file fewer reports because Form SH would be filed monthly. See *supra* note 124 (for more information on 1,000 Managers was estimated). However, fewer Managers actually filed Form SH.

<sup>293</sup> See *supra* PRA Table 2 and note 133. The lower range was calculated using 346 Managers. 20 hours per submission × 346 submissions by Managers each month × 12 months × \$217.55 = \$18,065,352. The Commission estimates that 346 Managers would have been required to file Form SH had Form SH be subject to the same \$10 million and 2.5% threshold.

<sup>294</sup> See *supra* PRA Table 1 and note 143. The lower range was calculated using 346 Managers.

<sup>295</sup> Depending on what amendments are needed the Commission believes that each amendment could take up to the original 20 hours to complete, at a cost of \$217.55 per hour = \$4,351. *Id.* See also Form SHO, Special Instructions at 4.

common for Managers who do not hold short positions often and are likely to decrease with time as Managers become more experienced with filing Proposed Form SHO. As part of the filing of Proposed Form SHO, Managers would need to ensure that there is not duplicative reporting.<sup>296</sup> The burden to ensure that there is not duplicative reporting would likely vary by Manager, as larger Managers with multiple accounts may be more likely to have duplication issues. As part of updating systems to comply with the reporting requirements of Proposed Rule 13f-2, Managers must calculate the market value of the trade using the official closing price as of the close of regular trading hours for the trade settlement date in question, which may not be the fair market value at the time in which the trade occurred.<sup>297</sup> However, the Commission believes that in most cases this would be a small burden on Managers as the data needed for the calculation would be publicly available and the Commission believes that Managers may already track the end of day fair market value of short sales. Even in cases that the reportable equity security is not traded on an exchange, the Commission believes that Managers may be able to calculate the value of their short positions by using publicly available closing prices from the OTC Reporting Facility. In circumstances where closing prices of non-reporting company issuers are not available, the Commission believes the tracking such information would still not impose a large burden as a Manager can use the price at which they last purchased or sold any share of that security, which would be readily available to the Manager.

The Commission also believes that there would be costs associated with tracking short positions in relation to the threshold.<sup>298</sup> Particularly, Managers must track their average short positions over the month to be aware if the maximum position exceeds \$10 million as well as if it exceeds the 2.5% threshold, or in the case of equity securities of a non-reporting company issuer, if it exceeds the \$500,000 threshold. However, the Commission

<sup>296</sup> See Form SHO, Special Instructions at 6.

<sup>297</sup> See Form SHO, Special Instructions at 7. See also PRA Table 2 in Part VI (for an estimate of these burden hours).

<sup>298</sup> Based on the number of registered investment companies reporting short positions and the number of hedge funds engaged in a strategy including short selling, we preliminarily believe that only a small fraction of Managers would be likely to have monitoring responsibilities pursuant to the proposed rule and, given the proposed reporting thresholds, an even smaller fraction would be likely to have reporting obligations.

believes that the proposed Reporting Thresholds would generally lower the burden on Managers as fewer Managers would be required to report than if the Commission did not propose a reporting threshold. For example, the Commission believes that certain types of Managers would not meet a Reporting Threshold.<sup>299</sup> However, the Commission believes that the costs associated with Proposed Rule 13f-2 and Proposed Form SHO would not be dependent on the type of Manager, with the exception that Managers who do not currently report to EDGAR may have increased costs associated with complying with Rule 13f-2. Additionally, certain types of Managers may be less likely to trigger the threshold, resulting in lower overall costs for these Managers. Using Form SH data, the Commission estimates that an average of 442 Managers would have been required to file Proposed Form SHO each month under the threshold in place during temporary rule 10a-3T. However, only 346 Managers would be required to file under the proposed Threshold A.<sup>300</sup>

The Commission understands that the cost of tracking short positions could be higher for certain types of securities. For example, tracking the short position in an exchange traded fund as a percent of shares outstanding would be more difficult as the number of shares outstanding changes frequently. Additionally, Managers who hold short positions in non-reporting company issuers may have difficulty calculating the value of their position, however Managers may use the last price at which a the Manager traded even though the price may be stale. The Commission also believes that the cost to track and report activities information may vary across activity categories. Short selling and buy to cover activities would likely be the most common forms of reported activities and would therefore account for the majority of the costs. However, other categories of reportable activity, such as option exercises and assignments, tender conversions, and seasoned market purchases that reduce or close a short position would be reported less frequently and may require more attention to file as Managers would have less experience with reporting such activities.

Requiring Proposed Form SHO to be filed on EDGAR in Proposed Form SHO-specific XML would not impose

<sup>299</sup> See *supra* Section VIII.C.2 and *supra* note 185 (for a discussion on why certain types of managers are more likely to have reporting requirements).

<sup>300</sup> See *supra* Table I. See also *supra* note 77 (for more information on Form SH data).

significant incremental costs on Managers. We expect most Managers who would be required to file Proposed Form SHO would likely have experience filing EDGAR forms that use similar EDGAR Form-specific XML data languages, such as Form 13F. In that regard, we note the process for filing Proposed Form SHO, as well as the XML-based data language used for Proposed Form SHO, would be similar to the filing process and data language used for Form 13F.<sup>301</sup> We expect that Managers with such experience that choose to file Proposed Form SHO directly in Proposed Form SHO-specific XML would incur some compliance costs associated with doing so.<sup>302</sup>

In addition, Managers would be given the alternate option of filing Proposed Form SHO using a fillable web form that would render into Proposed Form SHO-specific XML in EDGAR, rather than filing directly in Proposed Form SHO-specific XML using the technical specifications published on the Commission's website. We expect Managers who do not have experience filing Form 13F or other EDGAR Form-specific XML filings would likely choose this option. In that regard, we note that Managers (*i.e.*, certain "institutional investment managers" as defined by Section 13(f)(6)(A) of the Exchange Act, which may include entities such as investment advisers, banks, insurance companies, broker-dealers, corporations, and pension funds) are only required to file Form 13F if they exercise investment discretion with respect to accounts holding Section 13(f) securities having an aggregate fair market value on the last trading day of any month of any

<sup>301</sup> See EDGAR Filer Manual (Volume II) version 60 (December 2021), at 9-1 ("EDGAR Filer Manual Volume II") (describing process for submitting Form-specific XML filings directly to EDGAR); see also Form 13F XML Technical Specification, available at <https://www.sec.gov/edgar/filer-information/current-edgar-technical-specifications>.

<sup>302</sup> See *supra* PRA Table 2 (estimating the ongoing burden for the Proposed Form SHO-specific XML requirement at two hours per Manager per filing and two hours per amended filing). Assuming 1,000 Managers filing 12 filings per year would equal 12,000 filings per year, resulting in 24,000 total annual industry burden hours (12 filings × 1,000 Managers × 2 hours = 24,000) and \$6,480,000 in industry costs for filings per year (24,000 hours × \$270 per hour for a programmer = \$6,480,000) attributable to the Proposed Form SHO-specific XML requirement. In addition, based on an estimate of 420 amended filings per year, the total industry cost for the Proposed Form SHO-specific XML would be \$226,800 for amended filings (420 amended filings × 2 hours per amended filing × \$270 per hour = \$226,800). As such, the total annual industry cost attributable to the Proposed Form SHO-specific XML requirement (including amended filings) is \$6,706,800 (\$6,480,000 for filings + \$226,800 for amended filings = \$6,706,800).

calendar year of at least \$100 million.<sup>303</sup> Of Managers that do not have experience filing Form 13F, only a subset are subject to other EDGAR Form-specific XML filing requirements.<sup>304</sup> For any Managers that choose to file Proposed Form SHO using a fillable web form, whether or not they have prior experience with filing forms in EDGAR Form-specific XML, we do not believe the Proposed Form SHO-specific XML requirement (*i.e.*, the requirement to place the collected information in a fillable web form provided by EDGAR, rather than in an HTML or ASCII document to be filed on EDGAR as is required for most other EDGAR forms) would impose any additional compliance costs.<sup>305</sup>

The Commission is cognizant of the burdens Managers experienced of submitting Form SH in compliance with temporary Rule 10a-3T and has designed Proposed Rule 13f-2 and Proposed Form SHO to attempt to reduce those burdens. First, commenters on the temporary Rule 10a-3T stated that the 0.25% threshold was too low.<sup>306</sup> The two-pronged threshold in Proposed Rule 13f-2 is higher than the threshold in Rule 10a-3T, reducing the number of Managers likely to have a reporting obligation. For example, the Commission estimates that only 41% of positions reported under Rule 10a-3T would be required to report given the higher threshold in Proposed Rule 13f-2 and Proposed Form SHO, while still collecting 89% of the dollar value.<sup>307</sup>

<sup>303</sup> See 17 CFR 240.13f-1(a).

<sup>304</sup> For example, registered brokers or dealers that are subject to the reporting requirements set forth in 17 CFR 240.17h-2T must file Form 17H either electronically or in paper. Those that choose to file electronically must file Form 17H partially in EDGAR Form-specific XML. Insurance companies may offer variable contracts that are registered under the Investment Company Act of 1940, and would thus be required to file annual reports on Form N-CEN in EDGAR Form-specific XML as well as, in some cases, monthly portfolio information on Form N-PORT in EDGAR Form-specific XML. Corporations may make exempt offerings and be required to file Form 1-A, Form C, or Form D in EDGAR Form-specific XML either in part or in full, depending on the nature of the offering.

<sup>305</sup> See 17 CFR 232.101(a)(1)(iv); 17 CFR 232.301; EDGAR Filer Manual Volume II at 5-1 (requiring EDGAR filers generally to use ASCII or HTML for their filed documents, subject to certain exceptions).

<sup>306</sup> See Temporary Rule 10a3-T Comment letters (including Seward & Kissel LLP Letter), available at <https://www.sec.gov/comments/s7-31-08/s73108-43.pdf>; MFA Letter, available at <https://www.sec.gov/comments/s7-31-08/s73108-41.pdf>; IAA Letter, available at <https://www.sec.gov/comments/s7-31-08/s73108-38.pdf>; ICI Letter, available at <https://www.sec.gov/comments/s7-31-08/s73108-47.pdf>; SIFMA Letter, available at <https://www.sec.gov/comments/s7-31-08/s73108-52.pdf>. See also *supra* Part III.D.2. (for more information on Threshold A using Form SH data).

<sup>307</sup> See *supra* Table I: Various Threshold Levels for Monthly Average Positions and Monthly

Additionally the proposed threshold could be less burdensome to assess than the one in Rule 10a-3T because it requires the Manager to assess whether it is above the threshold on a monthly basis rather than on each individual day. Second, many commenters believed that weekly reporting was overly burdensome.<sup>308</sup> The short selling information required by Proposed Rule 13f-2 and Proposed Form SHO would be reported less frequently (monthly rather than weekly) and would involve reporting end of month positions rather than daily positions. Third, Managers would have more time to compile and file the Proposed Form SHO reports than they had to compile Form SH.

Notwithstanding these cost-reducing differences, the Commission does recognize that other differences could offset some or all of these cost reductions. In particular, Proposed Rule 13f-2 and Proposed Form SHO would require reporting additional information such as information on buy-to-cover activity and other activity that changes short positions. In addition, Proposed Rule 13f-2 and Proposed Form SHO would require that the information on activity include daily records and not be subject to its own threshold.<sup>309</sup> Also, unlike the Form SH required under Rule 10a-3T, the Proposed Form SHO that would be required by Proposed Rule 13f-2 would feature an XML Schema that would incorporate technical validations of certain data fields on the Form, and would flag technical errors and require the filer to correct the technical errors before successful submission on EDGAR. However, because the field validations contemplated by Proposed Rule 13f-2 and Proposed Form SHO would be limited to technical errors (*e.g.*, letters

Maximum Dollar Value. However, the Commission recognizes that Temporary Rule 10a-3T was in effect in 2008-2009 and the market may be different, particularly the average short position may be larger. Only Managers that exercise investment discretion with respect to accounts holding Section 13(f) securities having an aggregate fair market value of at least \$100 million were required to file Form SH. Additionally, the data lacked data validation according to the needs of end user when filed making the data hard to work with.

<sup>308</sup> See *supra* note 306 (the comment letters in note, as well Coalition of Private Investment Companies letter), available at <https://www.sec.gov/comments/s7-31-08/s73108-46.pdf>.

<sup>309</sup> Rule 10a-3T required Managers to report beginning and end of day Short Position. Number of Securities Sold Short each day if the particular data item exceeded the threshold. See P 3 Final rule 10a-3T, available at <https://www.sec.gov/rules/final/2008/34-58785fr.pdf>. However, in analysis of Form SH data intraday short selling volume could not be examined for Form SH because the data field for "Number of Securities Sold Short" was populated in only 7% of observations after filters were applied. See *supra* note 80 for more information on short volume in Form SH data.

instead of numbers in a field requiring only numbers) that we believe would be straightforward to resolve, we do not believe such resubmission costs would be significant. Finally, the rule could impose costs on Managers who were not required to report Form SH because Rule 10a-3T and Form SH did not apply to Managers that exercise investment discretion with respect to accounts holding Section 13(f) securities with an aggregate fair market value of less than \$100 million.

In connection with Proposed Rule 205, the Commission estimates that broker-dealers would have an initial technology cost to update order marking systems of \$170,000 for each of the 1,218 broker-dealers with a total maximum initial cost to all broker-dealers of \$207,060,000. This estimate likely significantly overstates the actual costs as many broker-dealers use third party order management systems.<sup>310</sup> In this case the operator of the third party order manager system would update their system and then apply it to all customers reducing the cost significantly. The Commission estimates that all but 126 of the broker-dealers use third party order management systems. In this case the direct compliance costs for these 126 broker-dealers would be \$12,420,000. The remaining broker-dealers would likely incur costs in the form of higher fees from the third party order management firms to account for their additional costs. However, these would be significantly lower than the costs to adjust a system from scratch as the costs would be divided among all clients of the third party order management firm. Additionally, the Commission believes that that some broker-dealers already track their customer's buy to cover orders. Therefore, the initial cost from the rule are likely to be lower than the upper bound estimate.

Additionally, the Commission estimates an upper bound that each instance of marking an order "buy to cover" would take approximately 0.5 seconds, assuming that this takes as long as a short sale mark took in 2003, which would lead to an ongoing annual burden of 7,107 hours per broker-dealer and a total burden of 8,652,750 hours.<sup>311</sup> This figure is likely an overestimate in light of technological advancements since 2003. Therefore, the Commission estimates a lower bound for this burden of 721,000 hours or 592 hours per broker-dealer, assuming that computing speed has increased by at least 12 times since

2007.<sup>312</sup> Further, to the extent that some broker-dealers already track their customer's buy to cover orders, the ongoing costs of this requirement would be low.

The 25 Plan Participants would face costs associated with the Proposal to Amend CAT, as they would be required to engage the Plan Processor to modify the Central Repository to accept and process new short sale data elements on order receipt and origination reports. Additionally the Commission estimates an external cost of \$3,904 per participant or \$101,520 total to compensate the Plan Processor for staff time required to make the initial necessary programming and systems changes.<sup>313</sup> However, these initial costs could be higher if the Commission underestimated the time and wages necessary for programming and systems changes for the plan processor to accept and process new data elements. Furthermore, the Commission believes that Proposal to Amend CAT would not impose additional ongoing cost to participants beyond those costs already accounted for in existing Paperwork Reduction Act estimates that apply for Rule 613 and the CAT NMS Plan approval order.<sup>314</sup>

The Commission believes that the proposed Proposal to Amend CAT would impose a one-time cost to Industry Members.<sup>315</sup> These costs would depend on whether implementing Proposed rules 6.4(d)(ii)(D) and (E) would involve creating additional fields in the order origination report, or if it is implemented within existing fields.

