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Via the SEC Portal

Ms. Vanessa Countryman
Office of the Secretary
U.S. Securities and Exchange Commission
100 F. Street NE
Washington, D.C. 20549

Re: Comment Letter to SEC Release No. 34-91809; File No. SR-NSCC-2021-005

Dear Ms. Countryman:

This firm represents Alpine Securities Corporation ("Alpine"). We submit this comment letter, on behalf of Alpine, in response the National Securities Clearing Corporation's ("NSCC") proposed rule change, referenced above, seeking to increase the minimum "Required Fund Deposit" imposed on members from $10,000 to $250,000 (the "Proposed Rule Change"). Alpine thanks the Commission for taking the time to consider this comment letter.

Through this comment letter, Alpine respectfully requests that the Commission disapprove the Proposed Rule Change for the reasons detailed herein. In addition, Alpine implores the Commission to carefully evaluate NSCC's ongoing practice, of which the Proposed Rule Change is just the latest example, of imposing excessive, escalating, and redundant margin charges based on overstated and unsupported justifications that such onerous margin charges are necessary to mitigate risk in the event of member default during the two-day settlement cycle, particularly in light of the deleterious impacts these charges have upon industry members, small-company issuers and the investing public. It is NSCC's margin charges, after all, that led to the highly-publicized recent events relating to Robinhood, and which forced Robinhood to raise more than a billion dollars overnight to meet NSCC's margin calls and, even then, to restrict trading by its customers because it was unable to satisfy the accompanying deposit requirements.[1]

[1] See *Why Robinhood Had to Risk Infuriating its Customers*, available at https://www.nytimes.com/2021/01/29/business/dealbook/robinhood-fundraise-customers.html. (discussing Robinhood's need to raise $1 billion from investors to cover margin charges imposed by NSCC's parent, the Depository Trust and Clearing Corporation ("DTCC"), due to trading surges in the Gamestop and AMC stocks).

Rather than approving NSCC continual efforts to impose new and ever-increasing margin charges to guard against its purported central counterparty exposure during the settlement cycle, NSCC should focus on expeditiously undertaking action that actually addresses that asserted risk: shortening the settlement cycle. Monetizing risk is simply not an efficient mitigation strategy as compared to this technologically feasible solution.

The Proposed Rule Change Impermissibly Targets and Disproportionately Impacts Smaller, Less Desirable NSCC Members

On its face, the Proposed Rule Change is extreme: it proposes a 2,500% increase to the minimum Required Fund Deposit. It is also designed to disproportionately impact small broker-dealer members with more limited capital resources because only small firms may struggle to post the $250,000 minimum or have the more limited trading activity that would allow them to operate with a Required Fund Deposit at or near the minimum. NSCC acknowledges this disproportionate, small-firm impact in the Proposed Rule Change by stating that "[t]he proposed changes could impose more of a burden on those Members that have lower operating margins, lower-cash reserves or higher costs of capital compared to other members."[2]

As a small, independent clearing-broker member of NSCC, Alpine is within the target zone of the Proposed Rule Change, although Alpine is not directly impacted at this time only because NSCC currently requires Alpine to maintain a Required Fund Deposit ***over $3 million***, plus daily and intraday margin calls that take Alpine's margin obligations to NSCC far over that amount, and which invariably exceed the value of the underlying transactions. Of particular concern to Alpine, however, is that NSCC is pursuing this increase as a baby step towards an even greater increase down the road.

This is not an idle concern. On two separate occasions this year, representatives from DTCC have informed Alpine that NSCC plans to seek an increase in the minimum capital requirement to ***$10 million*** for correspondent clearing firms, such as Alpine, and that NSCC expects that change will be implemented in the fourth quarter of this year. Such a change would obviously be hugely impactful, if not fatal, to Alpine, to other similarly situated smaller members, ***and to their customers who rely on Alpine and other small NSCC members for market access for trading***. Just the same as increasing the minimum to $250,000 under the Proposed Rule Change is likely fatal to several even smaller, or less active, members and their customers.

Notably, these proposed changes come on the heels of other recent significant increases in margin requirements that target clearing-broker members who provide services for the microcap and over-the-counter ("OTC") markets, such as Alpine. On February 1, 2021, NSCC began implementing a rule change, which altered several components of the Required Fund

[2] Proposed Rule Change, SEC Release No. 34-91809, at 14.

Deposit to substantial increase the margin charges for transactions in microcap/OTC stocks, including the volatility charge, the margin differential charge, the coverage component, and the backtesting charge.[3] Once NSCC began implementing that rule change, Alpine's Required Fund Deposit skyrocketed overnight, increasing from an average minimum of $2.5 million – an already enormous sum relative to the value of the positions to be cleared – to over $3.2 million, and has included several large unexpected margin call spikes that left Alpine struggling to locate capital to cover the calls.

