



### FINRA Proposes New Rules Governing Communications with the Public

On September 21, 2009, FINRA issued Regulatory Notice 09-55, requesting comments on proposed new rules governing communications with the public by FINRA member broker-dealers.<sup>1</sup> The new rules would replace current NASD Rules 2210 and 2211, related interpretive material, and parts of Incorporated NYSE Rule 472.<sup>2</sup> While based on the current requirements, the new rules are intended to revise and update them, including streamlining the categories of communications to which the requirements apply.<sup>3</sup> The new rules would revise the filing requirements for new firms, require filing of communications that currently are not required to be filed, and make other changes to the rules governing communications by broker-dealers. Certain content requirements that now apply only to advertisements and sales literature would apply to all retail communications, broadly defined as any written or electronic communication distributed or made available to more than 25 retail investors. Also proposed are new requirements for the disclosure of certain tax considerations, which would impact the marketing of municipal bonds and other products with tax advantages.

Given the comprehensive nature of the proposed revisions, we have included as an attachment to this briefing a chart that compares the existing rules to the proposed rules.

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#### Background

Currently, NASD Rules 2210 and 2211, and the Interpretive Materials that follow Rule 2210, govern communications with the public by FINRA member broker-dealers. Incorporated NYSE Rule 472 governs public communications by FINRA members that also are NYSE members. At present, there are six categories of public communications:

**Advertisements.** Written and electronic retail communications with an unlimited audience, such as newspaper, magazine, television and radio advertisements, billboards, and web sites.

**Sales Literature.** Written and electronic retail communications with a targeted audience, such as brochures, performance reports, telemarketing and seminar scripts, and form letters.

<sup>1</sup> <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p120005.pdf>. The text of the proposed rules can be found at <http://www.finra.org/web/groups/arbitrationmediation/documents/industry/p120006.pdf>.

<sup>2</sup> Incorporated NYSE Rules are rules of the New York Stock Exchange (“NYSE”) that FINRA has incorporated into its rulebook. They will apply to FINRA members that also are NYSE members until FINRA adopts a consolidated rulebook applicable to all members.

<sup>3</sup> The new rules are not intended to address FINRA/NASD’s interpretive guidance, such as its limitations on the use of “related performance information” in hedge fund marketing materials.

**Correspondence.** Written letters, e-mail, instant messages, and market letters sent to one or more existing retail customers and fewer than 25 prospective retail customers within a 30-calendar-day period.

**Institutional Sales Material.** Communications distributed exclusively to “institutional investors,” including registered investment companies, insurance companies, banks, broker-dealers, investment advisers, certain retirement plans, governmental entities, and individual investors and other entities with at least \$50 million in assets.

**Independently Prepared Reprints.** Reprints of articles from independent publications and reports published by independent research firms.

**Public Appearances.** Unscripted participation in live events such as interviews, seminars, and call-in television and radio shows.

The requirements for approval, filing, and retention of a particular communication depend on the category into which it falls. Current rules also include general and specific content standards. For example, all communications must be fair and balanced, and must provide a sound basis for evaluating the facts relating to the particular security, industry, or service to which the communication refers. Material facts may not be omitted, if doing so would make the communication misleading. In addition, there are specific content standards for different types of communications, securities or products.

## The Proposed Rules

Proposed FINRA Rule 2210 would incorporate, with certain changes and updates, current NASD Rules 2210 and 2211, NASD Interpretive Materials 2210-1 and 2210-4, and those provisions of Incorporated NYSE Rule 472 that do not pertain to research analysts and research reports. Other Interpretive Materials that follow NASD Rule 2210 would be renumbered. For example, NASD Interpretive Material 2210-2 would be replaced by new FINRA Rule 2211 (Communications with the Public About Variable Insurance Products), which is the subject of a separate proposal.

**Categories of Communications.** The new rules would reduce the number of categories of public communications from six to three:

**Institutional Communications.** Materials currently defined as “institutional sales material” in NASD Rule 2211.

**Retail Communications.** Any written or electronic communication distributed or made available to more than 25 retail investors (*i.e.*, any person other than an institutional investor, regardless of whether the person is an existing or prospective customer).

**Correspondence.** Any written or electronic communication that is distributed or made available to 25 or fewer existing or prospective retail investor customers.

Communications currently defined as “advertisements” and “sales literature” generally would fall under the definition of “retail communications,” while current “institutional sales material” would fall under “institutional communications.” Some communications currently defined as “correspondence” would continue as such -- the new definition will cover all communications distributed to 25 or fewer retail investors -- but communications sent to more than 25 retail investors now would be treated as retail communications.

