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Page 1 of * 68

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
Form 19b-4

File No.* SR - 2014 - * 004
Amendment No. (req. for Amendments *)

Filing by Financial Industry Regulatory Authority

Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial * ☑ Amendment * ☐ Withdrawal ☐

Section 19(b)(2) * ☑ Section 19(b)(3)(A) * ☐ Section 19(b)(3)(B) * ☐

Pilot ☐

Extension of Time Period for Commission Action * ☐

Date Expires *

Rule

- ☐ 19b-4(f)(1)
- ☐ 19b-4(f)(2)
- ☐ 19b-4(f)(3)
- ☐ 19b-4(f)(4)
- ☐ 19b-4(f)(5)
- ☐ 19b-4(f)(6)

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010

Section 806(e)(1) * ☐ Section 806(e)(2) * ☐

Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934

Section 3C(b)(2) * ☐

Exhibit 2 Sent As Paper Document ☐ Exhibit 3 Sent As Paper Document ☐

Description

Provide a brief description of the action (limit 250 characters, required when Initial is checked *).

Proposed Rule Change Relating to Amendments to FINRA Rule 5110 (Corporate Financing Rule—Underwriting Terms and Arrangements)

Contact Information

Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

First Name * Racquel Last Name * Russell

Title * Associate General Counsel

E-mail * Racquel.Russell@finra.org

Telephone * (202) 728-8363 Fax (202) 728-8264

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

Date 01/24/2014

By Alan Lawhead

(Name *)

(Title *)

Vice President and Director - Appellate Group

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

Alan Lawhead, alan.lawhead@finra.org

Required fields are shown with yellow backgrounds and asterisks.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFS website.

Form 19b-4 Information *

Add Remove View

The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

Exhibit 1 - Notice of Proposed Rule Change *

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies *

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO] -xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications

Add Remove View

Exhibit Sent As Paper Document

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Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit 3 - Form, Report, or Questionnaire

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Exhibit Sent As Paper Document

☐

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit 4 - Marked Copies

Add Remove View

The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

Exhibit 5 - Proposed Rule Text

Add Remove View

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

Partial Amendment

Add Remove View

If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of the Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),[1] Financial Industry Regulatory Authority, Inc. ("FINRA") is filing with the Securities and Exchange Commission ("SEC" or "Commission") a proposed rule change to amend FINRA Rule 5110 (Corporate Financing Rule—Underwriting Terms and Arrangements) to expand the circumstances in which termination fees and rights of first refusal are permissible; exempt from the filing requirements certain exchange-traded funds formed as grantor or statutory trusts; and make clarifying, non-substantive changes regarding documents filed through FINRA's electronic filing system.[1]

The text of the proposed rule change is attached as Exhibit 5.

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

At its meeting on February 15, 2012, the FINRA Board of Governors authorized the filing of the proposed rule change with the SEC. No other action by FINRA is necessary for the filing of the proposed rule change.

FINRA will announce the implementation date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date of the proposed rule change will be no later than 120 days following Commission approval.

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[1] The effective date of the electronic filing requirements under Rule 5110 was July 12, 2002. See Notice to Members 02-26.

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

FINRA Rule 5110 (Corporate Financing Rule—Underwriting Terms and Arrangements) (the "Rule"), among other things, regulates underwriting compensation, requires the filing of specified information in connection with public offerings in which members will participate, and prohibits unfair arrangements in connection with public offerings of securities. FINRA proposes to amend the Rule's provisions regarding unfair arrangements to: (1) expand the circumstances under which members and issuers may negotiate termination fees and rights of first refusal ("ROFR"), with specified conditions; (2) exempt from the filing requirements exchange-traded funds formed as grantor or statutory trusts; and (3) codify the electronic filing requirement.

Termination Fees and Rights of First Refusal

Rule 5110(f) (Unreasonable Terms and Arrangements) sets forth terms and arrangements that, when proposed in connection with a public offering of securities, are considered unfair and unreasonable. Rule 5110(f)(2)(D) addresses fees in connection with a public offering of securities that is not completed according to the terms of agreement between the issuer and underwriter ("terminated offering"). Specifically, paragraph (D) generally provides that it is unfair and unreasonable for a member to arrange for the payment of any compensation by an issuer in connection with a terminated offering ("termination fee" or "tail fee"). Paragraph (D) further clarifies that this prohibition does not include compensation negotiated and paid in connection with a

separate transaction that occurs in lieu of the proposed offering, or reimbursement of out-of-pocket accountable expenses actually incurred by the member.[2]

Currently, paragraph (f)(2)(E) of Rule 5110 provides that, in the event that an issuer terminates an offering with an underwriter and subsequently consummates a similar transaction, a termination fee may be permissible under certain circumstances. Historically, FINRA has only considered permitting termination fee arrangements under this provision where the subsequent transaction is an exchange offer or similar offering where members provide substantial structuring or advisory services (beyond that traditionally provided in connection with a distribution of a public offering).[3] In such cases, FINRA believes that a termination fee may be appropriate given the extent of the services provided by the member to the issuer.

FINRA has reevaluated its rules around termination fees and believes it is appropriate to update the Rule to provide members with a greater degree of flexibility and

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2 Rule 5110(f)(2)(C) prohibits payment of commissions or reimbursement of expenses to an underwriter prior to the commencement of the sale of the securities being offered, except for a reasonable advance against out-of-pocket accountable expenses actually anticipated to be incurred by the underwriter. To the extent such expenses are not actually incurred, any advance received must be reimbursed to the issuer.

Paragraph (D) currently provides that the reimbursement of out-of-pocket accountable expenses actually incurred by the member will not be presumed to be unfair or unreasonable under normal circumstances. The proposed amendment modifies paragraph (D) to specify that out-of-pocket accountable expenses must be bona fide.

3 See Notice to Members 97-82 (November 1997). Further, the Rule provides that a tail fee may not have a duration of more than two years from the date the member's services are terminated; however, the Rule provides that a member may demonstrate on the basis of information satisfactory to FINRA that an arrangement of more than two years is not unfair or unreasonable under the circumstances.

expand the circumstances under which participating members and issuers may negotiate termination fee arrangements. Specifically, FINRA is proposing to amend Rule 5110(f)(2) (Prohibited Arrangements) to generally permit termination fees where: (1) the agreement between the participating member and the issuer specifies that the issuer has a right of "termination for cause" (i.e., where a member fails materially to perform the underwriting services contemplated in the written agreement);[4] (2) the agreement specifies that an issuer's exercise of its right of "termination for cause" eliminates any obligations with respect to the payment of any termination fee;[5] (3) the amount of any specified termination fee is reasonable in relation to the services contemplated in the written agreement; and (4) the agreement specifies that the issuer is not responsible for paying the termination fee unless an offering or other type of transaction is consummated by the issuer (without involvement of the member) within two years of the date the engagement is terminated with the member by the issuer. FINRA believes the proposal provides members with a greater degree of flexibility in negotiating the terms of their agreements for terminated offerings, while also providing protection for issuers if a member fails materially to perform the underwriting services contemplated in the written agreement.

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4 The specific meaning of "termination for cause" would be dictated by the agreement. For purposes of this proposal, a "termination for cause" would include a member's material failure to perform the underwriting services contemplated in the written agreement, but is not required to include events that are outside the participating member's control.

5 Members would continue to be permitted to receive reimbursement of out-of-pocket, bona fide, accountable expenses actually incurred by the participating member in connection with a terminated offering.

Current Rule 5110(f)(2)(F) and (G) address "ROFRs", which provide a member with the right to underwrite or participate in future public offerings, private placements or other financings of the issuer. Rule 5110(f)(2)(F) deems as unfair and unreasonable any ROFR provided to a member that: (1) has a duration of more than three years from the date of effectiveness or commencement of sales of the public offering, or (2) provides more than one opportunity to waive or terminate the ROFR in consideration of any payment or fee.[6] Rule 5110(f)(2)(G) prohibits any payment or fee to waive or terminate a ROFR regarding future public offerings, private placements or other financings that exceed specified values or that is not paid in cash.

FINRA also has reevaluated its rules around ROFRs and proposes amendments to permit ROFRs in the case of both successful as well as terminated offerings. FINRA proposes that ROFRs would be permissible where: (1) the agreement between the participating member and issuer specifies that the issuer has a right of termination for cause (i.e., where a member fails materially to perform the underwriting services contemplated in the written agreement); (2) an issuer's exercise of its right of "termination for cause" eliminates any obligations with respect to the provision of any ROFR; and (3) any fees arising from services provided under a ROFR are customary for those types of services. As is currently the case, the Rule would continue to provide that the duration of any ROFR may not be for more than three years from the date of commencement of sales of the public offering (in the case of a successful offering). In the case of a terminated offering, the duration may not be for more than three years from the date the engagement is terminated by the issuer. In both cases, the agreement may

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6 Historically, FINRA has interpreted the Rule to permit ROFRs only in the case of successful offerings.

not provide for more than one opportunity to waive or terminate the ROFR in consideration of any payment or fee.[7]

Filing Requirements for Certain Exchange-Traded Funds

Rule 5110(b)(8) (Exempt Offerings) generally provides an exemption for investment companies from the filing requirements of the Rule.[8] Due to this exemption, exchange-traded funds ("ETFs") that are structured as investment companies generally are exempt. However, this exemption does not include certain other ETFs that are not investment companies. FINRA believes it is appropriate to add an exemption for these ETFs even if they do not fall under the definition of an "investment company" for the same reason that investment company ETFs are exempted from the Rule. Specifically, the creation structure of ETFs, whereby the component securities are deposited in return for shares of the fund, is not a distribution model that Rule 5110 was designed to address. Thus, FINRA is proposing to exempt offerings of securities issued by a pooled investment vehicle, whether formed as a trust, partnership, corporation, limited liability company or other collective investment vehicle, that is not registered as an investment company under the Investment Company Act and has a class of equity securities listed

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7 FINRA is proposing to redesignate Rule 5110(f)(2)(G) as Rule 5110(f)(2)(F), which prohibits any payment or fee to waive or terminate a ROFR regarding future public offerings, private placements or other financings that exceed specified values or that is not paid in cash.

8 Rule 5110(b)(8)(C) exempts from the Rule's filing requirements securities of "open-end" investment companies as defined in Section 5(a)(1) of the Investment Company Act of 1940 ("Investment Company Act") and securities of any "closed-end" investment company as defined in Section 5(a)(2) of the Investment Company Act that: (1) makes periodic repurchase offers pursuant to Rule 23c-3(b) under of the Investment Company Act; and (2) offers its shares on a continuous basis pursuant to Rule 415(a)(1)(xi) of SEC Regulation C.

for trading on a national securities exchange; provided that such equity securities may be created or redeemed on any business day at their net asset value per share.

Electronic Filing

Rule 5110(b) (Filing Requirements) generally provides that no member or person associated with a member shall participate in any manner in a public offering of securities subject to Rules 2310, 5110 or 5121 unless the specified documents and information relating to the offering have been filed with and reviewed by FINRA. FINRA proposes to amend the Rule to make clarifying, non-substantive changes regarding documents filed through FINRA's electronic filing system.[9]

Industry Consultation

FINRA engaged in an extensive consultative process regarding the proposed rule change, including through the issuance of a Regulatory Notice soliciting comment on the termination fee and ROFR provisions, the exemption for ETFs, and the codification of the electronic filings requirement. Commenters generally supported the proposal as set forth in the Notice, requesting certain clarifications and modifications. A summary of the comments received in response to the Regulatory Notice is discussed in Item 5 below.

