Managed Funds Association
The Voice of the Global Alternative Investment Industry
Washington, D.C. | New York

January 7, 2022

Via Website

Ms. Vanessa Countryman
Secretary
United States Securities and Exchange Commission
100 F Street NE
Washington, D.C. 20549

Re: Reporting of Securities Loans; File Number S7-18-21

Dear Ms. Countryman:

Managed Funds Association ("**MFA**")[1] submits these comments in response to the Securities and Exchange Commission's ("**Commission**") proposal on rule 10c-1 ("**Proposed Rule**").[2] We appreciate the Commission's efforts through the Proposed Rule to enhance transparency related to securities lending activities and to reduce information asymmetries between financial market participants regarding those activities, with the intended purpose of reducing costs for investors, which would include MFA's members. We are strongly concerned that the Proposed Rule is misguided in its attempt to develop a consolidated tape with respect to two very different types of securities lending activities, referred to by the Commission as the "Wholesale Market"[3] and the "Retail Market,"[4] which are governed by different contractual frameworks.

MFA is concerned that commingling Wholesale Market and Retail Market transactions will result in information that is misleading and not particularly useful to investors with respect to providing investors with actionable information about the prevailing rates and availability to borrow securities. At the same time, we are strongly concerned that transaction-by-transaction financing data even in anonymized form would provide the market with sufficiently detailed

[1] MFA represents the global alternative investment industry and its investors by advocating for regulatory, tax, and other public policies that foster efficient, transparent, and fair capital markets. MFA's more than 150 member firms collectively manage nearly $1.6 trillion across a diverse group of investment strategies. Member firms help pension plans, university endowments, charitable foundations, and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time. MFA has a global presence and is active in Washington, London, Brussels, and Asia.

[2] Reporting of Securities Loans, Exchange Act Release No. 93613 (Nov. 18, 2021), 86 Fed. Reg. 69,802 (Dec. 8, 2021) (the "**Proposing Release**").

[3] Transactions between lenders, lending agents, and broker-dealer borrowers.

[4] Transactions between broker-dealers and end-borrowers.

information as to allow market participants to reconstruct and/or reverse-engineer investment and trading strategies, leading to situations similar to the GameStop and AMC market events.[5]

MFA members are designated Retail Market because they are reliant on their broker-dealers to borrow securities under the umbrella of their brokerage account agreements to facilitate settlement obligations with respect to short sales. Transaction-by-transaction reporting of Retail Market activity, and even frequent aggregate transaction reporting, of such financing activity would effectively become a proxy for disclosure of actual short selling activity and short positions. Such disclosure would in turn increase the costs and risk associated with engaging in short selling.[6] The Proposed Rule is likely to reduce overall short selling activity, which would lead to:

- Impaired ability of investors to pursue fundamentally-driven actively-managed investment strategies (with material knock-on impacts to the efficiency of passive/index-based investing);
- An increase in imitative behavior (*i.e.*, uninformed copy-cat type investing) and herd behavior;
- A decrease in the economic incentives for individuals to engage in the fundamental research necessary to root out poor corporate governance, potential fraud, or simply to express that a company's stock is overvalued;
- An increase in the potential for manipulative activities (*e.g.*, short squeezes); and
- Diminished market quality from less efficient price discovery, inefficient capital allocation, lower trading volumes, higher market volatility, higher transaction costs (wider bid/offer spreads), and lower market efficiency.

Policies that enhance transparency should be carefully designed and analyzed to ensure that they serve the interests of investors and the markets overall. Unless adequately tailored, policies that require the contemporaneous public disclosure of individual investments or transactions in illiquid or non-fungible markets, will deter investment research and shareholder engagement because investors' investment and trading strategies will be instantly exposed to the public, which in turn allows other market participants to react in ways that are unfavorable to the original investor (*e.g.*, copycatting, trading against the investor, etc.). Such policies impair the ability of investors to effectively engage in actively managed (versus passive) investment strategies which are crucial for price discovery, market efficiency and liquidity, capital formation, and overall market resiliency.

MFA respectfully urges the Commission to carefully analyze whether its proposals, including this one, would enhance transparency in a manner that protects investors, maintains fair, orderly and efficient markets, and facilitates capital formation. The Proposed Rule imposes

[5] *See, e.g.,* Melvin Capital, Gamestop and the road to disaster, FT, February 6, 2021, available at: https://www.ft.com/content/3f6b47f9-70c7-4839-8bb4-6a62f1bd39e0.

