

Patrice M. Gliniecki  
Vice President and  
Acting General Counsel

Direct: (202) 728-8014  
Fax: (202) 728-8264

March 1, 2002

Ms. Katherine A. England  
Assistant Director  
Division of Market Regulation  
U.S. Securities and Exchange Commission  
450 5<sup>th</sup> Street, N.W.  
Washington, D.C. 20549-1001

**Re: Amendment No. 1 to File No. SR-NASD-2001-46; Electronic Filings  
With the Corporate Financing Department**

Dear Ms. England:

The National Association of Securities Dealers, Inc. (“NASD” or “Association”), through its wholly owned subsidiary NASD Regulation, Inc. (“NASD Regulation”), hereby responds to the comment letters received by the Securities and Exchange Commission (“Commission” or “SEC”) in response to the publication in the *Federal Register* of Notice of Filing of SR-NASD-2001-46,<sup>1</sup> and submits Amendment No. 1 to this filing as described below and as reflected in the proposed rule language attached as Exhibit 1.<sup>2</sup> The amendment clarifies that the information to be submitted through the Association’s electronic filing system is only information that is otherwise required to be filed pursuant to Rule 2710.

**Background**

On August 6, 2001, NASD Regulation, on behalf of the NASD, filed with the Commission proposed amendments to NASD Rule 2710 regarding electronic filings with NASD Regulation’s Corporate Financing Department (“Department”). NASD Regulation is proposing to amend Rule 2710 to: (1) require that members file certain information on offerings subject to Rules 2710, 2720, and 2810 through the Department’s electronic filing system, the Corporate Offerings Business Regulatory Analysis System (“COBRA”); (2) provide that all public offering documents that are filed with the Commission through its Electronic Data Gathering and Retrieval System (“EDGAR”) will be treated as filed with the Association; and (3) reduce the number of offering documents that are required to be

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<sup>1</sup> See Securities Exchange Act Release No. 44720 (Aug. 17, 2001), 66 FR 44657 (Aug. 24, 2001).

<sup>2</sup> Additionally, attached as Exhibit 2 is the full text of the proposed rule change marked to indicate changes from the text of the proposed rule change that was submitted as part of the preceding filing.

filed with the Association for members that file manually with the Commission instead of electronically through EDGAR.

The Commission published the proposed rule change for comment in the *Federal Register* on August 24, 2001. The public comment period announced in the *Federal Register* expired on September 14, 2001. The Commission received three comment letters on the proposed rule change.<sup>3</sup> The comments sent to the Commission and NASD Regulation's responses are summarized below.

### **Issues Raised in Comment Letters**

#### Increased Costs and Less Efficiency

The Commenters are concerned that the mandatory use of COBRA generally will be more costly and less efficient than the current process of manual filings. NASD Regulation does not believe that these concerns are justified.

NASD Regulation believes that COBRA filing reduces overall costs and enhances the efficiency of the Department's operations in several important ways. Electronic filing eliminates the need for the Department to handle and process thousands of packages that otherwise would be sent through the U.S. Postal Service or other couriers. Additionally, direct electronic filing into COBRA eliminates the need for analysts to input data from paper filings into COBRA. Electronic filing also mitigates against the possibility that paper records will be lost, such as in the event of a catastrophe. Further, COBRA eliminates the need for members to file registration statements with the Department if they have been filed with the SEC using EDGAR. Filers simply need to provide the Department with the EDGAR accession number in the COBRA Basic Information. This feature reduces members' printing and delivery expenses. For these reasons, NASD Regulation has emphasized that members can expect to receive a speedier review of their electronic filings under COBRA.

