

January 7, 2022

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

Re: File No. S7-18-21; Reporting of Securities Loans, RIN 3235-AN01, 86 Fed. Reg. 69802 (Dec. 8, 2021)

Dear Ms. Countryman:

The Depository Trust & Clearing Corporation (“DTCC”) appreciates the opportunity to comment on the above-captioned proposal by the Securities and Exchange Commission (“Commission”) regarding the requirement to report certain information (“10c-1 information”) related to securities lending transactions to a registered national securities association (“RNSA”) under proposed Rule 10c-1 (the “Proposal”).¹ In our view, the Proposal reflects a thoughtful approach to increase transparency and oversight of the growing securities lending market.

Nonetheless, we recommend that the Commission make certain clarifications and adjustments to the Proposal to further its objectives and limit ambiguity. In particular, we recommend that the Commission make clear in the final rule that a registered clearing agency’s provision of traditional securities depository, central counterparty, or incidental services, without more, does not give rise to a reporting obligation. As we describe in greater detail below, providing these services does not reflect new market activity, place the clearing agency in a position to provide the 10c-1 information, or affect material economic terms of a transaction. Accordingly, requiring the clearing agency to assume the obligations of traditional lending agents for providing such services would misplace the burden of responsibility and result in double reporting.

For similar reasons, the Commission should make clear that a clearing agency’s processing of a securities loan transaction, including through novation and netting, does not constitute a modification or a new transaction for reporting purposes. Such processing does not constitute new market activity or modify the material economic terms of the transaction, which the parties will have already reported. As a result, imposing a second reporting obligation on the parties would simply serve to disincentivize clearing, create confusing data, and impose unnecessary burdens.

Lastly, the Commission should leave open the possibility of clearing agencies one day working with their participants to develop reporting systems that would allow for a clearing agency to serve as a reporting agent.

¹ Reporting of Securities Loans, 86 Fed. Reg. 69802 (Dec. 8, 2021).

I. Background: DTCC's Activities in Securities Lending

DTCC is the parent company of The Depository Trust Company (“DTC”) and the National Securities Clearing Corporation (“NSCC”). DTC and NSCC are both registered with the Commission as clearing agencies and provide critical functions to the U.S. securities markets.

A. *DTC: a Securities Depository that Provides Custody, Settlement, and Incidental Services for its Participants.*

DTC is a central securities depository that performs a number of services for its participants. Most notably, DTC holds securities on behalf of its participants and effects transfers between participant accounts by book entry, including to facilitate the settlement of securities lending transactions. DTC also provides incidental services to its participants based on the securities held in their accounts. These services include announcing details of upcoming corporate events and providing participants with information about their entitlements; accepting and acting on their instructions with respect to their securities positions; and collecting, allocating, and reporting payments across various corporate action event types, including distributions, redemptions, and reorganizations. By virtue of its provision of these services, DTC is considered a “securities intermediary” under the Uniform Commercial Code.²

Importantly, DTC is not a party to any purchases, sales, or loans of securities between its participants, does not identify, guarantee, negotiate, or execute any such transactions for its participants, and does not otherwise act as an agent of its participants in connection with such transactions. Rather, its services are limited to custody, settlement, and related incidental services. Therefore, DTC is not informed of, and is not otherwise privy to, the terms of securities lending transactions between its participants for which it effects the necessary securities transfers.

B. *NSCC: a Central Counterparty that Provides Clearing, Settlement, Risk Management, and Related Services.*

NSCC is a central counterparty that provides clearing, settlement, risk management, and a guarantee of completion for broker-to-broker trades involving equities, corporate and municipal debt, American depository receipts, exchange-traded funds, and unit investment trusts.

NSCC is in the process of establishing a new Securities Financing Transaction Clearing Service (“SFT Service”) to provide central clearing for overnight loans of certain equity securities.³ Participants in the SFT Service will settle the “on-leg” of each securities loan (i.e., the initial transfer of securities by the lender to the borrower against cash collateral) bilaterally and submit the “off-leg” (i.e., the return of the securities and collateral) to NSCC for novation. For certain transactions, NSCC and DTC may also facilitate the settlement of the on-leg of the transaction.

