

FINANCIAL INFORMATION FORUM

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June 22, 2010

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

Re: File Number S7-10-10, Large Trader Reporting System

Dear Ms. Murphy,

The Financial Information Forum (FIF)¹ would like to take this opportunity to comment on the proposed Large Trader Reporting System discussed in File Number S7-10-10 (“the Proposal”). While our group has specific concerns and questions regarding the Large Trader Reporting System, we are also concerned about the potential for costly and duplicative effort if the Large Trader Reporting System is instituted prior to the finalization of the Consolidated Audit Trail proposal.²

The events of May 6 dramatically illustrate the need for a comprehensive and consistent regulatory reporting framework. As an industry, we have an opportunity to establish an operationally efficient and effective regulatory reporting framework that addresses the deficiencies of existing audit trail systems including OATS, OTS and Electronic Blue Sheets (EBS). In the Consolidated Audit Trail rule proposal, the Commission states:

“...because the EBS system is designed for use in narrowly-focused enforcement investigations that generally involve trading in particular securities, it is less useful for large-scale market reconstructions and analyses involving numerous stocks during peak trading volume periods.”

In recognition of the limitations of the EBS system, we respectfully request that the Commission address large trader identification in the context of the Consolidated Audit Trail. If the Commission chooses to move forward with the Large Trader Reporting System in order to

¹ FIF (www.fif.com) was formed in 1996 to provide a centralized source of information on the implementation issues that impact the financial technology industry across the order lifecycle. Our participants include trading and back office service bureaus, broker-dealers, market data vendors and exchanges. Through topic-oriented working groups, FIF participants focus on critical issues and productive solutions to technology developments, regulatory initiatives, and other industry changes.

² The Consolidated Audit Trail proposed rule (File No. S7-11-10) would “require national securities exchanges and national securities associations (“self-regulatory organizations” or “SROs”) to act jointly in developing a national market system (“NMS”) plan to develop, implement, and maintain a consolidated order tracking system, or consolidated audit trail, with respect to the trading of NMS securities.” FIF will comment on Consolidated Audit Trail in a subsequent comment letter.

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identify large traders within a six month timeframe, it will be important to clearly define the requirements of the system and address the following topics.

Requests for Electronic Blue Sheets (EBS)

The Proposal identifies new data that brokers will be required to provide in EBS, but it does not indicate that there will be any changes to the criteria that will be used by the SEC (“the Commission”) or other regulators to request EBS. Currently, EBS are requested for a symbol and a range of dates. In the EBS, brokers provide a variety of data for all trades executed for that symbol and related securities (e.g. options on the requested security) within the range of dates requested. Under the Proposal, we expect that brokers will include new data fields with execution time and Large Trader ID on the EBS record. However, if the Commission is also planning to change the request criteria for EBS then that should be specifically noted in the rule filing. While the proposed six month time frame is adequate to complete changes necessary to provide additional data on EBS, adding Large Trader ID and execution time to request criteria would require additional time to implement. We recommend expanding the EBS record to include the new fields while maintaining the current request mechanism.

Additionally, we recommend that EBS records require LTID only on those transactions occurring after the large trader notifies a broker dealer of its LTID. Retroactively applying the LTID to transactions occurring prior to the designation of an account as a large trader is a significant implementation challenge that for some firms will be virtually impossible to comply with.

Response Time for Blue Sheet Requests

In discussing the availability requirements for EBS records, the proposal indicates shortening the current 10 day EBS response time. Specifically, the Proposal states:

... records and information required to be made and kept pursuant to the proposed rule be available⁹⁵ for reporting to the Commission on the morning after the day the transactions were effected. While such information must be available for reporting to the Commission on the following day, the proposed rule further clarifies that transaction data would be required to be submitted to the Commission before the close of business on the day specified in the request for such transaction information.”

Clarification is requested as to whether “the day specified in the request” would be on the same day as the request was made.

In order to accommodate EBS extracts with a single process, FIF members respectfully suggest the SEC allow a full business day to respond to EBS requests. By basing response time on the time of the request rather than a time of day, firms could institute a single, consistent process building off of current EBS processing cycles. This would allow clearing firms that receive end of

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day files with executions sufficient time to uncompress these files in order to determine execution time for EBS reporting.

Additionally, it is important to note that most brokers extract EBS data from their core books and records and they execute the extract process in nightly batch. Therefore, to create an EBS, the broker must complete at least one batch cycle. If the EBS request is received too late to be input for nightly batch, it would have to be produced in nightly batch on the following night. Therefore, FIF members recommend that any requests made after business hours should be considered requested on the following business day in order to allow sufficient time for processing.

The Proposal also states that “the records and information required to be made and kept pursuant to the provisions of this rule shall be available on the morning after the day the transactions were effected (including Saturdays and holidays).” We request clarification as to whether by calling for availability on Saturdays and weekends, the SEC means that EBS records may need to be submitted on Saturday and holidays. It is unclear whether SIAC, as the current EBS processor can handle the delivery of EBS records during holidays. It is suggested that the proposal make clear that a full business day, during which the national securities exchanges are open, are allowed to respond to these requests.

