Exhibit 2c

SIFMA
Securities Industry and
Financial Markets Association

November 14, 2008

Via e-mail to pubcom@finra.org
Ms. Marcia E. Asquith
Office of Corporate Secretary
FINRA
1735 K Street, N.W.
Washington, D.C. 20006-1506

Re: Comments Regarding Proposed Research Registration and Conflicts of Interest Rules (FINRA Regulatory Notice 08-55)

Dear Ms. Asquith:

The Securities Industry and Financial Markets Association[1] is submitting this letter to the Financial Industry Regulatory Authority, Inc. ("FINRA") in response to FINRA's request for comments regarding proposed changes to its research analyst conflicts of interest and registration rules, set forth in FINRA Regulatory Notice 08-55. FINRA proposes to establish new FINRA Rule 1223 (Registration of Research Analysts) and new FINRA Rule 2240 (Research Analysts and Research Reports), the latter including new Supplementary Material (collectively, the "Proposed Rules").

I. Introduction

First and foremost, we commend FINRA's diligent efforts to create a comprehensive, consolidated approach to the registration of research analysts and the management of potential conflicts of interest related to research. In particular, we applaud FINRA's adoption of many of the recommendations set forth in the 2005 Joint Report on Research by the National Association of Securities Dealers ("NASD") and New York Stock Exchange ("NYSE").[2] As a general matter, we agree with FINRA that the Proposed Rules will help ensure that investors receive objective research, while permitting the flow of information to investors and minimizing burdens on members. In

[1] Securities Industry and Financial Markets Association ("SIFMA" or the "Association") brings together the shared interests of more than 650 securities firms, banks and asset managers. SIFMA's mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally. It has offices in New York, Washington D.C., and London and its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong.

[2] *See Joint Report by the NASD and the NYSE On the Operation and Effectiveness of the Research Analyst Conflict of Interest Rules* (December 2005), *available at* http://www.finra.org/web/groups/industry/@ip/@issues/@rar/documents/industry/p015803.pdf

particular, we strongly support FINRA's proposals to eliminate quiet period surrounding lock-ups and reduce the quiet periods for initial public offerings to 10 days. We also support the proposed, more flexible supervisory approach with respect to research analyst account trading and encourage the proposed elimination of the chaperoning mandate when reports are reviewed by non-research, non-investment banking personnel. We further support the expansion of the exemption for members with limited investment banking activities. Finally, we appreciate the guidance provided to members regarding the ways in which a member may distribute and differentiate research, including guidance regarding permissible ways for distributing different research products and services to certain classes of customers.

While we commend FINRA's efforts to produce a coherent and consolidated set of research rules, we believe there are certain critical modifications that FINRA should make to the Proposed Rules. We discuss these provisions and the modifications below.

II. SIFMA Urges FINRA to Make Certain Critical Modifications to the Proposed Rules

A. Proposed Rule 2240(b): Identifying and Managing Conflicts of Interest

1. Proposed Rule 2240(b)(2) (Preamble)

As a general matter, we endorse the overarching principle in Proposed Rule 2240(b)(1) that requires members to implement policies and procedures reasonably designed to identify and effectively manage conflicts of interest. We believe this principle appropriately captures the purpose of this rule, NASD Rule 2711, NYSE Rule 472, and Regulation AC. We also understand and support the need to set out certain specific minimum policies and procedures.

We are troubled, however, by the breadth and ambiguity of the language in the introductory sentence of Proposed Rule 2240(b)(2), "[a] member's policies and procedures must be reasonably designed to promote *objective and reliable research* that reflects the *truly held opinions* of the 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 certain current or prospective clients" (emphasis added). That sentence is problematic in three key respects. First, it purports to require members to design procedures to promote "*reliable*" research. The concept of "reliable" research is new and undefined. In that regard, "reliable" is not a term used in NASD Rule 2711 or 2210 or NYSE Rule 472, and it is not clear whether and how it differs from the notions of objectivity and independence, which are embodied in those rules and in the Sarbanes-Oxley Act of 2002 ("SOX"). It is also not clear whether and how this new standard differs from the requirements in NASD Rule 2210 that communications be "fair and balanced" and "provide a sound basis for evaluating the facts" and in NASD IM-2210 that recommendations have a "reasonable basis."

Second, the introductory sentence in Proposed Rule 2240(b)(2) is problematic because it uses the phrase "truly held" opinions. Again, the phrase "truly held" is a new and undefined concept. It is not clear what difference, if any, exists between (i) the requirement in Regulation AC that research accurately reflect the analyst's "personal views" about any and all of the subject securities or issuers, and (ii) the "truly held" opinions of research analysts referenced in the Proposed Rules.

Third, the introductory sentence of Proposed Rule 2240(b)(2) is problematic because it broadly prohibits the use of research to "*manipulate or condition the market*" or "*favor the interests of the member or certain current or prospective clients.*" While we support the general principle that members should implement policies and procedures reasonably designed to prevent market manipulation or front running of research, we believe this principle is already codified in Securities and Exchange Commission ("SEC") and FINRA rules (in particular, Regulation M and Rule 10b-5 under the Securities Exchange Act of 1934, as amended ("Exchange Act"), and FINRA front running prohibitions in NASD-IM-2110-4. As such, it is not clear why this language is necessary or what types of activities Proposed Rule 2240(b)(2) is designed to address.

For the above reasons, we urge FINRA to delete the introductory sentence of 2240(b)(2) so the section would simply state: "Such policies and procedures must at a minimum:" Alternatively, we ask FINRA to revise the introductory sentence to state: "A member's policies and procedures must be reasonably designed to promote independent and objective research that reflects the personal views of the analyst."

2. **Proposed Rule 2240(b)(2) (Specific Policies and Procedures To Identify and Manage Conflicts)**

With respect to the provision setting forth the specific types of policies and procedures that members are required to have, we urge FINRA to consider the following modifications:

a) **Proposed Rule 2240(b)(2)(C) (Analyst Compensation)**

Proposed Rule 2240(b)(2)(C) prohibits not only payments "based upon specific investment banking services transactions" but also those based upon "contributions to a member's investment banking services activities." We ask FINRA to confirm that – consistent with current rules – this prohibition does not prevent a member from compensating analysts for engaging in permissible vetting, commitment committee participation, due diligence, teach-ins, investor education, and other permissible banking-related activities. Indeed, in response to comments on an earlier set of revisions to the research analyst rules, NASD staff recognized that analysts' participation in certain types of banking activities could be considered in compensation decisions. Specifically, in its response letter regarding these revisions, the NASD staff said that "NASD believes screening potential investment banking clients is one of many factors to measure the quality of an analyst's research. As such, it may be considered in determining an

analyst's compensation; [as long as] it may not be given undue weight relative to evaluating the quality of other research work product."[3] The SEC also has provided interpretive guidance in the context of the Global Research Settlement[4] that permits settling firms to compensate analysts for vetting investment banking transactions subject to certain requirements and that also permits analysts to be compensated for providing their views regarding proposed transactions or candidates for transactions, commitment committee participation, and confirming disclosures in offering or other disclosure documents.[5]

b) Proposed Rule 2240(b)(2)(D) (Analyst Compensation)

Proposed Rule 2240(b)(2)(D) should be revised so that compensation committees are required to consider the enumerated factors *only to the extent* they are applicable. By way of comparison, NASD Rule 2711(d)(2) provides that compensation committees "must consider the following factors when reviewing a research analyst's compensation, *if applicable*" (emphasis added).

We also request that FINRA include in the Proposed Rules the following additional factors that are permissible for members to consider in determining analyst compensation: (i) the analyst's seniority and experience, and (ii) the market for the hiring and retention of analysts. These factors are critical to the proper determination of analyst compensation and, as such, are specifically identified in the Global Research Settlement and similarly should be included in the Proposed Rules.[6]

c) Proposed Rule 2240(b)(2)(E) (Information Barriers)

Proposed Rule 2240(b)(2)(E) requires members "to establish information barriers and other institutional safeguards to ensure that analysts are insulated from the review, pressure or oversight of persons engaged in investment banking services activities or other persons *who might be biased in their judgment or supervision*" (emphasis added). We request that FINRA clarify that members may rely on information barriers "*or*" other institutional safeguards reasonably designed to ensure that analysts are shielded from such pressures. Information barriers traditionally are used to restrict the flow of material, nonpublic information and may not always be appropriate to manage potential research conflicts. In some situations, institutional safeguards that do not rise to the level of an "information barrier" are more fitting. Accordingly, we believe members should be accorded the flexibility to rely on barriers or other safeguards.

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[3] *See* Letter from Philip A. Shaikun, NASD, to James A. Brigagliano, SEC, at p. 8 (July 29, 2003).

[4] The Global Research Settlement, which was reached among certain investment banking firms, the SEC, NYSE, NASD, and other regulators on April 28, 2003 is available at http://www.sec.gov/spotlight/globalsettlement.htm.

[5] *See* Letter from Dana Fleischman, Cleary Gottlieb, to James A. Brigagliano, SEC, (Nov. 2, 2004), available at http://www.sec.gov/divisions/marketreg/mr-noaction/grs110204.htm

[6] *See* Section I.5.d of the Global Research Settlement.

