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July 13, 2017

Submitted via email to: pubcom@finra.org

Ms. Jennifer Piorko Mitchell
Office of the Corporate Secretary
Financial Industry Regulatory Authority, Inc.
1735 K Street, N.W. Washington, D.C. 20006-1506

**Re: Regulatory Notice 17-15:
Proposed Amendments to the FINRA Corporate Financing Rule**

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 17-15 (the “Notice”), as more fully set forth below.

This letter was prepared by members of the Committee’s Subcommittee on FINRA Corporate Financing Rules. The comments expressed in this 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. Description of the Proposal

FINRA Rule 5110 (commonly known as the Corporate Financing Rule) is the principal FINRA rule regulating compensation received by underwriters participating in public offerings of securities. FINRA Rule 5110 prohibits FINRA member firms and their associated persons from participating in a public offering of securities if the underwriting terms and conditions, including the amount of compensation to be received, are unfair or unreasonable. The Corporate Financing Rule received its last substantial update in 2004 and was the subject of limited revisions to the section of the rule governing “prohibited arrangements” as recently as 2014 (“Current Rule 5110”). With the proposed changes described in the Notice (“Proposed Rule 5110”), FINRA seeks to modernize the Corporate Financing Rule while retaining its core purpose of ensuring that all underwriting compensation received by participating FINRA member firms in connection with a public offering of securities is fair and reasonable.

The Committee strongly supports FINRA's efforts to modernize and streamline the Corporate Financing Rule and believes the proposed changes will be welcomed by member firms. Nonetheless, room for improvement remains in various sections of Proposed Rule 5110, as discussed in our comments below.

II. Selected Proposed Changes in Proposed Rule 5110

A. Filing Requirements

1. Proposed Rule 5110(a)(3) – Timely Filing Requirements

The Committee commends FINRA's proposal to extend the required filing period from one to three business days following the filing of documents with the Securities and Exchange Commission (the "SEC") and agrees that this change should reduce instances of inadvertent late filings. However, we believe FINRA should retain the current reference to reliance on filings made by issuers in Proposed Rule 5110(a)(3)(B) such that a member firm would not be required to make a separate filing if such filing has already been made by the issuer. For example, issuers, through the assistance of counsel, regularly file shelf registration statements subject to the Current Rule 5110 filing requirements prior to engaging underwriters for a specific offering in order to better manage the timing of the review process. Although Footnote 8 to the Notice discusses such situations, we believe a specific reference in Proposed Rule 5110 would be helpful. Alternatively, rather than including the specific reference in Proposed Rule 5110(a)(3)(B), FINRA could clarify the availability of such reliance in the Supplementary Material.

2. Proposed Rule 5110(a)(4) – Documents and Information Required to be Filed

(i) **Proposed Rule 5110(a)(4)(A)(ii).** The Committee supports the modification in Proposed Rule 5110 that codifies current guidance that standard industry forms, such as the agreement among underwriters, are not required to be filed with FINRA in connection with an offering.

(ii) **Proposed Rule 5110(a)(4)(A)(iii).** Proposed Rule 5110 would require the filing of marked pages only when "changes to the offering and the underwriting terms and arrangements" are contained in an amendment to the registration statement. We appreciate that Proposed Rule 5110 seeks to limit the number of additional filings required in connection with each offering, and while this modification is helpful for certain types of "exhibit only" filings and amendments to update financial statements, as a practical matter, the inclusion of the broad reference to "changes to the offering" will limit the utility of this provision. Thus, we recommend that FINRA modify this proposed revision to delete the reference to changes "to the offering" and instead narrow the

requirement to focus on “changes relating to the disclosures made or to be made in any filing pursuant to Rule 5110 that impact the underwriting terms and arrangements for the offering.” In doing so, an additional FINRA filing including marked pages would be required only when the SEC filing contains changes that affect the “underwriting terms and arrangements.” We believe this revision would appropriately capture the documents relevant to FINRA’s review in this context and would alleviate the burden on member firms (and associated time and cost) to make unnecessary administrative filings.

