

FINRA Files Amended Communications Rules

Impact on Broker-Dealers

The Securities and Exchange Commission recently published for comment FINRA's proposal to revise its rules governing member firm communications with customers and the public.¹ The SEC has requested comments on the proposed rules by August 24, 2011.

The proposed rules will not become effective until approved by the SEC. Once approved, FINRA will announce the implementation date of the proposed rule change, which will be no later than 365 days following the SEC's approval. We will monitor the SEC's and FINRA's actions and issue a memorandum once the final rules have been adopted.

A separate Davis Polk Client Memorandum, [available here](#), analyzes how the proposed changes will likely affect the offer and sale of structured products.

Key Issues

The proposed rules would, among other changes:

- **Communication Categories:** reorganize the six categories of communications in the existing rules (advertisement, sales literature, institutional sales material, correspondence, public appearance and independently prepared reprint) into three groups (institutional communication, retail communication and correspondence) and assign different levels of principal approval, filing and content standards based on which group the communication falls into;
- **Internal Written Communication:** treat a member's internal written communication (including an electronic communication) that is intended to educate or train registered persons about the products or services offered by the member as "institutional communication" that is subject to proposed FINRA Rule 2210 and NASD Rule 3010(d)(governing the supervision, review and retention of correspondence);
- **Approval by Registered Principal:** require that an "appropriately qualified" registered principal of the member (determined based on the permissible activities under the principal registration rules) approve *all* retail communication prior to use,² subject to certain limited exceptions;³

¹ Exchange Act Release No. 64984, 76 FR 46870 (August 3, 2011). The proposal would incorporate NASD Rules 2210 and 2211 and related NASD Interpretive Materials, as well as portions of Incorporated NYSE Rule 472, as FINRA Rules 2210 and 2212 to 2216.

FINRA first proposed to amend these rules in September 2009. FINRA Regulatory Notice 09-55 is available [here](#). For a summary of the 2009 proposal, see Davis Polk's Client Memorandum: [FINRA Proposes Amendments to Communication Rules, Including New Pre-Filing Requirements for Structured Product Communications](#).

² In light of FINRA Regulatory Notice 10-52, certain broadly disseminated free-writing prospectuses would be subject to the principal review requirement.

³ Exceptions include retail communications: (i) that do not make any financial or investment recommendation or otherwise promote a product or service of the member; (ii) that are posted on online interactive electronic forums; and (iii) that are excepted from the definition of "research report" pursuant to NASD Rule 2711(a)(9)(A), such as communications that are limited to discussions of (cont.)

- **Recordkeeping:** add an explicit requirement that firms keep records of retail and institutional communications in the form and for the time periods prescribed by Rule 17a-4 under the Securities Exchange Act of 1934 and specify information that records of retail and institutional communications must include;
- **Pre-Filing Requirement:** require that *all retail communications* concerning security futures, bond mutual funds that include or incorporate bond mutual fund volatility ratings and registered investment companies that include self-created performance rankings or performance comparisons, be filed with FINRA at least 10 business days prior to first use or publication, subject to limited exceptions;
- **10 Day Post-Use Filing Requirement:** require that *all retail communications* relating to the following be filed within 10 business days of first use or publication:
 - registered structured products⁴ and collateralized mortgage obligations (this is a change from the 2009 proposal, which required that these communications be pre-filed with FINRA);
 - registered investment companies, if the communication does not contain self-created performance rankings or comparisons, public direct participation programs and government securities; and
 - templates for written reports produced by, or retail communications concerning, an investment analysis tool;
- **Filing Exclusions:** generally maintain existing exclusions from the filing requirements, with some changes, such as requiring the filing (either pre-use or post-use, depending on the subject-matter) of any free-writing prospectuses distributed by a broker-dealer in a manner reasonably designed to lead to broad unrestricted dissemination, including posting on a generally-available website;⁵
- **Filing Exclusion for Templates:** add a filing exclusion for retail communications that are based on templates that were previously filed and are being updated only with more recent statistics or non-narrative information; and
- **Content Standards:** reorganize, but generally continue the substance of, the existing content standards applicable to communications, while codifying certain existing interpretations, and require various disclosures in communications that include projections, tax considerations, testimonials or recommendations.

(cont.)

broad-based indices, commentaries on economic, political or market conditions and statistical summaries of multiple companies' financial data.

⁴ "Registered structured products" are securities that are registered under the Securities Act of 1933 and are "derived from or based on a single security, a basket of securities, an index, a commodity, a debt issuance or a foreign currency."

⁵ This requirement codifies FINRA Regulatory Notice 10-52, which withdrew in part a FINRA interpretive letter published in 2006 stating that issuer-created materials and all free-writing prospectuses, whether created by an issuer or by another offering participant, are excluded from the provisions of NASD Rules 2210 and 2011.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

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