State Street Corporation

Joseph J. Barry
Senior Vice President and Global Head of
Regulatory, Industry and Government Affairs

State Street Financial Center
One Lincoln Street
Boston, MA 02111-2900

Telephone: 617.664.1254
E-mail: jjbarry@statestreet.com
www.statestreet.com

April 1, 2022

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

Via e-mail: rule-comments@sec.gov

Proposed Rule – Reporting of Securities Loans (File Number: S7-18-21)

Dear Ms. Countryman:

State Street Corporation ("State Street") welcomes the opportunity to comment on the proposed rule ("proposed rule" or "Rule 10c-1") issued by the Securities and Exchange Commission ("Commission") that would establish a new reporting requirement for securities lending transactions and related data on securities placed on loan. The proposed rule is intended to implement Section 984 of the Dodd Frank Wall Street Reform and Consumer Protection Act and includes the dissemination of certain transactional and aggregate position information to the public.[1] State Street recognizes the Commission's desire for greater transparency in the securities lending market and is not opposed to the broader reporting of pertinent data. We are concerned, however, with several elements of the proposed rule which we believe create unnecessary burdens for market participants, increase the potential for unintended consequence for market liquidity and result in the inequitable distribution of costs among market participants.

Headquartered in Boston, Massachusetts, State Street is a global custody bank which specializes in the provision of financial and investment services to institutional investor clients. This includes investment servicing, investment management, data and analytics, and

---

[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Section 984 (b) – 'The (Commission) shall promulgate rules that are designed to increase the transparency of information available to brokers, dealers, and investors, with respect to the loan or borrowing of securities.'

investment research and trading. With $43.7 trillion in assets under custody and administration and $4.1 trillion in assets under management, State Street offers its clients the ability to transact and hold assets in more than 100 geographic markets.[2] In addition, State Street is one of the world's largest agent lenders, offering its clients the opportunity to generate additional income from their investment portfolio holdings by facilitating the loan of securities to qualified borrowers on pre-defined terms.[3] This generally includes the provision of an agent lender indemnity to protect the client in the event of a borrower default. As of December 31, 2021, lendable assets in State Street's securities lending program totaled $5.4 trillion, with $407 billion in active loans across 37 markets globally.

State Street is organized as a United States ("US") bank holding company, with operations conducted through several entities, primarily its wholly-owned state-chartered insured depository institution subsidiary, State Street Bank and Trust Company. This includes the activities of our Securities Finance group, which is responsible for the management of our agent lender program. Among other entities, the State Street organization includes State Street Global Markets, LLC, a direct wholly-owned subsidiary of State Street and a US registered broker-dealer regulated by the Commission.

We appreciate the opportunity to offer our perspective on the Commission's proposed rule informed by our role as a leading securities agent lender. We have identified four matters for consideration by the Commission that we believe would, if adopted, more effectively accomplish the objectives described in the proposed rule. In particular, State Street believes the four recommendations: (i) better focus the proposed rule on the information that is of interest to the Commission and the public, (ii) improve the balance of costs and benefits of the proposed rule as a whole, and (iii) distribute more fairly the costs and burdens of the new reporting regime across the various categories of market participants. These recommendations can be summarized as follows:

- Replacement of the proposed 15 minute window for the reporting of securities lending transactions to the Registered National Securities Association ("RNSA"), with end of day reporting on a T+1 basis;
- Replacement of the 'available to lend' metric for the calculation of a market 'utilization rate' with publicly available information on the issuer's total share float;
- Clarification that the costs incurred by the RNSA to establish and operate the reporting system for securities lending data should be equitably shared by both borrowers and lenders, along with a tiered fee structure that eliminates costs for General Collateral ("GC") transactions;

[2] As of December 31, 2021.

[3] Securities are generally lent pursuant to a securities lending authorization agreement between the client and the agent lender, and a securities borrowing agreement between the borrower and the agent, acting on behalf of the client as principal.

- Flexibility in any final rule for the reporting party (*i.e.* the lender of a security or its agent) to assume responsibility for the creation and assignment of Unique Transaction Identifiers ("UTI").

Each of these recommendations are addressed in greater detail below, including relevant policy and rulemaking context.

Reporting Timeframe

As proposed by the Commission, the reporting requirement for securities lending transactions would apply to 'any person that loans a security on behalf of itself or another person' and would require such persons to report 'specified material terms for each securities lending transaction and related information to an RNSA'.[4] Furthermore, the Commission envisions that the reporting of information to the RNSA would occur 'within 15 minutes after a loan is effected or the terms of the loan are modified.'[5] While we do not object to the imposition of a single-sided reporting obligation on the lender of a security (or its agent), we strongly oppose the use of a 15 minute reporting window which we believe does not reflect the particular characteristics of the securities lending market and which will result in the dissemination of incomplete and error prone information of little value to its participants. To be clear, we do not oppose the reporting of any of the data fields specified by the Commission in the proposed rule, only the mandate that this take place on a 'near' real time basis.