If the off-leg of the transaction satisfies certain requirements, NSCC will accept and novate it, which novation will consist of the termination of the deliver, receive, and related payment obligations under the transaction and their replacement with equivalent obligations between NSCC and each original counterparty to the transaction. Following novation, NSCC will be responsible for settling the off-leg of the transaction with both the borrower and the lender and will risk manage the transaction accordingly. NSCC will typically settle the off-leg of the transaction through DTC. In order to facilitate this settlement, the counterparties will have provided NSCC with authority to act as their agent in connection with the settlement of the transaction by sending instructions to effect the necessary transfers of cash and securities.

NSCC believes the SFT Service will significantly enhance the stability of the securities lending market by, among other things, (i) reducing counterparty credit risk by replacing the original parties to each trade with a central counterparty subject to comprehensive regulation, (ii) reducing the risk of market disorder and fire sales by centralizing responsibility for liquidating a defaulting party's positions in a single organization, and (iii) improving market access and increasing market liquidity. However, much like DTC, NSCC will not identify, negotiate, or

² U.C.C. § 8-102(a)(14).

³ See SEC, Notice of Filing of Proposed Rule Change to Establish the Securities Financing Transaction Clearing Service and Make Other Changes, SR-NSCC-2021-010 (Aug. 5, 2021), available at <https://www.sec.gov/rules/sro/nscc.htm#SR-NSCC-2021-010>.

execute securities loans on behalf the parties; it will simply novate previously executed transactions that are submitted to it.

II. Recommended Changes to the Proposal

A. *The Commission Should Confirm that a Registered Clearing Agency's Provision of Traditional Depository and Incidental Services Does Not Make the Agency a "Lending Agent" or "Intermediary."*

Proposed Rule 10c-1(a)(i)(A) would provide that a "bank, clearing agency, broker, or dealer that acts as an intermediary to a loan of securities (lending agent) on behalf of a person that owns loaned securities (beneficial owner)" must provide the 10c-1 information.⁴ Although the Proposal does not define the term "intermediary," the Commission notes that certain clearing agencies are offering to act as such.⁵

The Commission should make clear that a registered clearing agency's provision of traditional depository and incidental services does not give rise to an intermediary or lending agent relationship. As noted above, although DTC is considered a "securities intermediary" under New York commercial law given its custody, settlement, and related services, it does not enter into transactions with or on behalf of participants or identify, negotiate, execute, or guarantee obligations arising under such transactions. As a result, it does not have the 10c-1 information or a clear mechanism to obtain such information.

Further, depository activities and related incidental services do not affect supply or demand in the securities lending market, the pricing of securities lending transactions, or other relevant data regarding the securities lending market. As a result, imposing reporting obligations on securities depositories in connection with such activities would impose a heavy burden without serving the interests the Proposal is meant to further. Thus, we request that the Commission confirm that a registered clearing agency, such as DTC, would not have reporting obligations under the new Rule 10c-1 merely for performing traditional depository and incidental services.

B. *The Commission Should Confirm that a Registered Clearing Agency's Provision of Central Clearing and Incidental Services Does Not Make the Agency a "Lending Agent" or "Intermediary."*

Although Proposed Rule 10c-1 does not define "intermediary," the Commission indicates in the proposal that the "clearance of [] securities lending transaction[s] by itself" would not give rise to an intermediary or lending agent relationship.⁶ We agree and urge the Commission to make express in the final rule that a registered clearing agency's provision of central counterparty services, including novation, processing, settlement, netting, and incidental services, does not render the clearing agency a lending agent or intermediary.

The Proposal places the obligation of reporting on "lending agents" because they "are in the best position to know when securities have been loaned from the portfolios that the lending agent represents."⁷ The same is not true for a central counterparty like NSCC. As noted above, the proposed SFT Service would only be available for a securities loan that two counterparties have already negotiated and executed away from NSCC. NSCC will only process the transaction after the parties have submitted it to NSCC, which may in some cases be after the 15 minute reporting window. Even after NSCC receives the transaction, it will typically not have all of the 10c-1 information, such as the time the transaction was originally effected, the platform on which it was effected, and how many securities are available to lend. Moreover, the information that NSCC does have will be information received from third parties, rather than information of which it has first-hand knowledge or that it has independently compared and verified. Accordingly, the only way NSCC would be able to satisfy any reporting obligation would be to develop new data collection, comparison, and processing systems and impose reporting obligations on its members. This would dramatically increase the burden of information collection and processing for NSCC and its

⁴ 86 Fed. Reg. at 69851.

⁵ 86 Fed. Reg. at 69809, n. 78.

