

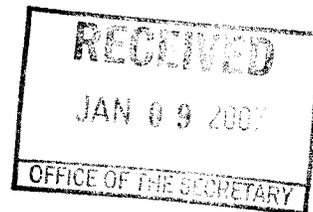
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Robyn A. Huffman
Managing Director
Associate General Counsel

January 5, 2007

Via Email

Ms. Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090



Re: File No. SR-NASD-2003-141, Mark-Up Policy for Transactions in Debt Securities, Except Municipal Securities

Dear Ms. Morris:

Goldman, Sachs & Co. (“Goldman Sachs”) appreciates this opportunity to comment on the proposal by the National Association of Securities Dealers, Inc. (the “NASD”) to adopt an interpretation of its mark-up policy for transactions in debt securities (the “Interpretation”).¹

Goldman Sachs applauds the NASD’s most recent approach to amending the mark-up policy. In particular, we believe that exempting certain transactions between dealers and “qualified institutional buyers” or QIBs (the “QIB Exemption”) is a significant milestone in promoting market liquidity without compromising investor protection, and we commend the NASD for striking this balance. We believe fundamental aspects of this approach apply equally to other debt securities beyond non-investment grade; nevertheless, we think that this proposal is sufficiently significant that it should be adopted as quickly as possible.

We believe that after many years of discussing and revising various versions of this proposal, it is important for market participants to have the greater clarity regarding their debt markup obligations that this Interpretation would provide. This is not to say that the Interpretation could not be modified and improved in important respects. We have reviewed both comment letters submitted by the Securities Industry and Financial Markets Association (“SIFMA”) and generally agree that changes proposed by SIFMA would materially enhance

¹ Notice of Filing of Amendment Nos. 3, 4, and 5 to a Proposed Rule Change Relating to Additional Mark-Up Policy for Transactions in Debt Securities, Except Municipal Securities, 71 Fed. Reg. 68856 (Nov. 28, 2006) (the “Proposing Release”).

the Interpretation. On balance, however, we believe it is important to identify a version of the Interpretation that can be adopted in relatively short order, rather than to have yet more lengthy delays as significant modifications to the Interpretation are identified by the industry and further considered by the NASD and the Commission.

Accordingly, we support adoption of the Interpretation as promptly as practicable. To this end, we set forth below several recommendations regarding how the NASD might address some of the more significant substantive issues that have been raised with respect to the Interpretation, consistent with the overall objective of implementing the Interpretation in relatively short order.

First, we agree in general terms with SIFMA's recommendation that the QIB Exemption be expanded to cover a wider range of privately-placed securities, regardless of rating, and we support this change if it can be made without undue delay in implementing the Interpretation. The main principle supporting the NASD's adoption of the QIB Exemption in the context of non-investment grade debt – i.e., the sophistication of QIB investors – applies with equal force to transactions by QIBs in other securities such as those that were originally offered and sold and continue to be offered and sold pursuant to a private placement exemption from registration under the Securities Act, including pursuant to Rule 144A. In our view, therefore, this modification is a logical and limited extension of the NASD's current proposal. If the SEC or NASD has concerns regarding this modification that might substantially delay adoption of the Interpretation, however, we recommend that expansion of the QIB Exemption be deferred and subject to further review after the Interpretation has been adopted.

Second, we also generally agree with SIFMA's concerns regarding the application of the Interpretation to certain structured credit products. The special features of these securities – including the wide variety of customized structures, the range of different factors that can affect their risk, pricing and liquidity, and the greater reliance of dealers on economic models in determining their prices – make application of the Interpretation more problematic than in the context of traditional corporate debt, which has been the primary focus of discussions to date regarding the Interpretation. Further consideration therefore should be given to the unique challenges presented by structured credit products. We would be pleased to meet with the SEC and NASD staffs to discuss the special trading and pricing characteristics of structured credit products and provide specific case studies illustrating those characteristics. We reiterate, however, the importance of avoiding further delay in providing the traditional corporate debt markets with the markup guidance offered by the Interpretation and support adoption of the Interpretation in its current form subject to a subsequent and thorough consideration of the special issues raised by structured credit products.

