

The Pulse of Finance



BY E-MAIL AND OVERNIGHT MAIL

December 5, 2011

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090
rule-comments@sec.gov

Re: File Number SR-FINRA-2011-064/Response of Newedge USA, LLC to Proposal Relating to Supplemental FOCUS Filing

Dear Ms. Murphy:

Newedge USA, LLC ("NUSA") appreciates this opportunity to comment on the Financial Industry Regulatory Authority's ("FINRA") proposal to adopt Rule 4524, which would require US-registered broker-dealers ("BD") and FINRA members to provide certain supplemental information in connection with their FOCUS filings relating to income and expenses. Newedge has been quite active over the years, both in the US and elsewhere, in working with regulators to develop rules and regulations designed to strengthen our financial markets. In the US, Newedge has provided input to, among others, FINRA, the Securities and Exchange Commission ("SEC") and the Commodity Futures Trading Commission ("CFTC") in connection with the formulation of various rules and initiatives. Given our broad experience across asset classes as both a world leading executing and clearing broker -- including securities, futures and OTC derivatives -- we feel strongly positioned to provide such input.

With respect to proposed Rule 4524, we acknowledge and support FINRA's desire to obtain more information from BDs relating to income and expenses divided along specific product lines. However, we also believe that: (a) the proposed reporting threshold is too low, in that the additional work required of BDs in providing information relating to relatively de minimus income-producing activities outweighs substantially any value FINRA staff will be able to derive from such information; (b) the rule should provide BDs with an additional 3-5 business days after having filed their FOCUS report to file the requested information, and; (c) the Staff should

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define more precisely certain of the product lines listed on the supplemental filing in order to avoid the possibility of duplicative or inconsistent reporting by member firms.

BACKGROUND

Newedge, which is one of the world's largest brokerage organizations, offers its customers clearing and execution facilities across multiple asset classes including futures, securities (fixed income and equities), options, FX and various OTC instruments.¹ Newedge maintains offices in over 15 countries, and is a member of over 85 exchanges worldwide. As of June 2011, Newedge had an estimated global market share in listed derivatives of 11% (clearing) and 11.9% (execution), and over Euro 50.8 billion of client assets on deposit. Newedge's primary function is that of a broker; *i.e.*, to execute and clear customer transactions across multiple asset classes on an agency or back-to-back principal basis. Newedge conducts very little proprietary trading, and then generally only as a hedge in connection with the facilitation of customer orders.

NUSA, a US-registered BD, futures commission merchant ("FCM") and FINRA member, is a wholly owned subsidiary of Newedge. NUSA currently is the largest US FCM according to customer segregated funds based on CFTC statistics. In connection with its securities activities, NUSA's primary function is that of a broker, executing and clearing transactions for customers across a variety of products including equities, fixed income and equity option products. NUSA offers its customers -- which are primarily institutional -- both voice brokerage and direct market access ("DMA") execution capabilities. NUSA is self-clearing, and provides correspondent clearing and prime brokerage services to other BDs and customers, respectively. NUSA engages in very limited proprietary trading activities, and then generally only to hedge or otherwise facilitate customer transactions. NUSA does not make markets, issue fundamental equity research, conduct underwriting activities, act as a dealer or provide investment banking advisory services. NUSA does engage in stock loan activities, as well as repurchase and reverse repurchase transactions. NUSA is subject fully to Rule 15c3-3 and files its FOCUS reports on a monthly basis.

DISCUSSION

FINRA proposes, through Rule 4524, to require member firms to provide certain additional income and expense related information, broken down by enumerated product lines, in connection with their FOCUS reports. Specifically, FINRA proposes that firms be required to file a new schedule to the Statement of Income (or Loss) page of the FOCUS report ("Supplemental Filing") that will provide the Staff with additional information concerning, among other things, the generation of revenues and allocation of expenses by business segment or product lines, the types and amounts of fees earned, the sources of trading gains and losses and the nature and extent of participation in securities offerings. See FR at 70523. FINRA believes such information will, in general, "allow [it] to better assess risk at a firm, and as a result, better allocate examination resources." See FR at 70524.

¹ "Newedge" refers to Newedge Group, a 50%-50% joint venture between Credit Agricole Corporate and Investment Bank (formerly Calyon) and Société Générale, headquartered in Paris, France, and all of its worldwide branches, subsidiaries and other units.

NUSA does not dispute that the Staff will be in a better position to assess firm risk by receiving more detailed information regarding member firms' income and expenses broken down according to business activities. However, NUSA does believe, as noted above, that proposed Rule 4524 should be modified to: (a) raise the reporting threshold to 5% of a firm's gross revenue (that is, firms will not have to report income and expense related information regarding business activities that during the previous reporting period accounted for less than 5% of the firm's gross revenue); (b) provide firms with an additional 3-5 business days after filing their FOCUS report to file their Supplemental Filing, and; (c) define more precisely certain product lines on the Supplemental Filing to avoid inconsistent or duplicative reporting by member firms. We discuss these recommendations below.

1. The Reporting Threshold Should Be Raised on the Proposed Supplemental Filing

Proposed Rule 4524 would require member firms to provide, along with their FOCUS filings, certain information relating to income earned and expenses paid broken down pursuant to various product line categories. The income-related information includes, among other things, net gains or losses on principal trades, commissions, interest/rebate/dividend income, fee income and "other" revenue. The expense-related information includes, among other things, compensation costs, commission and clearing costs, interest/rebate costs, costs incurred on behalf of affiliates or clients, fees paid under a service agreement to outsourcing providers; finder fees, technology, data and communication costs, research costs and promotional fees. Under the proposed rule, any business activity -- regardless of the amount of income earned or expenses paid during the previous reporting period -- would require some level of disclosure; however, the rule would provide that if a member's total dollar amount for a designated product line is \$5,000 or less for the reporting period, it would only be required to enter the dollar amount to complete the section, rather than a more detailed breakdown.

