



April 29, 2011

**VIA ELECTRONIC MAIL (rule-comments@sec.gov)**

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

**Re: Release No. 34-64080; File No. SR-FINRA-2011-13; Proposed Operations Professional Registration**

Dear Ms. Murphy:

The Securities Industry and Financial Markets Association (“SIFMA”)<sup>1</sup> appreciates the opportunity to comment on the referenced proposal, in which FINRA seeks the Securities and Exchange Commission’s (“SEC”) approval to adopt FINRA Rule 1230(b)(6) to establish a registration category and qualification examination requirement for certain operations and other support personnel and to adopt continuing education requirements for such personnel.<sup>2</sup> The Proposal also would adopt NASD Rule 1120 (Continuing Education Requirements) as FINRA Rule 1250 in the consolidated FINRA rulebook with minor changes.

As an initial matter, SIFMA would like to emphasize that it has been, and remains, generally supportive of the Proposal and respectfully disagrees with FINRA’s characterization in its rule filing that SIFMA “generally opposed” the proposed rule change. We agree that senior supervisors performing operational and related support functions play an integral role in the business of member firms and support extending registration requirements to appropriate operations and support employees who have “decision-making and/or oversight authority.”

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<sup>1</sup> 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](http://www.sifma.org).

<sup>2</sup> Securities Exchange Act Release No. 64080 (March 14, 2011), 76 *Federal Register* 15012 (March 18, 2011) (hereinafter, the “Proposal”).

Moreover, SIFMA appreciates a number of specific changes that FINRA made from the proposal announced in *Regulatory Notice* 10-25 (“RN 10-25”). In particular, the following changes are all sensible modifications and help clarify the scope and timing for implementation of the proposed rule: (i) including a materiality threshold in proposed FINRA Rule 1230(b)(6)(A)(iii) regarding commitments of capital and agreements, both in direct furtherance of the covered functions; (ii) codifying in proposed Supplementary Material .06 the exception from the registration requirement for those engaging solely in clerical or ministerial activities in a covered function and those whose function is supportive of, or advisory to, the performance of a covered function; and (iii) extending the proposed transition date from six to nine months, as originally proposed in RN 10-25, to 12 months.

#### I. Implementation, Grace Periods, and Qualification Examination

SIFMA remains concerned, however, that the Proposal would require the registration of a large number of industry professionals within a new FINRA registration category within a relatively brief time period and on a scale that is unprecedented. SIFMA appreciates that in response to its request for a transition period of 12 to 18 months, FINRA has extended the initial implementation period to 12 months. SIFMA believes that the currently proposed implementation schedule would still place an undue burden on the industry, however, and may cause serious disruption as firms reallocate employee time and resources away from other critical areas during a period in which the industry already is undergoing rapid and extensive changes. In addition, the consequences of inadvertently failing to identify a “Day-One” Operations Professional within 60 days after the effective date are severe. SIFMA therefore proposes that the two-month period to identify Day One Operations Professionals be extended to three months followed by a 12-month period for those employees to study for, take and pass the exam.<sup>3</sup> Based on the existing record in this rulemaking proceeding, the burden and risks that would be posed by FINRA’s accelerated timeframe would far outweigh the minor benefit of the rule becoming fully effective a few months earlier than an orderly process and timeframe would permit.

With regard to grace periods going forward, SIFMA believes that non-Day-One Operations Professionals associated with self-clearing or clearing firms also should be provided the benefit of a 120-day grace period to pass the Operations Professional

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<sup>3</sup> We note that requiring individuals already registered with FINRA to separately register as Operations Professionals will be administratively complex and will require many firms to make internal systems changes to track and monitor “dual” (or multiple) registrations. Although SIFMA is not arguing that individuals already registered with FINRA should be excluded from the requirement to register separately as Operations Professionals, we believe FINRA should take steps to facilitate the registration process, as it has with large scale registration initiatives in the past. For example, FINRA should provide firms with the ability to upload a “batch” file of Form U4 registration requests to the CRD system at the conclusion of the initial identification period for “Day One” individuals required to be registered as Operations Professionals.

