SIFMA
Securities Industry and
Financial Markets Association

March 5, 2007

BY E-MAIL TO: rule-comments@sec.gov

Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: File Nos. SR-NYSE-2006-78 and SR-NASD-2006-113; Proposed Rule Changes Relating to NYSE Rule 472 and NASD Rule 2711

Dear Ms. Morris:

The Securities Industry and Financial Markets Association ("SIFMA")[1] appreciates the opportunity to comment on the above-referenced rule filings ("Rule Filings") submitted to the Securities and Exchange Commission ("Commission") by the New York Stock Exchange LLC ("NYSE") and NASD, Inc. ("NASD" and, collectively with NYSE, "SROs").[2] We support the efforts of the SROs in reviewing NYSE Rule 472 and NASD Rule 2711 ("SRO Rules"), leading to the *Joint Report by NASD and the NYSE On the Operation and Effectiveness of the Research Analyst Conflict of Interest Rules*,

[1] The Securities Industry and Financial Markets 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] The Commission issued a notice of the Rule Filings on January 9, 2007. Securities Exchange Act Release No. 55072, 72 FR 2058 (January 17, 2007) ("Notice of Proposed Rule Change").

which the SROs issued in December 2005 ("Joint Report"). In particular, we are pleased that the SROs have taken affirmative steps to implement many of the rule changes recommended in the Joint Report. We urge the SROs to continue their review and assessment of their research rules.

We also appreciate the time and effort that the SROs have dedicated to developing joint interpretive guidance on the application of the SRO Rules.[3] This joint guidance has been comprehensive and thoughtful, has led to consistent application of the SRO Rules, and has greatly assisted member firms in their compliance with the SRO Rules.

We have specific comments on the Rule Filings, which are set forth below. However, from a more general policy standpoint, we note that NASD's and NYSE's proposals differ in a number of respects, including the proposed amendments regarding Quiet Periods and Personal Trading Restrictions. We recognize the challenges that the SROs face in reconciling their particular regulatory perspectives and constituencies. However, the differences in the proposals would create compliance and administrative burdens on dual member firms, as well as regulatory disparities between dual-member firms and NASD-only firms. We urge the SROs to harmonize their proposals in this important area, particularly in light of the SROs' stated intention of consolidating their member regulation functions during the second quarter of 2007.

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[3] *See JOINT MEMORANDUM OF NASD AND THE NEW YORK STOCK EXCHANGE, Discussion and Interpretation of Rules Governing Research Analysts and Research Reports (NASD Rule 2711 and NYSE Rules 351 and 472)*, included in NASD Notice to Members 02-39 ("2002 Joint Guidance"); *JOINT MEMORANDUM OF NASD AND THE NEW YORK STOCK EXCHANGE, Discussion and Interpretation of Rules Governing Research Analysts and Research Reports (NASD Rule 2711 and NYSE Rules 351 and 472)*, included in NASD Notice to Members 04-18 ("2004 Joint Guidance").

Specific Comments on the Rule Filings

SIFMA supports many of the aspects of the Rule Filings, including the proposals to narrow the definitions of the terms "Research Report" and "Research Analyst," the proposed uniform quiet period following IPOs, the proposed exception from the personal trading restrictions for firms that establish divestiture policies, the proposal to allow web-based disclosure of potential conflicts of interest, and the proposed extension of the anti-retaliatory provisions to include all member firm personnel.

In addition, we support specific aspects of the Rule Filings where the SROs have submitted differing proposals. For example, we generally support NASD's proposed amendments to ease the restrictions on personal transactions in investment funds. We also support NASD's proposal to eliminate the quiet period relating to lock-up agreements and NYSE's proposal to include earnings announcements in the exception from quiet periods for significant news or events.

However, we also have comments on a number of aspects of the Rule Filings, including some of those aspects that we generally support. Our specific comments are set forth below.