We believe the reporting threshold is too low, in that the value of the information provided to FINRA relating to very low-income producing business lines will not be worth the significant effort required by firms in assembling and reporting such information. Indeed, many if not most clearing firms (the group upon which this rule focuses) have annual gross revenue well in excess of \$25 million, and many such firms have annual gross revenue well in excess of \$250 million. To require such firms to provide detailed income and expense related information to FINRA regarding business lines that produce slightly more than \$5,000 during a specific reporting period -- or aggregate income and expense information regarding business activities amounting to even less than \$5,000 in revenues during the reporting period -- will, in our view: (a) not provide the Staff with useful information on which to target its examinations or otherwise assess the firm risk, and; (b) cause firms to deploy substantial resources to assemble and report such information, resources that could otherwise be used for critical trade monitoring, recordkeeping or reporting obligations.

In our view, the reporting threshold should be based on a percentage of gross revenue rather than a specific dollar amount. Such a basis would create a sliding scale of materiality that would yield useful information from each reporting firm, exclude non-material information, and thereby provide the Staff with a more manageable overall amount of information through which to assess member firm risks. Specifically, we suggest a reporting threshold of 5% of gross revenue for

such purposes; that is, firms would not be required to report any information on product lines that represent less than 5% of their gross revenue.²

2. Firms Should Have An Additional 3-5 Days to Report The Requested Information.

We suspect that many firms will not be able, at least initially, to transfer all of the required information from their current financial records to their Supplemental Filings on an automated basis; and that even the firms that will be able to do so may be required to reconcile the accuracy and completeness of such transfers on a manual basis. Consequently, we feel it is important that FINRA not underestimate the amount of work involved for firms in meeting this new proposed requirement. In this regard, we also note, somewhat disappointedly, the relative lack of a detailed cost/benefit analysis provided by FINRA (or the SEC) in connection with this rule proposal.

Proposed Rule 4524 would require firms to make their Supplemental Filing within 17 days of quarter end. Given the significant amount of work already involved in preparing a firm's FOCUS report, and considering the additional not insignificant amount of work that will be required in preparing the Supplemental Filing, we recommend that firms be given an additional 3-5 business days to submit the Supplemental Filing after having submitted their FOCUS reports. We do not believe this slight delay will impair the Staff's ability to assess firm risks in a timely manner, and the extra time will, in our view, be important to firms by giving them additional time to ensure the completeness and accuracy of their Supplemental Filings (under our proposal, firms would still be required to provide their FOCUS filings by the 17th day of the month). Indeed, FINRA states that its primary use for information in question is to "better illuminate industry trends" and thereby "allow[] for more focused and effective examinations" of member firms. See FR at 70523. We do not see how delaying the reporting of such information by 3-5 business days will impair the Staff's ability to use such information for these purposes.

3. FINRA Should Define More Precisely the Product Lines Listed on the Supplemental Filing Form.

Certain of the product categories proposed by FINRA on the Supplemental Filing should, in our view, be defined more precisely in order to avoid the potential for duplicative or inconsistent reporting by member firms. For example, FINRA lists each of the following as product lines in the Supplemental Filing: "commodities;" "foreign exchange" and "derivatives other than listed or unlisted options." However, for joint BD/FCMs such as Newedge that conduct substantial

² We note that in proposed Rule 4524 itself FINRA utilizes a gross percentage of revenue test (10%) with respect to firms being required to report detailed information regarding unregistered offering activities (i.e., firms are only required to report detailed information on such activities to the extent it accounts for 10% or more of their total revenue). Finally, we note that firms are required to breakout their business activities -- by percentage of total revenue -- on their pre-examination questionnaires. Since firms already are required to identify on their Form BD and pre-examination questionnaires business activities that account for 1% or more of their gross revenue, we believe setting a slightly higher threshold (5%) of reporting on the Supplemental Filing is adequate, since the Staff, during its examinations (which typically occur annually for clearing and carrying firms) can always ask for more detailed income and expense information on specific product lines so identified. Further, FINRA itself asserts that one of the primary purposes, if not the primary purpose, of the Supplemental Filing is to identify important information regarding income and expenses so that the Staff can better target their examinations of member firms.

and varied activities in the commodities, FX and OTC derivatives markets, we believe these categories are not sufficiently specific enough. For example, an FX swap or forward could be counted both in the "FX," "OTC derivatives" or "derivatives other than listed or unlisted options" categories. Similarly, a customer commodity referential swap could be counted in the "OTC derivatives" or "derivatives other than listed or unlisted options" categories, or potentially even in the "commodities" category. Similarly, the proposed Supplemental Filing form includes categories for "corporate debt," "US Government and Agency" securities and "asset backed securities."

Consequently, a structured GSE debt security could be counted in both the "asset backed securities" or "US Government and Agency" categories, while some CMO or CDO securities (backed by Fannie Mae) could, arguably, be counted in the "corporate," "asset backed" or "US Government or Agency" categories. In order to reduce reporting firms' regulatory and provide the Staff with more useful information, we believe such categories should be clarified.

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We appreciate Newedge being allowed to comment on this proposal. To the extent you have any questions regarding our response, do not hesitate to contact the undersigned at (312) 762-3018, or John Nicholas, Global Head of New Regulation Monitoring and Implementation, at (646) 557-8516.

Sincerely,

Newedge USA, LLC



Nancy Brda
Chief Financial Officer