INVITATION TO COMMENT:
Best Practice Guidelines Governing the Analyst/Corporate Issuer Relationship

The Association for Investment Management and Research® (AIMR®) seeks comment on proposed best practice guidelines, set forth below, governing the relationship between analysts and corporate issuers. These guidelines were developed by the AIMR-NIRI Task Force on the Analyst-Issuer Relationship, a joint working group of members of AIMR and the National Investor Relations Institute (NIRI).

Comments must be submitted in writing and be received by AIMR no later than 31 May 2004. AIMR will accept comments submitted electronically and by regular mail or fax. AIMR will consider all comments to be public unless the respondent specifically requests the comments be kept private. All public comments and replies will be posted on the AIMR website (http://www.aimr.org). Comments should be addressed to:

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Executive Summary

Investors benefit when investment professionals, whether analysts or investment managers ("analysts"), have a clear and open dialogue with management of corporations that issue publicly traded debt and equity securities ("corporate issuers"). Open communication facilitates fair and consistent information disclosure by corporate issuers to the market place and allows investors to make sound investment decisions and allocate their capital appropriately.

AIMR and NIRI convened a joint task force (Task Force) to develop best practices guidelines governing the relationship between analysts and corporate issuers to ensure the existence of good channels of communication. In pursuing its objective, the Task Force addressed the following issues:

- Information flow between analysts and corporate issuers,
- Analysts' conduct in preparing and publishing research reports and making investment recommendations,
- Corporate issuers' conduct in providing analysts with access to corporate management,
- Review of analyst reports by corporate issuers, and
- Research that is solicited, paid, or sponsored by the issuer ("issuer paid research").

After careful deliberation over several in-person meetings and conference calls, the Task Force drafted the proposed AIMR-NIRI Best Practice Guidelines (Guidelines) and associated guidance set forth in Appendix A of this Invitation to Comment. AIMR is issuing the proposed Guidelines for a period of public comment until 31 May 2004.

After AIMR members, NIRI members, and other market participants have had ample opportunity to comment on the proposal, the Task Force will review and analyze comments received and consider revisions to the original proposal as appropriate before requesting endorsement and approval by AIMR and NIRI's respective Boards of Governors.

Neither AIMR nor NIRI have the ability to enforce adoption or adherence to the proposed Guidelines on their members. Voluntary compliance by members of AIMR and NIRI, as well as other market participants, would be strongly encouraged but not required by either organization.

Summary of the AIMR-NIRI Best Practice Guidelines

The Task Force recommends that the following guidelines be adopted to govern the relationship between analysts and corporate issuers:

<u>Information Flow.</u> Analysts, investors and corporate issuers must not disrupt or threaten to disrupt the free flow of information between corporate issuers, investors, and analysts in an attempt to inappropriately influence the conduct of others.

<u>Analyst Conduct.</u> Analysts must issue objective research and recommendations, supported by thorough, diligent and appropriate research. Information in analyst reports must be clear and complete; facts should be distinguished from opinion. Analysts must not threaten to use their research reports or recommendations to affect their relationship with corporate issuers.

<u>Corporate Communication and Access.</u> Corporate issuers must:

- Provide access to corporate management to analysts and investors,
- Establish access policies that describes how access to corporate management will be granted and under what circumstances,
- Not discriminate among analysts based on prior research opinions or recommendations, and
- Not attempt to influence research or recommendations by threatening to deny analysts access to company representatives or by exerting pressure on analysts or their firms through other business relationships.

<u>Review of Analyst Reports.</u> Only those portions of an analyst report that do not contain conclusions or recommendations should be reviewed by corporate issuers. Such review should only be done for factual accuracy. Corporate issuers must only comment on historical or forward-looking information that is in the public domain.

Issuer Paid Research. Research must be objective, thorough, and free from bias. Analysts must only accept cash compensation for this research and such compensation must not be contingent on the content or conclusions of the research. Issuer paid research reports must be identified as such and certify that the analysis or recommendations in the report are the true opinion of the analyst. These reports must include disclosures regarding:

- The nature and extent of compensation,
- The analyst credentials,
- The nature and extent of any relationship between the analyst and the corporate issuer, and
- Any other matter which could impair the objectivity of the analyst.

