January 7, 2022

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

Re: Reporting of Securities Loans, 86 Fed. Reg. 69,802 (Release No. 34–93613; File No. S7–18–21).

Dear Secretary Countryman:

Better Markets[1] appreciates the opportunity to comment on the above-captioned rule proposal ("Release" or "Proposal") noticed for public comment by the Securities and Exchange Commission ("SEC" or "Commission"). The Proposal would implement Section 984(b) of the Dodd-Frank Act by requiring that lenders of securities report certain terms of those transactions to a registered national securities association ("RNSA"), and by further requiring that the RNSA make some of that information publicly available. Better Markets urges the SEC, after strengthening the rule as suggested below, to finalize this long-overdue, mandatory rulemaking without delay or dilution.

BACKGROUND

The $1.5 trillion market for securities lending, i.e. "the temporary transfer of a security by one party (the lender) to another party (the borrower) in exchange for cash or non-cash collateral, for a fee" plays a critical role in the functioning of the financial markets.[2] Broker-dealers borrow securities for their market-making activities or on behalf of clients who want to purchase

---

1 Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system that protects and promotes Americans' jobs, savings, retirements, and more.

2 Financial Stability Oversight Council 2021 Annual Report 45 (2021) ("FSOC 2021 Annual Report"), https://home.treasury.gov/system/files/261/FSOC2021AnnualReport.pdf.

1825 K Street, NW, Suite 1080, Washington, DC 20006
TELEPHONE (1) 202.618-6464
FAX (1) 202.618.6465
WEBSITE bettermarkets.com

securities.[3] Investors can use borrowed securities to engage in short-selling, allowing them to take a position in a security whose value they think will fall (which contributes to price discovery), or else to hedge against the risks of other positions.[4] Large institutional investors increasingly use securities lending to generate revenue.[5] Securities lending is also intimately connected with short-term funding markets, as a "large portion of cash collateral" given to lenders of securities by borrowers is reinvested in short-term funding markets, meaning issues in the securities lending markets can ripple through the broader economy. This occurred in March 2020, as the Financial Stability Oversight Council ("FSOC") has explained:

> "The fall in asset prices in March 2020 led to deleveraging by market participants that typically borrow securities, and the lower asset prices and lower demand for new securities lending in general reduced the amount of cash collateral reinvested in the STFMs. This deleveraging limited the supply of capital available in the STFMs, making it more difficult for issuers in the real economy to access capital."[6]

And yet, despite its size and the importance of the securities lending market to many market participants, and to the broader stability of the financial system, it is nearly impossible for anyone, including market participants and regulators, to comprehensively monitor the securities lending market because of "the lack of comprehensive, standardized statistics on securities lending activities."[7] This lack of transparency has already contributed to financial instability multiple times. For example, securities lending played an important, albeit underappreciated role, in the 2007-2009 financial crisis.[8] As the Financial Stability Board ("FSB") has explained, securities lending activities can allow non-banks to

> "effectively perform 'bank-like' activities, such as credit and maturity transformation, thereby subjecting its portfolio to credit and liquidity risks. As illustrated by AIG's behaviour as a securities lender prior to the recent financial crisis, lenders can use securities lending as a means of short term funding for financing leveraged investment in instruments that, while highly rated when purchased, can become illiquid, risky, and lose value quickly. That may give rise to the risk of a 'run' if securities borrowers start terminating the securities lending transactions and ask for their cash collateral to be returned."

---

3 Release at 69,805; *see also* Viktoria Baklanova, *et al.*, FRBNY Staff Reports, *Reference Guide to U.S. Repo and Securities Lending Markets* 22, (Sept. 2015), https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr740.pdf; Financial Stability Board, *Securities Lending and Repos: Market Overview and Financial Stability Issues* 6 (Apr. 2012), https://www.fsb.org/wp-content/uploads/r_120427.pdf. .

4 *See* Financial Stability Oversight Council 2020 Annual Report 45 (2020), https://home.treasury.gov/system/files/261/FSOC2020AnnualReport.pdf.