(iii) **Proposed Rule 5110(a)(4)(B)(iv).** The Committee supports FINRA’s decision to eliminate the current representation required to be made by participating members with respect to any association or affiliation with holders of unregistered equity securities acquired during the review period and to limit the required representation with respect to a participating member’s association or affiliation with any 5% beneficial owner of the issuer’s securities to include only the ownership of any class of the issuer’s “equity or equity-linked securities”. However, the Committee requests that FINRA provide additional guidance with respect to this requirement where beneficial owners of 5% or more of any class of the issuer’s equity securities are funds or other types of investment vehicles, which are usually in the form of limited partnerships or limited liability companies. In such cases, the Committee requests that FINRA limit the requirement to include a statement of association or affiliation only with respect to the general partner or investment manager of such fund or investment vehicle, and any limited partner beneficially owning more than 25% of the limited partnership or limited liability company membership interests of the fund or investment vehicle.

(iv) **Proposed Rule 5110(a)(4)(C).** Proposed Rule 5110 adds a new requirement for member firms to file a written notification to FINRA with respect to any underwriting compensation received by a participating member in connection with an offering that was filed with FINRA but that was ultimately not completed according to its terms. Any agreement governing such arrangement would also be required to be filed (presumably, to the extent it has not already been filed pursuant to Proposed Rule 5110(a)(4)(A)(ii)). The Committee notes that if such compensation is received for services actually rendered and/or for out-of-pocket expenses actually incurred in connection with such failed offering in compliance with the requirements of Proposed Rule 5110(f)(4), it is incongruous to treat such payments as underwriting compensation received in connection with a subsequent successful offering. In addition, the Committee believes that the lack of an endpoint for the notification requirement will almost certainly result in confusion and needless violations. We note that issuers may indefinitely suspend the SEC review of their offerings after an initial registration statement is filed with or submitted confidentially to the SEC and when such a suspension results in a protracted delay or the offering is

abandoned indefinitely, it is unclear when the underwriters' obligation to make the notification would be triggered. Therefore, if FINRA believes that this new filing obligation is necessary, the Committee requests that FINRA clarify the purpose of the obligation, confirm that any such payments are tied to the original failed offering and not a subsequent successful offering, and provide a sunset provision for the requirement.

B. Underwriting Compensation

1. Proposed Rule 5110(c) – Securities Acquisitions Not Considered Underwriting Compensation

The Committee generally supports FINRA's revisions to the so-called "Venture Capital Exceptions" from underwriting compensation for securities received by participating members or their affiliates in connection with an issuer's private placements or lending arrangements, particularly with respect to the adjustments to the percentage limits for such acquisitions. However, the Committee encourages FINRA to reconsider the proposed revisions to include the following:

(i) **Timing.** Expand the timing requirement of the Venture Capital Exceptions to allow for application to situations in which the participating member or its affiliate has made its investment in the issuer after the required filing date. The timing restriction, as currently drafted, is a significant detriment to capital formation and is particularly an issue in public offerings that have been substantially delayed and where the issuer is most in need of an infusion of capital. It may also unfairly impact a member firm if it or an affiliate participates in a private offering by the issuer without knowing that the issuer had previously confidentially submitted a registration statement to the SEC and is later invited to join the underwriting syndicate. Furthermore, where all other criteria for any one of the Venture Capital Exceptions is met, the participating member or its affiliate is not preferenced with respect to the other investors by virtue of the fact that the subject transaction occurs subsequent to the initial filing date for the offering.

(ii) **Price and Terms.** In order to meet each of the Venture Capital Exceptions, the participating member must acquire the issuer's securities "at the same price and with the same terms as securities purchased by all other investors." The Committee suggests that this clause be revised such that the participating member may acquire its securities "on no better terms" than the other investors. The Committee notes that member firms may choose to forego voting rights or other indicia of control when purchasing an issuer's securities and such a (detrimental) variation in the purchase terms should not deny a participating member the ability to rely on one of these exceptions.

