December 16, 2014

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Via email to rule-comments@sec.gov

Brent J. Fields, Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: Comments Regarding SR-FINRA-2014-047 - Proposed Rule to Adopt FINRA Rule 2241 (Research Analysts and Research Reports)

Dear Mr. Fields:

We are writing on behalf of our clients, Barclays Capital Inc., Citigroup Global Markets Inc., Credit Suisse Securities (USA) LLC, Deutsche Bank Securities Inc., Goldman, Sachs & Co., J.P. Morgan Securities LLC, Merrill Lynch, Pierce, Fenner & Smith Incorporated, Morgan Stanley & Co. LLC, RBC Capital Markets, LLC, and UBS Securities LLC (together, the "Firms") in response to a request for comment by the Securities and Exchange Commission ("SEC") regarding the above-referenced rule proposal by the Financial Industry Regulatory Authority, Inc. ("FINRA").[1] The Firms appreciate the opportunity to comment on FINRA's proposal to establish new FINRA Rule 2241 regarding equity research analysts and equity research reports (the "Proposed Rule"). As discussed more fully below, the Firms support much of the Proposed Rule. The Firms ask, however, that FINRA consider certain important modifications and clarifications to the Proposed Rule, which are consistent with the objectives of providing clarity to the industry and reducing costs and burdens on member firms without undermining investor protection.

I. Introduction

As an initial matter, the Firms greatly appreciate the time and effort that FINRA has spent engaging with market participants through the issuance of Regulatory Notices, the provision of opportunities for comment, and the consideration of industry comments prior to filing the Proposed Rule with the SEC.[2] The Firms also agree that many provisions of the Proposed Rule

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[1] Notice of Filing of a Proposed Rule to Adopt FINRA Rule 2241 (Research Analysts and Research Reports) in the Consolidated FINRA Rulebook, Release No. 34-73622, 79 Fed. Reg. 69939 (Nov. 24, 2014) ("Rule Filing"). In a separate comment letter, the Firms are also submitting comments regarding Notice of Filing of a Proposed Rule Change to Adopt FINRA Rule 2242 (Debt Research Analysts and Debt Research Reports), Release No. 34-73,623, 79 Fed. Reg. 69905 (Nov. 24, 2014) ("Debt Research Rule Filing").

[2] *See* FINRA Regulatory Notice 08-55, Research Analysts and Research Reports—FINRA Requests Comment on Proposed Research Registration and Conflict of Interest Rules (Oct. 2008) ("Reg Notice 08-55").

will help ensure that investors receive objective research, while facilitating the flow of information to investors and reducing burdens on member firms. In particular, the Firms support FINRA's decisions to: (i) eliminate the fifteen-day quiet period surrounding the expiration, waiver, or termination of a lock-up agreement; (ii) amend the definition of "research analyst" for purposes of the analyst registration requirements to limit these requirements to persons whose primary job function is to provide investment research; (iii) eliminate the annual attestation requirement; (iv) provide a more flexible framework for personal trading and conflicts of interest,[3] and a transitional structure for equity research analyst accounts to unwind, in an orderly and planned manner, holdings that might be construed as prohibited under the Proposed Rule; and (v) include a provision granting FINRA exemptive authority for good cause.

In addition to the aforementioned changes, the Firms appreciate certain important modifications and clarifications that FINRA made to the rule initially proposed in Reg Notice 08-55, including the following:

- clarification that members may rely on information barriers "or" other institutional safeguards reasonably designed to ensure that analysts are properly shielded from certain reviews, pressures, or oversight;

- clarification that the prohibition on analysts' participation in road shows and other marketing on behalf of issuers does not apply to investor education activities and only applies to road shows and marketing activities "related to an investment banking services transaction"; and

- clarification that commitment committee participation, permissible due diligence, and education of the sales force and investors are legitimate factors to consider in measuring the productivity and quality of research when determining analyst compensation, so long as they are not given undue weight.[4]

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[3] The Firms assume that the proposed principles-based approach to research analyst personal trading would continue to permit trading that is currently allowed in NASD Rule 2711(g)(5) (*e.g.*, allowance for trading in any registered diversified investment company as defined under Section (5)(b)(1) of the Investment Company Act of 1940).

