January 6, 2022

Vanessa A. Countryman, Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

VIA ELECTRONIC MAIL: rule-comments@sec.gov

Re: File Number S7-18-21: Reporting of Securities Loans (the "**Proposed Rule**")

Dear Ms. Countryman:

The Committee on Capital Markets Regulation (the "**Committee**") appreciates the opportunity to comment on the proposed rule of the Securities and Exchange Commission (the "**SEC**") on reporting of securities loans.[1] If adopted, the Proposed Rule would (i) require the reporting of certain terms of securities lending transactions to designated registered national securities associations ("**RNSAs**"), and (ii) require public disclosure of certain transaction-level and aggregate information regarding securities lending. The Committee is concerned that the Proposed Rule would harm U.S. capital markets by reducing overall short selling activity with negative effects for market liquidity and pricing efficiency.

Founded in 2006, the Committee is dedicated to enhancing the competitiveness of U.S. capital markets and ensuring the stability of the U.S. financial system. Our membership includes thirty-eight leaders drawn from the finance, investment, business, law, accounting, and academic communities. The Committee is chaired jointly by R. Glenn Hubbard (Emeritus Dean, Columbia Business School) and John L. Thornton (Former Chairman, The Brookings Institution) and is led by Hal S. Scott (Emeritus Nomura Professor of International Financial Systems at Harvard Law School and President of the Program on International Financial Systems). The Committee is an independent and nonpartisan 501(c)(3) research organization, financed by contributions from individuals, foundations, and corporations.

The Proposed Rule would be a significant departure from existing market practices. Presently, market participants can purchase access to private data providers (such as CBOE, FIS or IHS Markit)[2] that disclose certain securities lending activities involving the beneficial owners of securities, such as asset managers or pension funds, broker-dealer lending agents and other

[1] Reporting of Securities Loans, 86 Fed. Reg. 69802 (proposed Dec. 8, 2021), *available at* https://www.govinfo.gov/content/pkg/FR-2021-12-08/pdf/2021-25739.pdf [henceforth, the "**Proposed Rule**"].

[2] CBOE, Borrow Intensity Indicator (last accessed Dec. 22, 2021) https://www.cboe.com/services/analytics/hanweck/borrow_intensity_indicators/; FIS Global, FIS Securities Finance Market Data (last accessed Dec. 22, 2021) https://www.fisglobal.com/en/capital-markets-solutions/investment-banking-and-brokerage/securities-finance/fis-securities-finance-market-data; IHS Markit, Securities Finance (last accessed Dec. 22, 2021) https://ihsmarkit.com/products/securities-finance.html.

intermediaries.[3] This is often referred to as the "wholesale" securities lending market.[4] Existing private data providers generally do not provide details regarding securities lending activity between broker-dealers and end-user customers.[5] The Proposed Rule refers to loans from brokers to end customers as the "retail" market.[6]

The Proposed Rule's economic analysis acknowledges at length that short selling activity has a positive impact on capital markets by enhancing liquidity and stock price efficiency.[7] However, it then mistakenly argues that the Proposed Rule will reduce the cost of short selling and facilitate more short selling activity.[8] Instead, the Proposed Rule is likely to reduce overall short selling activity and thereby harm U.S. capital markets, in particular by signaling to the market that a short selling position is being established in a specific security, which would make it more costly to continue to build short positions and thus inhibit market participants from doing so.

First, the Proposed Rule would mandate the public disclosure of securities lending activity on a transaction-by-transaction basis as soon as 15 minutes after execution and publicly specify the security being lent.[9] To address this concern, we recommend that the SEC revise the Proposed Rule to require the public disclosure of aggregate securities lending transactions for each security on an end-of-day basis at the earliest. Second, we recommend that the SEC revise the proposal to clarify that its scope is limited to the "wholesale" securities lending market and not to short selling activity in the "retail" market. This would more closely align the Proposed Rule with the scope of information published by private data providers and would prevent the public identification of an individual market participant's short positions. Empirical research has demonstrated that the disclosure of a market participant's short positions reduces overall short selling activity and has a negative impact on market liquidity and pricing efficiency.