The Commission recognizes that costs would vary broadly across Industry Members, particularly depending on whether the Industry Member outsources the provision of an order handling system and regulatory data reporting to a service provider. In the

CAT NMS Plan Approval Order,<sup>316</sup> the Commission identified 126 Industry Members that do not outsource these activities. For these Industry Members, implementation is likely to require changes both to their order handling systems as well as their regulatory data reporting systems that produce their CAT reporting data. The Commission estimates that the 126 insourcing Industry members would incur an aggregate one-time cost of \$1,890,000 or \$15,000 individually to update software and hardware to facilitate reporting the new buy to cover elements to CAT.<sup>317</sup> Additionally, 60 insourcing Industry members would incur an aggregate cost of \$900,000 or \$15,000 individually to update systems to facilitate reporting the new bona fide market making exception elements to CAT.<sup>318</sup> However, these cost could be lower if the Commission is overestimating the number of insourcing industry members, in particular, the additional cost could drive some insourcing industry members to begin to outsource. The Commission believes that ongoing costs associated with reporting the newly required information to CAT would already be covered by ongoing cost estimates included in its cost estimates for the CAT NMS Plan. The Commission further believes that similar implementation and ongoing costs would be borne by each of the service providers that provide order handling systems and regulatory data reporting services to Industry Members that outsource these systems.

For Industry Members that outsource, the Commission believes that implementation costs would be far lower because the service bureaus that provide them with order handling systems and regulatory data reporting services would adapt those systems on their customers' behalf. The Commission estimates that the 1,092 outsourcing Industry Members would incur a onetime-aggregate expense of \$1,092,000 or \$1,000 individually to update hardware and software to facilitate reporting the new buy to cover elements to CAT.<sup>319</sup> Additionally, 44 outsourcing industry members would incur an aggregate one-time cost of \$44,000 or \$1,000 individually to update systems to facilitate reporting the new bona fide market making exception elements to CAT.<sup>320</sup> However, these costs could be higher if some

<sup>312</sup> According to an industry performance evaluations for server processors, computing speed has increased by at least 12 times since 2007 (the earliest year in the data). The Commission believes that computing performance has increased by a greater amount since 2003. The Commission re-estimated the processing burden using a factor of 12 (as a conservative estimate of improvements in processing speed). Dividing the estimated burden per broker-dealer of 7,107 hours by 12 yields a burden per broker-dealer of approximately 592 hours per broker-dealer and a total burden of 721,063 hours. See Year on Year Performance (for server processors), PassMark Software Pty. Ltd., available at <https://www.cpubenchmark.net/year-on-year.html>.

<sup>313</sup> See *supra* note 143.

<sup>314</sup> See *supra* Part VII.D.4.a (for more information on costs for CAT Plan Participants).

<sup>315</sup> See *supra* Part VII.C.1 (for a discussion of the PRA burdens associated with the Proposal to Amend CAT).

<sup>316</sup> See *supra* note 172.

<sup>317</sup> See *supra* Part VI.D.4.c (for a breakdown of PRA costs related to the Proposal to Amend CAT).

<sup>318</sup> *Id.*

<sup>319</sup> *Id.*

<sup>320</sup> *Id.*

<sup>310</sup> See *supra* PRA Table 4.

<sup>311</sup> See *supra* PRA Table 3.

current insourcing industry members begin to outsource as a result of the increased costs, which would lead to an overall reduced cost for the rule as outsourcing is less costly than insourcing. The Commission believes that the costs of service bureaus adapting those systems would be passed to their Industry Member customers.

Although, the Proposed Rule 205 and the Proposal to Amend CAT to add buy to cover would impose costs on broker-dealers who are CAT Reporters, the Commission believes they would be less costly than previous related proposals, such as the “open/close indicator” in the original CAT NMS plan proposal.<sup>321</sup> The originally proposed CAT NMS Plan would have included an “open/close indicator,” which could be used to identify orders buying to cover short positions. However, several commenters stated that an “open/close indicator” would be overly burdensome, with one commenter stating that such burdens would be, in part, the result of “the lack of a clear definition of the term [open/close] for equity transactions,” and the indicator was not adopted.<sup>322</sup> By contrast, Proposed Rule 205 includes a clear definition of when a “buy to cover” indicator would be required to be reported.<sup>323</sup> In addition, reporting buy to cover on some buy orders is a narrower requirement than reporting an “open/close indicator” on all buy and sell orders. Specifically, aside from focusing only on some buy orders, Proposed Rule 205 is designed to rely solely on information within the broker-dealer<sup>324</sup> and the Proposal to Amend CAT would require reporting on order receipt and order origination reports only.

## 8. Risk of Circumvention Through Derivatives

The Commission believes that the risk that Managers may attempt to circumvent the reporting requirement by trading derivatives may be high, particularly for stocks with liquid options.<sup>325</sup> The risk may also increase if a robust single-stock futures market

develops over time.<sup>326</sup> Indeed, Proposed Rule 13f-2 and Proposed Form SHO could be a catalyst for growth in derivatives markets as short sellers look for new avenues to take the economic equivalent of short positions while avoiding these proposed disclosures.

The Reporting Thresholds in Proposed Rule 13f-2 are on a Manager’s gross short position in the equity security itself, and does not included the calculation of derivative positions. Consequently a Manager seeking to build a large short position while avoiding reporting their positions on Proposed Form SHO could hold a short position just below a Reporting Threshold and use derivatives to take positions above that threshold.<sup>327</sup> Using derivatives to circumvent the short selling reporting may be costly. Options tend to be more expensive than equity transactions particularly for less liquid securities. Additionally some equities do not have listed options. Consequently, the Managers’ desire to avoid the costs associated with reporting Proposed Form SHO information articulated in Part V.4.i and V.4.ii is balanced against the increased cost of using derivatives such as options to execute a short position. Thus for some stocks, *i.e.*, those with illiquid or non-existent options, the threat of circumvention through options may be minimal. However, academic research has shown that investors have used options to circumvent other short selling restrictions, thus there is a significant risk that there would be some attempt to circumvent the rule using derivatives, particularly in stocks with liquid options markets.<sup>328</sup>

## E. Efficiency, Competition and Capital Formation

### 1. Efficiency

Markets function best and are most efficient when all relevant information regarding a security is known and is incorporated into prices.<sup>329</sup> This includes negative information. When negative information is not tradable,

stocks tend to be overpriced leading to an inefficient allocation of capital across the economy.<sup>330</sup> More efficient prices lead to better economic outcomes for the macro economy as capital flows into high value projects and out of low value projects. Short sellers have incentive to uncover negative information and to trade to profit from that information. As discussed in Part V.4.ii, more transparency in short selling would improve the amount of information that investors have to value a stock—increasing price efficiency. However, it could also disincentivize fundamental research which would harm price efficiency by limiting the amount of total information has been discovered. Overall the impact of the Proposals on price efficiency is uncertain.

Additionally, Rule 205 and the CAT amendment would increase the efficiency with which the Commission accesses and performs analysis relating to bona-fide market making data or buy to cover data for regulatory or enforcement purposes. Currently, the Commission does not have an efficient means to determine buy to cover transactions. The Commission could, in theory, estimate buy to cover information using existing CAT data. However, constructing positions for a broad set of traders from CAT is inefficient and due to CAT lacking all information relative to an investor’s position—*e.g.*, options assignments—could result in incomplete results.<sup>331</sup> Additionally, the amendment to CAT would improve the efficiency of the Commission’s oversight and enforcement of regulations relating to the bona fide market making exception by providing more efficient access to data on how individual market makers are using the exception. Currently the Commission must request information about the use of the market maker exception from specific broker-dealers.<sup>332</sup>

### 2. Competition

Investors compete with one another to gather information that they use to enact trading strategies. Academic research indicates that when short selling is costly, then investors owning the asset have an advantage in gathering information due to the reduced cost of acting on whatever information that

<sup>321</sup> See *supra* note 101. See also *supra* Parts VII.C, VII.D.4.b, and VII.4.c.

<sup>322</sup> See *supra* Part V.A (for more discussion on the original CAT NMS Plan proposal that would have included an “open/close indicator”).

<sup>323</sup> See *supra* note 104.

<sup>324</sup> One commenter on the CAT NMS Plan Notice stated that including an “open/close indicator” indicator for equities would require “involve parties other than CAT Reporters, such as buy-side clients, OMS/EMS vendors, and others.” See *supra* note 101.

<sup>325</sup> See *supra* note 202, R. Battalio, and P. Schultz, (2011), Grundy, Lim, and Verwijmeren (2012).

<sup>326</sup> See *supra* note 202, Jiang, Shimizu, and Strong (2019).

<sup>327</sup> Recently proposed rule 10B-1 would require reporting of swap positions above a certain threshold. Prohibition Against Fraud, Manipulation, or Deception in Connection with Security-Based Swaps; Prohibition against Undue Influence over Chief Compliance Officers; Position Reporting of Large Security-Based Swap Positions, Exchange Act Release No. 93784; available at <https://www.sec.gov/rules/proposed/2021/34-93784.pdf>. There is no reporting requirement for large options positions or other derivatives.

<sup>328</sup> See *supra* note 202.

<sup>329</sup> See Eugene F. Fama, Efficient Capital Markets a Review of Theory and Empirical Work, *The Fama Portfolio* 76–121 (2021).

<sup>330</sup> See *supra* note 281.

<sup>331</sup> See *supra* Parts VIII.C.5.iv and VIII.F.1.i (for further analysis of the use of CAT data to estimate buy to cover transactions).

<sup>332</sup> See *supra* Parts V.B and Part VIII.C.4 (for a further discussion of the inefficiencies of existing data with regards to oversight and enforcement of rules relating to bona fide market making).

they gather.<sup>333</sup> By increasing the cost of short selling for managers above the reporting thresholds, as discussed in Part VIII.D.1 and VIII.D.2, the rule may increase the advantage that investors who own the asset have over those who do not in terms of gathering information with the overall result being that investors not owning the asset may experience lower returns relative to those owning the asset due to increased cost of acting on negative information.

Relatedly, fund performance is a key determinate of investor flows. The Commission believes that the proposal could harm competition for fund flows among Managers who do and do not use short selling strategies. For instance, managers that are skilled at uncovering negative information may face additional costs when transacting on this information, potentially leading to lower returns. Thus Managers specializing in uncovering overpriced stocks may find themselves at a competitive disadvantage relative to managers who do not use short selling in terms of their ability to compete for fund flows.

The Commission believes that Proposed Rule 205 and the Proposal to Amend CAT would not alter significantly the competitive landscape for broker-dealer services. For smaller broker-dealers the direct costs associated with complying with Rule 205 and the CAT amendment would likely be borne by the larger entity that they contract with for the relevant services. Since many of the compliance costs are fixed, the increased expense to any one smaller broker-dealer would likely be relatively small and come in the form of increased costs for services from the entity that they contract with.<sup>334</sup> Because larger broker-dealers enjoy economies of scale, they should be able to absorb the costs associated with compliance more easily. Consequently, the Commission believes that the effect of Rule 205 and the CAT amendment would have minor impacts on broker-dealer competition.<sup>335</sup>

### 3. Capital Formation

One of the primary roles of the securities markets is to allocate capital (money) across the economy. If investors believe that a company is undervalued then, all else being equal, they will buy that stock; if many investors buy the stock, the price for

that stock will increase—lowering the cost of equity financing and making funding projects easier for the firm.<sup>336</sup> On the other hand, if investors believe that a company is overvalued then, all else being equal, they will sell or short sell the stock to invest in other more profitable ventures. If enough investors sell or short the stock, then the stock price will decline. A lower stock price implies more expensive equity financing and thus a higher weighted average cost of capital. When stocks are overpriced, they are inherently allocated too much capital, which deprives more productive ventures from receiving optimal capital and hinders economic progress. Consequently, short sellers contribute to capital formation by enhancing price efficiency which ensures an optimal allocation of capital across firms. Thus, to the extent that the Proposals discourage short selling, as discussed in Part VIII.D.1 and VIII.D.2, it may lead to the overpricing of some stocks and the underpricing of others.<sup>337</sup> This mispricing distorts optimal capital formation as it implies that some firms may have a cost of capital that is relatively too high or too low with respect to that firm's fundamentals and risk profile.

Additionally, academic research suggests that managers learn from stock price changes, using them as a way to tap into the 'wisdom of crowds' phenomena to improve decisions.<sup>338</sup> For instance, if a firm announces a capital investment or other project, and the stock price moves up or down, then managers may use this information as a signal about the market's perception of the value of that project. Thus stock price reactions may be an input into manager decisions in terms of when and how to invest capital. To the extent that the rule discourages short selling, it may make it more difficult for managers to extract signals from stock prices about the value of proposed capital investments—particularly low value projects as the Proposals may dampen

the market's ability to respond to negative information.

The costs associated with Managers monitoring their short positions for compliance with reporting Proposed Form SHO along with the negative economic effects detailed in Part VIII.D.1, VIII.D.2, and VIII.D.7 may harm capital formation, specifically capital formation using convertible debt if it increases the cost of short selling. Investors may be less inclined to purchase convertible debt if the cost of hedging that purchase by short selling the security becomes more expensive—through both the direct and indirect costs associated with Form 13f-2.<sup>339</sup> Thus, to the extent that the costs associated with Proposed Form SHO increase the cost of short selling they may also increase the cost of hedging convertible debt and may make that form of financing more expensive. This effectively increases the weighted cost of capital for firms that use convertible debt and may hinder their ability to fund operations, including new investments.

In contrast, the Proposals may have a positive influence on capital formation if they limit short selling based fraud. Specifically, in one type of fraud, investors holding convertible debt would short sell a stock in an attempt to drive down the price and then convert their debt to equity to cover their short positions at the lower price. To the extent that the rule facilitates better oversight and prosecution of this sort of fraud, it may facilitate capital formation by lowering the risk that convertible debt holders would engage in this sort of fraud.

Proposed Rule 13f-2 may also affect capital formation through investor confidence. Some Commenters have suggested that short selling, and in particular a lack of short selling disclosure leads some investors to have less confidence in financial markets,<sup>340</sup> although the results may be mixed. The Commission believes that improving short selling transparency would strengthen investor confidence which could help make investors more willing to invest, resulting in the promotion of capital formation.<sup>341</sup>

<sup>336</sup> A firm's external cost of finance is known as the weighted average cost of capital (WACC). It is simply the weighted average of the firm's cost of equity and the firm's cost of debt. Cost of equity (COE) is simply the return required by investors to assume the risks of owning the stock, computed as  $COE = (\text{dividends per share} / \text{market cap}) + \text{dividend growth rate}$ . In this computation, market cap is simply the number of shares outstanding multiplied by the current stock price. If the stock price decreases, then mechanically the firm's COE would go up. See, e.g., R.A. Brealey, S.C. Myers, F. Allen, and P. Mohanty, *Principles of Corporate Finance*, Tata McGraw-Hill Education (2012).

<sup>337</sup> See *supra* note 267, Miller (1977).

<sup>338</sup> See I. Goldstein and A. Guembel, *Manipulation and the Allocational Role of Prices*, 75 (1) *The Rev. of Econ. Studies* 133–164 (2008).

<sup>339</sup> See, e.g., Stephen J. Brown, Bruce D. Grundy, Craig M. Lewis and Patrick Verwijmeren, *Convertibles and Hedge Funds as Distributors of Equity Exposure*, 25 (10) *Rev. Fin. Stud* 3077–3112 (Oct. 2012).

<sup>340</sup> See NASDAQ, OTC Markets, and CFA Institute letters (in response to FINRA's short selling proposal) available at <https://www.finra.org/rules-guidance/notices/21-19#comments>.

<sup>341</sup> See Exchange Act Release No. 61595 (Feb. 26, 2010), 75 FR 11232, at 297 (Mar. 10, 2010), available at <http://www.sec.gov/rules/final/2010/34-61595fr.pdf>.

<sup>333</sup> See Dixon (2021), *supra* note 242.

<sup>334</sup> See *supra* Part VIII.D.7 (for a discussion of direct compliance costs).

<sup>335</sup> See also *supra* note 244, CAT Proposing Release (where the Commission discusses the implementation of CAT and its effect on broker-dealer competition).

