Securities Industry Association
120 Broadway - 35 Fl. • New York, NY 10271-0080 • (212) 608-1500, Fax (212) 968-0703 • www.sia.com, info@sia.com

May 27, 2005

Barbara Z. Sweeney
NASD
Office of the Corporate Secretary
1735 K Street, NW
Washington, D.C. 20006-1500

Re: Pre-Use Filing of Advertisements and Sales Literature for New Types of Securities and of Television, Video and Radio Advertisements -- NASD Notice to Members 05-25

Dear Ms. Sweeney:

The Securities Industry Association ("SIA")[1] is pleased to provide comments on Notice to Members 05-25 ("Notice"), which proposes to amend NASD's advertising rules to require members to file with NASD certain additional categories of advertisements and sales literature prior to first use ("Rule Proposal"). Specifically, the proposed changes would significantly expand NASD Rule 2210(c) by requiring member firms to file, prior to first use: (i) all television, video, and radio broadcasts that are 15 seconds or more ("Broadcast Amendments"); and (ii) advertisements and sales literature relating to new products ("New Product Amendments").

I. Executive Summary

SIA fully supports NASD staff's efforts to learn of new industry products and simultaneously halt potentially problematic advertisements in advance of dissemination to the public. We are deeply concerned, however, with the breadth and efficacy of the Rule Proposal. In particular, we believe that the proposed pre-filing requirements fail to fully appreciate the impact on NASD resources, likely delays in approval, and potential adverse financial and competitive impact on member firms. For the reasons we address below, we strongly believe the Broadcast Amendments and the New Product Amendments, as proposed, would result in a tremendous expansion of regulatory review

[1] The Securities Industry Association brings together the shared interests of more than 550 securities firms to accomplish common goals. SIA's primary mission is to build and maintain public trust and confidence in the securities markets. At its core: Commitment to Clarity, a commitment to openness and understanding as the guiding principles for all interactions between investors and the firms that serve them. SIA members (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. According to the Bureau of Labor Statistics, the U.S. securities industry employs nearly 800,000 individuals, and its personnel manage the accounts of nearly 93-million investors directly and indirectly through corporate, thrift, and pension plans. In 2004, the industry generated an estimated $227.5 billion in domestic revenue and $305 billion in global revenues. (More information about SIA is available at: www.sia.com.)

that is inappropriate, unnecessary, and potentially disadvantageous to investors. SIA, therefore, urges NASD to reconsider additional rule-making and instead use and enforce existing regulatory tools, including authority under Conduct Rule 2210(c)(5), to address issues that arise with regard to specific violations.[2] Such a case-by-case determination is more suitable and efficient than imposing additional burdens on all member firms.

II. Pre-Filing of Television, Video and Radio Broadcasts

As proposed, the Broadcast Amendments require member firms to pre-file with NASD, at least 10-days prior to first use, all television, radio and video (including Web videos) broadcasts that are 15 seconds or longer, and to also file the final broadcast within 10-days after first use. NASD permits firms to file storyboards but prohibits firms from broadcasting the final advertisements "until changes specified by the [NASD Advertising Regulation] Department have been made." Notably, other than a brief reference to regulatory concerns "several years ago" with certain day trading and electronic brokerage television advertisements, the Notice offers no empirical or compelling policy reason in support of a regulatory pre-screening and approval process for *all member firm broadcast communications.*[3] Also lacking is any cost-benefit analysis, impact statement or discussion of how NASD intends to staff and fund the mushrooming expense that would be associated with this greatly expanded review and approval procedure.

