

**NASAA Investment Adviser Representative Definition**  
**Model Rule USA 2002 102(16)**  
*Adopted 9/17/2008*

**Rule USA 2002 102(16) Investment Adviser Representative (ALTERNATIVE 1)**

- (a) Notwithstanding Section 102(16) of the Act, the term “investment adviser representative” as it applies to a person who is employed by or associated with a federal covered investment adviser only includes an individual who has a “place of business” in this jurisdiction, as that term is defined in rules or regulation promulgated under Section 203A of the Investment Advisers Act of 1940 by the U.S. Securities and Exchange Commission, and who either:
- (1) is an “investment adviser representative” as that term is defined in rules or regulations promulgated under Section 203A of the Investment Advisers Act of 1940 by the U.S. Securities and Exchange Commission; or
  - (2) (A) is not a “supervised person” as that term is defined in rules or regulations promulgated under the Investment Advisers Act of 1940 by the U.S. Securities and Exchange Commission; and  
(B) solicits, offers or negotiates for the sale of or sells investment advisory services on behalf of a federal covered investment adviser.

**Rule USA 2002 102(16) Investment Adviser Representative (ALTERNATIVE 2)**

- (a) Notwithstanding Section 102(16) of the Act, the term “investment adviser representative” as used in the Act and applied to federal covered investment advisers only includes a person who has a “place of business”, as that term is defined in paragraph (b)(4) of this rule, and who either:
- (1) is a “supervised person”, as defined in paragraph (b)(3) of this rule, provided the supervised person:
    - (A) has more than five clients who are natural persons, (other than “excepted persons”, as defined in paragraph (b)(1) of this rule); and
    - (B) more than 10% of whose clients are natural persons (other than “excepted persons” as defined in paragraph (b)(1) of this rule); and
    - (C) (i) on a regular basis solicits, meets with, or otherwise communicates with clients of a federal covered investment adviser; and  
(ii) does not provide only “impersonal investment advice”, as defined in paragraph (b)(2) of this rule; or who
  - (2) (A) is not a “supervised person” as that term is defined in paragraph (b)(3) of this rule; and  
(B) solicits, offers or negotiates for the sale of or sells investment advisory services on behalf of a federal covered investment adviser.
- (b) For purposes of this section:
- (1) “Excepted person” means a natural person who:
    - (A) immediately after entering into the investment advisory contract with the investment adviser has at least \$750,000 under management with the investment adviser; or
    - (B) the investment adviser reasonably believes, immediately prior to entering into the advisory contract, has a net worth (together with assets held jointly with a spouse) at the time the contract is entered into of more than \$1,500,000.

- (2) “Impersonal investment advice” means investment advisory services provided by means of written material or oral statements that do not purport to meet the objectives or needs of specific individuals or accounts.
- (3) “Supervised person” means any partner, officer, director (or other person occupying a similar status or performing similar functions), or employee of an investment adviser, or other person who provides investment advice on behalf of the investment adviser and is subject to the supervision and control of the investment adviser.
- (4) “Place of business” means:
  - (A) an office at which the “investment adviser representative” regularly provides investment advisory services, solicits, meets with, or otherwise communicates with clients; or
  - (B) any other location that is held out to the general public as a location at which the “investment adviser representative” provides investment advisory services, solicits, meets with, or otherwise communicates with clients.
- (c) Supervised persons may rely on the definition of “client” in SEC Rule 275.203(b)(3)-1 to identify clients for purposes of paragraph (a)(1) of this section, except that supervised persons need not count clients that are not residents of the United States.