As noted in Item 2 of this filing, FINRA will announce the implementation date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date of the proposed rule change will be no later than 120 days following Commission approval.

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[9] The effective date of the electronic filing requirements under Rule 5110 was July 12, 2002. See Notice to Members 02-26.

(b) Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act[10] which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest.

The proposed rule change provides more flexibility to issuers and participating members in the negotiation of termination fee and ROFR terms and arrangements, while also promoting just and equitable principles of trade by providing important protections for issuers who terminate agreements with members for cause. Issuers can benefit from the advice underwriters provide prior to raising capital, and may be able to utilize more of an underwriter's resources if they can wait to pay until they have the additional capital they plan to receive in a public offering. This may be especially true for foreign issuers that may need substantial advice and restructuring before accessing the U.S. capital markets. Accordingly, issuers may want to enter into termination fee or ROFR agreements if they provide an incentive to underwriters to devote additional resources when the risk of not receiving remuneration for those services is mitigated.

In addition, the proposed rule change provides an exemption for certain other collective investment vehicles that are not registered as investment companies, as exists for open-end and certain closed-end investment companies. The proposed rule change also formalizes that members must use FINRA's electronic filing system to file required information and documents relating to offerings in which they participate.

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[10] 15 U.S.C. 78o–3(b)(6).

4. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. As discussed above, the proposed rule change sets out consistent rules for all members entering into agreements with issuers for the provision of services in connection with a public offering of securities, and also enhances competition among members that provide underwriting services to issuers by broadening the types of compensation arrangements that firms can negotiate with issuers. In addition, the amendments require that any termination fee paid must be reasonable in relation to the underwriting services contemplated and any ROFR fees paid must be customary in relation to the services the member provides.

Further, the proposed rule change provides additional protections to issuers that choose to enter into a termination fee agreement or provide a right of first refusal by requiring that the agreement provide issuers with a right to terminate for cause. Thus, under the proposal, issuers would have no obligation to pay a termination fee or be bound to a member by a ROFR if that member has failed materially to provide the underwriting services contemplated in the agreement.

The proposed rule change also would promote competition by eliminating disparate filing requirements for exchange-traded collective investment vehicles not registered as investment companies as compared to those that are structured as investment companies. FINRA does not believe that the codification of the electronic filing requirement or the other non-substantive and clarifying amendments contained in the filing will impact competition. Therefore, FINRA does not believe that the proposed rule

change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

On June 6, 2012, FINRA published Regulatory Notice 12-27 ("Notice" or "Notice 12-27") requesting comment on FINRA's proposal to amend Rule 5110. A copy of the Notice is attached as Exhibit 2a. The comment period expired on July 23, 2012. FINRA received three comments in response to the Notice.[11] A list of the commenters in response to the Notice is attached as Exhibit 2b, and copies of the comment letters received in response to the Notice are attached as Exhibit 2c. A summary of the comments and FINRA's response is provided below.

In Notice 12-27, FINRA proposed amendments substantially similar to the instant proposal. FINRA proposed to expand the circumstances under which termination fees and ROFRs would be permissible while providing protections for issuers that terminate arrangements with members for cause. The Notice also proposed to eliminate the filing requirements for exchange-traded funds that are structured as grantor or statutory trusts.

Commenters generally supported the proposal as set forth in the Notice and requested certain clarifications and modifications. With respect to the "termination for cause" provision, two commenters expressed concern that the provision would give an

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[11] See Letter from Bradley J. Swenson, Chief Compliance Officer, ALPS Distributors, Inc., to Joseph E. Price, Senior Vice President, FINRA, dated July 23, 2012 ("ALPS letter"); letter from Sean Davy, Managing Director, Corporate Credit Markets Division, Securities Industry and Financial Markets Association, to Marcia E. Asquith, Corporate Secretary, FINRA, dated July 23, 2012 ("SIFMA letter"); and letter from Jeffrey W. Rubin, Chair, Federal Regulation of Securities Committee, Business Law Section of the American Bar Association, to Marcia E. Asquith, Corporate Secretary, FINRA, dated July 30, 2012 ("ABA letter").

issuer broad discretion regarding the circumstances in which it could avoid paying an agreed upon termination fee to a member in the event of a terminated offering.[12] One commenter suggested limiting the circumstances under which an issuer could exercise its right to terminate for cause to an action or event that is "within the direct control of the member" and results in a material failure on the part of the member to provide the underwriting services.[13] Commenters also suggested that the issuer's termination for cause should take into account current market, economic and political conditions.[14] Another commenter suggested that the issuer's termination for cause be limited to cases in which the issuer requests the member to perform customary and reasonable services in connection with the public offering and "it is determined that the member has materially failed to provide such services."[15]

FINRA continues to believe that it is an important issuer protection that members' arrangements include an issuer's right to terminate an agreement for cause, but has modified the proposal to provide that a "termination for cause" shall include the participating member's material failure to provide the underwriting services contemplated in the agreement, since agreements may be drafted broadly to include services that are not related to the member's role as an underwriter. FINRA also has

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12 See ABA and SIFMA letters.

13 See ABA letter.

14 See ABA and SIFMA letters.

15 See SIFMA letter. SIFMA also suggested that the termination for cause provision be operative as a function of the rule itself and not be required to be included in the written agreement. FINRA disagrees and believes it is important that the termination clause be known to issuers and set forth in any written agreement regarding the provision of underwriting services by a participating member in connection with a public offering of securities.

clarified in this filing that an issuer's termination of an agreement due to events that are outside the member's control need not constitute a "termination for cause" under the proposal.

One commenter suggested amending the "termination for cause" provision to allow related persons and affiliates of the issuer and member to be parties to the written agreement noting that, in certain cases, the provisions and associated obligations may be reflected in an agreement between these persons.[16] Rule 5110 defines the terms "issuer" and "participating member" broadly to include certain related persons and affiliates. FINRA has revised the proposal to reflect the term "participating member" when referencing the parties to a member's written agreement with an issuer.

Notice 12-27 proposed that the agreement between the issuer and member provide that any termination fee must be reasonable and any fee arising from services provided under a ROFR be customary. Commenters argued that requiring the inclusion of the reasonable and customary language in a written agreement between the issuer and member is unnecessary and suggested that FINRA require these standards in the rule, but not require that they be expressed in the written agreement.[17] FINRA agrees and has reflected those changes in the instant filing. One commenter also suggested that FINRA clarify whether an issuer's payment of termination fees would be considered underwriting compensation in connection with a subsequent public offering that has been

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16 See SIFMA letter.

17 See ABA and SIFMA letters. SIFMA stated that these standards should be "operative as a function of the rule itself and should not be required to be set forth in a written agreement . . . ."

consummated within two years of the termination of services.[18]

In Notice 12-27, FINRA proposed an exemption from the filing requirements for ETFs formed as a grantor trust or statutory trust in which the portfolio assets include commodities, currencies or other assets that are not securities. Commenters supported this proposed amendment and further suggested that FINRA modify the proposed rule language to define the term "ETF" and broadly exempt from the Rule all ETFs without regard to how they are structured and organized.[19] FINRA has amended the language of the proposal to exempt offerings of securities issued by a pooled investment vehicle, whether formed as a trust, partnership, corporation, limited liability company or other collective investment vehicle, that is not registered as an investment company under the Investment Company Act and has a class of equity securities listed for trading on a national securities exchange; provided that such equity securities may be created or redeemed on any business day at their net asset value per share. FINRA believes that the current exemption for investment companies would capture virtually all other ETFs.

6. Extension of Time Period for Commission Action

FINRA does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.[20]

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18 See SIFMA letter. Under the Rule, items of value, such as termination fees or fees paid for services rendered pursuant to a ROFR are counted as compensation if they are received within 180 days prior to filing an offering or during the offering period. See Rule 5110(c)(3)(A)(xiii).

19 See ABA and ALPS letters.

20 15 U.S.C. 78s(b)(2).

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2) or Section 19(b)(7)(D)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act

Not applicable.

10. Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act

Not applicable.

11. Exhibits

Exhibit 1. Completed notice of proposed rule change for publication in the Federal Register.

Exhibit 2a. Regulatory Notice 12-27.

Exhibit 2b. List of comments received in response to Regulatory Notice 12-27.

Exhibit 2c. Copies of comments received in response to Regulatory Notice 12-27.

Exhibit 5. Text of the proposed rule change.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. SR-FINRA-2014-004)

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of a Proposed Rule Change Relating to Amendments to FINRA Rule 5110 (Corporate Financing Rule—Underwriting Terms and Arrangements)

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on , Financial Industry Regulatory Authority, Inc. ("FINRA") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing to amend FINRA Rule 5110 (Corporate Financing Rule—Underwriting Terms and Arrangements) to expand the circumstances in which termination fees and rights of first refusal are permissible; exempt from the filing requirements certain exchange-traded funds formed as grantor or statutory trusts; and make clarifying, non-substantive changes regarding documents filed through FINRA's electronic filing system.[3]

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 The effective date of the electronic filing requirements under Rule 5110 was July 12, 2002. See Notice to Members 02-26.

The text of the proposed rule change is available on FINRA's website at http://www.finra.org, at the principal office of FINRA and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

FINRA Rule 5110 (Corporate Financing Rule—Underwriting Terms and Arrangements) (the "Rule"), among other things, regulates underwriting compensation, requires the filing of specified information in connection with public offerings in which members will participate, and prohibits unfair arrangements in connection with public offerings of securities. FINRA proposes to amend the Rule's provisions regarding unfair arrangements to: (1) expand the circumstances under which members and issuers may negotiate termination fees and rights of first refusal ("ROFR"), with specified conditions; (2) exempt from the filing requirements exchange-traded funds formed as grantor or statutory trusts; and (3) codify the electronic filing requirement.

Termination Fees and Rights of First Refusal

Rule 5110(f) (Unreasonable Terms and Arrangements) sets forth terms and arrangements that, when proposed in connection with a public offering of securities, are considered unfair and unreasonable. Rule 5110(f)(2)(D) addresses fees in connection with a public offering of securities that is not completed according to the terms of agreement between the issuer and underwriter ("terminated offering"). Specifically, paragraph (D) generally provides that it is unfair and unreasonable for a member to arrange for the payment of any compensation by an issuer in connection with a terminated offering ("termination fee" or "tail fee"). Paragraph (D) further clarifies that this prohibition does not include compensation negotiated and paid in connection with a separate transaction that occurs in lieu of the proposed offering, or reimbursement of out-of-pocket accountable expenses actually incurred by the member.[4]

Currently, paragraph (f)(2)(E) of Rule 5110 provides that, in the event that an issuer terminates an offering with an underwriter and subsequently consummates a similar transaction, a termination fee may be permissible under certain circumstances. Historically, FINRA has only considered permitting termination fee arrangements under this provision where the subsequent transaction is an exchange offer or similar offering

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[4] Rule 5110(f)(2)(C) prohibits payment of commissions or reimbursement of expenses to an underwriter prior to the commencement of the sale of the securities being offered, except for a reasonable advance against out-of-pocket accountable expenses actually anticipated to be incurred by the underwriter. To the extent such expenses are not actually incurred, any advance received must be reimbursed to the issuer.

Paragraph (D) currently provides that the reimbursement of out-of-pocket accountable expenses actually incurred by the member will not be presumed to be unfair or unreasonable under normal circumstances. The proposed amendment modifies paragraph (D) to specify that out-of-pocket accountable expenses must be bona fide.

where members provide substantial structuring or advisory services (beyond that traditionally provided in connection with a distribution of a public offering).[5] In such cases, FINRA believes that a termination fee may be appropriate given the extent of the services provided by the member to the issuer.