Compounding the issue further, NSCC keeps expanding the Required Fund Deposit to double and triple cover the same purported risk of member default. In the rule change implemented on February 1, 2021, for instance, NSCC claimed that, because it was enhancing the volatility charge as applied to microcap/OTC securities, it could eliminate the "Illiquid Charge" that it formerly imposed on transactions in those securities. In reality, the volatility charge went up because NSCC changed its formula to incorporate the Illiquid Charge into the volatility charge on microcap/OTC stock transactions. NSCC then also incorporated, *without notice and Commission approval,* its new volatility charge into its margin differential charge component, coverage component and backtesting charge component to also increase each of those charges, and then applied them in the aggregate.

The actual volatility in these stocks did not increase overnight, particularly across the board, and, thus, there was no increase in risk to NSCC to justify the enormous increase in margin. In fact, NSCC has provided no evidence or data to support the assertion that there are more fails or defaults with microcap stocks than with other share types, and no evidence or data to support the implicit assertion in that rule change, or in the new Proposed Rule Change, that small firms, or firms specializing in microcap/OTC stock transactions, fail more frequently than larger firms trading in registered exchange stocks. NSCC's position instead reflects its discriminatory view that its membership should limited to only the right kind of firms with the right kind of exchange memberships – i.e., large firms trading in stocks listed on a registered exchange.

Again, these margin increases are not felt by Alpine or other small broker-members alone. They inevitably have destructive impacts on the customers, and the small businesses who rely on the traders to raise capital. For example, due to the capital requirements necessary to post these Required Fund Deposit margin charges, Alpine has been forced to limit customer trading, and to decline customer orders to sell their stock, potentially costing the customers millions of dollars.[4] Alpine is certain that other brokers have faced the same restraints. And, as

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[3] *See* SR-NSCC-2020-003, SEC Release No. 34-88474, 85 F.R. 17910 (March 31, 2020); Order Approving Rule Change, SEC Release No. 34-90502 (November 24, 2020).

[4] As a result of the barriers to access caused by the SR-NSCC-2020-003, Alpine filed an Application for Review with the Commission pursuant to Sections 19(d) and (f) of the Exchange Act on March 1, 2021 (Admin. Proceeding File No. 3-20238). In December of 2018, Alpine also filed another Application for Review pursuant to Sections

indicated, what happened with Robinhood is illustrative of what is occurring industry wide, not an anomaly caused by a single unexpected event of extreme volatility (on, incidentally, an NYSE stock).

The trickle-down effect continues from there. By making it too expensive to trade, NSCC is effectively limiting access to all participants in these markets; if small-business investors lack the ability to sell their shares, not only are they directly harmed, but the small businesses who rely on these markets for liquidity also suffer because no rationale investor would buy shares she cannot sell.

NSCC's ongoing efforts to weed out the smaller firms through excessive capital and margin requirements needs to be closely scrutinized by the Commission *at the rulemaking stage*.[5] Small firms, like Alpine, are the only broker-dealers left who fully service the critical microcap and OTC markets that represent the core of the U.S. economy and jobs. Major clearing firms, such as Merrill Lynch, Fidelity, Morgan Stanley and UBS, choose to no longer service the OTC market. Online discount firms (e.g., E-Trade, Charles Schwab, etc.) do not process this business either.

There are more than 10,000 issued stocks trading in the OTC markets, over twice the number of exchange-listed companies. The aggregate value of OTCQX, OTCQB and Pink Securities was approximately $ 375.2 billion in 2018.[6] Alpine alone facilitates tens of millions of dollars of capital financing for small business each month through the deposit, clearance and liquidation of microcap securities on behalf of its customers who provide direct financing to thousands of innovative, startup and early stage development business that operate in the United States. This is undeniably a critically important market segment, but due in no small part to the enormous regulatory costs and burdens of compliance imposed by NSCC and other SROs, Alpine is one of a few remaining broker-dealers to fully service this vital market segment.

Of course, it is also the Commission's duty to prevent discriminatory and anti-competitive rules and practices by NSCC, of which the Proposed Rule Change is but the latest example. Section 17A(b)(3)(F) of the Exchange Act requires that clearing agency rules "are not

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19(d) and (f) challenging other components of the Required Fund Deposit as being so onerous and discriminatory that they impermissibly limit access to NSCC's clearing services (Admin. Proceeding File No. 3-18979), and a Petition for Rulemaking (Admin. Proceeding File No. 4-738) requesting rulemaking by the Commission to address NSCC's excessive margin charge practices. These Applications and Petition remain pending before the Commission with no substantive consideration and action by the Commission.

