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SECURITIES AND EXCHANGE COMMISSION
[Release No. 34-72626; File No. SR-FINRA-2014-006]

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Amendment No. 1 to Proposed Rule Change Relating to Per Share Estimated Valuations for Unlisted DPP and REIT Securities

July 16, 2014.

I. Introduction

On January 31, 2014, Financial Industry Regulatory Authority, Inc. (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)) filed with the Securities and Exchange Commission (“SEC” or “Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act” or “Exchange Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend provisions in the FINRA rulebook addressing per share estimated valuations for unlisted direct participation program (“DPP”) and real estate investment trust (“REIT”) securities. The proposed rule change was published for comment in the Federal Register on February 19, 2014.³ The Commission received eighteen (18) comment letters in response to the Notice of Filing.⁴

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Exchange Act Release No. 71545 (Feb. 12, 2014), 79 FR 9535 (Feb. 19, 2014) (Notice of Filing of Proposed Rule Change Relating to Per Share Estimated Valuations for Unlisted DPP and REIT Securities) (“Notice of Filing”). The comment period closed on March 12, 2014.

⁴ Letters to Elizabeth Murphy, Secretary, SEC, from Mark Goldberg, Chairman, Investment Program Association, dated February 5, 2014; David Bellaire, Executive Vice President and General Counsel, Financial Services Institute, dated February 5, 2014; Mark Kosanke, President, Real Estate Investment Securities Association, dated February 11, 2014; Steven Wechsler, President and CEO, National Association of Real Estate Investment Trusts, dated February 14, 2014; Kirk Montgomery, Head of Regulatory

On March 14, 2014, FINRA extended the time period in which the Commission must approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to approve or disapprove the proposed rule change to May 20, 2014.

On May 20, 2014, the Commission issued an order instituting proceedings pursuant to Section 19(b)(2)(B) of the Act⁵ to determine whether to approve or disapprove the proposed rule change. The order was published for comment in the Federal Register on May 27, 2014.⁶ The Commission received five (5) comment letters in response to the order.⁷

Affairs, CNL Financial Group, LLC, dated March 12, 2014; Dechert LLP, dated March 12, 2014; Jeff Johnson, CEO, Dividend Capital Diversified Property Fund Inc., dated February 28, 2014; David Bellaire, Executive Vice President and General Counsel, Financial Services Institute, dated March 12, 2014; Mark Goldberg, Chairman, Investment Program Association, dated March 12, 2014; Michael Crimmins, CEO and Managing Director, KBS Capital Markets Group, dated February 28, 2014; Steve Morrison, Senior Vice President and Associate Counsel, LPL Financial, dated March 12, 2014; Steven Wechsler, President and CEO, National Association of Real Estate Investment Trusts, dated March 12, 2014; Martel Day, Principal, NLR Advisory Services, LLC, dated March 12, 2014; Scott Ilgerfritz, Immediate Past-President, Public Investors Arbitration Bar Association, dated March 11, 2014; Mark Kosanke, President, Real Estate Investment Securities Association, dated March 12, 2014; Thomas Price, Managing Director, Securities Industry and Financial Markets Association, dated March 12, 2014; David Hirschmann, President and CEO, U.S. Chamber of Commerce, Center for Capital Markets Competitiveness, dated March 12, 2014; and Jacob Frydman, Chairman and CEO, United Realty Trust Incorporated, dated March 12, 2014. Comment letters are available at www.sec.gov.

⁵ 15 U.S.C. 78s(b)(2)(B).

⁶ Exchange Act Release No. 72193 (May 20, 2014), 79 FR 30217 (May 27, 2014) (Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change Relating to Per Share Estimated Valuations for Unlisted DPP and REIT Securities). The comment period closed on June 26, 2014.

⁷ Letters to Elizabeth Murphy, Secretary, SEC, from David Bellaire, Executive Vice President and General Counsel, dated June 26, 2014; Thomas Price, Managing Director, Securities Industry and Financial Markets Association, dated June 26, 2014; Mark Kosanke, President, Real Estate Investment Securities Association, dated June 26, 2014; Jason Doss, President, Public Investors Arbitration Bar Association, dated June 25, 2014; and Kenneth Mills, dated June 24, 2014. Comment letters are available at www.sec.gov.