The Proposed Rule, including the economic analysis, does not consider these potential negative impacts on short selling activity, including inhibiting position building (and related fundamental research), nor does it take into account the related effects on price efficiency, capital allocation, or market liquidity from doing so.

[3] *Id*., at 69806-69807.
[4] *Id*., at 69807.
[5] *Id*., at 69832.
[6] *Id.*, at 69805.
[7] *Id.*, at 69839.
[8] *Id.*
[9] *Id.*, at 69813.

1. PROPOSED RULE

If adopted, the Proposed Rule would create a new Rule 10c-1 under the Securities Exchange Act of 1934, as amended (the "**Exchange Act**"),[10] which would require any person who loans a security on its own behalf or that of another person (e.g., broker-dealer lending agents) to provide specified "material" terms of the subject transaction to an RNSA,[11] namely to the Financial Industry Regulatory Authority ("**FINRA**").[12] Certain 10c-1 information would be subject to public disclosure by the RNSA, including (i) "transaction data elements,"[13] and (ii) information on "securities available to loan and securities on loan" to be disclosed by parties acting as lending agents on an aggregate basis.[14] **Table 1** (on the next page) provides further details of the 10c-1 information that must be publicly disclosed.

The Proposed Rule would require the transaction data elements to be provided to an RNSA within 15 minutes after each loan is effected, whereas information on securities available to loan and securities on loan would be required by the end of the relevant business day.[15] Public disclosure would then be required as soon as practicable.[16] The Proposed Rule is intended to "increase the transparency of information available to market participants by allowing for the evaluation of the terms of recently effected [securities] loans and any signals that these terms provide."[17]

[10] 15 U.S.C. § 78a *et seq*.
[11] Proposed Rule, 86 Fed. Reg. at 69803.
[12] *Id*., at 69808 (noting that "currently, FINRA is the only RNSA").
[13] *Id*., at 69851-69852.
[14] *Id*., at 69852.
[15] *Id*., at 69812.
[16] *Id*.
[17] *Id*.

Table 1: Publicly Disclosed Data Elements

Transaction Data Elements	**Information on Securities Available to Loan and Securities on Loan by Broker-Dealer Lending Agents**
The legal name of the security issuer, and the Legal Entity Identifier ("LEI") of the issuer, if the issuer has an active LEI.	The legal name of the security issuer, and the LEI of the issuer, if the issuer has an active LEI.
The ticker symbol, ISIN, CUSIP, or FIGI of the security, if assigned, or other identifier.	The ticker symbol, ISIN, CUSIP, or FIGI of the security, if assigned, or other identifier
The date the loan was effected.	The total amount of each security available to lend by the broker or dealer, including the securities owned by the broker or dealer, the securities owned by its *customers* who have agreed to participate in a fully paid lending program, and the securities in its margin *customers'* accounts.
The time the loan was effected.	
For a loan effected on a platform or venue, the name of the platform or venue where effected.	
The amount of the security loaned.	
For a loan not collateralized by cash, the securities lending fee or rate, or any other fee or charges.	
The type of collateral used to secure the loan of securities.	
For a loan collateralized by cash, the rebate rate or any other fee or charges.	
The percentage of collateral to value of loaned securities required to secure such loan.	
The termination date of the loan, if applicable.	
Whether the borrower is a broker or dealer, a customer (if the person lending securities is a broker or dealer), a clearing agency, a bank, a custodian, or other person.	

