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A Close Look At The Treasury's Upcoming Form SHL Survey

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In August 2014, the U.S. Department of the Treasury and the Federal Reserve Bank of New York (FRBNY) will conduct a benchmark survey of foreign holdings of U.S. issuers' securities on Treasury International Capital Form SHL (TIC SHL). U.S. asset managers that advise investment funds with foreign investors may be required to file TIC SHL. This article provides an overview of the TIC SHL reporting requirements and explains how they may apply to investment managers.[1]

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Overview of TIC SHL

TIC Form SHL is a mandatory benchmark study commissioned by the Treasury and administered by the FRBNY every five years.[2] The survey reviews holdings of U.S. securities — including short- and long-term securities and selected money markets instruments — by foreign residents.[3] The survey is part of a series of TIC and related forms that are used to calculate U.S. balance of payment data, to formulate U.S. international financial and monetary policies and to generate International Monetary Fund statistics.

TIC SHL consists of two parts. Schedule 1 consists mainly of basic identifying information and a summary of the data, if any, reported on Schedule 2. Schedule 2, which is significantly more burdensome, requires detailed security-by-security reporting of foreign holdings of the reporter's securities.

Who Must Report

Reporting obligations are triggered in two ways. First, all U.S.-resident entities that are contacted by the FRBNY are required to file at least Schedule 1 and must file Schedule 2 if they exceed the reporting threshold, discussed below. Second, any entity that exceeds the exemption level, regardless of whether or not it is contacted by the FRBNY, must submit both Schedule 1 and Schedule 2.

The reporting threshold is met if the total value of reportable U.S. securities owned by foreign residents equals $100 million or more as of the close of business on June 30, 2014. For purposes of determining whether the threshold has been met, asset managers and other reporters must consolidate all U.S.-resident parts of their organization (including all U.S.-resident branches and subsidiaries), as well as any

U.S. investment funds they manage.[4]

What to Report

Investment managers report on behalf of their own organization (i.e., the adviser or its parent entity's and U.S. affiliates' securities held by foreign residents) as well as the U.S. investment funds they manage. The TIC SHL instructions define funds broadly to include "all investment vehicles that pool investors' money and invest the pooled money in one or more of a variety of assets," and include open- and closed-end funds, money market funds, real estate investment trusts, investment trusts, index-linked funds, exchange-traded funds, hedge funds and common trust funds.[5]

Any shares or similar units issued by the funds (including limited partnership interests) held by non-U.S. residents are within the scope of TIC SHL. In addition, managers that organize offshore feeder funds to U.S. master funds must report the securities held by the offshore feeder fund, even though the onshore and offshore funds may be affiliated with one another.

Reportable securities include equities, debt securities (both short- and long-term), and asset-backed securities issued by U.S. residents. Specific exclusions include derivatives contracts (including futures, forwards, swaps, options and warrants); securities held pursuant to repurchase agreements; loans and loan participation certificates; and annuities, including variable rate annuities.[6]

Securities are reported on Schedule 2 of TIC SHL on a security-by-security and country-by-country basis. Thus, a separate Schedule 2 would be filed for shares of Fund X held by residents of France and shares of Fund X held by residents of the U.K. Similarly, a separate Schedule 2 would be filed for shares of Fund X held by residents of Germany and shares of Fund Y held by residents of Germany.

In addition, in the case of shares with multiple classes, each class must be filed on a separate Schedule 2 with respect to each foreign country in which shareholders reside. Thus, asset managers could be required to file dozens or even hundreds of Schedules 2.

Reporting Dates

If required to file TIC SHL, an entity must submit the report by Aug. 29, 2014, the last business day of August. The report should encompass holdings as of June 30, 2014, the last business day of June.

Penalties for Failure to Report

TIC SHL is authorized and required by an act of Congress. There is potential civil and criminal liability for failure to file timely and accurate reports for any U.S. person or group subject to the reporting requirements. Any group that fails to provide timely and accurate data may be subject to a civil penalty between $2,500 and $25,000, or injunctive relief ordering compliance, or both.