Delivery of Blue Sheets

EBS records are currently submitted to SIAC which then disseminates the data to the Commission or SRO making the ad hoc request. We request clarification as to whether there will be a requirement for EBS submissions to be submitted directly to the Commission. If the Commission plans on implementing a new delivery process, (e.g., submission through a web based utility as FINRA has done), more than six months will be necessary to address connectivity and information security issues.

If the SEC will require direct submission of EBS requests to the Commission, establishing an automated submission process should be explored. For example, EBS records could be automatically submitted to the SEC on specific days of the month – such as the 15th and the 30th or every Friday. This would eliminate the burden of having to respond by the morning after the trade.

Inclusion of Exempt Transactions

EBS records essentially extract data from execution capture information which may not include sufficient data to exclude exempt transactions. We respectfully request that the SEC allow such transactions to be reported when submitting the EBS records.

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Reporting Responsibility

In order to assist implementation efforts, it would be helpful for the Commission to present different scenarios that clarify which entity is responsible for Large Trader compliance obligations (i.e., submitting/updating Form 13H, responding to EBS requests, recordkeeping, monitoring Unidentified Large Traders, etc.). Scenarios to consider addressing:

- Scenarios involving multiple broker-dealers in the execution of a transaction (e.g., an introducing broker sending an order to an executing broker who uses another broker dealer for clearing purposes.
- Scenarios where the Large Trader is a broker-dealer
- Scenarios where brokers execute orders on an omnibus (not fully disclosed) basis. Are these brokers also required to report trades executed for a Large Trader? If so, then the LTID would need to be recorded on the order as well as the trade, which would add a tremendous amount of complexity to this initiative.
- Scenarios where a Client instructs the executing broker to settle and clear the trades with multiple prime brokers. Does the executing broker have to pass the LTID of the Client to all prime brokers?

Form 13H Implementation Issues

The following items require further clarification/consideration in order to determine implementation time and cost.

- If firms with multiple affiliates decide not to file at the parent holding company level, it will pose significant monitoring issues in tracking the relevant affiliates/accounts. Firms will be required to develop a central repository for the information required to complete the Form 13H (i.e., obtain names of affiliates, general/limited partners, trading accounts, officers/executives), Repository will need to be maintained and updated in line with Form 13H filings.
- What kind of timing is “promptly” in relation to the need to file an initial Form 13H or Interim filing? May be difficult to accomplish if 1 or 2 days and perhaps initial information should only be provided at month end or quarterly if required.
- What is the deadline for filing any amendments/Interim Form 13H? Promptly, X number of days or within a certain amount of time after the end of the calendar quarter? This “prompt” requirement will result in timing issues (tracking and monitoring) in terms of obtaining all relevant updated information. Should there be a timing difference with respect to informing BDs of any new accounts and revising the Form 13H with updated information?

Scope of Broker Dealer Recordkeeping and Monitoring

It is unclear how existing data and processes would be sufficient to readily monitor Unidentified Large Traders. Given the proposed timeline, it will be challenging to identify these circumstances beyond the activity in a single account or a group of fully disclosed accounts.

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Trading thresholds or guidelines should be established to assist broker-dealers in identifying unidentified large traders. It would be difficult for individual broker-dealers or clearing firms to easily identify those entities looking to evade the rule. Broker-dealers would only see a portion of the alleged transactions, and clearing firms do not know the customers and would have difficulty identifying the same beneficial account owner holding accounts with multiple broker-dealers. Firms could create watch lists for accounts that approach the large trader thresholds but do not reach them and clearing firms could assist in creating these monitoring reports.

The definition of a large trader should be limited to the entity that has direct control over trading decisions. If the purpose of identifying large traders is to look for those individuals wishing to exploit the markets, grouping individuals who are truly independent of each other would only cloud the view. Affiliated firms that are owned by the same parent also should be treated separately if they are truly independent of each other and the parent company does not dictate trading policy. Grouping these firms together will only create unnecessary monitoring requirements.

Additional questions that we request clarification on are as follows:

- Would firms be required to restrict/deny trading by Unidentified Large Traders who are not in compliance?
- If a Prime Broker client is nearing the large trader reporting threshold and the BD is aware that the client has a Prime Brokerage relationship with another BD as well, is the BD required to proactively contact the client to obtain additional data, or is the BD only subject to actual knowledge of a client's position sent to their firm?
- Would it be sufficient to periodically obtain attestations from the firms with omnibus accounts that they have a monitoring process in place and will identify any large trader account when identified?
- If the foreign entity issue where a US broker-dealer may not be able to ascertain the identity of a large trader if it received the order from a foreign affiliate due to secrecy laws in the foreign jurisdiction. How does the SEC envision compliance by the US broker in such a scenario?
- To what extent are trades done on foreign exchanges in NMS securities considered eligible for determination of Large Trader status.
- Will firms be required to maintain records on the active and inactive status of Large Traders in order to aggregate "active" and "inactive" activity?

