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NASAA

March 10, 2003

Jonathan Katz
Secretary
United States Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549-0609

Re: Release No. 34-47110; File Nos. SR-NASD-2002-154; SR-NYSE-2002-49 - Research Analyst Conflicts of Interest (Amendments)

Dear Mr. Katz:

Please accept this letter from the North American Securities Administrators Association, Inc. (NASAA)[1] in response to the above-referenced Release relating to Research Analyst Conflicts of Interest.

On May 10, 2002, the Securities and Exchange Commission (the "Commission") approved amendments to New York Stock Exchange ("NYSE") Rules 472 and 351 and new NASD Rule 2711. These amendments changed the manner in which firms' investment-banking departments and research analysts manage and disclose conflicts of interest between their investment banking and research activities. In NASAA's April 18, 2002 letter to the Commission, we supported this effort and offered some suggestions that we thought would assist the SROs in encouraging firms to issue objective research reports.

The NASD and NYSE now issue these proposed amendments to incorporate some of NASAA's and other commentators' suggestions and reflect the findings of the SEC, SROs and state regulators in their inquiries into research analyst activity at firms. These proposed amendments also implement some, but not all, of the requirements of the Sarbanes Oxley Act of 2002.

[1] The oldest international organization devoted to investor protection, the North American Securities Administrators, Inc. was organized in 1919. Its membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico and Puerto Rico. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

We applaud the SROs in both the substance of the amendments to the rules and in the process the SROs followed in proposing these amendments. We think this is an example of how rulemaking should work. The SROs sought and acquired information from a variety of sources, including the results of investigations into research practices of investment banks by state and federal regulators, academia, industry and other interested groups. The SROs then compiled this data and issued the proposed amendments on which the Commission now seeks comment.

The following are NASAA's comments on the proposed amendments offered by the SROs. The comments apply to both the NYSE and NASD rules, as they are substantially similar in content.

Ban on Analysts Communicating with Potential Clients Prior to Engaging Analyst's Employer as an Underwriter for IPOs[2]

Information uncovered by the state regulators, the SEC, and the SROs provided evidence that the practice of analysts participating in promotional events to sell underwritings was widespread. It is clear that one of the job responsibilities of an analyst was to assist the investment banking division to win clients for the firm by implying that research on the issuer would be favorable if they chose the analyst's firm to perform securities work for the issuer.

We support the proposed amendments to the rules which will result in the prohibition of a significant amount of this "pitch" activity. The rules will prohibit an analyst from issuing a report or making a public appearance to discuss the company if that analyst communicated with that company in an effort to solicit investment banking business prior to the company hiring the analyst's employer as the underwriter for the company's IPO.

The rules, however, should be expanded to cover all securities work done by the firm for the company, not only IPO work. The state investigations showed that the pitch activity was used to influence companies to hire the firm to underwrite a secondary offering and perform other investment-banking services including private placement work. We think this type of pitch activity should be prohibited regardless of whether the firm is trying to solicit business to underwrite an IPO or a secondary offering. The rules should prohibit analysts from offering the promise of continued positive reports in return for any type of future investment banking business.

Prevention of Booster Shots[3]

Firms often issued favorable reports on a company for which it had performed investment-banking services, just prior to or after, the lock-up period for the IPO ended. Insiders of the issuer generally are prohibited from selling shares of stock they own in a company until a certain date has passed (the "lock-up period"), after which they may sell their shares on the secondary market. In our April 18, 2002 letter, we requested that rules be put in place to stop the

[2] See NYSE proposed amendment to Rule 472(b)(4) and NASD proposed amendment to Rule 2711(c)(4).
[3] See NYSE proposed amendments to Rule 472(f)(5) and NASD proposed amendments to Rule 2711(f)(e).

practice of firms issuing favorable reports on a company proximate to the date the lock-up period expires. The favorable report would cause the issuer's stock to rise and allow the insiders to sell stock at a premium. Regulators fear that the reports were being issued as pay back to the insiders for hiring the firm to perform investment-banking services.

We support the proposed amendments to the rules because they prohibit booster shot activity by barring firms who participated in the underwriting, from issuing reports within fifteen days before or after the lock-up period ends. The proposed rules provide an exception for issuing reports based upon the occurrence of significant news. We suggest that the SEC and SROs closely monitor this exception to see that this exception is not used for the purposes of evading the rules. We also believe that the fifteen-day period may not be long enough and as we previously suggested, the prohibition should be increased to thirty days before and after the lock-up period ends.

Notice Requirement for Discontinuing Coverage[4]

NASAA supports the addition of rules requiring firms to provide a notice of withdrawal when the firm discontinues coverage of an issuer. The recent inquiries into the firms indicate that firms may threaten to discontinue coverage on an issuer if the issuer does not hire the investment banking division of the firm to perform services for the issuer. The proposed amendment to the rule should also require that the firm file a report when it discontinues coverage on an issuer explaining the reason(s) the firm decided to terminate coverage.