5 Release at 69,804.

6 *See* Financial Stability Oversight Council 2020 Annual Report 45 (2020), https://home.treasury.gov/system/files/261/FSOC2020AnnualReport.pdf.

7 FSOC 2021 Annual Report at 46.

8 Hester Peirce, *Securities Lending and the Untold Story in the Collapse of AIG*, Mercatus Center Working Paper No. 14-12 (May 2014), https://www.mercatus.org/system/files/Peirce_SecuritiesLendingAIG_v2.pdf.

As indicated by this quote, securities lending contributed directly to the collapse of AIG, and accordingly it significantly contributed to the broader $20 trillion financial crisis.[9] AIG lent securities to borrowers and took cash from borrowers as collateral.[10] It then took that cash and used it to finance acquisitions of mortgage-backed securities—by 2007 AIG had "AIG invested up to seventy percent of its entire securities-lending operations in residential mortgage-backed securities and related instruments."[11] When AIG's counterparties became concerned about AIG's financial condition, they began to terminate their transactions, which required return of the cash collateral.[12] However, because of the problems in the housing market, the mortgage-backed securities in which AIG had invested its collateral were illiquid, making it difficult for AIG to meet its obligations to borrowers, exacerbating AIG's deterioration and, ultimately, requiring taxpayers to fund a bailout of AIG.[13] In other words, AIG had used securities lending (which had been generally understood to be a "relatively safe way for insurers to make money"[14]) to create a bank-like mismatch between the liquidity of its assets and its liabilities, exposing it to a bank-like run risk, but without access to the deposit insurance and other regulatory safeguards that mitigate the risks of runs for banks. When this run risk was realized, taxpayers were put on the hook to bailout AIG to prevent further damage to the financial system.

This is not the only recent example of the potentially destabilizing impact of securities lending and the lack of transparency surrounding it. As explained above, one reason to borrow a security is to engage in short-selling, i.e., to attempt to profit based on the view that a particular security will decrease in value. While short-selling can contribute to orderly markets by enhancing price discovery, it can also destabilize markets, which occurred in January 2021 with the stock of GameStop and other so-called "meme stocks."[15] Short interest (the ratio of shares sold short to shares outstanding) is typically less than 2.5% for large non-financial stocks and less than 13% for small non-financial stocks; it is rare that short interest is more than 50% for any given stock, and even rarer that it is over 90%.[16] For years, however, GameStop had consistently

---

9 Better Markets, *The Cost of the Crisis: $20 Trillion and Counting* (2015), https://bettermarkets.com/sites/default/files/Better%20Markets%20-%20Cost%20of%20the%20Crisis.pdf

10 Daniel Schwarcz, *A Critical Take on Group Regulation of Insurers in the United States*, 5 U.C. Irvine L. Rev. 537, 552 (2015).

11 *Id.*

12 *Id.* Securities lending transactions are typically open-ended, *i.e.*, either party can terminate at any time and recall their cash or securities, as the case may be. Viktoria Baklanova, *et al.*, FRBNY Staff Reports, *Reference Guide to U.S. Repo and Securities Lending Markets* 31, (Sept. 2015), https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr740.pdf.

13 Daniel Schwarcz, *A Critical Take on Group Regulation of Insurers in the United States*, 5 U.C. Irvine L. Rev. 537, 552 (2015).

14 *Id.* at 551-52.

15 Better Markets, *Short Selling: 10 Recommendations for Improving the SEC's Regulatory Framework* (May 4, 2021), https://bettermarkets.org/wp-content/uploads/2021/07/Short-Selling-10-Recommendations-for-Improving-the-SECs-Regulatory-Framework.pdf.