The new rules eliminate the categories “public appearance” and “independently prepared reprint”; however, they incorporate most of the filing exceptions and content standards that currently apply to such communications. Public appearances that include recommendations of securities would be subject to new disclosure standards.

**Approval, Review, and Recordkeeping.** The new rules would require a qualified registered principal of the firm to approve each retail communication before its use or its filing with FINRA, whichever comes first. The category of principal registration required for approving a communication would depend on the particular communication. A Series 16 supervisory analyst would continue to be permitted to approve research on debt and equity securities, and the current exception from principal approval for retail communications that another firm has filed with FINRA and were found to meet applicable standards would remain. The approval requirement would not apply to retail communications that are solely administrative in nature, such as advertisements solely related to recruiting; changes to a firm’s name, personnel, electronic or postal address, ownership, offices, business structure, partners, telephone or teletype numbers; or changes concerning mergers or acquisitions with or by another firm.

The current supervision and review standards for correspondence and institutional communications would remain. Recordkeeping requirements for retail and institutional communications would incorporate the form and time periods required by SEC Rule 17a-4.

**Filing Requirements and Review Procedures.** The new rules generally incorporate the filing requirements in NASD Rule 2210(c), but there are some important changes. NASD currently requires a firm that has not filed advertisements with FINRA or another self-regulatory organization to file its initial advertisement at least 10 business days prior to its use. This continues for one year after the initial filing. The new rules would change the filing requirements for new firms. First, the new-firm filing requirement would cover all retail communications, not just advertisements. Second, the one-year filing requirement would begin on the effective date of a firm's FINRA registration, rather than on the date that an advertisement is first filed with FINRA.

Currently, firms must file certain communications at least 10 business days prior to initial use and refrain from using them until any FINRA-required changes have been made. This applies to advertisements and sales literature for certain registered investment companies that include self-created rankings, advertisements concerning CMOs, and advertisements concerning security futures. The new rules would expand the list of communications requiring pre-use filing to include retail communications that include bond mutual fund volatility ratings, and retail communications concerning any publicly offered securities derived or based on a single security or basket of securities, an index, a commodity, a debt issuance, or a foreign currency.

The new rules would revise current filing standards for retail communications concerning closed-end investment companies, streamline the current exclusion for independently prepared reprints, and eliminate a filing exception for press releases made available only to members of the media.

**Content Standards.** The new rules would incorporate, reorganize, and amend the current content standards for public communications. The current standards for advertisements and sales literature generally would apply to retail communications. Promissory statements or claims would be expressly prohibited. Standards concerning disclosure of a firm's name would apply to correspondence as well as to retail communications, and a firm would be permitted to use the name disclosed on its Form BD and any fictional name by which it is commonly recognized or which is required by a state or other jurisdiction.

The new rules add language relating to comparative illustrations of mathematical principles of tax-deferred versus taxable compounding, much of which reflects previous FINRA guidance, and would apply to any such illustrations irrespective of the nature or content.

In addition to current requirements for communications (other than institutional sales material and correspondence) that present performance of non-money market mutual funds, the new rules would require disclosure of the maximum sales charge and total operating expense ratio based on the fund's prospectus or annual report, whichever is more current.

Current standards for communications containing recommendations would be revised to apply to retail communications, correspondence, and public appearances (the current standards apply only to advertisements and sales literature), and would require disclosure if the firm or any associated person with the ability to influence the communication's substance has a financial interest in the recommended issuer and the nature of any such interest. This would reduce the number of parties whose financial interests must be disclosed, especially for large firms with numerous officers and partners. It also would align the rules with the disclosure standards of proposed FINRA Rule 2240 concerning research.

The new rules also would amend the requirements for communications that include past recommendations, permitting retail communications and correspondence to set out or offer to furnish a list of all recommendations of the same type, kind, grade or classification of securities made by the firm within a preceding period of not less than one year, subject to certain conditions. This is similar to requirements found in Rule 206(4)-1(a)(2) under the Investment Advisers Act of 1940. The new rules would limit any reference to a FINRA staff review of a communication to either "Reviewed by FINRA" or "FINRA Reviewed."

