



Securities Industry Association

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Barbara Z. Sweeney
Office of the Corporate Secretary
NASD Regulation, Inc.
1735 K Street, NW
Washington, DC 20006-1500

Re: NASD Notice to Members 01-59; Proposed Amendments to Rule 2710 to
Address Shelf Offerings of Securities.

The Capital Markets Committee of the Securities Industry Association¹ is pleased to submit this response to the National Association of Securities Dealers, Inc.'s (NASDR's) proposed amendment to Rules 2710, and the related Corporate Financing Rules, as set out in Notice to Members 01-59. SIA commends the NASD for recognizing the practical problems of the application of the Corporate Financing Rules in the shelf offering context. Shelf registration provides qualified issuers with a fast and efficient mechanism for accessing the capital markets when conditions are most favorable for borrowing. The proposals are intended to ensure that NASD review does not contribute to unnecessary delays for such issuers.

After examining the proposed new filing requirements, we have concluded that the goal of simplifying the process for seasoned issuers has not been met. Procedures intended to relieve the burdens of review would be unavailable to most seasoned issuers. More significantly, technical provisions that treat individual members of a syndicate differently will introduce unforeseen risks to the underwriting process. For these reasons, we respectfully urge that the proposal be withdrawn and redrafted. We would welcome the opportunity to convene a working group consisting of staff from NASDR, and representatives of the underwriter and issuer counsel communities to design a system that provides real relief from the rule for deserving shelf issuers while preserving the important regulatory goals the rule serves.

¹ The Securities Industry Association brings together the shared interests of nearly 700 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. The U.S. securities industry manages the accounts of nearly 80 million investors directly and indirectly through corporate, thrift, and pension plans, and generates \$358 billion of revenue. Securities firms employ approximately 760,000 individuals in the United States.

General Comments

In a recent speech outlining his agenda for the SEC, Chairman Harvey Pitt stated, “on the capital-raising side, we need to distinguish between unseasoned and seasoned companies, and make it easy for seasoned companies to access our capital markets *within moments* of the decision to raise capital” (emphasis added).² SIA strongly agrees. With the proposed provision for notice filing, NASDR also appears to embrace this goal. However, most of the other changes proposed by the NASD – particularly, those relating to who must file, the timing of the filing and the conditions necessary for the new notice filing process – will result in obstacles that are incompatible with the goal.

NASDR offers insufficient justification for adding to the regulatory burden of seasoned issuers that would still be required to file under the NASD’s rule. The absence of evidence in this area contrasts with the convincing detail used in the release to describe the numerous practical problems associated with the application of the rule to shelf offerings. The NASD merely states that “shelf offerings of larger issuers eligible for Form S-3 also have been the subject of enforcement actions,” but fails to explain the nature or frequency of these incidences. Moreover, in explaining its decision not to expand filing exemptions to all shelf-registered offerings filed on S-3 and F-3, the agency states, “we are aware of manipulative and abusive practices involving listed issuers with less than a three-year reporting history,” but again offers no specifics. Thus, rather than attempting to identify a category of issuers and/or transactions for whom further regulatory relief may be appropriate, the proposal stretches and strains to capture as many shelf issuers as possible for continued heightened review. SIA would respectfully suggest that justification for the blanket treatment proposed must include more than anecdotal reports of abuse and the occasional enforcement action.

Specific Concerns

Below, SIA enumerates some of the problems inherent in the NASDR approach. Rather than tinkering with the proposed framework, SIA recommends development of a new proposal that focuses on streamlining eligibility criteria and simplifying and reducing any required steps.

Who files? – The rule will require individual filings from each member of a syndicate in shelf offerings that do not qualify for an exemption or for notice filing. Such members will have to wait for a “no objections” letter prior to the takedown. While the rule would permit the managing underwriter to make the filing on behalf of all members, the filing would have to identify each participating member. The problem with this proposal is that it does not take into account underwriters who are not invited into the syndicate until later in the process. The notice and proposed rule also do not make clear whether the compensation to all members may or may not be aggregated for purposes of

² Speech by SEC Chairman Harvey Pitt at the PLI 33rd Annual Institute on Securities Regulation (November 8, 2001). Available at <http://www.sec.gov/news/speech/spch520.htm>

determining if compensation is reasonable, and whether this will be determined on a per-member basis. Finally, the proposed rule does not make clear what the filing consequences (i.e., delay, disqualification) are for individual members with conflicts of interest.

Timing – If an offering is to take place more than 15 business days after effectiveness of the shelf registration statement, the proposed rule requires that a full filing be made at least 15 business days prior to the offering. A 15 business-day period for NASD review prior to the offering is simply too long and will significantly impair access to the market for seasoned issuers.