## F. Reasonable Alternatives

### 1. Alternative Approaches

#### i. Releasing Aggregated CAT Data

As an alternative to collecting, aggregating, and publishing Proposed Form SHO, the Commission could amend the CAT NMS Plan to collect additional information so that the Commission or the Plan Processor could aggregate and publish CAT Data.<sup>342</sup> Specifically, the Commission could retain proposed Rule 205 and the amendment to the CAT NMS plan requiring the reporting of bona fide market making and buy to cover information to CAT and then use CAT data to have either the Commission or the Plan Processor provide short selling information to the public. This alternative would effectively eliminate the thresholds for reporting. This alternative could not be implemented until the CAIS system in CAT is fully operational. Currently it would be extremely difficult to map Firm Designated IDs “FDIDs”—which are currently broker-dealer specific—to individual Managers on a large scale. However this functionality is anticipated once the CAIS system is fully operational.

CAT data currently contains a short sale mark and also provides the identities of the individuals transacting. Consequently the Commission or the Plan Processor could aggregate information on the number of short sales that Managers engage in from CAT and disseminate aggregated information to the public at monthly intervals—or more frequently. The Commission or Plan Processor could publish daily statistics on the number of short sales engaged in by Managers each day in the prior month as reported in CAT. Additionally, the reports could include information on options transactions that lead to short positions, such as purchasing a put option, or writing a call option.<sup>343</sup> Furthermore, a longer time series (for example, a rolling year) to estimate a Manager’s position could be aggregated using CAT data. These could be aggregated to create a market-wide short position estimate. However, this estimate would be inaccurate because the alternative does not consider collecting in CAT information on changes in positions that come from activity other than secondary market transactions, such as secondary offering

<sup>342</sup> This alternative presumes that the Customer and Account Information System “CAIS” system in CAT is operational, thus allowing the Commission to track trades of individual traders.

<sup>343</sup> In this alternative, however, CAT would not contain the information on option expirations or assignments.

purchases, conversions, creations and redemptions, and option exercises and assignments. This inaccuracy could also result in the market-wide short position estimate being less accurate than current short interest data.<sup>344</sup>

The alternative would result in lower benefits than Proposed Rule 13f–2 and Proposed Form SHO. For each trading day, the alternative would involve publishing the net change in short sale positions engaged in by Managers.<sup>345</sup> The data published under this alternative would have significant overlap with the data that would be published under Proposed Rule 13f–2 and Proposed Form SHO. One difference between this alternative and the current data proposed to be collected in Proposed Form SHO and published by the Commission is that the data in this alternative could be more comprehensive in terms of the breadth of Managers whose short selling information could be aggregated and published,<sup>346</sup> because the Commission could publish aggregated data on short selling transactions from all Managers instead of just those that meet the threshold. However, the published data would be less accurate in terms of estimating positions and changes in positions as they would not include certain activity, such as options assignments, that are not collected in CAT but that may affect a short position. In addition, the alternative would not permit the publication of information on the percentage of positions that are fully or partially hedged. As a result of these differences, this alternative would result in less clarity about bearish sentiment among Managers. Thus, in terms of price efficiency, this approach would not have many of the same benefits as Proposed Rule 13f–2 and Proposed Form SHO.

The alternative would also reduce the benefits of comparing the published data to short interest because the alternative would focus on transaction dates rather than settlement dates and the alternative would not be restricted to large positions. Short interest measures short positions as of two settlement dates per month. A comparison of the data in the alternative to the short interest data would require either publishing the position data as of

<sup>344</sup> FINRA’s process of gathering and validating short interest data takes approximately two weeks. See *supra* note 221.

<sup>345</sup> This contrasts with the Proposed Rule 13f–2 which requires reporting based on the settlement date which is normally two business days after the transaction day.

<sup>346</sup> This assumes the Managers that could be identified in CAT could include all those that would be responsible for reporting under Proposed Rule 13f–2 and Proposed Form SHO.

the transaction dates that correspond to the short interest settlement dates or users would have to use the activity data to offset the dates themselves. Further, the inclusion of more than just Managers with large short positions means that the information conveyed by the alternative relative to short interest would be less additive than under Proposed Rule 13f–2 and Proposed Form SHO.

This alternative would also mitigate some of the concerns associated with Managers being exposed to increased risk of short squeezes or other retaliation as discussed in Part VIII.D.1 and VIII.D.2. This reduced risk would come because it would be more difficult to determine whether the short selling activity reported was due to many Managers short selling small amounts, or just a few Managers short selling large amounts. It would also be more difficult to identify individual short sellers based on the data. A lower risk of retaliation or short squeezes may also mitigate some of the negative effects of the proposal with regard to less overall short selling or fundamental research that are described in Part VIII.D.2, depending on the delay in publication under the alternative.

Additionally, this approach would have lower compliance costs for Managers than the current proposal, as it would not require Managers to file Proposed Form SHO. While it would result in the same costs for Industry Member reporting as those associated with Proposed Rule 205 and the Proposal to Amend CAT, it would increase costs associated with the Plan Processor improving processing power for the aggregation of CAT data if such computations could not be performed with existing resources (without reducing other functionality). Any costs incurred by the Plan Processor would be passed along to Plan Participants and Industry Members.

As previously stated, the drawback to this alternative relative to the existing proposal is that it would take some time before CAT data could be used to develop an estimate of the size of short positions. Thus the data would not immediately provide the Commission or market participants with information about the size of individual large short positions. Consequently, to the extent that knowing the total size of short positions held by managers with large positions conveys fundamental information to the market, then this fundamental information would not be immediately available if the Commission were to adopt a version of this alternative. Additionally, the data provided by this alternative would lack

transactions outside of the purview of CAT that may affect short positions. Thus the data provided by this rule would always be estimates of total short positions, which could be quite inaccurate for some Managers. Another drawback to this alternative is that releasing CAT data to the public could increase security risks. CAT contains highly sensitive information and creating a process that would release portions of the data, even if aggregated, could present risks.

The Commission could also consider two variations of this alternative. The first, which can be referred to as the minimalist approach, would not include Proposed Rule 205 and the Proposal to Amend CAT and instead would provide Manager short selling statistics based on existing CAT data.<sup>347</sup> The advantage to this variation is that it would provide additional information about the short selling activity and positions of Managers, compared to what is currently available, while requiring no additional resources from Industry Members except, perhaps, those passed on from an increase in resources for the Plan Processor to build out processing capacity—if the Plan Processor is chosen to aggregate reports and if it currently lacks such capacity. An additional drawback to this variation relative to the alternative above is that it would further limit the data that regulators have access to. Thus the benefits to having bona fide market making and buy to cover information described throughout Part VIII.D would not occur.

Lastly, a larger expansion of CAT could achieve at least the same data value as in Proposed Rule 13f-2 and Proposed Form SHO. For example, CAT could expand to require the reporting of all the information currently proposed to be collected in Proposed Form SHO. Specifically, the Commission could expand CAT to include data on account positions, including short selling positions as well as hedging information associated with those positions. In addition, CAT could be expanded to capture information on changes in those positions, options assignments, options exercises, secondary offering purchases, conversions, and other position changes. Under this approach, regulators would have access to the same data as if Managers filed Proposed Form SHO but for all short sellers, not only the subset of Managers reporting on Proposed Form SHO. This approach would also result in additional

<sup>347</sup> Once again, this variation and the following variation presume that the CAIS system is fully operational.

information available to regulators not collected in the Proposed Form SHO that could improve investor protections. In addition, this alternative would reduce costs for Managers who are not Industry Members because they would not be required to report new information. However, costs would increase for Industry Members who would have to report a lot of new information on CAT report types that don't exist today and for Participants who would have to implement changes and work out technical specifications for new types of CAT reports. Further, more Industry Members would report this information to CAT compared to Managers require to report information on Proposed Form SHO. It would be a major undertaking for both the Plan Processor as well as for industry participants to build out and adapt systems to collect, process, and publish this information. This implementation would likely be very complex and take a significant amount of time to compile. Overall, the cost of this alternative is likely to exceed the costs of Proposed Rule 13f-2 and Proposed Form SHO.

Further, if the Commission were to expand CAT to collect additional information beyond what would be captured by the Proposal to Amend CAT and Proposed Rule 205, such as position information, then these additional expansions would incur significant direct costs.

#### ii. FINRA Reporting

As discussed in part VIII.C.4.i, FINRA already collects and, together with the listing exchanges, disseminates aggregate short interest that it collects from member broker-dealers. Consequently, the Commission could codify their existing process to ensure that it continues in perpetuity. This alternative would have no additional costs to market participants, but would substitute a Commission mandate for the publication of the short interest data.

Similarly, the Commission could require FINRA to publish a version of their short interest information that specifically identifies the aggregate short interest of Managers—separate from other short interest. To accomplish this, reporting broker-dealers would separately report in their reports to FINRA the short positions that originate from Managers. FINRA would then compile both total short interest, as they currently do, as well as a Manager specific short interest. Because broker-dealers already have experience reporting short interest data to FINRA and would thus not need to build out new systems to report the data, this

alternative may be less expensive than the existing proposal as it would only require a modification of an existing process. This alternative would not provide the Commission with the positions of any identified Managers or any Manager-specific activity data, nor would it provide information on which positions are fully or partially hedged, thus the benefits and risks associated with these data articulated throughout Part VIII.D would decline.

The Commission also expects that data on Manager short interest in addition to total short interest would likely not provide much incremental value over the existing short interest data due to the likely significant overlap of the short positions of Managers and total short interest, and the absence of activity information to better understand changes in short interest.<sup>348</sup> Thus, while the alternative that requires FINRA to produce separate short interest data for Managers would reduce costs to market participants relative to the existing proposal, it also may not provide the market or regulators a significant incremental benefit relative to existing short selling data.

#### iii. Broker-Dealer Reporting to EDGAR on Behalf of Managers

The Commission could modify the existing proposal to allow broker-dealers to file Proposed Form SHO reports with the Commission on behalf of Managers. This alternative may reduce costs as it could concentrate reporting with broker-dealers that have significant experience collecting and providing such information—increasing operational efficiency.<sup>349</sup> On the other hand, Managers may use multiple prime brokers and thus the reporting prime broker may not have easy access to information about all such Manager's positions and activity in a security. Consequently, the prime broker would either need to report based on its limited information, which may lead to less complete data, or to gather additional information from the Manager about potential activity associated with another prime broker.<sup>350</sup> Reporting only information known by one prime broker could also result in less information if a Manager that

<sup>348</sup> Analysis of Form SH data indicates that these data, which would be a subset of the data collected in this alternative, amounted to a high percentage of short interest.

<sup>349</sup> See MFA Letter, *supra* note 306 (p. 3 for 10a-3T).

<sup>350</sup> The latter could result in the additional complication of double reporting or prime brokers having to coordinate on who reports a position. Likely, the least costly solution could involve Managers being responsible for informing their prime brokers of their threshold status.

otherwise would have exceeded the threshold for reporting does not exceed the threshold at one or more prime brokers. Requiring additional data collection may increase complexity and costs as Managers and broker-dealers would need to develop systems by which a Manager provides information about their activity with other prime brokers to their reporting broker. Or, the Commission could allow broker-dealers to report on behalf of Managers only if the broker-dealer could report full information. Thus Managers using multiple prime brokers would have the option of providing comprehensive information to their reporting prime broker, or they could report Proposed Form SHO data themselves.

#### iv. Harmonization With European Disclosure Requirements

The Commission could also explicitly craft Proposed Rule 13f-2 and Proposed Form SHO to be consistent with European disclosure requirements. In 2012, the European Parliament and the Council of the European Union adopted regulations on short selling (the “SSR”) that standardized the reporting threshold for all EU member states.<sup>351</sup> Under the SSR, the trading entity reports to the regulator when their net short position reaches the initial threshold of 0.2% of the share capital of the company, and in 0.1% up and down increments thereafter.<sup>352</sup> The threshold for reporting to the regulator recently was lowered to 0.1%.<sup>353</sup> Net short positions are computed taking into account relevant derivative positions such as options. If the net short position reaches 0.5% of the share capital of the company, then the reported short position is made public with the identity of the short seller revealed. New filings are required to be made whenever the short position increases or decreases by 0.1% of the share capital of the firm. In the EU, trading entities must submit their data to the regulator

by 3:30 p.m. on the following trading day.<sup>354</sup> Trading entities accomplish public disclosure via a central website operated or supervised by the relevant competent authority.<sup>355</sup>

Consequently, the Commission could structure the rule to require Manager short selling reports that are consistent with the European regulations in terms of the thresholds for reporting, the computation of the threshold, the items reported, when short sale information is made public, and when new reports have been issued. The advantage to this alternative would be that managers who engage in short selling in both the United States and in Europe would face similar regulations in both places—which may decrease the cost of compliance with both regulations.<sup>356</sup>

The EU structure whereby individual short sellers’ names are made public may raise the risk that investors may gather less fundamental information relative to the existing proposal as the risk of retaliation towards short individual sellers may increase, as well as the ability for market participants to engage in copy-cat strategies that decrease the profitability of gathering information.<sup>357</sup>

The EU data is more timely than what is considered in this proposal as the forms are posted publicly immediately after receipt by the regulator, potentially facilitating greater price discovery but at the cost of lowering the value of gathering information. Further, the EU guidelines do not provide activity data. Thus, market participants could not learn from an analysis of how short selling positions change over time. For instance, firm managers could only see the size of net short positions and thus may be hindered in their ability to learn from when short sellers built their positions and whether the building of a short position was in response to a specific manager action or firm announcement.

## 2. Data Modifications

### i. Release Proposed Form SHO Data in Alternative Formats

The Commission could release the information included in Proposed Form SHO in a different manner. This alternative could take one of several forms. For example, the Commission could release each Proposed Form SHO report to the public exactly as it is filed, identifying the Managers. The Commission could also release the Forms as filed, but with the identities of the filers stripped. The Commission could also release the aggregated data as in the current proposal but it could publish the data in different ways in the aggregated Proposed Form SHO report, such as, for example, publish the number of entities underlying the aggregated data, publish aggregations of the various categories of changes in short positions, or publish increases in short positions separate from decreases.

In the first alternative, the Commission could release Proposed Form SHO as filed, allowing all market participants to know the identities of short sellers—similar to the EU regulation discussed above. This would increase the information that market participants have to evaluate sentiment in the market. For example, if a short seller is viewed as sophisticated and informed, then releasing identifying information would likely spur copy-cat trading strategies. This outcome has been documented with respect to the EU regulation and suggests that revealing the identities of the short sellers may diminish the value of becoming informed.<sup>358</sup> In addition, all the detailed information on daily short activities across the various activity categories could reveal trading strategies, particularly if the Manager is identified. This information would also allow market participants to better manage risk by allowing them to manage their exposure to Managers with large short positions. Additionally, releasing the names of large short sellers would further increase the likelihood that the short seller would be the victim of a short squeezes or other retaliatory actions as described in Part VIII.D.1.

Similarly, the Commission could publicly release individual Proposed Form SHO filings with identification information stripped from the released data. This alternative would allow market participants a clearer view into the activities of large short sellers, potentially improving their ability to learn from the actions of large short

<sup>351</sup> See European Parliament and the Council of the European Union, Regulation No. 236/2012 (Mar. 24, 2012), available at <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:086:0001:0024:en:PDF> (The SSR was adopted by the European Parliament and the Council of the European Union on March 14, 2012 and became effective on November 1, 2012).

<sup>352</sup> *Id.* (at Article 5(2)).

<sup>353</sup> The threshold was temporarily lowered in March 2020 in response to the COVID-19 pandemic. In October 2021, the change became permanent. See European Union, Commission Delegated Regulation No. 236/2012, Register of Commission Documents, available at [https://ec.europa.eu/transparency/documents-register/detail?ref=C\(2021\)6815&lang=en&utm\\_source=Cleverreach&utm\\_medium=email&utm\\_campaign=Update%20Shareholder%20Activism&utm\\_content=Mailing\\_13052681](https://ec.europa.eu/transparency/documents-register/detail?ref=C(2021)6815&lang=en&utm_source=Cleverreach&utm_medium=email&utm_campaign=Update%20Shareholder%20Activism&utm_content=Mailing_13052681).

<sup>354</sup> *Id.* (at Article 9(2)).

<sup>355</sup> *Id.* (at Article 9(4)).

<sup>356</sup> Due to uncertainties regarding the EU short selling data regarding the identities of short sellers and the ability to map those IDs to US Managers, the Commission cannot identify the number of US Managers that currently comply with EU regulations.

