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FINRA Proposes Revisions to Fixed-Income Research Rule *Clarifications Regarding Distribution of Third-Party Research to Institutional Investors, Non-U.S. Affiliate Distribution to Institutional Investors, Distribution of Institutional Research to Media and Other Non-Investors, and Institutional Public Appearances*

Earlier this week, FINRA filed with the SEC proposed revisions (the “Proposed Revisions”)¹ to Rule 2242,² FINRA’s new fixed-income research rule (the “Rule”). The Rule is scheduled to take effect on July 16, 2016. The Proposed Revisions will not impact the implementation of the rule as adopted, meaning that the Rule will become effective as adopted pending the adoption of these Proposed Revisions. The Proposed Revisions address:

- Which of the Rule’s requirements for distribution of third-party research³ apply to such research that is distributed only to institutional investors (“third-party institutional research”);
- Whether customer consent requirements apply to a non-U.S. affiliate’s distribution of institutional fixed-income research prepared by a FINRA member to non-U.S. institutional investors;
- Distribution of institutional fixed-income research to the media and other persons for informational rather than investment purposes; and,
- Disclosure requirements for public appearances of fixed-income research analysts when the audience is comprised solely of institutional investors.

Third-Party Institutional Research

The Proposed Revisions clarify the interaction of Rule 2242(j), which provides that institutional research is exempt from all of the Rule’s requirements except those expressly noted therein, and Rule 2242(g), which imposes specific requirements for distribution of third-party research.

The Proposed Revisions provide that firms distributing third-party institutional research must comply with the Rule’s third-party research review requirements. On the other hand, firms do not need to include the specific conflict of

¹ FINRA’s SEC filing in respect of the Proposed Revisions can be found [here](#).

² For a broader and more detailed description of the Rule generally, please see our October 2015 client publication regarding the Rule’s approval by the SEC: [FINRA’s New Fixed-Income Research Rule and Modifications to Equity Research Rule](#). For a description of FINRA’s earlier proposals in respect of the Rule, you may refer to our client publications regarding [Regulatory Notice 11-11](#) (April 2011), [Regulatory Notice 12-09](#) (March 2012), and [Regulatory Notice 12-42](#) (March 2013).

³ All references in this publication to “research” should be understood to refer only to fixed-income research. Rule 2241 regulates equity research and is not affected by the Proposed Revisions.

interest disclosures that are required for third-party retail research; instead, firms are required to include a more limited version of the “health warning” that the Rule mandates for institutional research.

The following chart describes the application of every provision of Rule 2242(g) (Distribution of Third-Party Debt Research Reports) to institutional third-party research if the Proposed Revisions are adopted:

Provision	Description	Under Proposed Revisions, applicable to third-party institutional research?
2242(g)(1)	Review requirement: Prohibition on distribution of third-party debt research if a firm knows or has reason to know such research is not objective or reliable.	Yes.
2242(g)(2)	Review requirement: Firms must establish policies and procedures reasonably designed to ensure that third-party research contains no untrue statement of material fact and is otherwise not false or misleading.	Yes, except with respect to “independent third-party research reports” as defined in Rule.
2242(g)(3)	Specific conflict of interest disclosures: Requires inclusion of specific conflict of interest disclosures, including relating to ownership of securities of the subject company by the member or its affiliates, principal trading in the fixed-income securities of the subject company, and other material conflicts.	No.
2242(g)(4)	Exemption for independent third-party research reports from 2242(g)(2): Firms must have have policies and procedures reasonably designed to ensure that third-party research contains no untrue statement of material fact and is otherwise not false or misleading.	Yes—with this exemption, no such procedures are required for independent third-party research reports.
2242(g)(5)	Independent research reports non-distribution: “A member shall not be considered to have distributed a third-party debt research report for the purposes of paragraph (g)(3) where the research is an independent third-party debt research report and made available by a member (a) upon request; (b) through a member-maintained website; or (c) to a customer in connection with a solicited order in which the...customer requests such independent debt research”.	No, technically. . Because the Proposed Revisions would not apply (g)(3) for third-party institutional research, this exemption is inapplicable.
2242(g)(6)	Labeling: Requires firms to ensure that a third-party debt research report is clearly labeled as such and that there is no confusion on the part of the recipient as to the person or entity that prepared the debt research report.	Yes.
2242(j)(4)	Health warning: Must be prominently disclosed on first page. 2242(j)(3)(A): “This document is intended for institutional investors and is not subject to all of the independence and disclosure standards applicable to debt research reports prepared for retail investors.” 2242(j)(3)(B): If applicable, “The views expressed in this report may differ from the views offered in [Firm’s] debt research reports prepared for retail investors.” 2242(j)(3)(C): If applicable, “This report may not be independent of [Firm’s] proprietary interests. [Firm] trades the securities covered in this report for its own account and on a discretionary basis on behalf of certain clients. Such trading interests may be contrary to the recommendation(s) offered in this report.”	Modified version is required: 2242(j)(3)(A) and (C) required, 2242(j)(3)(B) not required.

