



## Penson Financial Services

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February 27, 2009

*Via Electronic Mail (rule-comments@sec.gov)*

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

Re: File Number SR-NASDAQ-2008-104, The NASDAQ Stock Market LLC:  
Notice of Filing of Proposed Rule Change to Adopt a Modified Sponsored  
Access Rule

Dear Ms. Murphy:

Penson Financial Services, Inc. ("Penson"), as a member of The NASDAQ Stock Market LLC ("NASDAQ"), appreciates the opportunity to comment on SR-NASDAQ-2008-104, the proposed modification of the requirements for members to provide "sponsored access" to NASDAQ's execution system. Penson, the third largest clearing firm in the United States,<sup>1</sup> and its affiliates currently provide execution services to hundreds of active, retail and institutional broker-dealers, including sponsored access to NASDAQ.

While Penson appreciates the need to establish uniform principles of sponsored access across all relevant exchanges, Penson believes that NASDAQ Rule 4611(d), in its current form, adequately protects investors and the NASDAQ marketplace. Any change to the current sponsored access regulatory regime should be addressed through the establishment of industry wide best practices that advance the efficient and appropriate regulation of sponsored access.

Penson believes that the proposed definition of "sponsored access" is vague and overreaching and agrees with the assertion that the proposed modification of NASDAQ Rule 4611(d) takes a "one size fits all" approach to sponsored access without regard to the type of participant being sponsored<sup>2</sup> or the practical application of the manner of sponsored access. As a provider of NASDAQ sponsored access to broker-dealers, Penson recommends that any sponsored access regulation take into account existing Federal and State securities laws and regulation and the regulatory oversight currently provided by the Securities and Exchange

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<sup>1</sup> Penson ranks as the third largest clearing firm based on number of clients. See *Investment News*, "U.S. Clearing Firms Ranked by Broker-Dealer Clients," December 14, 2008.

<sup>2</sup> See Comment Letter from Jeff Bell, Executive Vice President, Wedbush Morgan Securities, February 23, 2009.

Commission (the “Commission”), the applicable self-regulatory organizations (“SROs”) and the applicable sponsored participant’s designated examining authority (“DEA”).

*NASDAQ Rule 4611(d) Adequately Protects Investors*

Trade activity sent directly to NASDAQ through a dedicated port provided by a member without first passing through the member’s trading risk control and supervisory systems before reaching NASDAQ – “traditional sponsored access” – is subject to adequate controls currently enumerated in NASDAQ Rule 4611(d). In its current form, NASDAQ Rule 4611(d) requires members to assume responsibility for the trades of its sponsored participants as if the trades were their own and also requires the termination of a sponsored participant’s access if the sponsored participant fails to comply with the requirements imposed by the sponsoring member or NASDAQ. It is Penson’s view that these requirements provide a powerful impetus for members to conduct their business and provide access to NASDAQ in a prudent manner as well as require sponsored participants to act in accordance with their commitments.

Penson questions the suitability of the controls proposed in the modification to Rule 4611(d). In their recent comment letter,<sup>3</sup> the Securities Industry and Financial Markets Association (“SIFMA”) provided an in depth discussion analyzing the contractual, financial and regulatory controls proposed by NASDAQ. Penson similarly believes that many of the proposed controls are unnecessary, unrealistic, onerous and inflexible and would, in reality, limit the ability of sponsored members to provide efficient services and offer competitive pricing to their clients and investors. In contrast, the controls provided in the current NASDAQ Rule 4611(d) have allowed members to voluntarily establish controls necessary to meet their own regulatory, financial and risk management requirements facilitating the safety of the marketplace and the protection of investors.

*A Vague and Unvarying Approach to Sponsored Access*

The proposed amendment expands regulation to (i) trading activity passing through a member’s system prior to reaching NASDAQ (“direct market access”) and (ii) access where a service bureau or other third party provides sponsored participants with the technology to access NASDAQ under the auspices of and via an arrangement with a member (“third party sponsored access”). Not only is NASDAQ’s definition of “direct market access” vague, in practice, it could be viewed as applying to the NASDAQ trading activity of every customer of a member. Moreover, direct market access and third party sponsored access were not previously considered sponsored access due to the general premise that the trading activity was already subject to the trading and supervisory infrastructure of the sponsoring member. The contractual, financial and regulatory controls proposed in the modification to NASDAQ Rule 4611(d) also seem to create the obligation for traditional sponsored trading activity to flow through a supervisory system, a concept opposite to the traditional sponsored access model. Consequently, Penson urges NASDAQ to revisit the proposed definition of “sponsored access” and limit the application of Rule 4611(d) to activities that currently constitute traditional sponsored access.

