BY EMAIL AND OVERNIGHT MAIL

June 15, 2007

Ms. Nancy M. Morris
Secretary
United States Securities and Exchange Commission
Mail Stop 1090
100 F Street NE
Washington, DC 20549-1090

Re: Amendments to Financial Responsibility Rules for Broker-Dealers
(Release No. 34-55431; File No. S7-08-07)

Dear Ms. Morris:

First Clearing, LLC ("First Clearing")[1] appreciates the opportunity to comment on the proposed rulemaking[2] by the Securities and Exchange Commission (the "Commission") to amend certain provisions of its financial responsibility rules applicable to broker dealers (the "Proposed Amendments"), including the following rules promulgated under the Securities Exchange Act of 1934: Rule 15c3-1 (the net capital rule)[3], Rule 15c3-3 (the customer protection rule)[4], Rules 17a-3 and 17a-4 (the books and records rules)[5], and Rule 17a-11 (which requires broker-dealers to notify regulators regarding certain aspects of their capital compliance and recordkeeping).[6]

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[1] First Clearing, along with Wachovia Securities, LLC and Wachovia Securities Financial Network, LLC, comprise the Retail Brokerage Group of Wachovia Corporation. First Clearing carries accounts and provides trade execution and other securities-related services for the Retail Brokerage Group as well as for approximately 130 unaffiliated correspondent retail broker dealers. Wachovia Securities, LLC is the third-largest broker-dealer in the United States by client assets and the fifth-largest provider of managed accounts through 2,685 locations in 49 states and the District of Columbia with approximately 8,100 Financial Advisors providing services to clients across 5.3 million client accounts. Wachovia Securities Financial Network, LLC is an introducing broker-dealer whose primary business is to partner with independent Financial Advisors to provide them with the suite of products and resources available through Wachovia Securities.

[2] Securities and Exchange Commission Release No. 34-55431, 17 CFR 240, File No. S7-08-07

[3] 17 CFR 240.15c3-1

[4] 17 CFR 240.15c3-3

[5] 17 CFR 240.17a-3 and 17 CFR 240.17a-4

[6] 17 CFR 240.17a-11

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We applaud the Commission for its efforts to update and refine these financial responsibility rules in order to address several emerging areas of concern regarding broker-dealer financial requirements. Given the nature and scope of the rulemaking proposal, we will focus our comments on the issues that are of greatest interest to us. This letter will address the proposed rule amendments in regards to the following areas:

- The Customer Protection Rule, including Proprietary Accounts of Broker-Dealers
- Banks Where Special Reserve Deposits May Be Held
- Expansion of the Definition of Qualified Securities
- to Include Certain Money Market Funds
- Allocation of Customers' Fully-Paid and Excess Margin Securities to Short Positions
- Treatment of Free Credit Balances

In addition, we will respond to the request by the Commission for comments with respect to Accounting for Third Party Liens on Customer Securities Held at a Broker-Dealer.

A. Proprietary Accounts of Broker-Dealers

The Proposed Amendments would modify Rule 15c3-3 to require broker-dealers to treat proprietary accounts they carry for U.S. or foreign broker-dealers ("PAB") much like customer accounts for purposes of the reserve formula requirements under Rule 15c3-3. A carrying broker-dealer would need to perform a separate reserve formula calculation with respect to cash and securities held in each PAB and establish a separate reserve account for such PAIB assets.[7] In these respects, the amendments codify many requirements set forth in a 1998 no-action letter regarding the proprietary accounts of introducing brokers,[8] in which the Commission staff specified conditions under which an introducing broker could include PAB assets as allowable assets in their net capital computations.

We believe that the Proposed Amendments should clarify that the PAB computation is limited to cash and securities in the introducing broker's PAB account and does not include any other type of unsecured receivables due from the broker-dealer carrying the account.

In order to appropriately address the treatment of proprietary assets of the introducing broker that do not derive from proprietary inventory transactions, we suggest that the Commission consider revising paragraph (c) of the net capital rule to specifically except receivables from a carrying broker-dealer related to transactions in introduced accounts which are customary and normal in the ordinary course of business, outstanding 30 days or less. These receivables would be related to commissions as well as transactional and other fees related to introduced accounts.