For over four years, the Department has worked with the legal community and our members to ensure that COBRA is as user-friendly and efficient as possible. Three staff members are available to train members and their counsel on using the system and assisting filers who are unfamiliar with the system with navigation and information reporting requirements. We have upgraded the system to make it even more user-friendly and efficient. Most notably is the development of COBRADesk as a "web-based"

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<sup>3</sup> Letter from Edward M. Alterman, Esq., Fried, Frank, Harris, Shriver & Jacobson to Jonathan G. Katz, Secretary, SEC, dated September 24, 2001 ("Fried"); Letter from Mark T. Lab, Esq., Simpson Thacher & Bartlett to Jonathan G. Katz, Secretary, SEC, dated October 1, 2001 ("Simpson"); Letter from Martin R. Miller, Esq., Willkie Farr & Gallagher to Jonathan G. Katz, Secretary, SEC, dated October 4, 2001 ("Willkie") (collectively referred to as the "Commenters").

interface. We are currently installing additional system upgrades that respond to users' comments on ways to improve the system. The Department and its vendor, Dealogic,<sup>4</sup> are committed to making system improvements that are necessary to address filer comments and technological advances.

Willkie stated that there would be no need to make COBRA mandatory if it really saved costs. Presumably, Willkie is implying that filers would voluntarily use COBRA if it were less costly than the current system. NASD Regulation, however, does not agree with this assertion. Paper filings slow the review process for all filers because the Department must maintain and dedicate resources to redundant and inefficient paper filing procedures. Consequently, many of the benefits of the electronic system will not be realized unless all filers use it.

Fried stated that electronic filings in the case of EDGAR are related to the fact that such documents are made publicly available. By contrast, filings with the Department are confidential. Fried argues, therefore, that there is no basis to require electronic filings with the Department. NASD Regulation does not believe that electronic filings should only be mandated when the goal of the system is public dissemination. As noted in the notice of proposed rulemaking, there are many efficiencies in having all filings made with the Department electronically. In addition, we note that the SEC recently proposed to require certain confidential filings to be made through EDGAR.<sup>5</sup>

#### Information Required by the Electronic Filing System

All of the Commenters objected to proposed Rule 2710(b)(6)(A)(vii), which would require a person filing information through COBRA to file "any other information required by the Association's electronic filing system." NASD Regulation intended the provision to require all information required under Rule 2710 to be filed exclusively through COBRA. NASD Regulation recognizes that, as drafted, the provision could be construed to allow the NASD to change the substance of what is required by Rule 2710 simply by making a program change to COBRA. To address this concern, NASD Regulation is rephrasing proposed Rule 2710 (b)(6)(A)(vii) to state "any other information required to be filed under this Rule," to make clear that the electronic filing requirements are based upon the Rule and not the electronic filing interface.

#### Y/N Boxes

The Commenters expressed concern with the feature in COBRA that requires filers to answer "yes" or "no" to questions requiring compliance with various provisions of

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<sup>4</sup> Dealogic (formerly CommScan, L.L.C.) is the third-party vendor that designed and developed COBRADesk in June 1999 as a client application and as a Web application in May 2000.

<sup>5</sup> See Securities Exchange Act Release No. 44868 (Oct. 4, 2001), 66 FR 50744 (Oct. 4, 2001) (Mandated EDGAR Filing for Foreign Issuers; Proposed Rule).

Rules 2710, 2720, or 2810. For instance, Fried and Simpson noted that certain questions may not apply to the types of offerings that are filed with the Department (*e.g.*, a question about compliance with Rule 2810 when the offering does not involve direct participation program securities).

NASD Regulation believes that the questions serve as reminders to filers as they complete a submission. The COBRA system does not require that these buttons be checked and they are merely intended to be useful reminders of various regulatory requirements for members. Similarly, questions that do not apply to offerings of the type being filed are included so that members can navigate to proper screens on the Web site. We have not received similar complaints from other firms that routinely make electronic filings and, in our view, the yes/no boxes serve as useful reminders to many filers.

### Security

The Commenters raised concerns regarding the security of information filed through COBRA. Fried and Simpson argued that no web-based system is entirely safe from unauthorized access and is at least as vulnerable as the United States Government's highest level of security. Willkie noted that it is nearly impossible to guarantee the security of information transmitted on the Internet.

