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June 4, 2004

Via Electronic and First Class Mail

Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, DC 20549

Re: Proposed Rule Changes of Self-Regulatory Organizations
(Release No. 34-49505; File No. S7-18-04)

Dear Mr. Katz:

The Self-Regulation and Supervisory Practices Committee of the Securities Industry Association ("SIA")[1] appreciates the opportunity to comment on the referenced rule proposal ("Rule Proposal"), which seeks to modify the Self-Regulatory Organization ("SRO") rule-making process for purposes of increasing regulatory transparency and efficiency. Among other things, the proposed amendments to Rule 19b-4 would require SROs to: (i) file proposed rule changes electronically with the Commission through a web-based system, rather than in paper form; (ii) post all proposed rule changes and amendments on their public websites no later than the next business day after filing with the Commission; and (iii) post and maintain a current and complete version of their rules on their websites. In addition, each SRO would be required to update its public website to reflect rule changes no later than the next business day after it has been notified of Commission approval of the rule change or Commission notice of an effective-upon-filing SRO rule.

The Committee commends the SEC Staff for undertaking this important initiative and wholeheartedly supports the Rule Proposal as a significant improvement to the existing regulatory rulemaking regime. As the SIA Committee tasked to monitor and comment upon rules and regulations governing broker-dealer self-regulation, we are keenly interested in the Rule Proposal. Central to our mission is increased regulatory transparency and efficacy, which we firmly believe must be predicated on public awareness and understanding of both the process of enacting and enforcing rules, as well as the actual substance of regulatory obligations. The proposed 19b-4

[1] The Securities Industry Association, established in 1972 through the merger of the Association of Stock Exchange Firms and the Investment Banker's Association, brings together the shared interests of nearly 600 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. According to the Bureau of Labor Statistics, the U.S. securities industry employs 780,000 individuals. Industry personnel manage the accounts of nearly 93-million investors directly and indirectly through corporate, thrift, and pension plans. In 2003, the industry generated an estimated $209 billion in domestic revenue and $278 billion in global revenues. (More information about SIA is available on its home page: www.sia.com.)

amendments will undoubtedly reduce delays and enhance the SRO rulemaking by allowing interested parties to better track rule filings and provide valuable information about actual market practices and potential consequences early in the process to avoid promulgation of unnecessary, ineffective or overly burdensome rules and regulations. Accordingly, we urge the Commission to act expeditiously in adopting the proposed rule changes.

Additionally, we respectfully suggest that further modifications are needed to fully realize the stated objectives of the Rule Proposal. As detailed below, we believe that the Commission should also require all SROs to:

- implement formal notice and comment procedures that solicit the views of their members in advance of filing a proposed rule change with the Commission;
- implement formal notice and comment procedures that solicit the views of their members in advance of issuing substantive interpretive guidance related to new or existing rules;
- post and cross-reference on their websites all regulatory interpretations, notices or information memoranda relating to their specific rules;
- convene a joint SRO Regulatory Review Committee to screen rule proposals relating to regulation of broker-dealers in order to identify and reconcile regulatory inconsistencies before submission of the proposals to the SEC pursuant to Rule 19b-4;
- articulate a reasonable basis for any inconsistency or non-conformity with existing rules of other SROs, as part of their Rule 19b-4 filing; and
- undertake an analysis of the potential administrative, operational or economic burdens in advance of filing with the Commission, and attest to the degree of such impact as part of their filing.

We believe that these measures, together with the proposed amendments, would greatly enhance the quality of SRO rule proposals by promoting well-developed submissions of SRO rules proposals, as well as efficiency of Rule 19b-4 review. Equally significant, a regulatory regime with these characteristics provides market participants with predictability and clarity of the regulations with which they must comply.

