June 15, 2000

Jonathan G. Katz, Secretary,
Securities and Exchange Commission,
450 Fifth Street, N.W., Stop 6-9
Washington, D.C. 20549.

Re: Proposed Rule 17a-25– File No. S7-12-00

Dear Mr. Katz:

The ad hoc Committee on Electronic Bluesheeting of the Securities Industry Association ("the Committee")[1] is pleased to submit this response to proposed Rule 17a-25, contained in Release No.34-42741 ("Release").

Overview.

The Release proposes a significant expansion in the role of the "electronic blue sheet" questionnaire forms ("EBS"). Proposed Rule 17a-25 would mark the first time that the Securities Exchange Commission ("Commission") has codified in its rules the requirement that broker-dealers electronically submit to the Commission staff, on request, information on customer and proprietary trading. The Commission characterizes the proposed rule as generally requiring only the specific information already required by the existing EBS system, with the exception that the proposed rule would also include three

[1] SIA brings together the shared interests of more than 740 securities firms to accomplish common goals. SIA member-firms (including investment banks, broker-dealers and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. The U.S. securities industry manages the accounts of more than 50 million investors directly and tens of millions of investors indirectly through corporate, thrift and pension plans. The industry generates more than $300 billion of revenues yearly in the U.S. economy and employs more than 600,000 individuals. (More information about SIA is available on its home page: http://www.sia.com.)

new data elements, consisting of prime brokerage identifiers, average price account identifiers, and identifiers used by depository institutions.

The general thrust of the proposed rule is a much more flexible approach to accessing trading data than the large trader reporting rules that were the antecedent to this proposal ("large trader reporting proposals"). Those rules were intended to implement authority granted to the Commission under provisions of the Market Reform Act of 1990. In its large trader reporting proposals, issued in 1991 and reproposed with certain clarifications in 1994, the Commission proposed rules that would have defined categories of "large traders." Broker-dealers would have been required to disclose to the Commission the identity and accounts of investors that the broker-dealer knew or had reason to know is a large trader, and broker-dealers would also have been required to keep extensive records of large trader transactions. SIA and other commenters raised strong concerns that the proposed rule would be unduly burdensome and costly.

The current proposal, to codify the existing SRO EBS requirements within the SEC's rules, and to expand those requirements in several respects, is preferable to the large trader reporting proposals. However, in some respects the proposal may be more expensive and burdensome to implement than the Release acknowledges. We urge the Commission to only implement the proposals in the Release that represent the most compelling ratio of regulatory cost to regulatory need. Specifically, subject to some clarifications that we describe below, we do not oppose

- the new prime brokerage identifier element;
- the new average price account identifier;
- depository institution identifiers; and
- the proposal to update the Commission on the names and contact information needed to route information request to the appropriate person at a broker-dealer.

However, we have significant concerns with other aspects of the proposal. Specifically,

- we are troubled by the proposed requirement that broker-dealers must include their customers' employers names in EBS format. Many firms do not currently keep this information in electronic format, much less on systems that can readily linked to EBS;
- The portion of the rule dealing with customer information also contains several ambiguities that should be clarified. We are not clear as to whose tax identification number it means to cover – the employee's or the employer's;

- we oppose the suggestion that execution times or order sequence numbers should be captured in EBS because we believe that it would be inordinately expensive, and possibly entirely unfeasible in some situations, to capture this information in a central electronic data base; and

- the proposal should be modified in some respects to better correspond with current accepted practice in complying with the EBS requirements of self-regulatory organizations.

Systems Changes Necessitated by the Proposed Rule.

While we believe that the rules proposed in the Release are for the most part preferable to the large trader reporting proposals, we believe that the Commission may not fully appreciate some of the costs that its proposal could entail. While several aspects of the proposal were informally discussed with SIA representatives several years ago, other aspects are new to us, and represent a departure from current regulatory practice in administering EBS requests. These concerns should be addressed in implementing the rule.

The Rule would require firms to keep in centralized automated format categories of information that in many instances may have been kept in other decentralized formats, and will require firms to link information systems that previously had not been linked. While EBS evolved as a mainframe-based system, much of the new information that the proposed rule would capture is not currently integrated into mainframe systems. Connecting data from other systems to integrate it with EBS will require fairly significant systems work by all of the firms required to participate in EBS under the proposed rule.

For example, we understand that customers' employers names are not now electronically maintained in many instances, and would have to be manually entered. Moreover, employer taxpayer identification numbers are not commonly maintained in any format by most broker-dealers, because there is no regulatory requirement to do so. Records of order execution times and order sequence numbers may also be maintained in ways that are not readily accessible, or may not be maintained at all, for reasons discussed further below. The three proposed new data element fields for prime brokerage identifiers, average price identifiers and depository institution identifiers are more likely to be found somewhere on firmwide systems, but are unlikely to be within a single mainframe system, and therefore will require new linkages between systems in order to be accessible to EBS.