FINRA has reevaluated its rules around termination fees and believes it is appropriate to update the Rule to provide members with a greater degree of flexibility and expand the circumstances under which participating members and issuers may negotiate termination fee arrangements. Specifically, FINRA is proposing to amend Rule 5110(f)(2) (Prohibited Arrangements) to generally permit termination fees where: (1) the agreement between the participating member and the issuer specifies that the issuer has a right of "termination for cause" (i.e., where a member fails materially to perform the underwriting services contemplated in the written agreement);[6] (2) the agreement specifies that an issuer's exercise of its right of "termination for cause" eliminates any obligations with respect to the payment of any termination fee;[7] (3) the amount of any specified termination fee is reasonable in relation to the services contemplated in the

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5 See Notice to Members 97-82 (November 1997). Further, the Rule provides that a tail fee may not have a duration of more than two years from the date the member's services are terminated; however, the Rule provides that a member may demonstrate on the basis of information satisfactory to FINRA that an arrangement of more than two years is not unfair or unreasonable under the circumstances.

6 The specific meaning of "termination for cause" would be dictated by the agreement. For purposes of this proposal, a "termination for cause" would include a member's material failure to perform the underwriting services contemplated in the written agreement, but is not required to include events that are outside the participating member's control.

7 Members would continue to be permitted to receive reimbursement of out-of-pocket, bona fide, accountable expenses actually incurred by the participating member in connection with a terminated offering.

written agreement; and (4) the agreement specifies that the issuer is not responsible for paying the termination fee unless an offering or other type of transaction is consummated by the issuer (without involvement of the member) within two years of the date the engagement is terminated with the member by the issuer. FINRA believes the proposal provides members with a greater degree of flexibility in negotiating the terms of their agreements for terminated offerings, while also providing protection for issuers if a member fails materially to perform the underwriting services contemplated in the written agreement.

Current Rule 5110(f)(2)(F) and (G) address "ROFRs", which provide a member with the right to underwrite or participate in future public offerings, private placements or other financings of the issuer. Rule 5110(f)(2)(F) deems as unfair and unreasonable any ROFR provided to a member that: (1) has a duration of more than three years from the date of effectiveness or commencement of sales of the public offering, or (2) provides more than one opportunity to waive or terminate the ROFR in consideration of any payment or fee.[8] Rule 5110(f)(2)(G) prohibits any payment or fee to waive or terminate a ROFR regarding future public offerings, private placements or other financings that exceed specified values or that is not paid in cash.

FINRA also has reevaluated its rules around ROFRs and proposes amendments to permit ROFRs in the case of both successful as well as terminated offerings. FINRA proposes that ROFRs would be permissible where: (1) the agreement between the participating member and issuer specifies that the issuer has a right of termination for cause (i.e., where a member fails materially to perform the underwriting services

8 Historically, FINRA has interpreted the Rule to permit ROFRs only in the case of successful offerings.

contemplated in the written agreement); (2) an issuer's exercise of its right of "termination for cause" eliminates any obligations with respect to the provision of any ROFR; and (3) any fees arising from services provided under a ROFR are customary for those types of services. As is currently the case, the Rule would continue to provide that the duration of any ROFR may not be for more than three years from the date of commencement of sales of the public offering (in the case of a successful offering). In the case of a terminated offering, the duration may not be for more than three years from the date the engagement is terminated by the issuer. In both cases, the agreement may not provide for more than one opportunity to waive or terminate the ROFR in consideration of any payment or fee.[9]

Filing Requirements for Certain Exchange-Traded Funds

Rule 5110(b)(8) (Exempt Offerings) generally provides an exemption for investment companies from the filing requirements of the Rule.[10] Due to this exemption, exchange-traded funds ("ETFs") that are structured as investment companies generally are exempt. However, this exemption does not include certain other ETFs that are not investment companies. FINRA believes it is appropriate to add an exemption for these ETFs even if they do not fall under the definition of an "investment company" for the

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9 FINRA is proposing to redesignate Rule 5110(f)(2)(G) as Rule 5110(f)(2)(F), which prohibits any payment or fee to waive or terminate a ROFR regarding future public offerings, private placements or other financings that exceed specified values or that is not paid in cash.

10 Rule 5110(b)(8)(C) exempts from the Rule's filing requirements securities of "open-end" investment companies as defined in Section 5(a)(1) of the Investment Company Act of 1940 ("Investment Company Act") and securities of any "closed-end" investment company as defined in Section 5(a)(2) of the Investment Company Act that: (1) makes periodic repurchase offers pursuant to Rule 23c-3(b) under of the Investment Company Act; and (2) offers its shares on a continuous basis pursuant to Rule 415(a)(1)(xi) of SEC Regulation C.

same reason that investment company ETFs are exempted from the Rule. Specifically, the creation structure of ETFs, whereby the component securities are deposited in return for shares of the fund, is not a distribution model that Rule 5110 was designed to address. Thus, FINRA is proposing to exempt offerings of securities issued by a pooled investment vehicle, whether formed as a trust, partnership, corporation, limited liability company or other collective investment vehicle, that is not registered as an investment company under the Investment Company Act and has a class of equity securities listed for trading on a national securities exchange; provided that such equity securities may be created or redeemed on any business day at their net asset value per share.

Electronic Filing

Rule 5110(b) (Filing Requirements) generally provides that no member or person associated with a member shall participate in any manner in a public offering of securities subject to Rules 2310, 5110 or 5121 unless the specified documents and information relating to the offering have been filed with and reviewed by FINRA. FINRA proposes to amend the Rule to make clarifying, non-substantive changes regarding documents filed through FINRA's electronic filing system.[11]

Industry Consultation

FINRA engaged in an extensive consultative process regarding the proposed rule change, including through the issuance of a Regulatory Notice soliciting comment on the termination fee and ROFR provisions, the exemption for ETFs, and the codification of the electronic filings requirement. Commenters generally supported the proposal as set forth in the Notice, requesting certain clarifications and modifications. A summary of the

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[11] The effective date of the electronic filing requirements under Rule 5110 was July 12, 2002. See Notice to Members 02-26.

comments received in response to the Regulatory Notice is discussed in Item 5 below.

FINRA will announce the implementation date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date of the proposed rule change will be no later than 120 days following Commission approval.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act[12] which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest.

The proposed rule change provides more flexibility to issuers and participating members in the negotiation of termination fee and ROFR terms and arrangements, while also promoting just and equitable principles of trade by providing important protections for issuers who terminate agreements with members for cause. Issuers can benefit from the advice underwriters provide prior to raising capital, and may be able to utilize more of an underwriter's resources if they can wait to pay until they have the additional capital they plan to receive in a public offering. This may be especially true for foreign issuers that may need substantial advice and restructuring before accessing the U.S. capital markets. Accordingly, issuers may want to enter into termination fee or ROFR agreements if they provide an incentive to underwriters to devote additional resources when the risk of not receiving remuneration for those services is mitigated.

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[12] 15 U.S.C. 78o–3(b)(6).

In addition, the proposed rule change provides an exemption for certain other collective investment vehicles that are not registered as investment companies, as exists for open-end and certain closed-end investment companies. The proposed rule change also formalizes that members must use FINRA's electronic filing system to file required information and documents relating to offerings in which they participate.

B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. As discussed above, the proposed rule change sets out consistent rules for all members entering into agreements with issuers for the provision of services in connection with a public offering of securities, and also enhances competition among members that provide underwriting services to issuers by broadening the types of compensation arrangements that firms can negotiate with issuers. In addition, the amendments require that any termination fee paid must be reasonable in relation to the underwriting services contemplated and any ROFR fees paid must be customary in relation to the services the member provides.

Further, the proposed rule change provides additional protections to issuers that choose to enter into a termination fee agreement or provide a right of first refusal by requiring that the agreement provide issuers with a right to terminate for cause. Thus, under the proposal, issuers would have no obligation to pay a termination fee or be bound to a member by a ROFR if that member has failed materially to provide the underwriting services contemplated in the agreement.

The proposed rule change also would promote competition by eliminating disparate filing requirements for exchange-traded collective investment vehicles not registered as investment companies as compared to those that are structured as investment companies. FINRA does not believe that the codification of the electronic filing requirement or the other non-substantive and clarifying amendments contained in the filing will impact competition. Therefore, FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

On June 6, 2012, FINRA published Regulatory Notice 12-27 ("Notice" or "Notice 12-27") requesting comment on FINRA's proposal to amend Rule 5110. A copy of the Notice is attached as Exhibit 2a. The comment period expired on July 23, 2012. FINRA received three comments in response to the Notice.[13] A list of the commenters in response to the Notice is attached as Exhibit 2b, and copies of the comment letters received in response to the Notice are attached as Exhibit 2c. A summary of the comments and FINRA's response is provided below.

In Notice 12-27, FINRA proposed amendments substantially similar to the instant proposal. FINRA proposed to expand the circumstances under which termination fees

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13 See Letter from Bradley J. Swenson, Chief Compliance Officer, ALPS Distributors, Inc., to Joseph E. Price, Senior Vice President, FINRA, dated July 23, 2012 ("ALPS letter"); letter from Sean Davy, Managing Director, Corporate Credit Markets Division, Securities Industry and Financial Markets Association, to Marcia E. Asquith, Corporate Secretary, FINRA, dated July 23, 2012 ("SIFMA letter"); and letter from Jeffrey W. Rubin, Chair, Federal Regulation of Securities Committee, Business Law Section of the American Bar Association, to Marcia E. Asquith, Corporate Secretary, FINRA, dated July 30, 2012 ("ABA letter").

and ROFRs would be permissible while providing protections for issuers that terminate arrangements with members for cause. The Notice also proposed to eliminate the filing requirements for exchange-traded funds that are structured as grantor or statutory trusts.

Commenters generally supported the proposal as set forth in the Notice and requested certain clarifications and modifications. With respect to the "termination for cause" provision, two commenters expressed concern that the provision would give an issuer broad discretion regarding the circumstances in which it could avoid paying an agreed upon termination fee to a member in the event of a terminated offering.[14] One commenter suggested limiting the circumstances under which an issuer could exercise its right to terminate for cause to an action or event that is "within the direct control of the member" and results in a material failure on the part of the member to provide the underwriting services.[15] Commenters also suggested that the issuer's termination for cause should take into account current market, economic and political conditions.[16] Another commenter suggested that the issuer's termination for cause be limited to cases in which the issuer requests the member to perform customary and reasonable services in connection with the public offering and "it is determined that the member has materially failed to provide such services."[17]

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14 See ABA and SIFMA letters.

15 See ABA letter.

16 See ABA and SIFMA letters.

17 See SIFMA letter. SIFMA also suggested that the termination for cause provision be operative as a function of the rule itself and not be required to be included in the written agreement. FINRA disagrees and believes it is important that the termination clause be known to issuers and set forth in any written agreement regarding the provision of underwriting services by a participating member in connection with a public offering of securities.

FINRA continues to believe that it is an important issuer protection that members' arrangements include an issuer's right to terminate an agreement for cause, but has modified the proposal to provide that a "termination for cause" shall include the participating member's material failure to provide the underwriting services contemplated in the agreement, since agreements may be drafted broadly to include services that are not related to the member's role as an underwriter. FINRA also has clarified in this filing that an issuer's termination of an agreement due to events that are outside the member's control need not constitute a "termination for cause" under the proposal.

