

**INFORMATIONAL**

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**Independent  
Research  
Reports**

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**SEC Approves Rule  
Change Relating To  
Filing Requirements For  
Independently Prepared  
Research Reports****SUGGESTED ROUTING**

*The Suggested Routing function is meant to aid the reader of this document. Each NASD member firm should consider the appropriate distribution in the context of its own organizational structure.*

- Legal & Compliance
- Mutual Fund
- Registered Representatives
- Senior Management

**KEY TOPICS**

- Advertising And Sales Literature
- NASD Rule 2210
- Research Reports

**Executive Summary**

On January 13, 2000, the Securities and Exchange Commission (SEC) approved amendments to National Association of Securities Dealers, Inc. (NASD<sup>®</sup>) Rule 2210, which governs member communications with the public.<sup>1</sup> The amendments exempt from Rule 2210's filing requirements certain types of independently prepared research reports concerning investment companies. The amendments become effective on April 1, 2000.

Questions concerning this *Notice* may be directed to Thomas M. Selman, Vice President, Investment Companies/Corporate Financing, NASD Regulation, Inc. (NASD Regulation<sup>SM</sup>) at (240) 386-4533; Thomas A. Pappas, Director, Advertising/Investment Companies Regulation, NASD Regulation, at (202) 728-8453; or Joseph P. Savage, Counsel, Advertising/Investment Companies Regulation, NASD Regulation, at (202) 728-8233.

Attachment A includes the text of Rule 2210's amendments.

**Background**

NASD Rule 2210 requires that any "advertisement" or "sales literature" concerning a registered investment company be filed with NASD Regulation's Advertising/Investment

Companies Regulation Department (Department) and meet the content standards of Rule 2210 and any applicable SEC rules. Rule 2210 defines "sales literature" to include research reports. Consequently, a member that uses a research report as sales material must file it with the Department, even if the member did not commission the research contained in the report, and an independent, third party research firm prepared the report.

As the investment company industry has grown in recent years, so has the coverage of the industry by independent research firms. Many research firms publish reports that analyze and provide information about a wide variety of investment companies, including their performance, fees and expenses, and a description and narrative analysis of their investment strategies and portfolio management style.

NASD members use these independently prepared research reports in a number of ways. For example, a member may make an independent research firm's entire research service available to customers at a branch office. A member may also distribute or make available an independently prepared research report concerning a particular investment company as part of its selling process.

**Description Of Filing Exemption**

The amendments provide that certain types of independently prepared research reports concerning registered investment companies do not have to be filed with the Department if they are used as sales literature. Pursuant to new Rule 2210(c)(6)(G), all research reports—including customized reports prepared at the request of an investment company, its affiliates, or a member firm—must meet five requirements to qualify for the filing exemption. Customized reports also must meet a sixth requirement.

- 1) The report must be prepared by an entity that is independent of the investment company, its affiliates, and the member using the report.
- 2) The member using the report may not materially alter the report's contents, except to the extent necessary to make it consistent with applicable regulatory standards. In this regard, for example, the Department would allow a member to add performance information necessary for the report to meet SEC Rule 482's currentness standards.<sup>2</sup> Additionally, a member may correct any factual errors or clarify terms or other information in the report. In general, the investment company, its affiliates, or the member using the report would make these alterations.
- 3) The research firm must prepare and distribute reports based on similar research with respect to a substantial number of investment companies.

- 4) The research firm must update and distribute reports based on its research of the investment company with reasonable regularity in the normal course of the research firm's business (e.g., semi-annually).
- 5) Neither the investment company, its affiliates, nor the member using the research report may commission the research used by the research firm in preparing the report. While these entities may not commission the research used in preparing the report, this requirement does not preclude a member from paying fees to independent research firms for research services subscriptions, reproducing and distributing its reports, or preparing customized reports.
- 6) If a customized report is prepared at the request of the investment company, its affiliate, or a member, the report may include only information that the research firm has already compiled and published in another non-customized report that meets the requirements of Rule 2210(c)(6)(G). Additionally, the customized report may not omit information necessary to make it fair and balanced. As discussed above, members may alter customized reports to the extent necessary to make the report consistent with applicable regulatory standards. Additionally, a member may rely on the filing exemption for a customized report meeting the requirements of paragraph (G)(vi) even if the member did not request preparation of the customized report.

The amendments also make clear that, although research reports meeting these requirements are excluded from the NASD's filing requirements, they will be deemed filed with the NASD for purposes of Section 24(b) of the Investment Company Act of 1940 and SEC Rule 24b-3 thereunder. Section 24(b) of the Investment Company Act requires sales material for open-end investment companies, unit investment trusts, and face-amount certificate companies to be filed with the SEC within 10 days of distribution to investors. Rule 24b-3 provides that sales material filed with a self-regulatory organization will be deemed filed with the SEC for purposes of Section 24(b). The purpose of this provision is to make clear that members will not be required to file such reports with the SEC simply because they did not file them with the Department.

Except for the filing requirements, independently prepared research reports will continue to be regarded as sales literature for purposes of Rule 2210. These reports will remain subject to Rule 2210's content requirements (including the ranking guidelines, when applicable), spot-check procedures, and recordkeeping requirements, and a registered principal of the member must approve them prior to use.

The amendments apply to independently prepared research reports that are contained in software or that are electronically communicated, as well as printed reports.

**Effective Date Of Amendments**

The amendments are effective on April 1, 2000.

**ATTACHMENT A****Text Of Amendments To Rule 2210**

(Note: *New text is underlined.*)

Paragraph (c)(6) of Rule 2210 is amended by adding new paragraph (G) as follows:

(6) The following types of material are excluded from the foregoing filing requirements and (except for research reports under paragraph (G)) the foregoing spot-check procedures:

\* \* \*

(G) any research report concerning an investment company registered under the Investment Company Act of 1940, provided that:

(i) the report is prepared by an entity that is independent of the investment company, its affiliates, and the member using the report (the "research firm");

(ii) the report's contents have not been materially altered by the member using the report (except as necessary to make the report consistent with

applicable regulatory standards);

(iii) the research firm prepares and distributes reports based on similar research with respect to a substantial number of investment companies;

(iv) the research firm updates and distributes reports based on its research of the investment company with reasonable regularity in the normal course of the research firm's business;

(v) neither the investment company, its affiliates nor the member using the research report has commissioned the research used by the research firm in preparing the report; and

(vi) if a customized report was prepared at the request of the investment company, its affiliate or a member, then the report includes only information that the research firm has already compiled and published in another report, and does not omit information in that report necessary to make the customized report fair and balanced.

Although research reports meeting the above requirements are excluded from the foregoing filing requirements, they shall be deemed to be filed with the Association for purposes of Section 24(b) of the Investment Company Act of 1940 and Rule 24b-3 of the Securities and Exchange Commission thereunder.

**Endnotes**

<sup>1</sup> See Securities and Exchange Release No. 34-42340 (Jan. 13, 2000), 65 Fed. Reg. 3510 (Jan. 21, 2000).

<sup>2</sup>The Department has had a longstanding informal policy of allowing members to distribute a research report that does not meet the currentness standards of Rule 482, provided that: (i) it is the most recent version of the report, and (ii) it is accompanied by information that satisfies the currentness standards and is at least equally prominent to any non-current performance information contained in the report.

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