We also believe that the broad phrase "*persons who might be biased*" should be replaced with "*persons within the firm who may try to improperly influence analysts' views.*" We believe our recommended wording more accurately characterizes the types of individuals and improper conduct the rule is intended to address. As currently worded, the Proposed Rule could have unintended consequences, by requiring members to insulate an analyst from review by salespeople and investor clients because their holdings or activities may cause them to have a bias. Further, under the language of the Proposed Rules, members arguably may need to wall off an analyst from discussions with subject companies and traders because these constituencies also may have biases and could try to pressure the analyst. We believe FINRA did not intend to restrict analysts in this manner. As such, we urge FINRA to adopt our suggested language, which permits analysts to engage in legitimate and important activities, while requiring firms to have safeguards reasonably designed to protect the analysts against improper influences.

d) Proposed Rule 2240(b)(2)(F) (Anti-Retaliation)

Proposed Rule 2240(b)(2)(F) requires members to "prevent direct or indirect retaliation or threat of retaliation against research analysts by persons engaged in investment banking services or other employees as the result of content of a research report." This prohibition is broader than the current anti-retaliation provisions[7] because it applies to all employees rather than just those employees involved in the member's investment banking department. Also, the proposed provision does not explicitly provide members with the ability to discipline or terminate an analyst for any cause other than the writing of an unfavorable research report as is set forth in the current rules. We believe the current anti-retaliation provisions strike a reasonable balance between preventing retaliation while preserving a member's ability to evaluate, discipline or even terminate an analyst for causes other than the writing of an unfavorable research report such as poor quality or inaccurate written work product or careless fact checking. As such, we urge FINRA retain the current language in the anti-retaliation provision set forth in current NASD Rule 2711(j).

e) Proposed Rule 2240(b)(2)(H) (Trading by Analyst Accounts)

As noted earlier, we support Proposed Rule 2240(b)(2)(H) that provides a more flexible supervisory approach regarding research analyst account trading in securities of companies covered by the analyst. To the extent members have adopted internal policies prohibiting analysts from owning securities issued by companies the analyst covers, we ask FINRA to confirm that members may permit an analyst to divest any such holdings pursuant to a reasonable plan of liquidation within 120 days of the effective date of the member's policy even if the sale is inconsistent with the analyst's current

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[7] *See* NASD Rule 2711(j) and NYSE Rule 472(g)(2).

recommendation. This approach was proposed by the NASD and NYSE in 2007[8] and we believe it is consistent with the principles set forth in Proposed Rule 2240(b)(H).

f) **Proposed Rule 2240(b)(2)(J)(ii) (Limitations on Analysts' Activities)**

Proposed Rule 2240(b)(2)(J)(ii) would require members to prohibit analysts' participation in road shows and other marketing on behalf of issuers. We ask that FINRA clarify that – consistent with its current rules – this prohibition does not apply to investor education activities and only applies to road shows and marketing activities "in connection with investment banking services transactions."[9] Under the proposed prohibition, many legitimate marketing activities that occur outside of a deal context would be prohibited. For example, analysts frequently facilitate meetings between investors and company management in what are often referred to as non-deal road shows. We believe these types of interactions are beneficial to investors and should not be prohibited by Proposed Rule 2240(2)(J)(ii).

We also ask FINRA to confirm that, consistent with existing NYSE and NASD guidance,[10] analysts may listen to or view a live webcast of a transaction-related road show or other widely attended presentation by investment bankers to investors or the sales force from a remote location or, to the extent the event occurs at the member's offices, from a room that is separate from investment banking personnel, investors or the sales force.

B. Proposed Rule 2240(c): Content and Disclosure Requirements for Research Reports

We recommend that FINRA modify certain provisions in the content and disclosure requirements of the Proposed Rules so that they (i) are more consistent with existing FINRA and SEC rules and requirements, and (ii) provide clearer guidance to members regarding FINRA's expectations as set out below.

1. **Proposed Rule 2240(c)(1) (Ensuring "Purported Facts" Are Based on "Reliable Information")**

Proposed Rule 2240(c)(1) requires members "to ensure that purported facts in reports are based on reliable information." As we noted above, "reliable" is not a term used in current NASD Rule 2711 or 2210 or NYSE Rule 472. It is also unclear what "purported facts" are. We ask FINRA to modify this provision to require members to

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[8] *See* Proposed Rule Changes of the NYSE and NASD Relating to Research Analyst Conflicts of Interests, File Nos. SR-NYSE-2006-78, SR-NASD-2006-113 at 72 Fed. Reg. 2058, 2059 (Jan. 17, 2007) ("2007 Rule Proposals").

[9] *See* NASD Rule 2711(c)(5)(A). We believe that the Proposed Rule does not prohibit teach-ins or other internal meetings intended to educate the sales force, but ask FINRA to confirm our understanding.

[10] *See* NASD Notice to Members 07-04 (Jan. 2007) and NYSE Information Memo 07-11 (Jan. 2007).

adopt policies and procedures reasonably designed to ensure that facts are based on "sources believed by the member firm to be reliable."

2. **Proposed Rule 2240(c)(2) (Recommendations, Ratings, and Price Targets)**

Proposed Rule 2240(c)(2) requires members to ensure that any recommendation, rating or price target has a reasonable basis "in fact." We do not understand the reference to a reasonable basis "in fact." In that regard, a rating or price target is, by definition, a judgment or estimate and *not* a "fact." Accordingly, we ask FINRA to revert to the current language in the FINRA price target disclosure rule by deleting "in fact" from the proposed provision. In addition, we believe the provision should be revised to reflect that not all ratings are associated with a "valuation method." We would revise the provision to read ". . . is accompanied by a clear explanation, including of any valuation method utilized . . . . "

3. **Proposed Rule 2240(c)(5) (Preamble to Conflicts of Interest Disclosures)**

We urge FINRA to revise the language in the introductory sentence to Proposed Rule 2240(c)(5), which broadly requires members to disclose "*all* conflicts that reasonably could be expected to influence the objectivity of the research report and that are known or should have been known by the member or research analyst on the date of publication or distribution of the research report, including . . . " (emphasis added).

Read literally, this language would require members to engage in a sweeping exercise to identify – with respect to every research report – *all* possible conflicts (material or immaterial) that may be known to anyone at the member. Compliance with such a standard is simply not possible. The proposed language also assumes that conflicts *could be expected and do* influence the objectivity of research reports even though FINRA's existing research analyst rules and Reg AC assume the contrary, i.e., that potential conflicts can be managed using disclosures and certifications in order to preserve the objectivity of research analysts and research reports. In addition, this language appears to be somewhat redundant with the "catch-all" disclosure in Proposed Rule 2240(c)(5)(H), which requires disclosures of "any other material conflict of interest of the research analyst or member that the research analyst or an associated person of the member with the ability to influence the content of a research report knows or has reason to know at the time of the publication or distribution of a research report."

For these reasons, we urge FINRA to revise the language in the introduction to clarify that members must comply with the specific disclosures set forth in 2240(c)(5) (including the "catch-all" disclosure in 2240(c)(5)(H)). In particular, we ask FINRA to revise the introductory sentence to Proposed Rule 2240(c)(5) to read, "A member must disclose in any research report the following," the language used in the preamble to current Rule 2711(h)(1) and 2711(h)(2). To the extent that FINRA wants to state a

general principle regarding the purpose of the disclosures, we believe the rule should recognize that compliance with the specific disclosures constitutes compliance with the general principle.

4. **Proposed Rule 2240(c)(5)(F) (Disclosure of Significant Financial Interest)**

Proposed Rule 2240(c)(5)(F) establishes a new requirement that members disclose if they or their affiliates maintain a significant financial interest in the *debt* of the subject company. For a number of reasons, we believe that disclosure of financial interests in the *debt* securities of a subject company in an *equity* research report regarding the subject company is an unnecessary and burdensome requirement. First, to the extent that a member's ownership interest in a debt security may present a conflict of interest, the member is already required to disclose that interest under the catch-all provision requiring disclosures of material conflicts of interest. Also, while it is not clear what (if any) benefit this new disclosure requirement would have to investors, the costs to develop and implement this new requirement to members are clear: this new disclosure will take a significant amount of time and resources to implement because members may need to establish new methods to determine ownership thresholds and analyze and compile lists of instruments that qualify for inclusion in such calculations. Unlike equity holdings, which members were already required to calculate and aggregate with affiliate holdings pursuant to Section 13 of the Exchange Act, members do not generally identify and aggregate debt holdings among affiliates. As such, this requirement would impose significant infrastructure requirements on members and should be eliminated, given the questionable utility to investors.

5. **Proposed Rule 2240(c)(5)(H) (Material Conflict of Interest Disclosure)**

As noted above, Proposed Rule 2240(c)(5)(H) contains a "catch-all" disclosure requirement for "any other material conflict of interest..." While this disclosure is largely consistent with the current "catch-all" disclosure in NASD Rule 2711(h) and NYSE Rule 472(k), it differs in two key respects, which we believe will raise very difficult compliance issues for members. Specifically, under the current rules, members must disclose "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." Proposed Rule 2240(c)(5)(H), however, goes beyond the current requirement by mandating that members disclose not just *actual*, material conflicts of which the research analyst knows, but also any other material conflict of interest (including mere *potential*, material conflict of interests) that "an associated person of the member with the ability to influence the content of a research report knows or has reason to know." This proposal also goes beyond the current requirement by mandating that disclosures be made with respect to material conflicts of interest that are known not only at the time of publication, but also "at the time of the ... distribution of a research report."