<sup>357</sup> For analyses of how the SSR lead to increased copycat trading, lower price efficiency, and increased volatility, see Stephan Jank, Christoph Roling, and Esad Smajlbegovic, *Flying Under the Radar: The Effects of Short-Sale Disclosure Rules on Investor Behavior and Stock Prices*, 139 (1) J. of Fin. Econ. 209–233 (2021); Charles M. Jones, Adam V. Reed, and William Waller, *Revealing Shorts an Examination of Large Short Position Disclosures*, 29 (12) The Rev. of Fin. Studies 3278–3320 (2016).

<sup>358</sup> See *supra* Part VIII.F.1.iv (discussion in section).



sellers relative to the current proposal. For instance, the data would allow market participants to know whether short sentiment was broadly held—as would be indicated by many filings—or concentrated—as would be indicated by few filings. This information could potentially improve the market assessment of bearish sentiment relative to Proposed Rule 13f–2, improving price efficiency.

However, the indirect costs of this alternative would be greater than for Proposed Rule 13f–2 and Proposed Form SHO. Releasing all the information from Proposed Form SHO could reveal trading strategies that would be costly even if the identities of the short sellers remained anonymous. For example, releasing this information may increase the risk of copycat trading which eats into the profits of acquiring information. It may also provide information about how vulnerable short sellers may be to a short squeeze as it could give a signal about whether a short seller has a large and potentially vulnerable short position thus increasing this risk to short sellers. In this case, the negative effects of the rule on the value of collecting information and of short selling in general would be greater than the current proposal, leading to less price efficiency and potentially more volatility. Additionally, even though the data could be released anonymously, it is not clear that in all cases the identities of the individual short sellers would remain anonymous.<sup>359</sup> If market participants were able to back out the identities of individual short sellers, then the risk of retaliation or short squeezes would increase relative to Proposed Rule 13f–2 and Proposed Form SHO.

Alternatively, the Commission could release the data as specified in the current proposal but also include the number of entities whose Proposed Form SHO reports were collected. This information would provide the market with additional detail about whether short sentiment was broadly held by multiple managers, or narrowly held by

just one or a few. This information could be useful as market participants assess bearish sentiment in the market and adjust their actions accordingly. Adding this information may also increase the risk of short squeezes or other retaliatory actions in the case where there were very few reporters of Proposed Form SHO. In the Form SH data collected under Temporary Rule 10a–3T, 32% of stocks had only one Manager reporting a position per month.<sup>360</sup> Such a situation could signal to market participants that one, or a few, short sellers have large short positions that could potentially be vulnerable to a squeeze.

The Commission could collect Proposed Form SHO data as proposed but in the data made public, the Commission could aggregate at the issuer level as opposed to the security level. Aggregating at the issuer level would allow users of the data a simpler view into overall short selling for the whole firm. However, computing this aggregation introduces complexity, as different share issues sometimes have different prices or voting rights, thus it may not make economic sense to aggregate all short selling data across all share classes for the same issuer. This effect would decrease the information content of the data with respect to bearish sentiment, which decreases what market participants could learn from the data, but also would make it more difficult for market participants to copycat short selling strategies.

As another alternative, the Commission could release statistics on the Proposed Form SHO filings aggregated across Managers but not netted across the various activity categories. This would allow market participants to not only see the extent of the position changes of large short sellers but also how they achieve their position changes, including whether they create or cover positions in the equities market or by options exercises, for example. The Commission believes that such information could risk revealing trading strategies, even if aggregated across Managers, particular if Managers have correlated strategies. As a result, this would be more costly to Managers than Proposed Rule 13f–2 and would dissuade fundamental research more. On the other hand, while such information is of more regulatory value, by publicly releasing more detailed activity data, some market participants may benefit from learning the various ways that short sellers change their positions.

Similarly, the Commission could collect Proposed Form SHO data as proposed but publicly release the daily aggregate increases in short positions separately from the daily aggregate decreases in short positions as opposed to daily net changes to short positions as currently proposed. This approach would provide the public more detailed information and understanding on what drives changes to short positions. However, separating daily aggregate increase from decreases in short positions could increase the risk of revealing trading strategies, which could disincentivize short selling and harm market quality.

#### ii. Collect Data on Derivatives Positions

Investors can use derivatives to take an economically short position in a security. For example, an investor with a bearish view of a stock can purchase a put option in that stock. Consequently, for a more complete view of the total economic short position that a Manager has taken, the Commission could require Managers who report Proposed Form SHO to also disclose their derivatives positions on underlying equity securities in derivatives such as options and total-return swaps as an alternative to the existing proposal which does not directly collect information on derivatives.

Requiring this data would provide a more complete view of the economic short position that a Manager engaging in a large short sale has taken. Consequently, the information would aid market participants in gauging bearish sentiment in a security relative to Proposed Rule 13f–2 and Proposed Form SHO. This information may also help the Commission to better evaluate potentially risky short positions and respond more quickly in the case of a market event. The Commission could also better reconstruct market events, such as the recent meme stock events in January 2021, with options positions data.

Requiring options data to be reported on Proposed Form SHO would increase the compliance costs to Managers of reporting on Proposed Form SHO. While Managers generally track their options exposure carefully, it is frequently different trading desks that execute options trades and equity transactions. Thus, it is possible that Managers use separate systems to track their options and equity positions. For these Managers, collecting options and equity transactions to report the data required for Proposed Form SHO would require building a process to pull data from two separate systems—increasing the cost of complying with the rule.

<sup>359</sup> Issuers have been known to hire private investigators to try and uncover the identities of short sellers when they learn that their stock is being targeted by short sellers. See *supra* note 258. Additionally, researchers have used algorithms to unmask the identities of individuals from masked data released to the public by the SEC. See Huaizhi Chen, Lauren Cohen, Umit Gurun, Dong Lou, and Christopher Malloy, *IQ from IP: Simplifying Search in Portfolio Choice*, 138 J. of Fin. Econ. 118–137 (2020). While the Commission could design this alternative to avoid the specific vulnerabilities exploited by Chen et al (2020) it is possible that motivated researchers and market participants could find some other unforeseen way to link the public data to individual short sellers.

<sup>360</sup> See *supra* note 80 (for more information on methodologies and caveats for using Form SH data).

Requiring derivative position information may also be duplicative of other derivatives reporting requirements. For instance, recently proposed Rule 10B–1 requires individuals, or groups of individuals, who own security-based swaps that exceed a certain threshold to report certain information to the SEC, which information would be made publicly available.<sup>361</sup>

### iii. Report Net Short Positions Instead of the Gross Position With Hedging Information

The Commission could require managers reporting Proposed Form SHO data to report net short positions instead of gross short positions. Net short positions would take into account any hedging the Manager engages in. For instance, a Manager that has a large long position in options that is largely hedged using short sales in equities is not taking an economically significant short position in the security. Fully hedged short positions are less likely to be manipulative in nature, or to pose systemic risk. Consequently, the Commission could limit reporting to only Managers whose economic short positions surpass the thresholds. Doing so would limit the amount of data collected by the Commission and would thus reduce the cost of the alternative relative to Proposed Rule 13f–2 but also reduce somewhat the value of the data in terms of using it to reconstruct market events. For instance, during the recent meme stock phenomenon, for certain stocks it became difficult to hedge options transactions using the underlying security due to the significant price changes in the spot market. Consequently, positions that may have previously appeared to have been hedged, and thus low risk, may no longer be as hedged as previously supposed, and in this case, large short positions that were initially hedged may become systemically important as the hedge breaks down due to unforeseen extreme market events. In this case, it would be useful for the Commission to have information on large hedged short positions largely to aid in reconstruction of market events. This alternative would limit what the public and the Commission could learn from large hedged positions relative to the Proposed Rule 13f–2 and Proposed Form SHO. For instance, the alternative would preclude a comparison of total short interest with reported large hedged short positions, which may

provide additional information to the market about the activities of large, though perhaps non-information based, traders.

Additionally, the Commission could require Managers to report the delta value of their hedged positions rather than providing an indicator for whether a position is fully or partially hedged.<sup>362</sup> This alternative could have some of the same advantages as the other alternatives in this section. If the Commission published this information aggregated across Managers, then market participants would have a clearer view into economic—*i.e.* unhedged—short positions than is provided by the Proposed Rule 13f–2 and Proposed Form SHO. The cost of this alternative is an increased reporting burden for Managers as they would be required to compute for the report delta value of their hedge. However, knowing information about the delta of short seller's hedge can provide information about how vulnerable a short seller, or short sellers, may be to a short squeeze. If this information was not made public by the Commission, however, it would allow the Commission an improved view into individual short sellers with potentially risky short positions without raising those concerns.

### 3. Threshold Modifications

As an alternative to Threshold A's two-pronged threshold, the Commission could require reporting Proposed Form SHO at either higher or lower thresholds—or no threshold. When soliciting comments for Temporary Rule 10a3–T, commenters suggested thresholds ranging from 1% to 5%.<sup>363</sup> When selecting thresholds, the fundamental economic tradeoff is the value of the data versus the cost of collecting the data.

Alternative thresholds that are lower than Threshold A or Threshold B specified in Proposed Rule 13f–2 or an alternative that would not contain a threshold would produce more data as more entities would be required to report. In the Form SH data collected under Temporary Rule 10a–3T, the threshold of \$10 million or 2.5% would collect 89% of the dollar value of the short positions required to be reported.<sup>364</sup> Therefore, the increase in coverage from a lower threshold would be low relative to the coverage in the

proposed Threshold A. Notwithstanding the low potential for an increase in coverage, the Commission recognizes that this increased coverage could increase benefits. For example, this additional data from the alternative would enhance the benefits to the Proposed Form SHO data articulated above relative to Proposed Rule 13f–2 and Proposed Form SHO. Specifically, it would provide market participants with a clearer view of Manager bearish sentiment than the current proposal provides for as more managers would be required to report the data, making the data more comprehensive. A lower threshold would also allow the Commission to more easily reconstruct significant market events where short selling is involved and enhance Commission oversight of short selling—again because the data would be more comprehensive.

A lower or no threshold would increase the cost of reporting Proposed Form SHO data in terms of direct costs associated with Managers compiling and submitting the required data through EDGAR and in the indirect costs associated with revealing short sellers' information. In the Form SH data collected under temporary Rule 10a–3T, the number of reporting Managers for the *de minimis* threshold of 0.25% of shares outstanding or \$10 million was 442, compared to 346 for the \$10 million or 2.5% threshold in Threshold A of the proposed rule.<sup>365</sup> Additionally, Managers would likely be required to file reports for more securities, which would also increase compliance costs. Indirect costs include increased risk of copycat short selling strategies, which lead to herding and increased volatility, and short sellers engaging in strategic behavior to short sell just underneath Threshold A, which leads to lower price efficiency.<sup>366</sup> In some cases a lower threshold would decrease the indirect costs associated with the proposed rule because it would be harder to identify individual short positions from aggregate reporting if there are many entities reporting, thus lowering the chances that a given security would only have one Manager reporting a short position.<sup>367</sup> This effect may not be universally true, however. In particular, at thresholds just lower than proposed Threshold A, the number of securities where only one entity

<sup>362</sup> Delta is a ratio that measures the change in the value of short position when the value of the long position changes. For example, a delta of one means that a \$1 increase in value of the short position results in a \$1 decline in value of the long position.

<sup>363</sup> See *supra* note 79 (for links to specific comment letters).

<sup>364</sup> See *supra* Table I. See also *supra* note 81.

<sup>365</sup> *Id.*

<sup>366</sup> See *supra* notes 271 and 353 (for research documenting this behavior in Europe).

<sup>367</sup> See *supra* notes 257 and 278 (with accompanying text for more information on risks of identifying individual short sellers).

<sup>361</sup> See Exchange Act Release No. 93784 (Dec. 15, 2021), available at <https://www.sec.gov/rules/proposed/2021/34-93784.pdf>.

reported Form SH increases.<sup>368</sup> This result implies that there are a number of securities for which only one short seller held a significant short position at a level lower than the current cutoff. In these cases, lowering the threshold may increase the risk of identifying individual short sellers.

Conversely, raising the proposed Threshold A lowers many of the costs associated with providing Proposed Form SHO data as fewer entities would be required to report. It also limits somewhat the value of the data—again as the reported data would reflect a smaller portion of overall short positions. For example, in the Form SH data, a threshold of 5% or \$25 million suggested in comment letters reduce the coverage to 71% of dollar value of short positions compared to 89% in the proposed rule.<sup>369</sup> Higher thresholds may also come with increased risk of identification and retaliation towards short sellers because at some point the likelihood that more than one investor holds a very large short position diminishes. For example, according to analysis for Form SH data 41% of reported securities would reflect one Manager with a short position at a threshold of \$25 million and 5% compared to 24% of reported securities for the proposed Threshold A.<sup>370</sup>

For securities subject to Threshold B, the economic impact of either raising or lowering the dollar threshold would be similar. Raising the threshold would lower compliance costs, but also lower the quality of the data while lowering the threshold would do the opposite. For example, if the Commission raised Threshold B from \$500,000 to \$10 million, then under the assumption of one manager short selling each Threshold B security, the total number of short positions captured for Threshold B securities would decrease from 23.72% to 8.76%.<sup>371</sup> Similarly, under the same assumptions, lowering the threshold to \$50,000 would increase the number of short positions captured to 48.08%.

As another alternative to the proposed Threshold A, the Commission could establish a threshold based on one of the thresholds in Proposed Rule 13f–2—

<sup>368</sup> According to Form SH data, 32% of securities would have only one Manager reporting at or above the currently proposed threshold of \$10 Million and 2.5%. If the percent threshold was reduced to 1% along with the \$10 million threshold the number of securities with only one Manager reporting would increase to 35%. See also *supra* note 81.

<sup>369</sup> See SIFMA letter (discussing Temporary Rule 10a3–T). See also *supra* Table I. See also *supra* note 81.

<sup>370</sup> See note 80 (for more information on methodologies and caveats for using Form SH data).

<sup>371</sup> See *supra* Table II (analysis within table).

short position as a percent of shares outstanding or the dollar value of the short position. The advantage of this alternative is that it may reduce compliance costs by simplifying reporting requirements. Additionally it would lower overall compliance costs due to fewer entities being required to report as entities that may meet one threshold may not meet another and thus may not be required to report. An alternative including only the 2.5% threshold would have a bigger impact than an alternative including only the \$10 million threshold. Commission analysis based on Form SH data suggests that 342 Managers would meet the \$10 million threshold and 160 Managers would meet the 2.5% threshold, compared to 346 in Proposed Rule 13f–2.

The alternative of requiring a threshold based only on short positions as a percent of shares outstanding would largely eliminate reporting in larger securities. Short sellers will hit the 2.5% threshold in stocks with market capitalization below \$400 million before they hit the \$10 million dollar threshold. For stocks with market capitalization above \$400 million, short sellers will hit a \$10 million dollar threshold before hitting the 2.5% threshold. Consequently, if the Commission required reporting based only on the percent of shares outstanding, then there would be fewer reports of Proposed Form SHO for stocks with larger market capitalizations. Less visibility into the actions of short sellers in larger market capitalization stocks would provide less information about bearish sentiment in the economy, generally because larger market capitalization stocks tend to be more well-established and harder to manipulate.<sup>372</sup> Conversely, if the Commission required reporting based only on the dollar threshold, then there would be fewer reports among stocks with lower market capitalizations. Smaller market capitalization stocks tend to be easier to manipulate and less stable. Thus, less visibility into the actions of short sellers among smaller market capitalization stocks may mitigate somewhat the benefits of reduced manipulative behavior among these stocks articulated in Part VIII.D.1.

