

Communications With the Public

FINRA Requests Comments on Proposed New Rules Governing Communications with the Public

Comment Period Expires: November 20, 2009

Executive Summary

FINRA requests comments on proposed new FINRA rules governing communications with the public. These new rules would replace current NASD Rules 2210 and 2211, the Interpretive Materials that follow NASD Rule 2210, and portions of Incorporated NYSE Rule 472. While the proposed rules are based upon these rules' current provisions, the new FINRA rules would employ new communications categories and require the filing of certain types of communications that currently are not required to be filed. The proposal also would make a number of other changes to the communications rules.

The text of the proposed rules is available on our Web site at www.finra.org/notices/09-55.

Questions concerning this *Notice* should be directed to:

- Joseph P. Savage, Vice President and Counsel, Investment Companies Regulation, at (240) 386-4534; or
- Thomas A. Pappas, Vice President and Director, Advertising Regulation, at (240) 386-4553.

September 2009

Notice Type

- Request for Comment
- Consolidated Rulebook

Suggested Routing

- Advertising
- Legal & Compliance
- Operations
- Senior Management

Key Topic(s)

- Communications With the Public
- Supervision

Referenced Rules & Notices

- NASD Rule 2210
- NASD IM-2210-1 through IM-2210-8
- NASD Rule 2211
- NASD Rule 3010
- NASD Rule 3110
- Incorporated NYSE Rule 472
- NTM 05-59
- Regulatory Notice 08-39
- Regulatory Notice 08-55
- Regulatory Notice 09-10
- SEA Rule 17a-4

Action Requested

FINRA encourages all interested parties to comment on the proposed new FINRA rules. Comments must be received by November 20, 2009. Firms and other interested parties can submit their comments using the following methods:

- Mail comments in hard copy to the address below; or
- Email written comments to pubcom@finra.org.

To help FINRA process and review comments more efficiently, persons commenting on these proposed changes should use only one method. Comments sent by hard copy should be mailed to:

Marcia E. Asquith
Senior Vice President and Corporate Secretary
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1500

Important Notes: The only comments that will be considered are those submitted pursuant to the methods described above. All comments received in response to this *Notice* will be made available to the public on the FINRA Web site. Generally, comments will be posted on the FINRA Web site one week after the end of the comment period.¹

Before becoming effective, a proposed rule change must be authorized for filing with the Securities and Exchange Commission (SEC) by the FINRA Board, and then must be approved by the SEC, following publication for public comment in the *Federal Register*.²

Current Rules Governing Communications with the Public

NASD Rules 2210 and 2211, and the Interpretive Materials that follow Rule 2210, generally govern all FINRA firms' communications with the public. Incorporated NYSE Rule 472 governs communications with the public of member firms that also are members of the New York Stock Exchange.

NASD Rule 2210 divides communications into six separate categories, as follows:

- **Advertisement** generally includes written (including electronic) retail communications that do not have a limited audience, such as newspaper, magazine, television and radio advertisements, billboards and Web sites.
- **Sales literature** generally includes written (including electronic) retail communications that have a more targeted audience, such as brochures, performance reports, telemarketing scripts, seminar scripts and form letters.

- **Correspondence** includes written letters, electronic mail, instant messages and market letters sent to (i) one or more existing retail customers; and (ii) fewer than 25 prospective retail customers within a 30-calendar-day period.
- **Institutional sales material** includes communications that are distributed or made available only to institutional investors. NASD Rule 2211 defines the term “institutional investor” to include registered investment companies, insurance companies, banks, broker-dealers, investment advisers, certain retirement plans, governmental entities, individual investors and other entities with at least \$50 million in assets.
- **Independently prepared reprint** includes reprints of articles from independent publications, as well as reports published by independent research firms.
- **Public appearance** includes unscripted participation in live events, such as interviews, seminars and call-in television and radio shows.

These definitions are important because the principal approval, filing and content standards apply differently to each category. For example, firms generally must have a principal approve all advertisements, sales literature and independently prepared reprints prior to use. This pre-use approval requirement does not apply to (1) institutional sales material or (2) correspondence, unless it is sent to 25 or more existing retail customers and includes an investment recommendation or promotes a product or service of the firm. While such communications do not require principal approval, firms still must establish and maintain policies and procedures to supervise them for compliance with applicable standards.