⁶ 86 Fed. Reg. at 69809, n. 78; *see also* 86 Fed. Reg. at 69811 ("if the clearing agent cleared a securities lending transaction but did not act as an intermediary on behalf of a beneficial owner for the loan of securities, the clearing agency would not be responsible for providing the 10c-1 information to an RNSA").

⁷ *See* 86 Fed. Reg. at 69809.

members and impose an unnecessary impediment to the prompt clearance and settlement of securities lending transactions.

Thus, we request the Commission confirm and clarify that registered clearing agencies, such as NSCC, would not become "lending agents" or "intermediaries" under the new Rule 10c-1 with respect to cleared securities loans by virtue of having accepted such loans for clearing.

C. The Novation and Processing of a Securities Loan by a Registered Clearing Agency Should Not be Considered a New Loan or a Modification or Otherwise Give Rise to a Reporting Obligation.

Like many central counterparties, NSCC will clear and settle securities loans under the proposed SFT Service by novating, processing, and, in some cases, netting obligations under the transactions. These services do not reflect new market activity or affect the core economic terms of the transaction and therefore should not trigger a reporting obligation.

As a technical matter, the novation of a securities lending transaction results in the termination of the deliver, receive, and related payment obligations under the existing transaction and their replacement with obligations between NSCC and each original counterparty to the transaction. However, such "new" obligations do not represent new market activities – they are not indicators of any increased or reduced demand for, or the availability, price, or other data regarding, the securities subject to the transaction. Novation is simply the legal mechanism through which NSCC guarantees to each counterparty the performance of the obligations under a transaction that the counterparties already negotiated and executed away from NSCC and that was already subject to a reporting obligation.

Accordingly, requiring NSCC or the counterparties to report the novation would not reveal relevant information regarding the securities or the lending market. Rather, such a requirement would likely serve to cause confusion, as the resulting data could suggest the existence of greater market activity than actually exists. It may even disincentivize clearing, since it would impose greater reporting requirements for the cleared trades than for the uncleared trades.

Thus, we request the Commission make clear that the novation and processing of a securities lending transaction by a registered clearing agency does not give rise to a new loan or the modification of an existing loan subject to reporting under Rule 10c-1.

D. Registered Clearing Agencies Should be Permitted to Act as Reporting Agent.

For the reasons discussed above, we ask the Commission to make clear that clearing agencies are not intermediaries or lending agents or otherwise subject to reporting obligations on account of their provision of traditional depository, central counterparty, or incidental services. At the same time, however, the Commission should not foreclose the ability of clearing agencies and their participants to develop systems and procedures that would allow clearing agencies at some time in the future to serve in the role of a reporting agent.

Proposed Rule 10c-1 would permit a party subject to a reporting obligation to enter into an agreement with a broker or dealer to act as a reporting agent. We agree with the Commission that permitting the use of reporting agents to report 10c-1 information will "ease burdens on Lenders, including lending agents, that do not have or do not want to establish connectivity to the RNSA."⁸ However, we do not believe it is necessary to limit the scope of entities that may be reporting agents exclusively to broker-dealers. Clearing agencies are also subject to comprehensive regulation and examination by the Commission as well as a number of other regulators. Moreover, clearing agencies have experience acting as financial market infrastructures and performing functions as such. Accordingly, although we caution against imposing obligations on clearing agencies that would be duplicative and burdensome, we recommend that the Commission expand the scope of potential reporting agents to include registered clearing agencies and thereby provide market participants with the flexibility to develop new and efficient reporting systems and respond to any future market developments.

⁸ 86 Fed. Reg. at 69810.

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We appreciate the opportunity to comment on the Proposal and the Commission's consideration of our views. We look forward to continuing dialogue with the Commission regarding the securities loan reporting regime. If you have questions or would like additional information, please contact me at [REDACTED].

Very truly yours,



Michele Hillery

cc:

Honorable Gary Gensler, Chairman, Securities and Exchange Commission

Honorable Hester M. Peirce, Commissioner, Securities and Exchange Commission

Honorable Elad L. Roisman, Commissioner, Securities and Exchange Commission

Honorable Allison Herren Lee, Commissioner, Securities and Exchange Commission

Honorable Caroline A. Crenshaw, Commissioner, Securities and Exchange Commission

Ms. Theresa Hajost, Special Counsel, Office of Trading Practices, Division of Trading and Markets, Securities and Exchange Commission

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