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VIA ELECTRONIC MAIL

Marcia E. Asquith
Senior Vice President and Corporate Secretary
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 12-23: Supplemental FOCUS: FINRA Requests Comments on Proposed Supplementary Schedule for Derivatives and Other Off-Balance Sheet Items

Dear Ms. Asquith:

We are submitting this letter on behalf of certain broker-dealers who are our clients (the "Broker-Dealers"), in response to Regulatory Notice 12-23, "Supplemental FOCUS: FINRA Requests Comments on Proposed Supplementary Schedule for Derivatives and Other Off-Balance Sheet Items ("Notice 12-23")." The Broker-Dealers appreciate FINRA's efforts to more effectively assess the potential impact off-balance sheet activities may have on member firms' ability to fulfill their customer protection obligations and funding needs. While the Broker-Dealers support FINRA's goals in this regard, we believe that the classification of all firms not exempt from Securities and Exchange Commission ("SEC") Rule 15c3-3 as "carrying or clearing firms" does not properly reflect the business models of all such firms and leads, as shown by the proposal in Notice 12-23, to an overly broad regulatory approach to identifying potential risks. For this reason, we urge FINRA staff to try to refine the category of broker-dealers which would be required to file the proposed supplemental schedule.

The Proposed Supplemental Schedule. FINRA Rule 4524 (Supplemental FOCUS Information) requires each firm, as FINRA shall designate, to file such additional financial or operational schedules or reports as FINRA may deem necessary or appropriate as a supplement

to the FOCUS Report. Pursuant to Rule 4524, FINRA is proposing to require all carrying and clearing firms to file with FINRA on a quarterly basis a proposed Derivatives and Other Off-Balance Sheet Items Schedule ("OBS"). FINRA states that the information provided in OBS will permit FINRA to assess more effectively on an ongoing basis the potential impact off-balance sheet activities may have on carrying and clearing firms' net capital, leverage and liquidity, and ability to fulfill their customer protection obligations. Notice 12-23 does not define the term "carrying or clearing firm" but we assume that it includes all broker-dealers that are not exempt from SEC Rule 15c3-3.

Comments. As noted above, the Broker-Dealers believe that as proposed, the category of firms that would be required to file the OBS is not sufficiently tailored so as to capture those firms, but *only those firms*, that engage in the business activities giving rise to the risks FINRA seeks to make more transparent.

As the staff is aware, under current interpretations of Rule 15c3-3, a broker-dealer can be classified as a carrying or clearing firm for reasons unrelated to the particular risk profile of the firm. For example, broker-dealers that distribute variable insurance products and shares of investment companies (mutual funds), and firms that introduce their business to clearing firms, typically do business on a "check and app" basis, *i.e.,* customers are asked to pay for their investments by writing a check payable to a third party, which is the product manufacturer (in the case of insurance company securities and investment company shares), or the clearing firm in the case of other types of securities (such as equities). The point is that check and app firms do not seek to hold customer money or securities or engage in business lines that leverage off the holding of customer funds or securities.

Despite building business models pursuant to which customers pay for their investments by making a check payable to a third party, "check and app" broker-dealers may nonetheless be classified as "carrying" broker-dealers because current interpretations of SEC Rule 15c3-3 require that, in order to be classified as exempt from Rule 15c3-3, customer funds and securities must be forwarded to third parties by noon of the next business day following receipt. As has been noted in previous comment letters filed with FINRA and the SEC, it is virtually impossible for broker-dealers with sales forces "in the field" to consistently comply with a requirement that all customer checks be transmitted to the product manufacturer or other third party by noon of the next following business day.[1]

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[1]*See* Release No. 34-56376 (Sept. 7, 2007) and FINRA Rule 2330, which together permit broker-dealers distributing variable annuities up to seven business to hold customer checks made payable to the insurance company issuer, after an office of supervisory jurisdiction receives a complete and correct application. Such relief has made it possible for these types of distributors to rely on exemptive provisions of Rule 15c3-3.

In its request for comments on Notice 12-23, FINRA seeks specific comment on whether there is a category of carrying or clearing firms that should not be required to file the proposed OBS based upon *de minimis* off-balance sheet activity. While we believe the *de minimis* concept is a helpful starting place for consideration of the issues, we believe it is more important to try to identify the types of business or the types of transactions that FINRA believes give rise to a specific need to bring greater transparency to FOCUS reporting, and then, after identifying those business lines and/or types of transactions, require firms that engage in those particular activities to file the OBS. This closer examination is likely to result in a more targeted approach with respect to all firms, not just carrying and clearing firms. In other words, while the Broker-Dealers believe that the answer to FINRA's question regarding whether there are categories of firms that should be exempt from filing the OBS is "yes," the Broker-Dealers also believe that a *de minimus* standard alone may not result in identifying the firms that pose off-balance sheet risk to such a degree that regulatory attention is warranted.

Accordingly, the Broker-Dealers request that FINRA try to more closely identify the nature of the firms for whom off-balance sheet activity reporting is appropriate, and limit the application of the OBS to those firms, rather than assuming that all firms that are not exempt from Rule 15c3-3 are engaging in off-balance sheet activity as a regular course of business. We would be happy to discuss specific ideas with FINRA staff at its convenience.

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Please do not hesitate to contact Holly H. Smith (202.383.0245) if you have any questions regarding the issues addressed in this letter.

Respectfully submitted,

SUTHERLAND ASBILL & BRENNAN LLP

BY: Holly H. Smith
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