A. The Proposed Rule is Unnecessary, Overbroad, and Resource Inefficient

SIA believes that the Broadcast Amendments are unnecessary and impractical in view of existing regulatory safeguards that ensure broadcast communications are fair, balanced and in compliance with applicable advertising standards. Under the current regulatory infrastructure, advertisements are subject to multiple layers of scrutiny both before and after dissemination. These include principal review and pre-approval procedures, regulatory oversight by the NASD and SEC through routine and special examination programs, and internal reviews – all of which protect investors against potentially abusive advertising practices. In light of this regulatory framework, SIA sees little value being added from "shot-gun" rules that impose onerous and costly filing obligations on *all* member firms for *all* television, radio and video broadcasts, especially when there is no evidence of industry-wide abuse in advertising compliance.[4]

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[2] Conduct Rule 2210(c)(5) requires member firms to pre-file any and all advertisements and/or sales literature in cases where NASD determines there is cause to do so.

[3] Although NASD utilizes a 15-second threshold, our members advise us that virtually all member firm broadcasts are 15 seconds or greater.

[4] We also note that the Broadcast Amendments sweep in almost all categories of firm broadcasts and make no distinctions based on content or whether the advertisements present fairly low regulatory risk. For example, the new rules would capture generic corporate advertising that contains no product or performance information, internal production broadcasts aimed at employees and existing customers, as well as time-sensitive single use broadcasts that express market commentary. To the extent NASD decides

We are especially troubled by the sheer volume of advertisements affected and considerable resources needed to manage a pre-approval process for all television, radio and video broadcasts for all 5,200 NASD member firms.[5] While the full impact is not yet known, we are certain that the rule proposal would result in a palpable strain on limited regulatory resources, a result that ultimately will diminish, rather than enhance, the quality of regulatory oversight. SIA, therefore, respectfully suggests that investor protection is far better served by allocating NASD staffing and financial resources to other purposes.

Similarly, a pre-filing requirement would force firms to devote considerable time, effort and staffing resources to negotiate comments with NASD staff, often on matters that are highly creative and subjective in nature. Moreover, because advertising is expensive and involves months of planning, interjecting NASD staff in the late stages of production will either delay deployment of advertising (at significant added cost) or cause firms to procure less favorable, more expensive time-slots.[6] This is of particular concern for television commercials, which involve tight production schedules and considerable up-front cost commitments.

The delays associated with a pre-approval standard are further exacerbated due to the already existing backlog of filings under the current system. Today, the NASD review process for regular filings averages 4 to 8 weeks. Requests for expedited review average 3-5 business days and are often denied due to lack of NASD resources. Faced with certain further delays, we fear that firms will curtail legitimate advertising practices simply to avoid the costs and practical difficulties of the new rules. In light of the forgoing, SIA urges NASD to withdraw the Broadcast Amendments and instead utilize existing regulatory tools, including possible enforcement action, to address issues that arise with regard to specific violations.

III. New Product Sales Materials

NASD also seeks to amend Rule 2210(c)(4) to impose a pre-use filing requirement on advertisements and sales literature relating to "new types of securities that a member has not previously offered." Firms must file the new product marketing materials at least 10 business days prior to first use and continue to file with NASD for 90 days following the initial filing. The Notice explains that this amendment is intended

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to proceed with the Broadcast Amendments, we strongly suggest that NASD specifically carve out from any filing requirement these types of broadcasts, among others.

[5] SIA recognizes that not all 5200 NASD member firms will experience the same percentage increase. There is little doubt, however, that NASD Advertising Regulation Department will face an exponential increase in new filings, many of which fail to raise any issues of regulatory significance.

[6] A pre-approval requirement may cause firms to purchase "Network and Cable Scatter," which is far more expensive and of limited value and availability.

to alert NASD to new products intended for retail investors prior to publication of the marketing material, thereby affording NASD more time to address any sales practice issues that the new type of security presents. The amendment also would enable the NASD Advertising Regulation Department ("Department") to review "launch" material for products that a firm has not previously offered that may present significant compliance issues under the current marketing rules.

