January 28, 2010

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

Re: Comments to Securities Exchange Act Release No. 61168
File No. SR-FINRA-2009-090

Dear Ms. Murphy:

The Securities Industry and Financial Markets Association[1] ("SIFMA") appreciates the opportunity to comment on Proposed FINRA Rule 5320 ("Proposed Rule"). In its Proposed Rule, FINRA seeks to consolidate NASD Rule 2111 governing market order protection and NASD IM-2110-2 governing limit order protection (collectively, the "Manning Rules"). FINRA also seeks to harmonize its Proposed Rule with NYSE Rule 92, where appropriate. For the reasons discussed in its earlier comment letter,[2] SIFMA is generally supportive of FINRA's Proposed Rule 5320 and believes that it is an important step forward in FINRA's efforts to harmonize its rules with the NYSE rules. Such standardization will provide significant benefits to all participants in the securities industry.

It is critical, however, that certain important modifications are made to the Proposed Rule before the SEC approves it. These modifications, discussed more fully below and in our earlier comment letter, relate to: (i) the expansion of the "no-knowledge" interpretation for market making desks to apply to OTC equity securities; (ii) the requirement to obtain and use a unique market participant identifier ("MPID"); (iii) the expansion of the hours of effectiveness of the Proposed Rule; and (iv) the application of the Proposed Rule to customer orders that are not "market" or "limit" orders.

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[1] The Securities Industry and Financial Markets Association (SIFMA) brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit www.sifma.org.

[2] See Letter Regarding Regulatory Notice 09-15 and NYSE Information Memo 09-13 from Ann Vlcek, Managing Director and Associate General Counsel, SIFMA to Marcia E. Asquith, Office of the Corporate Secretary, FINRA, dated April 30, 2009.

SIFMA also would like to emphasize that it is essential for NYSE Regulation to replace Rule 92 with a rule identical to FINRA's final rule.[3] In light of the increasing automation and the move to competing liquidity providers on exchanges, SIFMA does not believe that there are significant and relevant differences between trading on the Exchanges and trading on other markets that would warrant a rule different from FINRA's rule.[4] While FINRA's efforts to harmonize its rules are greatly appreciated, the ultimate goals of regulatory consistency and simplification of compliance obligations will not be achieved unless the Exchanges' rules are consistent with FINRA's final rule.

I. FINRA Should Extend the "No-Knowledge" Interpretation to Market Making Desks that Trade OTC Equity Securities.

SIFMA fully supports FINRA's decision to adopt the NYSE no-knowledge interpretation for market making desks in its Proposed Rule 5320.02 regarding exchange-listed securities. This new standard allows firms to "wall off" customer orders from their market making desks and rely on the no-knowledge interpretation with respect to customer orders held at walled-off desks.

SIFMA believes, however, that this standard should be extended to OTC equity securities. In this regard, SIFMA disagrees with the view that the OTC equity securities markets have not evolved to permit automated routing of orders to market centers for execution at the probable best prices. The OTC market is indeed evolving in the same manner as the exchanges. In particular, the pink sheet and bulletin board markets have evolved to become sufficiently liquid and electronic to warrant the application of the no-knowledge interpretation to market making desks. Also, as with exchange-listed securities, many firms may prefer to handle retail-sized customer orders in OTC equity securities on an automated basis, separate and apart from their proprietary trading desks, including market making desks. Accordingly, the evolution of the market for OTC equity securities makes FINRA's existing approach to the no-knowledge interpretation obsolete.

Moreover, the adoption of two different standards for exchange-listed and OTC equity securities is inconsistent with the stated intention of harmonization of rule sets between FINRA and NYSE. The Proposed Rule would do just the opposite by imposing the legacy NYSE standard on exchange-listed securities and the legacy NASD standard on OTC securities. Such an approach introduces unnecessary complexity, as well as compliance and programming inefficiencies.

SIFMA believes these additional burdens are unnecessary because the goal of customer protection would be appropriately served by the application of the NYSE no-knowledge standard to both exchange-listed and OTC securities. Also, notwithstanding any changes in the application of the knowledge standard to exchange-listed and OTC securities, firms would be

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[3] NYSE Information Memo 09-13 requests comment on the applicability of FINRA's Proposed Rule to the New York Stock Exchange ("NYSE") and NYSE Amex LLC ("Amex LLC") (collectively, the "Exchanges").