Third, we believe that certain concerns that have been raised with respect to the Interpretation could be addressed by the SEC and NASD through clarifications in a release accompanying adoption of the Interpretation or otherwise, rather than through amendments to the Interpretation. In particular:

- In order to avoid any negative inferences that might otherwise be drawn in connection with the withdrawal of the “size proposal,” the NASD should confirm that large block trades may appropriately occur at a premium (or discount) to the current market price, and that accordingly that premium (or discount) may be taken into consideration when using the block trade price to determine prevailing market price for a subsequent trade. Although the NASD stated in the Proposing Release that it had withdrawn the “size proposal” because the QIB Exemption addresses the same concerns more effectively, in our view the QIB Exemption does not address potential pricing issues that can arise in block trades involving investment grade debt.
- The NASD could also provide additional guidance in an adopting release or otherwise regarding “contemporaneous” costs and, in particular, confirm the ability of dealers to make determinations in good faith regarding when a trade is or is not “close enough in time to the subject transaction that it would reasonably be expected to reflect the current market price for the security”.
- We also respectfully request that the NASD clarify the determination of “prevailing market price” when a dealer’s contemporaneous cost is determined by reference to its purchase of securities from a customer at a price that included an appropriate markdown. Currently, the Interpretation states that the best measure of “prevailing market price” is presumptively the dealer’s contemporaneous cost as incurred consistent with NASD pricing rules. SEC and NASD precedent indicates, however, that when a *non-market-maker* determines “prevailing market price” by reference to purchases from a customer (as opposed to purchases from another dealer), the non-market-maker should adjust the purchase price upwards to reflect an appropriately imputed markdown.² The continued validity of this concept under the Interpretation should be confirmed.

Finally, the NASD and the SEC should confirm that they will continue to work with the industry to address additional issues that may become apparent as dealers gain practical experience with applying the Interpretation. As stated by the NASD in the Proposing

² See, e.g., NASD Notice to Members 92-16 (for a non-market-maker “the price that the firm pays other broker/dealers (i.e., its cost) contemporaneously with retail sales is the best indicator of the prevailing market price”). If there are contemporaneous purchases from customers but no or very few wholesale purchases during the period, firms should consider using the prices contemporaneously paid to retail, after adjusting for an appropriate markdown”); In re First Honolulu Securities, Inc., 44 SEC Dock 63, Exchange Act Release No. 32933 (Sept. 21, 1993) (“We have looked to retail purchases (with an imputed markdown) only in the absence of inter-dealer transactions”); In re Michael Novick, 57 SEC Dock 1416, Exchange Act Release No. 34640 (Sept. 2, 1994) (imputing a markdown for prices paid by non-market-maker to customers); In re DBCC No. 4 vs. Miller, Johnson & Kuehn, Inc. (Feb. 10, 1994) (imputing a markdown for prices paid to customers in bond transactions).

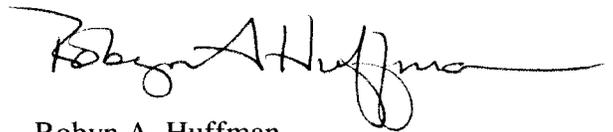
Release, the Interpretation is an “*important first step*” in developing markup guidance for debt securities – it should not become in effect the final stage in this process.³

We appreciate the significant efforts made by the SEC and NASD staff to meet with representatives of the industry in developing the current version of the Interpretation. We believe this productive dialogue should continue, focusing as necessary on the appropriate treatment of structured credit products, the expansion of the QIB Exemption to address transactions in other types of securities, and the potential modification of the “hierarchy” to make it more flexible, particularly with respect to the use of economic models.

* * *

Once again, we appreciate this opportunity to comment on the Interpretation. If you should have any questions regarding these comments, please do not hesitate to contact me at (212) 902 9957.

Sincerely,



Robyn A. Huffman
Managing Director
Associate General Counsel

cc: Mary L. Schapiro, Chairman and CEO, NASD
Marc Menchel, General Counsel, NASD
Stephen Luparello, Senior Executive Vice President, Regulatory Operations, NASD
Sharon Zackula, Assistant General Counsel, NASD
Erik R. Sirri, Director, Division of Market Regulation, SEC
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Catherine McGuire, Associate Director and Chief Counsel, Division of Market Regulation, SEC
Katherine A. England, Assistant Director Division of Market Regulation, SEC
Chester Spatt, Chief Economist and Director, Office of Economic Analysis, SEC

³ Proposing Release at 68863.