One commenter suggested amending the "termination for cause" provision to allow related persons and affiliates of the issuer and member to be parties to the written agreement noting that, in certain cases, the provisions and associated obligations may be reflected in an agreement between these persons.[18] Rule 5110 defines the terms "issuer" and "participating member" broadly to include certain related persons and affiliates. FINRA has revised the proposal to reflect the term "participating member" when referencing the parties to a member's written agreement with an issuer.

Notice 12-27 proposed that the agreement between the issuer and member provide that any termination fee must be reasonable and any fee arising from services provided under a ROFR be customary. Commenters argued that requiring the inclusion of the reasonable and customary language in a written agreement between the issuer and member is unnecessary and suggested that FINRA require these standards in the rule, but

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[18] See SIFMA letter.

not require that they be expressed in the written agreement.[19] FINRA agrees and has reflected those changes in the instant filing. One commenter also suggested that FINRA clarify whether an issuer's payment of termination fees would be considered underwriting compensation in connection with a subsequent public offering that has been consummated within two years of the termination of services.[20]

In Notice 12-27, FINRA proposed an exemption from the filing requirements for ETFs formed as a grantor trust or statutory trust in which the portfolio assets include commodities, currencies or other assets that are not securities. Commenters supported this proposed amendment and further suggested that FINRA modify the proposed rule language to define the term "ETF" and broadly exempt from the Rule all ETFs without regard to how they are structured and organized.[21] FINRA has amended the language of the proposal to exempt offerings of securities issued by a pooled investment vehicle, whether formed as a trust, partnership, corporation, limited liability company or other collective investment vehicle, that is not registered as an investment company under the Investment Company Act and has a class of equity securities listed for trading on a national securities exchange; provided that such equity securities may be created or redeemed on any business day at their net asset value per share. FINRA believes that the current exemption for investment companies would capture virtually all other ETFs.

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19 See ABA and SIFMA letters. SIFMA stated that these standards should be "operative as a function of the rule itself and should not be required to be set forth in a written agreement . . . ."

20 See SIFMA letter. Under the Rule, items of value, such as termination fees or fees paid for services rendered pursuant to a ROFR are counted as compensation if they are received within 180 days prior to filing an offering or during the offering period. See Rule 5110(c)(3)(A)(xiii).

21 See ABA and ALPS letters.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/sro.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2014-004 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2014-004. This file number should be included on the subject line if e-mail is used. To help the Commission process

and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (http://www.sec.gov/rules/sro.shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2014-004 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[22]

Elizabeth M. Murphy

Secretary

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[22] 17 CFR 200.30-3(a)(12).

Regulatory Notice 12-27

Corporate Financing Rule

FINRA Requests Comment on Proposed Amendments to FINRA Rule 5110 Regarding Deferred Compensation Arrangements in Public Offerings

Comment Period Expires: July 23, 2012

Executive Summary

FINRA is requesting comments on proposed amendments to FINRA Rule 5110 (Corporate Financing Rule) that address current deferred compensation arrangements for financial advisory services in connection with public offerings, eliminate an anomalous filing requirement for exchange traded funds structured as statutory or grantor trusts, and make certain ministerial amendments to, among other things, reflect electronic filing requirements.

The text of the proposed rule change is set forth in Attachment A.

Questions regarding this *Notice* may be directed to:

- Joseph E. Price, Senior Vice President, Corporate Financing/Advertising Regulation, at (240) 386-4623;
- Paul Mathews, Director, Corporate Financing Department, at (240) 386-4639; or
- Lisa Jones Toms, Associate Director and Senior Counsel, Corporate Financing Department, at (240) 386-4661.

Action Requested

FINRA encourages all interested parties to comment on the proposal. Comments must be received by July 23, 2012.

June 2012

Notice Type

- Request for Comment

Suggested Routing

- Compliance
- Corporate Finance
- Legal
- Senior Management

Key Topics

- Deferred Compensation Arrangements in Public Offerings
- Exemption for Exchange-Traded Fund Offerings

Referenced Rules & Notices

- FINRA Rule 5110
- NASD Rule 2830
- NTM 97-82

FINRA®
Financial Industry Regulatory Authority

Member firms and other interested parties can submit their comments using the following methods:

- Emailing comments to *pubcom@finra.org*; or
- Mailing comments in hard copy to:

  Marcia E. Asquith
  Office of the Corporate Secretary
  FINRA
  1735 K Street, NW
  Washington, DC 20006-1506

To help FINRA process and review comments more efficiently, persons should use only one method to comment on the proposal.

Important Notes: The only comments that FINRA will consider are those submitted pursuant to the methods described above. All comments received in response to this *Notice* will be made available to the public on the FINRA website. Generally, FINRA will post comments as they are received.[1]

Before becoming effective, a proposed rule change must be authorized for filing with the Securities and Exchange Commission (SEC) by the FINRA Board of Governors, and then must be filed with the SEC pursuant to Section 19(b) of the Securities Exchange Act of 1934 (SEA).[2]

Background and Discussion

A. Deferred Compensation Arrangements

The Corporate Financing Rule requires member firms to file with FINRA's Corporate Financing Department documents and information about the underwriting terms and arrangements in public offerings in which they will participate. Before a public offering is filed, investment banks may enter into engagement letters with issuers for underwriting and financial advisory services, and these engagement letters often have provisions that allow issuers to defer payment until after the completion of a capital-raising transaction (deferred compensation arrangement). A deferred compensation arrangement responds to issuer concerns that up-front payment for financial advisory services could adversely affect the issuer's business. To address the risks that an issuer having received financial advisory services might unreasonably cancel an engagement to avoid the deferred compensation payment, engagement letters often provide for termination fees (sometimes called tail fees) or rights of first refusal. A termination fee permits an underwriter to receive fees if its services are terminated and the issuer consummates a similar transaction with another underwriter in lieu of the transaction subject to the engagement letter. A right of first refusal (ROFR) grants an underwriter the right to act in an agreed upon capacity in a subsequent financing transaction. Both arrangements provide issuers and underwriters with greater flexibility to negotiate deferred compensation arrangements.

The Corporate Financing Rule only permits termination fees in exchange offers or similar transactions in which substantial structuring and advisory services beyond traditional underwriting and distribution services have been provided.[3] The rule permits ROFRs, but the staff has interpreted the rule to prohibit ROFRs when a member's participation in the original transaction is terminated.[4] The restrictions on the establishment of termination fees and ROFRs in the Corporate Financing Rule may unnecessarily interfere with the ability of issuers and underwriters to negotiate deferred or other appropriate compensation arrangements that may be better suited to the issuer's business interests. For this reason, FINRA proposes to amend the Corporate Financing Rule to permit termination fees and ROFRs in a wider set of circumstances.[5]

FINRA proposes to amend Rule 5110(f)(2)(D) to allow termination fees and ROFRs when the written agreement between the issuer and underwriter specifies that:

- the amount of the termination fee must be reasonable in relation to the services contemplated in the agreement and fees arising from services provided under an ROFR must be customary for those type of services;
- the issuer has a right of "termination for cause," which includes the member's material failure to provide the services contemplated in the agreement; and
- an issuer's termination for cause eliminates any obligations with respect to any termination fee or ROFR.

The proposed amendments would retain the requirements in the existing rule that termination fees can only be paid and ROFRs can be executed within certain time periods. The proposed amendments thus would require that an offering or other transaction described in the agreement must be consummated within two years of the date the engagement is terminated, and would continue to prohibit any ROFR with a duration of more than three years from the date of effectiveness or commencement of sales of a public offering.[6] These time limitations will help ensure that the issuer is not subject to a termination fee or ROFR even after its business and operations may have significantly changed.

B. Filing Requirements for Certain Exchange-Traded Funds

Most exchange-traded funds (ETFs) are structured as open-end investment companies or unit investment trusts (UITs) that offer redeemable securities. Investment companies and UITs are exempt from regulation under the Corporate Financing Rule and are not required to be filed with FINRA's Corporate Financing Department. However, some ETFs are structured as Delaware statutory trusts or grantor trusts. The portfolio assets in these trusts typically are commodities, currencies or other assets that are not securities. Currently, there is no exemption for public offerings of ETFs structured in this manner and therefore these offerings are required to be filed under the rule.

The provisions in the Corporate Financing Rule regarding underwriting terms and arrangements are not designed for the ETF distribution methodology by which a "basket" of the underlying assets is deposited into the ETF's portfolio and "creation units" of shares are provided to the broker-dealer in return. ETFs should be treated consistently, without regard to the chosen legal structure, which is dictated primarily by the nature of the assets in the portfolios rather than differences in distribution methods or underwriting terms and arrangements. Accordingly, the proposed amendments would exempt from the rule's filing requirement offerings of securities issued by ETFs formed as grantor or statutory trusts in which the portfolio assets include commodities, currencies or other assets that are not securities.

C. Administrative Changes

FINRA proposes to make certain ministerial amendments to certain provisions in the Corporate Financing Rule to, among other things, reflect the acceptance of electronic filings.

Endnotes

1. FINRA will not edit personal identifying information, such as names or email addresses, from submissions. Persons should submit only information that they wish to make publicly available. *See* NTM 03-73 (November 2003) (NASD Announces Online Availability of Comments) for more information.
2. *See* SEA Section 19 and rules thereunder. After a proposed rule change is filed with the SEC, the proposed rule change generally is published for public comment in the *Federal Register*. Certain limited types of proposed rule changes, however, take effect upon filing with the SEC. *See* SEA Section 19(b)(3) and SEA Rule 19b-4.
3. *See* Rule 5110(f)(2)(E).
4. *See* Rule 5110(f)(2), (F) & (G).
5. If an underwriter does not meet the requirements of proposed Rule 5110(f)(2)(D)(ii), then it would continue to be prohibited from receiving compensation for underwriting services in a terminated offering except for reimbursement of out-of-pocket accountable expenses.
6. Currently, Rule 5110(f)(2)(E) requires that the issuer consummate a transaction similar to the transaction contemplated in the agreement between the issuer and the underwriter within two years of termination of the agreement.

Attachment A

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5110. Corporate Financing Rule — Underwriting Terms and Arrangements

(a) No Change.

(b) Filing Requirements

(1) through (4) No Change.

(5) Documents to be Filed

(A) The following documents relating to all proposed public offerings of securities that are required to be filed under paragraph (b)(4) above shall be filed [with] through FINRA's electronic filing system for review:

(i) [Three copies of t]The registration statement, offering circular, offering memorandum, notification of filing, notice of intention, application for conversion and/or any other document used to offer securities to the public;

(ii) [Three copies of a]Any proposed underwriting agreement, agreement among underwriters, selected dealers agreement, agency agreement, purchase agreement, letter of intent, consulting agreement, partnership agreement, underwriter's warrant agreement, escrow agreement, and any other document that describes the underwriting or other arrangements in connection with or related to the distribution, and the terms and conditions relating thereto; and any other information or documents that may be material to or part of the said arrangements, terms and conditions and that may have a bearing on FINRA's review;

(iii) [Three copies of e]Each pre- and post-effective amendment to the registration statement or other offering document, [one] with a copy marked to show changes; and [three (3) copies of] any other amended document previously filed pursuant to subparagraphs (i) and (ii) above, [one] with a copy marked to show changes; and

(iv) [Three copies of t]The final registration statement declared effective by the SEC or equivalent final offering document and a list of the members of the underwriting syndicate, if not indicated therein, and one copy of the executed form of the final underwriting documents and any other document submitted to FINRA for review.