[6] *See* Proposing Release at 136-138.

unreasonably burdensome disclosure obligations that would not achieve these goals and instead would harm investors, impair fair, orderly and efficient market activity and impede capital formation.[7]

Finally, we are of the view that the Proposed Rule will saddle market participants with the costs of creating and maintaining an entirely new infrastructure for loan data reporting and dissemination. Those costs will greatly exceed any benefits that may come from the Proposed Rule and will certainly be borne by investors including, mutual funds, pension funds, and university endowments, which receive income from lending out their securities holdings. MFA estimates that public pension funds alone earned over $1 billion in 2020 from securities lending fees.[8]

I. Executive Summary

MFA respectfully urges the Commission to revise the Proposed Rule in a manner that would enhance securities lending transparency without harming the ability of investors to carry out their investment strategies.[9] MFA recommends that the Commission:

- Adopt a Final Rule Limited to Wholesale Securities Lending Activities, Providing Aggregate Data on an End-of-Day Basis.[10] We believe that focusing on the Wholesale Market would best capture the information that is most consistent with the rulemaking objectives outlined in Section 984(b) of the Dodd-Frank Act. This information is already partially

[7] The Proposed Rule would create a sweeping new data reporting and public dissemination regime applicable to persons who engage in securities lending activities. Specifically, Proposed Rule 10c-1 would require that any person that loans a security on behalf of itself or another person to report the material terms of those securities lending transactions and related information regarding the securities the person has on loan and available to loan to a registered national securities association ("RNSA"). Currently, the Financial Industry Regulatory Authority, Inc. ("FINRA"), a self-regulatory organization that regulates broker-dealers, is the only entity that comes within the meaning of an RNSA. The Proposed Rule would then, in turn, require that FINRA make available to the public certain information concerning each transaction and aggregate information on securities on loan and available to loan. The Proposed Rule also would require that certain securities lending transaction participants disclose information to FINRA regarding counterparties to a securities lending transaction, portfolio holdings, and otherwise grant to FINRA supplemental rulemaking authority over securities lending activities and impose requirements on persons FINRA was never intended to regulate.

[8] MFA estimate based on flow of funds data and an average 0.016 percent return on securities lending.

[9] We regret that the Commission has denied our request to provide an extension to the 30-day comment period for the Proposed Rule. *See* Industry request for an extension, available at https://www.sec.gov/comments/s7-18-21/s71821-9402961-262828.pdf. The Proposed Rule introduces a significant new regulatory framework with incredible operational complexities for a host of regulated and un-regulated securities lending participants. We are concerned that a 30-day comment period does not provide enough time by which securities lending participants can meaningfully evaluate and consider the Proposed Rule's ramifications, and violates the spirit of administrative law. We are concerned that a hastily adopted final rule under Section 984 that lacks a thorough evaluation by the public and the Commission will result in unnecessary costs and harm to investors and the market.

[10] *See* Proposing Release, 86 Fed. Reg. at 69,805 (referring to the "Wholesale Market" as loans from lending programs to broker-dealers).

collected by private data vendors today, and consists of true securities lending transactions, as opposed to the varied lending activities between prime brokers and their customers, such as stock loans made to facilitate customer short sale transactions.

- The Proposed Rule Should Require Dissemination of Aggregated Transaction Data, Including Aggregate Blended Rate Information, Rather Than Transaction-By-Transaction Data, on a Weekly Basis. We believe aggregate blended rate information that is disseminated on a weekly basis will be more useful information to investors without having adverse repercussions to other market segments. Similarly, aggregate trend information will better serve investors due to the non-fungible nature of the securities lending market. Investors do not negotiate each transaction over the course of the day, but rather review overarching contractual terms infrequently as well as fees or rebates periodically based on broad trends in the supply and demand for specific securities, the credit risk of the entities, and other general market conditions.

- Exclude Portfolio Holdings from Reporting and Dissemination Requirements as it Would Provide Misleading Information of Available Securities and Could Result in Harm to Investors. Requiring all securities in a portfolio eligible for lending to be reported would provide misleading information to the market and potentially put lenders and end-borrowers at risk. Lenders include pension funds, mutual funds, insurance companies and other institutional investors. While a lender's portfolio holdings may be eligible securities for lending, they are unlikely to be "available to lend" at all times. Brokerage firms and other intermediaries who manage securities lending programs on behalf of lenders do so within contractually established guidelines set by the lenders. Simplistic measures of available supply will result in misleading information.

