WILSON-DAVIS & CO., INC.

November 20, 2020

VIA EMAIL
rule-comments@sec.gov

Mr. Timothy J. Cuddihy
Managing Director
DTCC Financial Risk Management

RE: Response to Comment Letters Filed with the Commission Regarding File No. SRNSCC-2020-003 – Exchange Act Release No. 88474 (the "Rule Filing") and SRNSCC-2020-802 – Exchange Act Release No. 88615 ("Advance Notice" and collectively with the Rule Filing, the "Filings") by National Securities Clearing Corporation

Dear Mr. Cuddihy:

Wilson-Davis & Co., Inc. submits these comments in response to the September 3, 2020, letter from the DTCC Financial Risk Management to the U.S. Securities and Exchange Commission (the "SEC") in response to the comments filed with the SEC on the rule change proposed by the National Securities Clearing Corporation (the "NSCC") respecting SR-NSCC-2020-003 (the "Proposed Rule").

We submitted comments regarding the Proposed Rule on July 29, 2020, and find that several of our concerns remain unaddressed, or in fact were dismissed by the NSCC's response. We wish to reinforce our concerns regarding this Proposed Rule below.

This Proposal Fails to Meet NSCC's Mandate

The NSCC's mandate is to "remove impediments to and perfect the mechanism of a national system for the prompt and accurate clearance and settlement of securities transactions, and, in general, to protect investors and the public interest…" Securities Exchange Act of 1934 ("Exchange Act"), Section 17A(b)(3)(F).

This Proposed Rule breaches this mandate in every way. The proposal adds impediments to the system, creates more complicated algorithms that slow the clearance process, burdens settlements, and harms investors, firms and small businesses, which is clearly not in the public interest. Our specific concerns are further outlined below.

The Proposal is Overcomplicated, Unclear, and Fails to Provide Remedial Guidance

The Proposal is Incomprehensible

In the assessment of the NSCC's observance of federal regulations, the Federal Monetary and Capital Markets Department stated that:

> NSCC is required to file with the SEC and make public all proposed rule changes. The information in each filing is required to be presented by NSCC in a *clear and comprehensible manner in order to enable the public to provide meaningful comment* on the proposal and for the SEC to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act. SEC staff also maintains an active dialogue with NSCC management"[1] (emphasis added).

This proposal however is overly technical and complicated and even for those of us in the industry is not clear enough for us to provide "meaningful comment." Further, the proposal continues the NSCC's practices of relying on undisclosed "models" and calculations that do not provide its members or the industry with sufficiently clear, unambiguous rules to guide compliant conduct. It appears that the NSCC's priority of maintaining "proprietary" information takes precedence of its obligation to provide clear and comprehensible proposals. Members of the industry cannot adequately comment on the Proposed Rule when it involves mystery algorithms, and undisclosed reasoning.

Rather than imposing increasingly burdensome monetary requirements, a more effective approach to mitigating NSCC risk would be to transparently disclose the models and calculations on which the NSCC relies so that they that could be used by individual firms and information/service providers to assist them in avoiding high-risk transactions and positions before they place any firm or the system at risk.

The NSCC's response in its September 3, 2020, letter included a flat rejection that the Proposed Rule is complex and unclear, stating that it is "clear enough to enable Members to determine the Member's Required Fund Deposit" as required by statute. It is perplexing that the NSCC confidently claims that the rule is "clear enough" for the members, while we, the members (including other institutions), are stating that it is not.

The Impact of the Proposal is Unclear

This proposal fails to meet the requirements of SEC Rule 17Ad-22(e)(23), which requires a clearing agency to: 1) provide sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in the covered clearing agency; and 2) publicly disclose relevant basic data on transaction volume and values.