Firms must file certain advertisements and sales literature for review with FINRA's Advertising Regulation Department. For example, advertisements and sales literature concerning investment companies and variable insurance products must be filed within 10 days of first use, but firms are not required to file independently prepared reprints, correspondence or institutional sales material. The filing requirements also differ based on the firm using the material and its content.

Firms that previously have not filed advertisements with FINRA must file all advertisements at least 10 business days prior to use for a one-year period. Additionally, under NASD Rule 2210 and related Interpretive Materials, all firms must file advertisements concerning government securities, collateralized mortgage obligations (CMOs) and security futures at least 10 business days prior to use, and must withhold them from publication until any changes specified by FINRA staff have been made.

Incorporated NYSE Rule 472 requires a “qualified person” to approve prior to use each advertisement, sales literature or other similar type of communication. The NYSE Rule 472 definitions of “advertisement” and “sales literature” are similar to those used in NASD Rule 2210.

The communications rules include both general and specific content standards. Certain general standards apply to all communications, such as requirements that communications be fair and balanced, and provide a sound basis for evaluating the facts in regard to any particular security, industry or service, and prohibitions on omitting material facts whose absence would make the communication misleading. More particular content standards apply to specific issues or securities.

Proposal

Reorganization of Rules

The proposal creates a new FINRA Rule 2210 that would encompass, subject to certain changes, the provisions of current NASD Rules 2210 and 2211, NASD Interpretive Materials 2210-1 and 2210-4, and the provisions of Incorporated NYSE Rule 472 that do not pertain to research analysts and research reports. Each of the other Interpretive Materials that follow NASD Rule 2210 would receive its own FINRA rule number and would adopt the same communication categories used in FINRA Rule 2210.³

Communication Categories

The proposal reduces the number of current communication categories from six to three, as follows:

- ▶ **Institutional communication** would include communications that fall under the current definition of “institutional sales material” — *i.e.*, communications that are distributed or made available only to institutional investors. “Institutional investor” would have the same definition as under NASD Rule 2211(a)(3).
- ▶ **Retail communication** would include any written (including electronic) communication that is distributed or made available to more than 25 retail investors. “Retail investor” would include any person other than an institutional investor, regardless of whether the person is an existing or prospective customer.
- ▶ **Correspondence** would include any written (including electronic) communication that is distributed or made available to 25 or fewer retail investors, regardless of whether they are existing or prospective customers.

The proposal eliminates the current definitions of “advertisement,” “sales literature,” “institutional sales material,” “public appearance” and “independently prepared reprint” in NASD Rule 2210, as well as all of the definitions in NASD Rule 2211.⁴ The proposal also eliminates the definitions of “communication,” “advertisement,” “market letter” and “sales literature” in Incorporated NYSE Rule 472.

Communications that currently qualify as advertisements and sales literature generally would fall under the definition of “retail communication.” Communications that currently qualify as “institutional sales material” would fall within the definition of “institutional communication.”

Some communications that currently qualify as “correspondence” would continue to fall within that definition under the proposal. In addition, the proposed definition is not limited to form letters, market letters, electronic messages or instant messages, as it is under the current rule, but encompasses all communications distributed to 25 or fewer retail investors. However, communications sent to more than 25 retail investors in all cases would be considered retail communications.⁵

The proposal eliminates the terms “public appearance” and “independently prepared reprint.” However, as discussed below, the proposal largely incorporates the exceptions from the filing requirements and limited application of the content standards currently applicable to those communication categories. Also, public appearances that include recommendations of securities would be subject to new disclosure standards, as set forth below.

Approval, Review and Recordkeeping Requirements

Proposed FINRA Rule 2210(b)(1)(A) would require an appropriately qualified registered principal of the firm to approve each retail communication before the earlier of its use or filing with FINRA. The principal registration required to approve particular communications would depend upon the permissible activities for each principal registration category. The proposal eliminates Incorporated NYSE Rule 472(a)(1), which requires a “qualified person” to approve in advance each advertisement, sales literature or other similar type of communication by an NYSE member firm.