[4] Other important changes and clarifications include the following: (i) clarification that the factors enumerated in Proposed Rule 2241(b)(2)(F), to determine analyst compensation, must be considered only to the extent applicable; (ii) removal of the "in fact" language in the price target disclosure in Proposed Rule 2241(c)(1)(B); (iii) clarification in Proposed Rule 2241(c)(1)(B) that not all ratings are associated with a "valuation method"; (iv) streamlining the disclosures in Proposed Rule 2241(c)(4) by removing the superfluous language in the preamble; and (v) amendment of Proposed Rule 2241(h)(2) to prohibit a member from distributing third-party research that it knows or has reason to know is not objective or reliable, rather than imposing a duty of inquiry to definitively ascertain whether the third-party research is objective and reliable.

Recognizing these efforts, the Firms have nevertheless identified a few concerns and a number of important changes and clarifications to the Proposed Rule that FINRA should consider in order to provide greater clarity to the industry and reduce the burdens and costs on the industry without compromising investor protection. We set forth these comments below, which are organized sequentially to correspond to the relevant provisions of the Proposed Rule.[5]

II. Specific Areas of Comments

A. Proposed Rule 2241(a) Should Be Supplemented To Include Certain Important Definitions and Carveouts.

1. "Sales and Trading Department Personnel"

Proposed Rule 2241(a) should be amended to include a definition of "sales and trading department personnel." This is critical because there are several provisions that impose restrictions, prohibitions, or limitations relating to "sales and trading department personnel."[6]

The Firms believe a definition along the lines of the following would be consistent with a stated purpose of the Proposed Rule: "persons who are primarily responsible for performing sales and trading activities, or exercising direct supervisory authority over such persons." Such a definition would provide member firms with the flexibility "to establish and maintain supervisory programs [and reporting lines] best suited to their business models," but at the same time would not undermine investor protection because research analysts would be adequately insulated from those persons who are directly engaged in sales and trading activities.[7] The use of the term "primarily" is also an important clarification because it accurately captures those

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[5] The Firms note that certain comments below are also provided in its Debt Research Rule Filing comment letter for corresponding provisions in Proposed FINRA Rule 2242. These common comments appear in Sections II.A–II.D, II.F, II.G.2, and II.H-II.J of this letter.

[6] *See* Proposed Rule 2241(b)(1)(C) (requiring policies and procedures to identify and manage conflicts of interest related to the interaction between research analysts and sales and trading department personnel); Proposed Rule 2241(b)(2)(G) (requiring policies and procedures to establish information barriers or other institutional safeguards to ensure that research analysts are insulated from the review, pressure or oversight by sales and trading department personnel); and Proposed Rule 2241(i) (requiring member firms with limited investment banking activity to continue to comply with the requirements of Proposed Rule 2241(b)(2)(G)).

[7] *See* Rule Filing, *supra* note 1, at 69942 ("FINRA believes this approach [of mandated policies and procedures] will . . . impose less cost than a pure prescriptive approach by requiring member firms to adopt a compliance system that aligns with their particular structure, business model, and philosophy.") This suggested approach is also consistent with the approach adopted by the Commodity Futures Trading Commission ("CFTC") in Rules 1.71(a)(2) and 23.605(a)(2), under which the "business trading unit" includes persons who directly perform or exercise supervisory authority over the performance of the tasks listed in the rule.

persons whose job responsibilities are properly classified as sales and trading.[8] Notably, this is the same approach that FINRA took in its proposed amendments to NASD Rule 1050, which appropriately recognize that an individual's categorization as a "research" versus "sales and trading" employee should turn on that person's primary responsibilities.

