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December 18, 2008

VIA E-MAIL

Marcia E. Asquith
Office of the Corporate Secretary
Financial Industry Regulatory Authority
1735 K Street, NW
Washington, DC 20006-1500

Re: Regulatory Notice 08-68: Circulation of Rumors

Dear Ms. Asquith:

The Investment Company Institute¹ is writing to express concerns over the breadth of certain aspects of FINRA's proposed Rule 2030 relating to the origination or circulation of rumors ("Proposed Rule 2030"). We fully appreciate the importance of preventing the harm that malicious rumors can have on our trading markets and we strongly support the policy goals underpinning Proposed Rule 2030. We are concerned, however, that in combining the current FINRA and NYSE Regulation anti-rumor rules to craft Proposed Rule 2030, FINRA has broadened the current rules' scope in ways that may lead to unintended consequences.

BACKGROUND

FINRA is proposing to replace FINRA Rule 6140(e) and Incorporated NYSE Rule 435(5), as well as the Interpretation to Rule 435(5), with the following:

Rule 2030. Circulation of Rumors

No member shall originate or circulate in any manner a rumor concerning any security which the member knows or has reasonable grounds for believing is false or misleading or would improperly influence the market price of such security. A member must promptly report to FINRA any circumstance which reasonably would lead the

¹ The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of \$10.10 trillion and serve almost 90 million shareholders.

member to believe that any such rumor might have been originated or circulated.

As proposed, Rule 2030 would incorporate several important changes to the existing rules. It would expand the scope of prohibited activity by removing the qualification currently found in Rule 435(5) that the rumor be “of a sensational character” and “reasonably be expected to affect market conditions on the Exchange.” It would further expand the scope of the current rules by applying to all securities rather than those just reported to the consolidated tape and by removing the current exception in Rule 435(5) for discussions of “unsubstantiated information published by a widely circulated public media.” Finally, it would expand the reporting requirement. Currently, Rule 6140(e) has no reporting requirement and Rule 435(5) only relates to securities traded on the NYSE.

DISCUSSION

The basic prohibition in Proposed Rule 2030 is that “no member shall originate or circulate in any manner a rumor concerning any security which the member knows or has reasonable grounds for believing is false or misleading or would improperly influence the market price of such security.” The wording of this prohibition is extremely broad, without the current limitations that the rumor be “of a sensational character” and “reasonably be expected to affect market conditions on the Exchange,” and without the exception for discussions of widely circulated information.

We have several concerns about the language in the Proposed Rule. First, the breadth of this prohibition may lead to technical violations of the rule for legitimate conduct. Take, for example, a situation where a portfolio manager asks an analyst to explain the sudden movements in a particular stock, and the analyst replies that the stock is moving based on a rumor about the issuer. By repeating the rumor to the portfolio manager, it would appear that the analyst has circulated it in violation of Proposed Rule 2030. This cannot be the result FINRA intended.

To address this concern, we recommend that FINRA qualify the term “rumor” in the final rule along the lines of Incorporated NYSE Rule 435(5). Trading in securities involves the analysis of an almost constant flow of information from a great variety of sources. Not all of this information may be credible, and not all may be able to be quickly verified (or conversely, dismissed as rumor). Rule 435(5) limits its scope to rumors of a sensational character reasonably expected to affect the market. This is a sensible approach that reflects a balance between the need to prevent malicious rumors and the business reality of the volume of information that investment professionals deal with on a daily basis. It is also consistent with the approach taken by the U.K.’s Financial Services Authority, which recently suggested that “firms could impose prohibitions on passing on or discussing unverified information of a sensational nature, which has not already been widely circulated in the market, where there exists no legitimate business reason for doing so.”²

² See “Thematic Review: Rumours,” FSA Market Watch, Issue No. 30 (Nov. 2008), available at http://www.fsa.gov.uk/pubs/newsletters/mw_newsletter30.pdf.

Proposed Rule 2030 would also eliminate the exception in Rule 435(5) for discussions of information published by a widely circulated public media. We believe that this exception should be retained in the final rule. Once a rumor has been published publicly, it is unrealistic to believe that it will not be broadly discussed and evaluated by investment professionals. Indeed, we would expect investment professionals to discuss such matters in the normal course of their business.

Finally, we are concerned that the reporting requirement in the rule will prove problematic. Proposed Rule 2030 would require firms to “promptly report to FINRA any circumstance which reasonably would lead the member to believe that any such rumor might have been originated or circulated.” As mentioned above, there is an almost constant flow of information crossing the desks of investment professionals. It would be impossible as a practical matter to design a compliance procedure by which a firm could comply with the requirement to report “*any circumstance*” that suggests that a rumor “*might have been*” originated or circulated. Even if such a procedure were possible, it would serve no meaningful regulatory purpose to have firms filing numerous reports that simply say that a rumor might have been originated or circulated, with no attendant market or client impact.

This concern is borne, primarily, of the breadth of Proposed Rule 2030’s scope. To the extent that FINRA clarifies and appropriately limits that scope in the final rule, the reporting requirements obviously become more practical and easier to implement. Even with appropriate clarifications to the term “rumor,” however, we strongly recommend that FINRA consider whether a materiality standard could be added to the reporting requirement that would better serve regulatory policy purposes and result in more meaningful reports to FINRA.

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We appreciate the opportunity to comment on Proposed Rule 2030. If you have any questions regarding our views, please contact me at (202) 371-5430 or Mara Shreck at (202) 326-5923.

Sincerely,

/s/

Robert C. Grohowski
Senior Counsel
Securities Regulation – Investment Companies