- The Commission Should Explicitly Require an RNSA to Maintain Strict Confidentiality and Information Security Standards. The confidential and proprietary nature of the information that an RNSA is required to collect requires a heightened level of specified information security rather than simply a reference to policies and procedures as provided for in the Proposed Rule.

II. Background

Securities lending activities play a critical role in supporting efficient market functioning of the U.S. securities markets; and can be categorized into Wholesale Market and Retail Market activities. Importantly, Wholesale Market and Retail Market transactions are governed by very different structural and contractual frameworks.

Wholesale Market activities are subject to arm's length agreements on the borrowing of securities between lenders, lending agents and broker-dealer borrowers. In certain circumstances, lenders may engage in exclusive or semi-exclusive arrangements[11] with specific borrowers that may be subject to well-tailored contractual terms and conditions. In contrast,

[11] For instance, some borrowers may purchase the rights to a specific lending portfolio.

Retail Market activities rely on broker-dealers to locate, arrange, and facilitate short selling, and are governed by client-brokerage account agreements.

Rates of fees in the Retail Market (*i.e.*, between broker-dealers and their clients) are based on a myriad of factors, determined by: (i) supply and demand; (ii) counterparty/client credit; (iii) the volume of a client's borrow business; (iv) whether a borrower/client has exclusive access to a lender's portfolio; (v) the expected term of the client's borrow; (vi) dealer exposure if a client defaults; (vii) a dealer's ability to cover end-of-day failures to deliver; (vii) corporate actions; (viii) dividend requirements (as applicable to foreign securities); and (ix) other prime brokerage services being provided, such as clearing, settlement, custody, asset servicing and financing. Broker-dealers oftentimes incorporate these factors into an internal ratings-based approach to make rate determinations that are subsequently used when negotiating a securities lending contract with a borrower and when proposing specific rates for transactions each day.

As such, so-called "retail securities lending transactions" are not conducted in a competitive pre-loan quote environment against a pool of ready liquidity providers. Many investors borrow from broker-dealers with whom they have contractual relationships because of the overall suite of services they are receiving and the significant effort necessary to set up the documentation and operational workflows. Other investors may "shop" for rates and even negotiate contracts with broker-dealers that establish key parameters and then on a daily basis compare proposed rates for specific securities among their broker counterparties. Securities borrowed may be returned at any time for whatever reason including rejection of the fees being charged. Actual borrows will ultimately reflect the overall investment activities of the borrower and these contractual arrangements, and not merely the best rates generally available in the market. Conversely, clients will usually borrow from broker-dealers with whom they have contractual relationships given most of their borrow needs are considered "general collateral" or easy-to-borrow and rates do not vary widely. This activity does not lend itself to a best bid and offer system.

A consolidated tape disseminating commingled Wholesale Market transaction data, including exclusive arrangements which are likely to display discounted rates, with non-fungible Retail Market transactions, will provide investors with information that is difficult to discern for purposes of comparing available securities to borrow and borrow rates. As a result of this complexity, a consolidated tape for securities lending is unlikely to enhance competition nor provide useful information to investors on securities available to borrow and their borrow rates.

While the detailed transaction-by-transaction data may not be helpful for purposes of shopping for lower rates, it would provide enough information to allow the market to glean valuable information regarding the investment and trading strategies of market participants and enable sophisticated market participants to reverse-engineer and reconstruct trading strategies, short positions, or holdings, resulting in significant harm to investors. In particular, market participants may use detailed consolidated tape information as a proxy for short selling, and in turn, use such information to deter and to impede the ability of investors to engage in short-selling. Short selling, as the Commission recognizes significantly contributes to market liquidity, price discovery, and market efficiency.[12]

[12] Proposing Release at 69839. See also Exchange Act Release No. 61595, 75 Fed. Reg. 11232, 11235 (March 19, 2010).For example, the Commission has long recognized that short selling provides the market

III. Comments & Recommendations

A. The Commission Should Adopt a Final Rule Providing Aggregate End-of-Day Data on Wholesale Securities Lending Activities.