On July 11, 2014, FINRA filed a letter responding to comments and Amendment No. 1 to the proposed rule change.⁸ The text of Amendment No. 1 is available on FINRA’s website at <http://www.finra.org>, at the principal office of FINRA, and at the Commission’s Public Reference Room. Amendment No. 1 is described in Item II below, which has been substantially prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

II. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Amendment

As further described in the Notice of Filing, FINRA is proposing to amend (1) NASD Rule 2340 (Customer Account Statements) to modify the requirements relating to the inclusion of a per share estimated value for unlisted DPP and REIT securities on a customer account statement; and (2) FINRA Rule 2310 (Direct Participation Programs) to modify the requirements applicable to members’ participation in a public offering of unlisted DPP or REIT securities.

In response to comments received by the Commission, FINRA is proposing to amend the proposed rule change as follows:

1. FINRA is revising proposed NASD Rule 2340(c) to require general securities members to include in customer account statements a per share estimated value for a DPP or REIT security developed in a manner reasonably designed to ensure that the per share estimated value is reliable. Thus, FINRA is eliminating the voluntary or “not priced” option originally proposed. Moreover, FINRA is revising proposed NASD Rule 2340(c)(1) to state that the per share estimated value will be deemed to have been developed in a manner reasonably designed to ensure that it is reliable if the member uses one of the two specified methodologies.

⁸ Letter to Kevin O’Neill, Deputy Secretary, SEC, from Matthew Vitek, Associate General Counsel, FINRA, dated July 11, 2014 (“Response Letter”). FINRA’s Response Letter is available at www.sec.gov.

2. FINRA is eliminating the “no reason to believe that the per share estimated value is unreliable” standard from the general provision in proposed NASD Rule 2340(c). As revised, proposed NASD Rule 2340(c) would require disclosure of valuations and proposed NASD Rule 2340(c)(1) would deem valuations calculated under the two defined methodologies to have been developed in a manner reasonably designed to ensure that they are reliable. As a result, FINRA believes the “no reason to believe that the per share estimated value is unreliable” standard in the general provision in proposed NASD Rule 2340(c) is not necessary.

3. FINRA is removing the “over distribution” deduction from the per share estimated value in the “net investment” methodology in proposed NASD Rule 2340(c)(1)(A)(ii) and replacing it with enhanced disclosure of “over distribution” on customer account statements. As revised, proposed NASD Rule 2340(c)(2)(A) would require account statements that include a “net investment” per share estimated value for a DPP or REIT security to disclose, if applicable, prominently and in proximity to disclosure of distributions and the per share estimated value the following: “IMPORTANT – Part of your distribution includes a return of capital. Any distribution that represents a return of capital reduces the estimated per share value shown on your account statement.”

4. FINRA is revising the “net investment” methodology in proposed NASD Rule 2340(c)(1)(A) to make clear that firms may use the maximum offering percentage when the issuer provides a range of amounts available for investment unless the member has reason to believe that such percentage is unreliable, in which case the member must use the minimum offering percentage.

5. FINRA is modifying the “net investment” methodology in proposed NASD Rule 2340(c)(1)(A) to lengthen the time period in which members may use the “net investment”

methodology. The proposed rule change, as amended, would allow “net investment” values to be included on customer account statements at any time before 150 days following the second anniversary of breaking escrow. FINRA is making a parallel change to proposed FINRA Rule 2310(b)(5)(B)(i).

6. FINRA is modifying proposed FINRA Rule 2310(b)(5)(B) to clarify issuer disclosure requirements, including the elimination of the requirement to identify the service used to obtain a valuation, and require more frequent valuations. As revised, proposed FINRA Rule 2310(b)(5)(D)(i) would require that the per share estimated value be based on valuations of the assets and liabilities of the DPP or REIT performed at least annually by, or with the material assistance or confirmation of, a third-party valuation expert or service.

