

CLIENT ALERT

# SEC Adopts Rule for the Reporting of Securities Lending Transactions

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## AUTHORS

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## Introduction

On October 13, 2023, in a 3-2 vote, the Securities and Exchange Commission (the “SEC”) adopted new Rule 10c-1a (the “Final Rule”)<sup>1</sup> under the Securities Exchange Act of 1934 (“Exchange Act”) requiring the reporting of securities loan information to a registered national securities association (“RNSA”) by the end of the day on which such loans are effected or modified. Currently, the Financial Industry Regulatory Authority (“FINRA”) is the only RNSA. FINRA will be required to publish much of the information it receives, along with information pertaining to the aggregate transaction and distribution of loan rates for each reportable security, while keeping confidential other information, in specified periods.

The Final Rule is intended to increase the transparency of information available to securities lending market participants such as lenders, borrowers, and broker-dealers as well as the investing public and regulators with respect to securities lending.<sup>2</sup> The Final Rule reflects a number of changes from the rule proposed by the SEC in November 2021 (the “Proposed Rule”)<sup>3</sup> in response to comments, but is expected to impose significant operational and compliance burdens on securities lending market participants.

<sup>1</sup> See Reporting of Securities Loans, Exchange Act Release No. 93737 (Oct. 13, 2023) (the “Adopting Release”), available [here](#).

<sup>2</sup> See Adopting Release at 10.

<sup>3</sup> See Reporting of Securities Loans, Exchange Act Release No. 93613 (Nov. 18, 2021) (the “Proposing Release”). See also SEC Issues Proposed Rule for the Reporting of Securities Lending Transactions, Willkie Client Alert (Nov. 24, 2021), available [here](#).

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## SEC Adopts Rule for the Reporting of Securities Lending Transactions

### Persons with Reporting Obligations

Covered Persons. The Final Rule will require “covered persons” to report certain information about securities loans to FINRA. “Covered persons” include:

- **Intermediaries:** any person who agrees to a covered securities loan on behalf of a lender;
- **Lenders not using intermediaries:** any person who agrees to a covered securities loan as a lender when an intermediary is not used; and
- **Broker-dealers when borrowing customers’ fully paid or excess margin securities.**<sup>4</sup>

The Final Rule employs a single-sided approach to reporting. The reporting obligation generally applies to the lender, except that when a lender uses an intermediary, the reporting obligation falls on the intermediary, and when the borrower is a broker-dealer borrowing customers’ fully paid or excess margin securities, the reporting obligation falls on the broker-dealer.<sup>5</sup>

Reporting Agents. Covered persons may rely on “reporting agents” to fulfill their reporting obligation under the Final Rule. The term “reporting agent” means “a broker, dealer, or registered clearing agency that enters into a written agreement with a covered person,”<sup>6</sup> pursuant to which the covered person must provide the reporting agent with timely access to the reportable information. The reporting agent is also required to enter into a written agreement with FINRA permitting the reporting agent to provide the required information to FINRA on behalf of a covered person.<sup>7</sup>

Reporting agents must provide FINRA with a list naming each covered person on whose behalf the reporting agent is providing information and provide FINRA with any updates to the list of such persons by the end of the day on which such list changes.<sup>8</sup>

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<sup>4</sup> Final Rule 10c-1(a)(j)(1). In response to comments received with respect to the Proposed Rule, the Adopting Release clarifies that a clearing agency is not required to report information to FINRA when acting in the capacity of or engaged in activities as a central counterparty or a central securities depository in connection with a covered securities loan. This is because engaging in such activities, including novation, processing, settlement, netting and incidental services, does not involve lending or borrowing shares on its own behalf. See Adopting Release at 30, 74-75.

<sup>5</sup> See Adopting Release at 32.

<sup>6</sup> Final Rule 10c-1a(j)(4).

<sup>7</sup> See Final Rule 10a-1a(b)(3). The Final Rule will require that reporting agents establish, maintain and enforce written policies and procedures that are reasonably designed to provide the required information to FINRA on behalf of a covered person. See Final Rule 10a-1a(b)(2).

<sup>8</sup> See Final Rule 10a-1a(b)(4). The Final Rule also imposes books and records requirements on reporting agents. The Final Rule requires reporting agents to preserve certain documents for no less than three years, the first two in an easily accessible place. Reporting agents are required to preserve information not only provided to FINRA (including the time of transmission to FINRA), but also received from covered persons (including time of receipt). In addition, the Final Rule requires reporting agents to preserve written agreements entered into with covered persons and FINRA pursuant to the Final Rule. See Final Rule 10a-1a(b)(5).