[4] In particular, SIFMA does not believe that there are any issues specific to trading on the Exchanges, including issues related to floor members, upstairs member organizations or market structure generally, that would warrant different regulatory treatment. See, e.g., Exchange Act Rel. No. 58845 (Oct. 24, 2008) (describing NYSE's implementation of a new trading model, including the elimination of the specialist category); NYSE Arca Rule 6.16 (NYSE affiliate exchange currently enforces a rule substantially similar to FINRA's Manning Rule).

required to execute orders for such securities in conformance with FINRA's best execution requirements.[5] Application of the no-knowledge interpretation to OTC equity securities, then, would provide firms with the flexibility to adapt their order routing practices as changes occur without sacrificing customer protection.

For these reasons, SIFMA urges FINRA to eliminate paragraph (b) of Proposed Rule 5320.02 and to apply paragraph (a) to OTC equity securities in addition to exchange-listed securities.

II. Firms Relying on the "No-Knowledge" Interpretation Should Not Be Required to Obtain a Unique MPID for Market Making Desks.

As part of the adoption of NYSE Regulation's standard for the no-knowledge interpretation in the Proposed Rule, FINRA would require firms to obtain and use a unique MPID for their market making desks. SIFMA believes that FINRA should not require firms to obtain and use unique MPIDs for market making desks. Rather, the use of separate MPIDs should be optional and it should be left up to each firm to decide whether or not it wants to use separate MPIDs as part of its information barriers.

In this regard, separate MPIDs could pose considerable administrative burdens for firms with additional costs. For example, introducing additional new MPIDs would make FINRA's Order Audit Trail System ("OATS"), Trade Reporting Facility ("TRF"), and other regulatory reporting requirements even more complex and expensive than they already are, and would exacerbate the potential for operational and technical problems with such reporting. Firms also may need to make related changes to their clearing systems. Further, new MPIDs may require certifications with existing clients for which firms clear and for all destinations to which firms route.

SIFMA does not believe there is a commensurate regulatory benefit to these costs because there are other, equally effective, ways for firms to establish internal control systems to monitor that information barriers between market making and non-market making desks are working. Indeed, firms have developed such systems – without the need for a separate MPID – in order to comply with NYSE Rule 92's no-knowledge interpretation. These systems have worked well, and firms have relied on them to monitor that information barriers are working. Also, information barriers have been used successfully in a variety of other regulatory contexts to control the improper flow of information – without the need to track trading information through separate MPIDs.[6]

To be sure, in 2003, the NASD acknowledged that the use of multiple MPIDs would not be necessary to establish and enforce effective barriers for purposes of the Manning Rules. In Notice to Members 03-74, the NASD addressed firms' concerns that the voluntary, elective use of multiple MPIDs might actually undermine information barriers. Significantly, NASD responded that an effective system of internal controls would *not* depend on the use of one or

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5 See NASD Rule 2320.

6 See, e.g., Rule 200(f) of Regulation SHO (regarding aggregation units).

more MPIDs. Rather, "[a]n effective system of internal controls must include specific policies and procedures that prevent each of the desks separated by information barriers from obtaining knowledge regarding orders or trading activity of the other desks."[7]

For these reasons, SIFMA believes that the Proposed Rule should not require firms to obtain a unique MPID, but rather should require them to establish, maintain and enforce written policies and procedures that are reasonably designed to prevent the prohibited trading under the Proposed Rule. Such an approach would be consistent with existing regulatory guidance and would provide individual firms with the flexibility to address the surveillance issue in the best manner possible for each particular firm.[8]

III. Consistent with the Status Quo, the Proposed Rule Should Not Apply to Extended-Hours Trading.

FINRA should not extend the application of the Proposed Rule to extended-hours trading. While SIFMA appreciates FINRA's clarification that firms may limit the life of a customer order to the period of normal market hours (9:30 a.m. to 4:00 p.m. Eastern Time), this limitation is not practicable for many customers' orders, such as orders that are designated as good-til-cancelled ("GTC"). For these orders, the Proposed Rule will create significant costs for firms, requiring them to revise their systems and procedures.