We urge FINRA to revise Proposed Rule 2240(c)(5)(H) so that it is consistent with the current research disclosure provisions. As a practical matter, it would be very difficult – if not impossible – to comply with the two new requirements in the proposal. In that regard, members would be required to delay the distribution of any research reports until they have surveyed any persons who have the "ability to influence the content of the research report" to determine whether such persons "know or have reason to know of any material conflicts." Also, it is unclear how members could control and prevent the distribution of reports that already have been published, in order to determine whether additional disclosures are required. For example, if a member publishes a report, does it need to monitor and prevent any subsequent mailings of that report by its salespeople or other associated persons and, potentially, include additional disclosures in that report? We do not believe such a requirement would be practical or useful to investors. Indeed, to the extent any potential conflicts of interest arise after the publication of a report, such conflicts would not have influenced the substance or content of the report. For these reasons, we ask that FINRA revise Proposed Rule 2240(c)(5)(H) so that it is consistent with current disclosure requirements.

C. Proposed Rule 2240(h): Distribution of Third Party Research Reports

Regulatory Notice 08-55 describes the Proposed Rules as "incorporate[ing] in their entirety the current provisions regarding distribution and supervision of third party research" and refers the reader to Regulatory Notice 08-16, which sets out member's disclosure and supervisory review obligations. In fact, FINRA's proposed provisions regarding third party research reports seem to go *significantly beyond* the existing requirements in at least two respects and, as such, should be modified.

First, Proposed Rule 2240(h)(1)(A) imposes a new requirement that members adopt policies and procedures "to ensure that any third party research," including independent third party research, "is reliable and objective." Second, Proposed Rule 2240(h)(2) changes the third party research report disclosure requirements from specifically-delineated disclosures set out in current NASD Rule 2711(h)(13)(A) and NYSE Rule 472(k)(4)(i) to a broad requirement that members disclose "any material conflict of interest that can reasonably be expected to have influenced the choice of a third party research provider or the subject company of a third party research report."

In FINRA Regulatory Notice 08-16 (which is referenced in Regulatory Notice 08-55) FINRA recognized not only the value that third party research provides to investors, but also the large volume of third party research reports distributed by many members. For these reasons, FINRA revised the third party research rules to provide that "a member firm's approval of third party research reports shall be based on a review to determine that the report does not contain any untrue statement of material fact or any false or misleading information that (i) should be known from a reading of the report or

(ii) is known based on the information otherwise possessed by the member."[11] FINRA went further by excluding all independent third party research reports from that review.

Proposed Rule 2240(h)(1)(A), however, appears to overrule the carefully-crafted balance established by Regulatory Notice 08-16 by requiring members to ensure that any third party research – *including* independent third party research – "is reliable and objective." It is not clear what kind of review would be necessary to comply with this requirement, and, as noted above, it is not clear what would make research "reliable." For these reasons, we urge FINRA to eliminate this new requirement in 2240(h)(1)(A) or, at a minimum, allow members to apply the same review standard and exception that are provided for in 2240(h)(1)(C).

In addition to the departures from existing guidance noted above, Proposed Rule 2240(h)(2) contains significant changes from the existing disclosure requirements for third party research. Unlike NASD Rule 2711(h)(13)(A), which required four specific disclosures for third party research (other than independent third party research) distributed by members, Proposed Rule 2240(h)(2) requires third party research reports to disclose "any material conflict of interest that can be reasonably be expected to have influenced the choice of a third party research provider or the subject company of a third party research report." We believe the current disclosure requirements for third party research are well-established and well-functioning. As such, we urge FINRA to do what Regulatory Notice 08-55 purports to do and adopt those existing requirements.

See Appendix for a table highlighting our suggested modifications to Rule 2240(h).

D. Proposed Changes to Definitions

1. Proposed Rule 2240(a)(4) (Revision to the Definition of "Investment Banking Services")

The proposed revisions to the definition of "investment banking services" are overly broad, and might cover activities that are not investment banking services. As such, FINRA should retain the current definition of "investment banking services." In that regard, the definition of "investment banking services" has been modified to cover "all acts in furtherance of a public or private offering on behalf of an issuer." This modification creates an extremely broad definition that extends *beyond* those personnel and departments traditionally viewed as related to investment banking, and read literally, might apply to sales activities in connection with an offering or private placement. Therefore, we ask FINRA to maintain its existing definition of "investment banking services."

[11] *See* FINRA Regulatory Notice 08-13 (April 2008) at p. 3.

2. **Proposed Rule 2240(a)(10) (Definition of "Research Report")**

We support FINRA's proposal to exclude from the definition of "research report," sales material analyzing open-end registered investment companies not listed or traded on an exchange and public direct participation programs. As the self-regulatory organizations have observed in the 2007 Rule Proposals, those types of sales materials are already subject to "a separate regulatory regime, including NASD Rule 2210 and SEC Rule 482, and all sales literature must be filed with the NASD Advertising Regulation Department within ten business days of first use" with certain exceptions.[12] Because sales material analyzing open-end exchange traded funds ("ETFs") are also subject to the same regulatory regime and must be filed with FINRA within ten business days of first use, subject to certain exceptions, we urge FINRA to consider excluding such material from the definition of "research report."

We also recommend that FINRA modify Rule 2240(a)(10)(B)(ii) to exclude from the definition of "research report" any type of periodic report or other communication for any managed client account, whether such account is "discretionary" as the rule currently provides, or non-discretionary in nature. Reports distributed to "discretionary investment accounts" are excluded from the definition of "research report" because the member's discretion over the account presumably means the analysis provided is not for the purpose of the client's making an "investment decision" as the definition of "research report" currently requires. The client's representative generally makes all investment decisions for the discretionary account. We believe this rationale is equally applicable to all managed accounts, whether discretionary or non-discretionary, because clients who utilize managed accounts generally rely on their individual money manager to make investment decisions in line with their goals and will not rely upon research reports provided by the member to make "investment decisions" as required by Rule 2240(a)(10). An expansion of the exception for communications prepared for discretionary accounts to include all managed accounts would allow members to prepare written communications about portfolio managers and their funds and provide such communications to both their discretionary and non-discretionary managed clients. Accordingly, we ask FINRA revise 2240(a)(10)(B)(ii) to permit the distribution of periodic reports or other communications for investment company shareholders or *managed account* clients...."

E. Supplementary Material .01 Regarding Pitch Book Materials.

Proposed Supplementary Material .01 interprets 2240(b)(2)(J)(i) to prohibit pitch materials that suggest or imply that the member might provide favorable research coverage. The second sentence of the proposed interpretation provides an example of presumably prohibited materials that reads, "[f]or example, FINRA would consider the publication of a pitch book or related materials of an analyst's industry ranking to imply the potential outcome of future research because of the manner in which such rankings

[12] *See* 2007 Rule Proposals at 2068-9.

are compiled." The example does not provide members with a clear understanding of what is prohibited; and, further, it is not clear why the inclusion of an analyst's industry ranking necessarily suggests or implies that the member may provide favorable research coverage. We request that FINRA revise the example to make it clearer regarding what sort of materials are prohibited or provide an alternative example of prohibited pitch materials. We also ask that FINRA confirm that members may disclose in pitch materials the fact that research coverage will be provided for a particular issuer.

III. Web-Based Disclosures

We appreciate FINRA's efforts to pursue more web-based disclosure options for research reports, and are disappointed that the SEC staff has chosen to interpret SOX to disallow broad use of web-based disclosures. We continue to believe that web-based disclosure promotes efficiency, provides important information to investors in a meaningful and effective manner, and is consistent with important initiatives by the SEC to promote the use of electronic media.

In particular, price charts and ratings distribution tables are often cumbersome and difficult to produce in individual research reports, and it would greatly ease production burdens and streamline the research reports themselves if they could be provided through websites. The dynamic nature of such charts and tables make them particularly well suited for online disclosure where they may provide more meaningful information to investors.

In the 2007 Rule Proposals, the NASD and NYSE asked whether a web-based disclosure regime should be permitted for public appearances.[13] We urge FINRA to consider permitting such a regime because we believe a web-based disclosure regime is equally, if not more, appropriate for public appearances. In particular, web-based disclosures would allow investors to consider and appreciate more fully the disclosures related to public appearances. With web-based disclosures, investors would be able to download, review, and assess the disclosures (as opposed to simply hearing them recited before or after an appearance, at which time investors may not focus on the substance of the disclosures).[14]

IV. Request for an Extension of the Effective Date of the Proposed Rules

We believe FINRA should adopt the Proposed Rules, with the above suggested modifications, as soon as they are approved by the SEC. We request, however, that FINRA provide a 120-day "grace period" between the adoption of the Proposed Rules

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[13] *See* 2007 Rule Proposals at 2072.

[14] We also ask FINRA to confirm that to the extent a disclosure is required by both Proposed Rule 2240 and Rule 2210 and is presented in a "compendium report" as defined by Proposed Rule 2240(c)(8), members may rely on the delivery mechanisms set forth in 2240(c)(8) to satisfy their disclosures obligations for both rules.

and the implementation date of the Rules. Additional time is required because some of the Proposals, if adopted, such as the new disclosure regarding ownership of debt securities of a subject company, will require major modifications to information technology ("IT") systems and research report templates, and policies and procedures. Modifications to systems near year end are particularly difficult because many IT departments stop accepting new requests while they focus exclusively on producing year-end financials and completing existing requests.

