

Research Analysts and Research Reports

SEC Approves Amendments to NASD Rule 2711 and Incorporated NYSE Rule 472 to Conform to JOBS Act Requirements

Effective Dates: April 5, 2012, and October 11, 2012

Executive Summary

The SEC approved amendments to NASD Rule 2711 and Incorporated NYSE Rule 472 to conform to the requirements of the Jumpstart Our Business Startups Act (JOBS Act) and make certain additional changes to quiet period restrictions consistent with the policies underlying the JOBS Act. Most of the changes to NASD Rule 2711 and Incorporated NYSE Rule 472 are effective retroactively to April 5, 2012; changes to those rules regarding quiet periods after secondary offerings and after the expiration, termination or waiver of a lock-up agreement became effective upon approval by the Securities and Exchange Commission (SEC) on October 11, 2012.

The text of the amended rules is available at www.finra.org/notices/12-49.

Questions concerning this *Notice* should be directed to:

- ▶ Philip Shaikun, Associate Vice President and Associate General Counsel, Office of General Counsel, at (202) 728-8451.

Background & Discussion

The JOBS Act, which was signed into law on April 5, 2012, is intended to, among other things, help facilitate capital formation for “emerging growth companies” (EGCs) by improving the information flow about EGCs to investors. To that end, Section 105(b) of the JOBS Act amended Section 15D of the Securities Exchange Act (Exchange Act) to prohibit the SEC or any national securities association from adopting or maintaining any rule or regulation in connection with an initial public offering (IPO) of an EGC that:

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Notice Type

- ▶ Rule Amendment

Suggested Routing

- ▶ Compliance
- ▶ Investment Banking
- ▶ Legal
- ▶ Research
- ▶ Senior Management

Key Topics

- ▶ JOBS Act
- ▶ Quiet Periods
- ▶ Research
- ▶ Solicitation

Referenced Rules & Notices

- ▶ NASD Rule 2711
- ▶ Incorporated NYSE Rule 472

- ▶ restricts, based on functional role, which associated persons of a broker, dealer or member of a national securities association, may arrange for communications between an analyst and a potential investor; or
- ▶ restricts a securities analyst from participating in any communication with the management of an EGC that is also attended by any other associated person of a broker, dealer or member of a national securities association whose functional role is other than as securities analyst.

Section 105(d) further amends the Exchange Act to prohibit the SEC or any national securities association from adopting or maintaining any rule or regulation that prohibits a broker or dealer from publishing or distributing any research report or making a public appearance, with respect to the securities of an EGC either:

- ▶ within any prescribed period of time following the initial public offering date of the emerging growth company; or
- ▶ within any prescribed period of time prior to the expiration date of any agreement between the broker, dealer, or member of a national securities association and the emerging growth company or its shareholders that restricts or prohibits the sale of securities held by the emerging growth company or its shareholders after the initial public offering date.

These provisions became effective upon signature of the president on April 5, 2012. On August 22, 2012, the SEC's Division of Trading and Markets provided guidance on these provisions in the form of Frequently Asked Questions. The amendments approved by the SEC conform the applicable provisions of NASD Rule 2711 to the JOBS Act requirements in accordance with the SEC staff guidance.¹

Arranging and Participating in Communications

NASD Rule 2711(c)(4)² prohibits a research analyst from participating "in efforts to solicit investment banking business," including any "pitches" for investment banking business or other communications with companies for the purpose of soliciting investment banking business. The SEC staff guidance interprets the JOBS Act to now allow, in connection with an IPO of an EGC, research analysts to attend meetings with issuer management that are also attended by investment banking personnel, including pitch meetings, but not "engage in otherwise prohibited conduct in such meetings," including "efforts to solicit investment banking business." The guidance further explains that a research analyst that attends a pitch meeting "could, for example, introduce themselves, outline their research program and the types of factors that the analyst would consider in his or her analysis of a company, and ask follow-up questions to better understand a factual statement made by the emerging growth company's management." Accordingly, the amendments create an exception to NASD Rule 2711(c)(4) to reflect this guidance.³

The SEC staff guidance states that under Section 105(b) of the JOBS Act, an associated person of a broker-dealer, including investment banking personnel, may arrange communications between research analysts and investors in connection with an IPO of an EGC. As an example, the guidance states that an investment banker could forward a list of clients to a research analyst “that the analyst could, at his or her own discretion and with appropriate controls, contact.” The guidance acknowledges that FINRA does not have a rule that directly prohibits this activity and further states that such activity, without more, would not constitute conduct by investment banking personnel to directly or indirectly direct a research analyst to engage in sales or marketing efforts related to an investment banking services transaction, in violation of NASD Rule 2711(c)(6).⁴ As such, this JOBS Act provision required no conforming rule change.