Background

If investors are to make good investment decisions and allocate their capital appropriately, they need transparent information about corporate issuers presented in a fair and consistent manner. Although much of the information about corporate issues comes to investors from the issuers themselves, another important source of investor information is the research reports and investment recommendations prepared and distributed by financial analysts and their firms. In order to conduct high quality research and make recommendations that have reasonable and adequate bases, analysts must communicate directly with company representatives, especially investor relations officers and senior management. Only through such dialogue can analysts fully assimilate and understand the wealth of information in a company's public disclosure documents (e.g., company annual reports).

However, corporate issuers receive requests for information and access from many people, including their shareholders, institutional investors, financial analysts, retail investors, and the media, and cannot be expected to fulfill every request for direct access to specific individuals. Still, one objective of both the analyst and the corporate issuer is the same: to provide investors with thorough, detailed information about the company on which to base their investment decisions. By working together, both analysts and corporate issuers can achieve this goal most effectively.

These interactions between analysts and corporate issuers raise many issues with important implications for investors: Who should be given access to company management? What type of access should be allowed? Should companies differentiate among those seeking access? As long as material, non-public information is not disclosed, should companies limit the type of information available to some while providing more detailed information to others? Is it appropriate for corporate issuers to provide information to only those who make positive comments or recommendations about the company? Is it appropriate for analysts to make negative comments or recommendations if their request for information or access is denied? Should corporate issuers review analyst reports before they are published to insure that all the information contained in the report is correct? If there are no analysts voluntarily covering a particular company, is it appropriate for companies to pay analysts to provide research to the market? Is it appropriate for analysts to accept payment from a company to provide coverage? If so under what circumstances, and what, if any, disclosures should be given to investors about this relationship?

In August, 2003, AIMR and NIRI convened the Task Force, to address these questions. This project was an outgrowth of the previous AIMR project to develop Research Objectivity Standards (AIMR-ROS) and the partnership was authorized by the AIMR Board of Governors based on the NIRI comment letter on the AIMR-ROS proposal.

The Task Force, consisting of 6 AIMR members and CFA charterholders and 8 NIRI members and investor relations specialists, was charged with developing best practices guidelines which could be used to govern the relationship and interactions between analysts and the officers and management of the corporate issuers covered by the analysts. Several of the AIMR Task Force members live and work outside the United States. In addition, the Canadian Investor Relations Institute participated as a non-voting member. Representatives of the U.S. Securities and Exchange Commission, the National Association of Securities Dealers, and the New York Stock Exchange were invited and participated as observers.

Comments Requested

General Comments

AIMR seeks general commentary on the proposals set forth in this document, including, but not limited to, responses to the following questions:

1. Do you support AIMR and NIRI's effort to establish best practices guidelines in this area? Why or why not?

2. Is the language of the proposal sufficiently clear and concise? Is there any ambiguity in terms of the issues or their proposed solutions? How can the clarity and comprehensiveness of the Guidelines be improved?

3. Are there other conduct or ethical issues that arise out of the interactions and relationships between the analyst and the corporate issuer that should be addressed so that the Guidelines are comprehensive? If so, are there recommendations you could make to address these issues?

4. With respect to the issues addressed, do the proposed Guidelines represent "best practices"? If not, how can they be improved?

5. Are any of the proposed Guidelines too strict in that they would be too burdensome or costly for either analysts or corporate issuers to adopt? If so, how should the guidelines be revised so that the benefits exceed the costs? What other modifications, if any, should be made to this proposal?

6. Are the proposed Guidelines globally applicable? Are there non-U.S. issues relating to the analyst-corporate issuer relationship that are not addressed? How should the language or proposals be modified so that non-U.S. analysts and corporate issuers can comply with the Guidelines?

7. Do you think the AIMR-NIRI Best Practice Guidelines will be widely accepted and adopted by analysts and corporate issuers? What can AIMR and NIRI do to encourage their adoption?