*56 Act cross reference 401g2-1*

**NASAA Registration Requirements for Investment Advisers**  
**Model Rule USA 2002 403(a)**  
*Adopted 9/17/2008*

**Rule USA 2002 403(a) Application for Investment Adviser Registration [Licensure]**

- (a) INITIAL APPLICATION. The application for initial registration [licensure] as an investment adviser pursuant to Section 403(a) of the Act shall be made by completing Form ADV (Uniform Application for Investment Adviser Registration) in accordance with the form instructions and by filing the form electronically with IARD. The application for initial registration [licensure] shall also include the following:
- (1) Proof of compliance by the investment adviser with the examination requirements of Rule 412(e)-1;
  - (2) Such financial statements as set forth in Rule 411(b)-1, including a copy of the balance sheet for the last fiscal year, and if such balance sheet is as of a date more than 45 days from the date of filing of the application, an unaudited balance sheet prepared as set forth in Rule 411(b)-1;
  - (3) A copy of the surety bond required by Rule 411(e)-1, if applicable, shall be made available upon request of the [Administrator];
  - (4) The fee required by Section 410(c) of the Act [Rule 410(a)(3)], and;
  - (5) Any other information the [Administrator] may reasonably require.
- (b) FORM ADV PART II. The [Administrator] may:
- (1) accept a copy of Part II of Form ADV as filed electronically with IARD; or
  - (2) require a paper copy of Part II of Form ADV be filed directly with the [Administrator].
- (c) ANNUAL RENEWAL. The application for annual renewal registration [licensure] as an investment adviser shall be filed electronically with IARD. The application for annual renewal registration [licensure] shall include the following:
- (1) The fee required by Section 410(c) of the Act [Rule 410(a)(3)]; and
  - (2) [A copy of the surety bond required by Rule 411(e)-1, if applicable.]
- (d) UPDATES AND AMENDMENTS.
- (1) An investment adviser must file electronically with IARD, in accordance with the instructions in the Form ADV, any amendments to the investment adviser's Form ADV;
  - (2) An amendment will be considered to be filed promptly if the amendment is filed within thirty (30) days of the event that requires the filing of the amendment; and
  - (3) Within ninety (90) days of the end of the investment adviser's fiscal year, an investment adviser must file electronically with IARD an Annual Updating Amendment to the Form ADV.
- (e) COMPLETION OF FILING. An application for initial or renewal registration is not considered filed for purposes of Section 403(a) of the Act until the required fee and all required submissions have been received by the [Administrator].

*56 Act cross reference 202(a)-1*

**NASAA Registration Requirements for Investment Adviser Representatives**  
**Model Rule USA 2002 404(a)**  
*Adopted 9/17/2008*

**Rule USA 2002 404(a) Application for Investment Adviser Representative Registration [Licensure]**

- (a) INITIAL APPLICATION. The application for initial registration [licensure] as an investment adviser representative pursuant to Section 404(a) of the Act shall be made by completing Form U4 (Uniform Application for Securities Industry Registration or Transfer) in accordance with the form instructions and by filing the Form U4 electronically with IARD. The application for initial registration [licensure] shall also include the following:
- (1) Proof of compliance by the investment adviser representative with the examination requirements of Rule 412(e)-1;
  - (2) The fee required by section 410(d) of the Act [Rule 410(a)(4)].
- (b) ANNUAL RENEWAL. The application for annual renewal registration [licensure] as an investment adviser representative shall be filed electronically with IARD. The application for annual renewal registration [licensure] shall include the fee required by Section 410(d) of the Act [Rule 410(a)(4)].
- (c) UPDATES AND AMENDMENTS.
- (1) The investment adviser representative is under a continuing obligation to update information required by Form U4 as changes occur.
  - (2) An investment adviser representative and the investment adviser must electronically file promptly with IARD any amendments to the representative's Form U4; and
  - (3) An amendment will be considered to be filed promptly if the amendment is filed within thirty (30) days of the event that requires the filing of the amendment.
- (d) COMPLETION OF FILING. An application for initial or renewal registration is not considered filed for purposes of Section 404(a) of the Act until the required fee and all required submissions have been received by the [Administrator].

*56 Act cross reference 202(a)-2*

**NASAA Notice Filing Requirements for Federal Covered Investment Advisers**  
**Model Rule USA 2002 405(a)**  
*Adopted 9/17/2008*

**Rule USA 2002 405(a) Notice Filing Requirements for Federal Covered Investment Advisers**

- (a) NOTICE FILING. The notice filing for a federal covered investment adviser pursuant to Section 405(a) of the Act shall be filed electronically with IARD on an executed Form ADV (Uniform Application for Investment Adviser Registration). A notice filing of a federal covered investment adviser shall be deemed filed when the fee required by Section 410(e) of the Act [Rule 410(a)(5)] and the Form ADV are filed electronically with and accepted by IARD on behalf of the state.
- (b) FORM ADV PART II. The [Administrator] may:
  - (1) accept a copy of Part II of Form ADV as filed electronically with IARD; or
  - (2) deem Part II of Form ADV filed if a federal covered investment adviser provides, within 5 days of a request, Part II of Form ADV to the [Administrator]. Because the [Administrator] deems Part II of Form ADV to be filed, a federal covered investment adviser is not required to submit Part II of Form ADV to the [Administrator] unless requested.
- (c) RENEWAL. The annual renewal of the notice filing for a federal covered investment adviser pursuant to section 405(c) of the Act shall be filed electronically with IARD. The renewal of the notice filing for a federal covered investment adviser shall be deemed filed when the fee required by Section 410(e) of the Act [Rule 410(a)(5)] is filed with and accepted by IARD on behalf of the state.
- (d) UPDATES AND AMENDMENTS. A federal covered investment adviser must file electronically with IARD, in accordance with the instructions in the Form ADV, any amendments to the federal covered investment adviser's Form ADV.

