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*VIA E-MAIL AND FEDERAL EXPRESS*

August 12, 1997

Ms. Joan Conley  
Office of the Corporate Secretary  
NASD Regulation, Inc.  
1735 K Street, N.W.  
Washington, DC 20006-1500

**Re: NASD Regulation Request for Comment 97-37**

Dear Ms. Conley:

PSA The Bond Market Trade Association ("PSA")<sup>1</sup> welcomes the opportunity to comment on the above-referenced NASD Regulation Inc. ("NASDR") Request for Comment 97-37 ("RFC 97-37"), issued by NASDR in June 1997. RFC 97-37 solicits views on proposed amendments to NASD Conduct Rule 2210 (Communications with the Public), which would subject written or electronic communications prepared for a single customer to the general and specific standards of Rule 2210. PSA agrees with NASDR that all communications with the public—including those prepared for a single customer—should not contain information that could be considered exaggerated, unwarranted, or misleading. However, PSA strongly opposes the proposed amendments to Rule 2210 as an appropriate or necessary means of achieving this goal. Our specific comments follow.

**I. SUMMARY OF PROPOSED RULE CHANGES**

The proposed amendments to Rule 2210 would expand the existing categories of "communications with the public" covered under Rule 2210 by adding the new category of "correspondence." For purposes of Rule 2210, "correspondence" would be defined as any written or electronic communication prepared for delivery to a single customer, and not for dissemination to multiple customers or to the general public. All such correspondence would be subject to the general and specific requirements of paragraphs (d) and (f) of Rule 2210, but not the approval and recordkeeping requirements of paragraph (b) nor the filing and review requirements of paragraph (c). Finally, inclusion of "correspondence" within the category of "communications with the public" would require such correspondence to conform to all applicable SEC rules.

**II. DISCUSSION**

PSA supports NASDR's efforts to insure that the content of communications not be exaggerated, unwarranted or misleading. However, the proposed amendments to Rule 2210 attempt to achieve this goal by subjecting individual correspondence to a variety of content requirements that have traditionally been applied only to mass communications

with the public, such as advertising and sales literature. PSA believes that this approach is unnecessary and unwarranted, and would generate a variety of problems, which are discussed below in detail. In summary, however, our primary objections are as follows: First, the obligations and conduct of members in communicating with individual customers are adequately addressed by existing NASDR rules. These existing rules would be further supplemented and enhanced by the adoption of pending, proposed rules concerning supervision of communications, which PSA strongly supports. Second, the application of the specific (as opposed to the general) content requirements of paragraphs (d) and (f) of Rule 2210, which were designed to prevent exaggerated, unwarranted or misleading statements in members' sales literature and advertisements, would be inappropriate for most individual communications, especially electronic communications. Finally, the proposed amendments would unnecessarily inhibit the use of electronic communications media. For these reasons PSA opposes the adoption of amended Rule 2210 in the form currently proposed.

***A. Existing NASDR Rules Adequately Address Member Conduct Relating to Correspondence for Use with a Single Customer***

Existing NASDR rules already address the obligations and conduct of members when communicating with customers. For example, Rule 2110 requires members, when conducting business, to observe high standards of commercial honor and just and equitable principles of trade. Rule 2120 prohibits members from effecting any transactions in, or inducing the purchase or sale of, any security by means of any manipulative, deceptive or other fraudulent device or contrivance. Rule 2310 requires members, in recommending a transaction in a security, to have reasonable grounds for believing that the recommendation is suitable for the customer. IM-2310-2 provides interpretative guidance concerning fair dealing with customers.

In addition, under the proposed amendments to Rule 2210, communications prepared for delivery to a single current or prospective customer would, as described above, become subject to the general standards of paragraphs (d) and (f) of that rule. Among other things, these general standards require that such communications be based on principles of fair dealing and good faith, and provide a sound basis for evaluating the facts regarding any particular security or type of security identified, industry discussed, or services offered. These general standards also prohibit the omission of material facts or qualifications, as well as the inclusion of any exaggerated, unwarranted or misleading statements or claims in such communications.

Existing NASDR rules also establish extensive supervisory review requirements governing communications with customers. For example, Rule 3010(d) requires members to establish procedures for the review and endorsement by a registered principal in writing, on an internal record, of all transactions and all correspondence of its registered representatives pertaining to the solicitation or execution of any securities transaction. In early 1997, the SEC published for comment proposed amendments to Rule 3010, which had previously been recommended for adoption by NASDR. As amended, Rule 3010 would require members to develop written procedures designed to provide reasonable

review and supervision of registered representatives' correspondence with the public relating to a member firm's business, and would require evidence of the implementation and execution of these procedures.<sup>2</sup> These amendments would require firms to supervise all correspondence relating to a firm's business, including correspondence prepared for a single customer. PSA strongly supported these rule changes because they would allow firms the ability to integrate electronic communications into their business activities in a manner that is best calculated to meet their own business needs, while simultaneously providing effective regulatory oversight by establishing appropriate general standards for supervisory review and monitoring of members' communications with customers and the public.<sup>3</sup>