Specific Comments:

AIMR seeks comments on the following, specific provisions of the proposal:

1. What other measures could the proposed Guidelines include to discourage discrimination or retaliation by corporate issuers against analysts because of their previous research or recommendations?

2. What other measures could the proposed Guidelines include to discourage analysts from issuing biased research reports as a means to pressure corporate issuers for special access or inside information?

3. The AIMR-NIRI Best Practice Guidelines currently require corporate issuers to adopt access policies and recommend that companies disclose these policies on request. Some argue that, without required written disclosure, corporate issuers have no incentive to apply access policies consistently. Others would say that corporate issuers, concerned about legal liability arising from written disclosure of the access policies, need to have flexibility in deciding whether or not to make such a public disclosure (e.g., on the issuers' websites or in regulatory disclosure documents). Should the proposed Guidelines require corporate issuers to disclose their access policies in writing or should the decision to disclose be the prerogative of the corporate issuer and only verbally upon individual request?

4. What other factors, besides those proposed, should corporate issuers consider when determining to whom to grant access, and under what circumstances?

5. What other elements, besides those proposed, should be included in corporate issuer access policies?

6. Is it appropriate for analysts to request or allow corporate issuers to review their research reports or recommendations, in their entirety, even if issuers are permitted to comment only on factual information?

7. Currently the guidance of the AIMR-NIRI Best Practice Guidelines state that if analysts publicly disclose their earnings models, they should disclose the components that are included and/or excluded from the earnings forecasts and provide an explanation or justification for each inclusion/exclusion. Some argue that disclosure of analysts' earnings models is necessary so that corporate issuers and others can assess whether analysts' earnings estimates are valid and to make an "apples to apples" comparison of those estimates with companies' earnings guidance and/or other analysts' estimates.

Others would say that analysts' earnings models are proprietary information and a critical part of analysts' and their firms' competitive advantage in the marketplace. Is it appropriate for the Guidelines to recommend that analysts disclose a breakdown of their earnings models?

8. Given that many corporate issuers find it difficult to secure analyst coverage, should analysts be permitted to conduct "issuer paid" or "issuer sponsored" research? If so, is it appropriate for the proposed Guidelines to only permit analysts who conduct "issuer paid research" to be paid in cash? Should there be other restrictions on the timing or type of compensation? If other types of compensation should be permitted, how would that compensation be defined or described? Should incentive-based compensation be permitted? If so, would disclosure of such incentive-based compensation arrangements be adequate to alert investors to the potential conflict of interest?

9. What additional disclosures, if any, should be required for issuer paid research?

APPENDIX A:

Best Practices Governing the Analyst/Corporate Issuer Relationship

Standard I: Information Flow

Analysts, Investors, and Corporate Issuers must not disrupt or threaten to disrupt the free flow of information between corporations, investors, and analysts in an attempt to inappropriately influence the behavior of those with whom they are communicating.

Standard II: Analyst Conduct

A. *Analysts must issue objective research and recommendations that have a reasonable and adequate basis supported by thorough, diligent, and appropriate research and investigation.*

B. *Analysts must distinguish between fact and opinion and must ensure that the information contained in their reports is clear and complete.*

C. *Analysts must not bias or threaten to use their research reports or recommendations in an effort to improve their relationship with Corporate Issuers.*

Standard III: Corporate Communication and Access

A. Corporate Issuers must not:

1. *discriminate among recipients of information disclosed by the issuer based on the recipient's prior research, opinions, recommendations, earnings estimates, or conclusions;*
2. *deny or threaten to deny information or access to company representatives in an attempt to influence the research, recommendations, or actions of analysts and investment professionals; or*
3. *attempt to influence the research, recommendations, or actions of analysts or investment professionals by exerting pressure through other business relationships.*

B. *Corporate Issuers must provide access to corporate management, officers, or knowledgeable company officials to qualified persons or entities, including analysts and investors. Corporate Issuers must establish and adhere to policies that set forth how the company will respond to requests for access and under what circumstances and to whom companies will grant access to corporate management and officers. These policies should be disclosed to analysts and investors upon request. The policies should address:*

