

**MEMO# 25348**

July 22, 2011

## **FINRA Files With SEC Proposed Amendments to Advertising Rules; July 27th Conference Call**

URGENT/ACTION REQUESTED

[25348]

July 22, 2011

TO: ADVERTISING COMPLIANCE ADVISORY COMMITTEE No. 5-11  
CLOSED-END INVESTMENT COMPANY COMMITTEE No. 37-11  
SEC RULES COMMITTEE No. 65-11 RE: FINRA FILES WITH SEC PROPOSED AMENDMENTS TO ADVERTISING RULES; JULY 27TH CONFERENCE CALL

The Financial Industry Regulatory Authority has filed with the Securities and Exchange Commission 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 Proposal is summarized below.

Comments on the Proposal must be filed with the SEC no later than 21 days after publication in the Federal Register. We will hold a conference call to discuss the Institute's comments on the proposal on Wednesday, July 27th at 2:00 ET. If you or someone else from your firm would like to participate on the call, please contact Gwen Kelly at [gwen.kelly@ici.org](mailto:gwen.kelly@ici.org) for the dial-in information. If you cannot participate on the call, you can email your comments to Dorothy Donohue at [ddonohue@ici.org](mailto:ddonohue@ici.org).

### **Communications Categories**

The Proposal would eliminate the current definitions of "advertisement," "sales literature," "institutional sales material," "public appearance," and "independently prepared reprint" in NASD Rule 2210, as well as "correspondence" and all other definitions in NASD Rule 2211. The Proposal also would eliminate the definitions of "communication," "advertisement," "market letter," and "sales literature" in NYSE Rule 472. The definitions would be replaced by three communication categories:

- “Institutional communication” would include communications that fall under the current definition of “institutional sales material” (i.e., communications that are distributed or made available only to institutional investors).
- “Retail communication” would include any written (including electronic) communication that is distributed or made available to more than 25 retail investors within any 30 calendar-day period. “Retail investor” would include any person other than an institutional investor, regardless of whether the person is an existing or prospective customer.
- “Correspondence” would include any written (including electronic) communication that is distributed or made available to 25 or fewer retail investors within any 30 calendar-day period, regardless of whether they are existing or prospective customers. [\[3\]](#)

## Approval, Review and Recordkeeping Requirements

An appropriately qualified registered principal would be required to approve each retail communication before the earlier of its use or filing with FINRA. Proposed FINRA Rule 2210(b)(1) would except from the principal approval requirements four categories of retail communications. First, proposed FINRA Rule 2210(b)(1)(C) would except retail communications filed by another member who has received a letter stating that the communications appear to be consistent with applicable standards. [\[4\]](#) Proposed Rule 2210(b)(1)(D) would except from the principal approval requirements three additional categories of retail communications, provided that the member supervises and reviews such communications in the same manner as required for supervising correspondence under Rule 3010(d). These communications include:

- Retail communications excepted from the definition of “research report;” [\[5\]](#)
- Retail communications posted on an online interactive electronic forum; [\[6\]](#) and
- Retail communications that do not make any financial or investment recommendation or otherwise promote a product or service of the member. [\[7\]](#)

Proposed Rule 2210(b)(1)(E) would allow FINRA to grant an exemption from the principal approval requirements “for good cause shown after taking into consideration all relevant factors, provided that the exemption is consistent with the purposes of FINRA Rule 2210, the protection of investors, and the public interest.” FINRA states its belief that given the rapid changes to technology used to communicate with customers, it will be useful to have exemptive authority with regard to the principal pre-use approval requirements applicable to retail communications in certain circumstances.

Proposed Rule 2210(b)(1)(F) would provide that, notwithstanding any other provision of Rule 2210, a registered principal must approve a communication prior to the member filing it with FINRA. This would clarify that if a firm chooses to file a communication with FINRA, a principal would be required to approve it prior to that filing (even if FINRA rules would not otherwise require a principal to approve the communication).

Proposed Rules 2210(b)(2) and (3) generally would maintain existing supervision and review requirements with regard to a member’s correspondence and institutional sales material.

Proposed Rule 2210(b)(4)(A) would incorporate by reference the recordkeeping form and time period requirements of Securities Exchange Act of 1934 Rule 17a-4.; Proposed Rule 2210(b)(4)(B) would maintain the current recordkeeping requirements for correspondence

(by means of cross-referencing NASD Rules 3010(d)(3) and 3110(a)).

## Filing Requirements

Similar to current requirements, firms would be required to file: (i) at least ten business days prior to use any retail communication for a period of one year beginning on the effective date a member becomes registered with FINRA; and (ii) at least ten business days prior to use retail communications concerning any registered investment company that includes self-created rankings, and retail communications that include bond mutual fund volatility ratings (which communications would have to be withheld from use until any changes specified by FINRA staff have been made).

FINRA's filing requirements would be expanded to require firms to file, within ten business days of first use, retail communications concerning: (i) closed-end funds, including retail communications distributed after the fund's initial public offering; and (ii) publicly offered structured products.

The current exclusions for certain communications from the filing requirements generally would be retained, including the exclusions for: (i) correspondence; (ii) institutional sales material; (iii) press releases that are made available only to members of the media; and (iv) independently prepared reprints.