Rather than proceed with the current proposal, the Commission should amend the Proposed Rule to require reporting and dissemination of securities lending information only with respect to lending activity in the "Wholesale Market" among beneficial owners/lenders, lending agents, and broker-dealer borrowers. MFA believes that the goals of Section 984 are best served by focusing on the Wholesale Market, as those transactions are more likely to be at arm's-length and fungible, and the data collected will be a more useful benchmark to market participants.

In the Proposing Release, the Commission provides an overview of the securities lending activities and distinguishes between the Wholesale Market and the Retail Market.[13] What is clear from the Proposing Release is that the Wholesale Market really serves as the central hub for securities lending activities, and because the activities are instrumental to overall securities lending activities, we believe that the Commission should focus its efforts on wholesale lending activities. This information is already partially collected by private data vendors today, and consists of true securities lending transactions, as opposed to the varied trading activities between prime brokers and their customers classified by the Commission as the "Retail Market."

On this point, we believe and agree with the Securities Industry and Financial Markets Association ("SIFMA") that only true securities lending transactions – *i.e.*, made pursuant to a written securities lending agreement and recorded on a broker-dealer's books and records as a borrow/loan – should be reportable under the Proposed Rule.[14] This would also exclude short arranged financing in connection with prime brokerage activities resulting in short positions. It is

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with important benefits, including the following: (i) market liquidity is often provided through short selling by market professionals, such as market makers and block positioners, who offset temporary imbalances in the buying and selling interest for securities; (ii) short sales effected in the market add to the selling interest of stock available to purchasers and reduce the risk that the price paid by investors is artificially high because of a temporary imbalance between buying and selling interest; and (iii) short selling can contribute to the pricing efficiency of the equities markets, i.e., market participants who believe a stock is overvalued may engage in short sales in an attempt to profit from a perceived divergence of prices from true economic values. For MFA members engaged in equity strategies, short selling is an integral component of prudent risk management.

[13] *See* Proposing Release, 89 Fed. Reg. at 69,831(referring to the "Retail Market" as loans from a broker-dealer to the end borrower).

[14] *See* SIFMA letter to the SEC on Reporting of Securities Loans; File No. S7-18-21, on January 7, 2022 ("SIFMA Letter") (stating that only securities lending transactions between unaffiliated counterparties that are made pursuant to a written securities lending agreement and recorded on a firm's books and records as a borrow/loan should be reportable under the Proposed Rule).

important to note that short sale transactions are not documented or booked as a securities loan between the parties.[15]

Finally, we are of the view that attempting to cover the Retail Market within the scope of this specific proposal would turn a securities lending reporting regime into a proxy for short sale disclosure, which is intended to be addressed under a separate statutory section (*i.e.*, Section 929X of the Dodd Frank Act). While the Proposed Rule acknowledges the many benefits of short selling activities, including enhancing liquidity and price efficiency,[16] the Commission then incorrectly argues that the Proposed Rule will reduce the cost of short selling and facilitate more short selling activity. Instead, the Proposed Rule is likely to reduce overall short selling activity and thereby harm U.S. capital markets. In particular, signaling to the market that a short selling position is being established in a specific security would make it more costly to continue to build short positions and thus inhibit market participants from doing so.

As noted above, the Proposed Rule is likely to reduce overall short selling activity, which would lead to:

- Impaired ability of investors to pursue fundamentally-driven actively-managed investment strategies (with material knock-on impacts to the efficiency of passive/index-based investing);
- An increase in imitative behavior (*i.e.*, uninformed copy-cat type investing) and herd behavior;
- A decrease in the economic incentives for individuals to engage in the fundamental research necessary to root out poor corporate governance, potential fraud, or simply to express that a company's stock is overvalued;
- An increase in the potential for manipulative activities (*e.g.*, short squeezes); and
- Diminished market quality from less efficient price discovery, inefficient capital allocation, lower trading volumes, higher market volatility, higher transaction costs (wider bid/offer spreads), and lower market efficiency.

In addition, and as we have alluded to above, the Proposed Rule conflates the usefulness of data as between the Wholesale Market and the Retail Market. While the scope of information and reporting timeframes in the Proposed Rule do not provide useful information to Wholesale Market participants, it would simply create confusion in the Retail Market and provide enough information for other market participants to reverse engineer investment and trading strategies.

[15] *Id.* (explaining that the terms governing any resulting short positions are typically governed by a brokerage account agreement and the U.S. margin rules as opposed to being governed by or subject to a written securities lending agreement).