As another alternative, the Commission could structure the Reporting Thresholds to include the

<sup>372</sup> See, e.g., Carole Comerton-Forde, Tālis J. Putniņš, *Stock Price Manipulation: Prevalence and Determinants*, 18 (1) Rev. of Fin. January 2014, Pages 23–66, available at <https://doi.org/10.1093/rj/rfs040> (for evidence on small and less liquid stocks higher exposure to manipulative behavior by investors).

nominal economic value of short derivative positions. Specifically, reporting on Proposed Form SHO would be required if a Manager's total short position in the stock and in derivatives such as options and security-based swaps exceeded the relevant Reporting Thresholds. This alternative would decrease the likelihood that Managers seek to avoid the Reporting Thresholds by transacting in derivatives and thus, may increase the benefits of the data from Proposed Form SHO.<sup>373</sup> Making it more difficult to circumvent the reporting requirements using derivatives may also decrease strategic, and sub-optimal, trading around the Reporting Thresholds which leads to lower price efficiency.<sup>374</sup> However, increasing the amount of information that is provided in Proposed Form SHO may increase copycat activity that leads to herding and increased volatility. Conversely, increasing the reports may dilute the information and reduce the amount of herding. This alternative could also result in some situations in which Managers would have a reporting obligation despite having large long positions in the equity over the entire month, which would increase costs for the Managers and would provide less relevant information. Additionally, including derivatives in the Reporting Threshold computations would increase the complexity of the rule and the cost of implementing the rule. For instance, Managers may need to pull information from multiple systems to determine the total value of their short position for reporting. Pulling information from multiple systems can be costly.<sup>375</sup> Additionally, while valuing short positions in most equities is fairly straight forward, this is not true for derivatives. There are often multiple methodologies used by different market participants to value derivative contracts such as options. Thus, an alternative including a threshold for a Managers short exposure in derivatives would be significantly more

<sup>373</sup> See *supra* Part VIII.D.8.

<sup>374</sup> See *supra* Part VIII.D.1 (for further discussion on strategic trading around the threshold and how the rule is designed to reduce it).

<sup>375</sup> Industry practices may change with regard to security-based swaps in the case of the adoption of proposed Rule 10B–1, which would require persons with large positions in security-based swaps to track all related securities. See Exchange Act Release No. 93784 at 23 (stating that “proposed Rule 10B–1 would require public reporting of, among other things: (1) Certain large positions in security-based swaps; (2) positions in any security or loan underlying the security-based swap position; and (3) positions in any other instrument relating to the underlying security or loan or group or index of securities or loans”) available at <https://www.sec.gov/rules/proposed/2021/34-93784.pdf>.

complicated than Proposed Rule 13f-2 and Proposed Form SHO.

An alternative could also involve requiring the thresholds to be based on activity and not just positions. This alternative would increase the amount of information available to the Commission regarding the activities of entities engaging in a high volume of short selling. This alternative may provide additional insight into Managers that sell short but do not hold short positions. Specifically, entities with high volumes of short selling are likely to be market makers who use short selling to maintain two sided quotes in the absence of inventory and other high frequency traders. These entities trade in large volumes, but tend to end trading sessions fairly flat on inventory in larger stocks. Consequently, requiring reporting based on activity may not significantly improve the market's ability to assess of bearish sentiment. However, one area where reporting based on activity may be beneficial would be in identifying short selling attacks that are relatively short lived. For example, an investor with a convertible bond may seek to distort the stock price right around the exercise date of their bond as such contracts stipulate that the holder of the convertible bond receives more shares if the stock price is lower. In this case, an attempted manipulator may seek to aggressively short sell right around a convertible bond exercise date. Activity that may be concentrated enough in time to not trigger a Reporting Threshold based on average position over the prior month as is currently stipulated in the proposal. While this activity information may be helpful in flagging unusual short selling activity as the Commission could conceivably build reports based on existing CAT data that would be more effective at detecting such behavior and Proposed Rule 13f-2 would identify these activities if the market participant exceeds the Reporting Thresholds.

The Commission could measure the thresholds as of the last settlement day of the month rather than on any day of the month, as in the \$10 million prong, or as the average position over the month, as in the 2.5% prong for Threshold A and the \$500,000 threshold in Threshold B. This alternative would have the advantage of simplifying compliance with Proposed Rule 13f-2 and Proposed Form SHO and thus may reduce compliance costs. In the Form SH data, end of month thresholds reduced the number of reporting Managers for the \$10 million threshold from 342 to 247, and for the 2.5%

threshold from 160 to 127.<sup>376</sup> It would also line the Reporting Thresholds up with the positions reported in Proposed Form SHO whereas a Manager's reported information on Proposed Form SHO under Proposed Rule 13f-2 could be below the Reporting Thresholds.<sup>377</sup> This alternative may also invite more strategic trading around the end of the month than the proposal, which is structured to prevent trading around the threshold. For instance, Managers with short positions near the threshold may temporarily reduce their positions to below a Reporting Threshold on exactly the days that short positions are measured for compliance with the threshold to avoid reporting. This inefficient trading may reduce price efficiency right around the reporting days as trading to avoid holding a position that would trigger reporting is not trading based on economic considerations but rather trading based on regulatory considerations and thus is inefficient and may harm price efficiency on these days.

Instead of Threshold B, the Commission could require the two prong, \$10 million maximum position or 2.5% average position, reporting threshold for short positions in an equity security of a non-reporting company issuer that is required for equity securities of reporting company issuers. This approach may be less complex as all short positions would be subject to the same reporting threshold. Further, it would retain a threshold that relates to the size of the short position to the size of the issue to ensure capturing positions that are relatively large whereas the proposed Threshold B imposes a flat threshold that could result in some relatively large positions not being filed on Proposed Form SHO.

However, this alternative would increase the burden for Managers as information for non-reporting issuers can be hard to find, making threshold calculations difficult. In particular, information for the number of shares outstanding can be difficult to obtain for non-reporting issuers and when it is available it is often stale and inaccurate. This could lead to problems with the calculations for the 2.5% threshold. Because the alternative would require knowing shares outstanding of such securities each day, this alternative would effectively impose new recordkeeping costs on Managers as Managers would need to track daily

changes in shares outstanding in order to assess the 2.5% threshold. Further, there are multiple sources from which Managers can obtain shares outstanding for securities in non-reporting company issuers. At times these sources may report different numbers for total shares outstanding. Consequently, Managers could also feel the need to track the sources used to identify shares outstanding each day and would incur costs to determine which sources to trust for compliance.

Additionally, the Commission could enhance record keeping requirements associated with the alternative where Threshold A applies to all securities to require Managers to record and report on Form SHO the source of data used to calculate shares outstanding in relation to determining compliance with Threshold A. This could improve the quality of the information reported in the Proposed Form SHO for securities of issuers who do not report with the Commission, by improving the quality of the data that Managers use when calculating their positions. It may also help mitigate concerns that Managers may try to game different data sources to avoid complying with the regulation. For securities of reporting issuers, accurate shares outstanding information is readily available, thus concerns about gaming data sources or using low quality information is not as relevant. However enhanced record keeping requirements would increase the costs to Managers. While the Commission believes that most Managers have ready access to this information, requiring that Managers record and report the information would impose require Managers to further build out systems, in conjunction with the systems already required to report Form SHO, to also capture the source of information used.

#### 4. Other Alternatives

##### a. Alternative Reporting Frequency or Additional Reporting Delay

As alternatives, the Commission could require reporting at different frequencies than the monthly reporting proposed by the rule. Specifically, the Commission could require reporting at frequencies that are shorter than a month. For example, the Commission could require reporting daily, weekly, bi-weekly, or whenever there is a significant change in short position (as is currently the standard in the European Union), but at least monthly. These alternatives could require reporting if the average short position surpasses the threshold for the month prior to the reporting period or if average positions surpass the threshold

<sup>376</sup> See *supra* Table I.

<sup>377</sup> For example, a Manager's position could exceed the \$10 million threshold on the 7th of the month but be below \$10 million and 2.5% on the last settlement day of the month.

for the prior period (e.g. week, or two weeks). The fundamental tradeoff with such thresholds compares the simplicity of the rule with the potential to game the threshold by strategic trading. Such alternative frequencies face the fundamental tradeoff of increased cost and increased transparency of the data. Put simply, increasing the reporting frequency increases the number of reports and thus increases the cost associated with reporting by a similar factor. Increased reporting frequency could also result in collecting more information than the current proposal. The difference between the information collected in the current proposal and this alternative would mainly come from the frequency and timeliness of the reports. The improved timeliness could increase the risk of copycat strategies, but also improve price efficiency. An additional difference to the data may come from Managers who for a short time have short positions that are subject to Threshold A and are above the 2.5% threshold but below the \$10 million threshold, but do not maintain an average short position over 2.5% over the month. These Managers may be required to report with more frequent disclosures.<sup>378</sup>

The Commission could also consider different reporting windows for Managers who meet the threshold short positions to report Proposed Form SHO. The current proposal requires Managers to report Proposed Form SHO within 14 calendar days of the end of each month. Shorter time horizons may increase the cost of reporting as Managers would have less time to gather and submit the data on Proposed Form SHO and may need to build costlier procedures to ensure compliance with the reporting requirement.<sup>379</sup> A mitigating factor is that most of this reporting is likely to be done electronically, consequently it may not take the full 14 calendar days for Managers to gather and file the required data to the Commission.

Additionally, the Commission could adopt different horizons for releasing the aggregated data after the reporting deadline. The fundamental tradeoff in terms of the delay between reporting and when the Commission releases the aggregated data is that a shorter delay increases the relevance of the data, in terms of the bearish sentiment it contains which may improve managerial decision making, as well as providing more timely information

about bearish sentiment in the market. At the same time a shorter delay increases the likelihood of copycat behavior which decreases the incentive that short sellers have to gather information potentially leading to lower price efficiency and greater volatility. The converse is true for longer delays. Additionally, a shorter delay provides less time for the Commission to aggregate the data and run checks on the aggregated data to ensure the Commission's aggregation is error-free, and also provides less time for amendments to be filed, both of which could harm the quality of the data.

#### b. Requiring Information From Customers for Proposed Rule 205

To enhance the value of the buy to cover mark in CAT, the Commission could also modify components of Regulation SHO whereby broker-dealers would be required to gather information from customers regarding whether a purchase meets the definition of buy to cover. In Proposed Rule 205, broker-dealers would be required to mark transactions a buy to cover based only on information to which they currently have access and they would not be required to net such activity across the same customer's accounts at that broker-dealer. This may miss some buy to cover trades that may occur if a Manager uses a broker to execute short sales and a prime broker (or prime brokers) for other long positions. In this case, the broker-dealer managing the purchase of shares would not know that the buy is actually a buy to cover and would thus not mark the trade as such. The current proposal may also miss some transactions that may occur if a Manager uses multiple accounts at the same broker-dealer to trade.

To close this gap in buy to cover data, the Commission could require broker-dealers to collect information from customers concerning whether a given buy trade is a buy to cover trade, when considering positions held at other broker-dealers. This alternative would increase the accuracy of the buy to cover information collected via Proposed Rule 205, which would enhance the benefits discussed in Part VIII.D. However, this alternative would impose significant costs on broker-dealers that do not already collect such information relative to the current proposal as it would require broker-dealers to alter their systems to collect this additional information from customers. It would also impose costs on customers who would likewise need to alter their own systems and to report such information to their broker-dealer. The number of customers incurring those costs would

be limited to the number of customers employing multiple broker-dealers to execute trades and maintain positions. For customers with only one broker-dealer, this alternative would not impose any additional costs as in this case their only broker-dealer would have a comprehensive view of the customer's positions from which to determine whether a trade was buy to cover or not.

The Commission could also require broker-dealers to aggregate trades across all accounts by the same purchaser at the same broker-dealer when determining buy to cover status of an order under Proposed Rule 205. This alternative would include short positions held in any account other than the purchasing account, as well as offsetting long positions held by the purchaser in the purchasing account or any other account for purposes of the broker-dealer's "buy to cover" order marking determination. This alternative could create more comprehensive buy to cover marks in CAT but would also come with additional compliance costs for broker-dealers as they would need to build out systems to track the net positions of customers across all accounts in real time to determine whether a given order qualified as a buy to cover transaction.

#### c. Report Proposed Form SHO in Inline XBRL

The proposal would require Proposed Form SHO to be filed in Proposed Form SHO-specific XML, a structured, machine-readable data language. As an alternative, the Commission might require Proposed Form SHO to be filed in Inline eXtensible Business Reporting Language ("Inline XBRL"), a separate data language that is designed for business reporting information and is both machine-readable and human-readable. Compared to the proposal, the Inline XBRL alternative for Proposed Form SHO would provide more sophisticated validation, presentation, and reference features for filers and data users. However, given the fixed and constrained nature of the disclosures to be reported on Proposed Form SHO (e.g., the information would be as of a single reporting date rather than multiple reporting dates, and Managers would not be able to customize the content or presentation of their reported data), the benefits of these additional features would be muted. Compared to the proposal, this alternative would impose greater initial implementation costs (e.g., licensing Inline XBRL filing preparation software) upon reporting persons that have no prior experience

<sup>378</sup> Many Commenters on temporary Rule 10a-3T stated that weekly reporting was overly burdensome. See *supra* note 306.

<sup>379</sup> See Seward & Kissel LLP letter (discussing Temporary Rule 10a3-T) at 5, available at <https://www.sec.gov/comments/s7-31-08/s73108-43.pdf>.

structuring data in Inline XBRL.<sup>380</sup> By contrast, because many Managers that would be Proposed Form SHO filers would likely have experience structuring filings in a similar EDGAR Form-specific XML data language, such as in the context of submitting Form 13F, the Proposed Form SHO-specific XML requirement would likely impose lower implementation compliance costs on Proposed Form SHO filers than an Inline XBRL requirement would impose.

### G. Request for Comments

The Commission requests comment on all aspects of this Economic Analysis, including whether the analysis has: (1) Identified all benefits and costs, including all effects on efficiency, competition, and capital formation; (2) given due consideration to each benefit and cost, including each effect on efficiency, competition, and capital formation; and (3) identified and considered reasonable alternatives to the proposed new rules and rule amendments. We request and encourage any interested person to submit comments regarding the proposed rules, our analysis of the potential effects of the proposed rules and proposed amendments, and other matters that may have an effect on the proposed rules. We request that commenters identify sources of data and information as well as provide data and information to assist us in analyzing the economic consequences of the proposed rules and proposed amendments. We also are interested in comments on the qualitative benefits and costs we have identified and any benefits and costs we may have overlooked. In addition to our general request for comments on the Economic Analysis associated with the proposed rules and proposed amendments, we request specific comment on certain aspect of the proposal:

- Q35: *Short Selling Data*. The Economic Analysis discusses several existing sources of short selling data and the limitations of each.

- Are the Commission's descriptions of existing short selling data accurate? Why or why not? Please explain. Are there other relevant existing data sources that the Commission should consider as a part of the baseline? If so, please describe them.

- Are the Commission's descriptions of the various limitations in existing short selling data accurate? Please explain. Are there limitations that the Commission has not discussed? If so, please describe these limitations.

- Q36: *Additive Information in Proposed Rule 13f-2 and Proposed Form SHO, Proposed Rule 205, and the Proposal to Amend CAT*. These Proposed Rules would require the reporting of short sale information to EDGAR or to CAT.

- Would Proposed Rule 13f-2 and Proposed Form SHO provide information to the public that is additive to what the public can already access? Would these proposals solve some or all of the data limitations discussed in the Economic Analysis? Why or why not?

- Would Proposed Rule 205 and the Proposal to Amend CAT solve the data limitations discussed in the Economic Analysis? Why or why not? Are there significant limitations, beyond those discussed above, in the design of the data for the public in Proposed Rule 13f-2 and Proposed Form SHO that limits the utility of the data to the public?

- Are there significant limitations, beyond those discussed above, in the design of the data available to regulators in Proposed Rule 13f-2 and Proposed Form SHO, Proposed Rule 205, and the Proposal to Amend CAT?

- Q37: *Market Oversight and Investor Protection*. The Economic Analysis describes how the information from the Proposed Rules could be used to, for example, strengthen regulatory oversight of short selling and facilitate market reconstructions.

- Would the Proposed Rule 13f-2 and Proposed Form SHO help to strengthen regulatory oversight and facilitate market reconstructions? Please explain. What would the role of each of the components of Proposed Form SHO to these regulatory activities? Are there any other regulatory activities facilitated by these proposed rules? If so, please describe.

- Would Proposed Rule 205 and the Proposal to Amend CAT help to strengthen regulatory oversight and facilitate market reconstructions? Please explain. Are there any other regulatory activities facilitated by these proposed rules? If so, please describe.

