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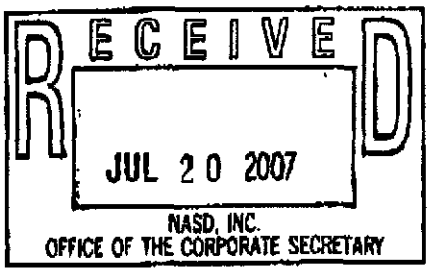

VIA ELECTRONIC MAIL

July 19, 2007

Barbara Z. Sweeney
Office of the Corporate Secretary
NASD
1735 K Street, NW
Washington, D.C. 20006-1506

RE: Proposed Rule 2721

Dear Ms. Sweeney:

In June 2007, the NASD issued Notice to Members 07-27 (NTM 07-27) which proposes Rule 2721 in an effort to lessen potential abuses on the part of NASD member firms or their controlling entities in the area of private placements. If adopted, this rule would impose upon the member firms or their controlling entities, various disclosure requirements, filing requirements, and restrictions on the use of proceeds from private offerings performed pursuant to the exemptions provided under SEC Regulation D. We have provided three alternative viewpoints as part of our comments to the proposed rule in an effort to allow the NASD to consider the rule from as many different perspectives as possible. In part I, we briefly discuss Congress' original intent in passing Regulation D. In part II, we provide our comments in support of particular additions to the proposed rule. Hereafter, in Section III of this letter, we provide comments in support of making amendments or deletions to the rule. In part IV, we provide the arguments in favor of not adopting the rule at the current time. We sincerely hope that these comments prove helpful in the NASD's efforts to improve upon its overall rulemaking for the benefit of its member firms and the protection of investors.

I. Introduction

Congress's original intent in 1982 for Rule 504 was to set aside a clear and workable exemption for small issuers to be regulated by state blue sky requirements, but by the same token, to be subjected to federal anti-fraud provisions and civil liability provisions. Similarly, Rules 505 and 506 under Regulation D were created by Congress to provide smaller or startup entities easier and cheaper access to often much needed

result of Rule 2721 if it becomes adopted in its current state. The proposed rule can and should be more narrowly tailored and can be revised to better address the specific concerns of the NASD as well as to better balance the interests of investors as protected by the NASD with the original intent of Regulation D.

II. Comments In Support of Additions to the Proposed Rule

A. Proposed Rule 2721 Lacks Any Protections for Member Firms or Control Entities in the area of Confidentiality

One of the many purposes served by a private placement memorandum ("PPM") is to inform the investor of the reasons to purchase a security as well as all of the risks associated with the purchase of the security (i.e., the reasons to not purchase the security). Many of the reasons offered in PPMs for the purchase of a security in a private offering include the existence of highly confidential and unique business strategies, competitive advantages, trade secrets, patents involving unique technology giving the member firm or a control entity a powerful edge over potential investors, and other similar highly confidential information. Proposed Rule 2721 offers no protections for confidentiality or ability to protect such information from the eyes and ears of individuals within and without the NASD, many of which come from and go to larger member firms that would greatly value information about such confidential matters easily derived from most PPMs. Therefore, in the case that Rule 2721 in some form is adopted, there should be added to any final Rule 2721, the right on the part of the member firm or its control entity to make and enforce as confidential and the right to black out confidential portions of the PPM prior to providing this confidential information to the NASD.

B. The Proposed Rule Lacks an Exemption Involving Prior Issued Convertible Debt or Other Classes of Securities.

Proposed Rule 2721, Subsection (e)(8) provides for an exemption in the case of securities issued in stock splits and restructuring transactions. However, there is no mention of transactions involving conversions from one class of securities (e.g., bonds or preferred stock) to another class of securities (e.g., common stock). Similar to stock splits and restructuring transactions, stock conversions involve non-cash transactions and the conversions are executed by an already existing investor that wishes to swap one type of security for another without the need for additional consideration or investments on the part of the investor. Therefore, stock conversions should also be included under the exemptions listed in Subsection (e)(8).