16 *See* Securities & Exchange Commission, *Staff Report on Equity and Options Market Structure Conditions in Early 2021* at 25 (Oct. 14, 2021), https://www.sec.gov/files/staff-report-equity-options-market-struction-conditions-early-2021.pdf, [hereinafter "SEC Staff GameStop Report"].

experienced short interest of over 50%, as investors increasingly viewed the prospects of the struggling video game retailer with skepticism.[17] And from 2019 to 2021, "GME short interest hovered around 100%, hitting its high of 109.26% on December 31, 2020."[18] Such an extraordinarily high short interest can lead to a destabilizing short squeeze, which can in turn lead to significant volatility in the price of the shorted stock, if not the broader markets. And indeed, this is exactly what happened, with GameStop and other heavily-shorted stocks experiencing sudden, rapid price rises and drops despite little change to these companies' business fundamentals. This volatility infamously resulted in trading halts by Robinhood and other broker-dealers, so they could meet their financial commitments to clearinghouses,[19] and resulted in significant losses for some investors (*i.e.* those who had bought during the rapid price increase).[20] Further, such incidents have a negative impact on the signaling and financing purposes of the securities markets, undermining public confidence in the markets.[21] If regulators and the public had better and more timely information about the amount of shares of GameStop and other meme stocks that had been lent and borrowed, they may have been able to proactively head off or mitigate the impact of the destabilizing events of January 2021 before they occurred.

Ultimately, the importance of transparency into the securities lending market (and by extension, the activities it facilitates, such as short-selling and risky shadow-banking activities), led Congress to promulgate Section 984(b) of the Dodd-Frank Act, which required the SEC, within 2 years, to "promulgate rules that are designed to increase the transparency of information available to brokers, dealers, and investors, with respect to the loan or borrowing of securities."

<u>OVERVIEW OF PROPOSAL</u>

The Proposal would implement Section 984(b) of the Dodd-Frank Act by requiring that securities lenders, or lenders' agents (collectively, we will refer to lenders and lenders' agents as "reporters") report to an RNSA the material terms of a securities lending transaction.[22] Specifically, a reporter would be required to report the following information to the RNSA ***within 15 minutes*** after each loan is effected, and the RNSA would be required to make the information ***public as soon as practicable***, but not later than the next business day:

---

17 *See* SEC Staff GameStop Report at 25.

18 *Id.*

19 Meagan Leonhart, *Robinhood Now Faces Roughly 50 Lawsuits After GameStop Trading Halt—Here's How Customers Might Actually Get Their Day in Court*, MSNBC (Aug. 31, 2021), https://www.cnbc.com/2021/02/17/robinhood-faces-lawsuits-after-gamestop-trading-halt.html.

20 Drew Harwell, *As GameStop Stock Crumbles, Newbie Traders Reckon With Heavy Losses*, Wash. Post (Feb. 2, 2021), https://www.washingtonpost.com/technology/2021/02/02/gamestop-stock-plunge-losers/.

21 *Game Stopped? Who Wins and Loses When Short Sellers, Social Media, and Retail Investors Collide: Hearing Before the House Financial Services Committee: Part II* 7-8(testimony of Dennis M. Kelleher) (Mar. 17, 2021), https://bettermarkets.org/sites/default/files/Kelleher%20HFSC%20Testimony%20GameStop%20Hearing%203-17-2021%20FINAL%20%282%29.pdf.

22 The Financial Industry Regulatory Authority ("FINRA") is currently the only RNSA.

- Legal name and ticker symbol of the issuer of the loaned securities;
- Time and date of the loan;
- Name of the platform or venue, if applicable;
- Amount of securities loaned;
- Rates, fees, charges, and rebates for the loan as applicable;
- Type of collateral provided for the loan and the percentage of the collateral provided in relation to the value of the loaned securities;
- Termination date of the loan, if applicable; and,
- Borrower type, *e.g.*, broker, dealer, bank, customer, clearing agency, or custodian.[23]

Moreover, reporters would be required to report the following information to an RNSA ***within 15 minutes***, which would ***not be publicly reported***:

- The legal names of the parties to the loan;
- If the lender is a broker-dealer, whether the security loaned to its customer is loaned from the broker-dealer's inventory; and
- Whether the loan will be used to close out a fail to deliver pursuant to Rule 204 of Regulation SHO or whether the loan is being used to close out a fail to deliver outside of Regulation SHO.[24]

Finally, the Proposal would require the reporting of certain information by the ***end of each business day***, which would be made ***public only in aggregated form***, including the following, depending on the circumstances:

- The legal name and LEI of the security issuer;
- The ticker symbol or CUSIP of the security;
- The total amount of each security that is not subject to legal or other restrictions that prevent it from being lent; and
- The total amount of each specific security on loan owned by a person.[25]

COMMENTS

I. THE PROPOSAL WILL CONTRIBUTE TO FINANCIAL STABILITY AND SHOULD NOT BE DILUTED IN RESPONSE TO SPECIOUS INDUSTRY CONCERNS

Broadly speaking, increasing transparency into the securities lending market, as the Proposal would do, is sound public policy. It will increase the transparency that investors, other market participants, and regulators (including the SEC) have into the opaque securities lending market. As the SEC correctly points out, this will enable both borrowers and lenders to know

---

23 Release at 69,851-52.
24 *Id.* at 69,852.
25 *Id.*

whether the terms of securities loans are consistent with market conditions and practices.[26] It will also give the SEC and other regulators better insight into the markets they oversee with respect to fraud and systemic risk.[27] Thus, it will allow the SEC to use the acquired data to spot fraud, manipulation, and other wrongdoing and unlawful activity. And it will better equip the SEC and other regulators to spot excessive buildup of risk and other threats to financial stability as a result of securities lending and the activities (such as short-selling and liquidity and maturity transformation) that securities lending facilitates. Moreover, the Proposal is not only good public policy but also mandatory public policy, a statutory requirement from Congress.

For these reasons, the SEC must not only finalize the Proposal without undue delay but do so without diluting the Proposal in any way absent credible, specific evidence that such dilution will not have an impact on the utility of the data reported. This is critical because the Proposal represents the ***bare minimum to ensure that the Proposal meets the statutory requirement to*** "to increase the transparency of information available to brokers, dealers, and investors, with respect to the loan or borrowing of securities."[28] Were the SEC to exempt particular firms or transactions from the reporting requirements, reduce the elements that are required to be reported, allow further delays in the timing of reports, or otherwise change the Proposal so that the reported data is less comprehensive, timely, and usable, it would no longer be consistent with the letter and spirit of Section 984(b).

The SEC should be especially wary of arguments from the industry that it should dilute the Proposal to reduce the burden on the industry of collecting and reporting the necessary data. The financial industry often seeks to weaken or eliminate regulations by arguing that the requirements will have a devastating impact on their business, which will in turn harm the public interest and even investors.[29] These sorts of claims are typically exaggerated if not entirely groundless.[30] Here, however, it would be particularly misguided for the SEC to dilute the rule out of concern for burdens on the industry. Congress presumably understood that reporting requirements would result in some burden on the industry, but it decided that increasing transparency was more important than avoiding those burdens. The SEC cannot reverse Congress's policy judgment by instead prioritizing the purported burdens on industry of reporting meaningful securities lending data over the public interest benefits gained from the reporting of that data.

II. <u>THE SEC SHOULD CONSIDER REQUIRING REPORTING ON THE USE OF COLLATERAL</u>

As noted above, one of the ways that securities lending poses risks to financial stability is

---

26 *Id.* at 69,803.
27 *Id.*
28 Dodd-Frank Act Section 984(b).
29 *See, e.g.,* Marcus Baram, *The Bankers Who Cried Wolf: Wall Street's History of Hyperbole About Regulation*, Huffington Post (Jun. 21, 2011), https://www.huffpost.com/entry/wall-street-history-hyperbole-regulation_n_881775.
30 *Id.*

that securities lenders can use the collateral they receive, typically cash, to finance risky bank-like activities such as liquidity and maturity transformation, without any of the safeguards of bank regulation. The FSB has correctly noted that this re-use of collateral poses a variety of risks to financial stability.[31] The problem is exacerbated because many securities lenders use lending agents to facilitate their securities lending activities. Lending agents typically receive a proportion of profits from the reinvestment of collateral, but do not also share in any losses.[32] Thus, lending agents may have an incentive to seek out excessively risky investments.[33]

Because of these potential threats to financial stability arising from collateral re-use, the FSB has called for greater transparency into collateral and cash management principles by securities lenders.[34] Another commenter has pointed out that this would be "a prudent course to follow" and further argued that increased "transparency will give all market stakeholders (including regulators and the counterparties providing cash to securities lenders) greater ability to accurately assess the riskiness of the transaction."[35] As is, the Proposal will provide some information that will be useful in identifying how securities lending activities pose risks to financial stability, but without more information on how securities lenders (or their lending agents) use the collateral they receive as part of securities lending transactions, the threat remains that there will continue to be a buildup of dangerous and unseen risk in the financial system as a result of securities lending activity. Therefore, we urge the SEC to consider requiring that securities lenders or their agents report information on how they use collateral.