- Would the additional regulatory oversight of short selling from the Proposed Rules help deter manipulative short selling behavior? Why or why not? What are some other potential benefits to investors of the regulatory activities facilitated by the Proposed Rules?

- Q38: *Market Quality*. The Economic Analysis describes both potential improvements to market quality and potential harms to market quality that could result from the published data from Proposed Rule 13f-2 and Proposed Form SHO. In addition, the Economic Analysis describes potential improvements to market quality that could result from Proposed Rule 205 and Proposed Amendments to CAT.

- Overall, would the Proposed Rules, on net, improve or harm market quality? Please explain. Please discuss the extent, if any, to which each proposed rule contributes to the overall effect on market quality.

- Would the information published from Proposed Rule 13f-2 and Proposed Form SHO be useful to market participants and provide information that is not already reflected in prices? Please explain. For example, would the published data help market participants better understand existing short interest information by lining up the position information with a short interest settlement date, by identifying the aggregate positions held by reporting Managers, by identifying the extent to which reporting Manager positions are fully or partially hedged, or by revealing the daily changes in reporting Manager short positions? Please explain. As a result, would such information improve price efficiency and market liquidity? Please explain.

- Would the regulatory activities facilitated by Proposed Rule 13f-2 and Proposed Form SHO, Proposed Rule 205, and the Proposal to Amend CAT improve price efficiency and market liquidity? Please explain.

- Would the compliance costs associated with Proposed Rule 13f-2 and Proposed Form SHO lead to a reduction in shorting significant enough to negatively affect price efficiency and/or market liquidity? Why or why not?

- Would the published data from Proposed Rule 13f-2 and Proposed Form SHO result in short selling Managers being more vulnerable to fundamental information leakage, the revelation of trading strategies, or short squeezes and other forms of retaliation? Please explain. Would any of these effects be significant enough to negatively affect price efficiency and/or market liquidity? Why or why not? For example, would these effects significantly reduce the incentive of Managers to engage in fundamental research? Please explain and identify the particular part of elements of the published data that would result in such effects.

- Would Managers seek to reduce their short positions to avoid exceeding

<sup>380</sup> See Inline XBRL Filing of Tagged Data, Securities Act Release No. 10514 (June 28, 2018), 83 FR 40846 at 40862, available at <https://www.sec.gov/rules/final/2018/33-10514.pdf> (discussing costs associated with Inline XBRL filing of operating company financial statements and investment company risk/return summaries, including software licensing costs).

a Reporting Threshold or to report a lower short position than the Manager typical holds? Please explain. What would be the effect of such behavior on price efficiency and market liquidity? Please explain.

- To what degree does the structure of the data, such as the level of aggregation, threshold structure and delayed publication help to mitigate any potential negative effects of Proposed Rule 13f-2 and Proposed Form SHO? Please explain.

- Despite these mitigating factors, could market participants identify the particular Managers and their reported positions and activity? If so, what are the additional risks and costs faced by such Managers? Please explain.

- Are option market makers likely to exceed the Reporting Thresholds? If so, what would be the effect on price efficiency and market liquidity of such inclusion? Please explain.

- Q39: *XML Requirement.*

- Would requiring the proposed short sale disclosures to be filed on EDGAR in Proposed Form SHO-specific XML increase the economic effects of the disclosure requirement by making the reported data more useful to users? Why or why not?

- How would the costs and benefits of an Inline XBRL requirement compare to the Proposed Form SHO-specific XML requirement for the proposed short sale disclosures?

- Would requiring short sale disclosures to be filed in Proposed Form SHO-specific XML facilitate more efficient review and analysis of the reported short sale disclosures by the Commission? Why or why not?

- Would the costs of the XML requirement vary by the type of Manager likely to file Proposed Form SHO? If so, please explain which Managers would incur higher or lower costs.

- Q40: *Compliance Costs.*

- Has the Commission appropriately evaluated the compliance costs associated with the Proposed Rules? Please explain. What are the primary cost drivers of the Proposed Rules?

- Would Proposed Rule 13f-2 and Proposed Form SHO have lower compliance costs than former Rule 10a3-T? Please explain.

- Would the Proposed to Amend CAT to add information on buy to cover and bona fide market making require an additional field or fields to CAT? If so, what would the estimated cost be to add said fields?

- Would Proposed Rule 205 and Proposal to Amend CAT to include buy-to-cover information be less costly than the “open/close” indicator that was not

included the CAT NMS Plan? Please explain.

- Would the Reporting Thresholds impose a significant burden on Managers who do not meet the threshold but must track their positions to know if they at some point exceed the threshold? Please explain.

- Would the compliance costs associated with the Proposals vary by the various type of Manager? Would the costs of the XML requirement vary by the type of Manager likely to file Proposed Form SHO? If so, please explain which Managers would incur higher or lower costs.

- Do Managers other than registered investment advisers and option market makers hold large short positions such that they would exceed the Reporting Thresholds in Proposed Rule 13f-2? If so, which types of Managers are likely to hold such short positions? Would the effects of including such Managers in Proposed Rule 13f-2 be any different than those described herein? Please explain.

- Q41: *Other Economic Effects.*

- Has the Commission appropriately evaluated the potential impact of the Proposals on corporate managerial decision making? Why or why not?

- Would the Proposals result in less securities lending and potentially lower returns for investors in mutual funds, pension plans, and other securities lenders?

- Please discuss whether and how the adoption of the Proposals would impact securities lending market.

- Are there any economic effects not discussed in the Economic Analysis? If so, please describe them.

- Q42: *Potential Circumvention.*

- Has the Commission accurately characterized economic short disclosure in equity versus in derivatives markets? Why or why not?

- Would market participants circumvent reporting requirements by trading derivatives? Why or why not?

- How costly would it be to include reporting regarding securities other than equities, such as options and security based swaps, in Proposed Form SHO?

- What additional benefit would there be to requiring reporting in Proposed Form SHO of short positions arising from securities other than equities, such as options and security based swaps, in Proposed Form SHO?

- Q43: *Efficiency, Competition, and Capital Formation.*

- Has the Commission appropriately evaluated the potential impact of the Proposals on efficiency, competition, and capital formation? Please explain.

- Would the Proposed Rules have any effect on efficiency other than the potential effects on price efficiency?

- Would Proposed Rule 13f-2 and Proposed Form SHO alter the competitive landscape in the market to attract investor flows by disadvantaging Managers who sell short relative to Managers who do not sell short? Please explain.

- Would the overall effect on price efficiency of the Proposed Rules be significant enough to affect capital formation? Please explain. Would additional information on short selling help corporate managers make better investment decisions, thereby improving capital formation? Please explain. Would the Proposed Rules reduce capital formation by discouraging investment in convertible securities by raising the cost to hedge? Please explain. Would the Proposed Rules promote capital formation through enhanced investor confidence? Please explain.

- Q44: *Alternatives, Generally.*

- Are the Commission's descriptions and analyses of potential alternatives to the Proposed Rules accurate? Why or why not? Are there any other alternatives? If so, please describe the alternative(s) including how the benefits and costs of the alternative(s) compare to the benefits and costs of the Proposed Rules.

- Q45: *Alternative Approaches.*

- Has the Commission appropriately evaluated the alternative whereby short selling information would be collected using CAT, including bona fide market making and buy to cover information, then aggregated and published? Why or why not? Would this alternative raise any security issues associated with CAT, either in the collection of such new information or in the publication of aggregated CAT data? Please explain.

- Has the Commission appropriately evaluated the alternative whereby the bi-monthly short interest collected by FINRA would be codified, FINRA would be required to publish a version of its short interest information that specifically identifies the aggregate short interest of Managers, and/or non-FINRA Managers would be required to report to FINRA? Why or why not?

- Has the Commission appropriately evaluated the alternative whereby broker-dealers would file Proposed Form SHO reports with the Commission on behalf of Managers? Why or why not?

- Has the Commission appropriately evaluated the alternative whereby Proposed Rule 13f-2 and Proposed Form SHO would be explicitly crafted to be consistent with European disclosure requirements, including reporting thresholds? Why or why not?

- **Q46: Data Modification Alternatives.**

- Has the Commission appropriately evaluated the alternative whereby the information included in Proposed Form SHO would be released in a different manner, including releasing Proposed Form SHO reports exactly as they are filed, identifying the Managers, releasing Proposed Form SHO as filed but stripped of Manager identities, releasing the number of entities whose Proposed Form SHO reports were filed, aggregating at the issuer level as opposed to the security level, releasing aggregations of the various categories of changes in short positions, and/or releasing the daily aggregate increases in short positions separately from the daily aggregate decreases in short positions? Why or why not?

- Has the Commission appropriately evaluated the alternative whereby Managers who report Proposed Form SHO would also be required to disclose their derivatives positions on underlying equity securities? Why or why not?

- Has the Commission appropriately evaluated the alternative whereby Managers would report net short positions instead of gross short positions, taking into account any hedging that the Manager engages in, and/or the delta value of their hedged positions? Why or why not?

- Has the Commission appropriately evaluated the alternative whereby Managers would report data sources on Proposed Form SHO? Why or why not?

- **Q47: Threshold Modifications.**

- Has the Commission appropriately evaluated the alternative whereby the Reporting Thresholds would be modified compared to Thresholds A and B in Proposed Rule 13f-2, including a higher or lower or no threshold, a threshold based on short position as a percent of shares outstanding or dollar value of the short positions, including the nominal economic value of short derivative positions, a threshold based on activity, and/or measuring the threshold as of the last settlement day of the month? Why or why not?

- Would decreasing the threshold to include more Managers improve the quality of the data provided? Would increasing or decreasing the threshold increase the risk of copycat trading strategies? Would increasing or decreasing the threshold to include more Managers' positions in the aggregated reports reduce the risk of identifying individual investment Managers? Please explain.

- Would including the nominal economic value of short derivative positions as a consideration for the

threshold increase, decrease or have no impact on the risk copycat trading? Please explain. Including the nominal economic value of short derivative positions as a consideration for the threshold may require some Managers to report short positions that are part of hedges of large long positions. Would this information be beneficial? Please explain.

- Has the Commission appropriately evaluated the alternative of including a threshold based on short selling activity? If not, please describe the costs or benefits of this alternative relative to the proposal. Would a short selling activity threshold provide additional beneficial information? Please explain. Would a short selling activity threshold be more burdensome on Managers? Please explain. If the Commission were to adopt a threshold based on short selling activity, what should the level of the threshold be?

- Has the Commission appropriately evaluated the alternative of calculating the threshold based on positions on the last day of the month? If not, please describe the costs or benefits of this alternative relative to the proposal. Would such a threshold provide data that is as beneficial as the current proposal? Would calculating the threshold based on the last day of month lead to Managers strategically lowering their short positions to avoid reporting? Please explain.

- Has the Commission appropriately evaluated the alternative of using the two prong threshold for short positions in an equity security of a non-reporting company issuer? If not, please describe the cost or benefits of this alternative relative to the proposal. Is reliable shares outstanding information available for non-reporting issuers? Please explain.

- **Q48: Other Alternatives.**

- Has the Commission appropriately evaluated the alternative whereby reporting would be required at a different frequency, a different reporting window, and/or releasing aggregated data at a different horizon than in Proposed Rule 13f-2? Why or why not?

- Has the Commission appropriately evaluated the alternative whereby Regulation SHO would be modified, including requiring broker-dealers to collect information from customers concerning whether a given buy trade is a buy to cover trade when considering positions held at other broker-dealers, and/or requiring broker-dealers to aggregate all accounts at the same broker-dealer when determining buy to cover status of an order? Why or why not?

- How costly it would be to have Managers who use prime brokers inform their introducing brokers when buying-to-cover?

- Has the Commission appropriately evaluated the alternative whereby Proposed Form SHO information would be submitted in Inline XBRL? Why or why not?

## IX. Regulatory Flexibility Act Certification

The Regulatory Flexibility Act ("RFA")<sup>381</sup> requires federal agencies, in promulgating rules, to consider the impact of those rules on small businesses. Section 603(a) of the Administrative Procedure Act, as amended by the RFA, generally requires the Commission to undertake a regulatory flexibility analysis of all proposed rules, or proposed rule amendments, to determine the impact of such rulemaking on "small businesses" unless the Commission certifies that the rule, if adopted, would not have a significant economic impact on a substantial number of "small entities."

*Certification for Proposed Rule 13f-2 and New Proposed Form SHO.* Although Section 601(b) of the RFA defines the term "small business," the statute permits agencies to formulate their own definitions. The explanation of the term "small entities" and the definition of the term "small business" in Rule 0-10<sup>382</sup> of the Exchange Act do not explicitly reference Managers. Rule 0-10 does provide, however, that the Commission may "otherwise define" small entities for purposes of a particular rulemaking proceeding. For purposes of Proposed Rule 13f-2 and related Proposed Form SHO, therefore, the Commission has determined that the definition of the term "small business" found in Rule 0-7(a)<sup>383</sup> under the Investment Advisers Act of 1940<sup>384</sup> is more appropriate to the functions of institutional managers such as the Managers with reporting obligations under Proposed Rule 13f-2. The Commission believes that the proposed definition would help ensure that all persons or entities that might be Managers subject to reporting requirements under Proposed Rule 13f-2 will be included within a category addressed by the Rule 0-7(a) definition. Therefore, for purposes of this rulemaking and the RFA, a Manager is a small entity if it: (i) Has assets under management having a total value of less than \$25 million; (ii) did not have total

<sup>381</sup> 5 U.S.C. 601 *et seq.*

<sup>382</sup> 17 CFR 240.0-10 ("Rule 0-10").

<sup>383</sup> 17 CFR 275.0-7(a) ("Rule 0-7(a)").

<sup>384</sup> 15 U.S.C. 80b-1 *et seq.*



assets of \$5 million or more on the last day of its most recent fiscal year; and (iii) does not control, is not controlled by, and is not under common control with another investment adviser that has assets under management of \$25 million or more, or any person (other than a natural person) that had total assets of \$5 million or more on the last day of its most recent fiscal year.<sup>385</sup> The Commission requests comments on the use of this definition from Rule 0–7(a) under the Investment Advisers Act of 1940.

Under Proposed Rule 13f–2, Managers are not required to report on Proposed Form SHO unless they meet or exceed a specified Reporting Threshold. Managers with short interest positions in equity securities of a reporting company issuer would be subject to a two-pronged short reporting threshold structure—a short position in an equity security with a U.S. dollar value of \$10M or more, or a monthly average short position as a percentage of shares outstanding of the equity security of at least 2.5% (Threshold A). Managers with short interest positions in equity securities of a non-reporting company issuer would be subject to a single-pronged short reporting threshold structure—a short position in an equity security with a U.S. dollar value of \$500,000 or more at the close of regular trading hours on any settlement date during the calendar month (Threshold B). While the parameters of the Reporting Thresholds under Proposed Rule 13f–2 relate to the number and dollar value of shares of short positions, rather than assets under management, the Commission nevertheless believes that application of the Reporting Thresholds would result in Proposed Rule 13f–2 not applying to a significant number of “small businesses” as defined under Rule 0–7(a).

With respect to the first prong of Threshold A, the \$10M trigger would represent forty (40) percent of the assets of an entity that qualifies as a “small entity” under Rule 0–7(a). The Commission believes it is also unlikely that a significant number of small entities would place 40% of their respective assets under management in a short position in a single security. Further, many types of institutional investment managers that could be

small entities, including bank trustees, endowments, and foundations, are subject to fiduciary standards that prohibit them from investing in large, concentrated short positions. Such restrictions would deter small entities (with less than \$25M of assets under management) from investing over \$10M (greater than 40%) of their assets in a single short position, and therefore prevent them from triggering the first prong of Threshold A.<sup>386</sup>

With respect to the second prong of Threshold A, smaller Managers (those with under \$25M in assets under management) would likely try to leverage their assets through a combination of traditional short sales and derivative and similar transactions that create economically short exposure to a security. Such entities therefore, would likely engage in strategies that do not lend themselves to a clear determination that the second prong of Threshold A under Proposed Rule 13f–2 has been met.<sup>387</sup> Further, the Commission estimates, based on an analysis of U.S. common stocks,<sup>388</sup> that Managers that qualify as small entities under Rule 0–7(a) would not meet the 2.5% reporting threshold for securities representing over ninety-eight percent (98%) of the overall market value.<sup>389</sup>

When it comes to meeting the dollar value limits of Threshold B and the first prong of Threshold A, it is important to note that for the subset of Managers that engage in the most short selling activity, hedge funds,<sup>390</sup> less than twenty-five (25) percent have less than \$50M in

<sup>386</sup> See Molk and Partnoy, *supra* note 187 (describing impediments that have kept different types of institutional investment managers from engaging in short selling).