III. Comments in Support of Modifications or Deletions to the Proposed Rule

A. Proposed Rule 2721 Subsection (d) Should be Eliminated

Subsection (d) of proposed Rule 2721 should be eliminated as it arbitrarily sets a figure in the amount of eighty-five percent (85%) as the baseline under which a member or even its control entity cannot fall below when making decisions on how to utilize

offering proceeds. The use of proceeds section of most PPM's describes the anticipated or expected use of proceeds rather than the guaranteed or definite use of proceeds. The reason for any PPM to not be required to conform or even substantially conform to the described uses of the offering proceeds is to allow maximum flexibility to management due to the nature of smaller or startup businesses. The future capital requirements and use of any smaller company is highly speculative and uncertain. Any restrictions on the use of proceeds from an offering and on the parties responsible for running the day to day business affairs of the company will harm the company's management and a board's ability to run its business operations as it sees fit, which in turn, will harm the interests of shareholders. The NASD is not in any position to see the future, as a divine oracle or otherwise, of any smaller member company or control entity and therefore should not attempt to arbitrarily confine a smaller company management's discretionary use of offering proceeds to only 15% of the proceeds raised from any private offering.

Further, the 85% restriction on proceeds proposed under Subsection (d) does not eliminate the risk of abuse targeted by this restriction, namely that the proceeds are somehow not used by management in a way that serves the best interests of the company, *be it in the form of promoting either short-term or long-term profitability.* This perhaps being the unspoken but implied target of this Subsection (d), a more specific but separate rule can be proposed that requires that all proceeds obtained through a member's private offering be utilized in a manner that serves the best interests of the Company and all of its shareholders. However, a more specific rule may not be necessary due to such abuses usually being successfully resolved through private shareholder actions or derivative actions against organizations or their management. The NASD is therefore not needed to police such private shareholder actions when the courts have taken on this role successfully for many years at the request of private shareholders.

B. Rule 2721, Subsection (b), Should be Removed from the Proposed Rule Because A Notice Filing Requirement Does Not Correct the Types of Alleged Abuses Targeted by the NASD.

Under proposed Rule 2721, Subsection (b), no member or control entity may offer or sell any security in a Member Private Offering unless the PPM has been filed with the NASD at or prior to the time of the first placement of any such offering with an investor. Yet, under paragraph (c) of NTM 07-27, the NASD states that unlike filings under Rules 2710, 2720, and 2810, a member could begin offering MPO securities immediately after filing the PPM. This appears to equate to a new requirement for a notice filing rather than a prior review and approval by the NASD. Such notice filings already exist at the state level in many states. Further, a notice filing only guarantees that a PPM is created and sent to the NASD to put them on notice of a private offering. This notice can be successfully made with merely a requirement that a Form D be filed concurrently with the NASD. However, a notice filing does not guarantee that any PPM will actually be timely distributed to the investor or that the PPM will be ultimately provided at all. This notice filing also does not guarantee that the PPM will even contain adequate information or disclosures desired by the NASD, as the NASD will not have an opportunity to review and approve the PPM prior to the PPM's distribution by the member firm or control

entity. Therefore, the notice filing requirement found under Subsection (b) should remain the subject of state regulatory agencies and should be removed from the text of the proposed rule with the focus of any remaining rule being that of providing guidelines for a PPM that is presented to investors by or through a member firm. Alternatively, a concurrent filing of Form D with the NASD could suffice for this notice filing of a securities offering by a member firm or through a member firm by a control entity.

C. The Requirement that a Member's "Control Entity" Be Subject to Rule 2721 Should Be Deleted From the Rule

An attempt to require the member firm's "control entity" to come under the purview of NASD regulation is an attempt to create regulatory responsibility that has not previously existed. If the member firm has not participated in the offering in any manner and the only connection between the member and the parent is one of ownership, the NASD does not currently have clear or proper authority to affect or regulate the business conduct of such a controlling entity. A control entity is an entirely separate legal entity that should be run independently of the member. Therefore, no NASD jurisdiction should be proper in this case over a control entity.

However, if the NASD remains committed to including a control entity feature within any final rule, there should be an inclusion of a control entity only in the case that the control entity issues securities under all of the following circumstances: 1) there is the issuance of securities to customers of the member firm; 2) the securities are issued through the member firm or its representatives, and 3) there are underwriting or brokerage fees paid to the member firm or its representatives for the sale of any of the securities being offered. These circumstances, when combined, would create a sufficient nexus to warrant further regulatory interest on the part of the NASD towards a control entity.