2. ANALYSIS

The Proposed Rule Could Inhibit Market Participants from Building and Adjusting Short Positions

The Proposed Rule acknowledges the significant benefits of short selling for U.S. capital markets. For example, the Proposed Rule notes that, "academic research shows that short sellers, through their research, contribute to price efficiency by gathering and trading on relevant private information."[18] The Proposed Rule also notes that short sellers serve as effective monitors of corporate management and that short selling increases market liquidity.[19]

The Proposed Rule's economic analysis then mistakenly argues that the Proposed Rule will reduce the cost of short selling and facilitate more short selling activity – thus augmenting the aforementioned benefits. Unfortunately, the exact opposite is likely to occur, as the Proposed Rule would potentially reduce overall short selling activity by inhibiting and increasing the cost of building short positions. First, it would do so by potentially including in its scope all individual customer short positions even though they are not traditionally considered or documented as securities lending transactions. Second, it would do so by disclosing "wholesale" and a newly expanded universe of "retail" securities lending activity on a transaction-by-transaction basis for *specific securities* as soon as 15 minutes after they are effected. The public disclosure of elevated "wholesale" or "retail" securities lending activity in a specific security would likely signal to the market that a short selling position is being actively established in that security. This could have several potential negative effects on short sellers that would discourage overall short selling activity.

Most obviously, such public disclosure would signal to all other market participants that a short position is being established. This disclosure alone will have a market impact that will increase the costs associated with establishing a short position through information leakage and slippage. Second, the public disclosure could impair the economics of establishing the short position by leading to copycat short selling activity, which would diminish returns and could increase the cost to borrow the security due to increased demand. It is further possible that the initial short seller would be unable to fully establish their short position due to a lack of immediate supply of the security for borrowing. These risks are particularly acute for less liquid or hard to borrow securities. Another risk is that the Proposed Rule could facilitate "short squeezes" whereby "long" market participants become aware that a short position is being established and quickly take the other side of the trade, posing the immediate risk of significant losses for the short seller, which would discourage the short seller from further building its position and reduce overall short selling activity. Together, by increasing the costs of executing short sale transactions and decreasing potential returns, the Proposed Rule would reduce the benefits of and incentives to conduct the fundamental research that short sellers would otherwise conduct.

We recommend that the SEC revise the Proposed Rule so that (i) securities lending activity is disclosed in the aggregate for all transactions in a specific security on an end-of-day basis at the

[18] *Id*., at 69839.
[19] *Id*.

earliest and (ii) the public disclosure of securities lending arrangements is limited to the "wholesale" market and does not cover short selling activity in the "retail" market. This would better enable short sellers to establish short positions and reduce the likelihood that the Proposed Rule would have a negative impact on overall short selling activity and U.S. capital markets.

It is unclear whether there are any benefits specific to the disclosure of trading activity between broker-dealers and their customers. However, as we have noted throughout this letter, there are significant potential costs to market quality from such disclosures. By contrast, there may be potential benefits from the mandatory public disclosure of "wholesale" securities lending activity on an end-of-day basis (at the earliest) by providing more standardized information regarding the securities available to borrow and associated costs thereby enhancing competition among securities lenders.[20] We therefore recommend that the SEC solely consider mandating public disclosure of the "wholesale" market on an end-of-day basis at the earliest. This would more directly achieve the SEC's goal of enhancing transparency in the securities lending market, because access to information from the private data providers is not publicly available and securities lenders only voluntarily provide such data today.[21]

The Proposed Rule Could Result in the Disclosure of Market Participants' Short Selling Positions

The Proposed Rule would apply its transaction data disclosure requirements to securities lending activity between broker-dealers and their customers and could effectively require the disclosure of short transactions. For example, the Proposed Rule states with regards to "onward lending" that a broker-dealer lending agent that, "loans…securities to a hedge fund…would be responsible for providing the 10c-1 information to the RNSA regarding the securities lending transaction between the broker-dealer and the hedge fund because the broker-dealer is lending the securities."[22] Such transaction data, as described in **Table 1** must then be publicly disclosed.[23]

Although the Proposed Rule would not explicitly require the public disclosure of the identity of the customer borrowing the security, it would require the public disclosure of extensive information regarding each onward securities lending transaction so market experts could potentially determine the identity of a securities borrower and their short positions. For example, the Proposed Rule would require the public disclosure of the securities lending fee or rate charged on each securities lending transaction.[24] Securities lending fees and rates are typically specific to each customer.[25] The Proposed Rule would also require that each securities lending transaction be disclosed within 15 minutes when practicable which would enable market experts to better identify a specific market participant building a short position, particularly in a less liquid or hard to borrow security.