(iii) **Proposed Rule 5110(c)(1)(B).** The Committee requests that FINRA revise Proposed Rule 5110(c)(1)(B) to read "investment or loan" instead of "investment and loan" in order to make clear that this provision does not require

a participating member or its affiliate to make both an investment in and a loan to the issuer in order to rely on the exception.

2. Supplementary Material .01(a)(3) – Reimbursement of Fees and Expenses of Counsel

Supplementary Material .01 includes “fees and expenses of counsel to participating members (except for reimbursement of “blue sky” fees)” as “underwriting compensation” related to a public offering. The Committee requests that FINRA clarify that fees and expenses of counsel to the underwriters would only be deemed to be underwriting compensation to the extent that such fees are actually paid by or on behalf of the issuer and reimbursement is actually received by a FINRA member.

3. Proposed Supplementary Materials .01(b) – Payments That Are Not Deemed To Be Underwriting Compensation

The Committee requests that FINRA expand the list of payments that are not deemed to be underwriting compensation as follows:

(i) **Bankruptcy Proceedings.** The addition of an exemption for securities acquired by a participating member in connection with a court-approved bankruptcy process.

(ii) **Supplementary Materials .01(b)(11).** The expansion of the exemption for “listed securities purchased in public market transactions” to include the acquisition of “securities that are not deemed restricted securities under Securities Act Rule 144(a)(3).”

4. Proposed Supplementary Material .01(b)(12) – Exemption for Securities Acquired as a Result of an Employee Plan

The Committee supports the expansion of the exclusion for securities received as a result of certain employee benefit plans, but recommends that the exception from underwriting compensation for securities received “through any stock bonus, pension, or profit-sharing plan that qualifies under Section 401 of the Internal Revenue Code (the “IRC”) or a similar plan” be clarified to specifically include securities received under a written compensatory benefit plan in an offering exempt from registration pursuant to Rule 701 under the Securities Act of 1933 (the “Securities Act”). As with IRC Section 401 qualified plans, grants by issuers pursuant to Securities Act Rule 701 plans are for the purpose of compensating employees and are wholly unrelated to any underwriting compensation in connection with a public offering. Furthermore, the need to obtain and review diligence questionnaires from each person who has received securities from the issuer pursuant to such a plan during the review period for an offering in order to confirm that no grant was made to an associated person of an underwriter is extremely burdensome, especially when an offering has been delayed by the issuer and the relevant review period is lengthy. Expressly including Securities Act Rule 701 plans would be in accord with the expanded exemption to “similar plans” in Proposed Rule 5110 and would minimize any interpretive confusion. Moreover, as the reference to “similar

plans” might itself lead to confusion and interpretive questions, we recommend that FINRA also expressly include within the exemption any other “employee benefit plan (as such term is defined in Securities Act Rule 405).”

C. Proposed Rule 5110(d) – Lock-Up Restrictions

The Committee commends FINRA for revising the lock-up restrictions under Proposed Rule 5110(d)(1) to clarify that the 180-day restricted period begins with the date of commencement of sales in the public offering and to minimize the impact of the lock-up restrictions by including some important additional exemptions. However, we note that, as revised, the lock-up restrictions of Proposed Rule 5110 would also potentially expand the current provision in certain respects. In particular, the application of the current provision is limited to “public equity offerings” rather than all offerings and covers only equity securities received in transactions that are not registered with the SEC.