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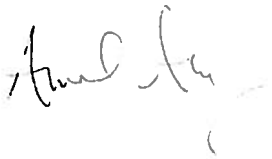
SIFMA appreciates the opportunity to submit this letter to you. We would be pleased to discuss this matter further and to provide any additional information you believe would be helpful in connection with your consideration of this matter. Please feel free to contact me with any questions you may have in this regard at (212) 313-1268.

Very truly yours,



Amal Aly
SIMFA Managing Director and
Associate General Counsel

CC: Mary Schapiro, Chief Executive Officer
Marc Menchel, Executive Vice President and General Counsel for Regulation
Grace Vogel, Vice President, Member Regulation
Stephen Luparello, Senior Executive Vice President, Regulatory Operations

APPENDIX

	Current Rule*		Proposed Rule		Suggested Modifications	
	Third party research	**Exception for independent third party research**	**Third party research**	**Exception for independent third party research**	**Third party research**	**Exception for independent third party research**
Disclosures by distributing member firm	Four enumerated disclosures. NASD Rule 2711(h)(13)(A). *citations only to NASD rules for these purposes.	No disclosures required if independent third party research is not "distributed" by the member. NASD Rule 2711(h)(13)(B).	Disclosure of "any material conflict of interest that can reasonably be expected to influence the choice of a third party research provide or the subject company." Proposed Rule 2240(h)(2).	No disclosures required if independent third party research is not "distributed" by the member. Proposed Rule 2240(h)(4)	Maintain current disclosure requirements set forth in Rule 2711(h)(13)(A).	No modification suggested.
Review for untrue statements of material fact and false or misleading information	Review is limited to untrue statements or false or misleading information that should be known from reading the report or is known to the member. NASD Rule 2711(h)(13)(C).	Review requirement does not apply to independent third party research. NASD Rule 2711(h)(13)(D).	Review for untrue or false or misleading information that should be known from reading the report or is known to the member pursuant to Proposed Rule 2240(h)(1)(C).	Review requirement does not apply to independent third party research. Proposed Rule 2711(h)(3).	No modification suggested.	No modification suggested.
Review to ensure that research is "reliable and objective"	Not in current rule.	N/A	Requires review to ensure that third party research distributed is "reliable and objective." Proposed Rule 2240(h)(1)(A).	No exception or accommodation for independent third party research.	Eliminate this new review requirement. Alternatively, apply the standard of review set forth in Proposed Rule 2240(h)(1)(C).	Eliminate this new review requirement. Alternatively, apply the exception set forth in Proposed Rule 2240(h)(3).

Dechert LLP

Office of the Corporate Secretary-Admin.

NOV 14 2008

FINRA
Notice to Members

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November 14, 2008

Marcia E. Asquith
Office of the Corporate Secretary
Financial Industry Regulatory Authority
1735 K Street, NW
Washington, DC 20006

Re: FINRA Regulatory Notice 08-55

Dear Ms. Asquith:

The Financial Services Group of Dechert LLP is pleased to have the opportunity to comment on the Financial Industry Regulatory Authority's ("FINRA") proposal to adopt FINRA Rule 2240 (the "Rule"[1]) relating to research analysts' conflicts of interest (the "Rule Proposal").[2] Specifically, we are concerned that the portion of the Rule Proposal which amends the definition of "research report" to exclude sales literature relating to open-end registered investment companies that are not listed or traded on an exchange or public direct participating programs ("DPPs") is too narrow. We agree that this exclusion is consistent with the definition of research report added to the Securities Exchange Act of 1934 (the "Exchange Act") by Section 501 of the Sarbanes-Oxley Act of 2002 ("SOX"). However, consistent with Section 501 of SOX, the exclusion should also encompass sales literature relating to hedge funds and private equity funds (collectively, "private funds") so that no public or private fund sales literature would be subject to the requirements of the Rule.[3]

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1 Proposed FINRA Rule 2240 amends and replaces NASD Rule 2711. Unless otherwise indicated herein, all references to the Rule includes NASD Rule 2711.

2 Financial Industry Regulatory Authority, Regulatory Notice 08-55, *Research Analysts and Research Reports* (Oct. 2008).

3 We note that other organizations have advanced similar, and in come cases identical, conclusions with regards to other types of investment products in connection with SR-NASD-2006-113, an earlier NASD rule filing that included the proposed change to Rule 2711. *See, e.g.*, Letter from Michael D. Udoff, Securities Industry and Financial Markets Association, to the U.S. Securities and Exchange Commission, dated March 5, 2007 (noting that sales materials related to exchange traded funds ("ETFs") and private funds should also be excluded from the definition of research report); Letter from Donald S. Weiss, Bell, Boyd & Lloyd LLP, to the U.S. Securities and Exchange Commission, dated March 1, 2007 (noting that sales materials related to private funds should also be excluded from the definition of research report); Letter from Jack Hollander, Investment Program Association, to the U.S. Securities and Exchange Commission, dated March 5, 2007 (noting that sales materials related to non-traded real estate investment trusts should also be excluded from the definition of research report); Letter from David A. Hebner, Wachovia Securities, LLC, to the U.S. Securities and Exchange Commission, dated February 28, 2007

Dechert is an international law firm serving clients in the United States and worldwide. The Financial Services Group of Dechert provides advice and assistance to a wide variety of U.S. and non-U.S. investment companies and private funds, as well as investment advisers, fund administrators, broker-dealers, insurance companies, commercial banks, and thrift institutions. An extensive part of our services for these clients involves assistance in compliance with federal and state securities laws in the organization, distribution, and operation of investment funds, including those registered with the Commission and those not subject to registration. The comments that follow reflect our own views and not necessarily those of any client of the firm.

As we explain in detail below, and based on the rationale previously advanced by FINRA,[4] sales literature relating to private funds, the attributes of which are similar to those of sales literature relating to open-end registered investment companies and public DPPs, should also be excluded from the definition of "research report." Additionally, the public policy concerns that prompted the adoption of the conflict of interest rules for research analysts – and the concerns that justify regulating "research reports" – are not present in the context of sales literature relating to private funds.

I. Background

The Rule's definition of "research report," which was adopted in whole from Section 15D(c)(2) of the Exchange Act, is a "written (including electronic) communication that includes an analysis of equity securities of individual companies or industries, and that provides information reasonably sufficient upon which to base an investment decision."[5] Section 15D, added to the Exchange Act by SOX Section 501, mandated the adoption of rules to "address conflicts of interest that can arise when securities analysts recommend equity securities in research reports . . . in order to improve the objectivity of research and provide investors with more useful and reliable information."

The breadth of the definition of "research report" has created significant uncertainty about the scope and application of the Rule, including its application to mutual fund sales literature. The *Joint Report by NASD and the NYSE on the Operation and Effectiveness of the Research Analyst Conflict of Interest Rules*, published in December 2005 (the "Joint Report"), noted the very broad definition of "research report," and recommended codifying certain interpretations of the definition so that the Rule would not apply to sales literature relating to "registered investment companies." (The Joint Report did not include the qualifier "open-end" to registered investment companies, which is in the Rule Proposal.) The Rule Proposal, among other things, amends the definition of "research report" to exclude sales literature relating to open-end registered investment companies that are not listed or traded on an exchange or public DPPs.

(noting that sales materials related to ETFs, closed-end funds and hedge funds should also be excluded from the definition of research report).

4 *See Self-Regulatory Organizations; New York Stock Exchange LLC and the National Association of Securities Dealers, Inc.; Notice of Filing of Proposed Rule Changes to Amend NYSE Rules 472 and 344, and NASD Rules 1050 and 2711 Relating to Research Analyst Conflicts of Interest*, Securities and Exchange Commission ("SEC"), Release No. 34-55072, SR-NASD-2006-113 (Jan. 9, 2007) (the "2006 Rule Proposal").

5 NASD Rule 2711(a)(9).

In connection with the distribution of private funds, registered broker-dealers produce sales literature that is directed to accredited investors interested in private funds and that contains information, such as performance information, about private funds, which a fair reading would lead one to believe may be "sufficient upon which to base an investment decision," i.e., a "research report." After the Joint Report was published, FINRA staff verbally reiterated to us their belief that the Rule applies to private fund sales literature. Accordingly, and consistently with the observation of the Joint Report, we have assumed that it is FINRA's view that the Rule applies to private fund sales literature.

II. The Proposed Exclusion Should Be Expanded Consistent With the Apparent Purpose of the Definition of Research Report and to Eliminate Confusion

We urge FINRA to expand the proposed exclusion so that the Rule will not apply to private fund sales literature because the risks that the Rule is intended to address are absent with respect to sales literature relating to securities that are not traded in secondary markets or that are redeemable by the issuer. Instead, the proposed exclusion should be expanded so that the definition of "research report" is limited to communications: (i) relating to equity securities that are traded in public secondary markets, (ii) relating to equity securities that are not redeemable at the option of the investor, and (iii) published by a person who is not the distributor or agent of the issuer.

Section 15D and the Rule were not intended to address communications that are clearly presented as sales literature and that are governed by the rules and standards applicable to sales literature. While sales literature is expected to be "fair and balanced,"[6] there should be no expectation that it is objective analysis. Accordingly, we believe the Rule Proposal should be amended to ensure that sales literature relating to private funds is not subject to the requirements of the Rule. Moreover, sales literature that is clearly marketing material and not objective analysis should not be subjected to the additional regulatory regime designed to preserve the objectivity of research.