1. *How the company defines access,*
2. *How the company prioritizes requests for access or information,*
3. *How the company will respond to each request, and,*
4. *Under what circumstances and to whom different types or levels of access will be granted.*

Standard IV: Reviewing Analyst Reports and/or Models

A. *Prior to publication of their reports, Analysts may request that Corporate Issuers review for factual accuracy only those portions of an Analyst's research report that do not contain or disclose conclusions, recommendations, valuations, or price targets.*

B. *Corporate Issuers may review for factual accuracy only those portions of an Analyst's research report that do not contain or disclose the conclusions, recommendations, valuations, or price targets, prior to publication and with the permission of the Analyst. Corporate Issuers must not explicitly or implicitly request information that would disclose the conclusions, recommendations, valuations, or price targets, or comment on these matters. A Corporate Issuer is only permitted to comment on historical or forward-looking information that is in the public domain.*

Standard V: Issuer Paid Research Reports

A. *When engaging in research paid for by the Corporate Issuer, Analysts must:*

1. *Only accept cash compensation for their work and must not accept any compensation contingent on the content or conclusions of the research or the resulting impact on share price.*

2. *Disclose in the report:*

- *The nature and extent of the compensation received for drafting the report.*
- *The nature and extent of any personal, professional, or financial relationship they, their firm or its parent, subsidiaries, agents, or trading entities may have with the subject-company, its personnel, parent, subsidiaries, or agents.*
- *Their credentials, including professional designations and experience that qualifies them to produce the report.*
- *Any matters which could reasonably be expected to impair their objectivity in drafting the report.*

3. *Certify that the analysis or recommendations, if any, contained in the report represent the true opinion of the author or authors.*

B. *When hiring Analysts to produce research for their company, Corporate Issuers must:*

1. *Engage qualified Analysts who are committed to producing objective and thorough research that fully discloses any matters which could reasonably be expected to impair their objectivity.*

2. *Pay for the research in cash and only in a manner that does not influence or seek to influence the content and conclusions of the research.*

3. *Not attempt explicitly or implicitly to influence the research, recommendations, or behavior of Analysts or otherwise pressure Analysts to produce research or recommendations favorable to the Corporate Issuer.*

4. *Ensure that the disclosures required of the analyst in Standard IV(A) are included in the research report, that are published or distributed, in whole or in part, by the Corporate Issuer.*

Guidance for the Standards

Corporate Communication and Access to Company Representatives

Information is the lifeblood of efficient, effective, and fair capital markets. Investors need transparent information that is fairly and consistently disclosed if they are to make good investment decisions and allocate their capital appropriately. Shareholders, investors, and others receive most of the information they need directly from Corporate Issuers: prospectuses, annual financial statements, regulatory filings, proxies, press releases, conference calls, etc. But this wealth of information may raise questions that can only be addressed by dialog with company representatives. Such direct communication or access to company management can include participating in company conference calls, contacting the investor relations officer, or one-on-one meetings with the chief executive or financial officer.

Investors may also rely on various investment professionals, principally financial analysts, to assist them in their investment decision-making process. Financial analysts add value to

investors by sifting through publicly available information; conducting additional market, industry, and company-specific research; performing independent financial analysis; and providing reports on these activities. Although some place more emphasis on the research and analytical process, investors expect financial analysts to draw conclusions about the valuation and future prospects of a company and to make recommendations about whether investors should purchase, sell, maintain, or avoid investing in company securities.

Financial analysts would fail in their due diligence if they did not seek direct communication with company representatives, especially investor relations and other senior management executives to fully understand the information in a company's public disclosure documents (e.g., company annual reports). In order to conduct high quality research and make recommendations with reasonable and adequate bases, financial analysts require such access. Those companies who hold regular telephone or web-based conference calls that allow financial analysts and others to question management directly on past events, current plans, and future prospects have long recognized this need. Every qualified financial analyst ought to be afforded the opportunity to participate fully in telephone or web-based conference calls and other subject-company investor- and analyst-relations activities. It is in the best interest of investors if adequate opportunities are available for raising questions and receiving answers that will help make analysts' research complete. One-on-one meetings with individual or groups of analysts can also help companies develop good working relationships with the investment community and provide a wider dissemination of information about the company to investors at-large.