2. "Research Report"

Proposed Rule 2241(a) should be amended to include an exclusion from the definition of "research report" for private placement memoranda and similar offering-related documents prepared in connection with investment banking services transactions. As an initial matter, the Firms note that such offering-related documents are typically prepared by investment banking personnel, or other non-research personnel on behalf of investment banking personnel. Thus, including such materials in the definition of "research report" would have the incongruous effect of turning investment banking personnel into research analysts (because a research analyst is defined as someone who produces a "research report"). Additionally, NASD Rule 2711(a) currently includes an exclusion from the definition of "research report" for "communications that constitute statutory prospectuses" (which also are prepared by or with input from investment banking personnel). The Firms believe that the basis for excluding prospectuses from the definition of "research report" should apply equally to private placement memoranda and similar offering-related documents prepared by non-research personnel in connection with investment banking services transactions.

B. Proposed Rule 2241(b)(2) Should Be Modified To Clarify that Compliance with All of the Prohibitions, Prescriptions, and Restrictions in that Provision May Be Sufficient To Satisfy that Provision.

Proposed Rule 2241(b)(2) contains detailed prohibitions, prescriptions, and restrictions regarding the written policies and procedures that member firms must adopt "to promote objective and reliable research that reflects the truly held opinions of research analysts and to prevent the use of research reports or research analysts to manipulate or condition the market or favor the interests of the member or a current or prospective customer or class of customers." These requirements build on and significantly expand the prohibitions and restrictions currently

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[8] The Proposed Rule contains many references to individuals "engaged in" specified activities, including sales, trading, and investment banking. The Firms believe that in determining the universe of individuals engaged in specified activities, member firms should not conclude that simply because an individual might, *e.g.*, occasionally speak to a customer or have persons from sales reporting to him or her, the individual must be classified as sales personnel or as someone "engaged in" sales. Rather, an individual should be classified as, *e.g.*, sales, when he or she is primarily responsible for performing such functions or directly supervising individuals performing such functions.

in NASD Rule 2711.[9] However, unlike NASD Rule 2711, they are identified as "the minimum" policies and procedures that member firms must adopt.[10] While the Firms understand that they are subject to each of the requirements listed in Proposed Rule 2241(b)(2) and that there may be circumstances that may necessitate additional requirements, they respectfully request that FINRA eliminate the "at a minimum" language in this provision because it is not clear what additional policies and procedures this language would require in every situation– particularly in light of the detailed and extensive nature of the requirements in Proposed Rule 2241(b)(2).

The Firms also do not believe that this language is necessary, given not only the extensive prohibitions, restrictions, and prescriptions in Proposed Rule 2241(b)(2), but also the broad principles-based language that serves as an overlay in Proposed Rule 2241(b)(1). To this point, Proposed Rule 2241(b)(1) contains a broad principles-based requirement that member firms establish, maintain, and enforce written policies and procedures to "identify and manage conflicts of interest" relating to (i) the preparation, content, and distribution of research reports, (ii) research analysts' public appearances, and (iii) the interaction between research analysts and those outside the research department, including investment banking and sales and trading department personnel, subject companies, and customers.

For the above reasons, the elimination of the phrase "at a minimum" would provide clarity regarding the applicability of existing rules, but would not diminish investor protection given the broad principles-based requirements in paragraphs (b)(1) and (b)(2) of the Proposed Rule.

C. Proposed Rule 2241(b)(2)(B) Should Be Clarified by Eliminating a Redundant or Unclear Term.

As currently drafted, Proposed Rule 2241(b)(2)(B) permits non-research personnel to have input into research coverage, so long as research management "independently makes all final decisions regarding the research coverage plan."

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[9] For example, the Proposed Rule includes several prohibitions relating to sales and trading that go beyond the requirements outlined in NASD Rule 2711 or Section 15D of the Securities Exchange Act of 1934, which focus primarily on the activities of, and prohibitions related to, investment banking personnel. *See* Proposed Rule 2241(b)(1)(C) (requiring policies and procedures to identify and manage conflicts of interest related to the interaction between research analysts and sales and trading department personnel); and Proposed Rule 2241(b)(2)(G) (requiring policies and procedures to establish information barriers or other institutional safeguards to ensure that research analysts are insulated from pressure by persons engaged in sales and trading).