As noted in footnote 19 to the Proposed Amendments, paragraph (c) of the net capital rule already provides an exception to the non-allowability of certain unsecured receivables for

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7 Proposed amendments to paragraphs (e) – (g) of Rule 15c3-3; Rule 15c3-3a passim.

commissions receivable from another broker-dealer outstanding 30 days or less.[8] Furthermore, footnote 19 states "...This exception is limited to receivables from a clearing broker-dealer related to transactions in accounts introduced by the broker-dealer."[9] In our view, the reference in the footnote to receivables associated with "transactions in accounts" does not reflect the broader range of services rendered in today's securities industry environment by clearing brokers to introducing brokers that are related to transactions in introduced customer accounts. As such, we suggest that the language in the exception in paragraph (c) be broadened to encompass receivables of the introducing broker that are related to commissions as well as transactional and other fees in order to clarify the scope of this exception.

B. Banks Where Special Reserve Deposits May Be Held

The Proposed Amendments would prohibit a broker-dealer from counting toward its reserve account requirements under the customer protection rule (i) any cash deposited at an affiliated bank, and (ii) any cash deposited at an unaffiliated bank to the extent such deposit exceeds 50% of the broker-dealer's excess net capital (based on its most recently filed FOCUS report) or 10% of the bank's equity capital (based on its most recent Call Report or Thrift Financial Report).[10]

We recommend that the Commission not revise the customer protection rule to exclude cash deposited with an affiliated bank for purposes of satisfying the reserve account requirement. Cash is not subject to any clearance or settlement risk. Cash is also not subject to market movements and is not impacted by market manipulation schemes. While cash may be fungible, banks that conduct transactions with an affiliate are subject to heightened scrutiny by the Federal banking supervisors pursuant to Sections 23A and 23B of the Federal Reserve Act.[11]

Special Reserve Bank Accounts for the Benefit of a Broker-Dealer's Customers are governed by an agreement between the clearing broker and a bank - which must be approved by the broker-dealer's designated examining authority – that is required to contain no-lien provisions which precludes the bank from exercising any right of set-off against the account. This type of agreement provides enhanced assurance as to the integrity of the monies deposited by broker-dealers for the benefit of customers at affiliated as well as non-affiliated banks. Finally, eliminating the ability of a broker-dealer to deposit Customer Reserve monies with an affiliated bank may competitively harm the broker-dealer by eliminating an option which could provide the firm with the highest rate of return on deposited funds. This could be especially problematic in situations where certain clearing brokers, based on their organization and business model, do not have qualified securities for deposit.

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8 Securities and Exchange Commission Release No. 34-55431, 17 CFR 240, File No. S7-08-07. Section II. A. 1

9 Ibid. Section II. A. 1.

10 Proposed paragraph (e)(5) under Rule 15c3-3.

11 12 U.S.C Section 221 et seq.

If the Commission is concerned that the risk of loss is higher at an affiliated bank versus a non-affiliated bank, the Commission should consider allowing Customer Reserve deposits at only those affiliated banks that are considered "well capitalized" banks.[12] Additionally, the Commission could explore with the Federal Reserve Board of Governors the possibility of jointly adopting regulations that would further ensure the integrity and availability of cash deposited by a broker-dealer in a Special Reserve Bank Account held with an affiliated bank.

If the Commission's concern runs to the concentration of broker-dealer customer funds at any one bank, we would recommend that the Commission modify the proposed rule to limit the amount of the cash deposited in any bank to 50% of the broker-dealer's excess net capital or 10% of the bank's equity capital thresholds, irrespective of whether the bank is affiliated or non-affiliated.