(B) [All d]Documents that are filed with the SEC through the SEC's Electronic Data Gathering, Analysis, and Retrieval ("EDGAR") System that are referenced in FINRA's electronic filing system shall be treated as filed with FINRA.

(6) No Change.

(7) Offerings Exempt from Filing

Notwithstanding the provisions of subparagraph (1) above, documents and information related to the following public offerings need not be filed with FINRA for review, unless subject to the provisions of Rule 5121(a)(2). However, it shall be deemed a violation of this Rule or Rule 2310, for a member to participate in any way in such public offerings if the underwriting or other arrangements in connection with the offering are not in compliance with this Rule or Rule 2310, as applicable:

(A) through (E) No Change.

(F) exchange offers of securities where:

(i) the securities to be issued or the securities of the company being acquired are listed on The Nasdaq Global Market, the New York Stock Exchange, or the American Stock Exchange; or

(ii) the company issuing securities qualifies to register securities with the SEC on registration statement Forms S-3, F-3, or F-10, pursuant to the standards for those Forms as set forth in subparagraphs (C)(i) and (ii) of this paragraph; [and]

(G) offerings of securities by a church or other charitable institution that is exempt from SEC registration pursuant to Section 3(a)(4) of the Securities Act[.]; and

(H) offerings of securities issued by an exchange-traded fund formed as a grantor trust or statutory trust in which the portfolio assets include commodities, currencies or other assets that are not securities.

(8) through (9) No Change.

(c) Underwriting Compensation and Arrangements

(1) No Change.

(2) Amount of Underwriting Compensation

(A) No Change.

(B) For purposes of determining the amount of underwriting compensation, all items of value received or to be received from any source by the underwriter and related persons which are deemed to be in connection with or related to the distribution of the public offering as determined pursuant to subparagraph[s] (3) [and (4)] below shall be included.

(C) through (D) No Change.

(3) No Change.

(d) 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) Any accountable expense allowance granted by an issuer to the underwriter and related persons that includes payment for general overhead, salaries, supplies, or similar expenses of the underwriter incur[ ]red in the normal conduct of business.

(B) through (C) No Change.

(D) [The payment of a] Any compensation by an issuer to a member or person associated with a member in connection with an offering of securities that is not completed according to the terms of agreement between the issuer and underwriter, except: [those negotiated and paid in connection with a transaction that occurs in lieu of the proposed offering as a result of the efforts of the underwriter and related persons and provided, however, that]

(i) the reimbursement of out-of-pocket accountable expenses actually incurred by the member or person associated with a member[shall not be presumed to be unfair or unreasonable under normal circumstances.];

(ii) a termination fee or a right of first refusal, as set forth in a written agreement between the issuer and the member, provided that the agreement specifies:

a. the amount of any termination fee must be reasonable in relation to the services contemplated in the agreement and any fees arising from services provided under a right of first refusal must be customary for those type of services;

b. the issuer has a right of "termination for cause," which shall include the member's material failure to provide the services contemplated in the agreement;

c. an issuer's "termination for cause" eliminates any obligations with respect to any termination fee or right of first refusal; and

d. the termination fee requires that in order for the issuer to be responsible for paying the fee, an offering or other transaction (as set forth in the agreement) must be consummated within two years of the date the engagement is terminated by the issuer.

[(E) Any "tail fee" arrangement granted to the underwriter and related persons that has a duration of more than two years from the date the member's services are terminated, in the event that the offering is not completed in accordance with the agreement between the issuer and the underwriter and the issuer subsequently consummates a similar transaction, except that a member may demonstrate on the basis of information satisfactory to FINRA that an arrangement of more than two years is not unfair or unreasonable under the circumstances.]

([F]E) Any right of first refusal provided to the underwriter or related persons to underwrite or participate in future public offerings, private placements or other financings that:

(i) has a duration of more than three years from the [date of effectiveness or] commencement of sales of the public offering or the termination date of the engagement between the issuer and underwriter; or

(ii) has more than one opportunity to waive or terminate the right of first refusal in consideration of any payment or fee;

([G]F) Any payment or fee to waive or terminate a right of first refusal regarding future public offerings, private placements or other financings provided to the underwriter and related persons that:

(i) has a value in excess of the greater of 1% of the offering proceeds in the public offering where the right of first refusal was granted (or an amount in excess of 1% if additional compensation is available under the compensation guideline of the original offering) or 5% of the underwriting discount or commission paid in connection with the future financing (including any overallotment option that may be exercised), regardless of whether the payment or fee is negotiated at the time of or subsequent to the original public offering; or

(ii) is not paid in cash.

(H) through (I) redesignated as (G) through (H).

([J]I) When proposed in connection with the distribution of a public offering of securities on a "firm commitment" basis, any over[ ]allotment option providing for the over[ ]allotment of more than 15% of the amount of securities being offered, computed excluding any securities offered pursuant to the over[ ]allotment option.

(K) through (L) redesignated as (J) through (K).

[(M) 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) Lock-Up Restriction on Securities

(1) No change.

(2) Exceptions to Lock-Up Restriction

(A)(i) through (ii) No Change.

(iii) if the aggregate amount of securities of the issuer held by the underwriter [or] and related persons do not exceed 1% of the securities being offered;

(iv) through (viii) No Change.

(B) No Change.

(h) Non-Cash Compensation

(1) No Change.

(2) Restrictions on Non-Cash Compensation

(A) through (B) No Change.

(C) Payment or reimbursement by offerors in connection with meetings held by an offeror or by a member for the purpose of training or education of associated persons of a member, provided that:

(i) associated persons obtain the member's prior approval to attend the meeting and attendance by a member's associated persons is not conditioned by the member on the achievement of a sales target or any other incentives pursuant to a non-cash compensation arrangement permitted by paragraph ([d]h)(2)(D);

(ii) through (iii) No Change.

(iv) the payment or reimbursement by the issuer or affiliate of the issuer is not conditioned by the issuer or an affiliate of the issuer on the achievement of a sales target or any other non-cash compensation arrangement permitted by paragraph ([d]h)(2)(D).

(D) No Change.

(E) Contributions by a non-member company or other member to a non-cash compensation arrangement between a member and its associated persons, provided that the arrangement meets the criteria in paragraph ([d]h)(2)(D).

A member shall maintain records of all non-cash compensation received by the member or its associated persons in arrangements permitted by paragraphs ([d]h)(2)(C) through (E). The records shall include: the names of the offerors, non-members or other members making the non-cash compensation contributions; the names of the associated persons participating in the arrangements; the nature and value of non-cash compensation received; the location of training and education meetings; and any other information that proves compliance by the member and its associated persons with paragraphs ([d]h)(2)(C) through (E).

(i) No Change.

* * * * *

EXHIBIT 2b

Alphabetical List of Written Comments

1. Sean Davy, Securities Industry and Financial Markets Association (July 23, 2012)

2. Jeffrey W. Rubin, Federal Regulation of Securities Committee, Business Law Section of the American Bar Association (July 30, 2012)

3. Bradley J. Swenson, ALPS Distributors, Inc. (July 23, 2012)

EXHIBIT 2c

sifma
Invested in America

July 23, 2012

Submitted via email to pubcom@finra.org

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 12-27

Dear Ms. Asquith:

The Securities Industry and Financial Markets Association ("SIFMA")[1] appreciates the opportunity to comment on Regulatory Notice 12-27, which sets forth FINRA's proposed amendments to paragraph (f)(2) of FINRA Rule 5110 (the "Corporate Financing Rule") regarding certain deferred compensation arrangements in public offerings (the "Deferred Compensation Proposal").[2]

The Deferred Compensation Proposal attempts to address certain significant limitations in the Corporate Financing Rule as currently formulated and SIFMA fully supports the substance of the proposed revisions. SIFMA believes the proposed changes will benefit all offering participants by allowing issuers of publicly offered securities greater freedom to negotiate agreements that defer their obligation to compensate their underwriters until the actual consummation of the relevant public offering, while at the same time protecting underwriters and related persons from issuers that seek to unfairly forego the payment of compensation that would otherwise be due under the terms of such agreements.

Nonetheless, although SIFMA agrees with the rationale and intent of the Deferred Compensation Proposal and encourages swift action to implement the changes reflected therein, we do suggest certain modifications to the actual text of the proposed revisions (set forth in Attachment A to the Deferred Compensation Proposal) as further detailed below.

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[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit www.sifma.org.

[2] SIFMA is not commenting in this letter on the other aspects of Regulatory Notice 12-27 relating to matters other than deferred compensation arrangements.

Discussion of Suggested Modifications (see Annex A for proposed textual changes to reflect these comments):

1. We agree that the provisions with respect to termination fees and rights of first refusal should be set forth in a written agreement. However, we note that in certain cases these provisions and associated obligations may be reflected in an agreement between persons related to the actual issuer of the securities to be publicly offered and/or an affiliate of the member, rather than the issuer and member themselves. For example, a parent company may enter into an engagement letter with an affiliate of a member for financial advisory services related to the potential sale of the assets of a subsidiary. Such letter may include a right of first refusal permitting the member to act as an underwriter in a subsequent, side-by-side or alternative U.S. public offering in which the subsidiary is the actual issuer of the securities. Although the definition of "issuer" under Rule 5110(a)(1) does encompass affiliates as well as certain others, the definition of "member" is more narrow. Accordingly, we suggest that proposed clause (f)(2)(D)(ii) be broadened to allow for the possibility that an affiliate of a member may be the signatory to the agreement that contains the relevant provisions.

2. We believe that proposed Rule 5110(f)(2)(D)(ii) should be modified to clarify that the restrictions with respect to termination fees and rights of first refusals apply only to the extent they relate to a public offering of securities that is subject to the rule (and not, for example, financial advisory or other services provided in connection with an M&A transaction).

3. We agree that the termination fee relating to services to be provided in connection with a public offering should be reasonable in relation to the services contemplated and any fees arising from services provided under a right of first refusal should be customary for such services. We also agree that the issuer should have the ability to terminate its obligations in respect of a public offering-related termination fee and/or right of first refusal "for cause". However, we believe these provisions should be operative as a function of the rule itself and should not be required to be set forth in a written agreement to have effect. This would also have the effect of making any such requirements immediately operative rather than requiring members to renegotiate and amend currently outstanding agreements as these (and potentially future) changes to Rule 5110(f)(2)(D)(ii) are adopted.

   Alternatively, if FINRA continues to require that specific language actually be included in the written agreement between the issuer and member (or affiliate of the member) for the proposed provisions set forth in Regulatory Notice 12-27 to have effect, then we request that FINRA clarify in the rule itself or in

accompanying guidance that (i) the requirement relating to the inclusion of the specific language shall apply only in respect of agreements that are entered into after the date of effectiveness of the amended rule and (ii) the substance of the provisions set forth in Rule 5110(f)(2)(D)(ii) will apply in respect of agreements that were entered into prior to the date of effectiveness if, with respect to any FINRA filing required in connection with a relevant public offering, the member represents to FINRA that, notwithstanding anything to the contrary in the agreement, the provisions in the agreement with respect to a public offering-related termination fee and/or right of first refusal shall be subject to the limitations imposed by Rule 5110(f)(2)(D)(ii).