Proposed Rule 2210(b)(1)(B) continues to permit a Series 16 supervisory analyst approved pursuant to Incorporated NYSE Rule 344 to approve research reports on debt and equity securities. Proposed paragraph (b)(1)(C) maintains the current exception from the principal approval requirements for retail communications that another firm has filed with FINRA and that were found to meet applicable standards. Proposed paragraph (b)(1)(D) clarifies that the principal approval requirement does not apply to any retail communication that is solely administrative in nature.⁶

Proposed FINRA Rules 2210(b)(2) and (3) maintain the supervision and review standards for correspondence and institutional communications that currently are found in NASD Rules 2211 and 3010(d).

Proposed FINRA Rule 2210(b)(4)(A) sets forth the record-keeping requirements for retail and institutional communications. This provision incorporates by reference the record-keeping form and time period requirements of SEA Rule 17a-4. Paragraph (b)(4)(A) specifies that such records would have to include:

- a copy of the communication and the dates of first and (if applicable) last use;
- in the case of an institutional communication, the name of the person who prepared or distributed the communication;
- the name of any registered principal who approved the communication and the date approval was given;
- the source of any statistical table, chart, graph or other illustration used in the communication; and
- for retail communications that rely on the exception under paragraph (b)(1)(C), the name of the firm that filed the retail communication and a copy of FINRA's review letter.

Proposed FINRA Rule 2210(b)(4)(B) cross-references NASD Rules 3010(d) and 3110(a) with respect to correspondence record-keeping requirements.

Filing Requirements and Review Procedures

Proposed FINRA Rule 2210(c) generally incorporates the same filing requirements as NASD Rule 2210(c), subject to certain changes.

NASD Rule 2210(c)(5)(A) currently requires a firm that previously has not filed advertisements with FINRA or another self-regulatory organization to file its initial advertisement with FINRA at least 10 business days prior to use. This filing requirement continues for a year after the initial filing.

Proposed FINRA Rule 2210(c)(1)(A) alters the filing requirements for new firms in two respects. First, the proposal expands this new firm filing requirement to cover all retail communications, rather than just advertisements. Second, the proposal triggers the one-year filing requirement beginning on the effective date a firm becomes registered with FINRA, rather than on the date an advertisement is first filed with FINRA.

NASD Rule 2210(c)(4) currently requires firms to file certain communications at least 10 business days prior to first use and to withhold them from use until any changes specified by FINRA staff have been made. These communications include advertisements and sales literature for certain registered investment companies that include self-created rankings, advertisements concerning collateralized mortgage obligations (CMOs), and advertisements concerning security futures.

Proposed FINRA Rule 2210(c)(2) expands the categories of communications that fall within this pre-use filing requirement. These include retail communications concerning any registered investment company that include self-created rankings, retail communications concerning CMOs and security futures, and retail communications that include bond mutual fund volatility ratings.

The proposal also requires firms for the first time to file prior to use retail communications concerning any publicly offered securities derived or based on a single security, a basket of securities, an index, a commodity, a debt issuance or a foreign currency.⁷ The purpose of this provision is to require the filing of retail communications concerning publicly offered structured products, such as exchange-traded notes, that currently are not required to be filed. This provision excludes retail communications that already are subject to a separate filing requirement found elsewhere in proposed paragraph (c), such as retail communications concerning registered investment companies or public direct participation programs.

The proposal revises the current filing standards for retail communications concerning closed-end investment companies. Currently NASD Rule 2210 requires firms to file within 10 business days of first use advertisements and sales literature concerning a closed-end fund that are distributed during the fund's initial public offering (IPO) period, as well as all advertisements and sales literature concerning continuously offered (interval) closed-end funds.⁸ Proposed FINRA Rule 2210(c)(3)(A) requires firms to file all retail communications concerning closed-end funds within 10 business days of first use, including those that are distributed after the fund's IPO period. FINRA believes that investors deserve the same protections concerning retail communications about closed-end funds that are distributed after the IPO period as those that are distributed during the IPO.

Proposed FINRA Rule 2210(c)(5) specifies that a firm must provide with each filing the actual or anticipated date of first use, the name, title and Central Registration Depository number of the registered principal who approved the communication, and the date approval was given. These requirements generally reflect current FINRA policy.

