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Via Electronic Mail: rule-comments@sec.gov

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. S7-03-10; Release No. 34-61379

Dear Ms. Murphy,

The Securities and Exchange Commission ("Commission") has requested comments regarding its proposed new Rule 15c3-5 under the Securities Exchange Act of 1934.[1] The proposed rule would require broker-dealers to establish greater risk management controls to regulate customer trading that occurs via sponsored and direct market access arrangements. I appreciate the opportunity to comment on the new Proposed Rule. I believe the rule's most important benefits—mitigating the dangers of "naked" access and reducing the potential for regulatory arbitrage—likely outweigh the rule's potential, significant costs.

The new Proposed Rule would require broker-dealers to adopt risk management controls that are reasonably designed to guard against financial, regulatory and other risks that occur when customers access the financial exchanges through sponsored or direct (i.e. "naked" access.) The language of the Proposed Rule suggests the Commission is particularly concerned with "direct" or "naked" access, whereby market participants execute trades directly, by using the broker-dealer's own Market Participant Identification (MPID). According to one report cited by the Commission, "naked access" accounts for 38 percent of trading volume nationally.[2] This Proposed Rule 15c3-5 is a welcome acknowledgment by the Commission of the systemic risks that "naked" access poses to the financial markets.

Allowing customers to trade via "naked" access leaves the entire financial market vulnerable to innocent human errors. One powerful example of this occurred on September 30, 2008, when the human errors of one market participant caused Google stock to drop in value by

[1] 17 C.F.R. Part 240.
[2] Jonathan Spicer, Naked Access Now 38 Percent of U.S. Trading, December 14, 2009, http://www.reuters.com/article/idUSTRE5BD0HT20091214

93% in one day.[3] Similar events have occurred in Japan, where one of the country's largest brokerage firms (Mizuho Securities) suffered a large loss after one of its traders mistakenly transposed an order's price and quantity, leading to a sale of 610,000 shares for one yen.[4] In today's volatile and fast-paced financial markets, these huge swings in value can have devastating effects on individual investors, companies and on the economy as a whole. The new Proposed Rule 15c3-5 would prevent these problems from reoccurring, by requiring broker-dealers to adopt a pre-trade clearing system that would catch any clearly erroneous trades before they are placed on an exchange. The rule would also prevent customers from engaging in trades beyond the credit capacity of their broker-dealers. This would help prevent credit defaults that can have harmful spillover effects on the wider market. The Commission appropriately cited many of these incidents as justification for the proactive approach embodied in its own proposed Rule 15c3-5.[5]

Adoption of this Proposed Rule by the Commission would also help reduce the potential for regulatory arbitrage between exchanges. As of January 13, 2010, the Financial Industry Regulatory Authority (FINRA) has adopted, and the Commission has approved, new requirements for risk management controls by broker-dealers that provide direct market access to trading customers.[6] This requirement goes beyond the applicable rules governing the New York Stock Exchange (NYSE), where broker-dealers are allowed to rely on contractual assurances that their customers have instituted appropriate risk controls.[7] Enacting Proposed Rule 15c3-5—which requires all broker-dealers to have direct and exclusive responsibility for risk management controls--would eliminate this discrepancy. Promulgating the same Rule for both of the major national exchanges (as well as the ATSs) would make it difficult, if not impossible, for the risks of "naked" access to find a new home in a different regulatory forum.

As Commission Chairwoman Schapiro has said publicly, "Unfiltered access is similar to giving the car keys to your friend and letting him drive unaccompanied."[8] This Proposed Rule 15c3-5 will rightly bring an end this (heretofore permitted) behavior. This is no small benefit to the public interest, and likely outweighs the potential costs of the Proposed Rule. In particular, the Proposed Rule will impose a disproportionately high cost of compliance on small broker-dealers (estimated to be around 1,000 out of 5,000).[9] In today's volatile and interconnected financial markets, this burden is just one of the many unfortunate but necessary costs of doing business.

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[3] Michael J. de la Merced, *The Strange Case of the Google Stock Plunge*, New York Times Dealbook Blog, http://dealbook.blogs.nytimes.com/2008/09/30/the-strange-case-of-the-google-stock-plunge/

[4] *Mizuho Securities Loses $223M in Trading Error*, http://www.risk.net/oprisk-and-compliance/news/1499817/mizuho-securities-loses-usd223m-trading-error

[5] Proposed Rule 15c3-5, C.F.R. Part 240.

[6] Nasdaq Market Access Approval Order, Securities Exchange Act Release No. 61345 (January 13, 2010) (SR-NASDAQ-2008-104).

[7] *See, e.g.*, NYSE Rule 123B.30, NYSE Alternext Equities Rule 123B.30, NYSE Amex Rule 86, NYSE Arca Rules 7.29 and 7.30, NYSE Rule 86.

[8] SEC Press Release, Jan. 13, 2010, http://www.sec.gov/news/press/2010/2010-7.htm

[9] Based on Commission estimates cited in Proposed Rule 15c3-5, note 33, 17 C.F.R. Part 240.