Costs Associated with Broker Dealer Recordkeeping and Monitoring

The Commission estimates the ongoing costs to broker-dealers of monitoring for compliance with the rule to be about 1.2 million dollars a year. This figure assumes that the rule will apply to 300 broker-dealers and that a Compliance Attorney will need to devote 15 hours per year of

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their time (about 17 minutes a week) to ensure compliance with this rule. Initial costs were estimated to be about 4 million dollars a year assuming, among other things, it would affect 300 broker-dealers.

FIF believes that the Commission significantly underestimates the costs of the proposal as it relates to broker-dealers. The Commission estimates that 300 broker-dealers that are "carrying firms" would be subject to the rule, which includes reporting requirements for broker-dealers that carry an account for an Unidentified Large Trader. Thus the rule would not apply to introducing broker-dealers, who may accept orders on behalf of an Unidentified Large Trader. However, in order to rely on the "monitoring safe harbor", these carrying broker-dealers are required to establish "policies and procedures reasonably designed to assure compliance with the identification requirements." The proposal further states that

Policies and procedures shall be deemed to satisfy this requirement if they include:

(1) systems reasonably designed to detect and identify Unidentified Large Traders based upon transactions effected through an account or a group of accounts considering account name, tax identification number, or other information readily available to such broker-dealer...

..."The Commission would consider "other readily available information" to include, for example, those instances where a single customer effects the requisite transactions through a single registered representative, trading desk, or branch office in his or her personal accounts, accounts of family members, or accounts of others, pursuant to written trading authorizations. In that case, a broker-dealer should be able to identify a large trader based on readily available information. Similarly, customer authorization to transfer funds or securities among accounts in order to receive approval for trading activities, meet margin requirements, or to settle transactions, would be considered to be readily available information, as broker-dealers could use that information to readily identify accounts that may be related."

This other readily available information might only be available at the introducing broker-dealer and therefore clearing firms might reasonably require the broker-dealers that introduce customer accounts to them to implement their own policies and procedures reasonably designed to detect and identify Unidentified Large Traders. FIF notes that it is not unusual for clearing broker-dealers to require their correspondents that clear through them to establish regulatory related policies and procedures beyond that which is required by SROs and federal rules and regulations. Accordingly, FIF believes that these rules would indirectly apply to much more than the 300 broker-dealers identified by the SEC. More realistically, over 1,500 broker-dealers would have some level of initial and ongoing costs to comply with the Large Trader Reporting obligation.³

³ As of June 10, 2010, there are about 1657 FINRA Members that have been assigned MPIDs and can report NMS trades

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In addition, FIF believes that broker-dealers will need to allocate much more than 4,500 hours to monitor compliance with the Large Trader definition. Ongoing operational responsibilities will include:

- Responding to the Commission's and SROs requests for information about Large Traders
- Carrying out, testing, and maintaining systems designed to determine Unidentified Large Traders including determining on an on-going basis which accounts are subject to Large Trader Reporting

FIF believes that these requirements are similar in nature to those of FINRA's Anti-Money Laundering policies and procedures requirements and would also include requirements related to continuing education for a full-time compliance professional. Accordingly, FIF believes a better estimate of on-going cost associated with the proposal to range from \$30,000,000⁴ to \$750,000,000.⁵

Summary

In order to meet the goal of identifying large trader activity, we believe that within a six month time period, firms could:

- Populate the Large Trader ID and execution time fields on EBS reports
- Shorten the response time from 10 days to a full business day
- Monitor activity within a single account or group of fully disclosed accounts.

As discussed above, additional time beyond the proposed six months will be required if firms need to modify systems to:

- Respond to Blue Sheet requests using LTID or any other criteria other than a symbol and a range of dates as a query mechanism
- Support delivery requiring connectivity to a new reporting entity
- Monitor & Determine Unidentified Large Trader Activity beyond account-level aggregation
- Support modifications to the order transmission process if downstream broker-dealers will be required to capture the LTID

Beyond development costs there will be additional costs incurred to operate and maintain a large trader reporting system. Monitoring for Unidentified Large Traders beyond the account level is a significant on-going cost.

The Consolidated Audit Trail filing states that there is a "heightened need for a single uniform electronic cross-market order and execution tracking system that includes more information than is

⁴ 300 broker-dealers with one Compliance Attorney dedicating 370 hours annually

⁵ 1,500 broker-dealers with one Compliance Attorney dedicating 2,000 hours annually

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captured by the existing SRO audit trails, and in a uniform format. “ We respectfully request that the Commission integrate large trader reporting into the Consolidated Audit Trail system.

Sincerely,



Manisha Kimmel
Executive Director
Financial Information Forum