[16] Proposing Release, 86 Fed. Reg. at 69,839.

Given the nature of securities lending transactions in the Wholesale Market, transaction information should be disseminated in aggregate form, including aggregate blended rate information, no sooner than end-of-day, especially as many loans are not finalized until the end of the business day.

MFA is of the view that greater transparency through reporting and dissemination of securities lending information in the Wholesale Markets will best achieve the goals of Section 984 of the Dodd-Frank Act. Accordingly, MFA recommends that the Commission adopt a final rule that only requires reporting and dissemination of securities lending transactions in the Wholesale Markets. We urge the Commission to conduct a more fulsome cost-benefit analysis, and revise the proposal accordingly.

B. The Proposed Rule Should: Only Require Dissemination of Aggregated Transaction Data, Including Average Blended Rates on a Weekly Basis; Exclude Portfolio Holdings Information; and Impose More Prescriptive Confidentiality and Information Security Requirements on RNSAs.

MFA strongly believes that the Proposed Rule will not yield the benefits the Commission is seeking to achieve and is concerned that it will result in harmful unintended consequences to investors and the overall market. Specifically, we have strong objections to the dissemination of transaction-by-transaction data as we are concerned that dissemination of such information, even in anonymized form, would inadvertently lead to the disclosure of valuable information regarding the strategies of market participants and enable sophisticated market participants to reverse engineer trading strategies or holdings, and use such information to the detriment of investors. We urge the Commission to conduct a cost-benefit analysis of the impact of the Proposed Rule on trading strategies and the detrimental impact on investors, the markets, and capital formation.

In addition, we believe that the data collected by RNSAs, if not properly protected, could be subject to information security incidents that could disrupt the overall market if disclosed to unlawful actors. Should the Commission decide to proceed with the Proposed Rule, we strongly urge the Commission to modify it as detailed below.

i. Disseminate aggregate weekly data, including aggregate periodic blended rate information, rather than transaction-by-transaction data.

The Commission should modify the Proposed Rule to provide for dissemination of aggregate transaction data only on a weekly basis, including aggregate blended rate information, rather than transaction-by-transaction data. We believe weekly aggregate blended rate information that disregards outlier rates will be more useful information to market participants, as many contractual terms may not be finalized until the end of the day for individual securities lending. Similarly, aggregate trend information will better serve investors due to the non-fungible nature of securities lending activities. Importantly, dissemination of aggregate weekly information would minimize the likelihood of negative unintended consequences that could harm individual investors and impede the overall liquidity and robustness of securities lending transactions.

Paragraph (b) of the Proposed Rule would require that lenders and lending agents report to FINRA, within 15 minutes of a transaction's execution, certain information related to the transaction. Once received by FINRA, the Proposed Rule would require that FINRA assign each loan a unique transaction identifier and make the loan information and data elements publicly available as soon as practicable. In doing so, the Commission appears to be applying a trade reporting standard to securities lending transactions that is analogous to trade reporting in traditional equity and fixed-income securities. While we welcome and have long supported the real-time access to post-trade market data that is the hallmark of those *securities markets*, we do not believe there is equivalent rationale supporting this style of transparency for *securities lending activity*. The Commission suggests that securities lending activities can experience an improvement in transparency in the same way that the fixed-income markets did when FINRA implemented the Trade Reporting and Compliance Engine (TRACE).[17] We believe that the analogy to TRACE-like reporting is misguided because many types of lending activities are non-fungible and therefore entirely different to trading in fixed-income securities markets. A ticker-tape public dissemination of loan data on a trade-by-trade basis will not yield the same transparency benefits as it did for fungible products such as fixed-income transactions.

Instead, we are concerned that ticker-tape loan data will provide investors with misleading information that may not be reflective of the actual market or what is available to the Retail Market. In particular, disseminating rate information on a transaction-by-transaction basis can create confusion and paint a misleading picture of rate information. As rates in the Retail Market are based on many variables specific to a broker-dealer-client contractual relationship besides supply and demand, transaction-by-transaction rate information disseminated in ticker-tape fashion will not provide an accurate data point for investors but may actually result in a distorted representation of the actual market.

Moreover, we are greatly concerned that the dissemination of transaction-by-transaction data under the Proposed Rule will result in harmful unintended consequences for investors and the overall market. Transaction-by-transaction data will allow other market participants to reverse engineer investment and trading strategies and also make it difficult for investors to establish and manage short positions without being exposed to undue costs and risks. The Proposed Rule will impair the ability of investors to use short selling as an investment tool, leading to significant harm to investors and the markets.