While qualified financial analysts ought to have equitable access to company representatives, the specific type of access that a company might offer to a particular analyst or other investment professional can depend on company-specific resource constraints. However, to meet the needs of investors and shareholders, companies are advised to provide as much access as possible. Companies demonstrate their commitment to good investor communication by establishing a minimum level of access so that any interested party would be able to obtain some direct communication with company representatives. Minimum levels of access can include:

- annual meetings,
- telephone or email access to a company investor relations officer,
- teleconferences,
- regular meetings with individual and small institutional investors,
- publicly accessible webcasts using freely available internet technology with pre-notification and the opportunity to pose questions.

Assessing the quality of management is a critical aspect of a financial analyst's overall assessment and valuation of a company and requires analysts to develop and maintain an appropriate working relationship with subject-company representatives. Financial analysts can only conduct this assessment by regular interactions with management. Analysts must not use one-on-one discussions with management as an avenue for soliciting or accepting material non-public information. Rather, these meetings are a critical opportunity to ask important questions about results and plans already publicly addressed by the company and assessing management's answers.

In recommending that companies permit financial analysts to have greater access to company management, it is also understood that companies have limited resources. The primary responsibility of company management is to manage the business. Since companies receive information or access requests from many people, including shareholders, institutional investors, financial analysts, retail investors, and the media, they cannot be expected to fulfill every request for direct access to specific corporate officers.

To manage the company efficiently and provide adequate access to important constituencies, however, companies are advised to set clear written policies about who is eligible for access, under what circumstances, and the manner in which requests for access will be prioritized and addressed. These policies will allow financial analysts and others who request access to understand and have realistic expectations about the type and frequency of access that is available to them. Equitable access policies ensure that no analyst has a competitive advantage in talking to management, avoids the perception of favoritism, and diminishes the chance of communication of inside information. Companies should disclose their policies on request so that financial analysts and others can set reasonable expectations for themselves and the company in this regard.

While companies vary widely in size, structure, and methods of handling investor relations, every company is advised to adhere to ethical principles for managing access in a fair, consistent, and efficient manner. Policies must be reasonable and fair and clearly define the different levels of access that are available and set forth the qualifications that persons or entities need to qualify for a particular level of access. Other types of access can include:

- direct contact with senior company management as needed or during regularly scheduled meetings or events,
- direct contact with other company personnel on request,
- one-on-one visits with senior company management on request, and
- access to the company only through contact with Investor Relations officers.

After the levels of access are defined, companies are advised to develop clear criteria for the type of credentials or experience that would qualify individuals (e.g., financial analysts or their employers) to participate at each access level. Although the qualification criteria can be determined by each company, companies might consider the following as part of these criteria:

- whether the individual has a professional credential (e.g. Chartered Financial Analyst® (CFA®) designation),
- level of experience in financial analysis,
- demonstrated knowledge about the company and its sector or sectors,
- quality of previous published research, and
- extent of client base (as a proxy for investment potential).

The weight that companies give to each of the criteria they select will vary depending on the factor or factors a company decides are most important. For example, a company may place a greater emphasis on the level of investment potential than the analyst's experience with the

company. It is recommended that analysts who work for well-recognized research firms be presumed to be qualified and to have legitimate reasons for seeking access.

Companies must apply their access policies consistently and fairly. Once companies establish the criteria they will use for each level of access, it is critical that they do not apply the criteria selectively or deny access to qualified individuals or entities or allow higher levels of access to individuals who do not meet the criteria. After a company discloses and explains its access policy and the reason why a particular level of access is denied, financial analysts are expected not to try to circumvent the policy.