The Committee requests additional clarification and FINRA’s rationale for this proposed change, as it does not appear to us to serve any investor protection motive. In addition, the Committee asks FINRA to provide further guidance with respect to whether it is intended that the lock-up restriction would prevent participating members from selling securities acquired as underwriting compensation in the public offering itself. If that is, in fact, the intent, we would like to understand why FINRA believes such a limitation is necessary given that any such sale would require appropriate disclosure and utilization of a qualified independent underwriter (“QIU”) if applicable under FINRA Rule 5121, which would appear to address any issuer or investor protection concerns.

D. Proposed Rule 5110(e) – Non-Cash Compensation

The Committee notes that FINRA has determined to delay addressing the provisions covering the receipt by member firms of non-cash compensation pending a separate consolidated review of the non-cash compensation rules generally. However, the Committee believes that the provisions of Current Rule 5110, as included in Proposed Rule 5110, governing the receipt any non-cash compensation require more immediate attention. If applied literally, the non-cash compensation provisions state that members may not receive any non-cash compensation other than those limited items set forth in the provision itself, and those items do not include certain forms of non-cash consideration such as securities, derivative instruments or rights of first refusal that are expressly permitted elsewhere in the rule. We believe that such an inherent conflict should not be deferred, but instead should be addressed in the Proposed Rule 5110 amendments.

E. Exemptions from the Filing and/or Rule Compliance Requirements

1. Proposed Rule 5110(g)(1) and FINRA Rule 5121(a)(2) – Issuers Required to File with FINRA due to the Required Participation of a Qualified Independent Underwriter

The Committee requests that FINRA reconsider its requirement that registration statements relating to offerings that would otherwise meet an exemption from the filing requirements pursuant to Proposed Rule 5110(g)(1) be filed with FINRA solely because an offering requires the engagement of a QIU pursuant to FINRA Rule 5121(a)(2). This requirement is outdated because FINRA no longer requires member firms to register to act as a QIU and, instead, relies on each member firm to confirm that it meets the QIU requirements in connection with a particular offering. Accordingly, as a practical matter, FINRA is not engaged in a review of whether the member firm meets the QIU requirements. Moreover, FINRA Rule 5121 requires prominent disclosure of all conflicts of interest as well as QIU arrangements in the prospectus supplement for the related offering. Finally, we note that this requirement regularly causes issuers, which are otherwise exempt from the Current Rule 5110 filing requirements (see discussion of the “experienced issuer” exemption below), to file and pay a filing fee for the aggregate dollar amount of securities originally registered on a shelf registration statement in connection with a single take-down requiring QIU participation, even if only a limited number of securities registered on the registration statement remain unsold or the registration statement is nearing its three-year expiration at the time of the offering. Accordingly, the Committee believes that this filing requirement is unduly burdensome on capital formation, serves no investor protection role and should be removed from Proposed Rule 5110(g)(1).

2. Proposed Rule 5110(g)(1)(C) and (i)(6) – Experienced Issuer Exemption

The Committee appreciates the attempt to streamline the exemption for offerings by issuers that meet the so-called “pre-1992” requirements for filing registration statements on Forms S-3, F-3 and F-10 by incorporating the historical reporting and public float criteria required at that time into the new defined term “experienced issuer”.¹ Including the criteria for the exemption directly in the rule effectively eliminates the need for participating members to consult Notice to Members 93-88 (issued November 1993) and nearly 25-year old registration statement forms just to determine applicable eligibility thresholds.² However, while simpler on its face, the new definition does not

¹ An experienced issuer is an entity with 36 calendar months reporting history preceding the filing of the registration statement and either (i) a minimum of \$150 million aggregate market value of voting stock held by non-affiliates or (ii) a minimum of \$100 million aggregate market value of voting stock held by non-affiliates and a minimum annual trading volume of such stock of three million shares (mirroring the thresholds for eligibility to file on SEC Form S-3 that existed prior to October 21, 1992).

² See, e.g., FINRA (then NASD) Notice to Members 93-88, available at http://finra.complanet.com/en/display/display_main.html?rbid=2403&element_id=1551.

benefit from related SEC and FINRA interpretive guidance, including guidance published as part of Notice to Members 93-88. Therefore, the Committee believes that this approach will lead to additional confusion, interpretive questions and calculation issues when determining whether issuers can rely on this exemption.