Unlike transactions in the cash market, securities loans do not involve the outright purchase or sale of a security. Furthermore, they are negotiated not by reference to a spot market price, but rather as part of a larger credit relationship informed by various considerations, such as the risk profile of the counterparty, the type of collateral provided, the overall volume of transactions with the counterparty, the ability to make a profit on the underlying collateral and the particular characteristics of the security being borrowed (*e.g.* GC or 'easy to borrow', 'warm' or 'hard to borrow' securities). Similarly, while securities lending transactions are managed throughout the course of the trading day, they are not typically finalized until the end of day once all terms and conditions have been fully determined. In practice, this approach results in a large amount of intra-day 'cancel and rebook' activity, for instance to accommodate changes in borrower demand or the reallocation of transactions across client accounts, that are of no particular value in determining either market pricing or relative supply and demand.

As such, the 15 minute reporting window proposed by the Commission would inevitably result in a high volume of 'false positive' information on securities lending transactions that is more likely to confuse the market than to provide meaningful transparency. Moreover, the requirement to disseminate information on a 'near' real time basis would be much more costly for reporting parties to implement, due to the need to build-out fully automated data capture

---

[4] Proposed Rule, page 3.
[5] Proposed Rule, page 34.

and reporting systems, while investing substantial resources in data validation and reconciliation processes. Finally, greater costs are also likely to create additional dis-incentives for institutional investors to participate in the securities lending market, with broadly negative implications for liquidity.

As an alternative, we recommend that the Commission mandate the reporting of transactional information by the lender of a security (or its agent) on an end-of-day T+1 basis, an approach that is consistent with the requirements of the European Union ("EU") Securities Financing Transaction Regulation ("SFTR"), and that would result in significantly more complete and accurate data. The reporting of securities lending transactions on an end-of-day T+1 basis is also broadly consistent with the requirements envisioned by the Commission in its recently issued proposed rule on the reporting of short positions and short activity by asset managers.[6]

Available to Lend Securities

In addition to mandating the reporting of individual securities lending transactions to the RNSA, the Commission proposes to require the lender of a security (or its agent) to disclose on a daily basis the 'total amount of each security that is available to lend' in their lending portfolios and the 'total amount of each security that is on loan'.[7] This information would then be aggregated and publicly disseminated by the RNSA, no later than the next business day. In the preamble of the proposed rule, the Commission specifies that the term 'total amount of each security that is available to lend' means 'any security (in a portfolio) that is not subject to legal restrictions that would prevent (the security) from being lent'.[8] While we recognize the Commission's desire to develop and publish a quantitative metric ('utilization rate') to help market participants assess relative demand for individual securities, we are concerned that the broad definition of 'available to lend' envisioned in the proposed rule will result in the dissemination of highly unreliable information that substantially overstates the actual amount of supply in the market.

Although clients who participate in securities lending programs generally agree to lend all portfolio assets, or categories of assets, securities lending authorization agreements typically place limits on both portfolio and counterparty exposure. Furthermore, the actual supply of available securities may be impacted by additional client instruction resulting from various idiosyncratic or market events, as well as discretionary transfers in and out of investment portfolios. As such, and as acknowledged by the Commission, the intended definition of 'available to lend' 'may overstate the quantity of securities that could actually be lent because the data would include securities that may become restricted' based on various parameters and considerations.[9] Clients are understandably highly sensitive to the potential release of proprietary information that would provide competitors with insight into their investments

---

[6] 'Proposed Rule: Short Position and Short Activity Reporting by Institutional Investment Managers', Securities and Exchange Commission, File Number S7-08-22 (March 16, 2022).
[7] Proposed Rule, page 41.
[8] Proposed Rule, page 59.
[9] Proposed Rule, Question 48, pages 64-65.

portfolios and trading strategies. In our experience, the prospect of being obligated to disclose, even in aggregate form, all portfolio holdings may be enough to drive certain clients out of the securities lending market, with important implications for liquidity.

We therefore recommend that the Commission adopt in any final rule an alternative metric to help estimate the supply of 'available to lend' securities ('utilization rate') by using publicly available data on the issuer's total share float.

Reporting System Buildout and Maintenance Costs

The Commission specifies in the preamble of the proposed rule that the costs associated with the establishment and maintenance of the reporting system for securities lending transaction and related data should be borne by those who 'directly provide information' to the RNSA.[10] Since the Commission also proposes to make the lender of a security (or its agent) responsible for the reporting of such information, this approach has the practical effect of imposing all systems-related cost for the new reporting mandate solely on agent lenders and their clients (*i.e.* institutional investors, such as pension plans and mutual funds). This is true notwithstanding the fact that enhanced transparency in the securities lending market primarily benefits the borrower client (*i.e.* hedge funds and other similar opportunistic investors).