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## SEC Adopts Rule for the Reporting of Securities Lending Transactions

Other Vendors. The Adopting Release notes that the ability to use a reporting agent does not prevent covered persons from contracting privately with third-party vendors to assist in reporting, but the use of a third-party vendor that is not a reporting agent does not relieve a covered person of its reporting obligation.<sup>9</sup>

Market participants that engage in covered securities loans will need to consider entering into written agreements with one or more reporting agents or third-party vendors prior to the Final Rule's implementation. As noted below, reporting requirements will begin 24 months after the Final Rule's effective date, January 2, 2024 (the "Effective Date"), and covered persons will only have 12 months from the date FINRA's rules are adopted to begin reporting information (the "Reporting Date").

### Securities Loans Required to Be Reported

Loans of "reportable securities" are "covered securities loans" required to be reported to FINRA under the Final Rule.<sup>10</sup> "Reportable securities" include securities that are already subject to reporting requirements under existing reporting regimes, specifically, the National Market System Plan governing the consolidated audit trail (the "CAT"), FINRA's Trade Reporting and Compliance Engine ("TRACE"), and the Municipal Securities Rulemaking Board's ("MSRB") Real Time Reporting System ("RTRS") or any reporting system that replaces one of these systems.<sup>11</sup>

The Adopting Release explains that reportable securities include:

- Loans of equity securities (both exchange-listed equities and equities traded over-the-counter);
- Debt securities (including corporate debt and asset-backed securities); and
- Crypto asset securities if they are required to be reported to the CAT, TRACE or RTRS.<sup>12</sup>

Positions at a clearing agency resulting from central counterparty or central securities depository services, short sales, short positions or repurchase agreements (or "repos") are not covered securities loans; however, loans that are used for short sales are.<sup>13</sup>

In addition, securities that are not required to be reported under the existing reporting regimes or the Final Rule include:

- Fixed-income transactions in securities with a maturity of one calendar year or less at issuance, such as money market instruments and non-U.S. dollar-denominated debt (for TRACE);

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<sup>9</sup> Id.

<sup>10</sup> Final Rule 10c-1a(j)(3).

<sup>11</sup> See Adopting Release at 57.

<sup>12</sup> Id. at 59, 64.

<sup>13</sup> See Adopting Release at 69-72.

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## SEC Adopts Rule for the Reporting of Securities Lending Transactions

- Equity transactions in “restricted securities,” as that term is defined in Rule 144 of the Securities Act of 1933 (for the CAT); and
- Municipal securities transactions excepted under MSRB Rule G14, including a small number of transactions for securities without assigned CUSIP numbers, municipal fund securities (*i.e.*, 529 Plans, ABLE programs, local government investment pools), and inter-dealer transactions ineligible for comparison of trade settlement date at a clearing agency (for RTRS).<sup>14</sup>

### Information Required to Be Reported to FINRA

Public Data Elements. The Final Rule requires the following information to be reported to FINRA, which FINRA will make publicly available:<sup>15</sup>

- Legal name of the security issuer, and its LEI, if available;
- Ticker symbol, ISIN, CUSIP, FIGI or other security identifier;
- Date and time when the covered securities loan was effected;
- Name of the platform or venue where the covered securities loan was effected;
- Amount, such as size, volume, or both, of the reportable securities loaned;
- Type of collateral and percentage of collateral to value of securities loaned;
- Rebate rate, securities lending fee or rate, or any other fee or charges;
- Termination date of the covered securities loan; and
- Borrower type (broker-dealer, customer, clearing agency, bank, custodian, or other person).

Confidential Data Elements. In addition, there are certain confidential data elements that are required to be reported to FINRA, but that FINRA is not permitted to make publicly available:

- Legal name of the parties, CRD or IARD number, MPID, and LEI of each party, and whether such person is the lender, the borrower, or an intermediary;
- If the lender is a broker or dealer and the borrower is its customer, whether the security is loaned from the broker’s or dealer’s inventory to a customer of such broker or dealer; and
- Whether the covered securities loan is being used to close out a fail to deliver pursuant to Rule 204 of Regulation SHO or to close out a fail to deliver outside of Regulation SHO.

Modifications. In addition, covered persons must report modifications of the public data elements.<sup>16</sup> When reporting modifications, reporting persons must provide:

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<sup>14</sup> Id. at 57-58.

<sup>15</sup> Final Rule 10c-1a(c),(e).

<sup>16</sup> Final Rule 10c-1a(d).