*56 Act cross reference 202(b)-1*

**NASAA Electronic Filing Requirements for Investment Advisers**  
**Model Rule USA 2002 406(e)-1**  
*Adopted 9/17/2008*

**Rule USA 2002 406(e)-1 Electronic Filing With Designated Entity**

- (a) DESIGNATION. Pursuant to section 406 of the Act, the [Administrator] designates the web-based Investment Adviser Registration Depository (“IARD”) to receive and store filings and collect related fees from investment advisers and investment adviser representatives on behalf of the [Administrator].
- (b) USE OF IARD. Unless otherwise provided, all investment adviser and investment adviser representative applications, amendments, reports, notices, related filings and fees required to be filed with the [Administrator] pursuant to the rules promulgated under the Act, shall be filed electronically with and transmitted to IARD. The following additional conditions relate to such electronic filings:
  - (1) Electronic Signature. When a signature or signatures are required by the particular instructions of any filing to be made electronically through IARD, a duly authorized officer of the applicant or the applicant him or herself, as required, shall affix his or her electronic signature to the filing by typing his or her name in the appropriate fields and submitting the filing electronically to IARD. Submission of a filing in this manner shall constitute irrefutable evidence of legal signature by any individuals whose names are typed on the filing.
  - (2) When filed. Solely for purposes of a filing made electronically through IARD, a document is considered filed with the [Administrator] when all fees are received and the filing is accepted by IARD on behalf of the state.
- (c) ELECTRONIC FILING. Notwithstanding subsection (b) of this rule, the electronic filing of any particular document and the collection of related processing fees shall not be required until such time as IARD provides for receipt of such filings and fees and [30 days] notice is provided by the [Administrator]. Any documents or fees required to be filed with the [Administrator] that are not permitted to be filed with or cannot be accepted electronically by IARD shall be filed directly with the [Administrator].
- (d) HARDSHIP EXEMPTIONS. This section provides two “hardship exemptions” from the requirements to make electronic filings as required by the rules.
  - (1) Temporary Hardship Exemption.
    - (A) Investment advisers registered [licensed] or required to be registered [licensed] under the Act who experience unanticipated technical difficulties that prevent submission of an electronic filing to IARD may request a temporary hardship exemption from the requirements to file electronically.
    - (B) To request a temporary hardship exemption, the investment adviser must:
      - (i) File an Application for a Temporary or Continuing Hardship Exemption, Form ADV-H, in paper format with the [Administrator] where the investment adviser’s principal place of business is located, no later than one business day after the filing (that is the subject of the Form ADV-H) was due; and
      - (ii) Submit the filing that is the subject of the Form ADV-H in electronic format to IARD no later than seven business days after the filing was due.
    - (C) Effective Date--Upon Filing. The temporary hardship exemption will be deemed effective upon receipt by the [Administrator] of the complete Form ADV-H. Multiple temporary hardship exemption requests within the same calendar year may be disallowed by the [Administrator].

- (2) Continuing Hardship Exemption.
- (A) Criteria for Exemption. A continuing hardship exemption will be granted only if the investment adviser is able to demonstrate that the electronic filing requirements of this rule are prohibitively burdensome.
- (B) To apply for a continuing hardship exemption, the investment adviser must:
- (i) File Form ADV-H in paper format with the [Administrator] at least twenty business days before a filing is due; and
  - (ii) If a filing is due to more than one [Administrator], the Form ADV-H must be filed with the [Administrator] where the investment adviser's principal place of business is located. The [Administrator] who receives the application will grant or deny the application within ten business days after the filing of Form ADV-H.
- (C) Effective Date--Upon Approval. The exemption is effective upon approval by the [Administrator]. The time period of the exemption may be no longer than one year after the date on which the Form ADV-H is filed. If the [Administrator] approves the application, the investment adviser must, no later than five business days after the exemption approval date, submit filings to IARD in paper format (along with the appropriate processing fees) for the period of time for which the exemption is granted.
- (3) Recognition of Exemption. The decision to grant or deny a request for a hardship exemption will be made by the [Administrator] where the investment adviser's principal place of business is located, which decision will be followed by the [Administrator] in the other state(s) where the investment adviser is registered.