[10] *See* Proposed Rule 2241(b)(2) (stating that "Such policies and procedures *must at a minimum*...") (emphasis added).

The Firms ask FINRA to eliminate the term "independently" because that term appears to be redundant with the notion of research management "making final decisions." If FINRA does not believe the term "independently" is redundant, it is unclear what is contemplated here because non-research personnel may, in fact, have input into research coverage under the terms of the Proposed Rule. Thus, if FINRA declines to eliminate this term, the Firms ask FINRA to confirm that member firms would satisfy the "independent" standard in Rule 2241(b)(2)(B) as long as research management makes the final determination regarding coverage decisions.[11]

D. Proposed Rule 2241(b)(2)(G) Should Be Clarified and Also Modified To Be Consistent with FINRA's General Supervisory Requirement that Firms Have "Reasonably Designed" Policies and Procedures.

As currently drafted, Proposed Rule 2241(b)(2)(G) requires member firms to "establish information barriers or other institutional safeguards to ensure that research analysts are insulated from the review, pressure or oversight by persons engaged in investment banking services activities or other persons, including sales and trading department personnel, who might be biased in their judgment or supervision."[12]

The Firms appreciate that this language has been clarified to permit member firms to establish "other institutional safeguards" (and not only "information barriers"), but ask FINRA to consider additional important modifications that are necessary (i) to provide clarity regarding certain requirements of this provision, and (ii) to conform this provision to FINRA's well-established "reasonably designed" standard for policies and procedures.

With respect to (i), the Firms believe the following changes are necessary to provide greater clarity:

- First, the term "review" in Proposed Rule 2241(b)(2)(G) should be eliminated because it appears to be redundant with the term "oversight." Moreover, the reason for including this provision relates to the oversight of research activities. As noted in the Rule Filing: "FINRA is including the provision to emphasize that the conflicts management must extend to persons other than investment banking personnel, including sales and trading department personnel, who may be placed in a position to

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[11] This request is consistent with the following general description of the requirement in the Rule Filing: "The proposed provision does not preclude investment banking personnel from conveying customer interests or providing input into coverage decisions, so long as final decisions regarding the coverage plan are made by research management." Rule Filing, *supra note* 1, at 69943.

[12] Proposed Rule 2241(b)(2)(G).

supervise or influence the content of research reports or public appearances."[13] If FINRA does not agree that the terms "review" and "oversight" are redundant, FINRA should clarify what the term "review" would require that is not already captured by the other provisions in Proposed Rule 2241. For example, Proposed Rule 2241(b)(2) already includes provisions that impose limits and prohibitions on investment banking personnel having input into analysts' compensatory evaluations and prepublication reviews of research reports by certain non-research personnel.

- Second, the Firms ask FINRA to clarify that the "information barriers or institutional safeguards" required by Proposed Rule 2241(b)(2)(G) are not intended to prohibit or limit activities that would otherwise be permitted under other provisions of Proposed Rule 2241.

- Finally, the Firms ask FINRA to clarify that "bias" and "pressure" for purposes of this provision are intended to address "persons who may try to improperly influence research views." The Firms appreciate that these terms may appear in certain provisions of the Sarbanes-Oxley Act of 2002,[14] but that fact should not prevent FINRA from providing clarifying guidance regarding their meaning for purposes of the Proposed Rule, particularly because these terms are so broad and ambiguous on their face.[15] For example, if a research analyst is pressured to change the format of a research report to comply with the research department's standard procedures or the member firm's technology specifications, it is not clear whether the member firm would have to assess whether the person applying the pressure had some sort of bias against the analyst.

Additionally, with respect to (ii), the Firms ask FINRA to modify Proposed Rule 2241(b)(2)(G) to conform to paragraphs (b)(1) and (b)(2) of the Proposed Rule by imposing a "reasonably designed" standard on the policies and procedures that member firms must adopt. The "reasonably designed" standard is also the legal standard that has historically been required by FINRA's general supervision rule and which is required by FINRA's new supervision rule, Rule 3110.

