

retaliating, or threatening to retaliate, against a research analyst who publishes an adverse, negative, or otherwise unfavorable research report that may adversely affect the broker-dealer's present or prospective investment banking relationship.²⁰² The SOA specifies that the rules may not limit the authority of a broker-dealer to discipline an analyst for causes other than such research report in accordance with the policies and procedures of the firm. The SROs have extended the anti-retaliation provisions to cover public appearances and have clarified that the rule would not preclude termination of a research analyst for causes unrelated to issuing or distributing adverse research or for making an unfavorable public appearance regarding a current or potential investment-banking relationship.

Commenters did not oppose this provision. The Commission believes that the SRO proposals are designed to protect the objectivity and independence of research analysts, and meet the requirements of Section 15D of the Exchange Act, which requires that a rule be adopted that prohibits broker-dealers engaged in investment banking activities from, directly or indirectly retaliating or threatening to retaliate, against a research analyst who publishes a negative, adverse, or otherwise unfavorable research report that may adversely affect the broker-dealer's present or prospective investment banking relationship with an issuer. The Commission further believes that the SROs' determination to apply the retaliation provision to cover adverse statements made in public appearances is consistent with Sections 6(b)(5), 6(b)(8), 15A(b)(6) and 15A(b)(9).

L. Small Firm Exemption [NYSE Rule 472(m) and NASD Rule 2711(k)]

The SROs have proposed an exemption from certain of the requirements that legal or compliance personnel must act as intermediaries regarding communications for firms that engage in limited underwriting activity.²⁰³ Current NASD Rule 2711(b)(1) and (3) and current NYSE Rule 472(b)(1) and (3), the gatekeeper provisions, prohibit a research analyst from being subject to the supervision or control of any employee of a member's investment banking department, and further require legal or compliance personnel to intermediate certain

communications between the research department and non-research personnel.

As the Commission noted in the May 2002 approval order when the Commission approved these gatekeeper provisions, several commenters argued that they would impose significant costs, especially for smaller firms that would have to hire additional personnel. Commenters said that personnel in smaller firms often perform multiple functions, and therefore the separation rules impose a greater burden on these firms. These comments raised the prospect that the rules might force some firms to curtail their research, potentially reducing research coverage for smaller companies and companies of regional or local interest.

To temporarily address those concerns while the SROs considered whether an exemption was appropriate, the effectiveness of the gatekeeper provisions was delayed until July 30, 2003, or until a superseding permanent exemption is approved and becomes effective, for those members that over the previous three years, on average per year, have participated in 10 or fewer investment banking transactions or underwritings as manager or co-manager and generated \$5 million or less in gross investment banking services revenues from those transactions ("small firms").²⁰⁴ The rules approved today create a permanent exemption from the gatekeeper provisions for small firms, and supersede the temporary exemption filed by the SROs in May 2003.²⁰⁵

However, the permanent exemptions for small firms, unlike the temporary exemptions, do not apply to NASD Rule 2711(c) and NYSE Rule 472(b)(4), which restrict communications between the research department and the issuer, because the SROs do not believe that it would be appropriate to provide for a permanent exception from the gatekeeper provisions for the voluntary submission of sections of a draft research report to a subject company for the purpose of checking the factual accuracy of the draft report.²⁰⁶ In addition, for the purposes of the small firm exception computations, the SROs have determined that "investment banking services" shall not include municipal securities transactions.²⁰⁷

²⁰⁴ See Securities Exchange Act Release No. 47876 (May 15, 2003); see also Securities Exchange Act Release No. 46165 (July 3, 2002), 67 FR 46555 (July 15, 2002).

²⁰⁵ See NYSE Rule 472(m) and NASD Rule 2711(k).

²⁰⁶ *Id.*

²⁰⁷ NYSE notes its belief that municipal securities underwritings are not subject to the same potential conflicts of interest as equity securities. See NYSE Amendment No. 3.

The SRO proposals also require members that qualify for this exemption to maintain records for three years of any communication that otherwise would be subject to the review and monitoring provisions of NASD Rule 2711(b)(3) and NYSE Rule 472(b)(1), (2), and (3).

The Commission finds that the exceptions for small firms from certain of the rules addressing the relationships between research, investment banking, and companies that are the subject of research reports, are appropriate to address concerns unique to smaller firms who may share supervisory personnel across different offices or departments. The Commission finds that the proposals are consistent with the Exchange Act, particularly Sections 6(b)(5), 6(b)(8), 15A(b)(6), and 15A(b)(9).

M. Implementation

Commenters requested that the SROs coordinate the effective dates of their proposed changes and ensure that firms have adequate time to implement new rules.²⁰⁸ In response to comments, the SROs decided upon the following implementation schedule for the proposed amendments (all time periods run from the date that the Commission approves the filings) in order to provide reasonable time periods for members and member organizations to develop and implement policies, procedures and systems to comply with the new requirements:

NYSE suggests the following effective dates for the provisions contained in SR-NYSE-2002-49:

Firm and Affiliate Compensation Disclosure Provisions—(NYSE Rules 472(k)(1)(i)d.2. and (k)(1)(iii)a.)—180 days, except upon written request to the Exchange for an extension of up to an additional 90 days thereafter.

Analyst and Firm Compensation Disclosure Provisions—(NYSE Rules 472(k)(1)(ii)a., (k)(1)(iii)a., (k)(2)(i)c.2. and f.)—180 days, except upon written request to the Exchange for an extension of up to an additional 90 days thereafter.

Client Disclosure Provisions—(NYSE Rules 472(k)(1)(i)d.1, (k)(1)(ii)b.1. and (K)(2)(1)c.1)—180 days, except upon written request to the Exchange for an extension of up to an additional 90 days thereafter.

Exceptions to Disclosures Required In Rule 472(k)(1) and (2)—(NYSE Rule 472(k)(3)(1)):

As applied to disclosures under Rule 472(k)(1)(i)a., 2., and 3.; effective immediately.²⁰⁹

²⁰⁸ See SIA March 10th letter.

²⁰⁹ NYSE notes the disclosures required pursuant to Rule 472(k)(1) and (2), approved as part of the original amendments have been renumbered as part of Amendment No. 3 and remain in effect. See NYSE Amendment No. 3.

²⁰² See 15 U.S.C. 78o-6(1)(C).

²⁰³ See NYSE Rule 472(b) and NASD Rule 2711(b).