The proposal would add exclusions for: (i) retail communications that are based on templates that were previously filed with FINRA, the changes to which are limited to updates of more recent statistical or other non-narrative information; (ii) retail communications previously filed that are to be used without material change; (iii) retail communications that do not make any financial or investment recommendation or otherwise promote a product or service of the firm; and (iv) communications that refer to types of investments solely as part of a listing of products or services offered by a member firm.

Proposed Rule 2210(c)(9)(A) would allow FINRA to grant an exemption from the pre-use filing requirements "for good cause shown." In addition, proposed Rule 2210(c)(9)(B) would allow FINRA to grant an exemption from the filing requirements "for good cause shown after taking into consideration all relevant factors, provided that the exemption is consistent with the purposes of FINRA Rule 2210, the protection of investors, and the public interest."

## Content Standards

The proposal would reorganize, but largely incorporate, the current content standards applicable to communications with the public currently found in NASD Rule 2210(d), NASD IM-2210-1, and NASD IM-2210-4. [\[8\]](#) Content standards that currently apply to advertisements and sales literature generally would apply to retail communications. Some of the more significant changes to the content standards include: (i) new rule language that would clarify that previous FINRA guidance concerning comparative illustrations of tax-deferred versus taxable compounding applies whether that illustration appears in a communication promoting variable insurance products or some other communication, such as one discussing the benefits of investing through a retirement plan or account; (ii) an express prohibition on promissory statements or claims; [\[9\]](#) (iii) disclosure requirements for retail communications and public appearances that include recommendations; [\[10\]](#) (iv)

disclosure requirements for retail communications and correspondence that include past specific recommendations; [\[11\]](#) and (v) express exclusions from the requirements regarding recommendations for communications that recommend only registered investment companies and for those that meet the definition of “research report” or that are public appearances by research analysts that include certain disclosures.

In a change from the Notice and consistent with Institute comments, proposed Rule 2210(d)(5) would maintain the current standard requiring that disclosure of the maximum sales charge and total operating expense ratio in certain retail communications be based on the fund’s prospectus. (In the Notice, FINRA had proposed requiring these communications to disclose the maximum sales charge and total operating expense ratio as stated in the fund’s prospectus or annual report, whichever is more current.)

## **Investment Company Rankings in Retail Communications**

Proposed FINRA Rule 2212 would generally replicate the requirements currently applicable to the use of investment company rankings in retail communications with three changes. First, the requirements would apply to retail communications instead of advertisements and sales literature; second, reprints and excerpts of certain articles or reports would be excluded from the requirements; and third, investment company rankings for more than one class of an investment company with the same portfolio would be required to be accompanied by prominent disclosure of the fact that investment companies or classes have different expense structures.

## **Investment Analysis Tools**

The requirements for the use of investment analysis tools in FINRA Rule 2214 would generally remain the same as current requirements. Two minor changes proposed include requiring members to: (i) provide FINRA staff with access to an investment analysis tool and related templates for written reports within ten business days of first use; and (ii) disclose whether the investment analysis tool is limited to searching, analyzing, or in any way favoring securities in which the member serves as an underwriter.

## **Social Media**

As stated earlier, proposed Rule 2210(b)(1)(D)(ii) would except from prior principal approval 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 pursuant to Rule 3010(d). FINRA states that it will consider further guidance related to mobile electronic devices but does not believe this proposed rulemaking is the appropriate vehicle to address all issues related to new technologies.

Dorothy M. Donohue  
Senior Associate Counsel

## endnotes

[1] See File No. SR-2011-035 (July 14, 2011) (“Proposal”), which can be accessed at <http://www.finra.org/web/groups/industry/@ip/@reg/@rulfil/documents/rulefilings/p123893.pdf> (“Proposal”).

[2] The rule filing was preceded by FINRA Regulatory Notice No. 09-55 (September 2009) on which the Institute commented (“Notice”). 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.

[3] The definitions of “public appearance” and “independently prepared reprint” would be eliminated. They would remain excepted from the filing requirements, and the content standards applicable to them would remain limited. Proposed Rule 2210(f) sets forth standards that would apply to public appearances. Proposed Rule 2210(c)(7)(I) excepts certain independently prepared reprints from the filing requirements.

[4] There currently is a similar provision in NASD Rule 2210(b)(1)(D).

[5] This category carries forward a current exception from the principal pre-use approval requirements for market letters.

[6] This codifies a current interpretation of the rules governing communications with the public that allows members to supervise communications posted on interactive electronic forums in the same manner as is required for supervising correspondence set forth in Regulatory Notice 10-06 (January 2010).

[7] FINRA states that it revised the proposed principal approval requirements in this manner to address concerns raised by ICI and other commenters. FINRA also states that it generally considers this exception to cover communications that are more administrative in nature, such as communications that inform investors that their account statement is available online, or of the date of an expected dividend payment. It further states that communications that are intended to educate investors about products or services do not fall within this exception.

[8] NASD IM-2210-1 provides general guidelines to ensure that communications with the public are not misleading and NASD IM-2210-4 contains limitations on the use of FINRA’s name in communications with the public.

[9] FINRA states that its staff already interprets NASD Rule 2210 (d)(1)(B) to prohibit promissory language in member communications.

[10] Differing from the Notice, under the Proposal, financial interests of an associated person of a member in the security being recommended only would have to be disclosed if the associated person has the ability to influence the content of the communication.

[11] The modified requirements would be based on Investment Advisers Act of 1940 Rule 206(4)-1 (requiring disclosure for investment adviser advertisements that include past recommendations).

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