[5] Instituting proceedings before the Commission to obtain review or rulemaking, after an SRO rule has already been approved, is not only a costly and lengthy process, as Alpine's own experience can attest (*see supra*), any relief comes too late. The damage to the firm and its customers has already been done.

[6] *See* https://www.prnewswire.com/news-releases/otc-markets-group-reports-2018-trading-statistics-and-highlights-300779908.html.

designed to permit unfair discrimination … among participants in the use of the clearing agency . . . ."[7] Similarly, "promot[ing] efficiency, competition and capital formation" are each central to the purpose of the Exchange Act, and the Commission is required to ensure these critical factors are protected in evaluating SRO rules. *See* 15 U.S.C. §§ 78c(f), 78s(f). As Congress noted in amending the Exchange Act in 1975, which added Sections 17A and 19 to the Exchange Act, "it is in the public interest to assure . . . fair competition among brokers and dealers, among markets and between exchange markets and over-the-counter markets."[8]

There can be little question that the Proposed Rule Change, and the other recent increases in Required Fund Deposit requirements, represent a conscious effort by NSCC to try to eliminate small clearing firms, especially those that service disfavored markets, from NSCC's membership. The drastically increased minimum deposit requirements in the Proposed Rule Change concedes as much. This is facially discriminatory and anticompetitive. And, it must be recognized that DTCC's board is comprised of representatives affiliated with large banking and brokerage firms, without a single representative from a small brokerage firm, which clearly factors into the types of policy choices and rules passed by NSCC.

NSCC's Risk-Mitigation Justification is Unsupported

Returning back to NSCC's acknowledgement that the Proposed Rule Change "may" disproportionately burden members with "lower operating margins, lower-cash reserves or higher costs of capital compared to other members."[9] NSCC insists that such anticompetitive burdens, which will undoubtedly put some members out of business, are "necessary" and "appropriate" to reduce the "risk" that these members create for NSCC and other members.[10]

However, NSCC's description of the risk mitigation that would be achieved, even taking NSCC at its word,[11] is underwhelming, to say the least. Specifically, NSCC states that, prior to proposing this rule change, it conducted an "impact study" over approximately one year (June 3, 2019 to May 29, 2020) to determine the anticipated "backtesting coverage" if the minimum Required Fund Deposit were increased to $250,000.[12] Over an entire year, NSCC observed that, had the $250,000 minimum been in place, a mere ***44*** backtesting deficiencies would have been

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[7] 15 U.S.C. § 78q-1(A)(b)(3)

[8] S. Rep. 94-75 (1975).

[9] Proposed Rule Change, SEC Release No. 34-91809, at 14

[10] *See id.,* at 14-18.

[11] It is impossible to check any of NSCC's conclusions against actual data, because NSCC does not provide any of its studies, models or data to the public in connection with its proposed rule changes, despite being obligated to publish its proposed rule changes for public notice and comment. *See* 15 U.S.C. § 78s(b).

[12] Proposed Rule Change, at 6.

eliminated across only ***13*** members.[13] But even this does not fully reflect the *de minimus* "mitigation" the change would provide, for NSCC claims that "[o]verall, a $250,000 minimum requirement would have increased NSCC's twelve-month [backtesting] coverage ***by 0.14%*** to 99.41%," and only ***0.03%*** higher than if NSCC imposed a more modest, $100,000 increase.[14] In other words, NSCC already has backtesting coverage of 99.27% based on the existing $10,000 minimum Required Fund Deposit, a greater "confidence" level than is required by Section 17A of the Exchange Act and Exchange Act Rule 17Ad-22, without even taking into account the significant additional margin charges that NSCC imposes on actual trading activity.[15]

While Alpine appreciates that NSCC must guard against risk, it strains credulity to accept that it is necessary, appropriate or efficient to impose new capital requirements that may put some existing NSCC's members out of business, and leave its customers stranded, to achieve such a minute and inconsequential additional level of purported risk mitigation. NSCC's economists may desire, even admirably, to drive NSCC's "confidence" level right to 100%, but the *Commission* must be more circumscribed and realistic in balancing the relative impacts. The Commission should not allow NSCC to impose costly new burdens that would have an anticompetitive and discriminatory impact on small broker-dealer members and their customers where they are so plainly unnecessary and would promote neither efficiency nor capital formation.