*56 Act cross reference 202(a)-A*

**NASAA IARD Transition Filing for Investment Advisers**  
**Model Rule USA 2002 406(e)-2**  
*Adopted 9/17/2008*

**Rule USA 2002 406(e)-2 IARD Transition Rule**

- (a) Electronic Filing of Form ADV.
- (1) By (date to be determined), each investment adviser registered [licensed] or required to be registered [licensed] under the Act must resubmit its Form ADV electronically (if it has not previously done so) with IARD unless it has been granted a hardship exemption under Rule 406(e)-1(d).
  - (2) If the amendment to Form ADV is made after (date to be determined), or at an earlier date if an investment adviser has filed its Form ADV (or any amendments to Form ADV) electronically with IARD, the registrant [licensee] must file amendments to Form ADV required by this section electronically with IARD, unless it has been granted a hardship exemption under Rule 406(e)-1(d).
- (b) Electronic Filing of Form U4. By (date to be determined), for each investment adviser representative registered [licensed] or required to be registered [licensed] under the Act, Form U4 must be submitted electronically (if it has not previously been done) with IARD, unless the investment adviser (filing on behalf of the investment adviser representative) has been granted a hardship exemption under Rule 406(e)-1(d).

*56 Act cross reference 203(d)-1*



**NASAA Withdrawal of Investment Adviser Representative Registration**  
**Model Rule USA 2002 408(a)-1**  
*Adopted 9/17/2008*

**Rule USA 2002 408(a)-1 Withdrawal Of Investment Adviser Representative Registration [Licensure]**

The application for withdrawal of registration [licensure] as an investment adviser representative pursuant to Section 408(a) of the Act shall be completed by following the instructions on Form U5 (Uniform Termination Notice for Securities Industry Registration) and filed electronically upon Form U5 with IARD within 30 days of the date of termination.

*56 Act cross reference 204(e)-1(b)*

**NASAA Withdrawal of Investment Advisers Registration**  
**Model Rule USA 2002 409-1**  
*Adopted 9/17/2008*

**Rule USA 2002 409-1 Withdrawal Of Investment Adviser Registration [Licensure]**

The application for withdrawal of registration [licensure] as an investment adviser pursuant to Section 409 of the Act shall be completed by following the instructions on Form ADV-W (Notice of Withdrawal from Registration as Investment Adviser) and filed electronically upon Form ADV-W with IARD.

*56 Act cross reference 204(e)-1(a)*

**NASAA Late Fee Payment Remedies Requirements for Investment Advisers**  
**Model Rule USA 2002 410 [410(a)-1]**  
*Adopted 9/17/2008*

**Rule USA 2002 410 [410(a)-1] Promptly Remedied**

For purposes of sections 410(c), 410(d) and 410(e) of the Act [Rules 410(a)(3), 410(a)(4) and 410(a)(5)], an investment adviser, an investment adviser representative and a federal covered investment adviser, respectively, will have “promptly remedied” a delay in payment or under payment of fees if the adviser or representative remits the fee payment to the [Administrator] within ten business days of receipt of notification from the [Administrator] of the delay or underpayment. If such payment is not received within the ten business day period, an investment adviser, an investment adviser representative and a federal covered investment adviser will be found to have refused to pay the fee.

*56 Act cross reference 401(n)-1*

**NASAA Minimum Financial Requirements for Investment Advisers**  
**Model Rule USA 2002 411(a)-1**  
*Adopted 9/17/2008; Amended 9/11/2011*