More fundamentally, however, the Committee believes that even the proposed criteria is outdated and no longer appropriate. Instead, an exemption from the FINRA filing requirement should be available to any issuer that is eligible to file a registration statement under the SEC's current requirements for such forms. Currently, issuers that do not meet the "pre-1992" exemption are required to file both the base prospectus and all related prospectus supplements relating to any takedown offerings (or just the base prospectus for well-known seasoned issuers ("WKSIs")), which, after receiving "immediate clearance," are subject to potential post-offering review. If all offerings, filed or not, are subject to the same post-offering review, the Committee questions the value to issuers and investors of this filing requirement. Furthermore, the Committee is concerned that this requirement disproportionately burdens issuers most in need of capital, including younger, smaller issuers. Finally, with respect to WKSI issuers, the Committee finds FINRA's continued retention of the requirement for WKSIs to file base prospectuses unsupportable because (i) FINRA does not review base prospectuses and (ii) Proposed Rule 5110 does not provide for any required disclosure regarding underwriting compensation in the base prospectus.

If, however, FINRA believes that limiting the exemption beyond the current requirements for Forms S-3, F-3 and F-10 is necessary for the protection of investors, the Committee requests that FINRA consider revising the experienced issuer definition to also cover issuers with a 12 month reporting history if they have (i) a public float of at least \$75 million and (ii) an average daily trading volume (as defined by Regulation M) in their common equity securities of at least \$1 million. The Committee also requests that FINRA include issuers that meet these criteria that are filing on Form N-2 as eligible for this exemption.

3. Proposed Rule 5110(g)(1)(E) – Exchange Offers

The Committee requests that FINRA revise the exemption from the filing requirements for exchange offers to include situations where the securities to be acquired in the exchange are convertible into securities that are "listed on a national securities exchange as defined in Section 6 of the Exchange Act." Furthermore, the Committee notes that, in many cases, the role played by FINRA members acting as distribution managers in connection with an exchange offer is limited to contacting investors and recording their intention to tender, as indicated by the nominal compensation received for such services. Accordingly, we request that FINRA consider exempting from the filing requirements exchange offers where the compensation to be received by the distribution manager does not exceed 2% of the registered aggregate dollar amount of the offering and no FINRA member acts as an underwriter for the securities.

4. Proposed Rule 5110(g)(1)(H) – Exemption from the Filing Requirements for Offerings by “Closed-End” Investment Companies that are Operated as “Tender Offer Funds”

Proposed Rule 5110 includes a new exemption from the filing requirements for certain offerings by “tender offer funds.” The exemption is limited to follow on offerings by such issuers only if such issuer has previously filed its initial public offering with FINRA. FINRA’s stated rationale in the Notice with respect to this exemption is that such offerings are adequately covered by the requirements of FINRA Rule 2341 and the Investment Company Act of 1940, as amended. The Committee notes that the same rationale should cover initial public offerings by such entities. In practice, FINRA has agreed that the underwriting limits of such issuer’s offerings should be governed by FINRA Rule 2341, but has required a formal exemption request process for an offering specific exemption from the requirements for Current Rule 5110. This approach is unduly burdensome on member firms. Therefore, if FINRA intends to continue to require the filing of initial public offerings by such issuers under Proposed Rule 5110, the Committee requests that FINRA clarify in Proposed Rule 5110 that the underwriting terms and arrangements for such offerings, while subject to the filing requirements of the Rule, will be reviewed for compliance with the requirements of FINRA Rule 2341.

5. Proposed Rule 5110(g)(2)(L) – Public Utility Holding Company Act Exemption

The Committee requests clarification as to whether the exemption from the filing and rule compliance requirements of Proposed Rule 5110 for “securities issued pursuant to a competitively bid underwriting arrangement meeting the requirements of the Public Utility Holding Company Act” remains tied to the requirements of the Public Utility Holding Company Act, which was repealed effective 2005 and replaced by the Energy Policy Act of 2005.