1. Proposed Amendments to Definition of Research Report

Under the SRO Rules, the term "Research Report" is currently defined, subject to specific exclusions, to mean "any 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." This definition reflects the intention of the SRO Rules to address the specific conflict between a member firm's need to issue accurate reports of the performance and business

operations of individual companies and industries and the firm's desire to solicit investment banking business from the same companies.[4] We believe this definition, which also has been adopted by Congress[5] and the Commission,[6] properly focuses the requirements of the SRO Rules on a particular set of communications: analyses of traditional operating companies or specific industries.

The SROs have proposed to amend their respective definitions of the term "Research Report" to exclude sales material regarding: (a) open-end registered investment companies that are not listed or traded on an exchange; and (b) public direct participation programs ("DPPs"). In addition, the SROs specifically requested comment as to whether exchange traded funds ("ETFs") also should be excluded from the Research Report definition. We support the proposed exclusions in principle, with the additional recommendation that ETFs also be excluded. In this regard, we agree with NASD and NYSE that applying the SRO Rules to Research Reports regarding investment companies, including ETFs is not necessary given the separate regulatory regime that applies to those materials.[7]

In addition, however, we believe that the current definition of Research Report does not include sales materials regarding investment companies or other investment

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4 As the SROs pointed out in the Joint Report, "The 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." Joint Report at 2.

5 *See* Section 15D(a)(2) of the Securities Exchange Act of 1934 ("Exchange Act").

6 *See* Rule 500 of Regulation AC under the Exchange Act.

7 *See* Notice of Proposed Rule Change, 72 FR at 2068-69, 2074; Joint Report at 30-31; *see also* Securities Act Rule 482 and NASD Rule 2210 (providing, among other things, that all advertisements and sales literature regarding registered investment companies must be filed with NASD within ten (10) business days of first use).

products. As noted above, the Research Report definition is limited to "analyses of equity securities of *individual companies or industries*" (emphasis added).[8] While investment companies and DPPs may be equity securities, we believe they generally have not been understood to be considered "individual companies or industries" for purposes of the SRO Rules. In any event, we believe that the definition of Research Report should reflect the true intent of the SRO Rules, and should clearly exclude all entities that are not traditional operating companies, such as investment companies (including ETFs) and DPPs.

2. Proposed Amendments to Prohibit Pre-Publication Review of Research Reports by All Non-Research Personnel

The SRO Rules currently provide that investment banking and other "non-research" personnel generally may not review or approve a Research Report before publication. However, non-research personnel are permitted to review a Research Report before publication to verify the factual accuracy of the report or to identify any potential conflict of interest, as long as legal or compliance personnel are included in the communications involved in such a review. These restrictions are intended to prevent Research Reports from being reviewed for the purpose of influencing their content.[9]

Under the proposals, the SRO Rules would be amended to prohibit pre-publication review of a Research Report by *any* non-research personnel, except for legal

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[8] For example, we note that the term "Research Report" as originally proposed included written communications presenting "an opinion or recommendation concerning an equity security." *See* Securities Exchange Act Release No. 45526 (March 8, 2002), 67 FR 11526 (March 14, 2002). In response to commenters' concerns that the definition was too broad, the SROs narrowed the definition so that it applied only with respect to equity securities of individual companies and industries rather than to all equity securities. *See* Securities Exchange Act Release No. 45908 (May 10, 2002), 67 FR 34968 (May 16, 2002).

[9] *See* Securities Exchange Act Release No. 45526 (March 8, 2002), 67 FR 11526, 11533 (March 14, 2002).

and compliance personnel. We support a prohibition on pre-publication review by investment banking personnel. However we do not support a prohibition on pre-publication review by other non-research personnel because such a prohibition would prevent the review of Research Reports reviewed by technical experts within the firm (*e.g.*, tax and accounting personnel), who provide valuable input and insight . These types of reviews improve the quality and accuracy of Research Reports and are not intended to influence the content of the Reports. In addition, the proposed amendments to the SRO Rules could be read literally to prohibit member firms from providing completed, but unpublished, Research Reports to personnel who are responsible for preparation for formatting and publication, such as corporate communications or media publishing personnel.