It should not be overlooked that these systems changes would have to be made while the securities industry is in the midst of an ongoing onslaught of other systems challenges. SIA deeply appreciates that the Commission abstained from issuing this proposal until Year 2000 conversion efforts concluded. Nevertheless, there are other important ongoing systems challenges, of great importance to the industry as well as the

Commission and the investing public. These include conversion of the trading cycle from a three-day to a one-day cycle, conversion of market centers from fractional-based trading to trading based on decimals, addressing significant Internet security issues, as well as other matters.

For all of the foregoing reasons, we do not agree with the Commission's statement that "no major changes would be necessary for broker-dealer systems." We believe that some firms will need to make fairly substantial changes, particularly in the context of other demands being made on their information technology and systems development staffs. We hope that the Commission will be mindful of these competing demands on broker-dealers' information technology and operations personnel as it considers whether and how to proceed with adoption and implementation of this proposal.

Specific Comments.

1. The Three New Data Elements.

We believe that the industry can accommodate the new data elements requiring prime brokerage identifiers, average price account identifiers and depository institution identifiers. As noted above, these will require systems changes, which could be expensive for some firms.[2] However, these are generally elements that major firms already capture somewhere, and the approach should be feasible, assuming a reasonable implementation schedule.

However, there are some ambiguities in the prime brokerage and average price account data elements that we would like the Commission to clarify.

Prime Brokerage Identifiers. We query the proposal on prime brokerage identifiers in one respect. As drafted, proposed Rule 17a-25(b)(1)(i) could be read as applying not only to prime broker arrangements, but also step-outs and give-ups and similar activities in other clearing relationships. The text of the proposing release only speaks of prime brokerage arrangements, so we assume that it is not the Commission's intent to apply this data field more broadly. We request that the Commission redraft this subsection of the proposed rule to clarify this. If our assumption is incorrect, it should be emphasized that the cost of making the necessary systems changes will be considerably higher than the Commission's cost-benefit analysis supposes. Many clearing firms either do not maintain coded identifiers for step-outs and similar aspects of ordinary

2 We are uncertain the Commission is correct in its estimate that the new data fields would only apply to about 100 firms. Certainly, far more firms than that participate in prime brokerage arrangements and average price accounts. Presumably the Commission thinks that many of these firms would not have to participate in EBS. We would like a better understanding of how the Commission arrives at that understanding.

correspondent clearing relationships, or if they do, they do not necessarily identify them the same way that they identify prime brokerage arrangements. Therefore, if the Commission intends to capture clearing arrangements beyond prime brokerage arrangements, the systems changes that would be required would be quite substantial. We strongly encourage the Commission to clarify that it does not intend to reach beyond prime brokerage arrangements, or to explain why it needs this information and work with the industry to develop a rough estimate of what the additional costs would be before proceeding.[3]

Average Price Account Identifiers. Proposed Rule 17a-25(b)(2) is somewhat unclear about what information broker-dealers would be required to include in their data submissions regarding average price account identifiers. The text of the proposing release suggests that the Commission simply wants sufficient information to enable it to avoid double-counting a transaction. This could be done by using a single identifier to denote that an account – whether the master account or a subaccount – is part of an average price account arrangement. However, the rule itself is not clear on whether a broker-dealer can simply generate one identifier showing that a trade is allocated, or must generate separate identifiers for the master account and for each sub-account. Many broker-dealers currently have no need to generate such separate identifiers. We urge the Commission to only require a single identifier.[4]

2. Customer Information.

We are very concerned about the suggestion that the names of customers' employers should be kept in EBS-accessible format. Many firms currently maintain this information only on "hard copies" of new account forms. Often these firms have begun to capture this information electronically for new accounts as they are opened, but have not tried to capture this information electronically for existing accounts. To do so would be extremely burdensome – requiring some firms to manually enter this information for

3 We have been advised that data concerning prime brokerage arrangements is usually easier for executing brokers to automatically pull up on their systems than for prime brokers. Therefore, if the Commission's intention is to require the prime broker to give up this information on behalf of all firms that participate in the prime brokerage arrangement, this will require significantly more systems work than if the executing brokers are asked to include this as a data field in their EBS reports.

4 We understand that broker-dealers often maintain price and trade information in omnibus average price account memory trays until that information is transferred to the subaccounts, typically about once per business day. There is no need for the memory tray for the master account to retain that information once it has been transferred to the subaccounts. We assume that the Commission is not suggesting that firms should redesign their systems to retain this information in master account memory trays as long as there is no double-counting of average price account information in a firm's EBS report. We would appreciate it if the Commission could confirm our understanding in any adopting release.

hundreds of thousands of accounts. We question whether the administrative convenience that this requirement would give to the SEC in its investigations could outweigh the burden that this would pose for many broker-dealers.

