

Transcript:

Regulation of Research under Rule 15a-6, Regulation AC and FINRA Rules

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Ben: SEC Rule 15a-6 provides an exemption from registration for foreign broker-dealers that distribute research reports to major U.S. institutional investors – that is, institutional investors with \$100 million under management.

Kathy: Rule 15a-6 does not regulate the content of the research reports. But, if the foreign broker-dealer has a relationship with a U.S. broker-dealer for purposes of distributing the research and facilitating broader contacts under the Rule – known as a chaperoning arrangement – or if the research is distributed to institutional investors who don't qualify as "majors," there are additional SEC and FINRA requirements affecting content and disclosures. And, the anti-fraud provisions of the Exchange Act apply to the distribution of all foreign research into the United States.

Ben: Where the foreign broker-dealer has a chaperoning arrangement with a U.S. registered broker-dealer, the reports should state that all trades in securities described in the research should be effected through the U.S. registered broker-dealer, not the foreign firm. If the foreign research is distributed to U.S. institutional investors other than major U.S. institutional investors, then the U.S. broker-dealer also must accept responsibility for the content of the research.

Kathy: Regulation AC may apply to the research if the foreign broker-dealer is an affiliate of the U.S. broker-dealer. Regulation AC requires that the research report include an attestation by the analyst that no part of his or her compensation is tied to the recommendations or views expressed in the research. Otherwise, disclosure must be made as to the nature, source and amount of the compensation, and that such compensation could influence the views expressed in the research report. The analyst must also certify that the views expressed in the research accurately reflect his or her personal views.

Ben: NASD Rule 2711, which governs the conduct of research analysts and the content of research reports, applies to all research distributed by a FINRA member firm, including research prepared by a foreign broker-dealer under Rule 15a-6. Among other things, Rule 2711 requires the member to

disclose information pertaining to investment banking and other relationships with the issuer, ownership interest in the subject securities, market-making and other relationships. Certain disclosures – such as ownership of the subject securities – relate to the member and its affiliates (including the foreign broker-dealer if it's an affiliate). Other disclosures – such as market making – relate only to the member firm. Some content requirements, including ratings charts and an explanation of the rating system, do not apply to the foreign research. However, it's advisable to include these whenever possible.

Kathy: A Rule 15a-6 relationship that involves the distribution of foreign research that is “globally branded” is subject to greater regulation under FINRA rules. Globally branded research is research that uses a single marketing identity for both the U.S. and the foreign broker-dealer. Because the global brand connotes that the research is proprietary to the U.S. firm, all of Rule 2711's content and disclosure requirements apply. The reports also must disclose that U.S. prohibitions limiting the interaction of investment banking and research personnel may not apply to personnel associated with the foreign broker-dealer, and that the foreign research analysts may not be licensed in accordance with U.S. standards.

Ben: All foreign research distributed by a FINRA member firm must be reviewed by a qualified principal or supervisory analyst. And the firm should have written supervisory procedures designed to monitor compliance with all aspects of the distribution of foreign research under Rule 15a-6.

Kathy: Our website page contains more information on these disclosure requirements and other issues affecting the distribution of foreign research into the United States under Rule 15a-6. And, we've also posted a template that may be useful in preparing your firm's disclosures under Rule 15a-6, Regulation AC and NASD Rule 2711.