In addition, this aspect of the proposals would be inconsistent with the terms of the Global Research Analyst Settlement.[10] Under the terms of the Global Settlement, the settling firms are directed to establish an oversight/monitoring committee or committees, which, among other things, is responsible for monitoring the overall quality and accuracy of the firm's research reports. The terms of the Global Settlement provide that the oversight/monitoring committee is to be comprised of representatives of research management and may include non-research personnel other than investment banking personnel. Moreover, the Global Settlement requires that the oversight/monitoring committee review, beforehand where practicable, all changes in ratings and material changes in price targets contained in the firm's Research Reports. Accordingly, the

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[10] *See* Commission Litigation Release No. 18438 (October 31, 2003).

Global Settlement expressly contemplates pre-publication review of Research Reports by non-research personnel.

The SROs have rules in place to address other concerns that might arise from pre-publication review of Research Reports by non-research personnel. For example, the SRO Rules require any such reviews to be conducted through legal or compliance personnel and NASD Rules prohibit member firms from purposefully establishing, increasing, decreasing, or liquidating positions in anticipation of the issuance of a Research Report.[11] Accordingly, we urge the SROs to develop a standard for pre-publication review of Research Reports that addresses the fact that review by member firms' non-research personnel provides useful assistance in the preparation of Research Reports without influencing the content of the Reports.

3. Proposed Amendments to Quiet Periods

The SRO Rules currently include restrictions on a member firm's ability to issue Research Reports ("Quiet Periods") when the firm is participating in an offering of securities. In addition, the SRO Rules include a Quiet Period that begins 15 days before and ends 15 days after the expiration or waiver of a "lock-up" agreement to which the member firm is a party.

The SRO Rules also include an exception that allows member firms to issue Research Reports during a Quiet Period concerning "significant news or events" as long as legal or compliance personnel approve the Research Report. In previous interpretive guidance, the SROs have stated that they generally "would not regard an announcement about earnings to fall within the exception because an earnings announcement itself

[11] *See* NASD IM-2110-4.

generally is not a causal event or news item that materially affects a company's operations, earnings or financial condition."[12]

The Rule Filings propose several changes to the Quiet Periods. We support the SROs' harmonized proposal to establish a uniform 25-day Quiet Period following IPOs and to eliminate the Quiet Period following secondary offerings. However, as described below, we have specific comments on the proposals regarding the Quiet Period relating to lock-up agreements and the exception from the Quiet Periods for significant news or events. In particular, we note the SROs have submitted differing proposals in these particular areas. We believe the proposals would result in inconsistent requirements, and we urge the SROs to harmonize these aspects of the proposals.

(a) ***Quiet Period Relating to Lock-Up Agreements***

NASD's proposal would eliminate the formal Quiet Period relating to the expiration or waiver of lock-up agreements, but would require member firms to certify in any Research Report issued within 15 days before and after a lock-up expiration or waiver that there is a "bona fide" reason for issuing the report. NYSE's proposal would retain the Quiet Period, but would decrease it from 15 days to 5 days before and after the expiration or waiver of a lock-up agreement.

As NASD noted in the Joint Report, the quiet periods surrounding lock-up releases are intended to prevent member firms from issuing optimistic "booster shot" reports that are intended to try to raise the stock price of a company just before previously locked-up shares become freely saleable into the market by a company or its major

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[12] 2004 Joint Guidance, Notice to Members 04-18 at 235.

shareholders.[13] We agree with NASD's conclusion that the changes to internal structure of investment banks and the other safeguards imposed by the current SRO Rules appear to have addressed concerns regarding Research Reports issued near the expiration of lock-up agreements and therefore obviate the need for a quiet period that inhibits the flow of information to the marketplace.[14] In addition, we share NASD's view that elimination of the quiet periods around the expiration of lock-up agreements will permit information to flow to investors without sacrificing the overall objectivity of the research.[15] Accordingly, we support NASD's proposal to eliminate the Quiet Period relating to lock-up agreements.

However, we do not support NASD's proposed certification requirement. In our view, the factors cited by NASD in support of its proposal to eliminate the Quiet Period are sufficient to address the concerns relating to the issuance of overly optimistic Research Reports around the expiration or waiver of a lock-up agreement. We also concur with NASD's view, expressed in the Joint Report, that knowingly inaccurate Research Reports are prohibited under any circumstances, regardless of whether they are issued around the expiration of a lock-up agreement.[16]

For example, the SRO Rules require a reasonable basis for any recommendation or price target and the valuation method used to determine a price target.[17] In addition, Regulation AC under the Exchange Act requires the analyst to certify in the Research

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13 Joint Report at 34.

