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Via Electronic Submission: rule-comments@sec.gov

Vanessa A. Countryman
Secretary of the Commission
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

**Re: Position Reporting of Large Security-Based Swap Positions - Proposed Rule
(File Number S7-32-10) (the “Proposing Release”)**

Dear Ms. Countryman:

We appreciate this additional opportunity to comment on the rule proposed by the Securities and Exchange Commission (the “Commission”) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”) which would require any person with a security-based swap (“SBS”) position that exceeds a certain threshold to promptly file with the Commission a schedule disclosing certain information related to its SBS positions and positions in securities underlying such transactions (the “Proposed Rule”). Our comments are focused on certain of the questions raised by the Commission in connection with the reopening of the comment period for the Proposed Rule and publication of supplemental data and analysis regarding the proposed reporting thresholds in the equity SBS market by the Division of Economic and Risk Analysis (“DERA”).¹ We write from the perspective of our clients that are large institutional investors who transact in the SBS market.

We support the Commission’s efforts to protect investors and maintain fair, orderly and efficient markets. While we continue to have significant concerns about the Proposed Rule and the Commission’s statutory authority to adopt the Proposed Rule, as discussed in our previous letter,² we appreciate the opportunity to comment on specific questions raised in the Reopening Release.

¹ Proposed 17 C.F.R. § 240.10B-1; *see also* Reopening of Comment Period for Position Reporting of Large Security-Based Swap Positions, SEC Release No. 34-97762 (June 20, 2023) (the “Reopening Release”), *available at* <https://www.sec.gov/rules/proposed/2023/34-97762.pdf>; Memorandum of the Division of Economic and Risk Analysis (June 20, 2023) (the “DERA Analysis”), *available at* <https://www.sec.gov/comments/s7-32-10/s73210-207819-419422.pdf>.

² *See* Comment Letter from Ropes & Gray LLP, Position Reporting of Large Security-Based Swap Positions (File Number S7-32-10) (March 21, 2022), *available at* <https://www.sec.gov/comments/s7-32-10/s73210-20120761-272941.pdf>.

In this comment letter we respectfully urge the Commission to consider the following changes to the Proposed Rule:

1. Modify the reporting threshold for equity SBS to remove the dollar threshold and increase the percentage threshold to 10% of any class of an issuer's equity securities;
2. Allow reporting parties to offset long and short SBS positions (*e.g.*, offsetting long positions with short positions where the underlying reference security is the same); and
3. Fully consider the impacts of the Proposed Rule and particularly the costs that will be imposed on institutional investors in a comprehensive cost-benefit analysis.

I. The Commission Should Modify the Reporting Thresholds for Equity SBS to Remove the Dollar Threshold and Increase the Percentage Threshold to 10% of a Class of an Issuer's Equity Securities

We urge the Commission to eliminate the dollar-based threshold and adopt a single reporting threshold for equity SBS positions of 10% of a class of an issuer's equity securities. By removing the arbitrary dollar threshold and adopting only a percentage threshold, the Commission will be in a better position to achieve its policy goals of (i) providing market participants and regulators with information that may indicate that a person is accumulating a large SBS position and (ii) alerting market participants and regulators to the existence of concentrated exposures to a limited number of counterparties. In both cases, we believe that a 10% threshold would enable the Commission to focus on those positions that actually are significant and have the potential to be impactful to the market, given the wide range of sizes of market capitalization of issuers over whose securities our clients enter into equity SBS positions.

The proposed reporting threshold for equity SBS is bifurcated, including both a dollar threshold and a threshold based on the total number of shares attributable to the SBS position as a percentage of the outstanding number of shares of that class of equity securities. The Commission notes in the Proposing Release that "these thresholds were constructed to be low enough to capture any positions that could potentially have a significant effect on the equities markets, and potentially issuers of equity securities and their security holders, yet also high enough to avoid over-reporting, which could limit the effectiveness of the rule."³ We respectfully disagree that the proposed thresholds would achieve this intended balance.