Proposed FINRA Rule 2210(c)(7) generally duplicates the current exclusions from the filing requirements under NASD Rule 2210(c)(8), with certain modifications. Proposed paragraph (c)(7)(A) adds an exclusion for retail communications that are based on templates that were previously filed with FINRA, the changes to which are limited to updates of more recent statistical or other non-narrative information.⁹ Proposed paragraph (c)(7)(B) excludes retail communications that are solely administrative in nature.

Proposed paragraph (c)(7)(G) maintains but streamlines the exclusion for independently prepared reprints currently found in NASD Rule 2210(c)(8)(H). Although the proposal deletes language defining investment company research reports, it deems these communications part of the category of independently prepared reprints exempt from filing.

The proposal eliminates a current filing exclusion for press releases that are made available only to members of the media.¹⁰ FINRA staff has found that firms almost always post press releases on their Web sites, thus making them available to the general public. Accordingly, generally firms have not used this filing exclusion.

Content Standards

Proposed FINRA Rule 2210(d) reorganizes, but largely incorporates, the current content standards applicable to communications with the public that are found in NASD Rule 2210(d), NASD IM-2210-1, NASD IM-2210-4 and Incorporated NYSE Rules 472(i) and (j), subject to certain changes. Content standards that currently apply to advertisements and sales literature generally would apply to retail communications.

Proposed FINRA Rule 2210(d)(2)(B) expressly prohibits promissory statements or claims. FINRA staff already interprets NASD Rule 2210(d)(1)(B) to prohibit promissory language in firm communications and Incorporated NYSE Rule 472(i) specifically prohibits promissory statements.

Proposed paragraph (d)(3) applies the standards concerning disclosure of a firm's name to correspondence as well as to retail communications. Firms would be permitted to use the name under which a firm's broker-dealer business is conducted as disclosed on the firm's Form BD, as well as a fictional name by which a firm is commonly recognized or which is required by any state or jurisdiction.

Proposed paragraph (d)(4)(C) adds new language concerning comparative illustrations of the mathematical principles of tax-deferred versus taxable compounding. Much of this language reflects previous guidance that FINRA has provided regarding tax-deferral illustrations.¹¹ By placing this rule language in proposed FINRA Rule 2210, FINRA is clarifying that these standards apply to any illustration of tax-deferred versus taxable compounding, regardless of whether it appears in a communication promoting variable insurance products or some other communication, such as one discussing the benefits of investing through a 401(k) retirement plan or individual retirement account.¹²

NASD Rule 2210(d)(3) requires communications with the public, other than institutional sales material and correspondence, that present the performance of a non-money market mutual fund to disclose the fund's maximum sales charge and operating expense ratio as set forth in the fund's current prospectus fee table.

Proposed FINRA Rule 2210(d)(5) alters this standard by requiring disclosure of the maximum sales charge and total operating expense ratio based on the fund's prospectus or annual report, whichever is more current as of the date of publication or submission for publication of a communication.

Proposed Rule 2210(d)(7) revises in several ways the standards currently found in NASD IM-2210-1(6) applicable to communications that contain a recommendation.

First, the proposal applies these standards to retail communications, correspondence and public appearances. Currently the standards apply only to advertisements and sales literature.

Second, IM-2210-1(6)(A)(ii) requires a disclosure if the firm and/or its officers or partners have a financial interest in the securities of the recommended issuer and the nature of the financial interest. The proposal instead requires disclosure if the firm or any associated person with the ability to influence the substance of the communication has a financial interest in the recommended issuer and the nature of the financial interest. This change would substantially narrow the number of parties whose financial interests have to be disclosed, particularly for large firms with numerous officers and partners. It also would more closely align the recommendation provisions of proposed FINRA Rule 2210 with the disclosure standards of proposed FINRA Rule 2240 (which would replace current NASD Rule 2711 and portions of Incorporated NYSE Rule 472¹³) concerning research reports.