14 Notice of Proposed Rule Change, 72 FR at 2075; *see also* Joint Report at 35.

15 *Id.*

16 Joint Report at 35.

17 NASD Rule 2711(h)(7), IM-2210-1(6); NYSE Rule 472(j)(1) and 472(k)(i)(e).

Report that any such recommendation or price target be genuinely held.[18] Moreover, the anti-fraud and anti-manipulation provisions under the federal securities laws would prohibit a member firm from issuing a Research Report with the intent of manipulating the price of the security discussed in the Report.[19]

Adding another certification to the existing certifications and disclosures already required to be included in Research Reports would create an unnecessary administrative burden for member firms without providing any appreciable benefit to investors. For these reasons, we urge NASD to eliminate the Quiet Period relating to lock-up agreements without imposing a certification requirement, and we urge NYSE to make corresponding amendments to its Quiet Period requirements.

(b) ***Exception for Significant News or Events***

NYSE has proposed to amend Rule 472 to expressly include earnings announcements in the exception from the Quiet Periods for significant news or events. NASD has declined to make a similar proposal, and its proposal would retain the significant news or events exception only for the uniform Quiet Period following an IPO. As a practical matter, this exception only will be relevant if the SROs maintain a Quiet Period relating to lock-up agreements,[20] which, as noted above, we support eliminating. Nevertheless, if the SROs determine to maintain a Quiet Period relating to lock-up

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18 *See* Rule 501 of Regulation AC under the Exchange Act.

19 *See* Section 10(b) of the Exchange Act and Rule 10b-5 thereunder (prohibiting acts, transactions, practices or courses of business that operate as a fraud or deceit in connection with the purchase or sale of securities, including misrepresentations and omissions of material fact and prohibiting the use of any manipulative or deceptive device; *see also* Section 17(a) of the Securities Act.

20 During the 25-day period following an IPO, member firms generally are prohibited under the federal securities laws from distributing Research Reports on the issuer, unless the Research Report is preceded or accompanied by a statutory prospectus.

agreements, we believe earnings reports should be included in the exception for significant news or events.

We agree with NYSE that including earnings reports in the exception for significant news or events "will promote the flow of potentially important or noteworthy information to the market and investors in a timely manner."[21] In addition, we agree with NYSE's view that the announcement of a change to earnings estimates or a release of earnings that vary from street expectations will, in many instances, be accompanied by an announcement of some type of causal events.[22] We also concur with NYSE's view that earnings announcements and guidance are necessary pipelines of information for research analysts to support the basis of their investment recommendations.[23]

In the 2004 Joint Guidance, the SROs stated that "the significant news or event exception is intended to allow for coverage in research reports and public appearances of news or events that have a material impact on, or cause a material change to, a company's operations, earnings or financial condition, and that generally would trigger the filing requirements of SEC Form 8-K."[24] In the Joint Report, NYSE reiterated this view, and noted that Item 2.02 of Form 8-K requires a filing of Form 8-K if a company makes "any public announcement or release (including any update of an earlier announcement or release) disclosing material non-public information regarding its results of operations or

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21 Notice of Proposed Rule Change, 72 FR at 2070; *see also* Joint Report at 36.

22 *Id.*

23 *Id.*

24 2004 Joint Guidance, Notice to Members 04-18 at 234-35.

financial condition."[25] Based on this requirement, NYSE recommended including an announcement of earnings as an exception to the Quiet Periods.[26]

We agree with NYSE's analysis, and believe the significant news or events exception should be should be consistent with SEC requirements in order to maintain a flow of potentially sensitive information to the market and investors in a timely manner. We also note that the SROs' joint interpretive guidance limits the content of Research Reports issued pursuant to the exception to discussing the effects of the news or event that triggered the exception.[27] In addition, the SRO Rules currently require that legal or compliance personnel authorize publication of Research Report before it is issued pursuant to the exception for significant news or events. In our view, investors and market participants rely on member firms to analyze earnings reports and their potential effects at or near the time the earnings reports are made. For these reasons, we support NYSE's proposal to amend the significant news or events exception to include earnings reports, and we urge NASD to make corresponding amendments to its exception for significant news or events.