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<sup>3</sup> See Comment Letter from Ann Vlcek, Managing Director and Associate General Counsel, SIFMA, February 26, 2009.

In the event that NASDAQ elects to expand its regulatory scope beyond traditional sponsored access, such regulation should take into account the practical application of each manner of access, the types of sponsored participants and existing and applicable laws and regulations. All three methods of proposed sponsored access operate significantly different. This presents a challenge for the successful implementation of and compliance with NASDAQ's new proposed "one size fits all" controls. It is also unwise to conclude that non-broker dealers, regulated broker-dealers and NASDAQ members<sup>4</sup> are all in need of identical controls and procedures. Although NASDAQ noted that the new sponsored access definitions were "designed to address the changing needs of the marketplace with flexibility while maintaining rigorous oversight," the proposed modification of NASDAQ Rule 4611(d) fails to achieve this objective.

#### *Sponsored Access of Broker-Dealers*

As noted above, Penson currently provides sponsored access to broker-dealers who are subject to the oversight of the Commission, SROs and their own DEA. Penson does not believe it is NASDAQ's intention to (i) subject sponsored broker-dealers to new or duplicative contractual, financial and regulatory controls in addition to those already established by the sponsoring member or to which the sponsored participant may already be subject or (ii) require broker-dealers to ensure another broker-dealer's compliance with laws and regulations.

When a sponsoring member provides sponsored access to a broker-dealer, the Commission and the applicable SROs and DEAs continue to maintain regulatory oversight on the sponsored broker-dealer. Although the trading activity of sponsored broker-dealers is routed through the sponsoring member's market participant identification ("MPID"), the activity of these sponsored participants is identifiable and, as a result, the sponsored broker-dealer, as a direct regulated entity, can be held accountable for such activity. NASDAQ has the ability to directly query a sponsored participant's specific trading (either through the sponsoring member or directly from the sponsored participant), request additional information on the sponsored participant's trading activity and take such immediate action as deemed necessary including breaking trades, shutting off the sponsoring member's MPID or terminating the sponsored access and the relevant exchange agreement. Additionally, since this flow originated from a registered broker-dealer, NASDAQ can refer any action to the Commission or the applicable DEA. Therefore, Penson argues that any proposed modification of NASDAQ Rule 4611(d) should either exclude the sponsored access of broker-dealers or be revised to take into account the current oversight of broker-dealers and whether more efficient means of supervision by the Commission, SROs and appropriate DEAs exist.

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<sup>4</sup> Penson believes that NASDAQ, in its creation of the proposed modification to Rule 4611(d), failed to exclude sponsored access of NASDAQ members. Such regulation would be meaningless and would subject both sponsoring and sponsored members to controls that would not be required if the sponsored member accessed NASDAQ directly.

*Development and Implementation of Exchange Monitoring*

Penson is in agreement with the notion that exchanges may be in the best position to develop and implement system wide sponsored access monitoring tools.<sup>5</sup> As the exchange operator and owner, NASDAQ should be accountable for monitoring and controlling trading activity and should not be allowed to delegate this responsibility to sponsoring members. Sponsoring members have willingly accepted responsibility for the trading activity of their sponsored participants as a requirement for providing sponsored access. However, all marketplace participants, including exchanges, need to bear appropriate and commensurate responsibility for ensuring a safe and effective marketplace.

*Summary*

For all of the reasons noted above, Penson respectfully requests that the Commission oppose the proposed amendments to NASDAQ Rule 4611(d). Penson suggests that the Commission, SROs, DEAs and other market participants establish best practices to provide appropriate guidance of "sponsored access" prior to the establishment of any exchange regulation. Any best practices or future regulation should include only the sponsored access not currently subject to sufficient regulatory, financial or risk controls and should be designed to ensure efficient and effective operation of trading activity. Penson appreciates the opportunity to share its thoughts on the proposed rule.

Sincerely,



Nicole Harner Williams  
Vice President, Associate General Counsel  
Penson Worldwide, Inc.

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<sup>5</sup> See Comment Letter from John N. Jacobs, Director of Operations, Lime Brokerage LLC, February 17, 2009, Comment Letter from Jeff Bell, Executive Vice President, Wedbush Morgan Securities, February 23, 2009 and Comment Letter from Ann Vlcek, Managing Director and Associate General Counsel, SIFMA, February 26, 2009.