The Commission Should Remove the Dollar Threshold. The dollar-based threshold for SBS on equity securities should be removed altogether. A dollar-based threshold is not calibrated to the risks or potential impact of any given SBS position, given that the extent of securities outstanding for different issuers can vary substantially. For example, for an issuer with a market capitalization

³ Proposing Release at 77.

of \$77 billion (the mean market capitalization of the S&P® 500 Index), requiring reporting of an SBS with a gross notional amount of \$300 million would require reporting of an SBS that provides economic exposure to only 0.39% of the issuer's securities (assuming one class of securities). This seems unreasonably low, especially when disclosure of physical holdings of equity securities under Schedules 13D and 13G is only triggered at 5%. We appreciate the Commission's goal of establishing thresholds that are easy to calculate, but adopting thresholds that are more closely tied to the purposes of the Proposed Rule would provide more useful information to the Commission and the market, minimizing the "noise" of immaterial SBS transaction reporting and minimizing compliance burdens on institutional investors, a segment of the industry that may be ill-equipped to report the details of complicated SBS transactions. Given the wide range of market capitalization of issuers, we believe that a dollar-based notional threshold is inappropriate and will result in over-reporting of information in a manner that does not further the Commission's goals or provide useful information to either the Commission or the public. A low and arbitrary dollar threshold would impose significant compliance and operational burdens on institutional investors, and likely would harm liquidity in the equity SBS markets and deter institutional investors from investing in those markets.

If the Commission Adopts an Equity SBS Reporting Requirement, the Commission Should Adopt a Percentage Reporting Threshold of 10% of a Class of an Issuer's Equity Securities. Under the Proposed Rule, market participants would be required to file a Schedule 10B once the "Security-Based Swap Equivalent Position" (as defined in the Proposed Rule) represents more than 5% of a class of equity securities. Additionally, once a Security-Based Swap Equivalent Position represents more than 2.5% of a class of equity securities, the calculation of the Security-Based Swap Equivalent Position also includes in the numerator all of the underlying equity securities owned by the holder of the Security-Based Swap Position, as well as the number of shares attributable to any options, security futures, or any other derivative instruments based on the same class of equity securities.

If the Commission adopts an equity SBS reporting requirement, we believe that requiring reporting when a market participant holds SBS that provide exposure to more than 10% of a class of an issuer's equity securities would more appropriately balance the significant costs and burdens of the Proposed Rule against the Commission's stated goal of enhancing integrity of the SBS market by having tools to monitor for large concentrated positions, counterparty risk, and potentially fraudulent behavior, as compared with the currently proposed thresholds. In addition, a 10% reporting threshold would mitigate the risk of over-reporting, which the Commission acknowledged in the Proposing Release could limit the effectiveness of the Proposed Rule. Setting an appropriate threshold is critically important given the context of the near real-time reporting and public dissemination of the sensitive and proprietary information required by the Proposed Rule. Such

potential harm to investors' legitimate practices and to market liquidity more generally has also been acknowledged by the Commission.⁴

Fulsome details about all SBS transactions are already available to the Commission under market participants' Regulation SBSR transaction reports. According to the DERA Analysis, which used this data, during the measurement period, on a daily basis, there were on average 46 market participants with positions that exceeded the 10% threshold, and the largest number of market participants that exceeded the 10% threshold on any given day was 60. Additionally, the DERA Analysis notes that market participants had, on average on a daily basis, 174 gross positions that exceeded the 10% threshold, and the largest number of such gross positions on any given day was 292. This data indicates that there will be regular reporting of the most significant SBS positions if the Commission adopts a 10% threshold. This reporting is in addition to the reporting of every SBS that the Commission receives under Regulation SBSR.

We believe it would be appropriate to set the reporting threshold for SBS positions at a higher level than the thresholds the Commission has adopted for cash positions. Pursuant to its Schedule 13D/G beneficial ownership reporting regime, the Commission collects information from investors that accumulate positions in public securities (using a 5% reporting threshold). Unlike holding direct beneficial ownership of a security, a cash-settled SBS position provides no voting rights, dispositive rights or control over the underlying issuer. Accordingly, the holder of an SBS does not have the same potential impact on the issuer as the holder of shares of the issuer's securities. In addition, another reason why a threshold higher than the 5% Schedule 13D/G standard would be appropriate is that the Proposed Rule would require reporting in respect of a dramatically broader scope of products than Schedule 13D/G (including even SBS in respect of narrow-based indices that merely include the same class of shares as one of their components).