In light of these existing and proposed rules, the need to promulgate additional rules to address member conduct relating to correspondence prepared for use with a single customer appears duplicative and unnecessary. We believe that existing regulations already provide ample direction to member firms to prohibit the inclusion of unwarranted, exaggerated or misleading statements in communications prepared for single customers. These same regulations confer NASDR with the necessary supervisory and enforcement tools to oversee and sanction any member firm that engages in such conduct. Moreover, in light of the pending adoption of the amendments to Rule 3010 outlined above, we believe that it would be premature for NASDR to enact the proposals contained in RFC 97-37. Although the preamble to RFC 97-37 cites "several recent disciplinary decisions" as the basis for the proposed rules, PSA does not believe that these isolated instances of alleged misconduct are sufficient to justify the introduction of additional substantive regulations setting forth extensive and detailed requirements governing the content of such communications.

***B. The Application of the Specific Requirements of Rule 2210 Would be Inappropriate for Most Individual Customer Communications and Would Inhibit the Use of Electronic Communications Media***

Rule 2210 was developed to address mass forms of communications with the public such as advertising and sales literature, and not individual correspondence. Since the purpose, preparation and substantive content of each of these types of communications differ significantly, the application of certain provisions of Rule 2210 would be inappropriate in the case of most correspondence prepared for a single customer. This is especially true of e-mail and other forms of electronic communications which, because of their largely informal nature, are often more akin to oral communications than more formal, written correspondence.

Under the proposal, all correspondence would be required to contain the name of the person or firm preparing the material, if other than the member, and the date on which the material was first published, circulated or distributed. Any communication deemed to constitute a "recommendation" would obligate members to identify whether they usually make a market in the subject security, any ownership of options, rights or warrants to purchase the security that the member may have, and certain other information. In addition, a variety of specific, detailed requirements would apply to the use and

disclosure of the member firm's name. PSA believes that these detailed content requirements are inappropriate for most forms of communications prepared for individual customers.

Unlike sales literature and advertisements, electronic correspondence often takes the form of an ongoing dialogue between two parties, involving the exchange of multiple messages. If the specific content requirements of Rule 2210 were made applicable to all such communications, member firms would be required to repeat large amounts of information in each message. To insure compliance, firms would most likely develop boilerplate language or disclaimers for all communications prepared for use with a single customer. However, members may be restricted in their ability to incorporate such information in correspondence generated via electronic communications systems-especially, proprietary third-party systems-due to space constraints, field formats and other variables beyond their control.

It is particularly ironic that the proposed rule would require communications with single customers to include a variety of specific information and data, while simultaneously cautioning members to bear in mind the overall context in which a statement is made, and the overall clarity of the communication. For example, proposed language in paragraph (d)(1)(D)(iii) of Rule 2210 specifically notes that "[a] complex or overly technical explanation may be more confusing than too little information." However, the proposed rules could prevent member firms from exercising their judgment in such situations, and from tailoring the specific content of a communication in a manner that is most directly responsive to the customer's information needs.

Ultimately, customers who ostensibly are protected by this rule would suffer from its application. Instead of receiving clear, timely and succinct information from member firms (including responses to their direct questions or inquiries) customers would have to wade through a variety of disclaimers, extraneous references, and irrelevant and duplicative information that they neither requested nor care to receive. Timeliness and responsiveness of communication, which are principal advantages of electronic media, would also be impeded by the proposed rule. Significant time and effort will be required to ensure that each and every piece of correspondence with a customer fully complies with the specific content requirements of paragraphs (d) and (f) of proposed Rule 2210. For example, when transmitting statistical tables and charts, considerable effort and expense may be required to identify, verify and disclose sources and other required details prior to transmission. The ultimate effect of these requirements may be to inhibit the use of electronic and other types of communications with individual customers, and thereby deny both members and their customers the benefits and efficiencies such communications can provide.

### **III. CONCLUSION**

For the foregoing reasons, PSA strongly urges NASDR to withdraw the rule amendments proposed in RFC 97-37. Alternatively, and at a minimum, PSA recommends that the proposal be modified to indicate that only the general (but not the specific) requirements

of paragraphs (d) and (f) of Rule 2210 be made applicable to communications prepared for delivery to a single current or prospective customer.

PSA appreciates the opportunity to provide the views expressed herein. Should you have any questions or desire any clarification of the issues discussed in this letter, please contact the undersigned at (212) 440-9403, or Paul Saltzman, PSA Senior Vice President and General Counsel, at (212) 440-9459.

Sincerely,

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<sup>1</sup> PSA represents approximately 220 securities firms and banks that underwrite, trade and sell debt securities, both domestically and internationally. PSA's member firms account for in excess of 95% of all primary issuance and secondary trading activity in the domestic debt capital markets. More information about PSA can be obtained from website at <http://www.psa.com>.

<sup>2</sup> See SEC Release No. 34-38548, 62 Fed. Reg. 24147 (May 2, 1997).

<sup>3</sup> See PSA letter dated June 3, 1997 to Mr. Jonathan G. Katz, concerning Proposed Rule Change by NASD Regulation, Inc. to NASD Conduct Rules 3010 and 3110 (File No. SR-NASD-97-24).