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November 10, 2011

Via E-mail

Elizabeth M. Murphy,
Secretary,
Securities and Exchange Commission,
100 F. Street, NE,
Washington, DC 20549-1090.

Re: SR-FINRA-2011-057.

Dear Ms. Murphy:

We appreciate the opportunity to comment on Rule 5123 proposed by the Financial Industry Regulatory Authority, Inc. ("FINRA").

The proposed rule would prohibit members and persons associated with a member from offering or selling a security in reliance on an exemption from registration under the Securities Act of 1933 (which the proposed rule refers to as a "private placement"), or from participating in the preparation of a private placement memorandum, term sheet or other disclosure document in connection with such a "private placement", unless the member or associated person provides to each investor, prior to sale, information about the anticipated use of the offering proceeds and the amount and type of offering compensation and expenses. Additionally, the participating member or associated person would be required to file with FINRA the document containing the required information and any material amendments to the document.

We believe that the proposed rule's definition of "private placement", if applied literally, would be simply unworkable. The definition should be revised to focus on the non-public offerings which FINRA has indicated it is actually seeking to address. We also suggest below a number of additional changes to the proposed rule.

Definition of "Private Placement"

Because the proposed rule defines "private placement" by reference to Securities Act exemptions, the definition has to be analyzed in light of the structure of that Act. The Securities Act of 1933 contains (in Section 5) a general prohibition of unregistered offers and sales of securities involving the jurisdictional means, subject to a variety of exemptions which, broadly speaking, could be grouped into three categories:

- exemptions that permit non-public or limited offerings, generally referred to as "private placements" (for example, Sections 4(2), 4(5) and 3(b), and rules promulgated thereunder),

- exemptions that permit secondary market trading (for example, Sections 4(1), 4(3) and 4(4)), and

- exemptions reflecting a policy judgment that, under the specified conditions, the protections of Securities Act registration are not required (for example, Sections 3(a)(2), 3(a)(9) and 3(a)(10)).

We believe, based on FINRA's explanations, that proposed Rule 5123 is intended to address concerns with transactions being effected pursuant to the first category of Securities Act exemptions. The proposed rule's definition of "private placement" should be revised accordingly. This could be done by adding references to the specific Securities Act exemptions covered by the rule, or by replacing the definition with a reference to the definition of "private placement" in FINRA Rule 5122 (which is specifically limited to "non-public offering[s]").

Whatever approach is adopted, it is essential that transactions pursuant to the second category of Securities Act exemptions be excluded from operation of Rule 5123. Substantially all secondary market trading is effected pursuant to one or more of these exemptions. It will not be possible for members to comply with Rule 5123 in connection with ordinary secondary market trading. But the proposed rule's definition of "private placement", because it picks up this second category of Securities Act exemptions, literally encompasses such trading transactions. The definition therefore needs to be modified.

Application of the proposed rule to transactions covered by the third category of exemptions arguably raises a variety of more complex questions. Proposed Rule 5123 contains exemptions for certain Section 3(a)(2) and Section 3(a)(3) transactions, but it is very hard to understand why other transactions covered by those sections, or transactions subject to other Section 3(a) exemptions – for example, Section 3(a)(10) (transaction subject to a fairness hearing), or Section 3(a)(9) (exchange transaction with an existing holder, where no one is paid to solicit the exchange) – or transactions subject to Section 1145 of the Bankruptcy Code, are not also excluded. While members are not always involved in such transactions, to the extent they are,

application of the proposed rule would add a layer of regulatory and compliance complexity, for no apparent reason. We therefore submit that in revising the "private placement" definition of the proposed rule, FINRA should carefully consider how the rule would apply to transactions covered by the Section 3(a) exemptions, and why.

Other Comments

As currently proposed, Rule 5123(b) would require each member in a selling group to file the required private placement disclosure document with FINRA. We think this will result in needless inefficiencies; members should, if they choose, be permitted to file on a joint or coordinated basis. It is unclear how having one member file on behalf of the group would limit FINRA's "timely access to information about the private placement", as stated in the release. FINRA is free to address any such concern by prescribing the scope and format of the information to be included in any joint filing.

As a drafting matter, we would revise Proposed Rule 5123(c)(8), to delete the reference to "incorporation by reference". Since Forms S-3 and F-3 permit any issuer using them to incorporate by reference, the added language regarding "incorporation by reference" is unnecessary and confusing.

Finally, proposed Rule 5123(b) is unclear as to the timing of the required filing of amendments to a disclosure document. Under this provision, an initial disclosure document is required to be filed no later than 15 calendar days after the time of first sale, but an amendment to a disclosure document must be filed no later than 15 calendar days after such document is provided to investors. The provision should be amended to make clear that an amendment to the disclosure document prior to the time of first sale need not be filed earlier than the filing of the initial disclosure document.

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Once again, we appreciate the opportunity to submit these comments. If you have any questions please contact David Harms at 212-558-3882 or Robert Buckholz at 212-558-3876.

Sincerely,

Sullivan & Cromwell LLP

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