

Origination and Circulation of Rumors

FINRA Requests Comment on Proposed FINRA Rule Addressing the Origination and Circulation of Rumors

Comment Period Expires: July 16, 2009

Executive Summary

As part of the process of developing a new, consolidated rulebook (the Consolidated FINRA Rulebook), FINRA is requesting comment on proposed FINRA Rule 2030 relating to the origination and circulation of rumors.¹ FINRA initially sought comment on the proposed rule, which is based on FINRA Rule 6140 and Incorporated NYSE Rule 435(5), in *Regulatory Notice 08-68*. In response to the comments received, FINRA is proposing substantial changes to proposed FINRA Rule 2030. The proposed changes include amendments to the general prohibition in Rule 2030 and the proposed reporting requirement, as well as adopting Supplementary Material to Rule 2030 that will address exceptions for certain communications, the definition of the term “rumor,” additional rules of which member firms should be aware, and a firm’s obligation to adopt written policies and procedures concerning rumors. FINRA is requesting comment on the proposed revisions to Rule 2030.

The text of the proposed rule is set forth in Attachment A.

Questions concerning this *Notice* should be directed to Brant Brown, Associate General Counsel, Office of General Counsel, at (202) 728-6927.

June 2009

Notice Type

- Request for Comment
- Consolidated FINRA Rulebook

Suggested Routing

- Compliance
- Legal
- Registered Representatives
- Senior Management

Key Topic(s)

- Rumors

Referenced Rules & Notices

- Regulatory Notice 08-68
- FINRA Rule 6140
- Incorporated NYSE Rule 435(5)

Action Requested

FINRA encourages all interested parties to comment on the proposal. Comments must be received by July 16, 2009.

Member firms and other interested parties can submit their comments using the following methods:

- Emailing comments to pubcom@finra.org; or
- Mailing comments in hard copy to:

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

To help FINRA process and review comments more efficiently, persons should use only one method to comment on the proposal.

Important Notes: The only comments that FINRA will consider are those submitted pursuant to the methods described above. All comments received in response to this *Notice* will be made available to the public on the FINRA Web site. Generally, FINRA will post comments on its site one week after the end of the comment period.²

Before becoming effective, a proposed rule change must be authorized for filing with the SEC by the FINRA Board of Governors, and then must be approved by the SEC, following publication for public comment in the *Federal Register*.³

Background & Discussion

In *Regulatory Notice 08-68*, FINRA requested comment on proposed Rule 2030 addressing the origination and circulation of rumors. FINRA received numerous comments on the proposed rule and, in response to those comments, is proposing substantial changes to Rule 2030.⁴ The proposed changes to the rule are discussed below.

- **Amending the general prohibition.** As originally proposed, Rule 2030 prohibited a member firm from originating or circulating a rumor that “the member knows or has reasonable grounds for believing is false or misleading or would improperly influence the market price of a security.” This formulation was based largely on the existing prohibition in FINRA Rule 6140(e). In contrast, NYSE Rule 435(5) prohibits the circulation of rumors of a sensational character “which might reasonably be expected to affect market conditions on the [NYSE].” As amended, proposed Rule 2030 applies to a rumor that a member knows or has reasonable grounds for believing is false or misleading and is likely to influence the market price of a security.

- **Retaining an amended reporting requirement.** As originally proposed, Rule 2030 required a firm to report to FINRA “any circumstance which reasonably would lead the member to believe that any [rumor covered by the rule] might have been originated or circulated.” FINRA received several comments addressing the breadth and scope of the proposed reporting requirement, ranging from suggestions to reduce the scope of the requirement to suggestions that the rule not include any reporting requirement. FINRA continues to believe that the reporting of rumors will enhance FINRA’s efforts to ensure the integrity of the market. However, FINRA is proposing a revised reporting requirement that would require firms to promptly report rumors that the firm learns of and knows, or has reasonable grounds for believing, were originated or circulated for the purpose of improperly influencing the market price of a security. FINRA believes that a more focused reporting requirement will increase FINRA’s efficiency in dealing with reports and enhance FINRA’s ability to respond rapidly and appropriately to those rumors that are most likely to affect the market and harm investors.

In addition to the proposed changes to the language in Rule 2030, FINRA is proposing Supplementary Material to Rule 2030 to address several concerns raised by commenters.

- **Definition of the term “rumor.”** FINRA is proposing Supplementary Material that defines the term “rumor” for purposes of Rule 2030. Under the proposed definition, a “rumor” is defined as “a false or misleading statement or a statement without a reasonable basis.” In addition, the proposed Supplementary Material clarifies that “[a] statement will not be considered a ‘rumor’ if it is clearly an expression of an individual’s or firm’s opinion, such as an analyst’s view of the prospects of a company.”
- **Permissible communications.** The proposed Supplementary Material to Rule 2030 also includes three limited exceptions to the general prohibitions in Rule 2030. The first exception to the rule is based on the existing exception in NYSE Rule 435(5) for rumors that have been published by widely circulated public media provided the source of the rumor and its unsubstantiated nature are disclosed. Second, FINRA is proposing to except discussions of rumors among market participants when necessary to explain market or trading conditions and one’s view of the validity of the information, provided the communication is not intended to influence the price movement of a security and the information is communicated in a responsible way (*i.e.*, sourcing the information where possible, not embellishing the information, and presenting the information in as neutral and balanced a way as practicable under the circumstances). The final exception FINRA is proposing is an exception for internal firm discussions undertaken solely for the purpose of verifying, or inquiring into the truthfulness or accuracy of, a rumor, provided the unsubstantiated nature of the information and, where possible, the source of the information are disclosed.