Distribution of Research by Non-U.S. Affiliates to Non-U.S. Institutional Customers

The Proposed Revisions permit non-U.S. affiliates to distribute fixed-income research of their FINRA-member affiliate, including globally branded research, to the affiliate's non-U.S. institutional customers without receiving the customer consent normally required under the Rule for institutional research, subject to conditions. FINRA noted that some non-U.S. customers had struggled to understand why they were being asked to provide those consents, when they were not customers of a U.S. broker-dealer.

Specifically, the Proposed Revisions would add Supplemental Material .12 to the Rule, which permits distribution of a FINRA-member research report to a non-U.S. institutional customer of a non-U.S. affiliate, provided that:

- The non-U.S. institutional investor is not a customer of the FINRA member firm;
- The non-U.S. institutional investor is a customer of the non-U.S. affiliate distributing the report; and,
- The non-U.S. affiliate distributing the report has a reasonable basis to believe that the customer meets the definition of institutional account under Rule 4512.

Distribution of Institutional Fixed-Income Research for Informational Purposes

The Proposed Revisions add Supplemental Material .13 to the Rule permitting the distribution of published institutional research to persons and entities that do not qualify as institutional investors under the Rule "for informational purposes unrelated to investing in debt securities," subject to disclosure conditions described below.

The Proposed Revisions specifically permit distribution of institutional research to the following:

- Regulators for regulatory purposes;
- Academics for academic purposes;
- Issuers for the purpose of enhancing knowledge of their industry and competitors and market and economic factors; and,
- Media organizations for news gathering purposes.

The news will be welcome in particular to media outlets that had been informed by many firms that they would no longer be distributing research to them.

In respect of any such distributions, firms are required to disclose that:

- The firm may provide the recipient debt research reports that were prepared for institutional investors and are not subject to all of the independence and disclosure standards applicable to debt research reports prepared for retail investors; and,
- The institutional debt research reports would be provided only for informational purposes and not for the purpose of making an investment decision related to debt securities.

Public Appearances by Research Analysts

The Proposed Revisions would add Supplemental Material .14, which provides that the disclosures the Rule mandates for public appearances of debt research analysts (about fixed-income securities) are not required if attendance is limited to institutional investors eligible to receive institutional-only fixed-income research under the Rule.

The Proposed Revisions expressly require that firms utilizing the exemption maintain sufficient records to demonstrate that attendance at the public appearance was limited to such investors.

Concluding Thoughts

The Proposed Revisions provide clarifying guidance in areas where interaction among Rule provisions were not without doubt, and provide helpful relief in other respects. As firms producing fixed-income research gear up for the July 16 effective date of Rule, they should review policies and procedures to include any aspects of the Proposed Revisions applicable to their firm's business.

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