4. Proposed Amendments to Personal Trading Restrictions

The SRO Rules include a number of restrictions on personal trading by research analysts and members of their households. In addition, the SRO Rules provide an exception to the personal trading restrictions for transactions in investment funds. Specifically, the personal trading restrictions do not apply to transactions in:

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25 Joint Report at 36.

26 *Id.*

27 2004 Joint Guidance, Notice to Members 04-18 at 235.

- Any registered diversified investment company as defined under Section (5)(b)(1) of the Investment Company Act of 1940; or

- Any other investment fund over which neither the research analyst nor a member of the research analyst's household has any investment discretion or control, provided that:

  (i) The research analyst and household members collectively own interests representing no more than 1% of the assets of the fund;

  (ii) The fund invests no more than 20% of its assets in securities of issuers principally engaged in the same types of business as companies that the research analyst follows; and

  (iii) If the investment fund distributes securities in kind to the research analyst or household member before the issuer's initial public offering, the research analyst or household member must either divest those securities immediately or the research analyst must refrain from participating in the preparation of research reports concerning that issuer.[28]

The Rule Filings include proposed amendments to two aspects of the personal trading restrictions, and, as described below, we have specific comments on the proposals. We also note that the SROs have submitted differing proposals in this area, and we urge the SROs to harmonize these proposals.

(a) ***Proposed Divestiture Exception***

Both SROs have proposed to create an exception from the personal trading restrictions for member firms that voluntarily choose to prohibit analysts from owning shares of the companies they cover. Under the Rule Filings, the SRO Rules would be amended to provide an exception from the personal trading restrictions provided that, among other things:

(i) The member firm has adopted an internal policy that prohibits research analysts from owning any securities issued by the

[28] NASD Rule 2711(g)(5); NYSE Rule 472(e)(4)(v).

company for which the research analyst provides coverage and requires analysts to completely divest themselves of their existing holdings in such securities;

(ii) The research analyst abides by a reasonable plan of liquidation under which all securities issued by subject companies that the analyst follows are to be sold within 120 days of the effective date of the member firm's policy;

(iii) The research analyst files the liquidation plan with the member firm's legal or compliance department within fifteen days of the effective date of the member organization's policy and the analyst receives written approval of the liquidation plan from the legal or compliance department prior to the sale of any securities under the plan; and

We generally support the proposed divestiture exception. In addition, however, we respectfully request that the SROs consider applying the proposed standard under the divestiture exception to the current personal trading exceptions that allow sales of securities after an analyst joins a member firm or begins research coverage of a subject company.[29] Specifically, we request that the SROs extend the time period for sales after the beginning of an analyst's employment with a firm or coverage of a security from 30 days to 120 days.

(b) ***Proposed Amendments to Investment Fund Exception***

NASD has proposed to amend the investment fund exception to its personal trading restrictions to apply to any investment fund, provided that: (i) neither the analyst nor a member of the analyst's household is made aware of the fund's holdings or transactions other than through periodic shareholder reports and sales material based on such reports; and (ii) the analyst and household members collectively own no more than 1% of the assets of the fund. NYSE has not proposed amendments to the investment

[29] *See* NASD Rule 2711(g)(2)(A); NYSE Rule 472(e)(4)(iii).

fund exception from its personal trading restrictions. As such, NYSE would retain both the 1% ownership requirement and the requirement that no more than 20% of a fund's assets be invested in securities of issuers engaged in the same types of business covered by the analyst. In addition, NYSE has not proposed to add the requirement that the analyst may not be made aware of the fund's holdings other then through periodic reports and sales material.

