

Regulatory and Enforcement Alert

SEC Risk Alert Urges Investment Advisers and Broker-Dealers to Review Their Rule 13h-1 Compliance Programs

December 22, 2020

On December 16, 2020, the Office of Compliance Inspections and Examinations (“OCIE”)¹ of the U.S. Securities and Exchange Commission (“SEC”) published a Risk Alert (the “Risk Alert”)² discussing OCIE staff’s observations from its recent exams of SEC-registered investment advisers and broker-dealers for compliance with Rule 13h-1 under the Securities Exchange Act of 1934. Rule 13h-1 requires persons that transact in national market system (“NMS”) securities³ meeting certain daily or monthly thresholds (such persons are referred to as “Large Traders”⁴) to self-identify themselves to the SEC by filing a Form 13H and also imposes certain recordkeeping, reporting, and monitoring obligations on broker-dealers.

The Risk Alert explains that during recent exams OCIE staff observed that some investment advisers and broker-dealers either were not aware of Rule 13h-1 or were not familiar with certain of its requirements. OCIE staff further observed numerous instances of potential non-compliance with Rule 13h-1, including where Large Traders may not have self-identified with the SEC and/or may not have filed their annual Form 13H. OCIE staff observed that broker-dealers had potential compliance issues in the areas of recordkeeping, monitoring, and reporting.

The Risk Alert urges investment advisers and broker-dealers to thoroughly review and, where appropriate, amend and enhance their Rule 13h-1 compliance programs. These reviews should encompass practices, as well as written policies and procedures, including their implementation. Private fund advisers that are uncertain if the Large Trader obligations apply to them should contact counsel.

Key Takeaways

- **Investment advisers that transact in NMS securities should review their Rule 13h-1 compliance policies and procedures.** Each investment adviser should focus on: (i) identifying

¹ On December 17, 2020, the SEC issued a [Public Statement](#) announcing that the OCIE has been renamed the “Division of Examinations.”

² [Observations from Examinations of Broker-Dealers and Investment Advisers: Large Trader Obligations](#), Risk Alert, SEC OCIE (Dec. 16, 2020).

³ The term “NMS Security” generally refers to exchange-listed equity securities and standardized options, but does not include exchange-listed debt securities, securities futures, or open-end mutual funds.

⁴ Rule 13h-1 defines a Large Trader as a person whose transactions in NMS securities equal or exceed 2 million shares or \$20 million during any calendar day, or 20 million shares or \$200 million during any calendar month. Rule 13h-1 also applies to persons that exercise investment discretion over trading in NMS securities. An investment adviser that exercises investment discretion directly or indirectly on behalf of itself or others, for example, will become a Large Trader if it meets the transaction thresholds in the definition.

situations that could lead it to become a Large Trader, (ii) the timely filing of both the annual and any amended filings of Form 13H, if applicable, and (iii) notifying any broker-dealers through which it executes transactions of its Large Trader status. Advisers that transact in NMS securities but have not yet adopted written Rule 13h-1 policies and procedures can either adopt a standalone Rule 13h-1 policy or, perhaps more efficiently, add a Rule 13h-1 policy to the compliance manual they currently maintain for Investment Advisers Act compliance purposes.

- **Broker-dealers that transact in NMS securities should assess and make any necessary changes to their Rule 13h-1 supervisory and compliance policies and procedures.** Each broker-dealer should assess its policies and procedures with respect to: (i) evaluating whether Rule 13h-1 applies to it and its affiliates, (ii) the timely filing of both the annual and any amended filings of Form 13H, if applicable, (iii) complying with reporting requirements currently under Electronic Blue Sheets, forthcoming under the Consolidated Audit Trail (“CAT”), and applicable FINRA Rules, (iv) monitoring customer activity to identify customers that may be Large Traders but have not provided their Large Trader identification number, and the process of contacting such customers, and (v) identifying and associating new accounts for existing Large Traders.
- **Broker-dealers should review their reporting obligations.** Current reporting obligations for broker-dealers include Large Trader information in Electronic Blue Sheets and upcoming new reporting obligations include reporting customer identifying information as it relates to Large Traders to the CAT, which begins on **April 26, 2021**. OCIE recommends that broker-dealers review these new reporting requirements and ensure that they are ready to meet them by April 26, 2021.

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