I. Increased Regulatory Transparency and Public Input Before Filing

The Committee strongly supports requiring SROs to post on their public websites all proposed rule changes, as well as any amendments thereto, no later than the next business day after filing with the Commission. We also support timely updates of a rule filing's status, including whether a rule proposal was deemed not properly filed, or withdrawn by the SRO. As aptly noted in the Rule Proposal, several SROs post only selected rule filings on their websites, if at all. Uniform website accessibility, therefore, will permit interested persons to more readily monitor and offer input on proposed SRO rule changes, thus fostering a fundamental goal of our national self-regulatory system.

To fully achieve regulatory transparency and efficacy, however, public review and consultation needs to begin well before the SRO files the rule change with the Commission. Specifically, affected parties must have a reasonable opportunity to review and provide feedback on SRO proposals at the earliest stages of their development. To that end, we strongly recommend that the Commission modify Rule 19b-4 to further require SROs to publish and request comment on all rule proposals of a significant nature *in advance* of filing with the Commission.

Too often, in an attempt to keep pace with rapidly changing conditions and practices within the industry, SROs quickly file rule proposals without adequately canvassing all interested parties. Though clearly well-intentioned, this approach has resulted in a great deal of confusion, delayed effectiveness and costly back-end action to clarify or correct issues that could have been avoided had market participants been permitted to review, offer comments and provide alternative solutions to the rule proposal at the inception of the regulatory dialogue.[2] Indeed, although the option is available to them, some SROs routinely file proposed amendments with the Commission without ever notifying their members of a prospective rule change or soliciting public comment. Consequently, member firms may learn of a significant regulatory proposal only upon publication of the rule filing in the *Federal Register* --- well after it has undergone several reiterations both internally within the SROs and at the SEC. This is especially problematic when we consider the relatively short comment period usually afforded the public once the SRO rule filing becomes publicly available in the *Federal Register*. Typically twenty-one days, this time frame can be woefully inadequate to review and develop detailed, substantive and well-considered comments on significant rule filings.[3]

By implementing formal procedures that expressly require the SROs to engage market participants and other affected parties at the outset of the rule making process, the Commission will ensure that those most impacted are afforded a meaningful voice in the development of an SRO's rule's direction. This will result in a more fluent rule-making process, as well as more tempered, resource-efficient regulation that serves the interests of investors, regulators and broker dealers alike.

Notably, while some SROs rely upon internal vetting processes that may include review and majority approval of proposed rule changes by special committees, such processes do not ensure that the diverse perspectives and concerns of those impacted by a rule modification are adequately represented. Simply put, there is no assurance that a handful of industry representatives will provide the "big picture" view obtainable through broader notice and comment procedures. For example, such committees may not include industry members from the relevant business unit or with the requisite expertise to conduct a proper analysis of the rule's ramifications. Therefore, notwithstanding any incremental delays likely to be associated with implementing our recommendation, experience shows that increasing the speed of rule changes must be predicated upon sufficient public exposure and dialogue regarding possible changes to regulatory obligations well before filing with the Commission.

Finally, in recent years, the increasingly complex business and market environment has resulted in unintended and unforeseen consequences from new rule implementations. This has necessarily led to SROs issuing subsequent "clarifications" or interpretative "guidance" which

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[2] Consider, for example, the NASD's riskless principal trade reporting rules. At first blush, these rule changes appeared fairly straightforward. Yet, as everyone soon learned, compliance with the rules had far-reaching systems implications that were neither contemplated nor addressed in the adopting releases. Consequently, implementation was postponed several times while the NASD repeatedly clarified various aspects of the rule and incorporated suggestions of the industry.

[3] There have been numerous instances in which significant proposed rule changes have been published with only a 21-day comment period. Ironically, in many of these cases, the SRO in question itself spent months, or even years, developing the proposal. See e.g. NASD and NYSE Supervisory Controls Rule Proposals, SR-NASD-2002-162 and SR-NYSE-2002-36 (November 20, 2002). See also, NASD CEO Certification Proposal, SR-NASD-2003-176 (December 23, 2004) (the preceding NASD Notice to Members did, however, offer member firms an early opportunity to comment).

routinely is not noticed for public comment prior to effectiveness. Consequently, these too have led to instances of industry-wide confusion and repeated regulatory reiterations.[4] Thus, we similarly recommend that the Commission consider amending Rule 19b-4 to also require SROs to formally solicit the views of their members in advance of issuing substantive interpretive guidance related to new or existing rules.

