LPL Financial

Steve Morrison
Senior Vice President
Associate Counsel

75 State Street, 24th Floor
Boston, MA 02109
[redacted]
617 897 4095 office
800 775 4575 ext. 4095
617 556 4002

March 12, 2014

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

Re: File No. SR-FINRA-2014-006, Proposed Rule Change Relating to Per Share Estimated Valuations for Unlisted DPPs and REITS

Dear Ms. Murphy:

We appreciate the opportunity to comment on the proposed amendments to NASD Rule 2340 – Customer Account Statements and NASD Rule 2310 – Direct Participation Programs (collectively, the "Proposed Amendments") addressing values of unlisted direct participation programs ("DPPs") and real estate investment trusts ("REITs") in customer account statements. We are fully supportive of the efforts of the Securities and Exchange Commission ("SEC"), the Financial Industry Regulatory Authority ("FINRA") and the industry to increase transparency and provide customers with additional information that is useful when determining the valuation of their DPP and REIT investments. We look forward to continuing to work with FINRA and the SEC to improve upon these proposals.

On February 4, 2009, FINRA first discussed amending the rules related to customer account statements and disclosures to customers in relation to DPPs and REITs with the release of Regulatory Notice 09-09 – Customer Account Statements ("RN 09-09"). If implemented as first proposed, RN 09-09 would have limited the time period that the offering price of DPPs and REITs could be used as a basis for a per share estimated value to the period provided under Rule 415(a)(5) of the Securities Act of 1933 ("Initial Offering Period"). RN 09-09 also would have required firms to deduct organization and offering expenses from the per share estimated values during the Initial Offering Period. Moreover, RN 09-09 would have prohibited a firm from using a per share estimated value, from any source, if it "knows or has reason to know the value is unreliable," based upon publicly available information or nonpublic information that has come to the firm's attention. On September 29, 2011, FINRA revised certain elements of its proposal in Regulatory Notice 11-44 – Customer Account Statements ("RN 11-44"). On March 7, 2012, FINRA again revised its proposal with the release of FINRA Regulatory Notice 12-14 – Customer Account Statements ("RN 12-14" and collectively with RN 09-09 and RN 11-44, the

"Regulatory Notices"). Importantly, RN 12-14 improved upon the previous regulatory notices by requiring firms to show the "Net Offering Price"[1] on customer account statements and removed the requirement that member firms list a DPP or REIT security as unpriced if the member firm "knows or has reason to know that the value is unreliable." On January 31, 2014, FINRA submitted to the SEC its final proposal, which contained additional revisions of the Regulatory Notices. The SEC published this proposal in the Federal Register on February 19, 2014.

As stated above, we are fully supportive of FINRA's goals of providing greater transparency to DPP and REIT investors. We do, however, believe that there are several aspects of the Proposed Amendments that should be modified to better serve investor interests and provide greater transparency. In particular, the Proposed Amendments contained revisions of the Regulatory Notices that would provide for member firms to list the per share estimated price of a DPP or REIT, as determined by such DPP or REIT issuer, provided that the value has been calculated in accordance with the requirements of new FINRA Rules 2340 and 2310 and, more importantly, provided such member firm has "no reason to believe that the per share estimated value is unreliable." For the reasons outlined below, we believe that such an approach will likely lead to less investor transparency and greater customer confusion. In addition, due to the significant costs, operational changes and potential customer reaction to the Proposed Amendments, we believe it would better serve investor interests to provide for a longer implementation period in which to enact the Proposed Amendments.

I. Introduction

LPL Financial LLC ("LPL") is one of the nation's leading diversified financial services companies and is registered with the SEC as both an investment adviser and broker-dealer. LPL currently supports one of the largest independent registered representative bases (referred to herein as "financial advisors") in the United States, providing financial professionals with the front, middle, and back-office support they need to serve the large and growing market for brokerage services and independent investment advice, particularly in the market of investors with $100,000 to $1,000,000 in investable assets. As of December 31, 2013, LPL brokerage and advisory assets totaled $438 billion, of which $151.6 billion was in advisory assets. LPL self-clears its transactions and maintains custody of its brokerage client customer accounts.

LPL is one of the largest distributors of DPPs and REITs to the retail investor marketplace. In 2013, LPL sold in excess of $3.7 billion in REITs and DPP products. We believe that REITs and other DPP products offer investors exposure to non-traditional asset classes that can diversify a portfolio through a security less correlated to the overall market.

[1] Under RN 12-14, Net Offering Price is defined as the gross offering price less upfront underwriting compensation expenses.

