Congress of the United States
Washington, DC 20515

October 25, 2024

The Honorable Gary Gensler
Chair
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549–1090

Robert Cook
Chief Executive Officer
Financial Industry Regulatory Authority
1700 K Street, N.W.
Washington, D.C. 20006

Dear Chair Gensler and Mr. Cook:

I write to express my concerns regarding the Financial Industry Regulatory Authority, Inc. ("FINRA") proposal to adopt its Rule 6500 Series (the "Proposed Rules") to (1) require the reporting by broker-dealers of certain information about securities loans; and (2) provide for the publication by FINRA of such information.[1] I believe the Proposed Rules improperly add reporting requirements to the Securities and Exchange Commission's ("SEC") existing rule and will unnecessarily increase costs for broker-dealers, which are likely to be passed to retail investors. I also note that FINRA's Proposed Rules lack adequate economic analysis, which deprives the public of the ability to provide meaningful comments on the potential impacts of the rule to the broker-dealer industry, capital markets, and investors. Finally, the publication provided by the Proposed Rules raises confidentiality concerns for lenders and borrowers.

FINRA submitted the Proposed Rules in response to Securities Exchange Act Rule 10c-1a (the "SEC Rule"), which was adopted last year by the SEC.[2] The SEC Rule requires certain entities to report information about securities loans to a registered national securities association ("RNSA").[3] The SEC Rule also requires FINRA to make publicly available certain information that it receives regarding those loans and to implement rules regarding the format and manner to administer the collection and dissemination of certain information regarding securities lending transactions. On May 1, 2024, FINRA filed its Proposed Rules with the SEC. On August 5, 2024, the SEC instituted proceedings to determine whether to approve or disapprove the Proposed Rules.[4]

FINRA's Proposed Rules suffer from at least three fatal flaws. First, the Proposed Rules go beyond FINRA's mandate. As detailed by multiple industry associations, including SIFMA, ICI,

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1 Exchange Act Rel. No. 100046, 89 FR 38203 (May 7, 2024) (Notice of Filing of a Proposed Rule Change To Adopt the FINRA Rule 6500 Series (Securities Lending and Transparency Engine (SLATE™)).

2 Exchange Act Rel. No 98737, 88 FR 75644 (Nov. 3, 2023) (Reporting of Securities Loans).

3 The SEC Rule requirements apply to an RNSA. FINRA is currently the only RNSA and will be used interchangeably with RNSA in this letter.

4 Exchange Act Rel. No. 100655, 89 FR 65441(Aug. 9, 2024) (Order Instituting Proceedings). I note that the SEC Rule is currently subject to legal challenge regarding the sufficiency of the adoption of the rule. The challenge is based upon, among other things, that the SEC Rule conflicts with the Commission's statutory authority; imposes substantial costs that outweigh the purported benefits; and insufficiently complies with the Administrative Procedure Act. *See* "SEC's Sec Lending, Short Position Reporting Challenged," MarketsMedia (Mar. 7, 2024), https://www.marketsmedia.com/secs-sec-lending-short-position-reporting-rules-challenged/#:~:text=The%20SEC%20violated%20the%20Securities,the%20SEC's%20own%20prior%20views.

MFA, and ISLA, the Proposed Rules add data elements that were not included in the SEC Rule.[5] It is not clear what authority FINRA has to impose additional requirements beyond the SEC Rule and FINRA has failed to explain why such additional requirements are necessary and appropriate. For example, one association stated that the SEC Rule would "require reporting of twelve unique data elements plus three confidential data elements for new loan activity and up to fifteen data elements for loan modifications," but FINRA's Proposed Rules have "44 reportable data elements for new loan activity and 34 data elements for loan modifications."[6] This is a significant increase in reportable fields with little or no explanation from FINRA regarding its authority to add them. As one commenter put it, the Proposed Rules "significantly exceed FINRA's rulemaking mandate under [the SEC Rule]" and "it is improper to implement them through a Notice of Proposed Rulemaking pursuant to Rule 19b-4 under the Exchange Act."[7]

Second, FINRA's Proposed Rules lack adequate cost-benefit analysis. In 2013, FINRA published its framework for conducting economic impact assessments as part of developing rule proposals.[8] FINRA stated that it was "committed to enhancing its economic impact assessments of rules going forward." FINRA indicated that it should be transparent about how a "specific rule proposal addresses a regulatory need better than reasonable alternatives." FINRA explained that such analysis "helps commenters focus on the key assumptions and information that motivate the rule proposal, permitting them to provide more directed and impactful comments."

Here, FINRA's so-called economic analysis of the "potential costs" is, at best, cursory and fails to satisfy its economic analysis framework. For example, when discussing the costs of additional modifiers and indicators, FINRA stated only that "Covered Persons would incur costs for establishing processes to identify when the required modifiers must be appended and reporting such modifiers to [FINRA]." Similarly, FINRA notes in passing that Covered Persons "may incur a cost to track and report" other information that was not explicitly prescribed in the SEC Rule.[9] Simply stating that costs exist is not nearly sufficient to support FINRA's claimed consideration of the potential economic and competitive impacts on the industry and retail investors. Including numerous data reporting requirements beyond the SEC Rule would make reporting significantly more complex, costly and burdensome. FINRA's additional regulatory

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[5] *See* Letter from Tony Holland, Director of Market Practice, International Securities Lending Association to SEC (May 28, 2024), https://www.sec.gov/comments/sr-finra-2024-007/srfinra2024007-478631-1370174.pdf; Letter from Jennifer W. Han, Chief Counsel, Managed Funds Association to SEC (July 31, 2024), https://www.sec.gov/comments/sr-finra-2024-007/srfinra2024007-501475-1466443.pdf ("MFA Letter"); Letter from William C. Thum, Managing Director, Asset Management Group of the Securities Industry and Financial Markets Association (July 31, 2024), https://www.sec.gov/comments/sr-finra-2024-007/srfinra2024007-500655-1464942.pdf; Letter from Paul Cellupica, General Counsel, and Kimberly Thomasson, Assistant General Counsel, Investment Company Institute to SEC (July 30, 2024), https://www.sec.gov/comments/sr-finra-2024-007/srfinra2024007-498595-1461562.pdf ("ICI Comment").

