The Asset Management Industry
SERVING INDIVIDUAL INVESTORS
INVESTMENT COMPANY INSTITUTE

MEMO# 25394

August 9, 2011

Draft Institute Comment letter on FINRA's Proposed Amendments to Advertising Rules; Your Comments Requested By August16th

URGENT/ACTION REQUESTED

[25394]

August 9, 2011

TO: ADVERTISING COMPLIANCE ADVISORY COMMITTEE No. 8-11
CLOSED-END INVESTMENT COMPANY COMMITTEE No. 39-11
SEC RULES COMMITTEE No. 68-11 RE: DRAFT INSTITUTE COMMENT LETTER ON FINRA'S PROPOSED AMENDMENTS TO ADVERTISING RULES; YOUR COMMENTS REQUESTED BY AUGUST16TH

As we previously informed you, the Financial Industry Regulatory Authority (“FINRA”) filed with the Securities and Exchange Commission (“SEC”) proposed new rules and rule amendments governing member communications with the public. [1] The new rules would replace current NASD Rules 2210 and 2211, the Interpretive Materials that follow NASD Rule 2210, and portions of NYSE Rule 472 and related interpretive material. [2] The Institute has prepared a draft comment letter, which is attached and summarized below.

Comments on the Proposed Final Rule must be filed with the SEC no later than August 24th. Please provide any comments on the draft letter no later than August 16th to Tami Salmon by email at tamara@ici.org or phone at (202) 326-5825 or Bob Grohowski by email at rcg@ici.org or phone at (202) 371-5430.

The draft letter states that we are pleased that FINRA addressed many of the concerns we raised in our 2009 Letter, and we therefore support many elements of the Proposed Final Rule. The draft letter also recommends that FINRA revise several aspects of the Proposed Final Rule before the SEC approves a final rule. Finally, the draft letter states our views on how FINRA’s regulations regarding social media could be improved.

Summary of ICI Recommendations

Public Appearances

The draft letter strongly urges FINRA not to apply the proposed disclosure requirements regarding recommendations to public appearances. It points out that FINRA's reliance on Rule 2711 is misplaced because the disclosure and related oversight obligations imposed by Rule 2711 differ significantly from those that would be imposed on public appearances under the Proposed Final Rule.

The draft letter states that we would not object, however, to FINRA imposing a more general requirement that a person making a public appearance must disclose any of his or her actual, material conflicts of interest related to a particular recommendation of which the person knows or has reason to know at the time of the public appearance. It points out that revising the requirement in this manner would more closely align the Proposed Final Rule's requirements with those of Rule 2711 and address the policy concerns underlying the proposed disclosure requirements.

Text Box Requirement

The draft letter reiterates the view expressed in our 2009 Letter that FINRA should eliminate the requirement that funds present standardized performance information, maximum sales charge, and annual expense ratio in a prominent text box in print advertisements. The draft letter reasons that such a requirement is unnecessary to achieve the goal of ensuring that the required information is sufficiently prominent. Rather, the draft letter recommends that FINRA revise Rule 2210 to require funds to prominently present standardized performance, maximum sales charges, and expense ratios.

Exemptive Authority

The draft letter supports FINRA being allowed to grant exemptions from the principal approval and filing requirements. It recommends that the new authority be exercised in a way that assists as many member firms as possible. This could be accomplished by timely announcing in a regulatory notice the availability to all member firms of exemptive relief already individually granted to some number of firms. The draft letter states that any final release should include a more fulsome discussion of the new exemptive authority in order to assist the industry's understanding of FINRA's planned exercise of this authority.

Templates

The draft letter recommends that FINRA exclude from filing those retail communications that are based on templates that were previously filed with FINRA if the only change is a narrative factual update provided by an entity that: (i) provides general information about funds to the public; and (ii) is independent of the fund and its affiliates. It reasons that when the only change to the information in that type of communication is provided by an independent third party, filing is not necessary for investor protection.

Supervision of Internal Communications

The draft letter opposes treating internal communications as "institutional communications." It points out that this new proposed standard of supervision was not part of the 2009 Proposal, and FINRA offers no rationale for instituting this new requirement. It further states that we are not aware of any circumstances that would warrant the new supervision requirements, and believe that internal communications already are subject to sufficient oversight. Internal communications currently are, and should continue to be, supervised under Rule 3010, which is a rule specifically designed to address a member's

supervision of its registered representatives' activities. The draft letter therefore recommends that FINRA eliminate this part of the Proposed Final Rule.

Areas of Support

The draft letter supports many aspects of the Proposed Final Rule and praises FINRA for making many of the changes we recommended in our 2009 Letter. In particular, the draft letter supports, among other things, the Proposed Final Rule:

- requiring sales charge and expense disclosure appearing in retail communications to be based on that information as it appears in fund prospectuses;
- excluding from the filing and principal approval requirements communications to retail investors that do not make any financial or investment recommendation or otherwise promote a product or service of the member;
- excepting from the principal approval requirements any retail communication that is posted on an online interactive electronic forum, provided that the member supervises and reviews such communications in the same manner as required for supervising correspondence;
- not requiring prior principal approval of market letters;
- preserving the current filing exclusion for press releases made available only to members of the media;
- requiring firms to file all retail communications concerning closed-end funds within ten business days of first use;
- excluding from filing two types of templates (retail communications that previously have been filed with FINRA and that are to be used without material change and retail communications that are based on templates that were previously filed with FINRA, the changes to which are limited to updates of non-narrative information); and
- not requiring members to keep records of the person who distributed a retail or institutional communication.

Social Media

The draft letter describes the fund industry's increasing use of social media and states that it is critical that overly prescriptive requirements not jeopardize the industry's efforts to effectively communicate through new media. The draft letter states our belief that a longer-term, comprehensive approach that is based on a strong understanding of evolving media and technological capabilities, and that considers the costs and benefits associated with regulation, is worthy of pursuit. This effort should include an examination of such complex issues as how regulatory requirements can be squared with the lack of clear demarcation between personal and professional communications, and how the exploding use of electronic media networks along with unified communications (video, voice, and data) make retention of every record related to "business as such" impractical, unsustainable, and costly. The draft letter states that regulators should consider the advantages of a more flexible regulatory regime rather than requiring broker-dealers to supervise and maintain a record of every communication related to business as such, without weighing the costs and benefits of such requirements. Rather, to develop a more workable, cost effective way to protect investors, the Institute and its members would like to work with FINRA and SEC staff to modernize requirements using today's and tomorrow's technologies for the benefit of shareholders and consistent with investor protection.

Dorothy M. Donohue
Senior Associate Counsel

Attachment

endnotes

[1] See Institute Memorandum No. 25348, dated July 22, 2011. See also FINRA Notice of Filing of Proposed Rule Change to Adopt FINRA Rules 2210, 2212, 2214, 2215, and 2216 in the Consolidated FINRA Rulebook, 76 Fed. Reg. 46870 (August 3, 2011) ("Proposed Final Rule") available at http://www.sec.gov/rules/sro/finra/2011/34-64984.pdf.

[2] The rule filing was preceded by FINRA Regulatory Notice No. 09-55 (September 2009) ("2009 Proposal") on which the Institute commented. See Letter to Ms. Marcia E. Asquith, Senior Vice President and Corporate Secretary, Office of the Corporate Secretary, FINRA from Dorothy M. Donohue, Senior Associate Counsel, Investment Company Institute, dated November 19, 2009 ("2009 Letter").