II. Reliability of Estimated Values

We believe that permitting broker-dealers to exclude the per share estimated value for an unlisted DPP or REIT security will, contrary to best intentions, lead to a decrease in investor transparency. As discussed in our previous comment letters to the Regulatory Notices, broker-dealers are not well situated to opine on the appropriateness of the valuations provided by issuers of DPP and unlisted REIT products. While we appreciate that the intention is to provide additional checks and safeguards on the reliability of the valuations provided by issuers, we are concerned that shifting the valuation burden to the broker-dealer community will necessarily lead to less complete information being provided to investors. In particular, the Proposed Amendments' requirements that a broker-dealer have no reason to believe that the per share estimated value is unreliable would, absent the implementation of the "not priced" option under the Proposed Amendment, inevitably lead to unnecessary litigation. As a result, we believe that broker-dealers with significant exposure and distribution to this segment of the market would likely choose to display the per share estimated value as "not priced," to ensure that plaintiff's counsel cannot reasonably construct an argument that the broker-dealer should have known that an estimated valuation was inaccurate. This concern is particularly pronounced when an issue experiences a liquidity event and where the valuation that appears the day after such event will be based upon the demand for the issue as opposed to the actual "value" of the security. This disparity may be significant and may cause investors to question whether the estimated per share valuation previously provided on the account statement was appropriate. To avoid this outcome, broker-dealers would instead likely display a "not priced" valuation for the security on customer account statements both to remove the customer confusion and to avoid future litigation.

Further, we believe that the proposed language that a member firm has "no reason to believe that the per share estimated value is unreliable" is overly broad. By definition, an estimated value may be unreliable – particularly as to real property – where the value of the property is based upon a subsequent buyer's willingness to pay. In the case of certain REITs, the estimate relies on assumptions about future occupancy rates and cash flows. Instead, broker-dealers are more appropriately tasked with reviewing the valuation methodologies proposed by DPP and REIT issuers prior to permitting the product to be sold on their platforms. Furthermore, we believe that responsible broker-dealer custodians already have the authority, but not necessarily the obligation, to report that a particular security is "not priced." This option has been used in various circumstances when a broker-dealer has actual knowledge that the valuation of a particular security is incorrect.

The result of the Proposed Amendments, as written, is that investors will receive less, not more, information as to the estimated value of their DPP or REIT position, leading to a significant decrease in transparency even when compared to the current construct. The Proposed Amendment's approach may also have the unintended effect of causing additional customer confusion through perceived losses in net worth or account performance that may result from the issue reflecting a "not priced" valuation.

Instead, we respectfully submit that a better approach is to permit broker-dealers to rely upon the valuation provided by the DPP or REIT issuer, provided such issuer used one of the two

available presumptive valuation methods described in the Proposed Amendments.[2] It is our belief that so long as the DPP or REIT issuer is using these presumptive valuation methodologies, as described in their most recent offering materials, that the broker-dealer community should not be subject to second-guessing the valuations resulting from presumptively appropriate methods. Furthermore we believe that disclosures on account statements describing the valuation methodology would provide customers with the transparency sought by the Proposed Amendments. This solution would ensure that customers are provided an accurate representation as to how the issuer estimated the valuation.[3]

III. Timing of Implementation

FINRA has suggested that the rule changes be effectuated no earlier than 180 days following the SEC's approval of the Proposed Amendments. While FINRA has not proposed an exact timeframe in which to enforce these changes, we believe that the implementation timeframe should be substantial. The Proposed Amendments are not mere window dressing or slight deviations from the construct in place today. Instead, it is our belief that the Proposed Amendments will change how DPPs and REITs are structured in the future, will require significant customer education, will require changes to account statements and disclosures, and will fundamentally and beneficially, change the manner in which DPP and REITs are sold and distributed. Furthermore, there are substantial technical aspects of the Proposed Amendments, as more fully discussed by issuers and industry trade organizations, which we believe will require clarification before the Proposed Amendments' effective date to ensure a smooth transition to these significant new requirements.

In addition, we are concerned that existing DPP and REITs may need to make substantial alterations to the manner in which information is reported to customers. This wholesale shift in reporting could cause customer confusion and alarm. Rather than attempting to effectuate these changes quickly, we think, as an industry, we would be well suited to address these changes in a more methodical and pragmatic manner.

IV. Conclusion

Thank you for the opportunity to comment on the Proposed Amendments. We are highly supportive of the efforts of FINRA and the SEC to improve customer transparency in relation to the per share estimated value of DPP and unlisted REIT securities. We are ardent supporters of DPP and REIT investments and fully believe that such investments should be made available to appropriate investors who fully understand the risks and opportunities such products present.

---

[2] Net Investment or Independent Valuation.
[3] Account statement disclosures would be in addition to other materials provided investors that accurately describe the estimated per share valuation methodologies such as broker-dealer or issuer educational materials, other product offering materials and prospectuses, and public filings.

We look forward to continuing to work with the SEC and FINRA to discuss the best manner by which to implement these proposals and to further the awareness of the investing public about DPP and REIT investments. If you have any questions regarding this letter or would appreciate further dialogue on any of the issues we have discussed, please do not hesitate to contact me.

Sincerely,

Steven Morrison

cc: David Bergers
General Counsel
Sharyn Handelsman
Chief Compliance Officer