[6] Letter from Fran Garritt, Head of Business, and Mark Whipple, Chairman of the Board of Directors, International Securities Lending Association Americas to SEC (July 16, 2024), https://www.sec.gov/comments/sr-finra-2024-007/srfinra2024007-494003-1433147.pdf.

[7] MFA Letter.

[8] *See* Framework Regarding FINRA's Approach to Economic Impact Assessment for Proposed Rulemaking (Sept. 2013), https://www.finra.org/sites/default/files/Economic%20Impact%20Assessment_0_0.pdf ("FINRA Framework").

[9] Proposed Rules, 89 FR at 38215.

burdens will increase costs for broker-dealers and thus indirectly increase costs for retail investors.

FINRA also mentions that it "considered various alternatives and the potential costs and benefits of those alternatives," but provides little or no detail regarding such alternatives or why they were not chosen.[10] Instead, FINRA merely concludes that it "believes the requirements in the proposed rule are appropriate in light of the anticipated benefits." This does not approach FINRA's commitment that proposed rule changes should be transparent or the expectation that FINRA will address reasonable alternative options.[11] Accordingly, FINRA should provide detail on the alternatives – and why they were not adopted – to market participants and the SEC. Without this detail, the public's ability to provide meaningful feedback is limited. I encourage FINRA to conduct the type of detailed and comprehensive cost-benefit analysis to which it has publicly committed.

Third, I am concerned that by gathering and disclosing data beyond that required by the SEC Rule, FINRA's Proposed Rules may expose confidential position and trading information. For example, one commenter stated that FINRA's proposal to daily publish aggregate transaction activity by borrower type could effectively disclose individual loan amounts.[12] This appears to contradict the Commission's decision to delay the publication of loan amount information by 20 business days to prevent exposing short selling strategies. Another commenter indicated that FINRA's additional reporting requirements beyond the SEC's mandate could "reveal beneficial owners' confidential information to other market participants."[13] Further, as noted by various industry associations, FINRA has not provided detail about how it plans to package and sell the reported data.[14] Accordingly, market participants cannot review and analyze all of the confidentiality issues created by the Proposed Rules and, especially, the additional data reporting requirements.

Various commenters have raised legitimate concerns regarding the substance and implementation of the Proposed Rules that require additional review and consideration. I note that the SEC's Rule is currently subject to litigation in federal court,[15] and the SEC and FINRA should avoid pursuing any additional, related rules (including FINRA's Proposed Rules) until after this challenge is adjudicated. At a minimum, I believe it would be appropriate for the SEC to disapprove the Proposed Rules and require FINRA to submit a new proposal that is consistent with the requirements of the SEC Rule and supported by a robust cost-benefit analysis such that the public can provide the SEC and FINRA with meaningful comments. The Proposed Rules are an example of FINRA acting beyond its traditional mandate as a member-driven self-regulatory organization. Approving the Proposed Rules as currently constituted would harm market participants, including retail investors, violate legal requirements around public notice and

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10 Proposed Rules, 89 FR at 38216.

11 FINRA Framework.

12 MFA Letter.

13 ICI Comment.

14 *See* Letter from Sarah A. Bessin, Deputy General Counsel, Investment Company Institute, et al., to SEC (May 24, 2024), https://www.sec.gov/comments/sr-finra-2024-007/srfinra2024007-477911-1366774.pdf.

15 *See above* n.4.

comment, and sanction FINRA's unnecessary and potentially harmful overreach with respect to the securities lending market.

Please respond to the following requests/questions no later than November 15, 2024:

1. Describe FINRA's authority and rationale to include in the Proposed Rules additional data elements beyond those set forth in the SEC Rule.
2. Please specify the analysis FINRA and the SEC have conducted regarding the impact of each additional data element on the confidentiality of lenders and borrowers and whether each data element may expose position, trading or similar information.
3. Describe in detail the alternatives to the Proposed Rules that FINRA considered and why it chose not to propose each alternative.
4. Describe why FINRA failed to explain in detail the likely costs of the Proposed rules beyond merely noting that market participants "may incur" or "would incur" costs.
5. Describe why it is appropriate for FINRA to submit a separate rule change regarding fees and data products.
    a. Specifically, how does such a separate submission allow the public to provide direct and impactful comments on all related SEC and FINRA securities lending rules as a whole?
    b. When does FINRA expect to submit the rule change regarding fees and data products?
    c. What rationale would support proceeding with the Proposed Rules before the additional rule proposal is submitted?
    d. Please specify how FINRA will mitigate confidentiality concerns when publishing securities loan data products.
6. Describe why it is appropriate in the SEC's and FINRA's view to require the industry incur the costs and operational burden of implementing and complying with the Proposed Rules when the SEC Rule is itself subject to legal challenge?

Sincerely,

Bill Hagerty
United States Senator