A. Pre-Use Filing of New Product Marketing Materials May be Premature and Excessive in Light of Recent Guidance on New Product Review

SIA shares NASD's goals of fostering better oversight of new products offered to retail customers. We seriously question, however, whether expansions to NASD's advertising and sales literature rules are the most appropriate and efficient mechanism for NASD to monitor and regulate the introduction of new products. Indeed, the proposed pre-use filing requirement may be premature in light of the recently adopted NASD Best Practices for Reviewing New Products ("Best Practices").[7] Among other things, the Best Practices urge member firms to take a proactive approach to reviewing and improving their procedures for developing and vetting new products before they are introduced to the public.[8] Since NASD only recently issued the Best Practices, and it does not appear that NASD has identified any industry-wide sales practice concerns in the area of new product advertising, we strongly recommend that NASD not consider a pre-use filing obligation at this time. Instead, a more prudent approach may be to permit firms to adopt robust procedures around new products pursuant to the Best Practices and address any product or firm-specific issues as they arise. In any event, we believe the New Products Proposal is flawed on several fronts and requires further consideration and modification.

B. A Pre-Use Filing Standard is Overbroad, Costly, and Fails to Achieve NASD's Stated Objectives

As stated in the Notice, pre-use filing is designed to "provide NASD with more time to address any sales practice issues" that new types of securities present. SIA believes, however, that review of marketing material by NASD Advertising staff 10 days before first use is not the means to that end. On the contrary, we seriously doubt that NASD Advertising staff would have sufficient time to fully understand and analyze potential *sales practice issues* associated with entirely new types of securities. Due to the diversity and complexity of some new products, we believe that NASD simply may be ill equipped to conduct the requisite review and approval in a timely fashion. In the end, firms will be forced to delay bringing new products or services to the market, which could adversely effect investors and negatively impact member firms.

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[7] NASD Notice to Members 05-26 (April 2005).

[8] In the New Products Best Practices, NASD states that firms' procedures should, among other things: (i) include clear, specific and practical guidelines for determining what constitutes a new product; (ii) ensure that the right questions are asked and answered before a new product is offered for sale; and (iii) provide for post-approval follow-up and review, when appropriate.

This is of particular concern in the area of "non-conventional" investments, such as structured products that may be time sensitive to market movements. The specific terms of a structured note, for example, may change relatively quickly based on market conditions and interest rates. Moreover, because the marketing materials for these types of products often accompany offering documents and are finalized shortly before launching a product, a pre-use filing obligation could significantly disrupt business and delay the launch of a new security, thus potentially missing the market opportunity if conditions change. Alternatively, the New Product Amendments may have the unintended consequence of forcing member firms to avoid producing sales literature for securities that are particularly sensitive to market movements.

Historically, pre-use filing has been reserved for particular products where there was evidence of abuse, a propensity to mislead investors, or a lack of industry experience.[9] The New Product Amendments, on the other hand, capture all new product marketing materials *irrespective of:* the nature or complexity of the product or feature; public familiarity with the product or feature; the particular firm's prior advertising experience and/or compliance history; or the existence of any potential sales practice abuses (industry-wide or firm-specific) in connection with the particular product or feature.

Consequently, under the proposal, even if the marketing materials involve a fairly "conventional" product or feature that has been widely marketed by various other financial institutions, the firm would nevertheless have to pre-file the materials with NASD. Under such circumstances, NASD pre-approval provides nominal benefit and potentially could impede a member firm's ability to offer advantageous products to customers. SIA, therefore, respectfully requests that NASD withdraw the New Product Amendments as well.

C. A Post-Use Filing Standard Better Accomplishes NASD's Important Objectives Without Producing the Disadvantages of the Current Proposal

While SIA opposes any additional filing obligations for new product marketing materials, to the extent NASD determines that a filing regime is warranted, we believe that a limited, *post-use* filing standard pursuant to Rule 2210(c)(2) is more practical and equally effective in providing NASD with timely notice of a new industry product. Unlike the current proposal, our suggested alternative would provide NASD with sufficient time to conduct a more deliberative and analytical review without negatively impacting member firms' ability to bring new securities to the market. Under all circumstances, NASD should be more precise in defining what types of securities it envisions would be subject to additional regulation since the current proposal is extremely vague. Further, as described below, we recommend that NASD specifically exclude certain types of new product marketing materials from any filing requirements.