F. Proposed Rule 5110(h) – FINRA Rule 9600 Exemption Requests

The Committee notes that as revised in Proposed Rule 5110, a request for an exemption “from any or all of the provisions of this Rule that [FINRA] deems appropriate” may be granted “in exceptional and unusual circumstances, taking into consideration all relevant factors.” In contrast, under Current Rule 5110, FINRA may grant an exemption “for good cause shown” where such grant would be “consistent with the purposes of the Rule, the protection of investors, and the public interest.” The Committee questions whether this revision is intended to signal a change to the standard of review for exemption requests, and if so would like to understand the rationale for such a change. First, the Committee believes that the reasons for granting such an exemption should not be tied to the rarity of the situation, but rather its merits. Second, the Committee believes that this change in terminology represents a marked decrease in clarity compared with the more fully elucidated standard of review under Current Rule 5110. This lack of clarity could lead to inconsistent and potentially arbitrary results.

G. Proposed Rule 5110(i) – Definitions

1. Proposed Rule 5110(i)(2) – Bank

Proposed Rule 5110 helpfully expands and clarifies the exemption from the filing requirements for issuers with outstanding investment grade-rated debt (other than in respect of the issuer’s initial public equity offering) to expressly include banks.³ However, while Proposed Rule 5110(i)(2) provides that the term “bank” – for purposes of paragraph (c) of the Rule – includes only the regulated entity and paragraph (c) limits the exemption for banks to those entities defined pursuant to Section 3(a)(6) of the Exchange Act for the purposes of the exception from underwriting compensation under Proposed Rule 5110(c)(1)(A), the term “bank” is not defined for purposes of the exemption for banks under Proposed Rule 5110(g)(1). As the purpose of the filing exemption is to exempt offerings by issuers of investment grade-rated debt, such exemption should not be limited to Section 3(a)(6) banks, which definition is largely limited to U.S. domiciled banks and U.S.-based branches of non-U.S. banks. Accordingly, the Committee believes that the exemption unintentionally excludes non-U.S. bank issuers. The Committee requests that FINRA further clarify this exemption to expressly include non-U.S. banks either by including a new definition of bank or by adding further clarification to the exemption for issuers with outstanding investment grade-rated debt.

2. Proposed Rule 5110(i)(15) – Participating Member

The Committee agrees with FINRA that the term “participating member” should not include the “issuer,” but suggests that the definition be modified as follows to clarify this intent: “The term ‘participating member’ means any FINRA member that is participating in a public offering, any affiliate or associated person of the member, and any immediate family thereof, but does not include the issuer.”

3. Proposed Rule 5110(i)(18) – Public Offering

Proposed Rule 5110(i)(18) would define a public offering as “any primary or secondary offering of securities made pursuant to a registration statement, offering circular or similar offering document including exchange offers, rights offerings, and offerings of securities made pursuant to a merger or acquisition.” FINRA stated that adding the definition to Proposed Rule 5110 would allow it to delete the corresponding definition from FINRA Rule 5121⁴ and incorporate all of the Proposed Rule 5110 definitions into FINRA Rule 5121 by reference.

³ See Proposed Rule 5110(g)(1)(A). In this regard, we also suggest that FINRA further clarify this exemption from the filing requirements by revising it to also include (in addition to “corporations”) issuers that are limited liability companies, limited partnerships, business trusts or other legal persons.

⁴ FINRA has included this definitional change to FINRA Rule 5121 in the proposed amended rule language included in Attachments A and B to the Notice.

First, the Committee recommends that FINRA consider revising the definition to clarify that a public offering is “any primary or secondary distribution of securities made in whole or in part in the United States to the public,” which the Committee believes avoids circularity and more accurately reflects the types of offerings intended to be covered by Proposed Rule 5110.