We agree with the view expressed by both SROs in the Joint Report, and by NASD in its Rule Filing, that amending the investment fund exception "would simplify the ability of analysts to invest in mutual funds, variable insurance products and hedge funds that do not disclose their holdings other than through periodic reports or sales material based on such reports." In its Rule Filing, however, NYSE insists that maintaining the 20% asset diversification threshold "has the potential for limiting conflicts of interest in the issuance of research reports by analysts with a vested interest in a fund."

As a general matter, we question the need for any restrictions on investments in a registered investment company by an analyst or the analyst's household members. In our view, it is virtually impossible as a practical matter for any particular research report to materially affect the price of shares in a registered investment company. Nevertheless, if the SROs determine that a restriction is necessary, we support NASD's proposal to eliminate the asset diversification test and retain the ownership limitations. In our view, a 1% ownership limit would more than satisfy any conflict of interest concerns by significantly limiting the possible gain an analyst might be able to achieve through the

issuance of a Research Report. We also urge NYSE make corresponding amendments to its personal trading restrictions.

In addition, we question the need for NASD's proposed "awareness" test on an analyst's knowledge of a fund's holdings or transactions. NASD states in its Rule Filing, as both SROs stated in the Joint Report, that, "absent discretion or control of an account or the contemporaneous knowledge of the account's transactions, a minimal investment by a research analyst will not influence the analyst to compromise research objectivity to benefit the account." We recognize NASD's concern about maintaining analyst objectivity, but, as we noted above in connection with lock-up agreements, there are rules in place already to prohibit a research analyst from issuing a Research Report that is intended to increase the value of his or her personal holdings.[30] Accordingly, we believe that NASD's prohibition on an analyst's knowledge of a fund's holdings or transactions is not necessary.

5. Proposed Amendments to Permit Web-Based Disclosure of Conflicts of Interest

Currently, the SRO Rules require member firms to include numerous specific disclosures regarding potential conflicts of interest in every Research Report.[31] Under the Rule Filings, the SRO Rules would be amended to permit, in lieu of publication in the Research Report itself, the disclosure of conflicts of interest by including a notice on the cover of a research report that such conflicts of interest exist, together with information on how the reader may obtain more detail about these conflicts on the member's website.

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30 *See* Notes 17, 18, and 19, *supra*, and accompanying text.

31 *See* NASD Rule 2711(h); NYSE Rule 472(k).

We generally support this aspect of the proposals, and agree with the SROs statements that the volume of disclosures currently required under the SRO Rules, and by other requirements and other jurisdictions, may obscure the message that the disclosures are intended to convey.[32] In addition, we support applying a similar approach to disclosures in public appearances and we believe that investors may have increased access to disclosures regarding public appearances if web-based disclosure is permitted. For example, we believe media outlets would be more likely to post a website address for disclosures than displaying or announcing the disclosures in full.

However, we have specific comments regarding the SROs' proposed notification language. In its guidance regarding the clarity and prominence of disclosures that are included in Research Reports, the SROs have stated that member firms may include a general reference to disclosures on the front page of a Research Report as long as the reference is separated from, and in larger font size than, the Report's body text the body text, and the reference directs readers to the specific page in the report where the disclosures are located.[33] Similarly, the SRO Rules currently provide that when a member firm distributes a Research Report covering six or more subject companies (a "Compendium Report"), the Compendium Report may simply direct the reader in a clear manner as to where they may obtain applicable current disclosures, which may be a website, a toll-free number to call, or a postal address to write for the required disclosures.[34] In our view, this type of approach should apply with respect to web-based

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32 Notice of Proposed Rule Change, 72 FR at 2071; *see also* Joint Report at 39.

33 2002 Joint Guidance, Notice to Members 02-39 at 239.

34 NASD Rule 2711(h)(11); NYSE Rule 472(k)(1)(iii).

disclosures, and we believe that clearly directing readers to a specific website is consistent with directing them to a particular page in a Research Report, or to a toll-free number or a postal address.[35]

Instead of this more general approach, the SROs have proposed notification language that, in our view, would convey the impression that the member firm's objectivity is inherently compromised. Specifically, member firms using web-based disclosure would be required to state in the Research Report that the member firm and/or the research analyst preparing this report "*has* a conflict of interest that may affect the ability of the firm or the analyst to provide objective analysis about the company" (emphasis added). In our view, it is not necessary, or accurate, to state that a member firm has a conflict of interest just because that firm makes the disclosures required under the SRO rules. The intention of the disclosures is to inform investors of information that creates the *potential* for a conflict of interest, and the SROs' proposed warning language contradicts this intention. If the SROs adopt the proposed warning language, we believe many member firms may be discouraged from using the web-based disclosure.