Subjecting broker-dealers distributing private funds, as well as foreign funds sold in private placements in the United States and other types of equity alternative collective investment products, to the Rule's requirements is unnecessary because, as discussed in IV.A, below, private fund distribution practices were not the reason behind adopting the Rule. Imposing the requirements of the Rule on private fund distributors will affect the use of offering summaries, pitch books, power-point presentations, term sheets and other commonly used forms of sales literature that are not prospectuses or offering memoranda.[7]

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6 *See* NASD Rule 2210(d)(1).

7 NASD, SR-NASD-2006-112, *Proposed Rule Change to Amend NASD Rule 2711 to Codify Existing Interpretive Guidance Relating to Research Analyst Rules*, filed for immediate effectiveness on Sept. 27, 2006 and published at 72 F.R. 62331 (Oct. 24, 2006), codified an interpretation that excludes "periodic reports or other communications prepared for investment company shareholders or discretionary investment account clients that discuss individual securities in the context of a fund's or an account's past performance or the basis for previously made discretionary investment decisions" from the definition of "research report." This change clearly permits performance information in prospectuses and offering memoranda, while the Rule Proposal's exclusion is more limited and would prohibit the use of performance information in private fund sales literature that is not a prospectus or offering memorandum.

As noted above, FINRA apparently takes the position that the Rule applies to all types of sales literature that meet the definition of research report, whether such sales literature relates to private funds, public closed-end funds, ETFs and other equity alternative investment products. In our experience we have found that private fund distributors are generally unaware that FINRA takes this counterintuitive and surprising view.[8] Moreover, the fact that few are aware of FINRA view of the Rule's scope indicates confusion over the scope and application of the Rule with regard to private fund sales literature. This lack of awareness and confusion may also indicate that the effect of the Rule and its costs and benefits were not fully understood nor adequately considered at the time the Rule was adopted.[9]

III. FINRA's Rationale for Exempting Open-End Registered Investment Companies and Public DPPs From the Rule Applies Equally to Private Funds

Although not addressed in detail in the Rule Proposal, the 2006 Rule Proposal justified excluding from the definition of "research report" sales literature of open-end registered investment companies because such sales literature is subject to a separate regulatory regime, including FINRA Rule 2210 and SEC Rule 482, both of which set the content standards for sales literature.[10] FINRA also noted that registered fund sales literature is subject to filing with FINRA within ten days of its first use, but does not explain how the filing requirement justifies limiting the exclusion to open-end registered investment companies. We urge FINRA to consider that the filing requirement applicable to registered fund sales literature is a procedural requirement designed to assure that widely distributed registered fund sales literature is subject to orderly review, while private fund sales literature, because of its more sophisticated audience and limited non-public distribution, need not be subject to intensive review. Accordingly, the justification for the distinction FINRA draws between registered fund sales literature and private fund sales literature – that registered fund sales literature is subject to FINRA review – should not be considered a substantive protection that supports limiting the proposed exclusion to registered fund sales literature. The content requirements of FINRA Rule 2210 are equally applicable to both registered and private fund sales literature. Moreover, the Rule 482 requirements applicable to registered fund sales literature arise because of the need to reconcile such sales literature with the prospectus requirements of the Securities Act of 1933 ("Securities Act").

FINRA also proposed to exclude public DPP sales literature because it is subject to FINRA Rule 2210, including the requirement that it must be filed with FINRA within ten business days of its first use. The 2006 Rule Proposal noted that the sales literature of DPPs generally consists of "tombstone" advertisements and, therefore, is also subject to SEC Rule 134. FINRA asserted that public DPPs

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8 A review of the relevant literature has not identified any instance in which FINRA has publicly stated its expectation that the Rule would apply to private fund sales literature, nor are we aware of any instance where FINRA has sought to enforce the Rule against publishers of such sales literature. Nevertheless, the effect of comment letters such as the ones cited in footnote 3, above have highlighted for the first time the fact that industry participants believe there is ambiguity which FINRA should resolve.

9 We note that the definition of "Research Report" in the Rule is the same as the definition in SEC Regulation AC.

10 *See* 2006 Rule Proposal, *supra*, note 4. Because the Rule Proposal does not address the proposed definition of "research report," we will address the reasoning offered by the 2006 Rule Proposal, which attempted to amend the definition of "research report" in the same manner as the Rule Proposal.

typically are not traded on an exchange and do not have an active secondary market.[11] FINRA did not cite any source for this assertion. Public DPPs are sometimes exchange listed or traded in the secondary market because they are registered. In fact, it is precisely these characteristics that appear to make public DPPs more akin to individual operating company equity securities. Unregistered funds that are organized as DPPs or limited liability companies, by contrast, generally do not trade in secondary markets because of their structural characteristics such as redemption restrictions and resale prohibitions.

FINRA Rule 2210 regulates the content of private fund sales literature[12] and requires sales literature to be based on "principals of fair dealing and good faith." Sales literature must be fair and balanced and must not omit any material facts if the omission, in light of the context, would cause the communication to be misleading.[13] In addition, Rule 2210 prohibits members from making any false, exaggerated, unwarranted or misleading claim in communications with the public, and communications with the public may not predict or project performance, imply that past performance will recur or make any exaggerated claim, opinion or forecast. Rule 2210 also specifies that sales literature must disclose the relationship between the registered broker-dealer and the non-member or individual who is named. Finally, even if a non-member private manager prepares the sales literature, the sales literature is subject to the content requirements of Rule 2210 if a member uses it to sell a private fund.[14]

Although private fund sales literature is not subject to post-use review by FINRA, such review is not necessary.[15] Unlike open-end registered investment companies and public DPPs, the distribution of private fund sales literature is limited to sophisticated investors.[16] These investors are considered more

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11 *See id.* at 11.

12 The NASD and others have interpreted Rule 2210 to apply equally to the sales literature of registered funds and private funds. *See* NASD, Interpretative Letter, *Further Interpretative Advice to Members Concerning the Sale of Hedge Funds* (Oct. 2, 2003) [hereinafter SIA Letter]; *see also* NASD, Interpretive Letter, *Guidance Regarding Use of Related Performance Information in Sales Material for Private Equity Funds* (Dec. 30, 2003) [hereinafter Davis Polk Letter].

13 *See* NASD, IM-2210-1, *Guidelines to Ensure That Communications With the Public Are Not Misleading*; *see also* NASD, Notice to Members 03-07, *NASD Reminds Members of Obligations When Selling Hedge Funds* (Feb. 2003).

14 *See* SIA Letter, *supra* note 12.

15 The 2006 Rule Proposal noted that the "NASD Advertising Regulation Department review of registered investment company and public DPP sales literature reduces the likelihood that it will contain content that is not fair and balanced." 2006 Rule Proposal, *supra* note 4; *see also* Davis Polk Letter, *supra* note 12; SIA Letter, *supra* note 12.

16 Sophisticated investors are investors that are "qualified institutional buyers," as defined by Rule 144A under the Securities Act, "qualified purchasers," as defined by Section 2(a)(51) of the Investment Company Act of 1940 ("Investment Company Act"), or "accredited investors," as defined by Rule 501(a) under the Securities Act.

Though the SEC is proposing to revise the definition of "accredited investors," as it applies to natural persons, the SEC is not proposing to change the principle that select investors do not need as much regulatory protection as the public. SEC, Release 33-8766, *Prohibition of Fraud by Adverse to Certain Pooled Investment Vehicles; Accredited Investors in Certain Private Investment Vehicles* (Dec. 27, 2006) (proposing new standards to limit the number of investors that qualify as accredited investors because overall personal wealth has increased, as a result of inflation and increased personal residence values, so

capable of objectively evaluating sales literature and, therefore, the concerns related to the widespread public dissemination of research are not present. In fact, FINRA, in an interpretive letter concerning a particular class of private funds, noted that, with respect to related performance in sales literature, private funds do not present the same investor protection concerns compared to mutual funds.[17] Private funds also are generally not subject to the registration requirements of the Investment Company Act and Securities Act because their shares are sold to sophisticated investors in limited offerings.[18] Because sales literature for private funds is subject to the same content standards as apply to open-end registered investment companies and public DPPs, FINRA's justifications for the scope of the proposed exclusion should apply equally to private fund sales literature. Finally, any performance information in private fund sales literature must meet the same Rule 2210 requirements that apply to registered investment companies.[19] Accordingly, we urge FINRA to consider that, because Rule 2210 sets content standards for advertising and sales literature, it should not impose additional regulatory burdens on private fund sales literature by declining to extend the proposed exclusion.

IV. Regulatory Concerns Justifying the Regulation of Research Reports Do Not Apply in the Context of Private Fund Sales Literature

A. Private Funds Are Priced at Net Asset Value, Not by the Market

The conflicts of interest that FINRA sought to address when enacting Rule 2711 are not a regulatory concern for private funds. FINRA adopted the Rule to address the influence that investment bankers exerted on research analysts to speak favorably about specific companies or issuers.[20] FINRA noted that "[t]he primary biasing forces came from investment bankers who pressured research analysts to speak favorably of current and prospective clients and, with management acquiescence, linked analysts' compensation directly to their role in landing lucrative investment banking deals."[21] FINRA was concerned with research analysts having a financial interest in the issuers that they covered and, as a

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that the percentage of U.S. households that qualify for accredited investor status has increased from 1.87% to 8.47% between 1982 and 2003, while investment products have increased in complexity).