<sup>387</sup> *Id.* at 839 (positing that “institutions incorporate short selling into their strategies, not necessarily by taking net-short positions, but instead by combining leveraged long equity index positions with smaller actively managed short portfolios.”).

<sup>388</sup> A small entity, with less than \$25M in assets under management, would not be able to hold a short position of at least 2.5% in a company with a market capitalization above \$1B. Such companies represent over 98.5% of the overall market cap of U.S. equities. See also Stock Market Size Categories (2021), available at <https://stockmarketmba.com/sizecategories.php> (calculating approximately three percent (3%) of the U.S. stock market consists of common stocks of companies with less than \$2B in market capitalization (*i.e.*, small-cap and micro-cap stocks) and noting that micro-cap companies are generally too small for even most large institutional investment managers to invest in).

<sup>389</sup> An analysis by Commission of the daily dataset of the Center for Research in Security Prices (“CRSP”) showed that for the month of October 2021, on average, the number of companies with less than \$1B in market capitalization (2,293) constituted 1.51% of the overall market capitalization.

<sup>390</sup> See Molk and Partnoy, *supra* note 187, at 846.

assets under management.<sup>391</sup> Indeed, research shows that most hedge funds have assets under management above the amount that would qualify them as small entities under Rule 0–7(a), *i.e.*, above \$25M.<sup>392</sup>

For these reasons, the Commission certifies that Proposed Rule 13f–2 would not have a significant economic impact on a substantial number of small entities, as defined under Rule 0–10, for purposes of the RFA. The Commission requests written comments regarding this certification. The Commission requests that commenters describe the nature of any impact on small businesses and provide empirical data to support the extent of the impact.

*Certification for Proposed Rule 205.* As discussed in the PRA section above, the Commission believes that all broker-dealers whose accounts or whose customers’ accounts could hold a gross short position are potentially in scope for the requirements of Proposed Rule 205.<sup>393</sup> A broker-dealer is a small entity if it has total net capitalization (net worth plus subordinated liabilities) of less than \$500,000 on the date in the prior fiscal year as of which its audited financial statements were prepared pursuant to § 240.17a–5(d), and it is not affiliated with any person (other than a natural person) that is not a small business or small organization.<sup>394</sup>

Based on a review of data relating to the broker-dealers potentially in scope for Proposed Rule 205, the Commission does not believe that any of those broker-dealers would qualify as small entities under the above definition because they either exceed \$500,000 in total capital or are affiliated with a person that is not a small entity as defined in Rule 0–10. It is possible that in the future a small entity may come within the scope of Proposed Rule 205. Based on experience with broker-dealers that engage in short selling, however, the Commission believes that this scenario will be unlikely because firms that enter that market are likely to exceed \$500,000 in total capital or be

<sup>391</sup> See David Goldin, *Elephant in the room? Size and hedge fund performance*, Aurum (June 28, 2019), available at <https://www.aurum.com/insight/elephant-in-the-room-size-and-hedge-fund-performance/>.

<sup>392</sup> See Daniel Barth et al., *The Hedge Fund Industry is Bigger (and Has Performed Better) Than You Think* (Office of Fin. Research, Working Paper No. 20–01, Feb. 25, 2020, Revised Mar. 8, 2021).

<sup>393</sup> See *supra* Part VII.C.2. While recognizing that not all broker-dealers will necessarily enter purchase orders in securities in a manner that will subject them to the marking requirements of Proposed Rule 205, the Commission estimates, for purposes of the PRA, that all of the 3,551 broker-dealers registered with the Commission as of December 31, 2020, will do so.

<sup>394</sup> Exchange Act Rule 0–10(c).

<sup>385</sup> Rule 0–7(a), *supra* note 384. See generally *Reporting Threshold for Institutional Investment Managers*, Exchange Act Release No. 89290 (July 10, 2020), 85 FR 46016, 46031 n.90 (July 31, 2020) (stating that “[r]ecognizing the growth in assets under management at investment advisers since Rule 0–7(a) was adopted, the Commission plans to revisit the definition of a small entity in Rule 0–7(a).”).

affiliated with a person that is not a small entity.

For the foregoing reasons, the Commission certifies that Proposed Rule 205 would not have a significant economic impact on a substantial number of small entities for purposes of the RFA. The Commission encourages written comments regarding this certification, and requests that commenters describe the nature of any impact on small entities and provide empirical data to illustrate the extent of the impact.

*Certification for the Proposal to Amend CAT.* The proposed amendments to the CAT NMS Plan would impose requirements on the CAT NMS Plan Participants (the national securities exchanges registered with the Commission under Section 6 of the Exchange Act and FINRA), broker-dealers which are in scope for the requirements of Proposed Rule 205 and have the obligation to report order receipt and origination reports to the CAT, and broker-dealers that effect short sales utilizing the bona-fide market making exception pursuant to Rule 203(b)(2)(iii) of Regulation SHO and report to the CAT.

With respect to the national securities exchanges, the Commission's definition of a small entity is an exchange that has been exempt from the reporting requirements of Rule 601 of Regulation NMS, and is not affiliated with any person (other than a natural person) that is not a small business or small organization.<sup>395</sup> None of the national securities exchanges registered under Section 6 of the Exchange Act that would be subject to the proposed amendments are "small entities" for purposes of the RFA. In addition, FINRA is not a "small entity."<sup>396</sup> With respect to broker-dealers which are in scope for the requirements of Proposed Rule 205 and have CAT reporting obligations, as discussed above, the Commission does not believe that any of those broker-dealers would qualify as small entities pursuant to Exchange Act Rule 0-10(c).<sup>397</sup> Similarly, based on Commission knowledge and experience with broker-dealers that identify as market makers, the Commission does not believe that any broker-dealer that effects short sales utilizing the bona-fide

market making exception pursuant to Rule 203(b)(2)(iii) of Regulation SHO and reports to the CAT would qualify as a small entity pursuant to Exchange Act Rule 0-10(c), because they either exceed \$500,000 in total capital or are affiliated with a person that is not a small entity as defined in Rule 0-10. The Commission believes that it is possible, but unlikely, that in the future a small entity may come within scope of the Proposal to Amend CAT, because firms that enter either market are likely to exceed \$500,000 in total capital or be affiliated with a person that is not a small entity.

For the foregoing reasons, the Commission certifies that the Proposal to Amend CAT would not have a significant economic impact on a substantial number of small entities for purposes of the RFA. The Commission encourages written comments regarding this certification, and requests that commenters describe the nature of any impact on small entities and provide empirical data to illustrate the extent of the impact.

#### **X. Consideration of Impact on the Economy**

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, the Commission is also requesting information regarding the potential impact of Proposed Rule 13f-2, Proposed Rule 205, and the Proposal to Amend CAT on the economy on an annual basis. In particular, comments should address whether the proposals, if adopted, would have a \$100,000,000 annual effect on the economy, cause a major increase in costs or prices, or have a significant adverse effect on competition, investment, or innovations. Commenters are requested to provide empirical data and other factual support for their views to the extent possible.

#### **Statutory Authority and Text of Proposed Rules 13f-2 and 205, and Form SHO**

##### **List of Subjects**

*17 CFR Parts 240 and 249*

Reporting and recordkeeping requirements, Securities.

*17 CFR Part 242*

Brokers, Reporting and recordkeeping requirements, securities.

##### **Text of Proposed Rule Amendments**

In accordance with the foregoing, the Commission is proposing to amend title 17, chapter II of the Code of the Federal Regulations as follows.

#### **PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934**

■ 1. The general authority citation for part 240 continues to read as follows, and the sectional authority for § 240.13f-2(T) is removed.

**Authority:** 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z-2, 77z-3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78c-3, 78c-5, 78d, 78e, 78f, 78g, 78i, 78j, 78j-1, 78k, 78k-1, 78l, 78m, 78n, 78n-1, 78o, 78o-4, 78o-10, 78p, 78q, 78q-1, 78s, 78u-5, 78w, 78x, 78dd, 78ll, 78mm, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4, 80b-11, and 7201 *et seq.*, and 8302; 7 U.S.C. 2(c)(2)(E); 12 U.S.C. 5221(e)(3); 18 U.S.C. 1350; Pub. L. 111-203, 939A, 124 Stat. 1376 (2010); and Pub. L. 112-106, sec. 503 and 602, 126 Stat. 326 (2012), unless otherwise noted.

■ 2. Add § 240.13f-2 to read as follows:

#### **§ 240.13f-2 Reporting by institutional investment managers regarding gross short position and activity information.**

(a) An institutional investment manager shall file a report on Form SHO (cite to be added), in accordance with the form's instructions, with the Commission within 14 calendar days after the end of each calendar month with regard to:

(1) Each equity security of an issuer that is registered pursuant to Section 12 of the Exchange Act or for which the issuer is required to file reports pursuant to Section 15(d) of the Exchange Act over which 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 collectively have either:

(i) A gross short position in the equity security with a U.S. dollar value of \$10 million 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% or more; and

(2) Each equity security of an issuer that is not registered pursuant to Section 12 of the Exchange Act or for which the issuer is not required to file reports pursuant to Section 15(d) of the Exchange Act over which 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 collectively have a gross short position in the equity security with a U.S. dollar value of \$500,000 or more at the close of regular trading hours on any

<sup>395</sup> See 17 CFR 240.0-10(e) (stating that a broker-dealer is a small entity if it has total net capitalization (net worth plus subordinated liabilities) of less than \$500,000 on the date in the prior fiscal year as of which its audited financial statements were prepared pursuant to 17 CFR 240.17a-5(d), and it is not affiliated with any person (other than a natural person) that is not a small business or small organization).

<sup>396</sup> See 13 CFR 121.201.

<sup>397</sup> See *supra* note 395, and accompanying text.

settlement date during the calendar month.

(3) Form SHO and any amendments thereto must be filed with the Commission via the Commission's Electronic Data Gathering, Analysis, and Retrieval system ("EDGAR"), in accordance with Regulation S-T. Certain information regarding each equity security reported by institutional investment managers on Form SHO and filed with the Commission via EDGAR will be published by the Commission, on an aggregated basis.

(b) For the purposes of this rule:

(1) The term "institutional investment manager" has the same meaning as in Section 13(f)(6)(A) of the Exchange Act.

(2) The term "equity security" has the same meaning as in Section 3(a)(11) of the Exchange Act and Rule 3a11-1 thereunder.

(3) The term "investment discretion" has the same meaning as in Rule 13f-1(b) under the Exchange Act.

(4) The term "gross short position" means the number of shares of the equity security that are held short, without inclusion of any offsetting economic positions, including shares of the equity security or derivatives of such equity security.

(5) The term "regular trading hours" has the same meaning as in Rule 600(b)(77) under the Exchange Act.

#### **PART 242—REGULATIONS M, SHO, ATS, AC, NMS AND SBSR AND CUSTOMER MARGIN REQUIREMENTS FOR SECURITY FUTURES**

■ 3. The authority citation for part 242 continues to read in part as follows:

**Authority:** 15 U.S.C. 77g, 77q(a), 77s(a), 78b, 78c, 78g(c)(2), 78i(a), 78j, 78k-1(c), 78l, 78m, 78n, 78o(b), 78o(c), 78o(g), 78q(a), 78q(b), 78q(h), 78w(a), 78dd-1, 78mm, 80a-23, 80a-29, and 80a-37.

■ 4. Add § 242.205 to read as follows:

#### **§ 242.205 Purchase Order Marking for Data Collection Purposes.**

(a) A broker-dealer must mark an order to purchase an equity security for an account as "buy to cover" if the person purchasing the equity security has any gross short position in the equity security in the same account. The "buy to cover" mark applies to purchases made by the broker-dealer for its own account, or to purchases made by the broker-dealer on behalf of another person through the person's account held at that broker-dealer.

(b) Reserved

#### **PART 249—FORMS, SECURITIES EXCHANGE ACT OF 1934**

■ 5. The general authority citation for part 249 continues to read as follows:

**Authority:** 15 U.S.C. 78a *et seq.* and 7201 *et seq.*; 12 U.S.C. 5461 *et seq.*; 18 U.S.C. 1350; Sec. 953(b), Pub. L. 111-203, 124 Stat. 1904; Sec. 102(a)(3), Pub. L. 112-106, 126 Stat. 309 (2012), Sec. 107, Pub. L. 112-106, 126 Stat. 313 (2012), Sec. 72001, Pub. L. 114-94, 129 Stat. 1312 (2015), and secs. 2 and 3 Pub. L. 116-222, 134 Stat. 1063 (2020), unless otherwise noted.

■ 6. Add § 249.333 to read as follows:

#### **§ 249.333 Form SHO, report of institutional investment managers pursuant to Section 13(f)(2) of the Securities Exchange Act of 1934.**

This form shall be used by institutional investment managers that are required to furnish reports pursuant to Section 13(f)(2) of the Securities Exchange Act of 1934. (15 U.S.C. 78m(f)(2) and Rule 13f-2 thereunder (§ 240.13f-2 of this chapter)).

**Note:** The text of Form SHO will not appear in the Code of Federal Regulations.

OMB Number: XXXX-XXXX

#### **Form SHO**

#### **Information Required of Institutional Investment Managers Pursuant to Section 13(f)(2) of the Securities Exchange Act of 1934 and Rules Thereunder**

##### *General Instructions*

*Rule as to Use of Form SHO.* Institutional investment managers ("Managers") must use Form SHO for reports to the Commission required by Rule 13f-2 [17 CFR 240.13f-2] promulgated under Section 13(f)(2) of the Securities Exchange Act of 1934 [15 U.S.C. 78m(f)(2)] ("Exchange Act"). A Manager shall file a report on Form SHO in accordance with these instructions, with the Commission within 14 calendar days after the end of each calendar month with regard to: (1) Each equity security of an issuer that is registered pursuant to Section 12 of the Exchange Act or for which the issuer is required to file reports pursuant to Section 15(d) of the Exchange Act over which the Manager and all accounts over which the Manager (or any person under the Manager's control) has investment discretion collectively have either (A) a gross short position in the equity security with a U.S. dollar value of \$10 million or more at the close of regular trading hours on any settlement date during the calendar month, or (B) a monthly average gross short position as a percentage of shares outstanding in the equity security of 2.5% or more; and

(2) each equity security of an issuer that is not registered pursuant to Section 12 of the Exchange Act or for which the issuer is not required to file reports pursuant to Section 15(d) of the Exchange Act over which the Manager and all accounts over which the Manager (or any person under the Manager's control) has investment discretion collectively have a gross short position in the equity security with a U.S. dollar value of \$500,000 or more at the close of regular trading hours on any settlement date during the calendar month. For purposes of Rule 13f-2 and Form SHO, "regular trading hours" shall have the meaning ascribed in Rule 600(b)(77) under the Exchange Act [17 CFR 242.600(b)(77)].

A Manager that determines that it has filed a Form SHO with errors that affect the accuracy of the short sale data reported must file an amended and restated Form SHO within ten (10) calendar days of discovering the error.

*Rules to Prevent Duplicative Reporting.* If two or more Managers, each of which is required by Rule 13f-2 to file Form SHO for the reporting period, exercise investment discretion with respect to the same securities, only one such Manager must report the information in its report on Form SHO. If a Manager has information that is required to be reported on Form SHO and such information is reported by another Manager (or Managers), such Manager must identify the Manager(s) reporting on its behalf in the manner described in Special Instruction 5.

*Filing of Form SHO.* A reporting Manager must file Form SHO with the Commission via the Commission's Electronic Data Gathering, Analysis, and Retrieval system ("EDGAR"), in accordance with Regulation S-T. The Commission plans to publish certain data from the filings on an aggregated basis.