Second, we note that in transferring the definition of public offering from FINRA Rule 5121 to Proposed Rule 5110, FINRA has removed from the definition the clarifying exclusions for offerings of exempted securities as defined in Section 3(a)(12) of the Securities Exchange Act of 1934 (the “Exchange Act”) and offerings made pursuant to (i) Securities Act Sections 4(a)(1), 4(a)(2), or 4(a)(6), (ii) Securities Act Rules 504 (if the securities are “restricted securities” under Securities Act Rule 144(a)(3)), 505⁵ and 506, and (iii) Securities Act Rule 144A or SEC Regulation S, and has instead included these types of offerings in the list of offerings not subject to this Rule and FINRA Rules 2310 and 5121 under paragraph (g)(2). The Committee believes that the original formulation of the definition currently included in FINRA Rule 5121 is the clearer and more direct approach. As proposed, the participating member would, for example, be required to treat private placements and Regulation S offerings as “public offerings” but ones that are then exempted from the filing and compliance requirements of Proposed Rule 5110 and the compliance requirements of FINRA Rules 2310 and 5121, which is likely to lead to unnecessary confusion and interpretive issues. Therefore, the Committee requests that FINRA return to the current formulation of including the exemptions for these types of offerings within the definition of public offering when it moves the definition from FINRA Rule 5121 to Proposed Rule 5110. While the addition of the reference to “distributions” made “in whole or in part in the United States to the public” (as we propose in the immediately preceding paragraph) should help clarify the issue, we continue to believe the inclusion of the specified exclusions remains important to reduce interpretive questions. In addition, the Committee believes that the list of offering types that do not constitute a “public offering” should also expressly include offers and sales of securities pursuant to Sections 4(a)(3) and 4(a)(4) of the Securities Act and that the reference in Proposed Rule 5110(i)(18) to “Section 4(a)(6)” should instead refer to “Section 4(a)(5).”⁶

4. Proposed Rule 5110(i)(20) -- Review Period

The Committee supports the addition of the new definition clarifying and codifying the review periods essential for determining which payments, rights, interests or other benefits are required to be included as underwriting compensation for an offering. In particular, the Committee appreciates the express inclusion of durations that vary depending on the type of offering. We note that Proposed Rule 5110 clarifies the

⁵ Securities Act Rule 505 was repealed effective May 22, 2017. See SEC release No. 33-10238 (Oct. 26, 2016).

⁶ We note that former Section 4(6) of the Securities Act (which is referred to in the FINRA Rule 5121 definition of public offering) was redesignated as Section 4(a)(5) in connection with the adoption and implementation of the Jumpstart Our Business Startups Act of 2012.

understanding that the review period for either a firm commitment or a best efforts takedown offering under a shelf registration statement begins 180 days prior to the required filing date of the takedown and continues through to the 60th day following the final closing of the same takedown. However, the Committee requests additional guidance from FINRA with respect to when the review period would end for offerings with an indeterminate time period such as at-the-market offerings, which may continue for several years. The Committee also questions why FINRA has chosen to limit the review period specified in Proposed Rule 5110(i)(20)(C) to “firm commitment or best efforts takedown or any other continuous offering on behalf of *securityholders...*” and requests that FINRA revise this definition to include the issuer. As currently proposed, the reference to “on behalf of selling securityholders” appears to qualify “firm commitment”, “best efforts” and “other continuous offering” for the purpose of the review period definition, which we do not believe was intended.

H. FINRA Rule 5121 -- Public Offerings of Securities With Conflicts of Interest

Given the inter-relationship between FINRA Rules 5110 and 5121, FINRA’s inclusion of the full text of FINRA Rule 5121 in the Notice, and FINRA’s request in Regulatory Notice 17-14 for comments on the capital formation rules more generally, the Committee would like to take this opportunity to also comment on certain aspects of FINRA Rule 5121 that we believe unnecessarily impede smooth execution of public offerings.