17 Davis Polk Letter, *supra* note 12.

18 *See id.*

19 *See id.*

20 The NASD sought to address the circumstances that compromised the objectivity of research by research analysts "and to restore public confidence in the validity of research and the veracity of research analysts, who are expected to function as unbiased intermediaries between issuers and the investors who buy and sell their securities." *Id.* at 2.

21 Joint Report, *supra* at 2 ("In the succinct words of a retired Wall Street research analyst who testified before Congress in the summer of 2001: 'Investment banking now dominates equity research.'"). Congress expressed similar concerns when addressing research analysts' conflicts of interest. *See* S. COMM. ON BANKING, HOUSING AND URBAN AFFAIRS, PUBLIC COMPANY ACCOUNTING REFORM AND INVESTOR PROTECTION ACT OF 2002, S. Rep. No. 107-205, at 41 (2002) ("The Committee [on Banking, Housing and Urban Affairs] heard persuasive testimony that a serious problem exists regarding conflicts of interest between Wall Street stock analysts and their employing brokerage firms, on the one hand, *and the public companies that the stock analysts cover*, on the other hand. Growing knowledge of these conflicts is harming the integrity and creditability to the public of stock analyst recommendations.") (emphasis added).

result, attempting to manipulate the price of securities traded on an exchange through the issuance of unduly favorable research reports.[22]

By contrast, it is impossible to manipulate the price of a private fund. A private fund's value is calculated in the same manner as the value of an open-end registered investment company—using the fund's net asset value ("NAV"). Because private fund sales literature cannot affect the NAV of a private fund, subjecting such sales literature to regulation under a rule that was designed to prevent price manipulation is unnecessary, burdensome, and contrary to legislative intent.

B. Private Fund Sales Literature Does Not Contain Analysis

Private fund sales literature is more similar to open-end registered investment company sales literature than to single operating company equity security research reports. A "research report" has (i) "information reasonably sufficient upon which to base an investment decision" and (ii) "analysis" about securities of "individual companies." Although investors may use private fund sales literature to decide whether to purchase or sell a fund, private fund sales literature does not generally contain the type of analysis that is included in research reports for operating companies. Nor is the type of analysis performed on operating companies applicable to the private funds. The two main types of analysis that are in research reports for operating companies are technical analysis[23] and fundamental analysis. Technical analysis refers to:

> research into the demand and supply for securities, options, mutual funds and commodities based on trading volume and price studies. Technical analysts use charts or computer programs to identify and project price trends in a market, security, fund or futures contract. Most analysis is done for short- or intermediate-term, but some technicians also predict long-term cycles based on charts and other data.[24]

Fundamental analysis is the:

> analysis of the balance sheet and income statements of companies in order to forecast their future stock price movements. Fundamental analysts consider past records of assets, earnings, sales, products, management and markets in predicting future trends in these indicators of a company's success or failure. By appraising a firm's prospects, these analysts assess whether a particular stock or group of stocks is undervalued or overvalued at the current market price.[25]

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22 Conflicts included basing analysts' compensation on their contributions in support of investment banking transactions and the profitability of the investment banking unit, as well as analysts covering companies underwritten by the analysts' firms; investing in pre-initial public offerings of companies that they initially covered and for which their firms had acted as underwriters; and issuing favorable research reports or "buy" recommendations close to the expiration of a lock-up period. *Id.*

23 FINRA asserted that, in the discussion of the definition of "research report" under the research analyst rules, it would not exclude technical or quantitative analysis from the definition of research report. *See* NASD Notice to Members 04-18, *Research Analysts and Research Reports* (March 2004)

24 Dictionary of Finance and Investment Terms, 548-49 (4th ed. 1995).

25 *Id.* at 211.

Technical analysis is not applicable to a registered fund or private fund. Demand and supply, the basis of technical analysis for operating companies, do not influence the price of a registered fund or private fund, because, as noted earlier, a fund's price is based on the net value of its underlying portfolio securities. For example, the newsletters that broker-dealers produce include information about economic and market developments, but such information is general and is not about the underlying portfolio securities of the funds in which the investor is investing.

Similarly, with regard to fundamental analysis, analyzing assets, earnings, sales, products, management and markets in order to identify trends in a private fund would be meaningless because, in some cases, there is no such information, and, in other cases, only the information that relates to the underlying portfolio securities is meaningful. This information would not be about the private fund in which the investor is investing.

Finally, analysis in any of its forms involves the separate examination of constituent parts of an "individual company" engaged in commercial or industrial enterprises to form conclusions as a consequence of reasoning.[26] Unlike a single operating company equity security, which may be separated into its constituent parts (*e.g.*, price and market data, financial statement information, etc.),[27] a private fund is not composed of the same constituent parts of an operating company. Any analysis of a private fund would be problematic because a particular portfolio's securities are both concealed and ever changing.

FINRA should recognize that sales literature, regardless of whether the subject matter is a registered fund or private fund, is not a research report within the context of the Rule because it does not contain the technical or fundamental components of analysis. In addition, information about private funds does not contain information about individual companies that produce a product or provide a service.

Finally, private fund sales literature is likely to include information about the characteristics of the product and an assessment of its manager. Typically, this may be a restatement of information provided in fund offering documents (such as management style and tax consequences) coupled with personal evaluations. This type of discussion in the context of registered funds is not analysis[28] and, accordingly, should not be considered analysis in the context of private funds.

IV. Conclusion

For the foregoing reasons we urge FINRA to extend the Rule Proposal to exclude from the definition of "research reports" the sales literature of private funds because the risks that the Rule is intended to address are not present with respect to sales literature relating to securities that are not traded in secondary markets or that are redeemable by the issuer. Sales literature that is clearly marketing material and not objective analysis should not be subjected to the additional regulatory regime designed to preserve the objectivity of analysis. FINRA's previously articulated rationale for excluding from the definition of "research reports" the sales literature of open-end registered investment companies and public DPPs (*i.e.*, that Rule 2210 regulates such sales literature) applies equally to private funds. Finally, the regulatory concern that private fund sales literature will manipulate the value of a private fund is not

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26 *See* Webster's II New Riverside University Dictionary, 104 (1984).

27 *See* Black's Law Dictionary (5th ed. 1979).

28 FINRA staff, in discussions about interpreting the Rule, made this observation.

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an issue because private funds are priced at NAV, not by the market. In addition, private fund sales literature does not contain the type of analysis that research analysts manipulated, and this manipulation is what led to the adoption of Rule 2711.

We appreciate the opportunity to comment on this Rule Proposal. If you have any questions concerning the foregoing, please contact me. Thank you for your attention to this matter.

Very truly yours,

Elliott R. Curzon

cc: James A. Brigagliano
Associate Director SEC Division of Trading and Markets

Marc Menchel
FINRA Regulatory Policy and Oversight's Office of General Counsel

LEERINK SWANN

November 10, 2008

Via Electronic Transmission (pubcom@finra.org) and Overnight

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: Regulatory Notice 08-55

Dear Ms. Asquith:

Leerink Swann LLC ("Leerink")[1] is submitting this letter in response to the request by FINRA for comments on the Proposed Research Registration and Conflict of Interest Rules ("Notice")[2].

We appreciate and thank you for the opportunity to comment on the Notice, and, for the purpose of this letter, will initially comment on several of the proposed changes to quiet periods and lock-ups the firm supports and then focus our comments on two narrow and distinct issues. Those issues are: 1. the proposed restriction or limitation of research analysts participating in road shows or other marketing on behalf of issuers[3]; and 2. the selective distribution of research reports[4].

Quiet Period and Lock-Ups

We agree with the proposed changes to reduce the existing forty-day post-IPO research quiet period to ten days and the elimination of the black-out periods after a secondary offering and those surrounding the expiration of lock-up agreements[5]. The investing public stands to benefit from the

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[1] Leerink Swann LLC is a SEC-registered broker-dealer and a member of FINRA.
[2] *See* FINRA Regulatory Notice 08-55 ("Notice")
[3] *See* Proposed Rule 2240(b)(2)(J)(ii)
[4] *See* Proposed Rule 2240(g)
[5] *See* Proposed Rule 2240(b)(2)(G)

issuance of research containing valuable market information during those periods.

Those proposed changes are positive steps. The comments below raise questions relating to other proposals that require more discussion and consideration before submission to the Securities and Exchange Commission.