III. THE SEC SHOULD RE-EVALUATE THE TIMING DEADLINES IN THE PROPOSAL

In addition to strengthening the Proposal so it better addresses systemic risk, the SEC should also shorten the required time frames for the reporting and subsequent public dissemination of the required data. The Release states that requiring reporting within 15 minutes after lending transactions are effected or modified, coupled with the subsequent disclosure of the data elements as soon as practicable, would assist market participants "by allowing for the evaluation of the terms of recently effected loans and any signals that these terms provide," especially in a fast-moving market.[36] But setting aside whether those time frames actually serve the needs of market participants seeking contemporaneous input about the state of the market,

---

31 Financial Stability Board, *Securities Lending and Repos: Market Overview and Financial Stability Issues* 14-18 (Apr. 2012), https://www.fsb.org/wp-content/uploads/r_120427.pdf.

32 Frank M. Keane, *Securities Loans Collateralized by Cash: Reinvestment, Run Risk, and Incentive Issues* 7 Federal Reserve Bank of New York, Current Issues in Econ. & Fin., Volume 19 No. 3 (2013), https://www.newyorkfed.org/medialibrary/media/research/current_issues/ci19-3.pdf.

33 *Id.*

34 Financial Stability Board, *Strengthening Oversight and Regulation of Shadow Banking: Policy Framework for Addressing Shadow Banking Risks in Securities Lending and Repos* 9 (Aug. 29, 2013), https://www.fsb.org/wp-content/uploads/r_130829b.pdf.

35 Frank M. Keane, *Securities Loans Collateralized by Cash: Reinvestment, Run Risk, and Incentive Issues* 7 Federal Reserve Bank of New York, Current Issues in Econ. & Fin., Volume 19 No. 3 (2013), https://www.newyorkfed.org/medialibrary/media/research/current_issues/ci19-3.pdf.

36 Release at 69,812.

especially a fast-moving one, the Release does not adequately address the potential shortcomings of these time frames, including how they may hamper real-time regulatory oversight or allow manipulative activity based on information leakage or other means of exploiting the 15 minute reporting delay coupled with an indeterminate "as soon as practicable" deadline for public disclosure.

While there are certainly distinctions to be made, if high frequency traders can make huge and near-certain profits from accessing order data micro-seconds before it is widely available, it would seem that the opportunity for gaming a 15 minute reporting delay and a subsequent further delay in public access would be enormous. The public dissemination deadline is particularly weak. It is vague to the extent that its core requirement is that the information be made publicly available "as soon as practicable," and it is unacceptably lax to the extent its outside limit is the ***next business day.*** Clearly, with respect to the latter standard, the Release acknowledges that it is suboptimal, stating that the Proposal "will produce data that that may be less timely than existing commercial data."[37]

The Release reinforces the apparently untethered nature of the 15 minute reporting deadline by seeking input on whether the deadline should instead be quite dramatically different, either 90 seconds on the one hand or 30 minutes on the other.[38] Moreover, the rationale for the 15 minute reporting interval appears to some degree based on the fact that it coincides with other reporting timeframes, such as those followed by commercial vendors offering securities lending data in 15 minute increments,[39] or the TRACE requirement that trades be reported at the 15 minute time horizon.[40] Yet these alignments by themselves, without a more compelling justification, are not a convincing basis for the proposed time frames, given their potential drawbacks for market participants, regulators, and market integrity. Finally, given what the Release describes as the "automated nature of securities lending transactions,"[41] it would seem that shortening the reporting and public dissemination deadlines would be eminently feasible, without imposing significant cost.