Public appearances would have to meet general "fair and balanced" standards. Persons recommending securities at public appearances generally would be subject to the same disclosure requirements as research analysts making recommendations at public appearances. Firms also would be required to establish written policies and procedures to supervise public appearances, and make clear that scripts, slides, handouts, or other written and electronic materials used at such appearances are considered communications subject to the new rules.

**Use of Investment Company Rankings in Retail Communications.** The new rules generally would continue the standards applicable to the use of investment company rankings in communications, applying them to retail communications instead of advertisements and sales literature. Reprints or excerpts of articles or reports that are excluded from the filing requirements would be excepted from this requirement as well.

**Use of Investment Analysis Tools.** Proposed FINRA Rule 2214 replaces NASD IM-2210-6 with regard to the standards applicable to the use of investment analysis tools with retail customers. The standards would remain the same but some of the language in IM-2210-6 would be moved to supplementary material.

**Communications Regarding Security Futures.** The new rules would revise current standards in several respects to conform to NASD Rule 2220 (Options Communications).<sup>4</sup> For example, portions of the current requirements apply only to advertisements, while the new rules would apply these provisions to all retail communications. The new rules also would amend provisions requiring certain communications to be accompanied or preceded by the security futures risk disclosure document, limiting the disclosure document requirement to communications with the names of specific securities. Other changes would include a prohibition on security futures communications that suggest the availability of a secondary market; a requirement that any statement

referring to potential opportunities or advantages be balanced by an equally specific statement concerning corresponding risks; and clarification that communications containing historical performance of security futures must disclose all relevant costs, which must be reflected in performance.

### Comments/Effectiveness

FINRA is requesting comments on or before November 20, 2009. Comments may be submitted in hard copy by mail to Marcia E. Asquith, Senior Vice President and Corporate Secretary, Office of the Corporate Secretary, FINRA, 1735 K Street, NW, Washington, DC 20006-1500; or by e-mail to [pubcom@finra.org](mailto:pubcom@finra.org). Comments will be made publicly available on the FINRA web site.

Before they become effective, the new rules must be approved by the SEC following publication in the Federal Register and receipt and review of public comments.

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<sup>4</sup> Separately, FINRA is proposing to adopt NASD Rule 2220 into the Consolidated FINRA Rulebook, without substantive change, as FINRA Rule 2220.

**Comparison of Current and Proposed Rules**

	<b>NASD Rule</b>	<b>NYSE Rule</b>	<b>Proposed FINRA Rule</b>
<b>Categories of Communications</b>	2210(a)(1)-(6)	472.10	2210(a)(2), (3), (5)
<b>Approval Requirements</b>	2210(b)(1) (advertisements, sales literature, independently prepared reprints)	472(a)(1)	2210(b)(1) (retail communications) 2210(b)(2) & 3010(d) (correspondence)
<b>Approval Requirements – Institutional</b>	2211(b)(1) (institutional sales material & correspondence)	472(a)(1)	2210(b)(3) (institutional communications)
<b>Recordkeeping Requirements</b>	2210(b)(2) (advertisements, sales literature, independently prepared reprints)	472(d)	2210(b)(4)(A)(retail communications) 2210(b)(4)(B) (correspondence)
<b>Recordkeeping Requirements – Institutional</b>	2211(b)(2)	472(d)	2210(b)(4)(A) (institutional communications)
<b>Filing Requirements</b>	2210(c)(1)–(9)	---	2210(c)(1)-(8)
<b>Filing Requirements – New Filers</b>	2210(c)(5)	---	2210(c)(1)
<b>Filing Requirements – Types of Communications</b>	2210(c)(4) (advertisements and sales literature)	---	2210(c)(2), (3) (retail communications)
<b>Filing Requirements – Video &amp; Television Advertisements</b>	2210(c)(6) (advertisements)	---	2210(c)(4) (retail communications)
<b>Filing Requirements – Exceptions</b>	2210(c)(8)	---	2210(c)(7) (retail communications)
<b>Content Standards</b>	2210(d)(1) (all communications) 2210(d)(2) (advertisements and sales literature)	472(i), (j)	2210(d)(1) (all communications)
<b>Content Standards – Institutional</b>	2211(d)	472(i), (j)	2210(d)(1) (all communications)
<b>Content Standards – Testimonials</b>	2210(d)(1)(E) (all communications) 2210(d)(2)(A) (advertisements and sales literature)	472(j)(7)	2210(d)(6)(A) (all communications) 2210(d)(6)(B) (retail communications and correspondence)
<b>Content Standards – Recommendations</b>	IM-2210-1	472(j)(1), (2)	2210(d)(7)
<b>Content Standards – Comparisons</b>	2210(d)(2)(B) (advertisements and sales literature)	472(j)(4)	2210(d)(2) (retail communications)
<b>Content Standards – Disclosure of Member Name</b>	2210(d)(2)(C)(advertisements and sales literature)	---	2210(d)(3) (retail communications and correspondence)
<b>Misleading Communications</b>	IM-2210-1	472(i)	2010(d)(1), 2010(d)(7)
<b>Use of Investment Company Rankings</b>	IM-2210-3 (advertisements and sales literature)	---	2212 (retail communications)
<b>Use of FINRA’s Name</b>	IM-2210-4	---	2210(e)
<b>Use of Bond Mutual Fund Volatility Ratings</b>	IM-2210-5	---	2213
<b>Use of Investment Analysis Tools</b>	IM-2210-6	---	2214, 2210(d)(7)
<b>Communications re Security Futures</b>	IM-2210-7	---	2215
<b>Communications re CMOs</b>	IM-2210-8	---	2216

