

March 3, 2006

Ms. Barbara Z. Sweeney
Office of the Corporate Secretary
National Association of Securities Dealers, Inc.
1735 K Street, NW
Washington, D.C. 20006-1506

Mr. William Jannace, Director
Mr. Stephen A. Kasprzak, Principal Counsel
Rules and Interpretive Standards
New York Stock Exchange, Inc.
11 Wall Street
New York, NY 10005

Re: NASD Notice to Members 06-06 and SR-NYSE-2006-06
Proposed Gifts and Business Entertainment Policies

Dear Ms. Sweeney, Mr. Jannace and Mr. Kasprzak:

The Bond Market Association (“Association”)¹ appreciates this opportunity to respond to the request for comments on Notice to Members 06-06 (the “NASD Proposal”) and SR-NYSE-2006-06 (“NYSE Proposal” and collectively with the NASD Proposal, the “Proposals”) relating to gifts and business entertainment by member firms of the National Association of Securities Dealers, Inc. (“NASD”) and the New York Stock Exchange, Inc. (“NYSE” and collectively with the NASD, the “SROs”). The Association strongly supports the Proposals and believes that the “principles-based” approach to business entertainment is the appropriate regulatory approach to dealing with this important issue, the management of which is so fact-specific.

The Association agrees that the overriding principle of any gift and business entertainment policy should be to prevent a member of an SRO from using gifts or entertainment to cause an employee or agent of a present or potential customer to act contrary to the best interests of the customer. A “principles-based” approach recognizes that entertainment that would be ordinary for one representative of a customer, in light of relevant circumstances, such as that representative’s seniority or status or the occasion (e.g., the other attendees at a celebratory event), would be inappropriate for another

¹ The Bond Market Association, with offices in New York, Washington, D.C. and London, represents securities firms, banks and asset managers that underwrite, invest, trade and sell debt securities and other financial products globally. More information about the Association is available on its website at <http://www.bondmarkets.com>.

Ms. Barbara Z. Sweeney
Mr. William Jannace
Mr. Stephen A. Kasprzak
March 3, 2006
Page 2 of 6

representative of that customer or at a different event. The SROs' approach allows and requires each member to adopt specific policies and guidelines, consistent with this overriding principle.

As further described below, the Association has a number of relatively minor comments relating to the details of the Proposals.

I. Definition of Customer

The first comment of the Association relates to the definition of "customer" in the Proposals, which we think can be shortened and simplified without reducing its desired scope.² The Association suggests the definition be modified generally as follows:

The term "customer" means an accredited investor (as defined in Rule 501 of the Securities Act of 1933) that is not a natural person that maintains or may prospectively maintain a customer relationship with a member and has a representative act on its behalf in respect of such relationship.³ The term "customer relationship" means maintaining a securities account with a member or otherwise being a customer of a member for the purposes of investment banking or other securities-related activities. The term "representative" means persons who are employees, officers, directors, agents or representatives of a customer, acting in respect of the customer relationship; *provided, however*, such term shall not include a non-professional fiduciary or agent (e.g., an individual acting as trustee for a family member or on behalf of an investment club).

The Association believes that individuals should be excluded from the term "customer" since imposing tracking requirements on individuals would greatly increase members' recordkeeping burden, with little associated compliance benefit, and without significantly advancing the goals of the Proposals. In addition, the reduced scope of the term "representative" in the definition above is appropriate when non-professional fiduciaries are acting in their personal capacities.

II. Implementation of Recordkeeping Requirement

A major requirement of the Proposals is that members keep detailed records of the nature and cost of business entertainment in order to make such information available to customers upon request. The Association has been informed that few firms have existing systems in place to track entertainment expenses to the level of detail contemplated by

² The Association's proposed definition of customer is based on the definition contained in the NASD Proposal, which is substantially similar to the NYSE Proposal definition.

³ Such an entity is commonly referred to as an institutional accredited investor.