In light of these considerations, the SEC must closely re-examine the various timing requirements in the Proposal. At a minimum, the final rule should significantly shorten the 15 minute reporting timeframe and place a specific and much shorter outside time limit on the "as soon as practicable" public reporting requirement, one that displaces the unacceptable "next business day" standard.

IV. THE SEC SHOULD CLOSE ANY POTENTIAL LOOPHOLE THAT WOULD ALLOW EVASION BY CHARACTERIZING SECURITIES LENDING TRANSACTIONS AS REPURCHASE AGREEMENTS

In the Release, the SEC recognizes the risk that securities lenders will attempt to

37 *Id.* at 69,837.
38 *Id.* at 69,821.
39 *Id.* at 69,836.
40 *Id.* at 69,846.
41 *Id.* at 69,847.

circumvent the rule's requirements by recharacterizing securities lending transactions as repurchase agreements.[42] The SEC should correct this shortcoming in the rule to ensure that its coverage is as comprehensive as possible. In a repurchase agreement, or "repo," Firm A agrees to sell securities to Firm B, and promises to repurchase those securities later at a specific, higher price.[43] Because Firm B pays for the securities in cash, this is "economically equivalent to an interest-bearing cash loan against securities collateral."[44] It is also functionally nearly identical to a securities lending transaction, inasmuch as it involves the temporary transfer of securities in exchange for cash or other collateral.[45] The primary functional distinction between a repo and a securities loan is that a repo always involves an exchange of cash, while the collateral exchanged in a securities loan may or may not be cash, although cash remains the predominant collateral exchanged in a securities lending transaction.[46] There also may be differences in the mechanics of how repo transactions are effectuated versus how securities loans are effectuated.[47]

However, it is not clear that these distinctions between repos and securities loans are relevant to the public policy concerns that motivated Congress to enact Section 984(b) or that are motivating the Proposal, *i.e.*, the need for greater transparency into the market for securities borrowing. To that end, while the SEC has not proposed to adopt a formal definition of "securities loan" or "securities lending," in the Release it describes securities lending as "the market practice by which securities are transferred temporarily from one party, a securities lender, to another, a securities borrower, for a fee."[48] This would seem to largely cover repos, except that in a repo the recipient of securities is typically considered the lender in the transaction, whereas the giver of securities is typically considered the borrower;[49] in a securities lending transaction the recipient of securities is nominally considered the borrower and the giver nominally the lender. This distinction, however, is primarily one of form; as the Release points out, repos can be, and already commonly are, used by firms that are seeking to borrow securities.[50] Likewise, securities "lenders" also can, and often do, use the cash collateral received from "borrowers" as a funding

---

42 *Id.* at 69,816.

43 *See* Viktoria Baklanova, *et al.*, FRBNY Staff Reports, *Reference Guide to U.S. Repo and Securities Lending Markets* 1 (Sept. 2015), https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr740.pdf.

44 *See id.* at 4.

45 *See* Release at 69,843-44.

46 Frank M. Keane, *Securities Loans Collateralized by Cash: Reinvestment, Run Risk, and Incentive Issues* 3 Federal Reserve Bank of New York, *Current Issues in Econ. & Fin.*, Volume 19 No. 3 (2013), https://www.newyorkfed.org/medialibrary/media/research/current_issues/ci19-3.pdf.

47 *Id.*

48 Release at 69,804.

49 *See* Tobias Adrian, *The Shadow Banking System: Implications for Financial Regulation*, FRBNY Staff Report No. 382 (Jul. 2009) ("In a repo, the borrower sells a security today for a price below the current market price on the understanding that it will buy it back in the future at a pre-agreed price."), https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr382.pdf.