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## SEC Adopts Rule for the Reporting of Securities Lending Transactions

- The date and time of the modification;
- The specific modification and the data element being modified; and
- The unique identifier assigned to the original covered securities loan.<sup>17</sup>

Securities lending transactions predating the Reporting Date (as defined below) will only need to be reported on the date they are first modified following the implementation of the Final Rule. Securities lending transactions predating the Reporting Date that are not modified following the implementation of the Final Rule are not required to be reported.<sup>18</sup>

### Reporting to FINRA

**Timing.** Covered persons (or their reporting agents) must provide the required information to FINRA by the end of the day on which a covered securities loan is effected (even if not yet settled) or the terms of the loan are modified.

**FINRA Obligations.** Following the receipt of such information, FINRA must, as soon as practicable, but not later than the morning of the business day after the covered securities loan is effected or modified, assign a unique identifier to the covered securities loan and make publicly available the public data elements, other than the loan amount. FINRA is required to make the loan amount information publicly available 20 business days after the covered securities loan is effected or modified.

Finally, the Final Rule requires that FINRA make publicly available information pertaining to aggregate transaction activity and distribution of loan rates for each reportable security not later than the morning of the business day after covered securities loans are effected or modified.<sup>19</sup>

**Additional FINRA Rulemaking Required.** The Final Rule does not specify the format or manner in which the information is reported to FINRA and instead requires FINRA to adopt rules, subject to SEC approval, regarding the format and manner of its collection of information. FINRA will be required to maintain such information on its website or similar means of electronic distribution, without use restrictions, for a period of at least five years. The Adopting Release provides that FINRA is permitted to establish and collect reasonable fees under the Final Rule. In a change from the Proposed Rule, the Final Rule provides FINRA with discretion to charge fees to persons other than covered persons, which may lead to market participants other than covered persons bearing the costs of the Final Rule.

### Implementation Timeline

Reporting requirements will begin 24 months after the Effective Date. FINRA must propose rules to implement the Final Rule within 4 months of the Effective Date, and the SEC must review and approve FINRA's proposed rules. FINRA's

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<sup>17</sup> Final Rule 10c-1a(d)(1).

<sup>18</sup> Final Rule 10c-1a(d)(2).

<sup>19</sup> Aggregate transaction activity refers to information pertaining to the absolute value of a transaction such that net position changes should not be discernable in the data. Loan rate refers to the aggregate fee and rebate information provided to FINRA.

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## SEC Adopts Rule for the Reporting of Securities Lending Transactions

proposed rules must become effective no later than 12 months after the Effective Date. Covered persons thus will have 12 months from the date FINRA's rules are adopted to begin reporting information (*i.e.*, the Reporting Date). Finally, FINRA must begin to make information publicly available within 90 calendar days of the Reporting Date.

### Dissenting Commissioners

Although the changes to the Final Rule respond to commenters' concerns regarding the Proposed Rule, the number and significance of certain changes raise the question whether the Final Rule amounts to a fundamentally distinct reporting regime that would warrant a re-proposal of the rule. For example, Commissioner Mark T. Uyeda noted that the replacement of a 15-minute reporting requirement with an end-of-day reporting requirement is potentially up to a 32-fold difference in reporting time and one that the public has not had an opportunity to comment on.<sup>20</sup>

Commissioner Uyeda also observed that the SEC's adoption of Rule 13f-2 under the Exchange Act on the same day could have implications for the Final Rule that the public may not have had adequate time to consider given the short comment periods for both rules.<sup>21</sup> The rules are interrelated insofar as Rule 13f-2 requires position and activity reporting by persons who borrow securities to engage in short sales and the Final Rule requires the reporting of securities loans, many of which may be used to facilitate short sales. Commissioner Uyeda questioned the extent to which the information from the Final Rule could be used to estimate particular short selling positions and the extent to which such use was acceptable.<sup>22</sup>

Finally, timing considerations may pose issues in implementation. Commissioner Hester M. Peirce observed that 4 months to propose implementing rules was "extremely aggressive" given that FINRA has to create a system to generate unique identifiers. Further, she noted that the requirement for FINRA's rules to be effective within 12 months will constrain its ability to work with industry participants and that FINRA may not have time to resolve early-stage glitches given the 90-day deadline to start disseminating information once reporting begins.<sup>23</sup> The timeline also presumes that the SEC will approve FINRA's proposed rules.

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<sup>20</sup> Statement on Reporting of Securities Loans, Commissioner Mark T. Uyeda (Oct. 13, 2023), available [here](#).

<sup>21</sup> See Short Position and Short Activity Reporting by Institutional Investment Managers, Exchange Act Release No. 98738 (Oct. 13, 2023), available [here](#).

<sup>22</sup> Statement on Reporting of Securities Loans, Commissioner Mark T. Uyeda (Oct. 13, 2023), available [here](#).

<sup>23</sup> Reporting of Securities Loans, Commissioner Hester M. Peirce (Oct. 13, 2023), available [here](#).

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