It is important to note that other rules related to order handling, like Regulation NMS, do not apply outside of regular trading hours.[9] We do not see any reason for distinguishing between these rules and the Proposed Rule. It is also important to note that customers that send orders for extended-hours trading tend to be more sophisticated and, hence, we believe such orders should be handled like institutional orders even if they are smaller in size or submitted by an individual investor. Indeed, FINRA recognizes that extended-hours trading is inherently risky and that investors may not receive the same prices they would during normal or after-hours market trading. For this reason, firms are required to provide disclosures to customers that highlight the risks specific to extended-hours trading.[10]

The costs and burdens of extended-hours trading may be particularly onerous for firms that execute transactions in foreign securities during extended-hours trading because of the fluctuations in U.S. and non-U.S. currency exchange rates. For example, if a customer places a GTC limit of $14.20 to buy a foreign security, and the local market in extended-hours trading is $14.21 x $14.25 in U.S. dollars, the broker-dealer may place an order to buy the security for its

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7 See NASD Notice to Members 03-74, at p. 787.

8 FINRA's rule filing gives an example of a firm that "walls off" retail order flow from market making flow, and requires the market making and retail desks to have separate MPIDs. SIFMA notes that that is no longer the standard practice for many firms, which now handle retail orders with an electronic routing and market making system. The "separate" desk is one that deals primarily with institutional orders, which is essentially the old "block trading" desk. In this scenario, it would not make sense to require the market making desk to obtain a unique MPID (which highlights, SIFMA believes, the questionable utility of requiring separate MPIDs in order to rely on the no-knowledge interpretation).

9 See Rules 600(b)(64) of Regulation NMS.

10 See NASD Rule 2265.

own account at $14.24. If, however, the currency exchange rate moves by the time the broker-dealer's order is executed (in favor of the U.S. currency), the order may receive an execution price lower than the original order price (*e.g.*, $14.20) and equal to or lower than the customer's limit order. If the Proposed Rule is applied to extended-hours trading in this scenario, the broker-dealer would have "traded ahead" of the customer's order. To avoid trading ahead, the broker-dealer would need to create systems and procedures to monitor currency fluctuations between the various local currencies and the U.S. dollar. Such systems would be difficult to build and quite costly, and would not commensurately improve the handling of customers' orders.

IV. FINRA Should Clarify that the Proposed Rule Applies to Customers' Market and Limit Orders.

Currently, the Manning Rules only apply to "market" and "limit" orders in exchange-listed and OTC equity securities. The Proposed Rule, however, more broadly applies to "equity securities." SIFMA requests that FINRA clarify that the Proposed Rule does not apply to (i) securities that do not qualify as exchange-listed or OTC equity securities, or (ii) customer orders that do not qualify as market or limit orders (*e.g.*, "not held" orders). The latter clarification is important for customer orders that do not qualify for the "institutional account" or "large-sized order" exceptions, and it is also consistent with past guidance. In 2006, the NASD acknowledged that the Manning Rules do not apply to customers' not-held orders: "An order for which a customer has granted the firm discretion with respect to time or price would not be considered a 'market' order for the purposes of Rule 2111 and therefore would not be subject to the requirements of Rule 2111. However, this in no way changes a firm's best execution obligations with respect to the order under Rule 2320."[11]

SIFMA also does not believe that it is appropriate to apply the Proposed Rule to not-held orders because a not-held order, by definition, provides a broker-dealer with flexibility through a grant of price and time discretion to exercise its professional judgment in handling the order. Unlike a "held" order, a not-held order does not obligate the broker-dealer to execute the order at then-prevailing market prices. For these reasons, SIFMA asks FINRA to clarify that the Proposed Rule applies to customers' market and limit orders, and does not apply to not-held orders.

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[11] See NASD Notice to Members 06-03.

SIFMA appreciates the opportunity to provide comments on Proposed Rule 5320. SIFMA would be pleased to discuss any comments herein with the Securities and Exchange Commission, FINRA, and NYSE Regulation, or provide any additional assistance relating to rule harmonization in this area. If you have any questions or comments, please feel free to contact me at 202-962-7300.

Sincerely,

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