Instead, the Commission should modify the Proposed Rule to provide aggregate weekly reporting and dissemination. Such data would provide market participants with a better picture of overall market movements, especially as this market does not operate based on a competitive pre-loan quote system on a best bid or offer basis. Aggregate weekly data would provide a better indication of longer-term trends for transactions of varying maturity dates. With respect to rate data, market participants would be better served with a weekly aggregate blended rate that excludes outlier rates (*i.e.*, all rates beyond a certain percentage from the aggregate median rate). Such data would provide market participants with a better indication of market movements and a benchmark for the generally prevailing loan rate. This is the type of information to which market participants are accustomed and will help ensure a stable market. We note that last year FINRA

[17] Proposing Release, 86 Fed. Reg. at 69,837.

requested comments on its short interest position reporting.[18] Consistent with our comments to FINRA on short interest position reporting, we think that weekly dissemination of aggregate data balances the interests of investors and the public. In fact, we believe that the approach taken by FINRA under Rule 4560 is a more appropriate point of reference that the Commission should consider when finalizing any rule on securities lending transactions.

Accordingly, MFA recommends that the Commission modify the Proposed Rule by requiring the dissemination of aggregate transaction data only on a weekly basis, including end-of-day aggregate blended rate information that excludes outlier rates.

ii. Exclude portfolio holdings from reporting and dissemination requirements as it would provide misleading information of available securities and could result in harm to investors.

The Commission should modify the Proposed Rule by excluding the reporting and dissemination of portfolio holdings (including, for these purposes, client long positions custodied in a prime broker margin account) as such information would provide misleading information to the market of available securities and could result in harm to investors through information leakage of their portfolios. While a lender's portfolio holdings may be eligible securities for lending, they are unlikely to be "available to lend" at all times.[19] For instance, footnote 110 of the Proposing Release and its accompanying text highlight instances where entire portfolios would have to be included even though there may otherwise be portfolio restrictions.[20] Thus, requiring all securities in a portfolio eligible for lending to be reported would provide misleading information to the market and potentially places lenders and end-borrowers at risk.

The Proposed Rule would require that data elements concerning securities available to loan and securities on loan be reported to FINRA. This reporting requirement would apply to any lender or lending agent that had a securities loan that was reported to FINRA, or for which there was an open loan about which it was required to provide information to FINRA. Under the Proposed Rule, FINRA would disseminate information about these securities available to loan. As drafted, the Proposed Rule would seemingly require that information regarding an entire portfolio of securities be reported to FINRA, irrespective of whether those securities are subject to a loan or whether there is a willingness to loan. MFA strongly disagrees with this provision of the Proposed Rule and believes that this requirement should be stricken from any rule in its entirety.

To the extent the Commission determines to proceed with the Proposed Rule in its current form, we believe that only data on actual securities lending transactions should be reported and disseminated. We are concerned that the requirement to disclose securities "available to lend" is misleading because it does not reflect a likelihood or requirement to lend. The securities lending market is not characterized by a system of competitive pre-trade quotes.

[18] Short Interest Position Reporting Enhancements and Other Changes Related to Short Sale Reporting, FINRA Reg. Notice 21-19 (June 04, 2021).

[19] For example, certain portfolios may be subject to exclusive lending arrangements. In other circumstances, lenders will make their portfolio available to lend, but are not likely to lend 100% of their securities at once for risk management purposes.

[20] Proposing Release, 86 Fed. Reg. at 69,817.

Rather, borrowing and lending discussions between a broker-dealer and its client, which we do not consider to be traditional securities lending activity, generally take place throughout the day, with rates normally determined on settlement of a client's short position. In a majority of the cases, general collateral and easy-to-borrow securities, to the extent needed, are borrowed externally on settlement date. Harder to borrow securities are often put on hold to be borrowed on settlement date. In most instances, securities are actually borrowed two business days after the equity short has occurred and borrowed or returned periodically over the life of the short position.