1. FINRA Rule 5121(a)(1)(A) – “Primarily Responsible for Managing the Public Offering”

The Committee requests that FINRA clarify the meaning of “primarily responsible for managing the public offering” with respect to the conflicts of interest requirements under FINRA Rule 5121, as this reference continues to raise interpretive questions for member firms. We note that appointing a QIU increases the time and expense of a transaction because the issuer must be educated on the topic; a QIU must be identified and, in some cases, added to the transaction at a late stage in the transaction; and additional provisions to the underwriting agreement must be negotiated. The Committee believes that a QIU should be necessary only when *all* the lead managers or bookrunners have a conflict of interest and the offering does not meet the requirements of FINRA Rule 5121(a)(1)(B) or (C).

2. FINRA Rule 5121(f)(3) – Bona Fide Public Market

The Committee requests that FINRA clarify the definition of “bona fide public market”. As currently drafted, the definition states that a bona fide public market exists if the issuer of the offered securities has at least one series of securities “traded on a national securities exchange with an Average Daily Trading Volume (as provided by SEC Regulation M) of at least \$1 million.” However, we understand that the quoted language is intended to be applied consistent with FINRA Rule 5121(a)(1)(B) -- *i.e.*, that the securities being offered in the public offering have a bona fide public market. If this

is the correct interpretation, we urge FINRA to take this opportunity to eliminate the continuing confusion as to the proper application of this provision and make appropriate changes to the definition to make the intention clear. Furthermore, the Committee requests that FINRA consider including an exception for offerings of securities convertible into securities meeting the bona fide public market definition for the purposes of FINRA Rule 5121(a)(1)(B).

3. FINRA Rule 5121(f)(6) – Definition of Control

The Committee notes that this definition of control is inconsistent with either the SEC’s definition of control or with other FINRA measures of control, primarily because it establishes an unreasonably low control threshold at 10% beneficial ownership. As a result, members and issuers have had to include as “affiliates” for purposes of the FINRA Rule 5121 analysis persons or entities they would not, under ordinary circumstances, consider to be within a “control” relationship. Accordingly, we believe FINRA should revise this definition to use a 25% beneficial ownership threshold, consistent with the definition used for purposes of Form BD.⁷

We also request that FINRA delete the reference in the definition to beneficial ownership of preferred equity as a trigger for control. FINRA made a similar change when it eliminated beneficial ownership of subordinated debt in 2014 and stated that such ownership was “not a meaningful measure of control or affiliation” for purposes of FINRA Rule 5121,⁸ which reasoning we believe applies equally to preferred equity.

* * *

⁷ Form BD defines “control” as: “The power, directly or indirectly, to direct the management or policies of a company, whether through ownership of securities, by contract, or otherwise. Any person that (i) is a director, general partner or officer exercising executive responsibility (or having similar status or functions); (ii) directly or indirectly has the right to vote 25% or more of a class of a voting security or has the power to sell or direct the sale of 25% or more of a class of voting securities; or (iii) in the case of a partnership, has the right to receive upon dissolution, or has contributed, 25% or more of the capital, is presumed to control that company.”

⁸ SEC Release No. 34-71372 (Jan. 23, 2014). In this regard, we also note that the definition of “subordinated debt” set forth in FINRA Rule 5121(f)(13) is no longer used in FINRA Rule 5121 or Proposed Rule 5110 and should therefore be deleted.

Ms. Jennifer Piorko Mitchell
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The Committee greatly appreciates the opportunity to provide its comments with respect to this important rule-making effort and thanks the FINRA staff for its efforts and thoughtful approach to the issues addressed by the proposed amendments. Members of the Drafting Committee are available to meet and discuss these matters with the FINRA staff and to respond to any questions.

Very truly yours,

/s/ David M. Lynn

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