

MEMO# 14297

January 4, 2002

SEC REQUESTS COMMENT ON NASDR'S PROPOSED AMENDMENTS TO NASD RULES GOVERNING COMMUNICATIONS WITH THE PUBLIC; CONFERENCE CALL ON JANUARY 15, 2002

[14297] January 4, 2002 TO: ADVERTISING COMPLIANCE ADVISORY COMMITTEE No. 1-02 CLOSED-END INVESTMENT COMPANY COMMITTEE No. 1-02 SEC RULES COMMITTEE No. 1-02 UNIT INVESTMENT TRUST COMMITTEE No. 1-02 RE: SEC REQUESTS COMMENT ON NASDR'S PROPOSED AMENDMENTS TO NASD RULES GOVERNING COMMUNICATIONS WITH THE PUBLIC; CONFERENCE CALL ON JANUARY 15, 2002 The Securities and Exchange Commission has published for comment NASD Regulation Inc.'s proposed amendments to NASD rules governing member communications with the public.¹ The proposed amendments reflect many of the comments made in the Institute's letter in response to NASDR's 1999 request for comments.² In particular, the proposed amendments retain the distinction between institutional and retail investors and expand the definition of "institutional investor." A copy of the SEC's release is attached and highlights of the proposed amendments are briefly summarized below. Comments on the proposed amendments must be filed with the SEC by February 14, 2002. The Institute will hold a conference call on Tuesday, January 15th at 2:00 p.m. to discuss the proposed amendments. If you are interested in participating, please complete and return the attached form. If you are unable to participate in the call, please provide your comments to Tami Reed by January 15, 2002 (via phone: 202/326-5825; fax: 202/326-5839; or e-mail: tamara@ici.org). Institutional Investors The proposed amendments would create new Rule 2211, which would apply to institutional sales material and correspondence, and would exclude all communications to 1 SEC Release No. 34-45181, 66 Fed. Reg. 67586 (Dec. 31, 2001). 2 See Memorandum to Advertising Compliance Advisory Committee No. 17-99 and SEC Rules Committee No. 65-99, dated Sept. 10, 1999, and Memorandum to Unit Investment Trust Committee No. 20-99 and Closed-End Investment Company Committee No. 29-99, dated Sept. 15, 1999 (transmitting NASDR's request for comment) and Memorandum to Advertising Compliance Advisory Committee No. 22-99, SEC Rules Committee No. 88-99, Closed-End Investment Company Committee No. 40-99, and Unit Investment Trust Committee No. 30-99, dated Nov. 1, 1999 (transmitting Institute's comment letter to NASDR). 2 institutional investors from member pre-use approval and NASDR filing requirements, and from many of the content standards. In addition, the proposed rule change would define "institutional investor" as any: (1) person described in Rule 3110(c)(4),³ regardless of whether that person has an account with an NASD member;

(2) governmental entity or subdivision thereof; (3) qualified plan, as defined in Section 3(a)(12)(C) of the Securities Exchange Act of 1934, that has at least 100 beneficiaries; (4) NASD member or registered associated person of such a member; and (5) person acting solely on behalf of any such institutional investor.

Article Reprints In response to comments that article reprints should be exempt from most of the content standards of Rule 2210 (in addition to the exemption from the filing requirements as originally proposed), the proposed amendments would define a new type of communication with the public – an “independently prepared reprint” – which would be exempt from the filing requirements and most of the content standards. Independently prepared reprints would continue to be subject to the pre-use approval and record-keeping requirements of Rule 2210. An independently prepared reprint would consist of any article reprint that meets certain standards designed to ensure that the reprint was issued by an independent publisher and was not materially altered by the member.

Public Appearances The proposed amendments would “clarify the application of Rule 2210 to public appearances by defining [them] as a type of communication with the public” to include: participation in a seminar, forum (including an interactive electronic forum), radio or television interview, or other public appearance or public speaking activity. “The proposed rule change also would provide members with more flexibility than they currently have today, by subjecting public appearances only to some, but not all, of the content standards of Rule 2210.”

Standards Applicable to Member Communications The proposed rule change would substantially shorten and simplify the content standards applicable to member communications that are contained in Rule 2210(d). In addition to other changes, the proposed amendments would provide that “information may be placed in a legend or footnote only in the event that such placement would not inhibit an investor’s understanding of the communication,” rather than require that material information appear in the main text of a communication, as originally proposed.

Ranking Guidelines The proposed rule change would modify the ranking guidelines in several respects. First, the proposed rule change would clarify that no advertisement, item of sales literature or correspondence may present a ranking other than rankings: (1) created and published by a 3 Rule 3110(c)(4) defines “institutional account” to mean the account of a bank, savings and loan, insurance company, registered investment company, or registered investment adviser. It also includes the amount of any other entity or natural person with total assets of at least \$50 million. 3 Ranking Entity,⁴ or (2) created by an investment company or an affiliate, but based on the performance measurements of a Ranking Entity. Second, the proposed amendments would clarify that the ranking guidelines apply only to advertisements and sales literature. Third, the proposed rule change would permit the use of investment company family rankings, even in sales material that advertises only one investment company in the family, provided that “when a particular investment company is being advertised, the individual rankings for that investment company also must be presented.” In response to comments about the concerns of “cherry picking,” the proposed amendments will retain the existing language concerning the required ranking periods, as opposed to changing them to “short, medium and long-term periods” as originally proposed. Finally, the proposed rule change also would eliminate the requirement that certain disclosures appear in “close proximity” to any headline or other prominent statement that refers to a ranking.

Filing Requirements Regarding shareholder reports, the release notes that in NASDR’s experience, “members frequently use the MDFP or other supplemental information as marketing material that goes far beyond the SEC regulatory requirements for shareholder reports.” Consequently, despite receiving comments to the contrary, the proposed amendments do not propose an exclusion from the filing requirement for shareholder reports. Additionally, the proposed amendments do not propose to exclude generic fund advertisements from the filing requirements because NASDR is “concerned that an exclusion for generic advertisements

could lead some members not to file investment company sales material that should be filed due to their misunderstanding of Rule 135a.” Doretha VanSlyke Zornada Associate Counsel Attachment no. 1 (in .pdf format) 4 The proposed amendments define “Ranking Entity” as “any entity that provides general information about investment companies to the public, that is independent of the investment company and its affiliates, and whose services are not procured by the investment company or any of its affiliates to assign the investment company a ranking.”

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