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[13] Rule Filing, *supra* note 1, at 69943.

[14] *See* Section 501 Sarbanes-Oxley Act, Pub. L. No. 107-204, 116 Stat. 745 (2002).

[15] For example, the term "bias" has been defined broadly as "a tendency to believe that some people, ideas, etc., are better than others that usually results in treating some people unfairly." *Bias Definition*, Merriam-Webster.com, http://www.merriam-webster.com/dictionary/bias (last visited Dec. 16, 2014).

E. The Significant News and Events Exception and the Rule 139 Exception Should Be Added to FINRA Rule 2241(b)(2)(I).

While the Firms endorse the amendments to the blackout periods in the Proposed Rule, the Firms request that FINRA reintroduce certain exceptions available in NASD Rule 2711(f)(1)(B), regarding blackout periods for IPOs and secondary offerings, to Proposed Rule 2241(b)(2)(I). Specifically, the Firms urge FINRA to retain the exception in NASD Rule 2711(f)(1)(B)(i), which permits member firms to publish or distribute research reports and make public appearances concerning the effects of significant news or significant events on the subject company. The Firms also encourage FINRA to reinstate the exception in NASD Rule 2711(f)(1)(B)(ii), which permits member firms to publish or distribute research reports pursuant to Securities Act Rule 139 regarding a subject company and make public appearances concerning the subject company. The Firms assume that the omission of these exceptions was unintentional given FINRA's stated desire to eliminate the quiet periods altogether.[16]

F. FINRA Should Amend the Preamble to Proposed Rule 2241(b)(2)(L) To Eliminate Redundancy.

In contrast to the other provisions in the Proposed Rule, such as paragraphs (A)-(K), (M) and (N) of Proposed Rule 2241(b)(2), Proposed Rule 2241(b)(2)(L) has a broad preamble that requires member firms to establish, maintain, and enforce policies and procedures that would "restrict or limit activities by research analysts that can reasonably be expected to compromise their objectivity" before identifying specific prohibited activities related to investment banking services transactions. As noted above, Proposed Rule 2241(b)(1) sets out a broad principles-based requirement that member firms establish, maintain, and enforce written policies and procedures reasonably designed to identify and effectively manage conflicts of interest, and Proposed Rule 2241(b)(2) would further require those policies and procedures to be reasonably designed to promote objective and reliable research. In light of these general requirements, it is unclear what additional requirements are intended to flow from the preamble in Proposed Rule 2241(b)(2)(L) or why it is necessary to require an additional principles-based requirement in this provision.

Accordingly, for the sake of clarity, the Firms ask FINRA to revise the preamble to Proposed Rule 2241(b)(2)(L) to state simply that member firms' policies and procedures must: "prohibit research analysts' participation in pitches and other solicitations of investment banking

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[16] Rule Filing, *supra* note 1, at 69944 ("As reflected in the Joint Report, FINRA was in favor of completely eliminating the quiet periods around secondary offerings; however, SEC staff has since indicated its view that the Sarbanes-Oxley reference to 'public offering of securities' encompasses both initial public offerings and secondary offerings and therefore mandates a quiet period after such public offerings, except for EGCs.") (footnote omitted).

services transactions, and their participation in road shows and other marketing on behalf of an issuer related to an investment banking services transaction."

G. Certain New Disclosure Requirements in Proposed Rule 2241(c) Will Impose Significant Burdens and Costs on Firms, and Should Be Reconsidered.

Proposed Rule 2241(c) contains new disclosure requirements, which will result in significant burdens and costs for member firms that would outweigh any investor protection benefits. For these reasons and as described more fully below, the Firms ask FINRA to reconsider these provisions.