From the company perspective, Corporate Issuers must respect an analyst's duty to ask hard questions, point out potential risks to investors, and to make fair, unbiased assessments based on facts and their own forecasts. Analysts must be free to develop and publish research that is based on sound, competent analysis, even if that opinion is unfavorable or differs from the view of the subject-company. Companies must do their part in providing a transparent and continuing flow of information to the marketplace and accept analysts' right and responsibility to issue varying opinions. Analysts' conclusions will not be positive in every case. But the free flow of information must never be impeded by differences of opinion or issues that involve the relationship between a company and an analyst.

Corporate Issuers must not discriminate against, deny access, or threaten to deny access to any individual or firm based on that individual or firm's opinion, recommendation, earnings estimate, valuation or conclusion about the company or its investment potential. Financial analysts can have many legitimate reasons for offering a negative opinion about a company or its investment potential or to change a previously issued recommendation. Reasons for negative opinions or downgrades of recommendations can range from macroeconomic factors related to the overall economy or the industry to company fundamentals (e.g., changes to its management, restructuring, merger and acquisition activity, competition, product failures, legal issues, natural disasters, overvaluation). The valuation methodology used could also change, altering a company's valuation relative to its peers or to historical metrics. As long as the analyst has a reasonable basis and the opinion or recommendation is supported by adequate research, companies are advised not to challenge the analyst's right to change a rating or recommendation.

Analysts have a responsibility to be skilled and competent in conducting their research – to differentiate between fact and opinion, and to be fair and impartial in their analysis of subject-companies. Analysts must not let outside pressures threaten their impartiality and influence their research conclusions or recommendations. In addition, analysts must understand and respect legitimate constraints on dissemination of information by or access to company personnel. It is inappropriate for analysts to change their rating or recommendation:

- based solely on unsubstantiated rumor or unfounded speculation,
- for reasons related to opinion of other analysts or investors,
- to manipulate the stock price by taking advantage of quiet periods,
- to create an unsubstantiated high earnings estimate to justify a "sell" recommendation,
- to manipulate the stock price in front of stock option expiration dates or quarter-ending trade deadlines, and

- to pressure the issuer to disclose material nonpublic information.

Any change in rating or recommendation should be accompanied by documentation clearly communicating the reasons for the change. All research reports or recommendations must include a certification on the report by the analyst that the content and conclusions are the opinions of the analyst or analysts who authored the report.

Similarly, buy-side analysts and investors must not use their ownership or potential ownership positions in a subject-company to gain preferential treatment with regard to access to company management or material non-public information. For instance, threatening to sell securities or vote against management on a proxy unless the company provides the analyst or investor with exclusive information or access is inappropriate and unfairly puts pressure on the issuer to act in a discriminatory and unethical manner.

Corporate Issuers must avoid direct and indirect pressure on analysts for favorable coverage by threatening to cut off communication with the analysts or deny reasonable access to senior management. Similarly, Corporate Issuers must not pressure investors to vote with management by threatening to withhold access or company information or threatening to withdraw investment banking or trust business from the firm. Companies must not discriminate against those investment professionals who vote against management for reasons unrelated to pressuring the company for special treatment.

Issuer Review of Analyst Reports

The management and investor relations professionals for Corporate Issuers should take special precautions if they are invited or asked to review research reports or earnings generation models prior to publication. Any review must only be done to check factual accuracy of information already in the public domain that is included in the report. While review of the facts may be appropriate, analysts must not provide those sections of the research report that contain the conclusions, recommendations, valuations, or price targets. Otherwise, review or comment on these research reports may be perceived as an attempt by Corporate Issuers to influence the content of the report and the analyst's conclusion, recommendation, valuation, or price target.

Analysts should provide their compliance or legal department a draft research report before sections are shared with the subject company. The compliance department should approve in advance all changes to a research report or recommendation that occur as a consequence of subject-company verification and the analyst should provide written justification for any changes that occur after verification by the subject company. Firms should retain supporting documentation including the original report, the sections shared with the subject company, and any subsequent changes to the report or recommendation.