qualification examination (or an eligible qualification exam), during which time such persons may function as Operations Professionals; provided, however, that such personnel report to a person who holds the Operations Professional registration or other comparable principal registration such as a Series 24 or 27.<sup>4</sup>

We believe that the risk of allowing covered persons in clearing firms the same 120-day grace period as proposed to be allowed covered persons in non-clearing firms is extremely low for a number of reasons. First, once the rule is in place, there will be multiple registered persons throughout the operations and related functions of the clearing member. Second, the member has every incentive to promote or hire persons who are qualified to fill any open vacancy, and, as we have proposed, such a newly hired or promoted person would be supervised by a registered person. Third, such a person will not be directly interacting with clients of the member (unlike, for example, a sales representative).

On the other hand, preventing an Operations Professional from working until he or she passes the qualification exam could impede the ability of a clearing firm to hire and train new staff on a timely basis or quickly replace staff in the event of sudden departures. This would place clearing firms at a particular disadvantage, and, therefore, would be disruptive to member firm operations and present significant business continuity risk. Indeed, FINRA's 120-day grace period under NASD Rule 1021(d) for other supervisory licenses, such as the Series 24, recognizes that firms need flexibility to address these contingencies.

For all of these reasons, we strongly recommend that FINRA allow a 120-day grace period for covered persons at clearing firms and non-clearing firms alike to pass the required examination.

With regard to the qualification exam, we understand that FINRA and the SEC staff originally intended it to be a "spot-the-red-flags" exam that would train test takers to identify and escalate potential control problems. SIFMA strongly agrees with this original intent and believes that FINRA should not expand the test into a competency exam covering the details of different products, operations processes and rules and regulations. Because Operations Professionals work in such a broad range of functions, a competency exam covering particular areas of this broad spectrum would test on functions that would not be relevant to most personnel captured under the Operations Professional designation and would be difficult for many to pass. A high failure rate, of course, would cause

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<sup>4</sup> Respectfully, we do not believe FINRA has explained sufficiently why it has proposed to provide non-clearing firms the benefit of this grace period, but not clearing firms. FINRA only states in the Proposal that providing the 120-day grace period to non-clearing members will enable these firms to "manage their more limited staffs to comply with the proposed registration requirements without disrupting those firms' obligations to customers."

operational disruption by rendering unavailable those Operations Professionals who are unable to pass the exam before expiration of the deadline.

Finally, SIFMA appreciates FINRA's recognition that the existing licenses listed in proposed Rule 1230(b)(6)(D) are sufficient to qualify an Operations Professional to register without passing the new qualification exam. SIFMA also believes that FINRA should recognize the UK FSA-approved Securities & Investment Level 3 Investment Operations Certificate (IOC) and the Investment Administration Qualification (IAQ), both of which are widely recognized within the financial services industry in the United Kingdom.

## II. Covered Persons

We note that FINRA's rule filing describes covered persons generally as those "who are *directly responsible* for overseeing that tasks within the covered functions are performed correctly in accordance with industry rules, firm protocols, policies and procedures and who are *charged with protecting the functional and control integrity of the covered functions for a member*." SIFMA finds the italicized language above particularly helpful in identifying the depth of personnel that FINRA intends to include in the new registration category and respectfully requests that FINRA include this language in the text of the Rule.<sup>5</sup>

In addition, SIFMA remains concerned about the potential impact and unintended consequences of the proposed rule on arrangements between members and third-party service providers, and believes FINRA should limit its registration requirement to "associated persons" of the member, a term well understood in the industry and that is consistent with applicable law<sup>6</sup> and the approach used in FINRA's other registration rules.<sup>7</sup> Limiting application of the new registration requirements to "associated persons" would make interpreting the new requirement far more straightforward for member firms, and would resolve the complicated jurisdictional and practical issues otherwise arising from the lack of clarity in the scope of the Proposal. On the other hand, potentially requiring