1. Significant Financial Interests in Debt Securities Disclosure

Proposed Rule 2241(c)(4)(F) would require members to disclose, in an equity research report, if they or their affiliates maintain a significant financial interest in the debt of the subject company. Because the burden of this requirement is not counteracted by a sufficiently measurable benefit, this disclosure should not be added to the already lengthy list of required disclosures, which include a broad "catch-all" disclosure. In that regard, the Firms urge FINRA to adopt the approach it has taken in the proposed debt research rule by reminding member firms that potential conflicts created by a member firm's debt holdings are subject to the material conflict "catch-all" disclosure requirement. Specifically, in declining to include this separate requirement in the proposed debt research rule, FINRA explained that:

> FINRA did not include this provision in the proposed debt research rule because, ***unlike equity holdings, firms do not typically have systems to track ownership of debt securities***. Moreover, the number and complexity of bonds, together with the fact that a firm may be both long and short different bonds of the same issuer, ***make it difficult to have real-time disclosure of a firm's credit exposure***. Therefore, the proposed rule change only requires disclosure of firm ownership of debt securities in research reports or a public appearance to the extent those holdings constitute a material conflict of interest.[17]

The realities cited by FINRA detailing the difficulties associated with ascertaining debt ownership are equally relevant whether preparing the disclosure for an equity research report or a debt research report.[18] Firms would need to expend significant resources to build systems to track this information and integrate it into a research disclosure database.

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[17] *See* Debt Research Rule Filing, *supra* note 1, at 69914-915 (emphasis added).

[18] Additionally, although FINRA correctly noted that many global member firms are required, pursuant to U.K. Financial Conduct Authority ("FCA") Conduct of Business rules, to disclose financial interests held by the firm, the FCA standard for such financial disclosures is more akin to FINRA's proposed "catch-all" provision because firms

At the same time, it is not clear what benefit would be served if member firms are required to disclose their debt ownership in a particular issuer, given (i) the attenuated relationship between equity research ratings and the value of a particular credit that a member firm may hold, (ii) the fact that there are already extensive conflicts of interest disclosures in equity research (including equity ownership), and (iii) the fact that analysts may have no knowledge of a member firm's debt ownership interest in a particular issuer (which necessarily means that debt ownership could not have presented a conflict of interest in connection with the preparation of the research report).

For these reasons, the Firms respectfully request that FINRA apply the same standard to equity research reports as it proposes to apply to debt research reports – by addressing any such potential conflicts of interest through the material conflict "catch-all" disclosure requirement.

2. Expanded "Catch-all" Disclosure

Proposed Rule 2241(c)(4)(I) would significantly expand the "catch-all" disclosure in NASD Rule 2711(h)(1)(C), which currently requires the disclosure of "any other actual, material conflict of interest of the research analyst or member of which the research analyst knows or has reason to know at the time of publication of the research report or at the time of the public appearance." Under the proposed expanded disclosures, member firms would be required to also disclose any other material conflict of interest of the research analyst or the member firm that "an associated person of the member with the ability to influence the content of a research report knows or has reason to know…"

While the Firms understand that FINRA is proposing this expansion to address some perceived "gap" in the disclosure requirements,[19] the Firms respectfully submit that there has been no evidence presented of any gap or undisclosed conflicts that would require such an expansion. In contrast, the burdens and logistical difficulties of imposing this expanded disclosure would be very real and exceed any potential benefit. To this point, the expanded disclosure would create a logistical quagmire. It would slow down the research dissemination process and make it difficult to issue reports in a timely and efficient manner because it would require member firms to canvass all of research management, research supervisors, supervisory analysts, and legal and compliance personnel who may have the authority to review a research

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need only make such disclosure to the extent such holdings may reasonably be expected to "impair the objectivity of research recommendations" or are "significant in relation to the research recommendation." Financial Conduct Authority, Conduct of Business Sourcebook Rules 12.4.9(1)(a) and 12.4.10(1)(b).

[19] Rule Filing, *supra* note 1, at 69951 ("This provision would close a gap that exists whereby persons who oversee research and research analysts could influence the recommendation or conclusions in a research report without disclosing their own material conflicts of interest or those of the member of which only they, and not the research analyst, know or have reason to know.").

report before publication in order to determine if they are aware of a material conflict of interest that the analyst – who is the author of the report – does not know or have reason to know.

