

On November 6, 2002, NASD Regulation filed Amendment No. 3 to the proposed rule change.⁶ On March 6, 2003, NASD Regulation filed Amendment No. 4 to the proposed rule change.⁷ This notice and order approves the proposed rule change, as amended, and solicits comments from interested persons on Amendment Nos. 3 and 4.

II. Description of Proposed Rule Change

A. Summary

The NASD submitted the proposed rule change to modernize and clarify the rules governing member communications with the public. Among other things, the proposed rule change would exclude all communications to institutional investors from member pre-use approval and NASD filing requirements and from many of the content standards. Form letters and group e-mail to existing retail customers and fewer than 25 prospective retail customers also would be eligible for these exclusions, provided that a member developed appropriate policies and procedures to supervise and review such communications. In addition, the proposed rule change would exclude independently prepared reprints, and excerpts there from, from the filing and many of the content standards, and would exclude certain press releases from the filing requirements. The proposed rule change generally would simplify the content standards applicable to member communications.⁸

Pickering, to Jonathan G. Katz, Secretary, Commission, dated February 25, 2002 ("Wilmer-Becker Letter"); Forrest Fost, Associate Legal Counsel and Danielle Nicholson Smith, Senior Legal Analyst, T. Rowe Price Associates, Inc., to Jonathan G. Katz, Secretary, Commission, dated February 14, 2002 ("T. Rowe Letter"); Yoon-Young Lee, Wilmer, Cutler & Pickering, to Jonathan G. Katz, Secretary, Commission, dated February 13, 2002 ("Wilmer-Lee Letter"); Alexander C. Gavis, Associate General Counsel, Fidelity Investments, to Jonathan G. Katz, Secretary, Commission, dated February 15, 2002 ("Fidelity Letter"); Sullivan & Cromwell, to Jonathan G. Katz, Secretary, Commission, dated February 22, 2002 ("Sullivan Letter").

⁶ See letter from Barbara Z. Sweeney, Senior Vice President and Corporate Secretary, NASD, to Katherine A. England, Assistant Director, Division, Commission, dated November 4, 2002 ("Amendment No. 3").

⁷ See letter from Philip Shaikun, Assistant General Counsel, NASD, to Katherine A. England, Assistant Director, Division, Commission, dated March 6, 2003 ("Amendment No. 4").

⁸ NASD member broker/dealers that are dually registered as investment advisers will remain subject to the advertising standards of the Investment Advisers Act of 1940 and Commission rules thereunder, to the extent that their sales material promotes advisory products or services.

B. Description of Proposed Rule Change

1. Reorganization of Rule 2210

The proposed rule change would create new NASD Rule 2211, which would apply to institutional sales material and correspondence. The proposed rule change also would provide cross-references between NASD Rule 2210 and NASD Rule 2211 in appropriate places. Existing NASD Rule 2211, concerning telemarketing, would be renumbered as NASD Rule 2212.

2. Definition of "Public Appearance"

Existing NASD Rule 2210(d)(1)(C) provides that NASD members who engage in public appearances or speaking activities must follow the content standards of NASD Rules 2210(d) and (f). Consequently, public appearances already are subject to strict content requirements. The proposed rule change would clarify the application of NASD Rule 2210 to public appearances by defining "public appearance" as a type of communication with the public. Public appearances would include participation in a seminar, forum (including an interactive electronic forum), radio or television interview, or other public appearance or public speaking activity.

3. Institutional Sales Material

The proposed rule change would eliminate the pre-use approval and filing requirements applicable to communications that are distributed or made available only to institutional investors contained in NASD Rule 2210. Institutional sales material would be subject to new supervision and review requirements that are modeled on those in NASD Rule 3010, which apply to correspondence. Moreover, institutional sales material would continue to be subject to the record-keeping requirements and some, but not all, of the content standards in NASD Rule 2210.⁹

Under the proposed rule change, no member could treat a communication as having been distributed to an institutional investor if the member had reason to believe that the communication or any excerpt thereof would be forwarded or made available to any person other than an institutional

investor. For example, if a member had reason to believe that such a communication would be forwarded or made available to 401(k) plan participants or other beneficiaries of institutional accounts, it would be treated as retail sales material. NASD Regulation believes that plan participants and other beneficiaries of institutional accounts should receive the same protections under the advertising rules as other retail investors. Similarly, an advertisement in a publication designed for broker/dealers or other institutional investors may not be treated as institutional sales material if the member has reason to believe that the publication will be made available to any person other than an institutional investor.

The proposed rule change amended the definition of "institutional investor," first, to include governmental entities and their subdivisions. Second, the definition was amended to include employee benefit plans that meet the requirements of section 403(b) or section 457 of the Internal Revenue Code and have at least 100 participants.¹⁰ Third, the definition was amended to apply to qualified plans with at least 100 participants.¹¹ Fourth, the proposed rule change would define "institutional investor" to include any person acting solely on behalf of any institutional investor. Fifth, NASD Regulation clarified that the term "institutional investor" includes only associated persons who are registered with an NASD member.¹² Sixth, the definition would clarify that no member may treat a communication as having been distributed to an institutional investor if the member has reason to believe that the communication or any excerpt thereof will be forwarded or made available to any person other than an institutional investor. Thus, for example, if a member has reason to believe the employer sponsor of a retirement plan will make sales material available for inspection by the plan participants, then the member may not treat the sales material as having been distributed only to an institutional investor.

¹⁰ This category of institutional investor does not include participants of such plans.

¹¹ Again, this category of institutional investor does not include participants of such plans.

¹² The "broker/dealer-only" exception, which would become a part of the institutional investor definition, recognizes the special expertise that NASD members have with respect to brokerage products and services. While registered persons should have this expertise, as demonstrated by their completion of the qualifications process, there can be no assurance that other associated persons would.

⁹ The proposed rule change would revise the content standards to specifically indicate which type of communication is subject to each standard. Therefore, standards that apply only to "advertisements" or "sales literature" would not apply to institutional sales material. For example, the ranking guidelines in proposed IM-2210-3 would apply only to advertisements and sales literature and therefore would not apply to institutional sales material.