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<sup>5</sup> We also note that FINRA's Richard Ketchum, in responding recently to a question as to whether the new registration requirement would be too onerous, stated that FINRA has made "great effort from a definitional standpoint to target only people who have *substantial decision-making responsibility*." (Emphasis added). Although SIFMA very much appreciates the opportunity to have worked with FINRA in the early stages of the process before RN 10-25 was issued, respectfully we believe the text of the Rule should be revised as we propose to better reflect FINRA's intent. See "Q-and-A with FINRA Chairman and CEO Richard Ketchum," April 12, 2011, *SmartBlog on Finance*.

<sup>6</sup> See section 3(a)(21) of the Securities Exchange Act of 1934.

<sup>7</sup> See NASD Rules 1021, 1031, 1032, 1041, and 1050, each of which requires registration for a person "associated with a member" who meets the definition of representative or principal and/or performs specific functions.

firms to license third-party employees performing activities that have not to date required registration or qualification raises myriad complex and difficult issues for member firms – ranging from contract renegotiations with vendors to determining which FINRA member firm should sponsor the registrations of a vendor’s employees and which firm should “supervise” such employees in the common arrangement of a single vendor serving multiple FINRA member firms.<sup>8</sup>

Finally, we believe that, as a drafting matter, the title to subparagraph (b)(6)(A) should be changed from “Requirement” to “Covered Persons,” to be consistent with the structure of the Rule and for clarity’s sake.

Accordingly, SIFMA requests that the title and introductory sentence of proposed Rule 1230(b)(6)(A) be revised to read as follows:

“(6) Operations Professional

(A) Covered Persons

“Each of the following associated persons of the member, charged with responsibility for overseeing and protecting the functional and control integrity of the covered functions in paragraph b(6)(B) of this Rule, shall be required to register as an Operations Professional.”

With respect to proposed Rule 1230(b)(6)(A)(i), despite FINRA’s commentary in the statement of comments section of its rule filing that registration requirements apply up the “chain of command,” we believe it is still unclear “how *far* up the chain” the requirement is meant to apply. Presumably, FINRA does not intend that senior management up to and including, for example, CEOs of broker-dealers be required to add this registration to their current ones. Therefore, we believe the rule should be revised to refer to “direct responsibility” for the covered function (or alternatively, “primary responsibility”). We note that this would be consistent with FINRA’s general description of covered persons quoted at the beginning of this Section II, “Covered Persons.”

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<sup>8</sup> However, should the SEC determine to approve FINRA’s Operations Professional registration proposal in its current form, we believe it must acknowledge that, by expanding the scope of persons subject to registration to include personnel performing covered functions at non-members, FINRA effectively has expanded its regulation of outsourcing arrangements significantly. We note that on March 29, 2011, FINRA published for comment proposed Rule 3190 on the use of third-party service providers (or outsourcing), which SIFMA is in the process of evaluating. See *FINRA Regulatory Notice* 11-14. Respectfully, we believe that it is in the context of FINRA’s outsourcing proposal that it should address directly FINRA’s proposed supervisory framework for third-party service providers, rather than indirectly through this registration proposal. SIFMA is carefully analyzing FINRA’s outsourcing proposal and will file a comment letter addressing this issue in more detail, along with other important issues raised by that proposal.

With also note that proposed Rule 1230(b)(6)(A)(iii) includes as covered persons those individuals with the authority or discretion to commit a member to any material contract or agreement (written or oral) in direct furtherance of the covered functions. . . ” SIFMA respectfully requests that FINRA amend this provision to state that only written contracts are within the scope of this provision to avoid confusion arising from interpreting when an oral contract may arise in the context of back office operations.