Definitions[5]

In our April 18, 2002 letter, we expressed a concern that some of the definitions excluded too many employees of firms from the rules' purview, which limited their effectiveness. The proposed amendments to the definitions address most, but not all, of our concerns. For example, the proposed definition of "Research Analysts" picks up research directors, supervisory analysts and other committee members as being subject to the rules relating to research analysts. While this definition is an improvement to the definition currently in place, it does not completely capture our previous suggestions. We continue to believe that all associated persons who are afforded a public forum to offer opinions about the future performance of company stock should be covered by the rules without regard to the regularity or media used for that opinion.

We think that when any employee of a firm speaks publicly about the future performance of a company she is doing so with the express or tacit consent of that firm. By allowing that person to speak publicly, the firm has approved this person to provide analysis. This person should therefore be subject to the same disclosure requirements that are applied to the specific people currently within the definition of "Research Analysts." Corporate titles should not alone save a person from the rules' application.

[4] See NYSE proposed amendment to Rule 472(f)(5) and NASD proposed amendment to Rule 2711(f)(4).
[5] See NYSE proposed amendments to Rules 472.10 – 472.50 and NASD proposed amendments to Rule 2711(a).

Registration, Continuing Education and Exam Requirements[6]

NASAA supports the addition of rules requiring analysts to pass exams assuring that the individuals have some basic competency to provide analysis. Registration is an effective tool to assure that the analysts pass the required exam. The exam and registration requirements are also consistent with other broker dealer regulations. For example, a stockbroker who advises a retail customer to buy or sell stock must pass an exam and apply for registration. It is good regulation also to require an analyst who writes a report that a retail customer may use in deciding whether to buy, not buy, sell, or not sell a stock to be at least as qualified and knowledgeable as a stockbroker.

NASAA also supports having analysts participate in a continuing education program. The NYSE correctly observes in the Release that "Continuing Education Programs would place an obligation on members and member organizations to ensure that they are receiving the requisite ethics and professional responsibility training that NYSE believes they will require to properly conduct their duties as analysts." We think, however, that ethics and professional responsibility training should apply to all individuals employed by the firm who make policy and advise on conflict of interest issues, including for example, the investment banking managers, the CEO, and the General Counsel.

Forms of Compensation[7]

As we advocated previously, the proposals prohibit compensation to an analyst, regardless of the form of compensation, based upon a specific investment banking transaction. This is a natural and correlative principle, which flows from the rationale for all of these rule proposals. Additionally, a firm should be prohibited from formulating or conditioning a research result based upon the receipt of business or compensation from a subject company.

The proposed amendments, which detail a list of things the compensation committee must consider when compensating an analyst, should assist the firms in their efforts to promote unbiased coverage of an issuer. The SROs should be careful to provide notice that if a firm adheres to the letter of the proposed guidelines but otherwise compensates analysts for investment banking reasons, the firm will be violating these rules. This principle should also be applied elsewhere in the rules where appropriate.

Retaliating Against an Analyst for Not Issuing a Favorable Report

In our April 18, 2002 letter we urged the NYSE and NASD to adopt anti-retaliation rules which would provide severe penalties for attempts to intimidate or punish analysts for producing negative research reports. Later that year, the Sarbanes Oxley Act was passed requiring the SROs to develop rules "requiring that a broker or dealer and persons employed by a broker or dealer who are involved with investment banking activities may not, directly or indirectly, retaliate against or threaten to retaliate against any securities analyst employed by that broker or dealer or its affiliates as a result of an adverse, negative, or otherwise unfavorable research report

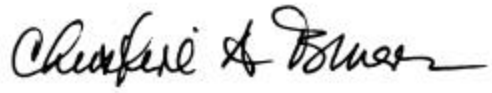
[6] See NYSE proposed amendment to Rules 344, 345A and NASD proposed amendment to Rule 1050 and 1120.
[7] See NYSE proposed amendments to Rule 472(h) and NASD proposed amendments to Rule 2711(d).

that may adversely affect the present or prospective investment banking relationship of the broker or dealer with the issuer that is the subject of the research report, except that such rules may not limit the authority of a broker or dealer to discipline a securities analyst for causes other than such research report in accordance with the policies and procedures of the firm."[8]

We look forward to the SROs crafting rules implementing the ban on retaliating against analysts who issue reports not favorable to a firm's current or prospective clients.

NASAA appreciates the opportunity to offer its findings and opinions to the Commission. The rulemaking process with respect to analyst regulation has moved a long way from its embarkation point. While regulators cannot assure that analysts' recommendations will be right, they can attempt to assure that recommendations are honest.

Sincerely,



Christine Bruenn
President

[8] See Sarbanes Oxley 2002 Section 15D(C). Securities Analysts and Research Reports.