Any U.S. person or group that willfully fails to submit any of the information required in the report on TIC SHL may be subject to a fine of up to $10,000, and, if an individual, may be subject to imprisonment for up to one year, or both. In addition, the requirement subjects officers, directors, employees and agents of any entity with filing obligations who knowingly participate in such willful violation to the same penalties.

Relation to Other TIC Forms

U.S. asset managers may be familiar with the TIC reporting system, which is comprised of a number of forms that collect data on cross-border holdings of and transactions in securities, derivatives activity, foreign currency market participation, and claims on and liabilities to foreign persons. TIC SHL shares similarities with TIC Form SLT (TIC SLT), which was introduced in 2011 and which is a monthly form that collects data on both holdings of foreign securities by U.S. residents and holdings of U.S. securities by foreign residents.

However, TIC SHL differs from TIC SLT in several important respects. First, TIC SLT only captures foreign holdings of U.S. securities, and not U.S. holdings of foreign securities. Thus, unlike TIC SLT, in assessing TIC SHL, potential reporters need only consider their role as issuers, and not as portfolio investors.

Second, while TIC SLT is limited to holdings of long-term securities (i.e. equities and fixed income securities with an original maturity of more than one year), TIC SHL requires reporting of both long- and short-term securities. While investment funds are unlikely to be issuers of short-term securities, asset managers themselves and their affiliates may need to assess whether entities in their organization issue such instruments.

Third, at $100 million, the reporting threshold for TIC SHL is a mere one-tenth that of TIC SLT's $1 billion threshold. Accordingly, a number of potential reporters who fall below the TIC SLT threshold may nevertheless have a reporting obligation under TIC SHL.

Conclusion

Although completing TIC SHL is a potentially burdensome exercise, entities that already file other TIC and related forms (in particular, TIC Form SLT) may be able to rely on existing reporting systems within their organizations. Investment managers are expected to make reasonable efforts to determine the extent to which fund shares are held by foreign investors. In doing so, they should be mindful that the relevant data may be held by a third party, such as a transfer agent, and should work with such vendors to compile the reports.

However, to the extent that shares are held through omnibus accounts administered by U.S. broker-dealers that serve both U.S. and foreign investors, investment managers need not look through to determine the investors' residency and may instead rely on the broker-dealers maintaining the accounts, which should report such holdings on their own TIC SHL filings.

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[1] For an overview of the of the other parts of the TIC reporting system and related reporting regimes that may apply to U.S. investment managers or their affiliates, see Julien Bourgeois, Philip Hinkle, and Matthew Barsamian, Foreign Holdings and Transactions with Foreign Persons: Reporting Responsibilities for US Investment Managers and Other Financial Institutions (PDF), The Investment Lawyer, Vol. 21, No.

4 (April 2014). For more in-depth discussion of particular forms, see DechertOnPoint TIC B Forms Are Amended to Explicitly Cover U.S. Investment Managers (PDF); DechertOnPoint Changes to TIC Form D Highlight U.S. Investment Managers' Potential Reporting Obligations Regarding Cross-Border Derivatives Positions (PDF); DechertOnPoint Treasury Is Adopting New Reporting Requirements Regarding Cross-Border Holdings Applicable to U.S. Investment Managers (PDF).

[2] During the years when the benchmark study is not conducted, the Treasury collects data on TIC Form SHLA, which is a survey that requires reporting by only the very largest U.S.-resident custodians and issuers.

[3] Related TIC Forms SHC and SHCA are administered every five years and annually, respectively, and collect data on the holdings of foreign securities by U.S. residents. The most recent SHC report was collected in March 2012.

[4] For purposes of the TIC forms, a U.S. resident is defined as "any individual, corporation, or other organization located in the United States, including branches, subsidiaries, and affiliates of foreign entities located in the United States."

[5] Foreign-Residents' Holdings of U.S. Securities, Including Selected Money Market Instruments (SHL), Department of the Treasury, Federal Reserve Bank of New York, Feb. 2014, at 11-12.

[6] Id. at 10.