7. FINRA is modifying proposed FINRA Rule 2310(b)(5) to specifically except DPPs that are subject to the Investment Company Act of 1940 (“1940 Act”) from the requirements under the rule in recognition that business development companies that fall under the definition of DPP are subject to an existing regulatory framework under the 1940 Act for determining and publishing net asset value on a regular basis. In addition, FINRA is revising proposed NASD Rule 2340(c)(1)(B) to state, in the case of DPPs subject to the 1940 Act, the appraised value methodology under Rule 2340(c)(1)(B) shall be consistent with the valuation requirements of the 1940 Act and the rules thereunder.

8. FINRA is extending the effective date of the proposed rule change to no earlier than 18 months following Commission approval. FINRA believes this extended timeframe will give industry participants time to make adjustments to product structures and any necessary operational changes.

FINRA is also proposing the following changes:

1. FINRA is proposing to change the title of NASD Rule 2340(c) from “Unlisted DPP/REIT Securities” to “DPP and Unlisted REIT Securities” to more accurately reflect the types of securities that are subject to the rule. FINRA also is changing the title of proposed NASD Rule 2340(c)(1)(B) from “independent valuation” to “appraised value” to more accurately reflect the per share estimated value methodology.

2. FINRA is revising the “net investment” methodology in proposed NASD Rule 2340(c)(1)(A)(i) to clarify that “another equivalent disclosure” means “another equivalent disclosure that reflects the estimated percentage deduction from the aggregate dollar amount of securities registered for sale to the public of sales commissions, dealer manager fees, and estimated issuer offering and organization expenses.”

3. FINRA is modifying the “appraised value” methodology to clarify in proposed NASD Rule 2340(c)(1)(B) that the member may include a per share estimated value reflecting an appraised valuation disclosed in the Issuer Report based on the valuations of the assets and liabilities of the DPP or REIT performed at least annually by, or with the material assistance or confirmation of, a third-party valuation expert or service and derived from a methodology that conforms to standard industry practice.

4. FINRA is eliminating the required disclosures in proposed NASD Rule 2340(c)(2)(A)(i) regarding characteristics of the per share estimated value and proposed NASD Rule 2340(c)(2)(B) on the “not priced” option. FINRA believes that streamlined disclosure will be more effective than also requiring an account statement to describe per share estimated value, its source, and the method by which it was developed, as would have been required under the originally proposed NASD Rule 2340(c)(2)(A)(i). In addition, FINRA believes the disclosures in proposed NASD Rule 2340(c)(2)(B) are no longer necessary because the revised proposal

requires a general securities member to include in a customer account statement a per share estimated value of a DPP or REIT security.

5. FINRA is modifying proposed FINRA Rule 2310(b)(5) to state that a member shall not participate in a public offering of the securities of a DPP that is not subject to the requirements of the 1940 Act or of a REIT unless they meet the requirements under the rule. In addition, FINRA is revising proposed FINRA Rule 2310(b)(5)(A) to clarify that the issuer of the DPP or REIT must agree to disclose a per share estimated value of the DPP or REIT security, developed in a manner reasonably designed to ensure it is reliable, in the DPP or REIT periodic reports filed pursuant to Section 13(a) or 15(d) of the Exchange Act.

6. FINRA is clarifying in proposed FINRA Rule 2310(b)(5)(D)(iii) that the valuation must be accompanied by a written opinion or report by the issuer, delivered at least annually to the broker-dealer, that explains the scope of the review, the methodology used to develop the valuation or valuations, and the basis for the value or values reported.

7. FINRA is making a technical change to delete FINRA Rule 5110(f)(2)(L) instead of the originally proposed deletion of FINRA Rule 5110(f)(2)(M) because FINRA renumbered the subparagraphs of FINRA Rule 5110(f)(2) after the filing of the proposed rule change.⁹

III. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change, as amended by Amendment No. 1, is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or

⁹ See Exchange Act Release No. 72114 (May 7, 2014), 79 FR 27355 (May 13, 2014) (Order Approving a Proposed Rule Change; SR-FINRA-2014-004).

- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2014-006 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2014-006. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change. The Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-FINRA-2014-006 and should be submitted on or before [INSERT 21 DAYS FROM DATE OF PUBLICATION IN THE FEDERAL REGISTER].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁰

Kevin M. O'Neill,
Deputy Secretary.

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¹⁰ 17 CFR 200.30-3(a)(12).