NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC.

NASAA

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March 12, 2004

Ms. Barbara Z. Sweeney
NASD
Office of the Corporate Secretary
1735 K Street, NW
Washington, DC 20006-1500

Via e-mail to pubcom@nasd.com

**RE: Comments on Proposed Amendments to NASD Rules 2710 (Corporate Financing) and 2810 (Direct Participation Programs)**

Dear Ms. Sweeney:

The North American Securities Administrators Association, Inc. (NASAA) appreciates the opportunity to comment on the Proposed Amendments to NASD Rules 2710, Corporate Financing, and 2810, Direct Participation Programs (DPPs). These proposals were included in Notice to Members (NtM) 04-07, posted February 3, 2004.

**RESCISSION OF NASD INTERPRETIVE POLICY REGARDING TRAIL COMMISSIONS CHARGED BY COMMODITY DPPS**

NASD members must file with NASD's Corporate Financing Department information about public offerings of securities to insure compliance with Rules 2710 and 2810. These Rules limit organization and offering (O&O) expenses, including underwriting compensation. Since 1982, trail commissions for sale of commodity DPPs have been excluded from the limitation on underwriting compensation. The NtM proposes to rescind this policy.

NASAA supports the proposal to include trail commissions within the limitations on compensation. Compensation for all DPPs is high. Under existing NASD policy, compensation is not capped when trail commissions are involved. Uncapped trail commissions result in very high selling compensation in commodity pool offerings. This puts the compensation payable for such offerings far out of line with that payable for other types of offerings.

We also note that current disclosure practices in commodity pool prospectuses make it difficult for investors to detect and understand the trail commissions. Trail commissions are typically payable out of the pool's "commodity trading costs." Embedding the trail commissions in trading costs makes it harder for investors to understand the actual costs of commodity trading and harder to spot the trail commissions. Because trail commissions may now be paid over many years, it is difficult for investors to understand how much broker compensation will be paid for a multi-year investment in a commodity pool. The steep differential in compensation also raises serious conflict of interest and investor suitability issues. We commend NASD for addressing the matter.

## PROPOSED AMENDMENTS TO PROHIBIT SALES LOADS ON REINVESTED DIVIDENDS IN REITS, DPPS, AND CLOSED-END FUNDS

NASAA also supports the amendment in the NtM that would prohibit sales loads on reinvested dividends in DPPs, real estate investment trusts (REITs), and closed-end funds. A sales load on reinvested dividends is another means to increase overall sales commissions. Investors generally perceive dividend reinvestment plans as transactions without expenses.

## PROPOSED AMENDMENTS TO THE NON-CASH COMPENSATION PROVISIONS IN THE RULES REGARDING THE "APPROPRIATE" LOCATION FOR TRAINING AND EDUCATION MEETINGS

The existing non-cash compensation provisions of NASD rules permit payments and reimbursements by an offeror for training and education meetings if certain conditions are met, including that the location is "appropriate." The NtM would include as appropriate for *bona fide* training and education those locations where significant DPP or REIT properties are located. NASAA does not object to this provision as long as program sponsors do not use "education" meetings as bonuses to agents for selling DPP or REIT products. Seminars labeled by sponsors and their affiliated dealers as training and education may be prone to abuse. We therefore encourage NASD to carefully review agendas and handout materials for such meetings to insure they meet the stated criteria. NASD also should make sure that associated persons attending such sessions are not unduly influenced by free entertainment or golf outings from the product sponsors.

## PROPOSED AMENDMENTS TO THE NON-CASH COMPENSATION PROVISIONS IN THE RULES TO INCLUDE "EQUAL WEIGHTING" AND "TOTAL PRODUCTION" LIMITATIONS FOR INTERNAL SALES CONTESTS

NASD rules on non-cash compensation prohibit gifts of more than minimal value from DPP and REIT sponsors. However, sponsors have been permitted in certain instances to provide incentives or rewards to individual broker/dealers and their registered representatives for selling the sponsors' products. Such incentives have conflict-of-interest and supervision implications. The NtM would make Rules 2710 and 2810 consistent with Rule 2820, which applies to variable contracts. An internal sales contest with respect to DPPs, for example, would have to be based on the total of an associated person's production for all DPP securities distributed by the employing broker-dealer.

While NASAA agrees that the limitations specified by the NtM are helpful, almost any sales contest still can cause conflicts for agents in providing suitable advice to clients. NASD should scrutinize sales contests carefully. Such scrutiny should include the reason a contest is necessary, the type and amount of remuneration offered, and whether disclosure to investors of special incentives is warranted.

Thank you for the consideration of these views. Should you have any questions, please contact Denise Voigt Crawford, Chair of NASAA's Corporation Finance Section and Texas Securities Commissioner, or Rebecca J. Alford. Chair of NASAA's Direct Participation Programs Policy Project Group, and Director of the Division of Corporate Finance for the Pennsylvania Securities Commission.

Sincerely,

Ralph A. Lambiase
NASAA President and
Director, Connecticut Division of Securities