

**MEMO# 15056**

August 20, 2002

# **NASD PROPOSED INTERPRETIVE MATERIAL REGARDING INVESTMENT ANALYSIS TOOLS**

ACTION REQUESTED [15056] August 20, 2002 TO: ADVERTISING COMPLIANCE ADVISORY COMMITTEE No. 15-02 INVESTMENT ADVISERS COMMITTEE No. 15-02 PENSION COMMITTEE No. 33-02 SEC RULES COMMITTEE No. 65-02 RE: NASD PROPOSED INTERPRETIVE MATERIAL REGARDING INVESTMENT ANALYSIS TOOLS NASD has issued a Notice to Members seeking comment on proposed Interpretive Material to NASD Rule 2210.1 The proposed Interpretive Material would provide a limited exception to Rule 2210(d)(2)(N), which prohibits NASD member firms from making predictions or projections of investment results to the public. The exception would allow NASD members to make available to their customers "investment analysis tools" under certain circumstances. NTM 02-51 is briefly summarized below. Comments on the proposed Interpretive Material must be filed with NASD by September 13th. If there are issues you would like us to consider addressing in a comment letter on the proposal, please contact me at (202) 326-5822 or frances@ici.org by Thursday, August 29th. As indicated in NTM 02-51, NASD previously has interpreted Rule 2210(d)(2)(N) to prohibit members from providing customers with access to automated tools that indicate the probability that an investment strategy will produce a desired result. Under the proposed Interpretive Material, members would be permitted to provide their customers direct access to "interactive analysis tools," which would be defined as interactive technological tools that produce simulations and statistical analyses showing a range of probabilities that various investment outcomes might occur. NTM 02-51 notes that while NASD members have not been permitted to provide their customers with direct access to such tools under current NASD rules, other financial advisors and institutions have offered public access to similar automated tools for some time. According to NTM 02-51, "[w]ith appropriate disclosures and other safeguards, NASD believes that investors could properly use these tools in making judgments about how an investment strategy might perform." 1 NASD Notice to Members 02-51 (August 2002) ("NTM 02-51"). NTM 02-51 is available on NASD's website at <http://www.nasdr.com/pdf-text/0251ntm.pdf>. 2 The proposed Interpretive Material would impose several disclosure and other requirements on the use of investment analysis tools and related sales material. For example, members would have to: (1) disclose the entire range of possible outcomes, giving both downside risk and upside gain; (2) disclose the universe of investments considered and state that other investments not considered might have characteristics similar to those that the tools analyze; (3) explain all material assumptions in a clear and understandable manner; and (4) disclose whether the tools search, analyze, or in any way favor certain securities within the universe of securities considered and explain the reasons for such selectivity. In addition, NASD members would be required to provide NASD's Advertising Regulation Department

with access to any investment analysis tools they intend to offer at least 30 days prior to first use and to file any sales material concerning the tools at least 30 days prior to use. Furthermore, the proposed Interpretive Material states that NASD members that offer an investment analysis tool are responsible for ensuring that use of the tool and all recommendations based on the tool comply with NASD's suitability rule (Rule 2310), the other provisions of Rule 2210, and the other applicable federal securities laws and SEC and NASD rules. Frances M. Stadler Deputy Senior Counsel

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