

a sponsor to each associated person during any year does not exceed \$100.00;

(ii) the value of all such items to be made available in connection with an offering is included as compensation to be received in connection with the offering for purposes of subparagraph (B); and

(iii) the proposed payment or transfer of all such items is disclosed in the prospectus or similar offering document,]

(F) Renumbered to (E).

(5)–(6) No Change

(c) Non-Cash Compensation

(1) Definitions

The terms “compensation,” “non-cash compensation” and “offeror” as used in this section (c) of this rule shall have the following meanings:

(A) “Compensation” shall mean cash compensation and non-cash compensation.

(B) “Non-cash compensation” shall mean any form of compensation received in connection with the sale and distribution of direct participation securities that is not cash compensation, including but not limited to merchandise, gifts and prizes, travel expenses, meals and lodging.

(C) “Offeror” shall mean an issuer, sponsor, an adviser to an issuer or sponsor, an underwriter and any affiliated person of such entities.

(2) Restriction on Non-Cash Compensation

In connection with the sale and distribution of direct participation securities, no member or person associated with a member shall directly or indirectly accept or make payments or offers of payments of any non-cash compensation, except as provided in this provision. Non-cash compensation arrangements are limited to the following:

(A) Gifts that do not exceed an annual amount per person fixed periodically by the Board of Governors¹ and are not conditioned on achievement of a sales target.

(B) An occasional meal, a ticket to a sporting event or the theater, or comparable entertainment which is neither so frequent nor so extensive as to raise any question of propriety and is not preconditioned on achievement of a sales target.

(C) Payment or reimbursement by offerors in connection with meetings held by an offeror or by a member for the purpose of training or education of associated persons of a member, provided that:

(i) associated persons obtain the member's prior approval to attend the meeting and attendance by a member's associated persons is not conditioned by the member on the achievement of a sales target or any other incentives pursuant to a non-cash compensation arrangement permitted by subparagraph (c)(2)(D);

(ii) the location is appropriate to the purpose of the meeting, which shall mean an office of the offeror or the member, or a facility located in the vicinity of such office, or a regional location with respect to regional meetings;

(iii) the payment or reimbursement is not applied to the expenses of guests of the associated person; and

(iv) the payment or reimbursement by the offeror is not conditioned by the offeror on the achievement of a sales target or any other non-cash compensation arrangement permitted by subparagraph (c)(2)(D).

(D) Non-cash compensation arrangements between a member and its associated persons or a company that controls a member company and the member's associated persons, provided that no unaffiliated non-member company or other unaffiliated member directly or indirectly participates in the member's or non-member's organization of a permissible non-cash compensation arrangement; and

(E) Contributions by a non-member company or other member to a non-cash compensation arrangement between a member and its associated persons, provided that the arrangement meets the criteria in subparagraph (c)(2)(D).

A member shall maintain records of all non-cash compensation received by the member or its associated persons in arrangements permitted by subparagraphs (c)(2)(C)–(E). The records shall include: the names of the offerors, non-members or other members making the non-cash compensation contributions; the names of the associated persons participating in the arrangements; the nature and value of non-cash compensation received; the location of training and education meetings; and any other information that proves compliance by the member and its associated persons with subparagraph (c)(2)(C)–(E).

(c) Renumbered as (d).

* * * * *

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the NASD included statements concerning the purpose of and basis for the

proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in item IV below. The NASD has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The NASD is proposing to codify a stated policy, practice, and interpretation that the more detailed non-cash compensation provisions in the Variable Contracts rule and Investment Company rule apply to the sale and distribution of public offerings of securities and direct participation securities as governed by the Corporate Financing rule and DPP rule, respectively. The NASD is proposing to conform the language in the Corporate Financing rule and the DPP rule to be consistent with the more detailed language contained in the Variable Contracts rule and the Investment Company rule. NASD staff has consistently applied the more detailed provisions in Variable Contracts rule and the Investment Company rule to the sale and distribution of public offerings of securities and DPP securities.

Since 1994, the Commission, the NASD, and the securities industry have raised concerns about actual and potential conflicts of interest in the retail brokerage business created by a broad range of compensation practices whereby program sponsors or issuers provide incentives or rewards to individual broker-dealers and their registered representatives for selling the issuer's products. NASD staff believes that the use of non-cash compensation can create significant point-of-sale incentives that may compromise suitability determinations and heighten the potential for loss of supervisory control over sales practices. In addition, NASD staff believes that the use of non-cash compensation incentives may result in the loss of investor confidence by increasing the perception of inappropriate practices.

Responding to these concerns, the NASD in January 1999 amended the Variable Contracts rule and the Investment Company rule to establish comprehensive restrictions on the use of non-cash compensation in connection with the sale and distribution of investment company securities and

¹ The current annual amount fixed by the Board of Governors is \$100.