WEDBUSH

March 31, 2010

By Electronic Mail (rule-comments@sec.gov)

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

Re: Risk Management Controls for Broker or Dealers with Market Access
Release No. 34-61379; File No. S7-03-10

Dear Ms. Murphy,

Wedbush Securities Inc. ("Wedbush") appreciates the opportunity to comment on the recent Securities and Exchange Commission ("SEC") proposed rule on "Risk Management Controls for Broker or Dealers with Market Access" ("Proposed Rule" or "15c3-5"). Wedbush is a leading provider of clearing services and sponsored access solutions for registered broker-dealers and non-registered entities. As a top liquidity and volume provider[1] to many market centers we are in a unique and highly qualified position to comment on the Proposed Rule changes.

Generally, we support the principles of the Proposed Rule and agree that policies, procedures, pre-trade and post-trade risk controls provide the best protection for the integrity of the financial markets and its participants. However, the requirements of the Proposed Rule should not be applied on a one size fits all basis. We are concerned that certain aspects of the Proposed Rule that will create an unlevel playing field and a potential race to the bottom for risk management. Lastly, we want to make clear a few points about market structure, review the costs of this proposal, and provide our ideas on ways to further improve the safety and soundness of the financial markets.

1. Market Access Requirements Should Not Be One Size Fits All

In today's financial markets, transactions are effected by a broad and diverse group of market participants including non-registered entities like; individual investors, institutions, professional traders, hedge funds, and registered entities like brokers or dealers[2] ("broker-dealers").

[1] NASDAQ Trader Website, #1 Liquidity Provider for NASDAQ or NYSE Securities for each month since June 2006.
[2] For the purposes of this comment letter we are referring to U.S. Registered Brokers or Dealers only.

WEDBUSH SECURITIES INC. Member NYSE/FINRA/SIPC
1000 Wilshire Boulevard, Los Angeles CA 90017 / PO Box 30014, Los Angeles CA (213) 688-8000 www.wedbush.com

Registered broker-dealers include those that are Self Regulatory Organization ("SRO") or Financial Industry Regulatory Authority ("FINRA") members. In all cases these entities are registered with the SEC and subject to all laws and rules promulgated by the SEC including 15c3-5.

Currently, in order for non-registered entities to access the markets a broker-dealer must be involved (e.g. sponsorship or direct market access). We support the idea that all market access must be conducted by a registered entity and subject to the requirements set forth in the Proposed Rule.

It should not be necessary that a broker-dealer sponsoring (e.g. sponsoring member) another broker-dealer (e.g. sponsored participant) should be required to apply an additional set of pre-trade risk checks. Since the sponsored participant, in this example, is subject to the Proposed Rule the sponsoring member should be allowed to allocate certain responsibilities including the pre-trade risk control aspects of the Proposed Rule.

Allocations of responsibilities such as these are commonplace and appropriate between broker-dealers. New York Stock Exchange ("NYSE") Rule 382 and FINRA Rule 3230 support this concept in clearing and execution relationships as the parties to the relationship are registered and regulated entities subject to all securities laws, rules, and regulations. Furthermore, support for this concept can be found in Regulation SHO where broker-dealers are allowed to, on the basis of reasonable grounds, rely on representations of "any person" in conjunction with short sale locate requirements.

In the release of the Proposed Rule, the SEC questions[3] whether broker-to-broker market access relationships should be treated differently under 15c3-5. Brokers seek market access from other brokers for a variety of reasons including improved economics from market centers (i.e. volume aggregation), reduced technology and operational costs (i.e. smart order routing), and in situations where the broker-dealer may not be a member of the receiving exchange (i.e. lack of membership). Each of these situations has benefits for both the broker-dealer placing the orders and the broker-dealer providing market access.

One contributing factor to Wedbush being one of the largest volume traders in the equities markets is volume aggregation. Volume aggregation was developed as a result of tiered pricing structures from the various market centers. Volume aggregation is no different in concept than any other consortium, cooperation, or other group that seeks to purchase larger quantities of goods and receive a discount based on those larger quantities. Clients benefit because volume aggregation provides the best economics available from the market center which in turn allows them to tighten trading spreads and reduce the incremental cost of trading. The largest global trading firms benefit from these pricing plans without the use of volume aggregation services. Volume aggregation is a mechanism to level the playing field with respect to market center economics.

Many broker-dealers, including Wedbush, outsource certain aspects of their trading to firms offering liquidity and smart order routing services. One primary reason is to reduce the technology and operational costs around accessing the ever-growing number of market centers. The costs to connect, develop interfaces, and maintain these connections are very significant. By using broker-dealers in this

[3] See page #35 of the Proposed Rule – "If a broker or dealer provides another broker or dealer with market access, should such an arrangement be treated differently under the proposed rule?"