4. With respect to termination "for cause", we believe the standard proposed by FINRA relating to a member's "material failure to provide the services contemplated in the agreement" will be difficult to apply as a practical matter. The provision, as currently set forth in Attachment A to the Deferred Compensation Proposal, may also be interpreted as providing the issuer with a broad right to determine what constitutes "for cause", which we believe is not FINRA's intent. Accordingly, we suggest that the proposed provision be modified to provide that a public offering-related termination fee and/or right of first refusal shall be terminable by the issuer if the issuer requests the member to perform customary and reasonable services in connection with such public offering (taking into consideration current market, economic and political conditions) and it is determined that the member has materially failed to provide such services.

   We believe the foregoing modification will address those situations in which specific services in connection with a public offering are not expressly set forth in the agreement, and/or there is a disagreement as to which services were "contemplated" in the agreement.

   Alternatively, if FINRA disagrees with the foregoing approach, we request at the very least that the current language in proposed Rule 5110(f)(2)(D)(ii)(b) be modified to provide that:

   > "the issuer's obligations to a member or associated person of a member in respect of a termination fee or right of first refusal relating to a public offering of securities shall be terminable by the issuer due to the member's material failure to provide the services contemplated in the agreement that relate to such public offering (unless such failure results from the issuer's own actions or inactions or is otherwise due to events or circumstances outside the member's control) or for any other reason constituting "for cause" as shall be negotiated and set forth in the agreement between the issuer and the member (or affiliate of the member)".

5. Finally, although there is language to such effect in Rule 5110(c)(3)(A)(xiii), we believe it would be helpful to clarify in proposed clause (f)(2)(D)(ii)(c) that any termination fee payable by the issuer will not be deemed underwriting compensation in connection with the later consummated public offering of securities in which the terminated member is no longer participating.

* * *

We thank you for your consideration of our comments. If you have any questions with regard to this letter, please do not hesitate to call the undersigned at 212-313-1118 or Dana Fleischman of Latham & Watkins LLP, our outside counsel for this matter, at 212-906-1220.

Respectfully submitted,

Sean Davy

Managing Director, Corporate Credit Markets Division
Securities Industry and Financial Markets Association

Attachment

Annex A

Rule 5110(f)(2) (Proposed changes to Attachment A to Regulatory Notice 12-27 – Clean Version)[3]

(D) Any compensation by an issuer to a member or person associated with a member in connection with a public offering of securities that is not completed according to the terms of agreement between the issuer and underwriter, except:

(i) the reimbursement of out-of-pocket accountable expenses actually incurred by the member or person associated with a member; and

(ii) a termination fee or a right of first refusal that is set forth in a written agreement between the issuer and the member (or an affiliate of the member), provided that:

a. the amount of any termination fee relating to services to be provided by the member or person associated with the member in connection with a public offering of securities must be reasonable in relation to the services contemplated in the agreement with respect to such public offering and any fees arising from services to be provided by the member or person associated with the member under a right of first refusal relating to a public offering of securities must be customary for those type of services;

b. the issuer's obligations to a member or person associated with a member in respect of a termination fee or right of first refusal relating to a public offering of securities shall be terminable by the issuer if the issuer requests the member to perform customary and reasonable services in connection with such public offering (taking into consideration current market, economic and political conditions) and it is determined that the member has materially failed to provide such services; and

c. with respect to any termination fee relating to services to be provided by the member or person associated with the member in connection with a public offering of securities, such termination fee shall be payable by the issuer only if an offering or other transaction (as set forth in the agreement) is consummated within two years of the date the engagement is terminated by the issuer (and any such termination fee will not be deemed underwriting compensation in connection with the later consummated offering).

[3] For certain alternative proposals, see accompanying letter.

Rule 5110(f)(2) (Marked version showing changes from Attachment A to Regulatory Notice 12-27)

(D) Any compensation by an issuer to a member or person associated with a member in connection with ~~an~~**a public** offering of securities that is not completed according to the terms of agreement between the issuer and underwriter, except:

(i) the reimbursement of out-of-pocket accountable expenses actually incurred by the member or person associated with a member; **and**

(ii) a termination fee or a right of first refusal~~, as~~ **that is** set forth in a written agreement between the issuer and the member **(or an affiliate of the member)**, provided that ~~the agreement specifies~~:

a. the amount of any termination fee **relating to services to be provided by the member or person associated with the member in connection with a public offering of securities** must be reasonable in relation to the services contemplated in the agreement **with respect to such public offering** and any fees arising from services **to be** provided **by the member or person associated with the member** under a right of first refusal **relating to a public offering of securities** must be customary for those type of services;

b. ~~the issuer has a right of "termination for cause," which shall include the member's material failure to provide the services contemplated in the agreement;~~ **the issuer's obligations to a member or person associated with a member in respect of a termination fee or right of first refusal relating to a public offering of securities shall be terminable by the issuer if the issuer requests the member to perform customary and reasonable services in connection with such public offering (taking into consideration current market, economic and political conditions) and it is determined that the member has materially failed to provide such services; and**

~~c. an issuer's "termination for cause" eliminates any obligations with respect to any termination fee or right of first refusal; and~~

c. ~~d. the termination fee requires that in order for the issuer to be responsible for paying the fee,~~**with respect to any termination fee relating to services to be provided by the member or person associated with the member in connection with a public offering of securities, such termination fee shall be payable by the issuer only if** an offering or other transaction (as set forth in the agreement) ~~must be~~**is** consummated within two years of the date the engagement is terminated by the issuer **(and any such termination fee will not be deemed underwriting compensation in connection with the later consummated offering)**.

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July 30, 2012

Marcia E. Asquith
Office of the Corporate Secretary
Financial Industry Regulatory Authority, Inc.
1735 K Street, N.W.
Washington, D.C. 20006-1506

Re: Regulatory Notice 12-27: Corporate Financing Rule: Proposed Amendments to FINRA Rule 5110 Regarding Deferred Compensation Arrangements in Public Offerings and Filing Requirements for Certain Exchange-Traded Funds

Ladies and Gentlemen:

This letter is submitted on behalf of the Federal Regulation of Securities Committee (the "Committee") of the Business Law Section (the "Section") of the American Bar Association (the "ABA") in response to the request for comments by the Financial Industry Regulatory Authority, Inc. ("FINRA") pursuant to FINRA Regulatory Notice 12-27 (the "Notice") as more fully set forth below.

This letter was prepared by members of the Subcommittee on FINRA Corporate Financing Rules of the Committee.

The comments expressed in this letter (the "Comment Letter") represent the views of the Committee only and have not been approved by the ABA's House of Delegates or Board of Governors and therefore do not represent the official position of the ABA. In addition, this letter does not represent the official position of the Section.

I. Background.

FINRA Rule 5110(f)(2) sets forth certain terms and arrangements that are deemed by FINRA to be "unfair and unreasonable" when proposed in connection with a public offering of securities. In particular, FINRA Rule 5110(f)(2) imposes limitations on the ability of a FINRA member to receive so-called "tail fees" or to exercise a right of first refusal ("ROFR") when a member's engagement in respect of a proposed public offering is terminated, or the proposed public offering is otherwise not consummated. The provisions relating to tail fees and ROFRs are set forth in FINRA Rules 5110(f)(2)(D), (E), (F) and (G).

In particular, FINRA Rule 5110(f)(2)(D) prohibits:

"The payment of any compensation by an issuer to a member or person associated with a member in connection with an offering of securities that is not completed according to the terms of agreement between the issuer and underwriter, except those negotiated and paid in connection with a transaction that occurs in lieu of the proposed offering as a result of the efforts of the underwriter and related persons and provided, however, that the reimbursement of out-of-pocket accountable expenses actually incurred by the member or person associated with a member shall not be presumed to be unfair or unreasonable under normal circumstances."

FINRA Rule 5110(f)(2)(E) prohibits:

"Any "tail fee" arrangement granted to the underwriter and related persons that has a duration of more than two years from the date the member's services are terminated, in the event that the offering is not completed in accordance with the agreement between the issuer and the underwriter and the issuer subsequently consummates a similar transaction, except that a member may demonstrate on the basis of information satisfactory to FINRA that an arrangement of more than two years is not unfair or unreasonable under the circumstances."

FINRA Rule 5110(f)(2)(F) prohibits:

"Any right of first refusal provided to the underwriter or related persons to underwrite or participate in future public offerings, private placements or other financings that:

(i) has a duration of more than three years from the date of effectiveness or commencement of sales of the public offering; or

(ii) has more than one opportunity to waive or terminate the right of first refusal in consideration of any payment or fee."

And, FINRA Rule 5110(f)(2)(G) prohibits:

"Any payment or fee to waive or terminate a right of first refusal regarding future public offerings, private placements or other financings provided to the underwriter and related persons that:

(i) has a value in excess of the greater of 1% of the offering proceeds in the public offering where the right of first refusal was granted (or an amount in excess of 1% if additional compensation is available under the compensation guideline of the original offering) or 5% of the underwriting discount or commission paid in connection with the future financing (including any overallotment option that may

be exercised), regardless of whether the payment or fee is negotiated at the time of or subsequent to the original public offering; or

(ii) is not paid in cash."

With respect to proposed capital raising transactions by issuers involving the distribution services of one or more FINRA members, the Notice recognizes that members often enter into engagement letters/agreements with issuers that provide the member with a ROFR in order to act in an agreed-upon capacity in a subsequent (public or private) financing transaction. In addition, the Notice recognizes that engagement letters and similar agreements often also provide for the payment by the issuer of a "tail fee" to the member in the event that a capital raising transaction is not consummated by the issuer, as contemplated by the engagement letter/agreement, but where the issuer subsequently consummates a similar transaction with a different member within a specified period of time (within two years after the termination of the first engagement).

As set forth in the Notice, FINRA's Corporate Financing Department currently interprets FINRA Rule 5110 to provide that (i) a member may not exercise a ROFR with respect to a subsequent public or private offering when a member's participation in the original (public offering) transaction is terminated on the grounds that the "payment" of a ROFR would not be permitted under FINRA Rule 5110(f)(2)(D), which rule only allows a member to receive reimbursement of its "out-of-pocket accountable expenses actually incurred" by the member if the original transaction is not completed according to the terms of agreement between the issuer and the member, and not the "payment" of any other "compensation" to the member, and (ii) a member may not receive a tail fee (termination fee) except in connection with an exchange offer or similar transaction in which substantial structuring and advisory services "beyond traditional underwriting and distribution services" have been provided.[1]

II. Proposed Amendments Relating to the Treatment of ROFRs and Tail Fees.

FINRA proposes to eliminate current FINRA Rule 5110(f)(2)(E), relating to tail fees, and to amend current FINRA Rule 5110(f)(2)(D) by providing that in addition to the receipt by a member of out-of-pocket accountable expenses actually incurred by the member, the following is also a permissible exception to the general requirement that a member not be allowed to receive any compensation in connection with a public offering of securities that is not consummated according to the terms of an engagement letter/agreement between the issuer and the underwriter:

"(ii) a termination fee or a right of first refusal, as set forth in a written agreement between the issuer and the member, provided that the agreement specifies:

---

[1] See also Notice to Members 97-82 of the former National Association of Securities Dealers, Inc.

a. the amount of any termination fee must be reasonable in relation to the services contemplated in the agreement and any fees arising from services provided under a right of first refusal must be customary for those type of services;

b. the issuer has a right of "termination for cause," which shall include the member's material failure to provide the services contemplated in the agreement;

c. an issuer's "termination for cause" eliminates any obligations with respect to any termination fee or right of first refusal; and

d. the termination fee requires that in order for the issuer to be responsible for paying the fee, an offering or other transaction (as set forth in the agreement) must be consummated within two years of the date the engagement is terminated by the issuer."