Finally, we believe FINRA should acknowledge in its Proposal, or in the Regulatory Notice announcing the Rule’s approval and setting an effective date, that member firms tailor their supervisory and supervisory control procedures to reflect their business size and organizational structure, and that as a result, the hierarchy of supervisors registered as Operations Professionals will vary depending on a particular firm’s system of supervision and the particular covered function. Moreover, FINRA should acknowledge that there is not a presumption that all “managers” with direct reports engaged in covered functions be registered, if in fact the responsibility for supervision of the activity, as contemplated under NASD Rule 3010, resides at a higher level in the organization.<sup>9</sup>

### III. Covered Functions – Proposed FINRA Rule 1230(b)(6)(B)

#### A. Client On-Boarding

Although we agree with FINRA that the term “on-boarding” is generally understood in the securities industry, we ask that FINRA please confirm that it does not intend to cover client facing or “front office” personnel, who may have some involvement in the on-boarding process. For example, in many firms, employees in branch offices who are not registered representatives may assist in gathering necessary new account forms and related documentation and information from customers as part of their clerical or administrative duties. Similarly, other of the covered function descriptions could inadvertently capture client facing or front office personnel and we ask that FINRA clarify that it does intend to require registration of these personnel.

#### B. Prime Brokerage

SIFMA believes that FINRA should strike the parenthetical “(services to other broker-dealers and financial institutions)” because “prime brokerage” activity is well understood in the securities industry,<sup>10</sup> and the reference to “financial institutions” is potentially

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<sup>9</sup> This could be accomplished through additional supplementary material to the Rule, as proposed below in Section III, E “Covered Functions (xiii), (xiv), and (xv).”

<sup>10</sup> Prime Brokerage Committee, SEC No-Action Letter, 1994 SEC No-Act. Lexis 466, January 25, 1994,

misleading because the term is not defined in the Rule and therefore creates unnecessary ambiguity.<sup>11</sup>

#### C. Approval of Pricing Models Used for Valuations

SIFMA proposes one change to the description of covered function (x) “Approval of pricing models used for valuations.” SIFMA believes that FINRA intends to capture those personnel who approve the systems or models that are used to value customer holdings, as opposed to firm risk management or credit functions that arguably could fall under this covered function as currently drafted. SIFMA, therefore, requests that this covered function be revised to read: “approval of pricing models used for the valuation of customer holdings.”

#### D. Financial Regulatory Reporting

FINRA originally proposed to use the term “Financial Regulatory Reporting” to identify this function. The revised proposal describes this covered function as “contributing to the process of preparing and filing financial regulatory reports.” We understand FINRA made this change in response to a comment on RN 10-25, but respectfully believe that the revised description is overbroad, interjects unnecessary uncertainty into the analysis as to whether an individual is covered and is inconsistent with the “depth of staff” concept in paragraph 6(b) (A) of the Rule. Accordingly, we request that FINRA strike “contributing to the process” from the description of this covered function.

#### E. Covered Functions (xiii), (xiv), and (xv)

SIFMA appreciates FINRA’s clarification that the scope of covered functions (xiii), (xiv) and (xv) includes only those individuals who both “define *and* approve” business requirements and policies. SIFMA believes that FINRA should further clarify in supplementary material that covered functions (xiii), (xiv), and (xv) do not require the license of all supervisors in these areas, but only those supervisors making decisions in defining, approving and/or validating firm requirements or policy. Supervisors participating in the process of *implementing* requirements or policy but who do not change the business requirements or firm policy or approve business systems as meeting requirements should not require a license. Otherwise, hundreds of lower level development managers in the Information Technology (“IT”) and other departments of SIFMA member firms who lack decision-making authority and do not “define and approve” potentially could be captured by the registration requirement. Imposing a

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<sup>11</sup> For example, for purposes of FINRA Rule 3160, “Networking Arrangements Between Members and Financial Institutions,” the term is as “federal and state-chartered banks, savings and loan associations, savings banks, credit unions, and the service corporations of such institutions required by law.” We note, however, that hedge funds commonly make use of prime brokerage arrangements.

licensing requirement on all these lower level managers is unnecessary to achieve the goals of the Proposal and would make it much harder to attract developers to work in the securities industry. In addition, technology projects and budgets naturally are subject to significant fluctuations and firms tend to “staff to the peaks” through temporary personnel. Imposing registration requirements on such temporary employees would be impractical.

