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March 14, 2011

Via E-mail

Marcia E. Asquith,
Office of Corporate Secretary,
FINRA,
1735 K Street, N.W.,
Washington, D.C. 20006-1506.

Re: Regulatory Notice 11-04: Proposed Amendments to FINRA Rule 5122

Dear Ms. Asquith:

We appreciate the opportunity to comment on the amendments to Rule 5122 proposed by the Financial Industry Regulatory Authority, Inc. ("FINRA") pursuant to FINRA Regulatory Notice 11-04 (the "Notice").

The proposed amendment would extend the filing and other requirements of FINRA Rule 5122, currently applicable only to private placements of securities issued by a FINRA member or a "control entity" of a member, to all private placements by all issuers, subject to certain exceptions based on the status of the investors in the private placement. We question whether the addition procedures contemplated by the proposed rule changes are really necessary, given the existing FINRA and Securities and Exchange Commission ("SEC") rules applicable to members' private placement activities. But if FINRA does choose to impose new requirements, it should tailor those requirements so that (1) members are in fact in a position to ensure compliance with the new requirements and (2) the resulting burden on capital raising activities, particularly by small issuers, is no greater than necessary.

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The existing regulatory framework already addresses potential abuses by FINRA members in connection with private placements. In April 2010, FINRA issued its

Regulatory Notice 10-22, in which it provided its views on a broker-dealer's obligation under the Federal securities laws to conduct a reasonable investigation of the issuer and the securities offered in a Regulation D private placement. In addition, existing NASD Rule 2310(a) requires members to have a reasonable basis for recommending a security to a customer, and Section 10(b) of the Securities Exchange Act, and Rule 10b-5 thereunder, provide a remedy for, among other things, a material misstatement or omission in connection with the sale of securities in a private placement. Taken together, these provisions would appear to provide a comprehensive approach to regulating the conduct of members in connection with private placements.

Existing Rule 5122, and the filings made thereunder, focus on a few narrow issues associated with the conflicts of interest that are present when a member conducts a private placement for itself or on behalf of an affiliated entity. There is no logical reason to extend those narrow provisions to private placements generally, because members do not have the same conflicts of interest when handling private placements for unrelated issuers. The Notice does not shed much light on what sort of review FINRA contemplates in respect of the presumably very large number of filings it would receive under the revised Rule, but we seriously question whether the additional filings required by the amended Rule will do anything to enhance member's compliance with those existing due diligence, suitability or anti-fraud requirements.

At the same time, the proposed amendments, as currently drafted, would limit the use of proceeds, and prescribe related disclosure, in all covered private placements. This would effectively result in FINRA's regulating activities and disclosure of the non-member private placement issuers. We question whether Section 15A of the Securities Exchange Act gives FINRA authority to do that. We also question whether members participating in private placements would have the practical ability to ensure that the issuers comply with those requirements, or that FINRA would be the practical authority to enforce such compliance. The proposed limitation should not be framed in terms of the issuer's use of proceeds, or take into account other expenses of the issuer, since those are matters beyond the member's control. If FINRA's concern is the compensation members receive in private placements, the proposal should be revised to address that point directly. However, the Notice does not, in our view, explain why a limitation on compensation would be necessary or appropriate.

If FINRA does impose an express limitation on the compensation a member may receive in a private placement, we suggest that it consider including exceptions and other provisions analogous to those of Rule 5110 – for example, the exceptions from "item of value" set forth in FINRA Rule 5110(c)(3)(B), and the provisions in FINRA Rule 5110(d) defining which items of value received by a participating member must be treated as compensation.

We are also concerned that the FINRA review contemplated by the proposed rule could seriously burden, and even disrupt, the normal private placement

process. Under the current Rule, and as proposed, an offering document would have be filed with FINRA prior to the first time it is provided to a prospective investor, and FINRA may conduct an *ex post* review to assure compliance with the Rule. The Notice goes on to state "if FINRA staff determines that an offering document presents an apparent investor protection issue, the responsible member should expect FINRA staff to contact the broker-dealer concerning the matter, whether or not the offer has already commenced" or, for that matter, closed. Unless the matters covered in the filing and reviewed by FINRA are limited to things within the member's control and ability to remedy, we do not see how an issuer could safely close a private placement without having received FINRA's sign-off. But we doubt that FINRA is, as a practical matter, in a position to provide such clearance to the presumably large number of filings that would result from the amended rule.

The Rule, as proposed to be amended, seems to have been drafted in contemplation of private placements that are primarily offerings for cash. We do not understand how the rule would apply, in practice, to non-cash transactions (for example, acquisitions or exchange offers effected in reliance on the private placement exemption), or to secondary sales of securities. We therefore suggest that the Rule exclude those categories of transactions, and be limited to primarily offerings for cash.

The Rule, as amended, would apply to any member or associated person who "participates" in a private placement (absent an exemption), applying the Rule 5110(a)(5) definition of "participation." That definition is quite broad and captures more than just FINRA members who offer or sell a security in an offering. Indeed, it captures members in a wide variety of roles that would afford the members little or no practical ability to ensure compliance with the Rule. We believe the current approach, under which the Rule applies only to members or associate persons who "offer and sell" in a private offering, should be retained.

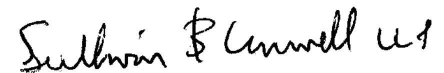
The Rule provides, and the proposed Rule would continue to provide, exemptions for private offerings to certain enumerated categories of investors. The Rule should be revised to make clear that the exemptions are available when the member has a "reasonable belief" that an investor falls within one or more the specified categories. We also suggest that an exemption be added for institutional accredited investors as defined under Regulation D. Private placements to accredited investors are an important source of funding, particularly for smaller companies. Such investors are deemed, under SEC regulations, as being capable of fending for themselves, and we see no reason to disadvantage them as the proposed Rule would do.

We would also suggest that the Rule include a "de minimis" exemption for an offering that includes a limited number of accredited investors or other non-exempt investors, provided that some minimum amount (say 80% or 90%) of the proceeds are raised from otherwise exempt investors under the Rule. Due to the nature of the investors

making up the exempt category, we believe it is reasonable to allow participation by a limited number of "other" investors.

Once again, we appreciate the opportunity to submit these comments. If you have any questions please contact David Harms or Robert Buckholz at 212-558-4000.

Very truly yours,



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