

MEMO# 13639

June 18, 2001

REGULATION FD AND THE USE OF CONFIDENTIALITY AGREEMENTS

[13639] June 18, 2001 TO: FIXED-INCOME ADVISORY COMMITTEE No. 8-01 RE: REGULATION FD AND THE USE OF CONFIDENTIALITY AGREEMENTS The Institute has received from outside counsel the attached memorandum on Regulation FD and the legal consequences of entering into confidentiality agreements. Although Regulation FD does not apply to municipal securities issuers, the discussion on confidentiality agreements is nevertheless noteworthy. The memorandum states that as a byproduct of enactment of Regulation FD, issuers increasingly are demanding confidentiality agreements prior to communicating with investment management personnel. The memorandum explains that while these arrangements free the issuer of Regulation FD concerns, they may expose an adviser's investment personnel to insider trading liability (either by being deemed a "temporary insider" or under the "misappropriation" theory) should they trade securities on the basis of material, nonpublic information received under the confidentiality agreement. The memorandum then suggests certain guidelines for members to consider before entering into such arrangements. First, fund complexes generally should inform their personnel about the implications of entering into confidentiality agreements with issuers, particularly in a volatile market where any trading restriction may be a significant impediment to an adviser's effectiveness. Second, any confidentiality agreement with an issuer should be reviewed, in advance, by the adviser's counsel. Third, confidentiality agreements should terminate at a fixed time, which would provide a clear standard for the extent of the restriction. Fourth, confidentiality agreements should be in writing so as to eliminate any confusion about their existence. Finally, any fund complex relying on so-called "Chinese Wall" procedures must ensure that they are demonstrably effective. The memorandum suggests that advisers should: (i) obtain written certifications from employees receiving information that they are aware of the procedures; (ii) ensure that material, nonpublic information received under the agreement is inaccessible to other employees; (iii) ensure that personnel involved with the issuer receive no information about the adviser's trades in that issuer's securities; and (iv) monitor activity in the issuer's securities for compliance with the Chinese Wall procedures. Barry E. Simmons Associate Counsel Attachment 2Attachment (in .pdf format)