WEDBUSH SECURITIES INC. Member NYSE/FINRA/SIPC
1000 Wilshire Boulevard, Los Angeles CA 90017 / PO Box 30014, Los Angeles CA (213) 688-8000 www.wedbush.com

space we reduce our operational costs, maintain best execution, and ultimately reduce the cost of trading for our clients. If these broker-dealers had an obligation to perform additional pre-trade checks it would surely raise the cost of trading and reduce the benefit to our clients. The broker-dealer with the most direct access to the required information and the most efficient ability to control the risks should have the responsibilities under 15c3-5.

Lack of exchange membership is less of an issue than in years prior, but it was not that long ago that membership in the NYSE required significant capital and ownership of an exchange seat. Seats on the NYSE have sold for as much as $4,000,000 in 2005[4]. As a result of these requirements many broker-dealers sought access to the NYSE through their clearing firms. Today, many broker-dealers are members of a handful of exchanges, but perhaps not all. As in years past, these firms will look to their clearing firms for access to the markets. Clearing firms have successfully allocated certain responsibilities to their broker-dealer clients through contracts, policies, procedures, and other risk management practices while ultimate responsibility remains with the clearing firm member.

The requirement of a registered broker-dealer to comply with 15c3-5 should provide the Commission with the basis to incorporate a broker-to-broker exemption where the exemption specifically allows the broker-dealer providing market access, on reasonable grounds, the ability to allocate certain pre-trade risk control responsibilities to the other registered broker-dealer. The scenarios noted above are real examples of why this exemption is important.

In Chairman Schapiro's remarks to the Securities Industry Financial Markets Association ("SIFMA") Annual Conference on October 27th, 2009 she noted in reference to the Proposed Rule, "…One proposal will address the risk of sponsored access to exchanges. It will focus on arrangements that enable unfiltered access by non-regulated entities — in many cases, high frequency traders — to exchange systems. I liken it to giving your car keys to a friend who doesn't have a license and letting him drive unaccompanied." Broker-dealers are licensed and should be allowed to use it and relied upon to use it properly.

2. An Un-Level Playing Field

We believe the Proposed Rule, without a broker-to-broker exemption, will create the unintended consequence of an "unlevel playing field" with respect to market access. Broker-dealers that do not achieve the best economics from the market centers will be faced with the choice of slower access to the markets, because of the second set of pre-trade risk checking, or losing the benefit of volume aggregation. To highlight the significance, consider this example. Under today's pricing schedules a firm providing liquidity for 100 shares of stock, on the NASDAQ Exchange, would earn a rebate of $.20. However, using volume aggregation, they can earn up to $.295 for the same transaction, an increase of 47.5%. If a firm, that does not already reach the top pricing tier of the market center, chooses to access the markets under their own market participant identifier ("MPID"), they will remain obligated to meet the requirements of 15c3-5, but will realize a 32% decrease in rebate income. If the same firm decides to access the market center through another firms pre-trade risk control system, they will suffer a time delay that would automatically put them at a disadvantage relative to their competition. Both examples will

[4] See the following URL: http://www.nyse.com/press/1135856420824.html.

WEDBUSH SECURITIES INC. Member NYSE/FINRA/SIPC
1000 Wilshire Boulevard, Los Angeles CA 90017 / PO Box 30014, Los Angeles CA (213) 688-8000 www.wedbush.com

lead to less liquidity in the markets and wider spreads because there is less competition among these liquidity providers. This will stifle innovation and consolidate more market share with fewer firms.

3. Don’t Create a Race to the Bottom in Risk Management

Since the release of the Proposed Rule our firm has been approached by many firms claiming to offer risk checking capabilities at various degrees of “fast”. In such a highly competitive marketplace we are concerned that third-party providers may deprecate their solutions in order to remain on the bleeding edge in terms of performance. Broker-dealers will have a difficult time assessing what is real vs. what is smoke and mirrors. Furthermore, a market-leading risk management firm that is successful in attracting significant volume is still susceptible to programming errors and bugs, but now a larger amount of the market would be impacted by a single bug.

The Proposed Rule and general industry best-practices dictate that certain pre-trade risk controls are needed to reduce risk to the marketplace. We agree that such risk controls are necessary and, in fact, require that firms we sponsor to the markets demonstrate and maintain appropriate pre-trade controls. In fact, in our experience, we have found that sponsored access clients currently deploy sophisticated and high performance risk management systems that are far superior to those offered by third party vendors.

We believe the exchanges should continue to improve their technology so that pre-trade risk controls are available on their platforms – for members and sponsored participants alike. Exchange rules should require that sponsored participants and direct members utilize these pre-trade risk filters to reduce risk while establishing a level playing field for all participants. Providing these pre-trade risk filters at the exchange level will create uniform and high quality controls and reduce risk for sponsoring members, sponsored participants, the exchange, regulators and the general public.

Pre-trade risk filters benefit the entire industry by helping to prevent computerized trading malfunctions, executions during trading halts, clearly erroneous transactions, and other potentially inappropriate activity. Certain pre-trade risk filters should be applied to all orders whether sponsored or not, thereby eliminating the performance or speed differential, and effectively encouraging firms to utilize these controls. To do otherwise would encourage a “race to the bottom” as broker-dealers and vendors vie for the highest performance risk systems that may or may not meet the desired objectives of risk management.