- **Market manipulation.** Because FINRA is proposing to include several exceptions to the general prohibitions in Rule 2030, FINRA is also proposing Supplementary Material that highlights the fact that knowingly originating or circulating false or misleading information with the intent to cause an impact on the price movement of a security is unlawful and violates FINRA rules as well as provisions of the federal securities laws and rules of the SEC. This provision emphasizes the fact that engaging in a discussion of potentially false or misleading information could violate FINRA or SEC rules or provisions of the federal securities laws even if the conduct does not violate Rule 2030.
- **Written policies and procedures.** Finally, FINRA is proposing Supplementary Material that specifically addresses a firm's obligation to adopt written policies and procedures concerning rumors. The Supplementary Material also notes a firm's obligation to develop and document appropriate training policies and programs that are reasonably designed to ensure that associated persons of the member firm comply with their responsibilities and obligations surrounding the origination and circulation of rumors.⁵

Endnotes

- 1 The current FINRA rulebook consists of (1) FINRA Rules; (2) NASD Rules; and (3) rules incorporated from NYSE (Incorporated NYSE Rules). While the NASD Rules generally apply to all FINRA members, the Incorporated NYSE Rules apply only to those members of FINRA that are also members of the NYSE (Dual Members). The FINRA Rules apply to all FINRA member firms, unless such rules have a more limited application by their terms. For more information about the rulebook consolidation process, see *FINRA Information Notice 03/12/08* (Rulebook Consolidation Process).
- 2 FINRA will not edit personal identifying information, such as names or email addresses, from submissions. Persons should submit only information that they wish to make publicly available. See *NASD Notice to Members 03-73* (November 2003) (NASD Announces Online Availability of Comments) for more information.
- 3 Section 19 of the Securities Exchange Act of 1934 (Exchange Act) permits certain limited types of proposed rule changes to take effect upon filing with the SEC. The SEC has the authority to summarily abrogate these types of rule changes within 60 days of filing. See Exchange Act Section 19 and rules thereunder.
- 4 The comments received in response to *Regulatory Notice 08-68* are available on FINRA's Web site at www.finra.org/notices/08-68
- 5 The Supplementary Material concerning training policies and programs is modeled on NASD Rule 2821(e), which governs member firms' responsibilities regarding deferred variable annuities. Specifically, Rule 2821(e) requires member firms to "develop and document specific training policies or programs reasonably designed to ensure that associated persons who effect and registered principals who review transactions in deferred variable annuities comply with the requirements of [the] Rule and that they understand the material features of deferred variable annuities."

Attachment A

Below is the text of proposed FINRA Rule 2030.

2030. Origination or Circulation of Rumors

No member shall originate or circulate in any manner a rumor concerning any security that the member knows or has reasonable grounds for believing is false or misleading and is likely to influence the market price of such security. If a member learns of a rumor that the member knows or has reasonable grounds for believing was originated or circulated for the purpose of improperly influencing the market price of a security, the member must promptly report the rumor to FINRA.

... **Supplementary Material:** — — — — —

.01 Definition of “Rumor.” A “rumor” is a false or misleading statement or a statement without a reasonable basis. A statement will not be considered a “rumor” if it is clearly an expression of an individual’s or firm’s opinion, such as an analyst’s view of the prospects of a company.

.02 Permissible Communications.

(a) Discussion of a rumor that is published by widely circulated public media is not prohibited provided its source and unsubstantiated nature are disclosed.

(b) This Rule does not prohibit the discussion of rumors among market participants when necessary to explain market or trading conditions. In that context, and with due regard that no member or associated person of a member is intending to influence price movement by discussing the information, it is appropriate to comment and present one’s view of the validity of such information in a responsible way (i.e., sourcing the origin of the information where possible; not embellishing the information; and presenting the information in as neutral and balanced a way as practicable under the circumstances).

(c) Associated persons of a member are permitted to discuss a rumor with other associated persons of the member if the discussion is undertaken solely for the purpose of verifying, or inquiring into the truthfulness or accuracy of, the rumor. In these situations, the member or associated person of the member must disclose the unsubstantiated nature of the information and, where possible, the source of the information.

.03 Market Manipulation. Knowingly originating or circulating false or misleading information with the intent to cause an impact on the price movement of one or more securities is unlawful and is in violation of FINRA rules (including but not limited to Rule 2010, just and equitable principles of trade, Rule 2020, and Rule 2030), as well as the antifraud and antimanipulation provisions of the federal securities laws (including but not limited to Sections 9 and 10 of the Exchange Act and the rules and regulations promulgated thereunder).

.04 Written Policies and Procedures. Members must maintain adequate written policies and supervisory procedures reasonably designed to identify and address the circulation of rumors. Members must also develop and document appropriate training policies and programs reasonably designed to ensure that associated persons of the member comply with their responsibilities and obligations surrounding the origination and circulation of rumors. Members must clearly identify who is responsible for issuing guidance when responding to rumors, including pertinent escalation procedures, and reporting obligations.