[Risk Alert: Does Your Firm Have Large Trader Filing Obligations?]

January 14, 2021

The SEC recently published a risk alert detailing observations from investment advisors' and broker-dealers' examinations relating to Large Trader Obligations. The Large Trader Rule, or Rule 13h-1, was adopted by the SEC to identify and accumulate information related to market participants that surpassed specified trading thresholds on a daily or monthly basis. The trading thresholds are based on the aggregate transactions, shares, or fair market value, in national market system securities ("NMS securities"). The filing ultimately allows the SEC to oversee the impact of Large Trader activity on the securities markets, including analyzing the trading patterns surrounding large market events or periods of unusual market volatility.

The risk alert can be viewed here.

Who is considered a Large Trader?

Rule 13h-1(a)(1)(i) defines a "large trader" as any person that "directly or indirectly, including through other persons controlled by such person, exercises investment discretion over one or more accounts and effects transactions for the purchase or sale of any NMS security for or on behalf of such accounts, by or through one or more registered broker-dealer, in an aggregate amount equal to or greater than the identifying activity level."

In simpler terms, a person or an entity with discretionary authority that meets or exceeds the threshold of the trading activity level can trigger the requirement to file Form 13H. The Form 13H filing can also be filed voluntarily.

What is an NMS Security?

NMS Securities are generally US exchange-listed securities and standardized options. Exchange-listed debt securities, securities futures, or open-end mutual funds are generally excluded from the definition. For the complete definition, please refer to 17 CFR § 242.600.

What are the Identifying Activity Levels that Trigger the Filing Requirement?

Rule 13h-1(a)(7) defines the term "identifying activity level" as "aggregate transactions in NMS securities" that are equal to or greater than:

- During a calendar day, either 2 million shares or shares with a fair market value of $20 million (*aggregate); or
- During a calendar month, either 20 million shares or shares with a fair market value of $200 million (*aggregate).

* *"Under no circumstances shall a person subtract, offset, or net purchase and sale transactions, in equity securities or option contracts, and among or within accounts, when aggregating the volume or fair market value of transactions for calculation purposes."* – § 240.13h-l(c)(1)(iii)

When Must an Advisor File a Form 13H?

Once the identifying activity level has been triggered, the advisor must file the initial Form 13H filing promptly through the SEC's EDGAR system. For the initial filing, promptly is considered filing within ten days. After the initial filing, advisors are required to submit annual filings (Form 13H-A) within 45 days after the end of each full calendar year and amend the Form 13H (Form 13H-Q) promptly following the end of a calendar quarter whenever the information contained within the filing becomes inaccurate for any reason. For example, Form 13H includes a list of brokers-dealers that the advisor, or the advisor's affiliates, utilize for trading eligible securities. If this list of broker-dealers changes, Form 13H must be amended promptly in the quarter after the change has taken place. If Form 13H information becomes inaccurate during Q4, the Commission permits Large Traders to complete the annual filing and also designate it as an amendment filing, as long as the submission is made promptly after the 4^{th} quarter's end.

Once the initial filing has been accepted, the SEC will assign a unique identification number to each large trader called the Large Trader Identification Number ("LTID"). The LTID must be provided to all broker-dealers effecting transactions on behalf of the advisor.

Are Broker-Dealers Impacted by Rule 13h-1?

Possibly. Broker-dealers are subject to certain recordkeeping and reporting requirements. Broker-dealers must retain books and records related to the reportable trading under this Rule for themselves (if deemed a Large Trader) and for other Large Traders (identified or unidentified) who are effected, directly or indirectly, by or through the accounts carried by or controlled by the broker-dealer.

The Rule offers a safe harbor where broker-dealers will be deemed not to have known or have reason to know that a person is a large trader if the proper policies and procedures are in place. In order to comply with the safe harbor, the broker-dealer must establish policies and procedures that:

- identify persons who have not identified as a Large Trader under the Rule based on transactions effected through an account or group of accounts carried by such broker-dealer (i.e. Unidentified Large Trader);
- treat all persons or entities identified as an Unidentified Large Trader by assigning a unique identifying number to each in the LTID format; and
- Notify any person or entity identified as Unidentified Large Trader of the potential reporting obligations under the Rule.

Additional reporting requirements for broker-dealers will go into effect this year. The Commission issued two exemptive orders in April of last year, allowing for the phased reporting of data by broker-dealers into the Consolidated Audit Trail system ("CAT"). Starting on April 26, 2021, broker-dealers that are considered Large Industry Members[1] are required to report certain customer identifying information related to Large Traders into CAT. Broker-dealers that are considered Small Industry Members[2] are required to begin reporting the similar information into CAT by December 13, 2021. Broker-dealers will be required to obtain and report LTIDs into CAT for accounts with Reportable Events[3]. Given the new reporting requirements, broker-dealers are strongly encouraged to review their policies and procedures and their current population of LTIDs, and accounts with Reportable Events, to ensure preparedness for the applicable reporting deadline.

Staff Observations for Investment Advisors

Advisors should review their policies and procedures in consideration of the following:

- Identify situations that could trigger Large Trader filing requirements, including regularly scheduled model or portfolio rebalancing or a new discretionary relationship with anticipated large trading volumes in eligible securities;
- Timely filing of initial, annual and amendment filings, when applicable; and
- Notifying broker-dealers utilized by the advisor of the firm's Large Trader status including the LTID, if applicable.

Staff Observations for Broker-Dealers

Broker-dealers should review their supervisory and compliance policies and procedures in consideration of the following:

- The applicability of the Rule to the broker-dealer and its affiliates;
- Asking for the LTID at account opening and on a regular basis afterward;
- Reviewing their CAT reporting to include LTIDs where appropriate;
- Availability of safe harbor options; and
- Timely reporting of initial, annual, and amendment filings, when applicable.

Conclusion:

Advisors and broker-dealers should review their current policies and procedures to ensure the necessary controls are in place for compliance with Rule 13h-1. Advisors that have daily or monthly trading volumes near these levels should closely monitor the activity. The initial filing process can take time if the advisor has not already established an account with EDGAR. Even if an advisor has missed a filing deadline, submitting the filing as soon as discovered and documenting the efforts taken to remediate the oversight will show good faith to the SEC.

Please contact your Foreside Consultant if you need assistance with filing Form 13H or have questions related to the requirements of the filing. Foreside can assist you with determining your filing obligations and assist with the preparation and submission of the Form 13H filing.

For additional information, please see the Division of Trading and Markets' *Responses to Frequently Asked Questions Concerning Large Trader Reporting* by clicking here.

[1] "Large Industry Members" are Industry Members other than Small Industry Members.

[2] "Small Industry Members" means an Industry Member that qualifies as a small broker-dealer as defined in SEC Rule 613.

[3] "Reportable Event" includes, but is not limited to, the original receipt or origination, modification, cancellation, routing, execution (in whole or in part) and allocation of an order, and receipt of a routed order.