Ms. Barbara Z. Sweeney
Mr. William Jannace
Mr. Stephen A. Kasprzak
March 3, 2006
Page 3 of 6

the Proposals, and that no such system is currently available from an outside vendor.⁴ Consequently, firms are required to either develop the technology needed to comply with the Proposals internally or wait until such systems become commercially available.⁵ Whether firms develop internally or purchase from outside vendors, each firm will be required to integrate its entertainment technology system with its other numerous internal reporting and compliance systems. In addition, as this effort will occur alongside firms' other current technological initiatives, implementation of this requirement will be particularly challenging for firms with smaller numbers of information technology personnel. Accordingly, the Association respectfully suggests that the SROs provide a significant transition period of at least one year for the recordkeeping requirement set out in the Proposals during which transition period members may develop and implement appropriate tracking and recordkeeping systems and institute the required internal training and education (which is itself a substantial and time consuming task, particularly for large organizations) with respect to this requirement.⁶ The Association acknowledges, however, that the transition period for the Proposals' policy component need not be as long as for the recordkeeping component.

III. Conforming the NASD and NYSE Proposals

The Proposals are largely similar and require that members adopt detailed policies and procedures that: (1) define specific types of appropriate business entertainment; (2) require supervision of a member's compliance with the policy; (3) ensure that detailed records of the nature and costs of the entertainment are maintained; and (4) mandate that all applicable personnel receive appropriate training and education. The development and implementation of such comprehensive policies will require significant coordination internally at member firms. In this regard, we commend the SROs for working together in the development of the Proposals and believe that both organizations should continue to work together to ensure that their respective business entertainment policies, when finalized, are substantially similar or identical to one another in order to minimize the overall costs associated with these policies and to avoid confusion among member firms.⁷

⁴ While the Association has read news reports that several vendors are currently developing systems to track entertainment expenses, it is important to note that even after such systems become available, members will still need a significant time period to implement the systems.

⁵ As a practical matter, it is more efficient for a number of outside vendors to develop a system for many firms to use.

⁶ The NASD has provided significant transition periods for the implementation of other technological systems. See e.g., NASD Notice to Members 98-33 (providing nearly 23 months from adoption to the full implementation of the Order Audit Trail System (OATS)); NASD Notice to Members 01-18 and 05-21 (providing nearly 18 months from adoption to implementation of the TRACE Reporting System).

⁷ Further in this regard, the Association strongly encourages the Municipal Securities Rulemaking Board ("MSRB") to comparably amend MSRB Rule G-20(b) with the goal of making the regulatory requirements applicable to its members identical those the policies of the SROs in order to eliminate any differences in compliance procedures.

Ms. Barbara Z. Sweeney
Mr. William Jannace
Mr. Stephen A. Kasprzak
March 3, 2006
Page 4 of 6

There are currently three differences between the NASD Proposal and the NYSE Proposal that the Association hopes can be resolved. *First*, while both the NASD Proposal and the NYSE Proposal require that a person associated with a member accompany the customer representative to each entertainment event, the NYSE Proposal expressly provides an exigency exemption “where circumstances make it impractical” for the associated person to accompany the representative. In order to prevent abuse, the NYSE Proposal requires that a member obtain prior written supervisory approval for, or where impractical, a prompt post event review of, each use of this exemption. The Association strongly suggests that the NASD incorporate this practical and limited exemption in its proposal.⁸

Second, the NYSE Proposal requires that members provide notice to customers that upon written request customers may obtain the business entertainment information applicable to it. The NASD Proposal requires only that members record and make such information available to customers. The Association believes that either approach would accomplish the goals underlying the Proposals, but encourages the SROs to adopt a consistent approach.

Third, the NYSE has stated that it intends to publish an Information Memo to be released in conjunction with its final rule that will provide a list of factors that members must consider in formulating criteria to evaluate the propriety of business entertainment. The NASD Proposal mandates only that the relevant criteria, to be chosen at the member’s discretion, be explicit in each member’s policies and procedures. The Association feels that many of the factors the NYSE proposes to include in its Information Memo are explicit or implicit in the policy statements contained in the Proposals and, consequently, are unnecessary. In addition certain factors, such as whether the business entertainment is “usual and customary within the industry” are ambiguous and impractical to implement.⁹ The Association is unsure how a member would determine the precise types of entertainment that other members or customers consider “usual and customary.”