In this regard, the proposed amendments would no longer use the term "tail" fee, but would instead use the term "termination" fee.

We support FINRA's proposals in concept as these arrangements allow issuers and underwriters to negotiate more flexible compensation arrangements and agree with the Notice that the current interpretation by FINRA of FINRA Rule 5110(f)(2) unnecessarily interferes with the business decisions of issuers and underwriters in this regard.

The aforesaid proposed amendments to FINRA Rule 5110(f)(2) would not otherwise modify or change the two-year time limit set forth in current FINRA Rule 5110(f)(2)(E) with respect to the payment of a termination fee (formerly known as a tail fee) or the three-year time limit set forth in current FINRA Rule 5110(f)(2)(F) with respect to the exercise of a ROFR or the other requirements relating to the exercise of ROFRs, including the permitted amount of any termination or waiver fees therefor in current FINRA Rules 5110(f)(2)(F) and (G).

III. Discussion of Proposed Amendments Relating to ROFRs and Tail Fees.

As noted above, the proposed amendment to FINRA Rule 5110(f)(2)(D) would permit FINRA members to receive termination fees and ROFRs arising from public offerings of securities that are not consummated, provided that the underwriter (FINRA member) and the issuer enter into a written agreement that specifies, among other things, (i) the amount of the termination fee and that such amount be "reasonable in relation to the services contemplated in the agreement" and (ii) that fees arising from services provided under a ROFR must be "customary for those type of services."

Requiring that the amount of any termination fee be "reasonable in relation to the services contemplated in the agreement" and that any fees arising from services provided under a

ROFR must be "customary for those type of services" is a regulatory standard against which the amount of any such fees should be determined or judged. As such, we do not believe that it is necessary or appropriate to have the parties agree to such standard in the agreement, and we suggest that the proposed amendment to FINRA Rule 5110(f)(2)(D) merely require that there be a written agreement between the member and the issuer that specifies the amount of any such fees or the method for the determination/calculation of such fees, but then provide, in the rule but, again, not in the relevant agreement, that in order for such fees to be deemed to be fair and reasonable, (i) any termination fee must be reasonable in relation to the services contemplated in the agreement and (ii) any fees arising from services provided under a ROFR to the member must be customary for those type of services. If the issuer and the underwriter – the parties to the applicable agreement – agree on the amount of any such fees (or the method for calculating/determining the amount of such fees), those parties, presumably, would have determined that the fees are reasonable or customary, as the case may be, so that the inclusion of a reasonable and/or customary standard, in addition to the amount of the fees or the method for determination of such fees, would seem to be superfluous and, thus, unnecessary to be restated in the applicable agreement.

In addition, the applicable agreement between the member and the issuer must specify that the issuer has the right to terminate such agreement "for cause," which shall "include" the member's "material failure to provide the services contemplated in the agreement." We suggest that an issuer's ability to terminate the applicable agreement for cause should arise *only* where, as a result of event(s) or action(s) within the direct control of the member, there is a material failure on the part of the member to provide the services, customary for those types of services, as contemplated in the agreement within a reasonable time period, but other than as result of market, political, economic or other action(s) or event(s) that are beyond the control of the member.

We also suggest that in order to prevent an issuer from "gaming" a termination to avoid having to make a payment of a termination fee to a member, a member would be entitled to receive a termination fee specified in an appropriate agreement more than two years after the date of the termination of the agreement by the issuer (other than for cause) if the issuer enters into an agreement with another member within 1-1/2 years after the termination of the agreement with the first member and that provides for another transaction to be consummated with the second member at a date that is more than two years after the termination of the agreement with the first member.

Finally, a proposed amendment to current FINRA Rule 5110(f)(2)(F) (which provision would be redesignated as FINRA Rule 5110(f)(2)(E)) would provide that a ROFR cannot have a duration of more than three years from the commencement of sales of the public offering "or the termination date of the engagement between the issuer and underwriter." In light of proposed FINRA Rule 5110(f)(2)(D)(ii)(c), as set forth above, that would provide that an issuer's "termination for cause" would eliminate any obligations with respect to any termination fee or ROFR, we suggest that the revised/amended language in proposed paragraph (f)(2)(E)(i) add at

the end of "or the termination date of the engagement between the issuer and underwriter" the following: "except with respect to a "termination for cause.""

IV. Proposed Amendment to Filing Requirements for Certain Exchange-Traded Funds.

Pursuant to the Notice, FINRA Rule 5110 would also be amended by adding a new exemption from filing under FINRA Rule 5110(b)(7)(H) in respect of "offerings of securities issued by an exchange-traded fund formed as a grantor trust or statutory trust in which the portfolio assets include commodities, currencies or other assets that are not securities."

We support such an amendment as it would provide equal treatment under FINRA Rule 5110 for (open-end) exchange-traded funds regardless of whether or not such a fund is required to be registered under the Investment Company Act of 1940 (the "1940 Act"). However, it is our view that, just as an exchange-traded fund's registration status under the 1940 Act should not lead to different results under FINRA Rule 5110, an exchange-traded fund's form of organization under state law and tax classification under the Internal Revenue Code of 1986 (the "IRC") should not lead to different results thereunder.

A statutory trust refers to an entity organized under and pursuant to the Delaware Statutory Trust Act, Chapter 38 of Title 12 of the Delaware Code, 12 Del. C. § 3801 *et seq.* A grantor trust is a form of classification that may be available to an exchange-traded fund under the IRC. However, an exchange-traded fund need not be organized as a statutory trust and need not be classified as a grantor trust. An exchange-traded fund may be organized as a Delaware statutory trust, but it may also be organized as a Maryland corporation, a Massachusetts business trust, a Delaware limited partnership, or in some other form. Moreover, an exchange-traded fund may be classified under the Internal Revenue Code as a grantor trust, but it may also be classified as a "regulated investment company" or a "partnership." Conditioning the exemption from filing under FINRA Rule 5110 on the form of organization of an exchange-traded fund or the tax classification of an exchange-traded fund would not serve any regulatory purpose, and would be as arbitrary as conditioning the exemption from filing under FINRA Rule 5110 on the registration status of the exchange-traded fund under the 1940 Act.

Also, exchange-traded funds that use futures, options on futures and other derivatives to obtain exposure to currencies and commodities (whether physical commodities such as corn, copper or gasoline or financial commodities such as interest rates and indexes) often have significant amounts of cash on their balance sheets in excess of the collateral required to establish and maintain their derivatives positions. This excess cash may be invested in Treasury bills, securities guaranteed as to principal or interest by the United States, fixed-income securities issued or guaranteed by corporations in which the United States has a direct or indirect interest, or other securities. Other exchange-traded funds that obtain exposure to currencies or commodities by holding bank deposits in foreign currencies or physical commodities (such as gold bullion) do not have any material amount of excess cash that may be invested in securities. Consequently, to condition the exemption from filing under FINRA Rule 5110 on the content of the exchange-traded fund's investment portfolio would not appear to serve any regulatory

purpose. Rather, the focus for the exemption should be on the fact that the exchange-traded fund is exchange-listed and open-end.

Furthermore, the term "exchange-traded fund" is nowhere defined in FINRA Rule 5110, and could be interpreted to include any vehicle for collective investment whose shares are listed for trading on a securities exchange, including, for example, a closed-end fund. A definition of the term "exchange-traded fund" for purposes of FINRA Rule 5110 would therefore be appropriate. The key distinguishing innovation that is characteristic of all exchange-traded funds and is critical for their successful operation is the existence of a secondary market for their shares on a securities exchange, where the shares trade throughout the trading day like any other equity security at prices determined by supply and demand, coupled with daily creation and redemption of shares at net asset value per share in large aggregations by certain eligible financial institutions. This innovation tends to cause the market price per share to track the net asset value per share over time, because differences between market price and net asset value create arbitrage opportunities for investors who can exploit them by increasing or decreasing the supply of exchange-traded fund shares by creating or redeeming exchange-traded fund shares at net asset value until the market price and the net asset value per share come back into equilibrium. This affords retail investors, who obtain their exposure to exchange-traded funds in the secondary market on a securities exchange, and depend for liquidity in their exchange-traded fund holdings on the existence of a secondary market in exchange-traded fund shares on a securities exchange, a high degree of assurance that they will be able to enter and exit an investment in an exchange-traded fund at a price per share that is a close approximation of net asset value per share.

In light of the foregoing, we suggest a clarification to the proposed exemption in FINRA Rule 5110(b)(7)(H) so as to state as follows:

> "offerings of securities issued by an Exchange-Traded Fund.
>
> The Term "Exchange-Traded Fund" means any issuer of securities that is an investment company or investment trust or similar form of enterprise that does not produce goods or services and that has a class of equity securities listed for trading on a national securities exchange, <u>provided</u> such equity securities may be created or redeemed on any business day at their net asset value per share in large aggregations by certain eligible financial institutions that are in privity of contract with the issuer."

Once again, the Committee appreciates the opportunity to submit these comments. Members of the Committee are available to meet and discuss these matters with FINRA and its staff and to respond to any questions.

Very truly yours,

/s/ Jeffrey W. Rubin
Jeffrey W. Rubin
Chair, Federal Regulation of Securities Committee

Drafting Committee:
David M. Katz
Mark T. Lab
Peter W. LaVigne
Marianne McKeon
James C. Munsell
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Via email to: Pubcom@FINRA.org

Mr. Joseph E. Price
Senior Vice President, Corporate Financing/Advertising Regulation
c/o Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K St NW
Washington, DC 20006-1506

Dear Mr. Price:

ALPS Distributors, Inc. (CRD#16853) writes for the express purpose of endorsing certain provisions of FINRA's proposed amendment to Rule 5110 that would eliminate the filing requirement for exchange traded funds ("ETFs") structured as grantor trusts. As noted within Regulatory Notice 12-27, many of the provisions within the Corporate Financing Rule regarding underwriting terms and arrangements are not designed for the typical ETF distribution methodology by which a basket of underlying assets is exchanged for creation units of shares of the ETF. We note specifically as follows:

- The information requested by the staff of the FINRA Department of Corporate financing ("the Staff") within Rule 5110 is not reflective of the process by which shares of ETFs structured as grantor trusts are brought to market. Specifically, the following rule sections do not appear applicable to ETFs within the spirit of the rule:
    - 5110(a)(3) Offering Proceeds: Public offering price ("POP") of all securities offered to the public… : The creation and redemption process does not contemplate a specific public offering price. The price at which ETF shares trade is market-driven and the primary method of share issuance contemplates an in-kind exchange of shares for creation units, rather than the traditional POP of an open-end or closed-end mutual fund. In addition, there are no securities received by an "underwriter" as contemplated by the rule.
    - 5110(a)(6) Underwriter and Related Persons: Because ETFs are not sold through a traditional underwriting syndicate, this definition may not apply to these products.
    - 5110(b)(4)(C) Requirements for Filing: This section of the rule specifically contemplates a managing underwriter and any other members that propose to participate in the

offering. As noted above, the basic structure of an ETF and the methodology by which shares come to market does not support a managing underwriter and supporting syndicate of broker-dealers.