---

[1] https://www.treasury.gov/resource-center/international/standards-codes/Documents/FSAP_DAR_Settlements_NSCC_Final_5%2011%2010.pdf

To our knowledge, the NSCC has not undertaken the requisite studies or gathered sufficient data to fully understand what the impact of the Proposed Rule will be, intended and unintended. This is a vital requirement given the NSCC mandate to "protect investors and the public interest" as per the Exchange Act. Our review of the results of the proposal points to immediate damaging effects to traders, small companies and their investors.

The NSCC's September 3, 2020, letter describes "three rounds of impact studies" and extensive daily "backtesting" as a demonstration of understanding the impact of the Proposed Rule. However, we have only received one impact study, which demonstrates a significant negative impact on our firm, followed by your September letter that utterly disregards our concerns regarding the significant negative impact on our services, our clients, small businesses, and the industry as a whole.

The Proposal is Unnecessary

The Proposed Rule does not fulfill the NSCC's obligations under the Exchange Act requiring the NSCC to:

> Effectively identify, measure, monitor, and manage its credit exposures to participants and those arising from its payment, clearing, and settlement processes, including by…maintaining sufficient financial resources to cover its credit exposure to each participant fully with a high degree of confidence; and
>
> Cover… its credit exposures to its participants by establishing a risk-based margin system that, at a minimum: 1) considers, and produces margin levels commensurate with, the risks and particular attributes of each relevant product, portfolio, and market; and 2) uses an appropriate method for measuring credit exposure that accounts for relevant product risk factors and portfolio effects across products;

Rules 17Ad-22(e)(4)(i) and Rule 17Ad-22(e)(6)(i) and (v).

The NSCC is Adequately Protected

We understand the NSCC's need for security and insurance against loss. However, the NSCC already has robust systems in place to adequately protect it against financial settlement risks and possible losses. Several of the proposed rules over the past several years have continued to add to the insurance burden on trades with no explanation of its supposed "appropriate method for measuring credit exposure." To our knowledge, the NSCC has not suffered a material settlement loss in recent memory, and yet continues to burden small businesses, traders and investors with Draconian efforts to mitigate imaginary risks. The margins that are being required do not appear to be "commensurate with the risks," particularly when the NSCC cannot point to examples of settlement losses that must be avoided.

The NSCC has shown no evidence to support the need for these proposed rules. In its September letter, the NSCC insists that the increased margin is necessary for its protection, consistent with statute, "backtesting" results, and impact studies, and yet it is unable to produce an example of suffered loss that would require the proposed change. As noted by a 2013 comment letter to proposed rule SR-NSCC-2012-810, "NSCC's proposal is specious as NSCC has never had to use the clearing fund deposits of a non-defaulting participant firm, even as the country recently experienced the steepest and most severe recession since the Great Depression."[2]

The Risk Could Be Eliminated by Changing the Settlement Rule

If the NSCC is truly concerned about risk protection, it is addressing the matter ineffectively and circuitously. The current NSCC practice is to assess margin deposits to cover the risk of loss resulting from market fluctuations between the trade date and the settlement date two days later. The risk could be addressed directly by modifying the settlement timeline.

If the NSCC proposed rules that would eliminate the two-day settlement cycle in favor of immediate, same-day electronic settlement, the market risk exposure would be eliminated. Instead of addressing the matter directly, the NSCC is consistently proposing complicated and burdensome rules that increase the insurance requirement, rather than decreasing—if not fully eliminating—the need for it.

The Proposal Hurts Small Companies and Their Investors

As discussed above, the proposal is unclear, complicated, and unnecessary. NSCC has again relied on undisclosed "models" and hidden calculations, so it is impossible to fully understand the impact of the proposed rules. However, based upon our review it appears that the proposal will directly harm small businesses.

The Proposal Dampens Capital Formation and Liquidity

The third leg of the SEC's three-part mission is "facilitating capital formation"[3] and there have been substantial effort, rules, committees and provisions put in place to bolster that goal.[4] This Proposed Rule, however, is contrary to the SEC's goal to promote investments in small companies.