Extensive review and comment on research reports could expose the company to liability under relevant securities regulations or may be viewed as an endorsement of the report and its conclusions. Issuer representatives should take care not to become "entangled" in an analyst's report. Corporate officials can become entangled when they become so involved in commenting on and/or reviewing an analyst's report that they can be viewed as having agreed with or

endorsed its contents. Issuers can minimize the threat of entanglement by limiting comment or review to discussion or correction of historical fact or other publicly disclosed information.

Best practice is for the issuer to refer analysts to the company's publicly disclosed information so that analysts can pursue further research under the "mosaic" theory. The mosaic theory states that an analyst may use significant conclusions derived from the analysis of public and non-material non-public information as the basis for investment recommendations and decisions even if those conclusions would have been material inside information had they been communicated directly to the analyst by the issuer. Under the mosaic theory, analysts are free to act on this collection, or mosaic, of information.

When reviewing research reports prior to publication, investor relations officers should not comment on changes in earnings projections, investment ratings, or any other information that could materially affect the market price of the issuer's securities. Investor relations officers should treat such reports as they would any other material non-public information.

When preparing research reports and developing valuation models, analysts should clearly distinguish between information that the analyst is attributing directly to management and the analyst's interpretation of comments by management.

Dispute Resolution

In solving disputes with analysts and when negotiating a change to a published research report because the issuer believes: 1) the report contains factual errors or omissions, 2) the analyst's opinions and conclusions are not supported by the facts or 3) the analyst has not been independent and objective, the issuer should:

1. Try initially to get agreement with the analyst on the facts.
2. If the issue cannot be resolved with the analyst, the issuer should discuss any disagreement on the facts with the research director.
3. If the issue is still unresolved, the issuer should discuss the disagreement with the compliance officer when either the research director does not offer assistance or when the research report's recommendation and the analyst's oral communication with clients are not the same.

Issuers, analysts, and investors should not publicly dispute research reports or disagreements or air grievances with research analysts in media outlets. Such behavior is inappropriate and could harm the reputation of the issuer and make it difficult to gain future coverage from other analysts.

Issuer Paid Research

Many companies, seeking increased visibility in the financial markets and with potential investors, hire firms or analysts to produce research reports analyzing their company. However, such issuer paid research is fraught with potential conflicts. Depending upon how the research is written and distributed, investors can be misled into believing that issuer funded research appears

to be from an independent source when, in reality, it is solicited and paid for by the subject-company.

It is critical that research analysts and firms that engage in issuer paid research adhere to strict standards of conduct that govern how the research is to be conducted, what disclosures must be made in the report, and what disclosures must ultimately be made to the investing public.

Analysts who conduct issuer paid research have the same ethical responsibilities as other analysts to engage in thorough, objective, and unbiased analysis and must fully disclose potential conflicts, including the nature of their compensation. Otherwise, they risk misleading investors by appearing to produce objective analysis. Disclosure of the nature and extent of compensation for the report as well as all personal and professional relationships between the issuer and the author of the report is critical to transparency for the investor and maintaining credibility of the research.

Best practice would be for analysts only to accept a flat fee for their work, paid in cash, prior to writing the report, without regard to their conclusions. Any compensation arrangement other than a flat fee is inappropriate as the content and conclusions of the reports could reasonably be expected to be determined or affected by compensation from the subject companies. This can be as direct as payment based on the conclusions of the report or more indirect such as stock warrants or other equity instruments that could increase in value based on positive coverage in the report. In those instances, analysts would have incentive to avoid negative information or conclusions that would diminish their compensation.

Analysts must disclose all matters that have the potential to bias their research including the nature and extent of the compensation they receive for drafting the report and any personal, professional, or financial relationship they or their firm may have with the subject-company. This would include any ownership in the stock or other securities of the company or recent trading activity. It would also be material to investors if the analyst's firm or a related entity provides any investor relations or other service relationship to the issuer. Also, research may not necessarily be paid for directly by an issuer. Research services could be purchased on behalf of the issuer by entities that have the issuer as a client. Any relationship that could reasonably be expected to bias the research must be disclosed. Analysts must also disclose their qualifications, including professional designation and experience, which makes them competent to produce the report. All disclosures must be prominent, be stated in plain language, and communicate the relevant information effectively.