Third, proposed FINRA Rule 2210(d)(7)(C) amends the provisions governing communications that include past recommendations, which are currently found in NASD IM-2210-1(6)(C) and (D) and Incorporated NYSE Rule 472(j)(2). The new proposed standards mirror those found in Rule 206(4)-1(a)(2) under the Investment Advisers Act of 1940, which apply to investment adviser advertisements that contain past recommendations.

Under the proposed standard, retail communications and correspondence could set out or offer to furnish a list of all recommendations of the same type, kind, grade or classification of securities made by the firm within the immediate preceding period of not less than one year, if the communication stated the name of each recommended security, the date and nature of the recommendation, the market price at that time, the price at which the recommendation was to be acted upon, and the market price of each such security as of the most practicable date. The communication also would have to include a prescribed legend warning that future recommendations may not be as profitable.

Fourth, proposed FINRA Rule 2210(d)(7)(D) expressly excludes from its coverage communications that meet the definition of "research report" for purposes of proposed FINRA Rule 2240 and that include all of the applicable disclosures required by that rule. Proposed paragraph (d)(7)(D) also excludes any communication that recommends only registered investment companies or variable insurance products.

Proposed FINRA Rule 2210(e) replaces current NASD IM-2210-4, which addresses limitations on firms' use of FINRA's name and any other corporate name owned by FINRA. This provision adds language that codifies FINRA's current position that any reference to FINRA staff's review of a communication is limited to either "Reviewed by FINRA" or "FINRA Reviewed."

Proposed FINRA Rule 2210(f) sets forth the standards that apply to public appearances. Public appearances would have to meet the general "fair and balanced" standards of proposed FINRA Rule 2210(d)(1), and the standards applicable to recommendations contained in proposed paragraph (d)(7) if the public appearance included a recommendation of a security. In this regard, associated persons who recommend securities in public appearances generally would be subject to the same disclosure requirements under proposed FINRA Rule 2210(f) as research analysts that recommend securities in public appearances pursuant to NASD Rule 2711(h). The proposal also requires firms to establish appropriate written policies and procedures to supervise public appearances, and makes clear that scripts, slides, handouts or other written and electronic materials used in connection with public appearances are considered communications with the public for purposes of proposed FINRA Rule 2210.¹⁴

Use of Investment Company Rankings in Retail Communications

Proposed FINRA Rule 2212 replaces NASD IM-2210-3 with regard to standards applicable to the use of investment company rankings in communications. The standards generally would remain the same, but would apply to retail communications instead of advertisements and sales literature. The proposal adds a new paragraph (h) that excludes from the rule's coverage reprints or excerpts of articles or reports that are excluded from FINRA's filing requirements pursuant to proposed FINRA Rule 2210(c)(7)(G).

Requirements for the Use of Investment Analysis Tools

Proposed FINRA Rule 2214 replaces NASD IM-2210-6 with regard to standards applicable to the use of investment analysis tools with retail customers. The standards would remain the same, but some language that is currently contained either in IM-2210-6's text or in footnotes would be moved to supplementary material.

Guidelines for Communications With the Public Regarding Security Futures

Proposed FINRA Rule 2215 replaces NASD IM-2210-7 with regard to standards applicable to communications concerning security futures. Proposed FINRA Rule 2215 revises the current standards in several respects to conform to NASD Rule 2220.¹⁵

First, portions of NASD IM-2210-7 apply only to advertisements. Proposed FINRA Rule 2215 applies these provisions to all retail communications.

Second, the proposal amends the provisions that require communications concerning security futures to be accompanied or preceded by the security futures risk disclosure document under certain circumstances. As revised, a communication concerning security futures would have to be accompanied or preceded by the risk disclosure document if it contained the names of specific securities.

Third, proposed paragraph (b)(2)(A) prohibits security future communications that contain any statement suggesting the certain availability of a secondary market for security futures. Fourth, proposed paragraph (b)(2)(C) requires any statement referring to the potential opportunities or advantages presented by security futures to be balanced by a statement of the corresponding risks, and requires the same degree of specificity.

Fifth, proposed paragraph (b)(4)(D) clarifies that communications that contain the historical performance of security futures must disclose all relevant costs, which must be reflected in the performance.