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[9] Products subject to current pre-use filing requirements include fund-created rankings, bond fund volatility ratings, collateralized mortgage obligations and securities futures.

D. The Term "New Types of Securities" Requires Further Clarification

As proposed, the New Product Amendments offer very little guidance as to what is meant by "a type of security that the member has not previously offered" or "new categories of investments that the member has not previously offered." Absent specific NASD guidance, the proposal potentially subjects new securities developed by member firms to merit regulation by NASD analysts who may not have sufficient expertise or resources to review and approve sales materials in a timely fashion. For this reason, we recommend that NASD specifically identify those types of securities that would be subject to additional filing requirements.

Furthermore, and consistent with NASD's focus on new product marketing materials targeting retail customers, we also recommend that NASD exclude altogether certain categories of marketing materials from filing (whether pre-use or within 10 days of first use or publication). These include marketing materials (i) directed at clients that qualify as accredited investors; and (ii) regarding unique, tailored products that are customized for particular customers.[10] Notably, we do not suggest that the foregoing categories of advertising and sales literature be excluded from the application of the Rule 2210. All such materials would still be subject to the content standards and other provisions of Rule 2210, including principal review and NASD spot check procedures.

We also recommend that NASD further narrowly define "new types of securities" so as to tie the definition to the overall investment characteristics of the security, as opposed to its specific terms. In this regard, NASD should be clear that changing terms of an existing product should not constitute a "new type of security." For example, the "non-conventional" securities referenced in the Notice can have various features and terms and, in some cases, are customized for particular customers. We do not believe that firms should be subjected to an additional filing requirement simply because the terms of a particular security vary from current offerings.[11] In that regard, it may be helpful for NASD to provide additional specific examples of securities that would be impacted by this proposal.

Finally, we suggest that NASD provide member firms with sufficient flexibility in defining a new type of security. While we recognize that this approach may be more difficult for NASD to administer and regulate, the diversity of NASD member firms warrants flexibility since many firms define "new type of security" differently based

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[10] While we recognize that an accredited investor standard is not necessarily a proxy for sophistication, customized securities and private placements are not generally considered products made available to "retail" investors. Our suggested approach is also consistent with NASD's efforts to modernize NASD's advertising rules. (See NASD Notice to Members 03-38 (July 2003).

[11] For example, a structured note may have various terms (*e.g.*, the length of the note, whether it is principal protected, the underlying index, currency, commodity or reference price to which the price of the security is tied, whether the note pays interest, or has knock-out options, etc.). We do not believe that a structured note that is tied to the performance of the S&P 500 Index should be subject to NASD filing requirements if the member firm already offers structured notes tied to a basket of securities in another broad-based index.

upon the firm size, business model, complexity of products offered and client mix. In this regard, member firms may decide to define as "new types of securities" those investments that are subject to review by a firm's new products committee[12] or otherwise would require an application for a proposed business expansion under Rule 1017.

IV. Conclusion

We thank NASD for the opportunity to comment on the Rule Proposal. We appreciate NASD's efforts to review and resolve potential regulatory concerns with member firm advertisements and sales literature prior to dissemination to the public. On balance, however, the burdens associated with the Rule Proposal greatly outweigh the intended public benefits. SIA therefore respectfully requests that NASD reconsider and modify the Rule Proposal as recommended herein. We welcome the opportunity to assemble a working group representing practitioners from a cross section of firms to assist NASD staff in exploring any or all of the issues discussed in this comment letter.

Any questions regarding this letter may be directed to the undersigned or Amal Aly, SIA Vice President and Associate General Counsel, at (212) 618-0568.

Very truly yours,

Ira Hammerman
Senior Vice President & General Counsel

cc: Mary Schapiro, Vice Chairman & President, Regulatory Policy & Oversight
Elisse Walter, Executive Vice President, Regulatory Policy & Oversight
Marc Menchel, Executive Vice President, General Counsel

[12] This would carve-out, of course, those products that are sent through a new products committee for operational, financial or technological reasons unrelated to the investment characteristics of the security.