Quiet Periods

Section 105(d) of the JOBS Act expressly permits publication of research and public appearances any time after the IPO of an EGC or prior to the expiration of any lock up agreement. While the JOBS Act refers only to the “expiration” of a lock-up agreement, the guidance states that Congress intended for the JOBS Act provisions to apply equally to the period before a “waiver” or “termination” of a lock-up agreement. Thus, in accordance with SEC staff guidance on this JOBS Act provision, the rule change amends NASD Rule 2711 to eliminate the following quiet periods with respect to an IPO of an EGC:

- ▶ NASD Rule 2711(f)(1)(A),⁵ which imposes a 40-day quiet period after an IPO on a member that acts as a manager or co-manager of such IPO;
- ▶ NASD Rule 2711(f)(2),⁶ which imposes a 25-day quiet period after an IPO on a member that participates as an underwriter or dealer (other than manager or co-manager) of such an IPO; and
- ▶ NASD Rule 2711(f)(4)⁷ with respect to the 15-day quiet period applicable to IPO managers and co-managers prior to the expiration, waiver or termination of a lock-up agreement, or any other agreement that such member has entered into with a subject company or its shareholders that restricts or prohibits the sale of securities held by the subject company or its shareholders after the completion of an IPO.

The SEC staff guidance notes that the JOBS Act makes no reference to quiet periods after a secondary offering or during a period of time after expiration of a lock-up agreement. Accordingly, the guidance concludes that NASD Rule 2711(f)(1)(B),⁸ which imposes a 10-day quiet period on managers and co-managers following a secondary offering and the remaining portion of NASD Rule 2711(f)(4)⁹ relating to quiet periods after the expiration, termination or waiver of a lock up agreement, remain fully in effect. Nonetheless, the guidance expresses the SEC staff’s belief that the policies underlying the JOBS Act are equally applicable to quiet periods during these other times. FINRA agreed that elimination of those quiet periods would advance the policy objectives of the JOBS Act and therefore NASD Rules 2711(f)(1)(B) and (f)(4) have been amended accordingly.¹⁰

Effective Dates

The changes to NASD Rules 2711(c)(4), (f)(1)(A), (f)(2) and (f)(4) (with respect to the 15-day quiet period *before* the expiration, termination or waiver of a lock-up agreement) and the corresponding changes to Incorporated NYSE Rule 472 are effective retroactively to April 5, 2012. The changes to NASD Rules 2711(f)(1)(B) and (f)(4) (with respect to the 15-day quiet period *after* the expiration, termination or waiver of a lock-up agreement) and the corresponding changes to Incorporated NYSE Rule 472 became effective upon SEC approval of the rule change on October 11, 2012.

Endnotes

1. FINRA notes that the SEC staff guidance interprets the JOBS Act provisions as applicable to Incorporated NYSE Rule 472 to the same extent as NASD Rule 2711. As such, the proposed rule change makes corresponding amendments to Incorporated NYSE Rule 472.
2. *See also* Incorporated NYSE Rule 472(b)(5).
3. A corresponding exception is created for Incorporated NYSE Rule 472(b)(5).
4. *See also* Incorporated NYSE Rule 427(b)(6)(ii).
5. *See also* Incorporated NYSE Rule 472(f)(1).
6. *See also* Incorporated NYSE Rule 472(f)(3).
7. *See also* Incorporated NYSE Rule 472(f)(4).
8. *See also* Incorporated NYSE Rule 472(f)(2).
9. *See also* Incorporated NYSE Rule 472(f)(4).
10. A corresponding change is made to Incorporated NYSE Rule 472(f).