Marketing Initiatives

Rule 2711 was adopted in 2002 with the purpose of improving "the objectivity of research and provide investors with more useful and reliable information when making investment decisions."[6] The Rule was later amended in 2003 to include a provision prohibiting analysts from participating in efforts to solicit investment banking business, including "pitches" for investment banking business to prospective investment banking clients.[7] The stated purpose of the NASD in adopting the prohibition was "to further the overriding goals of research objectivity and investor confidence by eliminating all participation by research analysts in solicitation efforts that could suggest a promise of favorable research in exchange for underwriting business."[8]

The current version of Rule 2711(c)(5) prohibits research analysts from participating in a road show related to an investment banking services ***transaction*** (emphasis supplied) and from communicating with current or prospective customers in the presence of investment banking department personnel or company management about such an investment banking services ***transaction*** (emphasis supplied). In submitting the proposal to amend Rule 2711 relating to road shows to the SEC on September 17, 2004, NASD stated that "by prohibiting research analyst participation in road shows, the proposed rule change will further reduce the pressure on research analysts to give an

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[6] *See* NASD Notice to Members 02-39, page 1
[7] *See* NASD Notice to Members 03-44
[8] *See* letter from Philip A. Shaikun, Associate General Counsel (NASD) to James A. Brigagliano, Esq., Assistant Director, Division of Market Regulation, dated July 29, 2003, Page 7.

overly optimistic assessment of a particular transaction."[9] Recognizing, however, that analysts provided a valuable service in the marketplace, the proposal allowed for research analysts to educate investors about a particular offering or other transaction, so long as the communication occurred outside the presence of the company or investment banking department personnel. This exception preserved the ability of the research analyst to give a candid assessment of a ***transaction or sale of securities***[10] (emphasis supplied). In announcing the approval of the amendment in Notice to Members 05-34 in May 2004, the NASD again stated that the rule, as amended, would "further reduce pressure on research analysts to give an overly optimistic assessment of a particular ***transaction***"[11] (emphasis supplied).

Interestingly, on September 24, 2004, one week after the amended proposal referenced *supra* was filed with the SEC, Judge Pauley approved the terms of Addendum A to the Global Research Analyst Settlement. Undertaking 11 prohibited research personnel at the settling firms "from participating in company-or Investment Banking-sponsored road shows related to a public offering or other investment banking ***transaction***" [12] (emphasis supplied).

It is clear that the intent of the regulatory authorities for the past seven years was to allow the research analyst to offer a candid assessment of a transaction or sale of securities outside of the presence of either his firm's investment bankers or representatives of the company. Proposed Rule 2240(b)(2)(J)(ii) prohibiting analysts' "participation in road shows and other marketing on behalf of issuers"[13] eliminates an important condition that the prohibition relate to the analyst's participation

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[9] *See* File No. SR-NASD-2004-141, dated September 17, 2004, Page 5
[10] *Id*
[11] *See* NASD Notice to Members 05-34, May 2005, page 2
[12] *See* Section 11.a of Addendum A, Undertakings, approved September 24, 2004
[13] *See* fn 3

in the marketing of a specific investment banking services transaction. Is it possible that FINRA intends to prohibit all participation in marketing by research analysts whether or not related to investment banking services? If that is the purpose, how then can "analysts, who are expected to function as unbiased intermediaries between issuers and the investors who buy and sell their securities"[14] carry out that role? Clarification is required and FINRA should understand the implications for issuers, private investors and institutions. Clearly, the impact will also be felt by companies - both private and public. Not every contact with a company should be looked at as marketing the investment banking services of the analyst's firm or jeopardizing the analyst's objectivity.

Research analysts are expected to analyze and understand the industry or sector they cover. Not every company will be a banking client or prospect of the analyst's firm at any given moment. We all know that things can change rapidly in today's financial services' world and opportunities, once unreachable, can develop overnight. How can the analyst be an unbiased intermediary if he is not able to take advantage of what companies make available to him in the way of marketing themselves?

Companies regularly sponsor analyst days to help analysts better understand the products, meet management and tour facilities. This activity is marketing in its purest sense. The proposed rule would appear to prohibit the analyst from attending one of these events if institutional investors or analysts from other firms were also in attendance. Would companies be forced to limit attendance to one analyst at a time or would one-on-one meetings also be prohibited?

Companies will often approach firms to provide an audience so that the company's management team can tell its story to salespeople and clients. Firms may often be able to provide exposure to some of its clients, particularly

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[14] *Notice* at 2

institutions and their portfolio managers, that the companies cannot otherwise obtain. The questions raised by salespeople and portfolio managers and their reaction to the story are of particular value to the analyst in better understanding sectors and industries, competitive issues, industry trends, etc. in order for him to serve as an unbiased intermediary. The benefit to the company in speaking with investment professionals cannot be overlooked. Would the proposed rule prohibit the analyst from attending these company marketing presentations if clients participate? If only the salespeople attend, can the analyst participate or would the analyst need to leave the room?

FINRA members often sponsor widely-attended, invitation-only client conferences and roundtables providing a large number of companies - both public and private - the opportunity to tell their stories to investors. Analysts will often moderate many of the sessions at these events. The sessions may include a number of different companies in the same sector discussing their products with the institutional clients. Again, a marketing initiative for companies facilitated by FINRA members. Will participation by analysts in these events be prohibited? Would they even be permitted to attend?

How do institutional clients value this access to company management? Company marketing is considered an integral part of the role of sell-side analysts and during company marketing meetings, it is standard industry practice for the companies to be accompanied by analysts. In surveys of institutional clients conducted by *Institutional Investor* over the past five years, "Management Access" has consistently ranked among the top priorities at either 4th or 5th. Considered by many to be the most prominent survey in the industry, the 2008 survey consulted 3000 individuals at 830 firms, including 87 of the then largest U.S. money managers.[15]

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[15] *Institutional Investor*, October 2004-2008

According to a proprietary report based on 1,052 in-person interviews with buy-side analysts from 395 targeted institutions and 230 interviews with portfolio managers from 506 targeted firms during the period of November 2007 through March 2008 conducted by Greenwich Associates, company marketing is a well-entrenched practice which institutions value highly and for which they directly allocate commissions[16]. Direct access to companies' management (non-deal road shows, one-on-one meetings and conference calls)) was considered in two ways: 1. as one of twelve qualitative factors in the Greenwich Quality Index; and 2. indications from buy-side firms of the percentage of commissions they pay for this direct access. In the survey, direct access to companies' management was the number two priority in allocating commissions. This result has been consistent throughout the past three years. In terms of actual amounts, buy-side analysts allocate 22% of commissions and buy-side portfolio managers allocate between 20-25% for this access. This empirical evidence clearly demonstrates the importance of research analysts continuing to be able to participate in these marketing events.

Research conferences and seminars were also included in the Greenwich survey and over the past three years were ranked as a high priority in allocating commissions. Analysts for buy-side firms responding ranked research conferences and seminars as the number three priority representing 13% of commissions allocated to the sell-side. Portfolio managers ranked the activity as number four representing 12% at both small and large clients.

A significant number of institutional clients demonstrate their view of the sell-side firms through portfolio manager and analyst votes on a quarterly, semi-annual or annual basis. These votes are important feedback to sell-side managers for the votes tell you what the firm does well and what it may need to improve upon. In one recent vote received by this firm, the management of the buy-side firm indicated that approximately 31% of

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[16] Greenwich Associates ("*Greenwich*"), 2008

commissions allocated were for company marketing meetings as "meetings with corporate management are the most highly valued service our brokers can provide … Points are awarded for small group meetings, one-on-ones at conferences, meetings in our office or field trips your analysts arrange to corporate headquarters". These type of comments are frequently made as demonstrated in the results of the *Institutional Investor* and Greenwich Associates surveys.

Marketing is an important component for all companies. The questions raised *supra* require further consideration in advance of any rule filing with the Securities and Exchange Commission.

Distribution of Member Research Reports

Proposed Rule 2240(g) is meant to codify FINRA's existing interpretation of Rule 2110 with regards to the timing and distribution of research reports and provide additional guidance concerning firms offering different research products and services to certain classes of clients with the proviso that the firm discloses its research dissemination practices[17]. The proposed rule and Supplementary Material raise a number of issues and necessitate clarification by FINRA.

The existing interpretation[18] referred to in the Notice appears to be narrower than represented in the Notice as it addresses the issue of a member firm's trading activities that occur in anticipation of a firm's issuance of a research report. The published interpretation does not permit a firm to purposefully change its inventory position through "trading activities undertaken with the intent of altering a firm's position in a security in anticipation of accommodating investor interest once the research report has been issued[19]". While the published interpretation does not refer to clients, firms understand that FINRA views

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[17] *Notice*, Proposed Supplementary Material .04
[18] *See* IM-2110-4
[19] *Id*

improperly giving advance notice of research reports and ratings to institutional (or other) clients as violating regulatory standards[20] and support that position. To the same end, in a subsequent rule filing submitted to adopt FINRA Rule 5280 (Trading Ahead of Research Reports), FINRA again addresses the issue of front-running research reports stating it "believes that a member should have an affirmative obligation to manage conflicts of interest in trading securities."[21] FINRA goes on to say that the proposal "will protect the investing public by preventing firms from utilizing non-public advance knowledge of the timing or content of a research report to benefit its own trading to the detriment of its own customers."[22] FINRA describes this approach as "more consistent with existing and proposed rules regarding supervision and the requirements of NASD Rule 2711 and NYSE Rule 472 to eliminate conflicts involving the publication and distribution of research reports."[23]

The Proposed Supplementary Material expands the existing interpretation to impose new requirements on firms that provide different research products and services - not solely research - for certain clients. Specifically, member firms would be required to inform its other clients that its alternative research products and services may reach different conclusions or recommendations that could impact the price of a security[24]. It must be emphasized that the proposal would now extend beyond "research reports", a defined term, to "research products and services", which is not defined. In the investment business (as in many others), clients that generate more commissions receive different levels of service and products. These products and service levels are varied and may not always relate to recommendations or ratings. In the institutional business, tiered relationships are rarely memorialized by written agreement. Firms rely on institutional salespeople and

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[20] *See* Phua Young, NASD Complaint, May 28, 2003.
[21] *See* File No. SR-FINRA-2008-054 dated October 29, 2008, page 6
[22] *Id*, page 7
[23] *Id*, page 6
[24] *Greenwich*

sales traders to "cover" clients and discuss levels of service with clients. In reality, clients in the institutional world understand that more commissions will result in more attention. The simplest way for a client to express its dissatisfaction with a sell-side firm is to stop sending order flow. Conversely, sell-side service may drop in relation to commission flow from the buy-side.