C. Expansion of the Definition of Qualified Securities to Include Certain Money Market Funds

The Proposed Amendments would expand the definition of "qualified securities" eligible to meet reserve account requirements to include money market funds (as described in Rule 2a-7 of the Investment Company Act of 1940 ("Rule 2a-7")) that: (i) invest only in securities issued or guaranteed by the United States as to principal and interest; (ii) are not affiliated with the broker-dealer; (iii) agree to redeem fund shares in cash no later than the business day following a redemption request by a shareholder; and (iv) have net assets equal to at least 10 times the value of the shares held by the broker-dealer for purposes of its reserve account requirements.[13]

Although we support the proposed expansion of the definition of "qualified securities" to include money market funds, we believe that this expansion should not come at the expense of prohibiting broker-dealers from depositing cash in affiliated banks to satisfy Customer Reserve Computation requirements. We strongly disagree with the Commission's view that this is an

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12 Congress adopted these capitalization standards in the Federal Deposit Insurance Corporation Improvement Act of 1991, and the standards are consistent across all four federal banking regulators. "Well capitalized" banks have: (i) a total risk-based capital ratio of 10.0%or greater; (ii) a Tier 1 risk-based capital ratio of 6.0% or greater; and (iii) a leverage ratio of 5.0% or greater. ["Adequately capitalized" banks have: (i) a total risk-based capital ratio of 8.0% or greater; (ii) a Tier 1 risk-based capital ratio of 4.0% or greater; and (iii) a leverage ratio of 4.0% or greater (or 3.0% or greater if the bank meets certain regulatory criteria).] See 12 CFR 6.4 (Office of the Comptroller of the Currency); 12 CFR 208.43 (Board of Governors of the Federal Reserve System); 12 CFR 325.103 (Federal Deposit Insurance Corporation); 12 CFR 565.4 (Office of Thrift Supervision).

Under this proposal, cash deposits for reserve account purposes could not be maintained at banks that are ["adequately capitalized" (total risk-based capital ratio of 8.0% or greater),] "undercapitalized" (total risk-based capital ratio of less than 8.0%), "significantly undercapitalized" (total risk-based capital ratio of less than 6.0%), or "critically undercapitalized" (total risk-based capital ratio equal to or less than 2.0%).

13 Proposed amendment to paragraph (a)(6) of Rule 15c3-3.

"operational benefit"[14] to firms which would be impacted from the proposed amendments discussed under B. above. Certain clearing firms, based on their organization and business model, do not have qualified securities to deposit into Special Reserve Bank Accounts.

We also believe that the definition of "qualified securities", if expanded to include money market funds, should not be limited to funds of non-affiliated companies of a broker-dealer. In our view, we do not think it is the case that a money market fund, comprised only of US issued/guaranteed instruments, sponsored by a company that is an affiliate of a broker-dealer which is subject to the same regulatory standards and oversight as non-affiliated funds, could be subject to any greater risk of loss than a non-affiliated money market fund. The assets of the fund – US issued/guaranteed instruments – have no correlation to financial health of a broker-dealer or to respective holding company of the broker-dealer or the affiliated company sponsoring the fund.

D. Allocation of Customers' Fully-Paid and Excess Margin Securities to Short Positions

The Proposed Amendments would add a new paragraph (d) (4) to Rule 15c3-3 requiring a broker-dealer with a possession or control deficit in a security included on its books and records as a proprietary short position or a short position for another person for more than 10 business days (or more than 30 calendar days if the broker-dealer is a market maker in the securities) to take prompt steps to obtain physical possession or control of such securities. Currently, there is no requirement to act when a customer's fully paid or excess margin long position allocates to a short position; instead, the broker-dealer includes the value of the security as a credit in the reserve formula. In proposing this amendment, the Commission expressed concern that under the current approach a broker-dealer may "monetize the customer's security ... contrary to the customer protection goals of Rule 15c3-3, which seeks to ensure that broker-dealers do not use customer assets for proprietary purposes."[15]

We are unclear as to the benefits of this proposed additional regulation given the potential impact on the practice of short selling which is a fundamental activity inherent within the securities industry. As noted above, when a customer's fully paid or excess margin long position allocates to a short position, the broker-dealer includes the value of the security as a credit in the reserve formula which already serves to provide the customer with adequate protection.