Notwithstanding the number of equity SBS positions referenced in the DERA Analysis that exceeded the 10% threshold, the Commission has cited no evidence of widespread abuse, market manipulation or heightened risk to the market due to equity SBS positions. At the same time, the Commission has acknowledged the potential detrimental impact of over-reporting on the effectiveness of the Proposed Rule as well as the potential harm to the market that would result from the near real-time reporting and public dissemination of the sensitive and proprietary information required by the Proposed Rule. The Commission should more appropriately balance

⁴ See, e.g., Proposing Release at 86 and Final Rule: Regulation SBSR – Reporting and Dissemination of Security-Based Swap Information, SEC Release No. 34-74244 at 535 (“While the Commission has considered whether there could be a reduction in the programmatic benefits of public dissemination associated with providing too much time before a security-based swap transaction must be reported and publicly disseminated, the Commission also has considered that 24 hours might be too little time for liquidity providers to manage inventory risk. If a liquidity provider who engages in a large trade, or in a trade in an illiquid security, cannot offset the risk within 24 hours, the costs for providing liquidity could rise, resulting in less liquidity provision (*i.e.*, less size provided at the desired price, or the same size provided at worse prices). This result might be avoided in a regulatory environment offering a longer delay between the time of execution of a security-based swap and the time that it must be reported and publicly disseminated.”), available at <https://www.sec.gov/rules/final/2015/34-74244.pdf>.

these considerations and, if it adopts this new reporting requirement, it should establish a reporting threshold of 10%.

II. The Commission Should Allow Reporting Parties to Offset Long and Short SBS Positions over the Same Underlying Security

We urge the Commission to amend the Proposed Rule to allow investors to offset long and short SBS transactions over the same underlying security for purposes of calculating whether a reporting threshold has been breached. Requiring reporting based on gross thresholds does not accurately reflect actual market exposures and will lead to unnecessary and uninformative over-reporting.

The Commission notes in the Proposing Release that calculating the reporting threshold and reporting on a gross basis would enable the Commission and market participants to identify when a market participant has a large, concentrated position in an SBS on a single issuer, which has the potential to impact not only the market for other SBS on the same issuer, but also the applicable reference securities, even if that gross position consists of smaller positions that offset each other. The Commission notes that this would be “particularly informative where the offsetting positions are not with the same counterparty, where it may not be possible to net out any payment obligations between any two counterparties.”⁵

In the Proposing Release, the Commission references three key goals of the Proposed Rule:

1. Providing market participants (including counterparties, issuers and issuers’ stakeholders) and regulators with access to information that may indicate that a person (or group of persons) is accumulating a large SBS position, which in some cases could be indicative of potentially fraudulent or manipulative purposes or may pose larger risk to the markets or an issuer;
2. Alerting market participants and regulators to the existence of concentrated exposures to a limited number of counterparties, which should inform those market participants and regulators of the attendant risks, allow counterparties to risk manage by requiring additional collateral and lead to better pricing of the SBS with respect to transactions with persons holding large positions in those SBS; and
3. In the case of manufactured or other opportunistic strategies in the CDS market, providing market participants and regulators with advance notice that a person (or a group of persons) is building up a large CDS position which could create an incentive to vote against their interests as a debt holder, possibly with an intent to harm the company, even if such conduct is not inherently fraudulent.

⁵ See Proposing Release at 70-71.