50 *See* Release at 69,844 (explaining that using repos to finance short sales is common in fixed-income markets); *see also* Viktoria Baklanova, *et al.*, FRBNY Staff Reports, *Reference Guide to U.S. Repo and Securities Lending Markets* 4, (Sept. 2015) ("Repo contracts can also be used to borrow securities"), https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr740.pdf.

source to finance their activities, much as AIG did when it bought mortgage-backed securities in the runup to the financial crisis, making them functionally "borrowers" of cash in addition to, or instead of, being lenders of securities. This distinction is further muddled because in a securities lending transaction, the securities "lender" often pays compensation to the "borrower," which in some cases may be higher than the fee paid by the securities "borrower" for the temporary use of the securities.[51] A situation where the nominal "lender" in a transaction pays compensation to the nominal "borrower" for the temporary use of the borrower's asset, is a transaction in which the distinction between "borrower" and "lender" is primarily a formal, rather than a functional, distinction.

As the Release correctly points out, one upshot of the significant overlap of the economics and functions of repos and securities lending transactions is the real risk that repos may be used to evade the requirements of the rule, if not in the short-term, at least in the medium- or long-term, which would, eventually, undermine the breadth and utility of the data collected and reported.[52] This is because many transactions that involve the temporary transfer of securities for compensation can be characterized as a repo or a securities lending transaction simply by changing the formal label applied to the transaction and to the counterparties, *i.e.* a transaction that could be fairly characterized as a securities lending transaction can become a repo simply by labeling it as such and designating the securities recipient a lender of cash rather than a borrower of securities. The SEC must account for this risk by, at a minimum, including a broad anti-evasion provision that prohibits any person from engaging in any practice intended to evade the rule's reporting requirements.

However, the significant overlap in functionality between repos and securities lending transactions also poses a risk that the rule will result in insufficient coverage even without intentional evasion by industry participants, because transactions that could fairly be characterized as securities lending transactions may already be labeled repos, for reasons that are irrelevant to the policy concerns that motivated passage of Section 984(b). Excluding these transactions simply because of the label the parties to the transaction happened to decide to put on it would undermine the purposes of Section 984(b). Accordingly, the SEC should consider including in the rule a definition of "securities loan" or "securities lending" that will ensure sufficient coverage of relevant transactions, *i.e.*, those where securities are temporarily transferred from one party to another, for compensation, with a commitment to return those securities in the future, consistent with Congressional intent. This definition should be concerned with the ***inclusion of transactions that could fairly be described as "securities loans,"*** rather than the exclusion of transactions that could fairly be described as repurchase agreements. In other words, an appropriate definition would include any transaction that is materially indistinguishable from a securities lending transaction, even if the same transaction could also be fairly described as a repurchase agreement or by some other label that superficially sets it apart from a lending transaction.

---

51 Financial Stability Board, *Securities Lending and Repos: Market Overview and Financial Stability Issues* 6 (Apr. 2012), https://www.fsb.org/wp-content/uploads/r_120427.pdf.

52 Release at 69,843-44.

V. THE SEC SHOULD CONSIDER THE PROPOSAL TO BE MERELY A FIRST STEP IN ADDRESSING ISSUES RAISED BY SHORT-SELLING

As pointed out above, one of the ways in which the Proposal will contribute to financial stability is by enabling greater transparency into the potentially destabilizing practice of short-selling. However, the Proposal represents a necessary, but not sufficient, step in addressing the shortcomings in current regulations around the practice of short-selling. As has been recommended by Better Markets, the SEC must take further action to address these shortcomings, including requiring enhanced and more timely disclosure of short-selling activities, strengthening regulatory safeguards to address the potentially destabilizing effects of short-selling, and enhancing the operational integrity of the clearing and settlement system that facilitates short-selling.[53]

CONCLUSION

We hope these comments are helpful as the Commission finalizes the Proposal.

Sincerely,

Stephen Hall

Stephen W. Hall
Legal Director and Securities Specialist

Jason Grimes
Senior Counsel

Better Markets, Inc.
1825 K Street, NW
Suite 1080
Washington, DC 20006
(202) 618-6464

shall@bettermarkets.org
jgrimes@bettermarkets.org

http://www.bettermarkets.org/

---

53 *See generally* Better Markets, *Short Selling: 10 Recommendations for Improving the SEC's Regulatory Framework*, https://bettermarkets.org/wp-content/uploads/2021/07/Short-Selling-10-Recommendations-for-Improving-the-SECs-Regulatory-Framework.pdf.