WHITE & CASE

Client**Alert**

Capital Markets

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FINRA Amends Rules Related to Research Analysts and Reports Pursuant to the JOBS Act

On October 11, 2012, the Securities and Exchange Commission ("SEC") published a rule amendment from the Financial Industry Regulatory Authority, Inc. ("FINRA") to amend NASD Rule 2711 and Incorporated NYSE Rule 472 to conform to the Jumpstart Our Business Startups Act (the "JOBS Act"). Consistent with the policies underlying the JOBS Act to encourage Emerging Growth Companies ("EGCs") to raise capital and pursue initial public offerings, the rules (i) reduce restrictions related to communication between EGCs and research analysts at investment banks and (ii) eliminate the research quiet period after an EGC's IPO or secondary offering.[1]

The rule amendments described in this Client Alert are effective immediately with retroactive effect to April 5, 2012. The only exception to retroactive implementation is with respect to the termination of the restriction on publishing research for ten days after a secondary offering by an EGC and on publishing research during the 15 days following the termination of a lock-up agreement related to an EGC. These changes, discussed below in more detail, are only effective as of October 11, 2012 since these were not mandated by the JOBS Act.

Communication Between Research Analysts and EGCs

Participation in Pitches to EGCs

NASD Rule 2711(c)(4) and NYSE Rule 472(b)(5) contained a blanket prohibition on research analysts participating in efforts to solicit investment banking business including, among other things, participating in any pitches for investment banking business to prospective clients. Section 105(b) of the JOBS Act amended Section 15D of the Securities and Exchange Act of 1934 (the "Exchange Act") to prohibit the adoption by the SEC or any national securities association[2] of any rules or regulations that, in connection with an IPO of an EGC, would restrict research analysts from participating in meetings with the management of an EGC that are also attended by other persons associated with a broker-dealer that are not research analysts (e.g., investment bankers).

1 The term "secondary offering" is understood to also include an offering that is a "follow-on" offering (e.g., an offering following an IPO that only includes primary shares).

2 The term "national securities association" covers FINRA but not the New York Stock Exchange. The SEC clarified in its Frequently Asked Questions published August 22, 2012 (the "FAQs") that Section 105(b) and (d) were intended to apply to NYSE Rule 472 to the same extent as NASD Rule 2711.

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The amendments to NASD Rule 2711 and NYSE Rule 472 align these rules with amended Section 15D by specifically allowing research analysts to attend pitch meetings attended by investment bankers in connection with an IPO of an EGC. However, consistent with the guidance provided by the SEC Staff in the FAQs,[3] the amendments prohibit a research analyst from engaging in otherwise prohibited conduct, including efforts to otherwise solicit investment banking business. The SEC gave the example that research analysts could attend pitches to EGCs with investment bankers and, for example, introduce themselves, outline their research program and ask management questions. However, the continuing prohibition on soliciting business means that attendance of research analysts at pitches still involves significant risks, and it may well be advisable for research analysts not to participate in all portions of a pitch.

The amendments do not address the Global Settlement entered into in 2003, and amended in 2010, among the SEC, self-regulatory organizations, other regulators and a dozen major investment banks to address conflicts of interest between the banks' research and investment banking functions (the "Global Settlement"). Notwithstanding the amendments, investment banks subject to the Global Settlement must continue to create and enforce firewalls between research and investment banking personnel designed to prohibit all communications between the two except where permitted by the Global Settlement. As a result, research and investment banking personnel at banks subject to the Global Settlement will not be able to participate in pitches. Research personnel may provide their views on a potential transaction or candidate for a potential transaction in accordance with the procedures set forth in the Global Settlement.

