

September 21, 2000

Katherine A. England, Assistant Director
Division of Market Regulation
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-1001

Re: **SR-NASD-00-13, Amendment No. 1**
Disclosure of Values for Direct Participation Program ("DPP") and
Real Estate Investment Trust ("REIT") Securities on
Customer Account Statements

Dear Ms. England:

Pursuant to Rule 19b-4, NASD Regulation, Inc. ("NASD Regulation") is filing Amendment No. 1 to the above-numbered rule filing to respond to comments received on the proposed rule change to amend Rule 2340 ("Rule") that was published for comment in Securities Exchange Act Release No. 43698, 65 F.R. 24523 (April 26, 2000). Also enclosed is a 3-1/2" disk containing this submission in Microsoft Word 7.0.

Two comments were received on the proposed rule change from Merrill Lynch Pierce Fenner and Smith ("Merrill") by letter dated June 2, 2000 and from the Investment Program Association ("IPA") by letter dated June 30, 2000. Copies of the letters are attached hereto.

Reliability of the Estimated Value

Merrill argues that the requirement under proposed paragraph (b)(2)(A) of the Rule that a member make an affirmative determination regarding the reliability of each externally provided estimated value imposes an unreasonable and inappropriate obligation on the member. Merrill requests that the rule language be revised to "prohibit" a member from providing an estimated value for a DPP or REIT security that it "believes" is inaccurate. Merrill recommends that NASD Regulation amend the Rule to incorporate a prior version of the provision previously proposed by NASD Regulation in SR-NASD-97-12 and published for comment by the Securities and Exchange Commission ("SEC") in Securities Act Release No. 38451 (March 27, 1997), which proposal was withdrawn from the SEC upon filing of SR-NASD-00-13.

The IPA states that it supports Merrill's comment, but expresses concern that members may justify their failure to include an estimated value on an account statement by claiming that an action since the date of the annual report makes the valuation information in the annual report inaccurate. The IPA recommends that the Rule be amended to require that a member must include on customer account statements any estimated value published by the general partner or trustee in an 8K or 10Q filing subsequent to the release of the annual report.

NASD Regulation does not, however, share the concern of the IPA regarding the possibility that members may rely inappropriately on this provision to avoid compliance with the requirement to include an estimated value on account statements. Once the member's obligation is triggered by publication of a per share estimated value in an annual report, the Rule would require that the member include in customer account statements either the value published in the annual report, or a value obtained from another third-party source, or a value developed by the member. Thus, a member would be required to develop a valuation to include on customer account statements if the member determines that the values available from the annual report and third-party sources are inaccurate.

NASD Regulation did not intend that the application of paragraph (b)(2)(A) would impose any obligation on members to guarantee the accuracy of an estimated value obtained from a third-party source.¹ In considering Merrill's comment, we believe that both the proposed rule language and the replacement language recommended by Merrill could be interpreted as imposing such an obligation and, thereby, exposing the member to legal liability for inaccurate valuations from third-party sources.

The purpose of the provision in question was to ensure that a member is not forced to include an estimated value from a third-party source on customer account statements that the member believes to be inaccurate at the time of use. In response to these comments, NASD Regulation proposes to amend the proposed rule change to include as new paragraph (b)(4) a separate provision that would permit a member to refrain from including “. . . a per share estimated value for a DPP or REIT security on an account statement if the member can demonstrate the value was inaccurate as of the date of the valuation or is no longer accurate as a result of a material change in the operations or assets of the program or trust.” Paragraph (b)(2)(A) would be deleted and paragraph (b)(4) would be renumbered (b)(5).

Attached is the text of the proposed rule change published by the SEC with the text treated

¹ A member would, of course, be liable for any material inaccuracy of an internally generated per share estimated value.

Katherine A. England, Esq.

September 21, 2000

Page No. 3

as if adopted and the amendments proposed herein marked by underlines for additions and brackets for deletions.

If you have any questions regarding this submission, please contact Suzanne E. Rothwell, Chief Counsel, Corporate Financing, NASD Regulation, Inc., at (202) 974-2747, fax number (202) 974-2732, e-mail rothwels@nasd.com.

Very truly yours,

Suzanne E. Rothwell
Chief Counsel, Corporate Financing

Attachment

ATTACHMENT

TEXT OF PROPOSED RULE CHANGE AS IF ADOPTED WITH PROPOSED CHANGES MARKED

Rule 2340 Customer Account Statements

(a) General

Each general securities member shall, with a frequency of not less than once every calendar quarter, send a statement of account (“account statement”) containing a description of any securities positions, money balances, or account activity to each customer whose account had a security position, money balance or account activity during the period since the last such statement was sent to the customer.

