



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.

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,

A handwritten signature in cursive script, appearing to read "Sean Davy", with a long horizontal flourish extending to the right.

Sean Davy

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

Attachment

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).