Indeed, NSCC's justification for the Proposed Rule Change is just as unsupported as its justifications for the onerous margin charges that NSCC has recently imposed on small firms, such as Alpine, servicing the microcap/OTC markets, which NSCC claims are necessary to cover its risk from member default during the two-day settlement cycle. For example, as indicated, Alpine provides sale-side or liquidation clearing services for its customers. On these transactions (which create CNS net short positions), Alpine's obligation is to deliver the stock by settlement date or T+2. However, as NSCC knows, prior to executing a trade, Alpine always has sufficient shares to cover all open short positions for its customers' trades in its account at DTC. As such, there is zero risk to NSCC that it will be unable to close-out the positions, even in the extremely unlikely event that Alpine were to suddenly cease to operate between T+0 and T+2. Alpine believes that all sale-side clearing firms operating in the microcap and OTC markets follow a similar practice.

Nevertheless, NSCC no longer gives any offsetting credit against margin requirements for the shares held at DTC, and instead imposes a panoply of separate margin charges that, in the aggregate, greatly exceed 100% the value of any net short positions. Thus, not only is NSCC facing zero counterparty risk, but it is grossly over-secured on any open positions from multiple

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[13] *Id.* at 7.

[14] *Id.* at 7-8, 15.

[15] *See id.,* at 15 (acknowledging that the current backtesting coverage is 99.27%.

different margin charges that cover the same asserted risk, at a cost that frequently requires Alpine to turn down customer orders to sell their stock because it lacks the capital to post the margin for the trade. There is simply no valid risk-based justification for NSCC's continual effort to increase the capital requirements to trade stock.

NSCC Should Focus Its Efforts on Eliminating the Asserted Risk, Instead of Continuing to Monetize It.

There is a much better approach to mitigate the asserted central counterparty risk exposure to NSCC than continuing to approve its demands for more and more capital from its members: shortening the settlement cycle. Monetizing risk is an inefficient mitigation strategy; it does not address the root cause of the risk and has negative collateral consequences on the industry. Simply put, the more capital being held at NSCC as a band-aid, the less capital there is circulating in the market.

In a series of white papers, DTCC has recognized that the margin requirements "strain" firm "liquidity" and have significant and detrimental impact on firms.[16] In its February 2021 white paper, DTCC acknowledged that "the most logical way to reduce the risks that drive margin requirements is to shorten the settlement cycle," and indicated that its goal is to move the United States to at least a T+1 settlement by 2023, and even shorter thereafter.[17]

Alpine appreciates and wholly supports DTCC's efforts to accelerate the settlement cycle if it reduces margin. However, DTCC's observations regarding the impact of margin charges, as well as its laudable goal to accelerate settlement, appear to be in conflict with NSCC's recent efforts to unnecessarily increase margin requirements further, including through the Proposed Rule Change, and the threatened $10 million minimal capital requirement for correspondent firms.

Among other things, Alpine is concerned about institutional hesitancy at NSCC to rollback any margin charges that is has already imposed, or may impose, in the meantime. In addition, the timeline for implementing an accelerated settlement seems unnecessarily protracted and, frankly, a T+1 cycle does not go far enough. DTCC claims that "NSCC and DTC can support T+1 and even same-day (T+0) settlement today, using existing technology."[18] Alpine appreciates that DTCC may need to wade through some industry intransigence to accomplish the change, but Alpine respectfully submits that such issues could be more expeditiously and

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[16] *See* DTCC, *Advancing Together: Leading the Industry to Accelerated Settlement* (February 2021), available at: DTCC-Accelerated-Settle-WP-2021.pdf; *see also, e.g.,* DTCC, *Modernizing the U.S. Equity Markets Post-Trade Infrastructure* (January 2018), available at modernizing-the-u-s-equity-markets-post-trade-infrastructure.pdf (dtcc.com); *see also* DTCC, *Project Ion Case Study* (May 2020), available at Project-ION-Paper-2020.pdf (dtcc.com)

[17] *See* DTCC-Accelerated-Settle-WP-2021.pdf

[18] *See id.*

efficiently overcome if DTCC and its subsidiaries focused on those efforts rather than spending resources devising new ways to increase costs to members.

In light of the detrimental impacts of the Required Fund Deposit charges on the industry, and the lack of any actual remaining uncovered risk, the Commission should disapprove any new margin charges, including the Proposed Rule Change, until (at the very least), accelerated settlement has been proposed. That issue is far more impactful and beneficial to the industry than more unnecessary capital and margin demands.

Conclusion

Alpine appreciates the Commission's consideration of this comment letter and its careful review of NSCC's Proposed Rule Change. For the foregoing reasons, Alpine respectfully requests that the Commission disapprove the Proposed Rule Change and instead direct DTCC to move forward expeditiously with its plans to propose an accelerated settlement cycle as a better approach to guard against NSCC's asserted central counterparty risks.

Respectfully Submitted

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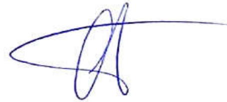

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