IV. Comments Supporting That the Rule Not Be Adopted

A. Currently Adequate Protections for Investors Possibly Subject to Abuses Discussed Under NTM 07-27

The NASD in its NTM 07-27 stated that the issues it is attempting to address through its proposed rule 2721 are as follows:

- Misleading, incorrect, or selective disclosures in PPMs;
- Omissions and misrepresentations regarding selling compensation and the use of offering proceeds; and
- A failure to provide PPMs ("Private Placement Memorandums") to investors.

NASD Conduct Rules 2110, 2120, and 2310 along with Section 5 of the Securities Act of 1933, Section 17(a) of the Securities Act of 1933, Section 10(b) of the Securities Act of 1934, SEC Rule 10b-5, and common law in the areas of negligence, breach of contract, and fraud have proven over time to be adequate to address problems that can arise with

member or nonmember "control entities" improperly affecting the issuance of private offerings to their customers or non-customers in the case of a control entity. Additionally, the broker's duty of fair dealing and duty to disclose risks and conflicts of interest to the customer provide even greater protections for brokerage customers. All of these areas of protection and recovery for investors provide adequate redress to investors that are harmed by the conduct of member firms or their control entities. As a result, additional protection that could be afforded under Rule 2721 would be duplicative and would simply add an unnecessary load to an already significantly large and complex assortment of previously effective and developed laws. Such additional regulation would also add to the already overburdened infrastructure of the NASD.

B. Unfounded Assumptions Not Based Upon Sufficient Evidence

The NASD appears to be making the assumption that NASD members require more oversight that nonmembers when involved with private placements for the member firms or their control entities. This assumption appears to be driving a belief that Rule 2721 will provide more protection for investors than is provided by current regulations and laws. This assumption that NASD Members are more prone to commit abuses than non-members in the area of private offerings, and thereby warranting disparate treatment from non-members, has not been shown to be based upon any conclusive evidence. Therefore, Rule 2721 may be premature and should only be proposed following accumulation of sufficient evidence that disparate treatment of member firms or control entities is actually required to reduce cases of alleged abuses related to private offerings. Further evidence that adoption of Rule 2721 will in fact be effective in eliminating the possible abuses targeted by the rule should also be performed before considering adoption of any form of Rule 2721.

C. Rule 2721 is Unduly Burdensome on Smaller or Startup Member Firms

The disparate treatment under proposed Rule 2721 unduly burdens the smaller NASD members' ability to raise capital, thereby acting as a form of protection for the larger NASD members from future competition as a result of the larger members not having any need to raise capital through private placements. Therefore, if one cripples the smaller member's ability to raise capital it cripples the smaller member or creates a situation where there are less new members in the future due to the small member's or potential member's inability to raise sufficient funds to pay the legal fees and expenses required to produce an adequate PPM. The overall effect of this rule will be to reduce the number of smaller member firms which is in contravention with the intent of Regulation D. Regulation D has allowed and empowered smaller companies, and smaller members alike, to raise sufficient capital without the incurrence of the prohibitive costs associated with a PPM. It is not larger member firms that need protection from the smaller member firms; it is actually the reverse which is often the case.

D. The Effect of Proposed Rule 2721 May be to Further Restrict Investor's Access to Member Firm Private Offerings

It is probably safe to assume that as a result of Rule 2721 being adopted that many member firms, control entities, and prospective member firms will be unable to incur the expenses associated with the proper preparation of a PPM. This will most likely lead to fewer private placement offerings in the future by member firms, their control entities, and prospective member firms. Reducing the number of private offerings available to the average investor further eliminates the average investors' ability to benefit from the next generation of successful member firms that are fortunate enough to find a public market or even private equity market. The higher returns that often result from private placements are needed more by the average investor than accredited investors, who are by definition already financially secure. Overall, Rule 2721 will have a chilling effect on private placements and will have the effect of continuing to erect more obstacles in front of the average hard-working individual who desires to somehow be enriched through the discovery of a unique private member firm, or control entity, that yields higher returns through someday going public or liquidating through a private sale. Over the last thirty years, some of the most rapidly appreciating stocks sold on the NYSE or NASDAQ were those in the financial services industry, including member firms. These opportunities should continue to be made available to such average investors as a means of creating upward economic mobility for the middle class of America.

Respectfully submitted,
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Dexter B. Johnson