The rule is unclear as to whether it would require the customer's or the customer's employer's tax identification to be included in EBS-accessible format. If it is the latter, this is information that many firms currently do not need and therefore do not have. The rule offers no explanation as to why this information is now considered necessary. While the cost of compliance is difficult to estimate, it would obviously be enormous, since it would require all broker-dealers that do not currently have the tax identification numbers of customers' employers to get that information and make systems changes to hold that information in an EBE-accessible format.

3. Execution Times and Order Sequence Numbers.

Expanding EBS to include execution times and order sequence numbers would be problematic, and we recommend that the Commission not include this as part of the proposed rule. A variety of firms would have significant logistical problems with this aspect of the proposal. For example, many clearing firms that handle proprietary accounts of introducing brokers do not typically keep this information about the introducing firm. The trade comparison systems of many broker-dealers do not have any need to systematically reconcile some trade details such as execution time or order sequence. Therefore, there is often no automated link between the order file, where this information would reside, and the trade file, which is the file that interfaces with EBS. While this information can usually be manually extracted, automated extraction would require building a new automated link, rather than just reconfiguring an existing link.

Connecting into EBS information maintained under OATS would raise additional difficulties. Many firms that rely on BRASS to handle their OATS compliance (primarily small to mid-sized broker-dealers, although some large firms also rely on BRASS for some aspects of their business) would also face serious difficulties ensuring compliance. At this time a great many firms rely on BRASS for this service. The information stream provided by BRASS for execution times, while robust with respect to order and trade time, is not tied to specific account numbers. Rather, firms typically keep account numbers separately. Tying this information would be a very complex task, although a rough cost estimate would be hard to ascertain without extensive discussion with BRASS. We have heard emphatically from some of our members that this would be a significant problem.

In many instances, trades done through allocation accounts would also face significant hurdles in complying with a requirement to report execution time or order sequence numbers to EBS. Allocation accounts are widely used by broker-dealers for their institutional business. These accounts are typically used to enable a broker-dealer to

execute a single block trade for several institutions, and then allocate the trade among them, or to give multiple executions for a single institution that are confirmed on an average price basis. However, they may also be used in situations where the trade desk happens to execute a single order from an institution in a single trade. Unfortunately, at many firms allocation accounts are currently designed to record the time the trade left the allocation account and went into the customer account, rather than the time the trade was executed in the allocation account. Expanding the time recordation element of allocation accounts would therefore be a more significant step than simply connecting an already-captured element to a different system.

4. SRO Requirements on Capacity Information.

Proposed Rule 17a-25(a)(2)(iii) would require, *inter alia*, automated disclosure of whether, in the case of transactions effected for a correspondent firm, the broker-dealer was "acting as principal or agent on the transaction or transactions." Existing SRO requirements, such as NASD Rule 8211(c)(3), have a similar requirement. However, the NASD has exempted from this requirement transactions in which the firm acts in multiple capacities in filling the order, and discloses on the confirmation words to the effect of "multiple capacities – details on request." The Commission should either modify the rule to reflect such interpretive guidance as the NASD and other SROs have given under existing EBS requirements, or at a minimum should be prepared to give no-action letters or other interpretive guidance consistent with existing SRO guidance.

5. Information to Facilitate Data Requests.

SIA has no objections to this proposal, which would merely obligate firms to keep the SEC staff current on the correct contact person within the firm for EBS requests.

6. Exemptions.

As recognized in the proposing release, we strongly agree that the Commission should use its exemptive authority to generally exempt small broker-dealers from automated reporting under proposed Rule 17a-25.

Conclusion.

We appreciate the opportunity to comment on proposed Rule 17a-25. We hope that the comments offered above will help the Commission to shape the rule so that it more effectively helps the Commission in market reconstructions, and in investigating and prosecuting the scourge of insider trading, without unnecessarily burdening broker-dealer systems or weakening the competitiveness of U.S. broker-dealers. If we can be of

further assistance, please do not hesitate to contact the undersigned, or George R. Kramer of the SIA staff at 202/296-9410.

Sincerely,

Bernard L. Madoff
Chair, SIA Ad hoc Committee
on Electronic Bluesheeting

Cc: The Honorable Arthur Levitt, Chairman
The Honorable Norman S. Johnson, Commissioner
The Honorable Isaac C. Hunt, Jr., Commissioner
The Honorable Paul R. Carey, Commissioner
The Honorable Laura S. Unger, Commissioner
Annette Nazareth, Director, Division of Market Regulation
Alton Harvey, Office Chief, Division of Market Regulation
Anitra Cassas, Attorney, Division of Market Regulation