All information that would reveal the identity of a Manager filing a Form SHO report with the Commission, or the identity of any Other Manager listed on the Cover Page of a Form SHO report, is deemed subject to a confidential treatment request under 17 CFR 240.24b-2. The Commission plans to publish only aggregated data derived from information provided in Form SHO reports.

Technical filing errors may cause delays in the filing of Form SHO. Technical support for making Form SHO reports is available through EDGAR Filer Support. Support for questions regarding non-technical issues related to Form SHO reporting is available through the Office of Interpretation and Guidance of the

Division of Trading and Markets (“TM OIG”) at [TradingAndMarkets@sec.gov](mailto:TradingAndMarkets@sec.gov).

#### *Instructions for Calculating Reporting Threshold*

A Manager shall file a report on Form SHO:

- With regard to each equity security of an issuer that is registered pursuant to section 12 of the Exchange Act or for which the issuer is required to file reports pursuant to section 15(d) of the Exchange Act (a “reporting company issuer”) in which the Manager meets or exceeds under either of the following circumstances: (1) The Manager, and all accounts over which the Manager, or any person under the Manager’s control, has investment discretion, collectively have a gross short position in the equity security with a U.S. dollar value of \$10 million or more at the close of regular trading hours on any settlement date during the calendar month; or (2) the Manager, and all accounts over which the Manager, or any person under the Manager’s control, has investment discretion, collectively have a monthly average gross short position as a percentage of shares outstanding in the equity security of 2.5% or more (“Threshold A”).

- With regard to any equity security of an issuer that is not a reporting company issuer as described above (a “non-reporting company issuer”) in which the Manager meets or exceeds a gross short position in the equity security with a U.S. dollar value of \$500,000 or more at the close of regular trading hours on any settlement date during the calendar month (“Threshold B”).

With respect to each equity security to which the circumstances described in Threshold A or Threshold B applies, the Manager shall report the information, as described in the “Special Instructions” below, aggregated across accounts over which the Manager, or any person under the Manager’s control, has investment discretion.

To determine whether the dollar value threshold described in (1) of Threshold A above is met, a Manager shall determine its end of day gross short position 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.

To determine whether the dollar value threshold described in Threshold B above is met, a Manager shall 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. If such closing price is not available, a Manager shall use the price at which it last purchased or sold any share of that security.

To determine whether the percentage threshold described in (2) of Threshold A above is met, the Manager shall (a) identify its gross short position (as defined in Rule 13f–2) in the equity security at the close of each settlement date during the calendar month of the reporting period, and divide that figure by the number of shares outstanding in such security at the close of that settlement date, and (b) add up the daily percentages during the calendar month as determined in (a) and divide that total by the number of settlement dates during the calendar month of the reporting period. The number of shares outstanding of the security for which information is being reported shall be determined by reference to an issuer’s most recent annual or quarterly report, and any subsequent update thereto, filed with the Commission.

#### *Special Instructions*

1. This form consists of two parts: The Cover Page, and the Information Tables.

#### *Cover Page*

2. The period end date used in the report (and in the EDGAR submission header) is the last settlement day of the calendar month. The date shall name the month, and express the day and year in Arabic numerals, with the year being a four-digit numeral (e.g., 2022).

3. Amendments to Form SHO must restate the Form SHO in its entirety. If the Manager is filing the Form SHO report as an amendment, then the Manager must check the “Amendment and Restatement” box on the Cover Page; and enter the amendment number. Each Amendment and Restatement must include a complete Cover Page and Information Tables. Amendments must be filed sequentially.

a. In the space designated on the Cover of Page of each Amendment and Restatement, a Manager shall (1) provide a written description of the revision being made; (2) explain the reason for the revision; and (3) indicate whether data from any additional Form SHO reporting period(s) (up to the past 12 calendar months) is/are affected by the Amendment and Restatement. If (3) applies, a Manager shall complete and file a separate Amendment and Restatement for each previous calendar month so affected (up to the past 12 months) and provide a description of the revision being made and explain the reason for the revision.

b. If the data being reported in an Amendment and Restatement affects the data reported on the Form SHO reports filed in at least three of the immediately preceding Form SHO reporting periods, the Manager, within two (2) business days after filing the Amendment and Restatement, must provide the Commission staff, via TM OIG at [TradingAndMarkets@sec.gov](mailto:TradingAndMarkets@sec.gov), with notice of (1) this circumstance; and (2) an explanation of the reason for the revision.

c. If a revision reported in an Amendment and Restatement changes a data point reported in the Form SHO being amended by twenty-five percent (25%) or more, the Manager must notify the Commission staff via TM OIG at [TradingAndMarkets@sec.gov](mailto:TradingAndMarkets@sec.gov) within two (2) business days after filing the Amendment and Restatement.

4. The Cover Page shall include only the required information. Do not include any portions of the Information Tables on the Cover Page.

5. Designate the Report Type for the Form SHO by checking the appropriate box in the Report Type section of the Cover Page, and include, where applicable, the Name and active Legal Entity Identifier (“LEI”) (if available) of each of the Other Managers Reporting for this Manager on the Cover Page, and the Information Tables, as follows:

a. If all of the information that a Manager is required by Rule 13f–2 to report on Form SHO is reported by another Manager (or Managers), check the box for Report Type “FORM SHO NOTICE,” include on the Cover Page the Name and active LEI (if available) of each of the Other Managers Reporting for this Manager, and omit the Information Tables.

b. If all of the information that a Manager is required by Rule 13f–2 to report on Form SHO is reported in this report, check the box for Report Type “FORM SHO ENTRIES REPORT,” omit the “Name and Active LEI (if available) of each of the Other Managers Reporting for this Manager” section of the Cover Page, and include the Information Tables.

c. If only a part of the information that a Manager is required by Rule 13f–2 to report on Form SHO is reported in this report, check the box for Report Type “FORM SHO COMBINATION REPORT,” include on the Cover Page the name and active LEI (if available) of each of the Other Managers Reporting for this Manager, and include the Information Tables.

#### *Information Tables*

6. Do not include any additional information in the Information Tables.

Do not include any portions of the Information Tables on the Cover Page.

7. In reporting information required on Information Tables 1 and 2, Managers must account for and report a gross short position in an ETF, and activity that results in the acquisition or sale of shares of the ETF resulting from call options exercises or assignments; put options exercises or assignments; tendered conversions; secondary offering transactions; or other activity, as discussed further below. In determining its gross short position in an equity security, however, a Manager is not required to consider short positions that the ETF holds in individual underlying equity securities that are part of the ETF basket.

8. *Instructions for Information Table 1—Manager’s Gross Short Position Information:*

a. Column 1. Settlement Date. Enter in Column 1 the last day of the calendar month of the reporting period on which a trade settles (“settlement date”).

b. Column 2. Issuer Name. Enter in Column 2 the name of the issuer of the security for which information is being reported. Reasonable abbreviations are permitted.

c. Column 3. Issuer LEI. If the issuer has an LEI, enter the issuer’s active LEI in Column 3.

d. Column 4. Title of Class. Enter in Column 4 the title of the class of the security for which information is being reported. Reasonable abbreviations are permitted.

e. Column 5. CUSIP Number. Enter in Column 5 the nine (9) digit CUSIP number of the security for which information is being reported, if applicable.

f. Column 6. FIGI. Enter in Column 6 the twelve (12) character, alphanumeric Financial Instrument Global Identifier (“FIGI”) of the security for which information is being reported, if a FIGI has been assigned.

g. Column 7. End of Month Gross Short Position (Number of Shares). Enter in Column 7 the number of shares that represent the Manager’s gross short position in the security for which information is being reported at the close of regular trading hours on the last settlement date of the calendar month of the reporting period. The term “gross short position” means the number of shares of the security for which

information is being reported that are held short, without inclusion of any offsetting economic positions—including shares of the reportable equity security or derivatives of such security.

h. Column 8. End of Month Gross Short Position (rounded to nearest USD). Enter in Column 8 the US dollar value of the shares reported in Column 7, rounded to the nearest dollar. A Manager shall report the corresponding dollar value of the reported gross short position by multiplying the number of shares of the security for which information is being reported by the closing price at the close of regular trading hours on the last settlement date of the calendar month. In circumstances where such closing price is not available, the Manager shall use the price at which it last purchased or sold any share of that security.

i. Column 9. Extent of Hedge for Short Position Identified in Column 7. Enter in Column 9 whether the identified position is fully hedged (“F”), partially hedged (“P”), or not hedged (“0”). A Manager shall indicate that a reported gross short position in an equity security is “fully hedged” if the Manager also holds an offsetting position that reduces the risk of price fluctuations for its entire position in that equity security, for example, through “delta” hedging (in which the Manager’s reported gross short position is offset 1-for-1), or similar hedging strategies. A Manager shall report that it is “partially hedged” if the Manager holds an offsetting position that is less than the identified price risk associated with the reported gross short position in that equity security.

9. *Instructions for Information Table 2—Daily Activity Affecting Manager’s Gross Short Position During the Reporting Period:*

a. Column 1. Settlement Date. Enter in Column 1 each date during the reporting period on which a trade settles (settlement date). The Manager shall report information for each settlement date during the calendar month reporting period as described in these instructions.

b. Column 2. Issuer Name. Enter in Column 2 the name of the issuer of the equity security for which information is being reported. Reasonable abbreviations are permitted.

c. Column 3. Issuer LEI. If the issuer has an LEI, enter the issuer’s active LEI in Column 3.

d. Column 4. Title of Class. Enter in Column 4 the title of the class of the security for which information is being reported. Reasonable abbreviations are permitted.

e. Column 5. CUSIP Number. Enter in Column 5 the nine (9) digit CUSIP number of the security for which information is being reported, if applicable.

f. Column 6. FIGI. Enter in Column 6 the twelve (12) character, alphanumeric FIGI of the security for which information is being reported, if a FIGI has been assigned.

g. Column 7. Number of Shares Sold Short. For the settlement date set forth in Column 1, enter the number of shares of the security for which information is being reported that resulted from short sales and settled on that date.

h. Column 8. Number of Shares Purchased to Cover an Existing Short Position. For the settlement date set forth in Column 1, enter the number of shares of the security for which information is being reported that were purchased to cover, in whole or in part, an existing short position and settled on that date.

i. Column 9. Number of Shares Purchased in Exercised Call Option Contracts. For the settlement date set forth in Column 1, enter the number of shares of the security for which information is being reported that are acquired in a call option exercise that reduces or closes a short position on that security and settled on that date.

j. Column 10. Number of Shares Sold in Exercised Put Option Contracts. For the settlement date set forth in Column 1, enter the number of shares of the security for which information is being reported that are sold in a put option exercise that creates or increases a short position on that security and settled on that date.

k. Column 11. Number of Shares Sold in Assigned Call Option Contracts. For the settlement date set forth in Column 1, enter the number of shares of the security for which information is being reported that are sold in a call option assignment that creates or increases a short position on that security and settled on that date.

l. Column 12. Number of Shares Purchased in Assigned Put Option Contracts. For the settlement date set forth in Column 1, enter the number of shares of the security for which information is being reported that are acquired in a put option assignment that reduces or closes a short position on that security and settled on that date.

m. Column 13. Number of Shares Resulting from Tendered Conversions. For the settlement date set forth in Column 1, enter the number of shares of the security for which information is being reported that are acquired as a result of the tendered conversions that reduces or closes a short position on that security and settled on that date.

n. Column 14. Number of Shares Obtained through Secondary Offering Transactions. For the settlement date set forth in Column 1, enter the number of shares of the security for which information is being reported that were obtained through a secondary offering transaction that reduces or closes a short position on that security and settled on that date.

o. Column 15. Other Activity that Creates or Increases a Manager’s Short Position. For the settlement date set forth in Column 1, enter the number of shares of the security for which information is being reported 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. Other activity to be reported includes, but is not limited to, shares resulting from ETF creation or redemption activity.

p. Column 16. Other Activity that Reduces or Closes a Manager’s Short Position. For the settlement date set forth in Column 1, enter the number of shares of the security for which information is being reported that resulted from other activity not previously reported on this form that reduces or closes a short position on that security and settled on that date. Other activity to be reported includes, but is not limited to, shares resulting from ETF creation or redemption activity.

**Paperwork Reduction Act Information**

Persons who are to respond to the collection of information contained in this form are not required to respond to the collection of information unless the form displays a currently valid Office of Management and Budget (“OMB”) control number.

OMB Number: XXXX–XXXX

**UNITED STATES  
SECURITIES AND EXCHANGE  
COMMISSION**

**Washington, DC 20549**

**FORM SHO**

**FORM SHO COVER PAGE**

Report for the Period Ended: [Month/Day/Year]

Check here if Amendment and Restatement ; Amendment Number: \_\_\_\_\_  
Description of the Amendment and Restatement, Reason for the Amendment and Restatement, and Which Additional Form SHO Reporting Period(s) (up to the past 12 calendar months), if any, is/are affected by the Amendment and Restatement: \_\_\_\_\_

Institutional Investment Manager (“Manager”) Filing Report:

Name: \_\_\_\_\_

Mailing Address: \_\_\_\_\_

Business Telephone and Facsimile Number: \_\_\_\_\_

Active Legal Entity Identifier (“LEI”): \_\_\_\_\_

Contact Employee:

Name and Title: \_\_\_\_\_

Telephone Number: \_\_\_\_\_

Facsimile Number: \_\_\_\_\_

Date Filed: \_\_\_\_\_

The Manager filing this report hereby represents that all information contained herein is true, correct and complete, and that it is understood that all required items, statements, schedules, lists, and tables, are considered integral parts of this form.

Report Type (Check only one):

[ ]FORM SHO ENTRIES REPORT. (Check here if all entries of this reporting Manager are reported in this report.)

[ ]FORM SHO NOTICE. (Check here if no entries reported are in this report, and all entries are reported by other reporting Manager(s).)

[ ]FORM SHO COMBINATION REPORT. (Check here if a portion of the entries for this reporting Manager is reported in this report and a portion is reported by other reporting Manager(s).)

Name and Active LEI of each of the Other Manager(s) Reporting for this Manager: [If there are no entries in this list, omit this section.]

Name: \_\_\_\_\_

Active LEI: \_\_\_\_\_

[Repeat as necessary.]

**INFORMATION TABLE 1—MANAGER’S GROSS SHORT POSITION INFORMATION**

Column 1	Column 2	Column 3	Column 4	Column 5	Column 6	Column 7	Column 8	Column 9
Settlement Date (Month End).	Issuer Name ....	Issuer LEI .....	Title of Class ...	CUSIP Number	FIGI .....	End of Month Gross Short Position (Number of Shares).	End of Month Gross Short Position (rounded to nearest USD).	Extent of Hedge for Position Identified in Column 7.

(Repeat as Necessary).

**INFORMATION TABLE 2—DAILY ACTIVITY AFFECTING MANAGER’S GROSS SHORT POSITION DURING THE REPORTING PERIOD**

Column 1	Column 2	Column 3	Column 4	Column 5	Column 6	Column 7	Column 8	Column 9	Column 10
Settlement Date.	Issuer Name	Issuer LEI ...	Title of Class.	CUSIP Number.	FIGI .....	Number of Shares Sold Short.	Number of Shares Purchased to Cover an Existing Short Position.	Number of Shares Purchased in Exercised Call Option Contracts.	Number of Shares Sold in Exercised Put Option Contracts.

Column 11	Column 12	Column 13	Column 14	Column 15	Column 16
Number of Shares Sold in Assigned Call Option Contracts.	Number of Shares Purchased in Assigned Put Option Contracts.	Number of Shares Resulting from Tendered Conversions.	Number of Shares Obtained Through Secondary Offering Transactions.	Other Activity that Creates or Increases Manager's Short Position.	Other Activity that Reduces or Closes Manager's Short Position.

(Repeat as Necessary).

Dated: February 25, 2022.

By the Commission.  
**Eduardo A. Aleman,**  
*Deputy Secretary.*  
[FR Doc. 2022-04670 Filed 3-15-22; 8:45 am]  
**BILLING CODE 8011-01-P**