Endnotes

- 1 *See Notice to Members 03-73* (November 2003) (NASD Announces Online Availability of Comments). Personal identifying information, such as names or email addresses, will not be edited from submissions. Submit only information that you wish to make publicly available.
- 2 Section 19 of the Securities Exchange Act of 1934 (Exchange Act or SEA) permits certain limited types of proposed rule changes to take effect upon filing with the SEC. The SEC has authority to summarily abrogate these types of rule changes within 60 days of filing. *See* Exchange Act Section 19 and the rules thereunder.
- 3 Proposed FINRA Rule 2211 (Communications with the Public About Variable Insurance Products), which replaces NASD Interpretive Material 2210-2, is the subject of a separate, proposed rule change. *See Regulatory Notice 08-39* (July 2008) (FINRA Requests Comments on Proposed New Rules Governing Communications About Variable Insurance Products).
- 4 NASD Rule 2211 currently defines the terms “correspondence,” “institutional sales material,” “institutional investor,” “existing retail customer,” “prospective retail customer” and “market letter.”
- 5 The definition of “correspondence” in NASD Rule 2211 currently includes market letters as well as written letters and electronic mail messages that are sent to one or more existing retail customers and fewer than 25 prospective retail customers. FINRA revised the definition of “correspondence” to include market letters in February 2009 in order to allow firms to send market letters to traders and other investors who base their decisions on timely market analysis without having to have a principal approve them in advance. Previously, firms were required to approve market letters prior to use, which sometimes inhibited the flow of information to these parties. *See Regulatory Notice 09-10* (SEC Approves Rule Relating to Supervision of Market Letters) (Feb. 2009).
- Proposed FINRA Rule 2210 continues to allow firms to send communications (including market letters) to institutional investors without having a principal approve such communications prior to use. FINRA believes that, by continuing to allow firms to send information to institutional investors without principal approval, the proposed rule change largely addresses the concerns that led to including market letters within the current definition of “correspondence.”
- 6 This exception to the principal approval requirement for administrative communications is similar to the current exclusion from FINRA’s filing requirements for advertisements and sales literature solely related to recruitment or changes in a firm’s name, personnel, electronic or postal address, ownership, offices, business structure, partners, telephone and teletype numbers, or concerning a merger with, or acquisition by, another firm. *See* NASD Rule 2210(c)(8)(B).
- 7 This proposed rule language is derived from a description of the term “structured product” in *Notice to Members 05-59* (September 2005) (NASD Provides Guidance Concerning the Sale of Structured Products) and is intended to cover retail communications concerning such products.

Endnotes continued

- 8 See "Ask the Analyst," *Regulatory & Compliance Alert* (Winter 1999) p. 13.
- 9 This exclusion is based in part on an earlier staff interpretation concerning how NASD Rule 2210's approval, record-keeping and filing requirements apply to statistical updates contained in pre-existing templates. See Letter from Thomas M. Selman, NASD, to Forrest R. Foss, T. Rowe Price Associates, Inc. (Jan. 28, 2002).
- 10 See NASD Rule 2210(c)(8)(G).
- 11 See "NASD Reminds Members of Their Responsibilities Regarding Hypothetical Tax-Deferral Illustrations in Variable Annuity Illustrations," *Member Alert* (May 10, 2004).
- 12 FINRA previously published this proposed rule language for comment as part of proposed changes to the rules governing communications about variable insurance products. See *Regulatory Notice 08-39* (July 2008) (FINRA Requests Comments on Proposed New Rules Governing Communications About Variable Insurance Products). Proposed FINRA Rule 2210 would incorporate these earlier proposed changes, which have been removed from the rule proposal concerning variable insurance products communications. FINRA expects to file with the SEC the proposed rule change to adopt FINRA Rule 2211 regarding communications with the public about variable insurance products in the near future.
- 13 See *Regulatory Notice 08-55* (October 2008).
- 14 The requirement to establish supervisory policies and procedures for public appearances is consistent with NASD Rule 3010(b) and Incorporated NYSE Rule 472(I).
- 15 FINRA is proposing to adopt NASD Rule 2220 (Options Communications) without substantive change into the Consolidated FINRA Rulebook as FINRA Rule 2220. See SEC Rel. No. 34-60066 (June 8, 2009), 74 Fed. Reg. 28308 (June 15, 2009).