The COBRADesk system has been designed by Dealogic and internally maintained by Electronic Data Systems Corporation ("EDS"). The COBRADesk system is one of many web-based systems designed and built by Dealogic that routinely are used by the financial services industry.

Web COBRADesk security features include: (i) multiple Web server and standby database server to provide scalability and redundancy; (ii) servers housed at secure data center run by EDS; (iii) multiple layers of security including multiple firewalls; (iv) integrated industry-standard Kerberos security; (v) users and firms authenticated at Web and database level; and (vi) all sessions between users and Web server protected by 128-bit encryption. EDS applies patches, runs systems through multiple testing stages, and does penetration testing.

Further, while NASD Regulation recognizes that the security of information sent over the Internet is of critical importance, we note that the information filed through COBRADesk tends to be less confidential and proprietary than other information members routinely sent over the Internet, using systems that are designed by Dealogic. Moreover, over 200 members currently are sending or have sent information using COBRADesk,<sup>6</sup> and the security of that information has not raised any concerns, prior to the comment letters received in response to the proposed rule change.

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<sup>6</sup> Thirty percent of the filings the Department received in 2001 were filed electronically.

### Required Information

The Commenters also raised concerns regarding the provision that the system will not accept filings without certain specified information being provided, some of which typically is not known at the time of the initial filing with the SEC.<sup>7</sup> For instance, Fried stated that the system will not accept a filing for an equity offering without the actual number of shares and price per share, numbers that are rarely known at the time of the initial SEC filing. Fried and Willkie argued that filers will be forced to insert incomplete or unreliable information merely to make a filing within the time required. Fried argued that the practitioner submitting the filing is forced to invent numbers and qualify them with general language disclaiming the accuracy of that information. Willkie added that filers would be forced to include a disclaimer on COBRA that the information was merely a “best guess” to be able to comply with the timing requirements of Rule 2710. Fried stated that COBRA demands the stock symbol, the information on affiliations and associations between the issuer and the underwriters and related persons, the SEC accession number, and a detailed analysis of the terms of the underwriting documents. Fried argued that the only viable alternative to providing the required information will be to provide unreliable or estimated information and provide a disclaimer in the appropriate drop down box.

NASD Regulation received the same or similar comments in connection with the proposed amendments to Rule 2710 that are pending at the SEC<sup>8</sup> and during other meetings with members and their counsel to discuss process improvements and opportunities to improve efficiency and fairness in the filing system. The proposed amendments to Rule 2710 include provisions that are intended to decrease the amount of information required to be filed with the NASD, where appropriate, particularly with regard to NASD association and affiliation information. NASD Regulation notes, however, that electronic filing does not require any more or less information to be filed initially than the Department requires in connection with paper filings.

Specifically, COBRA will accept filings without certain information being provided. There are five required fields in the system: (i) the filer’s E-mail address;<sup>9</sup> (ii) distribution method;<sup>10</sup> (iii) accession number;<sup>11</sup> (iv) compensation information;<sup>12</sup> and (v) the

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<sup>7</sup> Pursuant to Rule 2710 (b)(4), the filing must be submitted to the Department no later than one business day after the filing of any such document with the SEC.

<sup>8</sup> See Securities Exchange Act Release No. 42619 (Apr. 4, 2000), 65 FR 19409 (Apr. 11, 2000) (Notice of Filing of SR-NASD-2000-04).

<sup>9</sup> The filer’s E-mail address allows the Department to communicate with the filer.

<sup>10</sup> The information on distribution method is used to determine the amount of risk to be assumed by the participating members. The Department processes that information to calculate the maximum allowable compensation that a member may receive.

<sup>11</sup> The SEC accession number allows the staff a direct link to the documents through EDGAR.

number and value of the securities proposed to be offered.<sup>13</sup> The stock symbol, the information regarding affiliation and association between the issuer and the underwriters and related persons, and a detailed analysis of the terms and arrangements of the underwriting arrangement are not required fields.

