

is warranted because Regulation AC imposes core standards of integrity that should pertain to all research distributed by broker-dealers and covered persons. On the other hand, we note that Regulation AC is narrower than the SRO rules and the SOA in that its certification requirements apply only to the research analyst or analysts primarily responsible for the content of a research report; junior analysts are not required to certify.¹⁸ This distinction is reasonable because the core integrity standards promoted by Regulation AC are achieved where the analysts primarily responsible for the views expressed in the research report are required to certify. In comparison, the coverage of junior analysts by the SRO rules is appropriate because the concerns those provisions seek to address (for example, trading ahead of research reports) exist with respect to all analysts associated with a member firm and those persons who report to analysts.

2. Definition of "Covered Person"

In response to comments, we have added the definition of "covered person" to narrow the scope of persons to which Regulation AC applies. Covered person means persons associated with a broker or dealer,¹⁹ but not including an associated person that has no officers or employees in common with the broker or dealer and where the broker or dealer maintains and enforces written policies and procedures reasonably designed to prevent the broker or dealer or any of its controlling persons, officers, or employees from influencing the activities of research analysts and the content of research reports prepared by the associated person. In adopting Regulation AC, we have sought to focus the rule on research that appears to be most susceptible to pressures that might compromise its integrity, for example pressures to generate investment banking business.

We believe that it is unnecessary to apply Regulation AC to research published, circulated, or provided by associated persons who have a sufficient

level of independence from the broker or dealer with which they are associated. Associated persons who meet the independence criteria in this definition should have a sufficient level of independence so that pressures from the broker-dealer with which they are associated should not compromise their research. In order to avoid the possibility that an associated person might incorrectly believe that the broker-dealer had policies and procedures to prevent influencing the research of the associated person and, therefore, fail to certify when certification was required, we have added a provision to Regulation AC (Rule 504) that requires a broker or dealer to notify its associated persons that it issues research reports as to whether the broker or dealer maintains and enforces such written policies and procedures and whether the associated person has any officers (or persons performing similar functions) or employees in common with the broker or dealer who can influence the activities of research analysts or the content of research reports and, if so, the identity of those persons.²⁰ We also would not expect that such policies and procedures would interfere with other communications between the associated person and the broker-dealer made in the ordinary course of business and not in violation of any other provision of the securities laws.

We have also excluded from the rule investment advisers that are prohibited under section 203A of the Investment Advisers Act of 1940²¹ ("Advisers Act") from registering with the Commission as investment advisers and not otherwise registered or required to be registered as a broker-dealer. Section 203A was added to the Advisers Act by the National Securities Markets Improvement Act of 1996 ("NSMIA"), which amended the Advisers Act to divide responsibility for regulating investment advisers between the Commission and state securities authorities.²² Section 203A of the

Advisers Act effects this division by generally prohibiting investment advisers from registering with us unless they have at least \$25 million of assets under management or advise a registered investment company.²³ Advisers prohibited from registering with us are subject to the regulation of state securities authorities, but also continue to be subject to the federal securities laws, including the anti-fraud provisions of the federal securities laws.

We also make clear that no provision of the regulation shall apply to the publisher of any newspaper, news magazine, or business or financial publication of general and regular circulation that is not registered or required to be registered with the Commission as a broker or dealer or investment adviser. Regulation AC was never intended to govern media coverage of issuers.²⁴

3. Definition of "Research Report"

The Commission requested comment on whether the definition of "research report" should be broader or narrower than proposed. Commenters discussed several aspects of the proposed definition, including whether it should cover debt securities, whether it should include electronic communications, and guidance concerning what will and will not be considered a research report.

a. Application to Debt Securities

We specifically requested comment on whether the proposed definition of "research report" should be limited to cover only equity securities. Five commenters discussed the application of Regulation AC to fixed income and all supported the application to debt to some extent.²⁵

The Commission has determined that applying the requirements of Regulation AC to debt securities as well as equity securities would benefit investors because it would provide to debt investors the same benefits as equity

Advisers Act to make them inapplicable to state-registered advisers because "application of these provisions to state-registered advisers is more appropriately a matter for state law." Investment Advisers Act Release No. 1633 (May 15, 1997), 62 FR 28112 (May 22, 1997).

²³ Pursuant to authority under Advisers Act section 203(a)(1)(A) the Commission adopted Advisers Act Rule 203A-1, which made SEC registration optional for certain investment advisers that have between \$25 and \$30 million of assets under management. See Advisers Act Rule 203A-1(a)(1), 17 CFR 275.203A-1(a)(1).

²⁴ It is possible that a broker or dealer or covered person could provide a research report to a media entity intending that it be published. In that case, the report must be certified by the research analyst.

²⁵ See CSFB, Goldman, NASAA, SSB, and TBMA. We note that the SOA and the SRO rules apply only to equity securities.

¹⁸ The proposed definition of "research analyst" referred to any natural person "principally" responsible for research reports; the adopted definition refers to any natural person "primarily" responsible. This modification clarifies that, whether or not a natural person is considered to be principally responsible for research reports as a job description, any natural person who is primarily responsible for the preparation of the content of any research report is a research analyst for the purposes of Regulation AC unless otherwise exempted.

¹⁹ The term "person associated with a broker or dealer" is defined in Exchange Act section 3(a)(18), 15 U.S.C. 78c(a)(18).

²⁰ Associated persons of a member are required under SRO rules to provide prompt notice to his or her employer of employment with any other persons as a result of a business activity. See NASD Rule 3030.

²¹ 15 U.S.C. 80b-3a.

²² Pub. L. No. 104-290, 110 Stat. 3416 (1996) (codified in scattered sections of the United States Code). Section 203A was designed to allow the Commission to better use its limited resources by concentrating its regulatory responsibilities on advisers with national businesses, and to reduce the burden to investment advisers of the overlapping and duplicative regulation existing prior to the enactment of NSMIA. See S. Rep. No. 293, 104th Cong., 2d Sess. 2-4 (1996). In conjunction with implementing NSMIA, the Commission amended several "prophylactic" anti-fraud rules under the