

MEMO# 15527

January 9, 2003

NASD AND NYSE PROPOSED RULE CHANGES RELATING TO RESEARCH ANALYST CONFLICTS OF INTEREST

[15527] January 9, 2003 TO: SEC RULES COMMITTEE No. 5-03 INVESTMENT ADVISERS COMMITTEE No. 2-03 CLOSED-END INVESTMENT COMPANY COMMITTEE No. 4-03 COMPLIANCE ADVISORY COMMITTEE No. 1-03 RE: NASD AND NYSE PROPOSED RULE CHANGES RELATING TO RESEARCH ANALYST CONFLICTS OF INTEREST The Securities and Exchange Commission has published for comment proposed rule changes filed by the NASD and the New York Stock Exchange to amend their rules relating to research analyst conflicts of interest.¹ The Release states that the amendments are a result of interpretive issues raised by the industry since adoption of the analyst rules, preliminary findings from recent examinations, as well as changes required to comply with the research analyst provisions of the Sarbanes-Oxley Act. Comments on the proposed rule changes must be received by the SEC no later than March 10, 2003. We will be scheduling a conference call shortly to discuss the proposal and the Institute's comment letter. Information on the conference call will be sent under separate cover. In general, the proposed rule changes provide for further restriction on research analysts' compensation and trading activities and impose additional disclosure requirements for research reports. The rule amendments also further restrict the relationship between research and investment banking departments and the companies that are the subject of research reports, and impose registration, qualification and continuing education requirements on research analysts.² Most significantly, the proposed rule changes amend several of the definitions used in the rules. For example, the term "research report" is being amended to conform to the 1 Securities Exchange Act Release No. 47110 (December 31, 2002), 68 FR 826 (January 7, 2003) ("Release"). The Release can be found on the SEC's website at <http://www.sec.gov/rules/sro/34-47110.htm> ² For example, new NASD Rule 1050 would require all persons associated with a member that function as research analysts to register with the NASD. For purposes of Rule 1050, "research analyst" would be defined as any associated person who is directly responsible for the preparation of research reports. Before these persons' registrations could become effective, they would be required to pass a qualification examination for research analysts specified by the NASD. ³ Sarbanes-Oxley Act's definition by deleting the criterion of providing a "recommendation" from the criteria that determines what constitutes a research report. This would broaden the scope of the term for purposes of the rules' requirements.³ In addition, the definition of "public appearance" would be revised to include interviews with print media and the writing of a print media article by a "research analyst." Ari Burstein Associate Counsel ³ Under the rule amendments, the definition of "research report" would be defined as "a written or electronic communication which includes an analysis of equity securities or individual companies or industries, and which

provides information reasonably sufficient upon which to base an investment decision.”
“Research analyst” (under the NASD rules) is defined as “the associated person who is principally responsible for ... preparation of the substance of a research report ...”

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