An expansion of the "catch-all" disclosure also would create significant issues because such persons (especially legal and compliance personnel) may possess confidential information that could be captured by this expanded "catch-all," and would not fall under the narrow exception in Proposed Rule 2241(c)(5) for disclosure of material nonpublic information regarding specific potential future investment banking transactions of the subject company (the "MNPI exception").

For example, legal and compliance personnel typically have access to a member firm's systems that contain information about *all* of a member firm's proposed *and* on-going activities. Because the "catch-all" is designed to capture "conflicts that should reasonably be discovered by those persons *in the ordinary course of discharging their functions*,"[20] this prohibition could be read to require the disclosure of material nonpublic information learned by legal and compliance personnel, through the ordinary course, that is unrelated to investment banking transactions of the subject company, such as when the member firm is assisting an institutional investor or executive officer in divesting a significant block of the subject company's stock. Additionally, a research supervisor who has been brought across the wall (as well as legal and compliance personnel) may be aware that the member firm is advising a merger between two of the company's competitors; such information would not fall within the MNPI exception because the proposed transaction is not an investment banking transaction "of the subject company."

Moreover, the proposed expanded "catch-all" disclosure is not necessary given the following significant protections and safeguards:

- All of the conflict of interest disclosures that are currently required in NASD Rule 2711 and would be required under the Proposed Rule;

- The additional information barriers, safeguards, policies and procedures that member firms must implement under paragraphs (b)(1) and (2) of the Proposed Rule that must be reasonably designed to "identify and manage" conflicts of interest and "promote objective and reliable research"; and

- The safeguards provided by Regulation Analyst Certification, which assure that any views and opinions expressed in a research report reflect those of the primary research analyst, even if such report has been amended to reflect any comments or review by supervisory analysts, research management, or others.

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[20] *Id.* at 69947 (emphasis added).

3. Confirmation Regarding Hyperlinked Disclosures

The Firms appreciate the reaffirmation in Proposed Rule 2241(c)(6) that "[e]lectronic research reports may provide a hyperlink directly to the required disclosures"[21] and request confirmation that member firms may rely on hyperlinked disclosures for research reports that are delivered electronically, even if these reports are subsequently "printed out" by customers, thereby being converted to hard copy format.

H. Firms Should Not Be Required To Disclose Whether an Alternative Research Product or Service Does in Fact Contain a Contrary Recommendation.

Proposed Rule 2241(g) and Supplementary Material .07 would allow member firms to provide different research products and services to different classes of customers, so long as they: (i) are not differentiated with respect to timing of receipt of recommendations, ratings, or other potentially market moving information; (ii) are not labeled so as to provide different customers with essentially the same products or services at different times; and (iii) are accompanied by appropriate disclosures that different products and services may reach different conclusions. In the Rule Filing, FINRA noted that it "will read with interest comments as to whether a member should be required to disclose to its other customers when an alternative research product or service does, in fact, contain a recommendation contrary to the research product or service that those customers receive." In response to this request, the Firms submit that the proposed disclosure requirement in Supplementary Material .07 is appropriate, and that requiring disclosure of specific instances of contrary recommendations would be unworkable and unjustified in light of the costs.

Complying with a requirement to disclose each such instance would require extremely close tracking and coordination of the content of each and every product or service in order to identify when a recommendation is being made and to determine the extent to which each such recommendation might be deemed "contrary" to the current recommendations in all other products and services. This is particularly difficult because a single firm may publish tens of thousands of research reports each year and employ hundreds of analysts across various disciplines. As such, neither a research analyst responsible for a particular report nor a supervisory analyst responsible for reviewing such report could reasonably be expected to be aware of all other research products or services that may contain differing views. It is also challenging because different research products and services may focus on different types of analyses or time horizons, such as technical versus fundamental research, or long-term versus short-term research, further complicating the determination of when recommendations are contrary. Where a research product or service does not have formal ratings applied, such as a

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[21] Proposed Rule 2241(c)(6); *see also* Rule Filing, *supra* note 1, at 69946.

relative-value analysis, the mere determination of what constitutes a recommendation would be time-consuming and challenging.