Other Interactions With Research Analysts

Section 105(b) of the JOBS Act amended Section 15D of the Exchange Act to prohibit the adoption by the SEC or any national securities association of any rules or regulations that, in connection with an IPO of an EGC, would restrict investment bankers from arranging for communications between an analyst and a potential investor. The SEC confirmed in its FAQs that an investment banker may forward a list of potential investors to an analyst for that analyst to contact at his or her discretion. An analyst may also forward a list of potential investors that he or she plans to contact to an investment banker for scheduling purposes. These largely ministerial acts will not be considered violations of NASD Rule 2711(c)(6) or NYSE Rule 472(b)(6)(ii), which prohibit investment bankers from directing analysts to engage in sales or marketing efforts. FINRA has not made any change to its rules since the rules do not currently prohibit this type of activity. It should be noted, however, that investment banks that are subject to the Global Settlement must continue to create and enforce firewalls between research and investment banking personnel designed to prohibit all communications between the two except where permitted by the Global Settlement.

It should be noted that since the JOBS Act does not expressly address communications where investors are present together with company management, analysts and investment banking personnel, the SEC has taken the position in its FAQs that the JOBS Act does not affect NASD and NYSE rules prohibiting analysts from participating in roadshows or otherwise engaging in communications with customers about an investment banking transaction in the presence of investment bankers or the company's management.

Publication of Research Reports

NASD Rule 2711(f) and NYSE Rule 472(f) prohibited investment banks that act as managers or co-managers for registered public offerings from publishing research reports on the issuer, other than reports concerning the effects of significant news or events on the issuer, for 40 days in the case of an IPO and 10 days in the case of a secondary offering. In addition, the rules prohibited underwriters from publishing research reports concerning an issuer for 15 days prior to or after the expiration, waiver or termination of any lock-up agreement that the underwriter entered into with the issuer or its shareholders (subject only to a limited exception for reports concerning the effects of significant news or events on the issuer).

Section 105(d) of the JOBS Act expressly permits publication of research regarding an EGC any time after the IPO of an EGC or prior to the expiration of any lock-up agreement. In the FAQs, the SEC Staff clarified that such provision also applied to the waiver or termination of any lock-up agreement. The Staff further added that, even though the JOBS Act does not reference quiet periods for secondary offerings, the Staff believes the policies underlying the JOBS Act are equally applicable to quiet periods related to secondary offerings by EGCs.

The amendments to NASD Rule 2711 and NYSE Rule 472 carve EGCs out of the rules, allowing investment banks that act as underwriters for IPOs or secondary offerings by EGCs, or which enter into lock-up agreements in relation to such offerings, to publish research reports at any time after the offering, or before or after the expiration, waiver or termination of lock-up agreements in connection with the offering.

3 For a discussion of the FAQs, please see our *Client Alert* from August 2012 available at http://www.whitecase.com/alerts-08292012/.

The impact of the JOBS Act and rule amendments on research quiet periods is as follows:

- In reliance on the JOBS Act, underwriters have generally taken the position that they may commence publication of research 25 days after the effective date of the registration statement for an IPO. Underwriters have not been comfortable shortening this period any further since they do not want to publish research during the 25-day prospectus delivery period following an IPO under Rule 174 promulgated under the Securities Act of 1933 (the "Securities Act"). The amendments support this practice and are unlikely to result in any further changes to current practices.
- The amendments leave open the question of whether there is any restriction under the Securities Act regarding the publication of research with respect to an EGC. Section 105(d) prohibits the SEC and FINRA from adopting any rule that restricts the publication of research "within any prescribed period of time following the initial public offering date of the emerging growth company." Before the enactment of the JOBS Act, an investment bank could not publish research regarding a company that was not Rule 139-eligible after the company was "in registration." This meant that secondary offerings by such companies often required careful timing in order to enable the publication of research and the launch of an offering following the release of quarterly earnings. Section 105(d) appears to trump any prohibition on an investment bank from publishing research both before and after any secondary offering by an EGC (provided the analyst has not been brought over the wall with respect to the offering).
- The amendments eliminate the need to include "booster shot" language in lock-up agreements used in IPOs and secondary offerings by EGCs. The amendments leave open the question of whether the research blackout rules reenter into effect for an EGC that loses its status between the date of the offering and the termination of any lock-up agreement. We believe that the better argument is that they do not because the amendments refer to the blackout rules not applying to an offering of "the securities of an Emerging Growth Company."

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