Even in paper-based filings, members are required to submit a good faith estimate of the number of shares and the price per share if they do not have definitive information. NASD Regulation recognizes that this information may change while an offering is marketed.

In 2000, the Department issued a Fax Alert to all law firms filing with the Department, clarifying that their filings must provide the number of shares and price per share in order for it to be reviewed. The purpose of the Fax Alert was to address the disruptions and delays caused by incomplete filings. Incomplete filings (*e.g.*, missing price per share and number of shares) unnecessarily delay the review and clearance of an offering. The Fax Alert recognized that this information might change when an offering is being marketed. The Fax Alert program has been very successful, as evidenced by a decrease in the number of filings without necessary information from 282 for the year ended 2000 to 9 for the period up to and including the quarter ending on September 30, 2001. COBRA facilitates the filing and review process by providing for the electronic filing of changes.

### Browser

Fried stated that COBRA will not work when the filer uses Netscape Navigator, thereby forcing filers to use Internet Explorer. Simpson indicated that it had problems accessing the tutorial using Netscape, and it is concerned that only the most recent version of Internet Explorer works with COBRA.

The browser standards for accessing COBRA are Netscape Navigator 4.6 or greater and Microsoft Internet Explorer 5.0 or greater. Browser upgrades are available free of charge at their respective Web sites. An application designed for the Web must be supported by the current browsers to ensure maximum performance, reliability, flexibility, privacy, and security. COBRA's layout, screens, dialog boxes, scroll bars, list boxes, grids, and links conform to the latest browser versions. It is virtually impossible to develop a system for the Web using the latest Web technology that interfaces with all older browser versions.

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<sup>12</sup> The Department reviews the amount of compensation paid to members in underwriting to ensure that the underwriting terms and arrangements in public offerings in which NASD members participate are fair and reasonable. To comply with this requirement, the Department must calculate the maximum allowable compensation a member may receive in connection with a public offering.

<sup>13</sup> Data on the price per share and the number of shares are needed to determine the offering proceeds, which are used to calculate the filing fee and compensation limits.

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NASD Regulation acknowledges that there are minor problems that complicate -- but do not prevent -- the use of Netscape Navigator when accessing the tutorial or Help screens. These areas will be corrected in the next maintenance release due January 2002. The Department does not believe that these minimal technical requirements are costly or burdensome.

#### Corporate Financing Rule Amendments

Fried and Simpson questioned the practicability and legality of requiring a practitioner to certify compliance with proposed NASD rules that are pending at the SEC. Willkie recommended that this proposed rule change be postponed until such time as the SEC approves other proposed amendments relating to Rule 2710 (File No. SR-NASD-2000-04).

On November 19, 2001, the NASD filed Amendment No. 6 to File No. SR-NASD-2000-04 with the SEC. Due to programming requirements and the time it would take to implement programming changes once the proposed amendments are adopted, when NASD Regulation ported COBRADesk to the Web in April 2001, NASD Regulation included data screens that can accept information regarding transactions that would meet one of the five exceptions proposed in the Rule amendments. COBRA, however, does not require certification of compliance with the proposed amendments, and it is within a filer's discretion whether to include information in the screens designed to capture information regarding transactions that meet the proposed exceptions.

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NASD Regulation believes that the foregoing responds to material issues raised by the Commenters. Accordingly, NASD Regulation encourages the Commission to act as expeditiously as possible in approving the proposed rule change to ensure that the benefits it provides are realized as soon as possible. If the staff of the Commission has any questions, please contact Joseph E. Price, Director, Corporate Financing Department, NASD Regulation, at (240) 386-4642, or Gary L. Goldsholle, Associate General Counsel, NASD Regulation, at (202) 728-8104.

Very truly yours,

Patrice M. Gliniecki  
Vice President and  
Acting General Counsel