⁸ Situations in which a person associated with a member might be unexpectedly unable to accompany the customer representative, and where such an exemption makes sense, include a snow storm, sudden family illness, or a baby sitter cancellation.

⁹ The Association is unclear whether this factor refers to the securities industry or the customer’s industry.

Ms. Barbara Z. Sweeney
Mr. William Jannace
Mr. Stephen A. Kasprzak
March 3, 2006
Page 5 of 6

IV. Incorporate Prior NASD Guidance

In July 1999, the NASD published Notice to Members 99-55, which addressed questions relating to the NASD Rules 2820 and 2830 compensation arrangements in the distribution of variable products and investment company securities.¹⁰ In answers to questions numbers 16 and 17, the NASD explained, generally, that gifts of a personal nature (e.g., wedding gifts or gifts of a congratulatory nature for the birth of a child) and promotional items of nominal value¹¹ that display the issuer's or offeror's logo (e.g., golf balls, shirts, towels, pens, Lucites or other deal mementos) are outside of the \$100 annual gift limit specified in Rules 2820(g)(4)(A) and 2830(1)(5)(A).¹² The Association has been informed that these exemptions are heavily relied upon by members.

On page two of the NASD Proposal, the NASD states that its proposed interpretation "would supersede any prior guidance." The Association respectfully suggests that the SROs again strive for consistency by explicitly confirming that the exemptions for personal gifts and promotional items will continue to apply after the adoption of the Proposals.

In conclusion, the Association feels that the "principles-based" approach set forth in the Proposals is the most appropriate manner for dealing with situations involving highly fact-specific issues, such as business entertainment. Further, the Association encourages the SROs to consider applying a "principles-based" approach to other fact-based regulatory situations as they arise.¹³ We look forward to discussing these issues

¹⁰ This Notice is briefly referenced in the Background and Discussion section and footnote 4 of the NASD Proposal.

¹¹ The Association recommends that the SROs apply the "principles-based" approach set forth in the Proposals to the determination of which gifts are of "nominal" value; requiring each member to establish policies and procedures that identify the types of items which meet this test.

¹² The Association requests that the SROs confirm the Association's understanding that the \$100 gift limit includes only the value of the gift and not any applicable taxes and shipping costs.

¹³ Many U.S. and foreign regulators have reached the same conclusion and advocate for a "principles-based" approach to regulation. *See, e.g.*, Robert K. Herdman, Chief Accountant, U.S. Securities and Exchange Commission, Are Current Financial Accounting Standards Protecting Investors?, Testimony before the Subcommittee on Commerce, Trade and Consumer Protection, Committee on Energy and Commerce, U.S. House of Representatives (February 14, 2002), *in* <http://www.sec.gov/news/testimony/021402tsrkh.htm> (arguing that "[a]n ideal accounting standard is one that is principle-based and requires financial reporting to reflect the economic substance, not the form, of the transaction...[and] that is more responsive to emerging issues"); Andrew Whittaker, Director, General Counsel Division, FSA, Speech to the Fountain Court Chambers Conference on Better Regulation, Professional and Financial Regulation - Conflict or Convergence? (January 31, 2006), *in* http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2006/0131_aw.shtml (strongly advocating a "principles-based" approach since prescriptive standards "have shown themselves inadequate alone to prevent misconduct...[are] not only a barrier to entry, but also a barrier to compliance... [and] divert industry attention towards complying with the letter, rather than the purpose, of the standard, making it less, rather than more, likely that it will achieve its goal.")

Ms. Barbara Z. Sweeney
Mr. William Jannace
Mr. Stephen A. Kasprzak
March 3, 2006
Page 6 of 6

further with the staffs of the NASD and NYSE and appreciate your attention to our comments. Please contact the undersigned at (646) 637-9214 or via email at rsnook@bondmarkets.com with any questions that you might have.

Sincerely,

/s/ Randolph C. Snook

Randolph C. Snook
Executive Vice President and
Head of New York Office

cc: U.S. Securities and Exchange Commission
Chairman Christopher Cox
Commissioner Paul S. Atkins
Commissioner Roel C. Campos
Commissioner Cynthia A. Glassman
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