[20] Proposed Rule, 86 Fed. Reg. at 69837-69840.
[21] Id., at 69807.
[22] *Id*., at 69811.
[23] *Id*., at 69812.
[24] *Id*., at 69851-69852.
[25] *Id*., at 69831.

The Proposed Rule would also require broker-dealer lending agents to disclose the inventory of their securities "owned by [their] customers . . . and the securities in [their] margin customers' accounts."[26] Market experts would therefore not only have access to transaction-by-transaction information to reverse engineer the identity of market participants and their positions but also access to an inventory of all borrowed securities on a broker-dealer-by-broker-dealer basis. Since customers often borrow from a limited number of broker-dealers, a broker-dealer-by-broker-dealer public inventory would better enable market experts to identify specific market participants and the size of their short positions.

The Proposed Rule does not evaluate whether it would discourage overall short selling activity if it were to result in the effective disclosure of individual market participants' short selling positions, nor does it evaluate the costs associated with such disclosure. Past Committee research has found that the disclosure of individual market participants' short selling positions would indeed discourage short selling activity.[27] According to a 2018 report by the Committee on short selling,

> Short sellers are generally motivated to maintain a high degree of secrecy and anonymity given (i) concerns about revealing proprietary trading strategies, which could increase the costs of implementing the strategy, (ii) fears of potential litigation initiated by the shorted firm, and (iii) the potential loss of access to the shorted firm's management, arguably the most important concern for overall market efficiency… Short sellers are arguably even more sensitive about revealing trading positions to competitors than investors taking long positions, since short positions are always part of an active trading strategy, while long positions can be part of an active or passive strategy.[28]

Empirical research has also demonstrated that the disclosure of individual short selling positions has negative effects on market quality. For example, Jank, Roling and Smajlbegovic (2016) analyze the effects of mandatory short sale disclosure in the European Union, which imposed a mandatory disclosure rule for certain short positions in 2012.[29] The EU rule requires short sellers to notify regulators if a short position reaches 0.2% of the stock's issued share capital and publicly disclose any short positions that reach 0.5%.[30] The study found that short sellers restricted overall short selling activity in the face of the disclosure regulation and that the EU's mandatory disclosure requirements have caused a deterioration in market quality, noting that the transparency regulation has "impose[d] a negative externality on the informational efficiency of stock prices."[31]

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[26] *Id*., at 69852.
[27] COMMITTEE ON CAPITAL MARKETS REGULATION, *Short Selling's Positive Impact on the Markets and the Consequences of Short-Sale Restrictions* (2018), *available at* https://www.capmktsreg.org/wp-content/uploads/2018/09/CCMR-Statement-on-Short-Selling.pdf.
[28] *Id*., at 8.
[29] Jank et al., *Flying Under the Radar: The Effects of Short-Sale Disclosure Rules on Investor Behavior and Stock Prices*, Deutsche Bundesbank Discussion Paper No 25/2016, 2016), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2809498.
[30] *Id*., at 6.
[31] *Id*., at 32.

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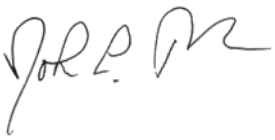
Thank you very much for your consideration of the Committee's position. Should you have any questions or concerns, please do not hesitate to contact the Committee's President, Professor Hal S. Scott (hscott@law.harvard.edu), or its Executive Director, John Gulliver (jgulliver@capmktsreg.org), at your convenience.

Respectfully submitted,



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