(b) DPP/REIT Securities

(1)(A) Voluntary Estimated Value

A general securities member may provide a per share estimated value for a direct participation program (“DPP”) or real estate investment trust (“REIT”) security on an account statement, provided the member meets the conditions of paragraphs (b)(2) and (3) below.

(B) Mandatory Estimated Value

If the annual report of a DPP or REIT includes a per share estimated value for a DPP or REIT security that is held in the customer’s account or included on the customer’s account statement, a general securities member must include an estimated value from the annual report, an independent valuation service, or any

other source, in the first account statement issued by the member thereafter, provided that the member meets the conditions of paragraphs (b)(2) and (3) below.

(2) A member may only provide a per share estimated value for a DPP or REIT security on an account statement if [:]

[(A) after considering any relevant information about the market and the particular investment in its possession, the member has no reason to believe that the estimated value is inaccurate; and

(B)] the estimated value has been developed from data that is as of a date no more than 18 months prior to the date that the statement is issued.

(3) If an account statement provides an estimated value for a DPP or REIT security, it must include:

(A) a brief description of the estimated value, its source, and the method by which it was developed; and

(B) disclosure that DPP or REIT securities are generally illiquid, and that the estimated value may not be realized when the investor seeks to liquidate the security.

(4) Notwithstanding the requirement in paragraph (b)(1)(B), a member may refrain from including a per share estimated value for a DPP or REIT security on an account statement if the member can demonstrate the value was inaccurate as of the date of the valuation or is no longer accurate as a result of a material change in the operations or assets of the program or trust.

(5) If an account statement does not provide an estimated value for a DPP or REIT security, it must include disclosure that:

- (A) DPP or REIT securities are generally illiquid;
- (B) the value of the security will be different than its purchase price; and
- (C) if applicable, that accurate valuation information is not available.

(c) **Definitions**

For purposes of this Rule, the following terms will have the stated meanings:

(1) “account activity” includes, but is not limited to, purchases, sales, interest credits or debits, charges or credits, dividend payments, transfer activity, securities receipts or deliveries, and/or journal entries relating to securities or funds in the possession or control of the member.

(2) a “general securities member” refers to any member which conducts a general securities business and is required to calculate its net capital pursuant to the provisions of SEC Rule 15c3-1(a), except for paragraph (a)(2) and (a)(3). Notwithstanding the foregoing definition, a member which does not carry customer accounts and does not hold customer funds and securities is exempt from the provisions of this section.

(3) “direct participation program” or “direct participation program security” refers to the publicly issued equity securities of a direct participation program as defined in Rule 2810 (including limited liability companies), but does not include securities on deposit in a registered securities depository and settled regular way, securities listed on a national securities exchange or The Nasdaq Stock Market, or any program registered as a commodity pool with the Commodities Futures Trading Commission.

(4) “real estate investment trust” or “real estate investment trust security” refers to the publicly issued equity securities of a real estate investment trust as defined in Section 856 of the Internal Revenue Code, but does not include securities on deposit in a registered securities depository and settled regular way or securities listed on a national securities exchange or The Nasdaq Stock Market.

(5) “annual report” means the most recent annual report of the DPP or REIT distributed to investors pursuant Section 13(a) of the Act.

(d) Exemptions

Pursuant to the Rule 9600 Series, the Association may exempt any member from the provisions of this Rule for good cause shown.

2710. Corporate Financing Rule – Underwriting Terms and Arrangements

* * *

(c) Underwriting Compensation and Arrangements

* * *

(6) Unreasonable Terms and Arrangements

* * *

(B) Without limiting the foregoing, the following terms and arrangements, when proposed in connection with the distribution of a public offering of securities, shall be unfair and unreasonable:

* * *

(xv)² for a member or person associated with a member to participate in a public offering of real estate investment trust securities, as defined in Rule 2340(c)(4), unless the trustee will disclose in each annual report distributed to investors pursuant Section 13(a) of the Act a per share estimated value of the trust securities, the method by which it was developed, and the date of the data used to develop the estimated value.

* * *

Rule 2810. Direct Participation Programs

* * *

(b) Requirements

* * *

(5) Valuation for Customer Account Statements

No member may participate in a public offering of direct participation program securities unless:

(A) the general partner or sponsor of the program will disclose in each annual report distributed to investors pursuant Section 13(a) of the Act a per share estimated value of the direct participation program securities, the method by which it was developed, and the date of the data used to develop the estimated value.

² The NASD has on file with the SEC rule filing SR-NASD-00-04, that would amend paragraph (c)(6)(B). If the amendments are approved, new paragraph (c)(B)(xv) would be renumbered.