Finally both analysts and issuers must be aware that, in many cases, the content or conclusions of the report itself may be considered material non-public information, especially where no other research coverage of the company is available. Both the analyst and the company should take steps to ensure equitable distribution of the report and consider blackout periods for appropriate periods to avoid insider trading conflicts.

If possible, research firms should designate a supervisory analyst or director of research to approve all research issued by the firm and ensure that the research conforms to these standards.

In sum, issuer paid research generates research coverage for companies not widely followed by the market but, in doing so, creates significant conflicts of interest that must be addressed by strict standards of conduct. Firms and analysts should follow the standards and guidance set forth in this document to address those conflicts of interest generated by issuer paid research and maintain the integrity of the information flowing to the markets.

Guidance for Corporate Issuers Providing Earnings Guidance

Corporate Issuers may choose to provide earnings guidance to analysts and investors. Earnings guidance is considered to be a point estimate, range, revenue estimates or the issuers own earnings model to forecast earnings. If an issuer provides specific earnings guidance in public documents or forums, then it may have a duty to update or correct that information publicly and in a timely manner when facts and circumstances change their forecasts. Material updates or corrections should be made in a news release before being provided to analysts.

Issuers that choose to give earnings guidance are encouraged to provide the following information:

- The components of earnings, including ranges for all key earnings items (e.g., revenues, expenses, gains, losses, margins, earnings per share, etc.)
- A sensitivity analysis, rather than simply an earnings per share forecast.

> *Example: Our projected revenue growth is seven percent to10 percent. Based on our estimated increase of five percent in cost of goods sold, we are projecting gross margins in a range of 50 percent to 55 percent, with the low end of the range based on seven percent revenue growth and the high end based on 10 percent revenue growth. Each one percent variance in revenue growth from our projected range results in an XX percent change in gross margin, all other things being equal. Each one percent variance from our projection in the increase in COGS would result in an XX percent change in gross margin.*

- Comments to the analyst on those items that have been made public that are not included in the research report or earnings generation model.

Issuers that choose not to provide earnings guidance should consider the following:

- Providing and discussing five-year growth rate projections to encourage a long term focus. Issuers should ensure that the growth rates are reasonable over that time period.
- Discussing the issuer's business cycle and its relevance to the current quarter. Pointing out any obvious omission of fact.
- Discussing each quarter's contribution to the company's long term strategies.

Analysts' earnings estimates may not match the earnings guidance provided by Corporate Issuers. If analysts determine to disclose their earnings model, they should disclose the components of earnings that are included and/or excluded from their earnings model and explain why each item is included or excluded.

Examples: Our EPS estimate for 2004 excludes non-operating gains resulting from the sale of assets, which the company has included in its guidance. We have excluded these gains because we believe asset sales are not core to the company's business and ongoing earnings generation power. We have included in our 2004 estimate $0.06 per share attributable to the company's ongoing share repurchase, and $0.02 per share resulting from lower interest rates based on the utilization of the proceeds of the asset sale to reduce debt and buy back stock.

We met with X company management last week where we saw a first-hand demonstration of the company's new product line. Management indicated in its earnings release that it has a goal of achieving 10 percent revenue growth and margin improvement this quarter. We believe the revenue growth goal can be achieved based on recent industry growth, market share trends and the strength of the new line. However, we also believe that price competition will intensify in the next 90 days and that margin improvement will be difficult to achieve.

Conclusion

Corporate Issuers and firms that employ analysts must establish and implement policies that govern the communication between analysts and the subject companies and are aimed at fostering good working relationships. Investors' interests are paramount. Only when Analysts and Corporate Issuers act with integrity and in a cooperative manner, respecting the responsibilities and duties of their respective professions, can an atmosphere conducive to objective research be achieved. Research analysts and corporate officers must put the integrity of their profession, the interests of the investors, and the interests of the capital markets above their own interests.