

F. Application of Regulation AC to Third Party Research

In Proposing Regulation AC, we did not propose to treat research prepared by third parties but distributed by a broker-dealer differently from research produced by the broker-dealer itself. Commenters argued that broker-dealers should not be responsible for certifying research by independent third parties. Moreover, they pointed out practical problems, including the difficulty of tracking analysts employed by third parties.⁴⁵ They also cited increased costs. They argued that firms would discontinue providing the valuable service of making third party research available to customers.⁴⁶

We have determined not to apply Regulation AC where a broker-dealer distributes research prepared by a third party research analyst whose employer satisfies certain independence criteria. The independence criteria require that the third party research analyst's employer does not have officers or employees in common with the broker-dealer or covered person distributing its research, and that the broker-dealer has written policies and procedures designed to prevent the broker-dealer, its controlling persons, officers, and employees from influencing the activities of the third party research analyst and the content of his or her research reports. We believe that research analysts employed by these independent third parties will not be sufficiently susceptible to pressures from distributing broker-dealers to warrant certification. Where a broker-dealer distributes the research of a third party that does not meet the independence criteria, however, the broker-dealer must confirm that the research report includes the same research analyst certification as required by Regulation AC.

Commenters argued that it would be difficult to track analysts employed by third parties, some of whom are overseas, in order to monitor their public appearances and obtain written statements from them. In response to commenters' concerns, we have determined that broker-dealers who distribute third party research are not required to obtain the public appearance certifications required by Rule 502 of Regulation AC with respect to public appearances by third party research analysts.

G. Application of Regulation AC to Foreign Research

In proposing Regulation Analyst Certification, the Commission did not distinguish between research that was issued by a U.S. entity and research that was issued by a non-U.S. entity. Several commenters raised the issue of the Regulation's effect on research originating from a foreign entity. These commenters generally opposed the proposed scope of Regulation AC, which captured foreign entities (and their associated persons) that issue research reports, including those who are not required to be registered with the Commission under section 15 of the Exchange Act.⁴⁷

In light of these comments, we have created a narrow exception for foreign persons that are located outside of the United States and are not associated with a registered broker-dealer that prepares and provides research on foreign securities⁴⁸ to major United States institutions in the U.S. in accordance with the provisions of Rule 15a-6(a)(2). In these instances, the foreign person is excepted from the requirements of Regulation AC.

In addition, in the case of a research analyst employed outside the United States by a foreign person located outside the United States, Rule 502 of Regulation AC only applies to public appearances while the research analyst is physically present in the United States.

H. Supervision and Oversight

Commenters requested that the Commission clarify that the certification pertaining to the analyst's personal views is not intended to prevent research supervisors or review committees from seeking changes to the research product.⁴⁹ One commenter argued that Regulation AC should not impede the ability of a supervisor or a review committee to require that a report follow a written firm policy on when a research report can upgrade or downgrade a rating, or when it must withhold a rating to prevent conflicts or for other reasons.⁵⁰ Commenters argued that certification also should not preclude the ability of an analyst or a firm to modify the report due to a change in the analyst's opinion or to remove statements that create legal or regulatory concerns.⁵¹

⁴⁷ See, e.g., Cleary and Thomson Financial.

⁴⁸ As defined in the rule, for purposes of Regulation AC, "foreign security" means a security issued by a foreign company for which a U.S. market is not the principal trading market.

⁴⁹ See, e.g., SIA and SSB.

⁵⁰ See SIA.

⁵¹ See SIA and SSB.

The certification required by Rule 501 of Regulation AC does not impede the oversight or review of research reports. If, at the end of the revision process, the analyst still believes that the report accurately reflects his or her personal views about the subject securities or issuers, then that analyst may certify and the firm may use the research report. If, however, after the review process the research report no longer reflects the analyst's personal views, then that analyst would be unable to certify and the firm would not be in compliance with Regulation AC if it uses the research report without a certification.

I. Regulation AC and Fraud Liability Under Federal Securities Laws

Several commenters requested that the Commission reiterate the position stated in the Proposing Release that Regulation AC does not impose new liability on analysts or their firms.⁵² Regulation AC formalizes and potentially adds rigor to analysts' responsibilities to express their views truthfully and without guile.⁵³ Regulation AC makes explicit the representations that are already implicit when an analyst publishes his or her views—that the analysis of a security published by the analyst reflects the analyst's honestly held views.⁵⁴

Regulation AC does not alter any other existing obligation under the federal securities laws for research analysts or broker-dealers.⁵⁵ A research report contains an inherent representation that the views expressed in the report are not knowingly false and do not omit material facts necessary in order to make statements made not misleading.⁵⁶ Thus, even without

⁵² See, e.g., Karr Tuttle, NASAA, SIA, and SSB.

⁵³ As the Commission stated in the Proposing Release, Regulation AC is not intended to create new duties under section 10(b) of the Exchange Act. As a result, no private liability will arise from a broker, dealer, or associated person's failure to make the required disclosure, or make, keep, and maintain required records. However, Regulation AC is subject to the full range of the Commission's enforcement authority. With regard to the enforcement of Regulation AC by the SROs, nothing in Regulation AC is inconsistent with Exchange Act Rule 19g2-1. See 17 CFR 240.19g2-1.

⁵⁴ The use of a certification process echoes and is consistent with one approach employed in the Sarbanes-Oxley Act of 2002, which requires certifications by officers of corporations relating to issuers' financial statements. See Sarbanes-Oxley Act sections 302 and 906, Pub. L. 107-204 (2002).

⁵⁵ See, e.g., Securities Act sections 17(a) and 17(b), 15 U.S.C. 77q; Exchange Act section 10(b), 15 U.S.C. 78j(b), and Rule 10b-5, 17 CFR 240.10b-5.

⁵⁶ See, e.g., Securities Act section 17(a), 15 U.S.C. 77q(a); Exchange Act Rule 10b-5, 17 CFR 240.10b-5; Exchange Act section 15(c)(1)(A), 15 U.S.C. 78o(c)(1)(A); and Exchange Act Rule 15c1-2(b), 17 CFR 240.15c1-2.

⁴⁵ See Alliance and Thomson Financial.

⁴⁶ See, e.g., Schwab.