Furthermore, there is, in our view, no practical way for agent lenders to try to recuperate even a portion of these new costs from borrowers through changes to existing market pricing conventions. In effect therefore, the costs associated with the establishment and maintenance of the reporting system for securities lending transactions envisioned by the Commission will substantially narrow, if not eliminate, existing revenue streams for agent lenders and their clients in what is already a low margin business, depriving buy-side investors, in the process, from access to incremental income used to reduce administrative expenses and/or enhance investor returns. We are particularly concerned about the cost implications of the intended funding structure for GC transactions, where margins are razor thin and where existing revenue share barely covers the agent lender's cost of capital.

In order to address this pressing concern, which has the strong potential to further dampen institutional investor participation in the market, we strongly urge the Commission to clarify in the final rule that the costs incurred by the RNSA to establish and operate the reporting system for securities lending transaction and related information should be equitably shared by borrowers and lenders, even if the actual reporting obligation remains single-sided. The information needed for this approach can be readily obtained by the RNSA since the data fields proposed by the Commission in Rule 10c-1 include the confidential reporting of the legal name of each counterparty to a transaction.

---

[10] Proposed Rule, page 72.

In our experience, the details of loan activity involving GC securities are unlikely to be of informational value to the market. This reflects the structure of GC transactions, where collateral is fungible and where supply substantially outstrips borrower demand, resulting in narrow and predictable fee spreads. Furthermore, since borrowers can easily access GC securities from multiple lenders at low and stable prices, there is little to no price differentiation between GC securities within an asset class. This results in a category of securities lending transactions that offer no particular informational value to the market in terms of assessing relative supply and demand, but which is important in supporting overall market liquidity. As such, we recommend that the Commission also consider the introduction of a tiered fee structure wherein market participants would not face a charge for reporting GC transactions to the RNSA. Another, and in our view, equally suitable approach to these concerns, would involve the exclusion of GC transactions from the scope of the reporting requirement. This would significantly reduce low-value 'noise' in the envisioned data set relative to the strong informational value of non-GC transactions. In either case, we believe that GC transactions can reasonably be defined by the Commission for these purposes as any securities lending transaction with fees/demand spread below 25 basis points.

Unique Transaction Identifier

The Commission proposes to require the RNSA, as the repository for information regarding securities lending transactions, to assume responsibility for the issuance and assignment of the UTI. This approach would further aggravate the practical challenges of the proposed rule for lenders of securities (or their agents), due to the need to accept and incorporate within their systems, third-party issued data. This includes the need to follow stringent internal risk management guidelines prescribed by prudential regulation for the use of third-party vendor data. Among these are requirements related to the management of potential business disruptions, whether from traditional or cyber-related events, as well as standards governing operational resilience.

As such, we recommend that the Commission amend its approach so as to permit the reporting party (*i.e.* the lender of a security or its agent) to produce and assign UTIs, provided that it has the capability to do so.[11] To the extent that the Commission's decision to place responsibility for the UTI on the RNSA is motivated by a concern for ensuring the 'uniqueness' of each UTI, we note that this can be achieved when the generating party (in this case, the lender of the security or its agent) creates a UTI using its Legal Entity Identifier ("LEI") as the prefix, followed by an alphanumeric code that is unique to the transaction reported by the entity. Using the LEI as a "mint" for ensuring the uniqueness of UTIs was the approach recommended by global standard setters in their 2017 technical guidance on 'Harmonization of the UTI.'[12] We believe that a similar approach can and should be used in the context of the Commission's rulemaking.

---

[11] This approach is consistent with the requirements of the EU SFTR where responsibility for the creation of a UTI is assigned to the reporting entity.

[12] "Technical Guidance: Harmonization of the Unique Transaction Identifier", Committee on Payments and Market Infrastructure and International Organization of Securities Commission (February 2017).

The Commission may also be concerned that allowing the reporting party to generate its own UTIs would risk the creation of identifiers that would reveal confidential information about the underlying transaction. This can, in turn, be addressed through a mandate that the reporting party must create UTIs in a manner that ensures that no sensitive information about the transaction can be gleaned from the identifier, with the exception of the LEI. In any event, we note that our recommended approach would not prevent the RNSA from assigning its own UTI to inbound transactional data from the reporting party for onward dissemination to the market.

Thank you once again for the opportunity to comment on the important matters raised in the proposed rule. To summarize, while we are not opposed to measures that seek to enhance transparency in the securities lending market, including the introduction of a single-sided reporting obligation on the lender of a security (or its agent), we do not support several aspects of the Commission's proposed rule, which we believe will create unnecessary burdens for market participants, increase the potential for market dislocation and lead to the inequitable distribution of costs among market participants.

We therefore recommend several adjustments to the intended framework that address: (i) the length of the reporting window for securities lending transactions, (ii) the reporting of information on 'available to lend securities', (iii) the allocation of costs for the establishment and maintenance of the reporting system by the RNSA, and (iv) the parties that may assume responsibility for the generation and assignment of UTIs.

Please feel free to contact me at jjbarry@statestreet.com should you wish to discuss the contents of this submission in greater detail. We welcome the opportunity to further engage with the Commission on the specifics of the proposed rule and we stand ready to provide whatever assistance may be appropriate.

Sincerely,

Joseph J. Barry