E. Treatment of Free Credit Balances

The Commission is proposing to add a new paragraph (j) to Rule 15c3-3 that would generally prohibit a broker-dealer from converting, investing or transferring customers' free credit balances except under certain circumstances. Among other provisions, this new paragraph would establish consent, notification and disclosure requirements for "sweep" arrangements

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[14] Securities and Exchange Commission Release No. 34-55431, 17 CFR 240, File No. S7-08-07, Section II. A. 3

[15] Ibid. Section II. A. 4.

under which free credit balances are automatically invested in a "money market mutual fund product" or an "interest-bearing account product at a bank" without a specific order or authorization from the customer for each such transfer. [16]

We recommend that proposed paragraphs (j)(2)(ii) and (iii) not limit the type of products broker-dealers can use for sweep arrangements to only money market funds or bank deposit products. The proposed rule should permit other products without specifically limiting the exact type. In addition, these paragraphs should also be revised to clarify that they cover not only the transfer of free credit balances, but also the transfer of balances from one sweep product to another if appropriate notice and disclosures have been provided to the customer.

Proposed paragraphs (j)(2)(ii)(B) and (iii)(A) would require broker-dealers to provide customers on an ongoing basis with all disclosures and notices required by the broker-dealer's SRO. We request that the Commission clarify the source and meaning of this requirement.

We also recommend that the Commission not adopt proposed paragraphs (j)(2)(ii)(C) and (B) to the extent such paragraphs would require clients be informed on quarterly statements that balances in sweep products can be withdrawn on demand. Such a requirement may conflict with prior disclosed terms of a money market fund or bank deposit account, which may indicate that it could take up to seven days to pay requests for withdrawals.

F. Accounting for Third Party Liens on Customer Securities held at a Broker-Dealer

The Commission requested comment as to how third-party liens against customer fully paid securities carried by a broker-dealer should be treated under its financial responsibility rules. In particular, the Commission specifically inquired whether a broker-dealer carrying securities subject to such liens should be required to: (i) include the amount of the customer's obligation to the third party as a credit item in the Reserve Formula; (ii) move the securities subject to the lien into a separate pledge account in the name of the pledgee or (s); or (iii) record on its books and records and disclose to the customer the existence of the lien, the identity of the pledgee(s), the obligation of the customer, and the amount of securities subject to the lien.[17]

In our view, each of the suggested approaches imposes burdens and requirements on broker-dealers that do not serve to address the concerns noted by the Commission concerning these accounts. We believe that third party liens against customer fully paid securities should not be included as a credit to the Customer Reserve Formula nor should they be segregated into special pledge accounts nor should the broker-dealers books and records be required to disclose any information relative to the lien. As the Commission notes in the Proposed Amendments, the loan is made directly to the customer and does not involve the broker-dealer.[18] The broker-dealer is not the recipient of any funds collateralized by the lien on the customer fully paid securities. As

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16 Ibid. Section II. A. 5.

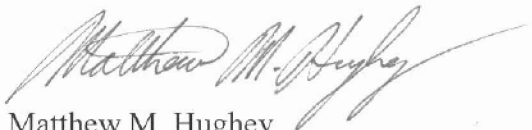
17 Ibid. Section III. B. 3.

18 Ibid. Section III. B. 3.

a practical matter, any broker-dealer that would be heading for a SIPA liquidation would be required by the supervisory authorities to transfer all customer accounts to another solvent broker-dealer that would substitute holding the fully paid for securities. In particular, we wish to note that the broker-dealer should not be penalized from a Customer Reserve Formula perspective, nor should it be required to segregate or otherwise incur books and records disclosure costs, simply because the customer has business transactions with third parties. Indeed, these accounts are already protected by existing Customer Reserve Formula and possession or control requirements.

We thank the Commission and its staff for their work in developing this proposing rule release and again appreciate the opportunity to comment on it. Please contact me at 804-398-6325 if you have any questions.

Sincerely,



Matthew M. Hughey
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