Exchanges have already introduced special order types and other risk mitigation solutions to address many of these issues. We strongly encourage the continued development of these capabilities and advocate that required filters be applied consistently to both sponsored participants and member participants. The final rules should explicitly allow broker-dealers to rely on exchange level controls as pre-trade risk controls and a part of its risk management program.

4. Additional Enhancements to Reduce Market Access Risk

Computerized trading has significantly increased the liquidity in the markets and thereby reduced the spread between the bid and offer on equities. Tighter spreads benefit the public and market participants by more maximizing the value in shares purchased or sold. The competitive nature of this business segment demands that these liquidity providers and active traders have the fastest access to the markets possible. These important needs should be balanced with the need for safe and secure markets.

Broker-dealers receiving or generating orders must establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks, such as legal and operational risks related to market access.

Wedbush has significant experience in successfully working with sophisticated clients who enter into sponsored access arrangements for NASDAQ and other markets. Under the current proposed sponsored access framework, we work closely with clients to understand, monitor, and support their risk management systems and compliance procedures on an ongoing basis. Under the current system of sponsored access, the sponsoring member generally has the responsibility for complying with the exchanges' rules and regulations in connection with the sponsored participant's activity. If not for sponsored access, many of these firms would become direct members of the exchanges and operate the same technology platforms, but would trade without the benefit of the sponsoring members' due diligence, oversight, and financial resources. The current system of sponsored access, thus, reduces risk by providing a second level of protection that improves overall risk management. Our involvement, on a sponsorship basis, has identified weaknesses in firms that are direct members of various exchanges and otherwise have the ability to access the market center directly. Sponsorship provides a second level of review and monitoring that adds value by reducing risk. However, we believe that in addition to the Proposed Rules there should be a centralized post-trade limit monitoring system that allows for an industry-wide view of positions and risk.

Wedbush and other Depository Trust & Clearing Corporation ("DTCC") members are working with the NSCC, a division of DTCC, to develop a platform to provide a global view of equity positions across broker-dealers, prime-brokers, and clearing firms ("Limit Monitoring System"). This system will allow for the establishment of credit limits and buying power controls and will include consolidated information across all market centers based on trade executions in real-time. Most importantly, this system will be developed and supported by the industry with the performance, accuracy, and quality that is present in all NSCC activities. This system would require that each market participant be provided a specific MPID for its trading activity. A firm with multiple executing relationships would have multiple MPID's aggregated by this system. In addition to providing important visibility into these positions, the system would have a mechanism to disable an MPID, multiple MPID's, or an entire entity across multiple broker-dealers.

We strongly encourage the exchanges to establish a common methodology for the termination of order flow for specific clients and support solutions like the limit monitoring system. Much of the focus in the Proposed Rule is surrounding Sponsored Access, but these new tools and capabilities will support all industry participants, sponsored or not, and improve the integrity and safety of our financial markets.

5. Estimated Costs Too Low

The cost estimates presented in the Proposed Rule are far too low. They do not include the hidden costs of becoming a broker-dealer, the impact of additional latency, or the loss of economics from volume aggregation. These additional costs far exceed the costs noted in the Proposed Rule. Additionally, in our analysis, it will cost more than $2,000,000 per year for our firm to buy or build the appropriate systems.

6. Summary

A. We support the general principles of the Proposed Rule.
B. A broker-to-broker exemption for U.S. Registered Broker-Dealers is appropriate and should be included in the final rule.
C. Broker-dealers should be permitted to rely on exchange level controls, where appropriate, to meet certain elements of its pre-trade risk control obligations.
D. Broker-dealers should utilize unique MPID's to segregate activities and enhance market transparency.
E. Industry participants and regulators should support the Limit Monitoring System as an important evolution in risk management.
F. Implementation costs are grossly underestimated.

We appreciate the opportunity to present our views on the above referenced matter and welcome a more in-depth discussion on any of the topics above or other issues related to market access.

Sincerely,

Edward Wedbush
President
Wedbush Securities Inc.

Jeff Bell
Executive Vice President
Wedbush Securities Inc.

Cc: The Honorable Mary L. Schapiro, Chairman, SEC
The Honorable Kathleen L. Casey, Commissioner, SEC
The Honorable Elisse B. Walter, Commissioner, SEC
The Honorable Luis A. Aguilar, Commissioner, SEC
The Honorable Troy A. Paredes, Commissioner, SEC
Robert W. Cook, Director, Division of Trading and Markets, SEC
James Brigagliano, Deputy Director, Division of Trading and Markets, SEC
David Shillman, Associate Director, Division of Trading and Markets, SEC

WEDBUSH SECURITIES INC. Member NYSE/FINRA/SIPC
1000 Wilshire Boulevard, Los Angeles CA 90017 / PO Box 30014, Los Angeles CA (213) 688-8000 www.wedbush.com