None of these goals is met by requiring reporting of gross (as opposed to net) SBS positions. With respect to the first policy goal, we believe that reporting on a net basis would better enable the Commission to achieve its goal. An SBS is just a right to receive (and an obligation to make) certain payments based on the return of the underlying securities or if certain events occur with respect to underlying securities. An SBS provides no voting rights and provides no ability to control the underlying issuer. If a market participant has offsetting long and short positions, that just means that the market participant has less economic exposure to the issuer. Reporting on a net basis would enable the Commission to understand if a market participant *actually* has built a large long (or short) position – albeit via swap transactions that do not provide direct voting or control rights. If a market participant has a concentrated long gross exposure to SBS with respect to a specific issuer but also has a concentrated short gross exposure to SBS in respect of the same issuer, the long exposure offsets the risk of the short exposure and vice versa. The ability – and incentive – for a market participant to manipulate the market is much lower when the market participant’s actual overall net exposure to the issuer is small. Similarly, a long CDS position does not create an incentive to vote against a market participant’s interests as a debt holder if the market participant has an offsetting short CDS position with respect to the same security; the market participant’s incentives instead arise from its net position.

This is true regardless of whether the long and short positions are with the same counterparty. If there are different counterparties, there is the risk that one of the counterparties will default on its SBS and not make its payments. However, that is not what happens in the ordinary course, and it does not make sense to impose burdensome reporting requirements on parties with limited economic exposure to an underlying issuer because there is some possibility that one of their counterparties will default. The Commission will be able to achieve the goals noted above even if it allows investors to net long and short positions entered into with the same counterparty.

III. The Commission Should Undertake a Comprehensive Economic Analysis Before Proceeding with the Proposed Rule

We urge the Commission to refrain from taking further action with respect to the Proposed Rule until it has conducted a sufficient economic analysis, including consideration of costs and benefits and reasonable alternatives. Particularly now that a significant amount of transaction data is available to the Commission pursuant to its Regulation SBSR reporting regime – which took effect only one month before the Proposed Rule was issued – the Commission should consider the amount and nature of information regarding all types of SBS positions (and related direct securities holdings) that is available to it through existing reporting requirements.

At the time the Proposed Rule was issued, the Commission lacked sufficient data to evaluate the impact the reporting thresholds would have on SBS market participants or the number of equity SBS market participants that would be required to file reports, making it impossible for the Commission to accurately calibrate the reporting thresholds or to analyze the impact the Proposed

Rule would have on the SBS market.⁶ SBS transaction reporting had been in effect for a short period of time, and the Commission relied on a limited data set gathered from filings made by registered investment companies, which represent only one portion of the SBS market.

We commend the Commission and DERA for providing additional data regarding equity SBS to market participants based on information that is now available to it under the Regulation SBSR reporting regime. The DERA Analysis includes data on the number of equity SBS market participants and equity SBS positions that would exceed various reporting thresholds. While this helps to fill one of the gaps in the Commission's original economic analysis, a number of gaps remain. For example, the data appears to include only equity SBS that reference U.S. listed securities, which represent only a portion of what would be covered under the Proposed Rule. Also, the data does not address debt SBS. No requirement should be adopted with respect to debt SBS or SBS that reference securities other than U.S. listed securities until the Commission has analyzed the relevant data with respect to those transactions.

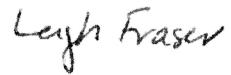
As noted in our previous comment letter, the Commission also should take into account the significant costs that would be incurred by institutional investors as a result of the Proposed Rule. These costs include not only direct operational, legal and compliance costs associated with monitoring positions and preparing reports, but also the costs associated with almost real-time public dissemination of proprietary information about SBS positions and investment strategies. By requiring almost immediate disclosure of an investor's positions and proprietary trading information, the Proposed Rule would have the effect of discouraging investors from participating in the market to avoid publicly disclosing sensitive and proprietary trading strategies and positions, a concern that the Commission does not appear to consider in any meaningful manner.

Before imposing these costly and burdensome requirements on institutional investors, most of whom are not set up to make real-time reports and are deeply concerned about the impact public dissemination would have on their ability to protect proprietary investment and trading strategies and positions, we urge the Commission to complete a comprehensive cost-benefit analysis and give the public an opportunity to review and comment on the data.

Thank you for your consideration of our comments.

⁶ See Proposing Release at 105 ("Because reporting transaction data regarding other types of [SBS] has only recently become mandatory, the Commission does not yet have a precise estimate as to the number of persons we would expect to file reports with respect to [SBS] Positions consisting of [SBS] based on equity securities and other debt securities (non-CDS).").

Very truly yours,



Leigh R. Fraser



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