For these reasons, we believe that the SROs' proposal to require warning language in connection with web-based disclosure is unnecessary. Nevertheless, if the SROs determine that a specific warning is necessary, we urge the SROs to modify the required language to avoid creating an automatically negative presumption about the member firm's objectivity, and we suggest the following as an alternative:

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[35] We note, however, that NASD has proposed to amend Rule 2711(h)(11) so that NASD member firms would be required to include the disclosures regarding potential conflicts of interest in Compendium Reports. NASD has not indicated the specific reasons for this aspect of its proposal, and we believe the amendment is not necessary. In addition, we note that NYSE has not proposed a similar change to Rule 472(k)(1)(iii).

> Important disclosures about [Member Firm's] relationships with the companies discussed in this Report appear at [www.memberwebsite.com].

6. Proposed Amendments Regarding Communications with Internal Sales Personnel.

Under the SRO Rules, research analysts are prohibited from engaging in communications about an investment banking transaction with a current or prospective customer if the analyst is in the presence of either investment banking department personnel or company management.[36] The SROs have proposed to extend this prohibition to apply to analysts' communications with internal sales personnel of the member firm in addition to communications with current and prospective customers.

NYSE states that the proposed amendment "is intended to further mitigate potential conflicts of interest in intra-office communications."[37] NASD states that the proposed amendment "would make the provision consistent with respect to a research analyst's ability to educate investors and sales personnel about an investment banking services transaction."[38] However, the proposed amendment does not take into account a substantially similar provision under the Global Settlement that carves out equity capital markets personnel from investment banking personnel. Specifically, the Global Settlement provides that research personnel may not appear jointly with investment banking personnel *other than members of the equity capital markets group* in communications regarding investment banking services transactions with the firm's internal sales personnel. We urge the SROs to amend this aspect of the proposals to

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36 NASD Rule 2711(c)(5)(B); NYSE Rule 472(b)(6)(i)(b).

37 Notice of Proposed Rule Change, 72 FR at 2072.

38 *Id.* at 2077.

exclude equity capital markets personnel so that the SRO Rules will be consistent with the terms of the Global Settlement.

7. Additional Issues

As noted above, we support the continuing review and assessment of the SRO Rules. We are hopeful that, as this review continues, the SROs will consider other recommendations from the Joint Report as well as additional issues, including, but not limited to:

- Eliminating the Series 7 prerequisite for the Series 86/87 Research Analyst Qualification Examination by importing relevant topics from the Series 7 into the Series 86/87;
- Revisiting the application of the SRO Rules to quantitative research to address certain ambiguities; and
- Expanding the personal trading exceptions to include diversified separately independently managed accounts where investment management is fully delegated to an independent investment advisor.

Conclusion

SIFMA reiterates its support for the overall goals of the Rule Filings but we respectfully urge the Commission and the SROs to carefully consider our specific comments and suggestions. In particular, we urge the SROs to amend those aspects of the Rule Filings that are not yet harmonized so that any amendments to their respective rules are consistent. SIFMA would be happy to discuss any of its comments on the Rule Filings with the Commission or the SROs in greater detail. If you have any questions, please contact John V. Ayanian (202.739.5946) or Theodore R. Lazo (202.739.5250) of Morgan, Lewis & Bockius LLP, or me at 212.618.0509.

Sincerely

Michael D. Udoff
Vice President and Associate General Counsel

cc: The Honorable Christopher Cox, Chairman
The Honorable Paul S. Atkins, Commissioner
The Honorable Roel C. Campos, Commissioner
The Honorable Annette L. Nazareth, Commissioner
The Honorable Kathleen L. Casey, Commissioner

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