SIFMA is particularly concerned about FINRA’s expectation with regard to covered function (xiii) (requiring registration of employees “[d]efining and approving business requirements for sales and trading systems and any other systems related to the covered functions, and validation that these systems meet such business requirements”). In SIFMA’s member firms, particularly in its larger members, IT developers typically do not fall within this covered function. Rather, IT development teams develop systems for the business according to business specifications and requirements for delivery back to the business for testing, validation and approval. In this process, the IT development team *implements*, but does not “define and approve” or validate the systems.<sup>12</sup>

Although the text of covered function (xiii) does not require managers of IT development teams to register unless they define and approve and/or validate systems as meeting business requirements, certain statements in FINRA’s rule filing create unnecessary ambiguity. FINRA provides in the statement of comments section of its rule filing that “the covered functions generally would not include a person who engages in administrative responsibilities, such as an initial drafter or a code developer,” but FINRA adds broadly that “a person who supervises or approves such activities generally would be required to register as an Operations Professional.” The text of covered function (xiii), however, does not require managers of IT development teams to obtain a license unless they define and approve and/or validate systems as meeting business requirements. As noted above, the hierarchy of supervisors within the scope of the covered functions will vary depending on how firms implement a covered function.

We therefore request that FINRA amend its rule filing to remove the above broad statement regarding covered function (xiii) because the statement conflicts with the text of the rule and may create confusion.

Lastly, as noted above in the discussion of “covered persons,” SIFMA is concerned about FINRA’s statement that registration requirements would apply up the “chain of command.” This statement is particularly problematic in the area of Technology. We therefore request FINRA to confirm that the Chief Information Officer, Chief Technology

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<sup>12</sup> In some cases, there are designated individuals within IT who are assigned a role in the nature of a business analyst to work with the business to develop the business requirements themselves as well as conduct validation and approval of systems to confirm the requirements are satisfied. SIFMA believes that these individuals should not require a license if a licensed individual in another division or department of the firm (*e.g.*, operations), approves and validates the systems, but if FINRA requires that individuals within IT be licensed, these are the only individuals who arguably should fall within the scope of category (xiii).

Officer or other senior executive responsible for a member firm's overall IT function need not register as an Operations Professional if not "directly" or "primarily" responsible for the covered functions, as proposed above.

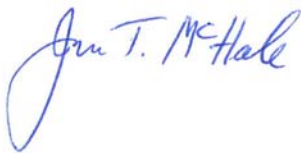
F. Posting of "Books and Records"

Finally, SIFMA believes that proposed FINRA Rule 1230(b)(6)(B)(xvi) is extremely difficult to understand and apply as currently written and should be deleted as redundant. As a practical matter, we are not aware of any separate "function" that consists of "posting entries to a member's books and records." Rather, part of the obligation of those performing covered functions (i) through (xv) is to comply with regulatory requirements as to books and records related to such functions. Such personnel, of course, already will be required to register by virtue of supervising their core covered functions. Therefore, we respectfully urge that this "catch all" provision be deleted.

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SIFMA appreciates the opportunity to provide comments on the Proposal. We would be pleased to discuss the Proposal and our comments in greater detail with the SEC and its staff. If you have any comments or questions, please do not hesitate to contact me at (202) 962-7386 or [jmchale@sifma.org](mailto:jmchale@sifma.org).

Sincerely,



James T. McHale  
Managing Director and Associate General Counsel

cc: Mr. Joseph Furey  
Mr. Marc Menchel  
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