



MODERN MARKETS
INITIATIVE

April 4, 2022

By electronic mail to rule-comments@sec.gov

Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-0609

Re: Short Position and Short Activity Reporting by Institutional Investment Managers 17 CFR Part 240, 242, and 249 (RELEASE NO. 34-94313; FILE NO. S7-08-22)

Dear Ms. Countryman:

Modern Markets Initiative (“MMI”), the education and advocacy organization devoted to the role of technological innovation in creating the world’s best markets, appreciates the opportunity to provide written comments to the U.S. Securities and Exchange Commission (the “SEC” or “Commission”) in connection with the “Short Position and Short Activity Reporting by Institutional Investment Managers 17 CFR Part 240, 242, and 249 (RELEASE NO. 34-94313; FILE NO. S7-08-22) (the “Proposal”).¹ MMI stands in broad support of global regulatory efforts to establish holistic, data-driven policies to best ensure the stability of the markets for all participants, and to offer tools for the advancement of secure savings and investment through innovation.

By way of background, MMI members collectively employ more than 2000 people in over 50 markets globally, and account for approximately 20 percent of daily trading volume in the US equity markets. MMI’s members are routinely engaged in providing liquidity across a variety of asset classes, and deploy automated trading technology systems to enhance efficiency of trading for retail and institutional investors.²

MMI believes that it is vital that the SEC have resources and access to data in order to be a strong cop on the beat. With respect to Section V of the Proposal, the “Proposed Amendment to “Regulation SHO to Aid Short Sale Data Collection,” MMI appreciates the SEC’s intent in establishing “buy to cover” provisions to provide additional context to the SEC regarding the lifecycle of short sales, including data on timing regarding short positions in a security. MMI agrees it is valuable for the SEC to have access to further data and transparency, for the purposes of surveillance,

¹ “Short Position and Short Activity Reporting by Institutional Investment Managers” 17 CFR Part 240, 242, and 249 [RELEASE NO. 34-94313; FILE NO. S7-08-22] at <https://www.sec.gov/rules/proposed/2022/34-94313.pdf> (See Section V, pages 59-67; and then footnote 89 on page 55).

² “A Report on Market Automation and Democratizing Markets: Narrowed Bid Ask Spreads” (June 2021) Kang, Wegner. <https://www.modernmarketsinitiative.org/reports-studies>

reconstructing market events, identification and investigations of any potentially abusive trading practices, among other important purposes.

However, MMI would like to express its concerns regarding significant interpretive and operational challenges to implementing the proposed “buy to cover” marking. We have done our best to analyze, gather information and submit comments within the abbreviated comment period of 30 days, noting this period overlaps with several other important proposed rulemakings by the SEC.

The below comments address, collectively, the SEC’s questions 15, 16, and 17 regarding “buy to cover.” MMI has two primary objections to this Proposal; and, depending on whether the Proposal is approved, numerous questions about the details.

MMI’s first concern with the Proposal is that it would double firms’ order marking compliance requirements by essentially forcing them to keep two separate position aggregations.³ The SEC states broker-dealers should already have the necessary mechanisms and procedures in place to comply with the marking requirements of Regulation SHO and should be able to continue to use the same or similar mechanisms to comply with Proposed Rule 205. However, a broker-dealer’s determination of whether to mark a sale order as “long,” “short,” or “short exempt” pursuant to Rule 200 relies on position aggregation of Sell orders on a net basis. Rule 205 would require firms to establish a new mechanism for tracking Buy orders on a gross basis.⁴ This would be expensive and complicated to implement, is very likely to cause operational confusion, and there are specific circumstances in which such an architecture for data collection is untenable.

MMI recommends that a refined Proposal seek to use a simple “mirror image” of the existing short sell marking rules and guidelines. This would allow firms to use the same position aggregations they already have, and simply apply them to Buy orders as well as Sell orders. (MMI notes that even if this approach is adopted, there will be further questions about the implementation, such as the treatment of open orders in position aggregation, and regardless, the new order marking requirement would demand firms adjust front-end systems, order entry and routing applications, and reporting systems.)

MMI’s second concern is that the Proposal appears to put the burden on a broker-dealer to look into its institutional customers’ accounts to determine the Buy order marking. The general order marking requirement of Regulation SHO requires institutions to ensure that orders are appropriately marked, and broker-dealers must ensure it is reasonable to rely on a customer’s representations before transmitting the orders. We assume that executing broker-dealers should likewise be able to reasonably rely on representations from customers concerning “buy to cover” purchase transactions effected for such customers. MMI recommends that this be made explicit.

³ (See page 55, footnote 89)

⁴ We note in footnote 89, the Proposal indicates a desire to make the implementation of this rule easier for firms; but the effect is the opposite.

The Commission considered, but dismissed, proposing to require a broker-dealer to look across multiple accounts held by the customer within the broker-dealer itself and/or to its customer's account(s) held at other firms. However, even if the broker-dealer only has to determine whether a purchase is being made for an account it holds that has an open short position, it is not reasonable to expect a broker-dealer to know the real-time position of an institutional client. Institutions may (and usually do) use multiple executing brokers, and the results of their intraday trades may not be known to the carrying broker in real-time. Third-party executing brokers who do not carry their clients' account(s) have no knowledge of an institution's positions (other than the sell long/short marking on orders as received). One key reason that institutions use multiple executing brokers is specifically to limit the information that any one broker-dealer may possess regarding the institution's strategies and positions. We would therefore question the value of any information provided by the "buy to cover" marking unless broker-dealers are explicitly able to rely on customer representations and marking of their positions.

Regardless of the final rule's treatment of the questions above, MMI would like to point out that there will remain various, more detailed questions about what to implement. One may look at the numerous "Reg SHO FAQs" regarding order marking as a guide – but the Proposal is silent on many of these issues. For example (but not intended to be exhaustive):

- How should open Buy orders be treated in the position aggregation for "buy to cover" marking?
- Should a market maker's Buy quotes be marked "buy to cover", or should be excluded from the scope of the rule?
- Should an entity's long positions in Call options, or open orders to purchase Call options, be included in the position aggregation for "buy to cover"?

Conclusion

MMI supports the overall objectives of the Proposal, however the implementation of the Proposal raises questions of additional complexity, cost, and burden which should be further reviewed and streamlined before a final rule is implemented.

Thank you for your consideration.

Very truly yours,



Kirsten Wegner
Chief Executive Officer
Modern Markets Initiative

cc: Haoxiang Zhu, Director, Division of Trading and Markets, SEC