Also, we have noted that a syndicate member may be invited into the syndicate after the SEC filing. If an offering is scheduled to commence prior to the 15th day after effectiveness, the rule would technically require this member to file with the NASD before it is asked to participate. The timing aspects of the rule will thus largely determine who can participate in the syndicate and thus negatively impact competition among underwriters.

Conditions for Use of Notice Filing – SIA applauds the introduction of the concept of notice filing to the review process. For eligible issuers, notice filing offers the promise of predictability, speed and efficiency to the process of accessing capital markets. Nevertheless, the eligibility requirements are too restrictive and, as a result, few if any seasoned issuers will actually benefit.

For example, the proposed rule would require full review of a member's participation if the member has a conflict of interest subject to rule 2720. There is no explanation for what purpose this restriction would serve. Rule 2720 already provides the remedy - QIU pricing – that follows from the disclosure of a conflict. Denying the disclosing member the benefit of notice filing would offer no additional investor protection benefit.

Moreover, the proposed rule would disqualify from notice filing those members that exceed 8% *and* those members that have received unregistered securities within the previous 180 days. The inclusion of both conditions seems unnecessary and arbitrary. Because the NASD has already proposed to count unregistered securities as compensation, the amount of securities received would presumably count toward the 8% limit imposed on users of the notice filing procedure. Therefore, receipt of such compensation should not be a reason in and of itself to disqualify a member from notice filing.

In a large syndicate, it may not be possible to review each underwriter in a timely manner to determine whether it, or any of its affiliates, has received unregistered securities within 180 days. This will further slow issuer access to the capital markets.

Finally, the requirement that a member who has received unregistered securities within 180 days file for a full review 15 business days before an offering will put the

member at a competitive disadvantage to other underwriters competing to participate in a shelf offering. As a general matter, any rule specifying a waiting period of a minimum number of days works counter to the goal of efficient access to markets. In the shelf context, 15 business days is an eternity. The backward-looking nature of this rule will result in arbitrary disqualifications of underwriters, and prevent them from competing on the basis of merit, price, and service.

New Market Transaction Exemption (MTE) – Although well-intentioned, the conditions necessary for this exemption are so restrictive and costly as to make it unavailable to most issuers. For example, one condition is predicated on compensation not exceeding the NASD’s guidelines for mark-ups on secondary market transactions (NASD IM-2440). NASD states that this proposed exemption is designed “to facilitate sales of securities from a shelf registration that are more similar to ordinary trading than to a public offering.” Introducing this guideline into dealings between issuer and underwriter would blur the policy considerations underlying the rules for secondary market trades and corporation financing transactions. Shelf offerings must still be treated as offerings governed by the Securities Act, and not as secondary market transactions. There is no exemption from the Corporation Financing Rule that would be worth the cost of having them so treated. The only limitation on compensation should be the 8% limit (as determined by the NASD), which permits compensation to be in any form not deemed to be unreasonable under Rule 2710 (c)(6). This clear standard for compensation has served underwriters well by reducing the legal and regulatory risk associated with committing capital. This risk would become unmanageable if compensation were determined using the retroactively focused, facts-and-circumstances analysis of the markup rule.

In addition, subjecting certain transactions to the 5% guideline of IM-2440 would make the exemption ineligible for most underwriters engaged in at-the-market offerings. Compensation arrangements for such transactions reflect the risk element involved and may, therefore, exceed the mark-up guideline under certain market conditions. Underwriter compensation is a matter of negotiation between an informed issuer and the underwriter. In all cases, the issuer is informed of the amount of compensation the underwriter will receive for his risk and service prior to the transaction.

Finally, the reference to the mark-up policy contradicts the first condition of the exemption, which by reference to condition (1) of paragraph (b) (10)(B) limits compensation to 8%.

Fees – Under the proposed fee structure, each member would pay a fee on each filing; however, there is no maximum fee proposed for a registration statement as there is today. Since additional costs would create new impediments to capital-raising, an explanation of the reasons warranting such an increase in costs, if intended, ought to be provided.

Conclusion

SIA recognizes the difficulty in carving out a segment of issuers and issues for whom the normal review process would no longer apply. On the other hand, each stroke of reform cannot be so encumbered with qualifications and exceptions as to render the whole effort moot. Our joint task should be to identify those categories of transactions for whom real deregulation is appropriate and to confidently provide it with as few restrictions as possible. As securities reform efforts progress, it would be incongruous if NASD rules were slowing down access to the capital markets just as new Securities Act rules were eliminating roadblocks for qualified issuers. We welcome the opportunity to meet with you at your convenience to discuss how we can achieve our mutual goals.

Very truly yours,

Kenneth Josselyn
Chairman, SIA Capital Markets Committee