A number of questions arise:

1. Is the use of the term "research products and services" meant to only apply to "research reports"?;
2. If not, what is the definition of "research products and services"?;
3. Is proposed Rule 2240(g) and proposed Supplementary Material .04 meant to apply solely to prohibiting a firm offering a trading advantage to one type of client over another client?; and
4. Should a carve-out from the notification provision be included for institutional clients? If not, can the notification be provided orally?

FINRA should provide clarification for the issues identified *supra*.

We recognize FINRA's objective to establish a "principle based" regulatory environment allowing a firm to develop policies and procedures based on the individual firm's size and business model. Clarification, however, is needed to allow firms to better understand how the specific proposals discussed *supra* "further the overriding goals of research objectivity and investor confidence".

Ms. Marcia E. Asquith
November 10, 2008

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If you have any questions or wish to discuss the comments, please contact me at 617-918-4564.

Very truly yours,

John I. Fitzgerald

JIF/gct

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November 11, 2008

VIA E-MAIL: pubcom@finra.org

Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506
Attn: Marcia E. Asquith

Re: Regulatory Notice 08-55 - Research Analysts and Research Reports

Dear Ms. Asquith:

On behalf of The National Venture Capital Association (the "NVCA"), we appreciate the opportunity to provide comments to FINRA on Regulatory Notice 08-55 on proposed FINRA Rules 1223 and 2240 regarding research analyst conflict of interest rules.

The NVCA is the premier trade association that represents the U.S. venture capital industry. It is a member-based organization, consisting of venture capital firms that manage pools of risk equity capital dedicated to be invested in high growth, entrepreneurial companies. NVCA's mission is to foster greater understanding of the importance of venture capital to the U.S. economy, and support entrepreneurial activity and innovation. The NVCA represents the public policy interests of the venture capital community, strives to maintain high professional standards, provides reliable industry data, sponsors professional development, and facilitates interaction among its members. Over the last ten years, venture-backed companies represented approximately 25 percent of initial public offerings in the U.S.

The NVCA supports FINRA's efforts to achieve a balance between ensuring objective and reliable research on the one hand, and permitting the flow of information to investors and minimizing costs and burdens to member firms on the other. We agree with FINRA that liberalizing the availability of research will provide investors with valuable market information, and that the other provisions of the research rules and SEC regulations are sufficient to protect the integrity of such research.

The proposed rules would benefit IPO issuers in particular by making research coverage available more quickly, easing restrictions on research coverage around lock-up expirations, waivers and terminations, providing greater flexibility to waive or modify lock-ups and making negotiation of lock-up agreements easier. We note, however, that the 25-day prospectus delivery

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requirement of the Securities Act may result in underwriters self-imposing a 25-day quiet period in connection with initial public offerings. Similarly, underwriters and issuers may have concerns that research issued shortly after a secondary offering could result in prospectus liability.

Overall, we believe the proposed rules are a step in the right direction, but that more can and should be done to restore the competitive position of the U.S. public equity market, especially new capital formation via initial public offerings. The number of initial public offerings in recent years has continued to decline as a result of the ongoing erosion of the competitive position of the U.S. public equity market. This loss of competitive advantage has resulted in a significant decline in capital markets activity generally, and caused seriously detrimental effects on the formation and efficient allocation of capital for emerging growth companies in particular. The recently released Interim Report of the Committee on Capital Markets Regulation (the "CCMR") found the U.S. market increasingly unable to capture initial public offerings and compete in the global marketplace, in large part due to the cost and competitive disadvantages of the regulatory process in the U.S.

Of particular concern to venture-backed companies is The Global Settlement of Conflicts of Interest Between Research and Investment Banking (the "Global Settlement") reached in April 2003, which fundamentally changed the ability of new and small companies to obtain research analyst coverage. The Global Settlement and the disincentives it created, resulted in the disappearance of research analyst coverage for small and mid-cap companies. That research coverage, formerly provided by analysts employed by the investment banks that brought such companies public, was critical to attracting sufficient interest and investment from institutional capital, without which such companies could not survive. Combined with the skyrocketing costs imposed on newly-public companies by Sarbanes-Oxley, the IPO window for venture-backed companies essentially closed.

The NVCA fully supports a regulatory framework that strikes a proper balance between investor protection and market integrity on the one hand and the cost, burden and intrusion imposed on market participants on the other. We further recognize that FINRA is part of a larger overall regulatory framework that must operate within a broader market context.

Thank you for the opportunity to comment on Notice 08-55. Please feel free to contact Ettore A. Santucci at 617-570-1531, William J. Schnoor at 617-570-1020 or Eric J. Graham at 617-570-1006 if we can be of any further assistance.

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Sincerely,

Goodwin Procter LLP

GOODWIN PROCTER LLP

cc: Mark G. Heesen, President
National Venture Capital Association

Please accept this in response to FINRA requests for Comment on Proposed Research Registration and Conflict of Interest Rules contained in Regulatory Notice 08-55

Proposed FINRA Rule 1223 is a step in the right direction by easing the requirement to pass the Series 86 exam so that only those associated persons "whose primary job function is to provide investment research" (combined with other criteria such as also passing the Series 87 exam) are required to pass it. However, the Series 86 exam as now designed should be eliminated in its entirety or revised to only test for knowledge of the regulations dealing with conflicts of interest and personal bias. The Series 86 exam is much too difficult - some say it is harder than bar exams and accountancy exams and on a par with one of the most difficult professional exams of all, the CFA.

I believe that part of the current economic crisis facing the U.S. is the result of analysts not identifying the risks inherent in derivative instruments. This failure is a result of over reliance on the traditional modeling and valuation techniques in the investment community. Of the five sections of the current Series 86 exam, four test "Analysis, Modeling and Valuation" in various applications and one section tests information and data collection.

Also, this emphasis on metrics and forecasting based on past performance has little to do with the thousands of smaller listed companies that have short operating histories and need research coverage. The Series 86 exam shows a bias in favor of analysts who cover large capitalized companies with several years of operating history. Some analysts are interested in covering smaller companies who do not have years of operating history. These analysts have no interest in taking the time and expending resources to memorize dozens of forecasting metrics, mathematical models and formulae that they are required to master in order to pass the Series 86 exam. In addition, the Series 86 exam virtually ignores non-data driven approaches to stock market analysis that may be better than the modeling and valuation techniques tested by the Series 86 exam and, if more widely used, could have prevented the current economic c! risis. One such ignored approach is known by economists as behavioral economics or behavioral finance. This approach recognizes that data does not always rule and that often markets are imperfect because they are driven by factors other than metrics such as sociological and psychological factors.

In addition, I believe that the current Series 86 exam prerequisite is governmental action that unnecessarily restricts a citizen's right to comment on the stock market, individual companies and their management and could be ripe for challenge on first amendment constitutional grounds.

Finally, in practice it is extremely difficult for FINRA members to comply with the myriad of regulations impacting communications with the public by a broker-dealer. The current definitions contained in FINRA Rule 2240 and Rule 2210 are sometimes tautological and define by negative reference. For example, the term "Research Report" in Rule 2240(a)(10) in the first paragraph gives a basic, short definition but then states: "The term does not include: . . ." and lists five categories as definitional carve-outs under subparagraph (A), three categories under subsection (B) and one category under subsection (C). To add to the confusion, Rule 2210(a) states that "communications with the public: consist of . . ." and then sets forth six broad categories that sometimes cross-reference each other. Often, it is very difficult for securities attorneys and compliance professionals to determine whether mat! erial is an "advertisement" under the definition contained in Rule 2210(a)(1) or "sales literature" as that term is defined in Rule 2210(a)(2). A large part of this confusion is the result of the definition of "sales literature" begriming this way: "Any written or electronic communication, *other than an advertisement . . .* (italics mine)." In a close-call as to whether particular material is advertising versus sales literature, this tautological drafting device makes a definitional comparison impossible. More confusion results because as the rules are now drafted sometimes the media used to disseminate material, as opposed to the content of the material, determines its communication status and the regulations that apply. FINRA should issue clear and workable definitions of "communications with the public," please.

In conclusion, FINRA should encourage, not discourage, market transparency by easing the overly burdensome restrictions on broker-dealers, especially smaller broker-dealers, who desire to issue research reports. Specifically, the Series 86 exam prerequisite should be eliminated or the exam should be redesigned. It is one thing to test analysts regarding their obligations to avoid conflicts of interests and to voice their true opinions. However, FINRA should not be the arbiter of determining which world view of the market is the correct one.

Respectfully submitted,
Daniel H. Kolber,
Atlanta, Georgia
24, 27, 87, 4, 53, 54, 7, 63, 65 FINRA Licenses,
Member of Georgia, New York, Florida, and Virginia Bars