The Firms believe the burdens associated with implementing this complicated system to track and analyze all recommendations in different research products and services would outweigh any related benefits. As recognized in the Rule Filing, different audiences for research have different concerns and objectives, so recommendations that may appear contrary in different research products may simply be appropriately tailored to the interests or objectives of their respective audiences.[22]

I. FINRA Should Eliminate the Provision Specifying that Failure To Comply with Policies and Procedures Amounts to a Violation of the Rule.

Proposed Supplementary Material .09 states that the failure of an associated person to comply with a member firm's written policies and procedures "shall constitute a violation of this Rule." The Firms appreciate the fundamental point that member firm personnel should comply with a member firm's policies and procedures and that member firms need to enforce these policies and procedures. The Firms are concerned, however, that this statement may create a perverse incentive for some member firms to implement policies and procedures that are the "bare minimum" necessary to comply with the Proposed Rule by punishing member firms that adopt policies and procedures that exceed the Proposed Rule. For example, if a member firm is considering adopting policies and procedures that are more restrictive than required by the Proposed Rule or that cover research activities that are not addressed by the Proposed Rule, that member firm should not be discouraged from doing so out of concern that a violation by an employee of those policies and procedures would be the equivalent of a violation of FINRA rules and trigger all the consequences of such violations.

The Firms are also concerned about the unprecedented nature of this statement. To that point, no other FINRA rule contains a statement that a violation of a member firm's policies and procedures established pursuant to that rule – regardless of whether those policies and procedures exceed the rule's requirements – constitutes a separate and independent FINRA rule violation. It is also unclear how this provision would intersect with other FINRA rules.

For these reasons, the Firms respectfully request that FINRA eliminate the statement in Proposed Supplementary Material .09 that "[f]ailure of an associated person to comply with such policies and procedures shall constitute a violation of this Rule." The Firms do not believe that eliminating this statement will diminish the effectiveness of the other provisions of Supplementary Material .09, which clarify that an associated person who engages in the

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[22] *See* Rule Filing, *supra* note 1, at 69948.

restricted or prohibited conduct covered by the Proposed Rule will be deemed to have violated the Proposed Rule regardless of the member firm's policies and procedures.

J. FINRA Should Provide a One-Year Implementation Period.

The Firms greatly appreciate FINRA's agreement to provide sufficient time for implementation of the Proposed Rule and FINRA's recognition that required systems changes often take time. In that regard, the Firms request that FINRA provide a "grace period" of one year or the maximum time permissible, if that is less than one year, between the adoption of the Proposed Rule and the date of implementation to fully incorporate policies, procedures, and processes to meet the various new requirements.

K. FINRA Should Confirm that Certain Provisions Are Designed To Supersede Aspects of the Global Research Settlement.

The Firms request that FINRA confirm, in any forthcoming Regulatory Notice announcing the adoption of the Proposed Rule, that certain provisions of the Proposed Rule, in particular paragraph (b)(2)(B) relating to investment banking input into coverage decisions, paragraph (b)(2)(D) relating to the determination of the research budget, and Supplementary Material .02 relating to joint due diligence, are designed to supersede the corresponding terms of the Global Research Settlement.[23]

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The Firms appreciate the opportunity to comment on the Proposed Rule. We would be pleased to discuss any of these points further and provide any additional information you believe would be helpful. Please feel free to contact me if you have any questions at (202) 663-6825 or Yoon-Young Lee at (202) 663-6720.

Sincerely,

Stephanie R. Nicolas

cc: Stephen Luparello, Director, Division of Trading and Markets, SEC
Robert L.D. Colby, Chief Legal Officer, FINRA
Philip Shaikun, Vice President and Associate General Counsel, FINRA

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[23] *See* Global Research Settlement Addendum A §§ I.3, I.7, and I.11(a) (revised Mar. 2010).