

**MEMO# 14650**

April 18, 2002

# **INSTITUTE LETTER ON NASD AND NYSE PROPOSED RULE CHANGES RELATING TO RESEARCH ANALYST CONFLICTS OF INTEREST**

[14650] April 18, 2002 TO: SEC RULES COMMITTEE No. 31-02 COMPLIANCE ADVISORY COMMITTEE No. 35-02 CLOSED-END INVESTMENT COMPANY COMMITTEE No. 16-02 RE: INSTITUTE LETTER ON NASD AND NYSE PROPOSED RULE CHANGES RELATING TO RESEARCH ANALYST CONFLICTS OF INTEREST The Institute has filed a comment letter with the Securities and Exchange Commission on proposed rule changes filed by NASD Regulation and the New York Stock Exchange to amend their rules to address research analyst conflicts of interest. The comment letter (a copy of which is attached) is substantially similar to the draft letter previously distributed to members.<sup>1</sup> The Institute's comments are limited to the effect of the proposals on investment advisory personnel, in particular portfolio managers of mutual funds and other discretionary accounts. The comment letter reiterates the comments made by the Institute in response to the NASD's proposal to amend NASD Rule 2210 to address analyst conflicts of interest,<sup>2</sup> particularly that the Institute strongly opposes the application of new disclosure requirements to portfolio managers. The letter notes that there are many differences in the potential conflicts of interest presented by "sellside" analyst recommendations and statements made by portfolio managers. Therefore, at least in the great majority of cases, any potential conflicts of interest for portfolio managers would be greatly attenuated. In addition, the letter notes that advisory firms already have stringent procedures in place to address potential conflicts relating to the personal investment activities of investment advisory personnel, including portfolio managers. The letter states that the Institute is therefore pleased that the proposing release specifically states that because most mutual fund portfolio managers are not principally responsible for the preparation of "research reports" as defined by the NASD's proposed rule change, a mutual fund portfolio manager generally would not be deemed to be a "research analyst," even if the portfolio manager is an associated person of a member firm and discusses 1 Memorandum to SEC Rules Committee No. 25-02, Compliance Advisory Committee No. 28-02 and Closed-End Investment Company Committee No. 12-02, dated March 27, 2002. 2 The NASD proposal would have imposed new disclosure requirements upon NASD members and their associated persons in an effort to address the potential conflicts of interest presented by analyst recommendations and would have applied to "portfolio managers of investment companies and other discretionary accounts ... where these managers are also associated persons of an NASD member." 2 the mutual fund's portfolio holdings in a television interview. The letter also states that the Institute believes that the NASD has properly excluded these

communications from the scope of the proposed rule as they do not present the types of concerns that the proposed rule change is designed to address. Finally, the letter seeks clarification on two aspects of the proposal. First, the letter requests clarification that the definition of “research report” would not include a report or statement, prepared by an investment adviser discussing the performance of a mutual fund, that includes a description of specific portfolio holdings. Second, the letter notes that the proposal does not contain a definition of the term “affiliate” for purposes of the disclosure requirements relating to a member organization’s ownership of securities. The letter therefore requests clarification that these disclosure requirements would not include the holdings of fiduciary accounts (e.g., mutual funds) managed by a member firm or its affiliate. Ari Burstein Associate Counsel Attachment (in .pdf format)

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