As outlined in our July 29, 2020 comments, our nationwide retail customers are typically investors in small businesses that invest via private placements under Regulation D, Regulation A+ offerings, or crowd funding. These small businesses have limited access to large money center financial intermediaries to undertake underwritten public offerings on their behalf. The proposal undermines the

---

[2] https://www.sec.gov/comments/sr-nscc-2012-810/nscc2012810-1.pdf
[3] https://www.sec.gov/news/speech/miller-bolstering-capital-formation-040819
[4] https://www.sec.gov/page/small-business-capital-formation-advisory-committee

SEC's congressionally mandated efforts to facilitate small business capital formation by adding uncertainty, reducing process predictability, and increasing costs, all without a statutorily required explanation or justification by the NSCC.

Investor liquidity is a fundamental requirement for small companies to attract initial investment equity. In order for capital formation alternatives to attract the required capital, it is critical that potential investors be able to predict liquidity alternatives that will determine the financial consequences of their investments. The Proposed Rule does not accomplish these results and does not, consequently, discharge the NSCC's obligations under Rules 17Ad-22(e)(4)(i) and Rule 17Ad-22(e)(6)(i) and (v) under the Exchange Act.

The NSCC's September letter dismisses the concern that the Proposed Rule is inconsistent with the JOBS Act claiming that the proposal is "not intended to advantage or disadvantage capital formation…[and instead] focuses entirely on managing the clearance and settlement risk." It is alarming that the NSCC's responsibility to facilitate capital formation may be so easily disregarded because the negative affect was "not intended." Indeed, most of our concerns revolve around the NSCC's *unintended* consequences, and the NSCC consistently communicates that as long as its *intended* goal is being achieved, the unintended consequences are irrelevant.

Firms and Investors Will Stop Participating in Small Business Trades

With this Proposed Rule, many brokerage firms will be unable to trade small company stock because the insurance requirement is too high. With each new restriction imposed by the NSCC on this matter, more trade firms refuse to do trades with this type of money call, which harms small companies trying to raise capital. Many members will simply not allow trading in these securities after this proposed change, and the consequence of that will be that these so-called "illiquid securities" will become even more illiquid because fewer members will be willing to trade them. This in another example of the NSCC not considering or addressing the dire unintended consequences of this Proposed Rule.

Further, investors will be dissuaded to invest. To support small companies, one must support small companies' investors. Investors will be far less inclined to purchase the stock of small businesses if it is uncertain how and if they will be able to liquidate their stocks and realize a return. If the SEC truly has a mission to "facilitate capital formation," it needs to prioritize not only small business fundraising but also ensuring that investors want to risk the investment in these companies. This proposal is misdirected and continues a concerning trend given the SEC's goals.

In the NSCC's September letter, the NSCC openly disregards the fact that small firms and small businesses will be disproportionately affected by the Proposed Rule and is clearly prioritizing its imagined risks over its obligation to "protect investors and the public interest."

Conclusion

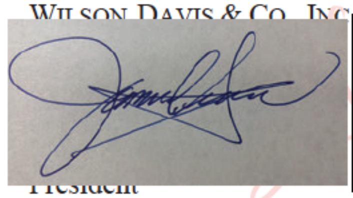
We reiterate that the Proposed Rule does not meet the NSCC's statutory mandate to facilitate prompt and accurate clearance and settlement of securities transactions. The Proposed Rule appears to be a significant deterrent to capital formation, small business investment, and liquidity. The proposal is unclear and complicated and is addressing a risk that has not been substantiated. Further, implementing this Proposed Rule is not fulfilling the NSCC's obligation to "remove impediments" to securities transactions and "protect investors and the public interest."

For the foregoing reasons, the Proposed Rule should be rejected.

We reserve the right to submit additional substantive comments. We will be happy to respond to your questions respecting the foregoing comments or the Proposed Rule.

Sincerely,

WILSON DAVIS & CO. INC.



[redacted]

President