II. Posting of Rules and Interpretative Guidance on SRO Websites

The Committee also supports requiring SROs to post and maintain a current and complete version of their rules on their websites. As noted in the Rule Proposal, current practice varies significantly among SROs as to the extent and timeliness to which they post and update their rules on their websites. Prompt and accurate notification of SRO rule changes, therefore, will provide greater regulatory clarity, as well as facilitate compliance of SRO rules.

By the same token, it is equally important for SROs to post and cross-reference on their websites all interpretations, informational memoranda and notices that relate to their specific rules. Now more than ever, such forms of interpretative "guidance" are increasingly becoming authoritative documents used by SRO staff in determining whether violations of the respective SRO's rules have occurred. Posting and cross-reference to this type of information therefore not only regulatory transparency, it highlights any existing or potential inconsistency between the interpretative material and the body of law it is intended to augment.

III. Identification and Elimination of Unnecessary Regulatory Inconsistency

In addition to the forgoing, we also suggest that SROs implement formal measures in order identify and eliminate unjustified regulatory inconsistency.[5] Duplicative and conflicting regulation across SROs, as well as government regulators, yields little benefit while depleting valuable administrative and economic resources from all segments of the securities industry. This includes not only the cost of compliance and supervision to broker-dealers, but needless expenditure of valuable regulatory staffing and operating resources to monitor and examine broker-dealer activity on substantially identical or similar subjects. The existence of multiple sets of rules governing identical areas is not burdensome *per se.* However, practical difficulties arise when there are variations of language or interpretations of parallel regulation, which can cause inconsistent application among firms, as well as differing enforcement by regulators of ostensibly similar rules. More so, particularly within the realm of investor protection rules, this can cause disparate levels of investor protection based solely upon their firm's SRO affiliation. Accordingly, we suggest that the SROs convene a joint Regulatory Review Committee to screen rule proposals relating to regulation of broker-dealers in order to identify and reconcile potential inconsistencies before the proposals are submitted to the SEC pursuant to Rule 19b-4. Moreover, and in all events, we recommend that the SEC amend Rule 19b-4 to further require SROs, when making a rule filing with the

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[4] See New York Stock Exchange ("NYSE") Information Memos 02-07 and 02-19 governing error accounts.

[5] Notably, the United States General Accounting Office ("GAO") in its report entitled *Securities Markets: Competition and Multiple Regulators Heighten Concerns about Self-Regulation* recommended that the SEC work with the SROs and broker-dealer community to implement a formal process for systemically identifying and harmonizing material regulatory inefficiencies caused by differences in rules or rule implementations among SROs.

Commission, to articulate a reasonable basis for any inconsistency or non-conformity with existing rules of other SROs.

IV. Pre-Filing Cost-Benefit Analysis

To further promote regulatory efficiency and expedite the SRO rule-making process, we suggest that the Commission also implement a formal mechanism that ensures that the SROs carefully and thoroughly deliberate the practical economic and administrative impacts of proposed rule changes. Specifically, as a pre-requisite to filing a rule change with the Commission, we believe that the SROs should undertake an analysis of the potential administrative, operational or economic burdens in advance of filing with the Commission, and to attest to the degree of such impact as part of their filing. We believe that such an approach requiring a "regulatory impact statement" is entirely consistent with the Commission's objectives, as well as the mandates of Section 3(f) of the Act.

V. Conclusion

The Committee appreciates the opportunity to provide comments on the Rule Proposal and we hope that our comments are helpful. If you have any questions or would like to discuss our comments further, please contact Amal Aly, Staff Advisor to the Self-Regulation and Supervisory Practices Committee at (212) 618-0568.

Sincerely,

John Polanin Jr.
Chairman
SIA Self-Regulation and
Supervisory Practices Committee