The Financial Services Practice Group of Winston & Strawn represents a broad range of financial institutions on all regulatory matters. If you have any questions regarding the matters discussed in this Briefing, if you need assistance in preparing comments to FINRA regarding the proposed rules, or if you need assistance in analyzing, developing, and/or reviewing systems, controls, and/or procedures relating to these matters, please contact any of the Winston & Strawn attorneys listed below or your usual Winston & Strawn contact.

**New York**

Edward J. Johnsen	<a href="mailto:ejohnsen@winston.com">ejohnsen@winston.com</a>	(212) 294-4741
Robert A. Boresta	<a href="mailto:rboresta@winston.com">rboresta@winston.com</a>	(212) 294-4711
Eric L. Cohen	<a href="mailto:elcohen@winston.com">elcohen@winston.com</a>	(212) 294-3540
Jeffrey H. Elkin	<a href="mailto:jelkin@winston.com">jelkin@winston.com</a>	(212) 294-6711
David A. Sakowitz	<a href="mailto:dsakowitz@winston.com">dsakowitz@winston.com</a>	(212) 294-2639

**Chicago**

Milton K. Buckingham	<a href="mailto:mbuckingham@winston.com">mbuckingham@winston.com</a>	(312) 558-6212
Christine A. Edwards	<a href="mailto:cedwards@winston.com">cedwards@winston.com</a>	(312) 558-5571
Basil V. Godellas	<a href="mailto:bgodellas@winston.com">bgodellas@winston.com</a>	(312) 558-7237
Wesley G. Nissen	<a href="mailto:wnissen@winston.com">wnissen@winston.com</a>	(312) 558-5804
Michael M. Philipp	<a href="mailto:mphilipp@winston.com">mphilipp@winston.com</a>	(312) 558-5905

**Washington**

Paul Pilecki	<a href="mailto:ppilecki@winston.com">ppilecki@winston.com</a>	(202) 282-5730
Peter Malyshev	<a href="mailto:pmalyshev@winston.com">pmalyshev@winston.com</a>	(202) 431-3912
Michael A. Mancusi	<a href="mailto:mmancusi@winston.com">mmancusi@winston.com</a>	(202) 282-5729

**London**

Zoe J. Ashcroft	<a href="mailto:zashcroft@winston.com">zashcroft@winston.com</a>	+44 (0)20 7105 0025
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**Charlotte**

David L. Batty	<a href="mailto:dbatty@winston.com">dbatty@winston.com</a>	(704) 350-7720
James T. Hedrick	<a href="mailto:jhedrick@winston.com">jhedrick@winston.com</a>	(704) 350-7725
W. Kent Walker, Jr.	<a href="mailto:kwalker@winston.com">kwalker@winston.com</a>	(704) 350-7730
Dean A. Warren	<a href="mailto:dwarren@winston.com">dwarren@winston.com</a>	(704) 350-7735

**Paris**

Jérôme Herbet	<a href="mailto:jherbet@winston.com">jherbet@winston.com</a>	+33(0)1 53 64 82 04
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**San Francisco**

William J. Harvey	<a href="mailto:wharvey@winston.com">wharvey@winston.com</a>	(415) 591-1425
James E. Topinka	<a href="mailto:jtopinka@winston.com">jtopinka@winston.com</a>	(415) 591-1519
Alisa Won	<a href="mailto:awon@winston.com">awon@winston.com</a>	(415) 591-1464