In addition, agent custodians for large lenders often designate securities to manage recall activities, credit restraints, upcoming securities deliveries or sales, corporate actions, or other events. Similarly, broker-dealers only have access (via rehypothecation) to client long portfolios based on funds borrowed (margin lending agreements), which any portion of the client's margined portfolio could conceivably be available to lend, even though brokers will only use securities that are needed or permitted by contract.[21] We agree with the position and reasoning taken by SIFMA in its letter that rehypothecating shares is traditionally done in a brokerage account and should not qualify as securities lending activities.[22] To the extent the Proposed Rule requests for such securities to be included, however, reporting what "could" be made available for loan would grossly inflate the optics of securities that are available.

Further, reporting portfolio holdings that have not been lent, such as with respect to broker-dealer customer margin accounts, can result in market participants reverse engineering investment or strategies and using such information to the detriment of those investors. Market participants could use this information to ascertain the long positions of those market participants since investment advisers are required to publicly disclose their prime brokerage relationships in Form ADV. In addition, the lending inventory of broker-dealers is largely composed of client's securities held as collateral. If enacted as proposed, a rule designed to increase transparency regarding the stock loan market would also have the effect of disclosing client long portfolios, which would surely be an unintended effect of the Proposed Rule.

In light of the securities lending market dynamics, reporting and disclosing full portfolio holdings can result in false understandings of supply and mislead investors on securities that are actually available to borrow. Moreover, lenders may be inclined to move securities positions to segregated accounts to avoid having to report holdings under the Commission's "available to lend" standard, which would further distort perceptions of supply.

Accordingly, MFA recommends that the Commission modify the Proposed Rule by excluding the reporting and dissemination requirement with respect to portfolio holdings.

[21] Prime brokers rely to a large extent on "internalization," *e.g.*, using one client's long position to source another client's short position.

[22] *See supra*, note 14.

iii. The Commission Should Explicitly Require an RNSA to Maintain Strict Confidentiality and Information Security Standards

The Proposed Rule would require an RNSA (*i.e.*, FINRA) to establish, maintain, and enforce reasonably designed written policies and procedures to maintain the security and confidentiality of confidential information that is submitted to FINRA. While MFA applauds the Commission's efforts to ensure that FINRA has policies and procedures in place to protect the confidentiality of information that is submitted to it, MFA believes that the Commission should require more prescriptive measures. For example, under Rule 613 of Regulation NMS (consolidated audit trail), each self-regulatory organization and RNSA subject to that rule is required to have system security features that ensure the security and confidentiality of information that address confidentiality, restrictions on use and access, information barriers, information security systems, user confirmation and access audits, among other things. Given the confidential and proprietary nature of some of the information that an RNSA will be collecting, MFA believes it is imperative that the Commission ultimately ensure that FINRA adopt more prescriptive confidentiality and information security in connection with any final rule.

iv. The Commission Should Limit the Proposed Rule's Scope to U.S. Securities

We note that the Commission should limit the scope of the Proposed Rule to U.S. securities, and also have a phased implementation schedule. On the former, MFA believes that applying the rule to all securities irrespective of the jurisdiction that principally regulates such offerings goes beyond what is intended by Section 984. We do not believe that Congress intended to capture extraterritorial lending activities when in enacted Section 984, and capturing such activities would not further the transparency goals of the Proposed Rule. Rather, it can inadvertently result in market participants segregating their foreign lending activities so as to limit U.S. assertion of jurisdiction activities.

v. The Commission Should Adopt a Phased Implementation

Finally, given the sweeping nature of the Proposed Rule, the costly operational requirements, and the potential for unintended consequences, we recommend that the Commission provide a phased-in approach of reporting requirements by reporting party, as well as a phased-in approach for the dissemination of data to minimize harm to investors. We believe that this approach would ensure that market participants are provided with accurate information that decreases the likelihood of harm to markets.

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We would be pleased to discuss our comments in further detail with the Commission staff. If you have any questions, please do not hesitate to contact the undersigned or the undersigned at [redacted].

Respectfully Submitted,

/s/ Jennifer W. Han

Jennifer W. Han
Executive Vice President
Chief Counsel & Head of Regulatory Affairs

cc: The Hon. Gary Gensler, Chair
The Hon. Hester M. Peirce, Commissioner
The Hon. Elad L. Roisman, Commissioner
The Hon. Allison Herren Lee, Commissioner
The Hon. Caroline A. Crenshaw. Commissioner
Mr. Haoxiang Zhu, Director, Division of Trading and Markets
Mr. David Saltiel, Deputy Director, Division of Trading and Markets
Ms. Jessica Wachter, Director, Division of Economic and Risk Analysis