

Regulatory Notice 15-02

Amended Rule Text

New language is underlined; deletions are in brackets.

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NASD Rule

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2300. TRANSACTIONS WITH CUSTOMERS

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2340. Customer Account Statements

(a) through (b) No Change.

(c) DPP[/ and Unlisted 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 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 must 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.]

A general securities member shall include in a customer account statement a per share estimated value of a direct participation program (DPP) or unlisted real estate investment trust (REIT) security, developed in a manner reasonably designed to ensure that the per share estimated value is reliable, and the disclosures in paragraph (c)(2) as applicable.

(1) For purposes of this paragraph (c), a per share estimated value for a DPP or REIT security will be deemed to have been developed in a manner reasonably designed to ensure that it is reliable if the member uses one of the following per share estimated value methodologies.

(A) Net Investment

At any time before 150 days following the second anniversary of breaking escrow, the member may include a per share estimated value reflecting the “net investment” disclosed in the issuer’s most recent periodic or current report (“Issuer Report”). “Net investment” shall be based on the “amount available for investment” percentage in the “Estimated Use of Proceeds” section of the offering prospectus or, where “amount available for investment” is not provided, another equivalent disclosure that reflects the estimated percentage deduction from the aggregate dollar amount of securities registered for sale to the public of sales commissions, dealer manager fees, and estimated issuer offering and organization expenses. When the issuer provides a range of amounts available for investment, the member may use the maximum offering percentage unless the member has reason to believe that such percentage

is unreliable, in which case the member shall use the minimum offering percentage.

(B) Appraised Value

At any time, the member may include a per share estimated value reflecting an appraised valuation disclosed in the Issuer Report, which, in the case of DPPs subject to the Investment Company Act of 1940 (“1940 Act”), shall be consistent with the valuation requirements of the 1940 Act and the rules thereunder or, in the case of all other DPPs and REITs, shall be:

(i) based on valuations of the assets and liabilities of the DPP or REIT performed at least annually, by, or with the material assistance or confirmation of, a third-party valuation expert or service; and

(ii) derived from a methodology that conforms to standard industry practice.

(2) Disclosures

(A) An account statement that provides a “net investment” per share estimated value for a DPP or REIT security under paragraph (c)(1)(A) shall disclose, if applicable, prominently and in proximity to disclosure of distributions and the per share estimated value the following statements: “IMPORTANT – Part of your distribution includes a return of capital. Any distribution that represents a return of capital reduces the estimated per share value shown on your account statement.”

(B) Any account statement that provides a per share estimated value for a DPP or REIT security shall disclose that the DPP or REIT securities are not listed on a national securities exchange, are generally illiquid and that, even if a customer is able to sell the securities, the price received may be less than the per share estimated value provided in the account statement.

(d) Definitions

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

(1) through (2) No Change.

(3) “direct participation program” or “direct participation program security” refers to the publicly issued equity securities of a direct participation program as defined in FINRA Rule 2310[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 any program registered as a commodity pool with the [Commodities] Commodity 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.

(5) through (6) No Change.

(e) No Change.

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FINRA RULES

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2300. SPECIAL PRODUCTS

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2310. Direct Participation Programs

(a) No Change.

(b) Requirements

(1) through (4) No Change.

(5) Valuation for Customer Account Statements

[No] A member shall not [may] participate in a public offering of the securities of a direct participation program (DPP) that is not subject to the requirements of the Investment Company Act of 1940 or of a REIT [securities] unless the issuer [general partner or sponsor] of the [program] DPP or REIT has agreed to disclose: [will disclose in each annual report distributed to investors pursuant to Section 13(a) of the Exchange 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.]

(A) a per share estimated value of the DPP or REIT security, developed in a manner reasonably designed to ensure it is reliable, in the DPP or REIT periodic reports filed pursuant to Section 13(a) or 15(d) of the Exchange Act;

(B) an explanation of the method by which the per share estimated value was developed;

(C) the date of the valuation; and

(D) in a periodic or current report filed pursuant to Section 13(a) or 15(d) of the Exchange Act within 150 days following the second anniversary of breaking escrow and in each annual report thereafter, a per share estimated value:

(i) based on valuations of the assets and liabilities of the DPP or REIT performed at least annually, by, or with the material assistance or confirmation of, a third-party valuation expert or service;

(ii) derived from a methodology that conforms to standard industry practice; and

(iii) accompanied by a written opinion or report by the issuer, delivered at least annually, that explains the scope of the review, the methodology used to develop the valuation or valuations, and the basis for the value or values reported.

(6) No Change.

(c) through (d) No Change.

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5100. SECURITIES OFFERINGS, UNDERWRITING AND COMPENSATION

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5110. Corporate Financing Rule — Underwriting Terms and Arrangements

(a) through (e) No Change.

(f) Unreasonable Terms and Arrangements

(1) No Change.

(2) Prohibited Arrangements

Without limiting the foregoing, the following terms and arrangements, when proposed in connection with a public offering of securities, shall be unfair and unreasonable.

(A) through (K) No Change.

[(L) For a member or person associated with a member to participate in a public offering of real estate investment trust securities, as defined in NASD Rule 2340(c)(4), unless the trustee will disclose in each annual report distributed to investors pursuant to Section 13(a) of the Exchange 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.]

(g) through (i) No Change.

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