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**SUBMITTED ELECTRONICALLY**

November 17, 2016

Ms. Gillian M. Burgess  
Counsel, Legal Division  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> Street and Constitution Avenue N.W.  
Washington, D.C. 20551

***Re: Incentive-Based Compensation Arrangements, File Number S7-07-16***

Dear Gillian:

Thank you for participating in the meeting with SIFMA on Wednesday, November 2, 2016 to discuss the re-proposed rule on incentive-based compensation arrangements under Section 956 of Dodd-Frank (the "Proposed Rule"). We appreciate the time taken by you and the other representatives of the Agencies to discuss issues that are critical to us and to SIFMA member firms. As part of the discussion, we recommended that certain types of assets be excluded from the definition of "average total consolidated assets" for purposes of the Proposed Rule, including those balance sheet assets of a carrying broker-dealer that are already effectively protected from the type of risk-taking that is the stated concern of the Proposed Rule — *i.e.*, the aggregate net balance owed to customers that is required to be "locked up" and deposited in a separate bank account and held exclusively for the benefit of those customers (the "Customer Reserve Account") pursuant to Rule 15c3-3 of the Securities Exchange Act of 1934 (the "Customer Protection Rule").

In the meeting, you asked for examples of other rules or regulatory actions in which certain assets that are consolidated on a company's financial statements for accounting purposes have been excluded from similar regulatory asset thresholds. The following discussion (i) summarizes our reasoning for excluding the assets in the Customer Reserve Account for broker-dealers and (ii) provides a relevant example of the exclusion of assets under management for investment advisers under the Proposed Rule. For more detailed analysis, please refer to the comment letter filed by National Financial Services LLC on July 21, 2016 (<https://www.sec.gov/comments/s7-07-16/s70716-23.pdf>) and the supplemental response filed by SIFMA in connection with the meeting on November 2.

**Exclusion of the "Lock Up"**

The assets "locked up" in the Customer Reserve Account should be excluded from the calculation of the carrying broker-dealer's "average total consolidated assets" for purposes of the Proposed Rule because the Customer Protection Rule (1) prohibits the carrying broker-dealer

from using the “locked up” customer assets to finance any part of its proprietary business; and (2) requires the carrying broker-dealer to invest the Customer Reserve Account assets only in cash or “qualified securities” (e.g., U.S. Treasury securities) – thereby protecting those assets and the customers for whose benefit they are held in case of the broker-dealer’s insolvency and reducing the risk of such insolvency. The employees of the carrying broker-dealer have no ability to take inappropriate risks with respect to the assets in the Customer Reserve Account – and their decision-making authority is so limited that these assets are already shielded from the behavior that Section 956 of Dodd-Frank is intended to prevent. Further, treating the Customer Reserve Account assets as if they may be vulnerable to inappropriate risk-taking would be inconsistent with the SEC’s long-standing policy regarding the inviolable manner in which carrying broker-dealers are required to safeguard those assets, as evidenced by a recent imposition of a \$415 million fine against a major broker-dealer.<sup>1</sup>

**Exclusion Example: Assets Under Management**

Under the Proposed Rule, for an investment adviser, “average total consolidated assets” is defined as total assets (exclusive of non-proprietary assets) shown on the balance sheet for the most recent fiscal year end. The SEC has further clarified that non-proprietary assets, *such as client assets under management*, would not be included, regardless of whether they appear on an investment adviser’s balance sheet. Thus, the Agencies have properly recognized that, although certain assets may be included on a firm’s balance sheet for accounting purposes, they are not vulnerable to the sort of risks that Section 956 of Dodd-Frank is intended to prevent. Those assets do not present a risk of “material financial loss” to a “covered institution” because the institution does not own them and they are already effectively protected from inappropriate risk taking by a robust regulatory regime. The extensive regulations and contractual obligations governing the broker-dealer “lock-up” in the Customer Reserve Account and investment adviser assets under management insulate them equally well from inappropriate risk and eliminate the need for Section 956 of Dodd-Frank to apply to them. Both types of assets should therefore be excluded from the calculation of a covered institution’s “average total consolidated assets” for purposes of the Proposed Rule.

\* \* \* \* \*

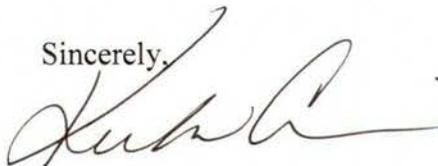
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<sup>1</sup> U.S. Sec. Exch. Comm’n, “Merrill Lynch to Pay \$415 Million for Misusing Customer Cash and Putting Customer Securities at Risk”, Press Release No. 2016-128 (June 23, 2016).

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National Financial Services LLC appreciates the opportunity to provide additional information on the Proposed Rule. We would be pleased to respond to any questions that you may have based on this letter or our July 21 comment.

Sincerely,



Karen M. Crupi  
Senior Vice President & Deputy General Counsel  
Chief Legal Officer, National Financial Services LLC

cc: The Honorable Mary Jo White, Chair, SEC  
The Honorable Kara M. Stein, Commissioner, SEC  
The Honorable Michael S. Piwowar, Commissioner, SEC

Mr. Stephen I. Luparello, Director, Division of Trading & Markets, SEC  
Mr. Gary Barnett, Deputy Director, Division of Trading & Markets, SEC  
Mr. Michael Macchiaroli, Associate Director, Division of Trading & Markets, SEC  
Mr. Thomas McGowan, Associate Director, Division of Trading & Markets, SEC  
Mr. Randall Roy, Deputy Associate Director, Division of Trading & Markets, SEC  
Mr. Raymond A. Lombardo, Assistant Director, Division of Trading & Markets, SEC  
Ms. Natasha V. Greiner, Branch Chief, Division of Trading & Markets, SEC  
Ms. Melissa R. Harke, Branch Chief, Division of Investment Management, SEC  
Mr. Kevin D. Schopp, Special Counsel, Division of Trading & Markets, SEC  
Mr. Sirimal R. Mukerjee, Senior Counsel, Division of Investment Management, SEC  
Ms. Jennifer Juergens, Financial Economist, Office of Financial Intermediaries, SEC  
Mr. David Bloom, Branch Chief, Division of Trading & Markets, SEC

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cc: Mr. Michael Solomon, FRB  
Mr. Michael Waldron, FRB  
Ms. Suzanne Williams, FRB  
Ms. Teresa Scott, FRB  
Mr. Joe Maldonado, FRB  
Ms. Meg Donovan, FRB  
Mr. Steve Bowne, FRB  
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Ms. Emily Rowland, SEC  
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Mr. Vladimir Ivanov, SEC  
Mr. George Papadakis, SEC