- 5110(b)(5)(A)(ii) Documents to be Filed: This section of the rule specifically requests copies of "any proposed underwriting agreement, agreement among underwriters, selected dealers agreement, agency agreement, purchase agreement..." The documents required to be filed under this rule section are applicable to a more traditional means of bringing shares to market, rather than the primary means by which ETF shares are created and redeemed via in-kind exchange of existing shares for creation units.
- 5110(b)(6): Information Required to be Filed: This section contemplates information such as maximum POP, underwriting discount and commission, transfer of issuer securities to the underwriter, all of which do not apply to most situations regarding ETF launches.
- 5110(c)(2)(D) Amount of Underwriting Compensation: For purposes of determining the currently effective guidelines of the maximum amount of underwriting compensation, factors listed include "the amount of risk assumed by the underwriter and related persons, which is determined by: a) whether the offering is being underwritten on a "firm commitment" basis or "best efforts" basis; and b) whether the offering is an initial or secondary offering." This language clearly contemplates a traditional underwriting model, whereas for ETFs, there is no risk to a member firm that acts to promote the fund, as there is no traditional underwriting process on a firm commitment or best efforts basis.
- 5110(c)(3)(A) Items of Value: Items of value to be included in the determination of underwriter compensation encompass traditional underwriter compensation ,such as underwriter discounts and commissions, as well as securities received by a firm in exchange for private placement-related services. Many of the items within this section do not apply to the process by which ETFs are brought to market.
- 5110(c)(3)(B) Exemptions from the definition of Items of Value: This rule section specifically lists those expenses typically incurred by broker-dealers that assist an issuer in raising awareness of the fund prior to launch and afterward. Examples include printing costs, "blue sky" registration costs, FINRA licensing and filing fees and cash compensation. As FINRA has already eliminated many of the costs related to ETF initial distribution from its list of "items of value," the proposed rule change is consistent with these exclusions.

As the Staff notes within the text of Regulatory Notice 12-27, ETFs, which are unique in their methodology and do not mirror those other products contemplated for filing by Rule 5110, should be approached consistently in their regulation, without regard to the chosen legal structure. The primary reason that these products are not currently exempted from the filing and approval requirements of the Corporate Financing Rule is due to the nature of the products in which they invest, which do not qualify the ETFs for registration as Registered Investment Companies under the Investment Company Act of 1940 ("1940 Act"). However, these ETFs structured as grantor trusts operate in much the same way as

those ETFs registered under the 1940 Act and their shares are routed into the public markets in much the same manner. While there are certain differences in registration requirements under the various securities acts, the mechanism by which ETF shares are brought to the public markets, via in-kind exchange of securities for creation units, is consistent amongst ETFs. Equally relevant, it does not mimic the mechanisms of other securities contemplated by Rule 5110, or the more traditional method of underwriting applicable to those products.

As proposed, the language of revised Rule 5110 would exempt ETFs that are structured as grantor trusts and include in their portfolios commodities, currencies or other assets that are not securities. While the language, as worded, is consistent with FINRA's statement that "ETFs should be treated consistently, without regard to the chosen legal structure," the qualifying language regarding portfolio holdings may serve to limit the proposed exemption for future ETF structures not yet contemplated within the markets. We suggest removing the limitation on portfolio holdings and including all ETFs within the filing exemption.

For the reasons listed above, ALPS Distributors, Inc. supports FINRA's proposed elimination of the requirement for filing with the Department of Corporate Financing those ETFs registered as grantor trusts under the Securities Act of 1933. Should you have any additional questions, please feel free to contact or Steven Price or Bradley Swenson at (303) 623-2577.

Sincerely,

Bradley J. Swenson, Chief Compliance Officer
ALPS Distributors, Inc.

cc: Steven B. Price, Deputy Chief Compliance Officer
ALPS Distributors, Inc.

EXHIBIT 5

Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

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5000. SECURITIES OFFERING AND TRADING STANDARDS AND PRACTICES

5100. SECURITIES OFFERINGS, UNDERWRITING AND COMPENSATION

5110. Corporate Financing Rule — Underwriting Terms and Arrangements

(a) No Change.

(b) Filing Requirements

(1) through (4) No Change.

(5) Documents to be Filed

(A) The following documents relating to all proposed public offerings of securities that are required to be filed under paragraph (b)(4) above shall be filed [with] <u>through</u> FINRA<u>'s electronic filing system</u> for review:

(i) [Three copies of the] <u>The</u> registration statement, offering circular, offering memorandum, notification of filing, notice of intention, application for conversion and/or any other document used to offer securities to the public;

(ii) [Three copies of any] <u>Any</u> proposed underwriting agreement, agreement among underwriters, selected dealers agreement, agency agreement, purchase agreement, letter of intent, consulting agreement, partnership agreement, underwriter's

warrant agreement, escrow agreement, and any other document that describes the underwriting or other arrangements in connection with or related to the distribution, and the terms and conditions relating thereto; and any other information or documents that may be material to or part of the said arrangements, terms and conditions and that may have a bearing on FINRA's review;

(iii) [Three copies of each] Each pre- and post-effective amendment to the registration statement or other offering document, [one] with a copy marked to show changes; and [three (3) copies of] any other amended document previously filed pursuant to subparagraphs (i) and (ii) above, [one] with a copy marked to show changes; and

(iv) [Three copies of the] The final registration statement declared effective by the SEC or equivalent final offering document and a list of the members of the underwriting syndicate, if not indicated therein, and one copy of the executed form of the final underwriting documents and any other document submitted to FINRA for review.

(B) [All documents] Documents that are filed with the SEC through the SEC's Electronic Data Gathering, Analysis, and Retrieval ("EDGAR") System that are referenced in FINRA's electronic filing system shall be treated as filed with FINRA.

(6) No Change.

(7) Offerings Exempt from Filing

Notwithstanding the provisions of subparagraph (1) above, documents and information related to the following public offerings need not be filed with FINRA for review, unless subject to the provisions of Rule 5121(a)(2). However, it shall be deemed a violation of this Rule or Rule 2310, for a member to participate in any way in such public offerings if the underwriting or other arrangements in connection with the offering are not in compliance with this Rule or Rule 2310, as applicable:

(A) through (E) No Change.

(F) exchange offers of securities where:

(i) No Change.

(ii) the company issuing securities qualifies to register securities with the SEC on registration statement Forms S-3, F-3, or F-10, pursuant to the standards for those Forms as set forth in subparagraphs (C)(i) and (ii) of this paragraph; [and]

(G) offerings of securities by a church or other charitable institution that is exempt from SEC registration pursuant to Section 3(a)(4) of the Securities Act[.]; and

(H) offerings of securities issued by a pooled investment vehicle, whether formed as a trust, partnership, corporation, limited liability company or other collective investment vehicle, that is not registered as an investment company under the Investment Company Act and has a class

of equity securities listed for trading on a national securities exchange; provided that such equity securities may be created or redeemed on any business day at their net asset value per share.

(8) through (9) No Change.

(c) Underwriting Compensation and Arrangements

(1) No Change.

(2) Amount of Underwriting Compensation

(A) No Change.

(B) For purposes of determining the amount of underwriting compensation, all items of value received or to be received from any source by the underwriter and related persons which are deemed to be in connection with or related to the distribution of the public offering as determined pursuant to subparagraph[s] (3) [and (4)] below shall be included.

(C) through (E) No Change.

(3) No Change.

(d) 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 (C) No Change.

(D) [The payment of any] Any compensation by an issuer to a member or person associated with a member in connection with an offering of securities that is not completed according to the terms of agreement between the issuer and underwriter, except: [those negotiated and paid in connection with a transaction that occurs in lieu of the proposed offering as a result of the efforts of the underwriter and related persons and provided, however, that]

(i) the reimbursement of out-of-pocket accountable, bona fide expenses actually incurred by the member or person associated with a member [shall not be presumed to be unfair or unreasonable under normal circumstances.]; and

(ii) a termination fee or a right of first refusal, as set forth in a written agreement between the issuer and the member, provided that:

a. the agreement specifies that the issuer has a right of "termination for cause," which shall include the member's material failure to provide the services contemplated in the written agreement;

b. an issuer's exercise of its right of "termination for cause" eliminates any obligations with respect to the payment of any termination fee or provision of any right of first refusal;

c. the amount of any termination fee must be reasonable in relation to the services contemplated in the agreement and any fees arising from services provided under a right of first refusal must be customary for those types of services; and

d. the issuer shall not be responsible for paying the termination fee unless an offering or other type of transaction (as set forth in the agreement) is consummated within two years of the date the engagement is terminated by the issuer.

[(E) Any "tail fee" arrangement granted to the underwriter and related persons that has a duration of more than two years from the date the member's services are terminated, in the event that the offering is not completed in accordance with the agreement between the issuer and the underwriter and the issuer subsequently consummates a similar transaction, except that a member may demonstrate on the basis of information satisfactory to FINRA that an arrangement of more than two years is not unfair or unreasonable under the circumstances.]

([F])(E) Any right of first refusal provided to the underwriter or related persons to underwrite or participate in future public offerings, private placements or other financings that:

(i) has a duration of more than three years from the date of [effectiveness or] commencement of sales of the public offering or

the termination date of the engagement between the issuer and underwriter; or

(ii) has more than one opportunity to waive or terminate the right of first refusal in consideration of any payment or fee.

(G) through (I) redesignated as (F) through (H).

[(J)](I) When proposed in connection with the distribution of a public offering of securities on a "firm commitment" basis, any over[ ]allotment option providing for the over[ ]allotment of more than 15% of the amount of securities being offered, computed excluding any securities offered pursuant to the over[ ]allotment option.

(K) through (M) redesignated as (J) through (L).

(g) Lock-Up Restriction on Securities

(1) No Change.

(2) Exceptions to Lock-Up Restriction

Notwithstanding paragraph (g)(1) above, the following shall not be prohibited:

(A) the transfer of any security:

(i) through (ii) No Change.

(iii) if the aggregate amount of securities of the issuer held by the underwriter [or] and related persons do not exceed 1% of the securities being offered;

(iv) through (viii) No Change.

(B) No Change.

(h) Non-Cash Compensation

(1) No Change.

(2) Restrictions on Non-Cash Compensation

In connection with the sale and distribution of a public offering of securities, no member or person associated with a member shall directly or indirectly accept or make payments or offers of payments of any non-cash compensation, except as provided in this provision. Non-cash compensation arrangements are limited to the following:

(A) through (B) No Change.

(C) Payment or reimbursement by offerors in connection with meetings held by an offeror or by a member for the purpose of training or education of associated persons of a member, provided that:

(i) associated persons obtain the member's prior approval to attend the meeting and attendance by a member's associated persons is not conditioned by the member on the achievement of a sales target or any other incentives pursuant to a non-cash compensation arrangement permitted by paragraph ([d]h)(2)(D);

(ii) through (iii) No Change.

(iv) the payment or reimbursement by the issuer or affiliate of the issuer is not conditioned by the issuer or an affiliate of the issuer on the achievement of a sales target or any other non-cash compensation arrangement permitted by paragraph ([d]h)(2)(D).

(D) No Change.

(E) Contributions by a non-member company or other member to a non-cash compensation arrangement between a member and its associated persons, provided that the arrangement meets the criteria in paragraph ([d]h)(2)(D).

A member shall maintain records of all non-cash compensation received by the member or its associated persons in arrangements permitted by paragraphs ([d]h)(2)(C) through (E). The records shall include: the names of the offerors, non-members or other members making the non-cash compensation contributions; the names of the associated persons participating in the arrangements; the nature and value of non-cash compensation received; the location of training and education meetings; and any other information that proves compliance by the member and its associated persons with paragraphs ([d]h)(2)(C) through (E).

(i) No Change.

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[1] No Change.

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