**Rule USA 2002 411(a)-1 Minimum Financial Requirements for Investment Advisers**

- (a) An investment adviser registered [licensed] or required to be registered [licensed] under the Act who has custody of client funds or securities shall maintain at all times a minimum net worth of \$35,000 except:
  - (1) An investment adviser having custody solely due to direct fee deduction and complying with the terms described under Rule 411(f)-1(b)(3) and related books and records, as described in Rule 411(c)-1, shall not be required to comply with the net worth or bonding requirements of this Rule.
  - (2) An investment adviser having custody solely due to advising pooled investment vehicles and complying with the terms described under Rule 411(f)-1(a)(5) or Rule 411(f)-1(b)(4) and related books and records, as described in Rule 411(c)-1, shall not be required to comply with the net worth or bonding requirements of this Rule.
- (b) An investment adviser registered [licensed] or required to be registered [licensed] under the Act who has discretionary authority over client funds or securities but does not have custody of client funds or securities shall maintain at all times a minimum net worth of \$10,000.
- (c) An investment adviser registered [licensed] or required to be registered [licensed] under the Act who accepts prepayment of more than \$500 per client and six or more months in advance shall maintain at all times a positive net worth.
- (d) Unless otherwise exempted, as a condition of the right to transact business in this state, every investment adviser registered [licensed] or required to be registered [licensed] under the Act shall by the close of business on the next business day notify the [Administrator] if such investment adviser's net worth is less than the minimum required. After transmitting such notice, each investment adviser shall file by the close of business on the next business day a report with the [Administrator] of its financial condition, including the following:
  - (1) A trial balance of all ledger accounts;
  - (2) A statement of all client funds or securities which are not segregated;
  - (3) A computation of the aggregate amount of client ledger debit balances; and
  - (4) A statement as to the number of client accounts.
- (e) For purposes of this Rule, the term "net worth," shall mean an excess of assets over liabilities, as determined by generally accepted accounting principles, but shall not include as assets: prepaid expenses (except as to items properly classified assets under generally accepted accounting principles), deferred charges, goodwill, franchise rights, organizational expenses, patents, copyrights, marketing rights, unamortized debt discount and expense, all other assets of intangible nature, home, home furnishings, automobile(s), and any other personal items not readily marketable in the case of an individual; advances or loans to stockholders and officers in the case of a corporation; and advances or loans to partners in the case of a partnership.
- (f) For purposes of this Rule, "custody" is defined in Rule 411(f)-1(d)(2).
- (g) For purposes of this Rule an investment adviser shall not be deemed to be exercising discretion when it places trade orders with a broker-dealer pursuant to a third party trading agreement if:
  - (1) the investment adviser has executed a separate investment adviser contract exclusively with its client which acknowledges that a third party trading agreement will be executed to allow the

- investment adviser to effect securities transactions for the client in the client's broker-dealer account; and
- (2) the investment adviser contract specifically states that the client does not grant discretionary authority to the investment adviser and the investment adviser in fact does not exercise discretion with respect to the account; and
  - (3) a third party trading agreement is executed between the client and a broker-dealer which specifically limits the investment adviser's authority in the client's broker-dealer account to the placement of trade orders and deduction of investment adviser fees.
- (h) The [Administrator] may require that a current appraisal be submitted in order to establish the worth of any asset.
- (i) Every investment adviser that has its principal place of business in a state other than this state shall maintain only such minimum net worth as required by the state in which the investment adviser maintains its principal place of business, provided the investment adviser is registered or licensed in such state and is in compliance with such state's minimum capital requirements.

*56 Act cross reference 202(d)-1*

**NASAA Financial Reporting Requirements for Investment Advisers**  
**Model Rule USA 2002 411(b)-1**  
*Adopted 9/17/2008*

**Rule USA 2002 411(b)-1 Financial Reporting Requirements for Investment Advisers**

- (a) Every registered [licensed] investment adviser who has custody of client funds or securities or requires payment of advisory fees six months or more in advance and in excess of \$500 per client shall file with the [Administrator] an audited balance sheet as of the end of the investment adviser's most recent fiscal year. Each balance sheet filed pursuant to this Rule must be:
  - (1) Examined in accordance with generally accepted auditing standards and prepared in conformity with generally accepted accounting principles;
  - (2) Audited by an independent certified public accountant; and
  - (3) Accompanied by an opinion of the accountant as to the report of financial position, and by a note stating the principles used to prepare it, the basis of included securities, and any other explanations required for clarity.
- (b) Every registered [licensed] investment adviser who has discretionary authority over client funds or securities, but not custody, shall file with the [Administrator] a balance sheet, which need not be audited, but which must be prepared in accordance with generally accepted accounting principles or such other basis of accounting acceptable to the [Administrator] and represented by the investment adviser or the person who prepared the statement as true and accurate, as of the end of the investment adviser's most recent fiscal year.
- (c) The financial statements required by this Rule shall be filed with the [Administrator] within 90 days following the end of the investment adviser's fiscal year.
- (d) Every investment adviser that has its principal place of business in a state other than this state shall file only such reports as required by the state in which the investment adviser maintains its principal place of business, provided the investment adviser is registered or licensed in such state and is in compliance with such state's financial reporting requirements.

*56 Act cross reference to 203(c)-1*

**NASAA Recordkeeping Requirements for Investment Advisers**  
**Model Rule USA 2002 411(c)-1**  
*Adopted 9/17/2008; Amended 9/11/2011*

*NOTE: Italicized information is explanatory and not intended for inclusion in the rule text.*

**Rule USA 2002 411(c)-1 Recordkeeping Requirements [ALTERNATIVE 1]:**

- (a) Every investment adviser registered [licensed] or required to be registered [licensed] under the Act shall make and keep true, accurate and current the following books, ledgers and records:
- (1) A journal or journals, including cash receipts and disbursements records, and any other records of original entry forming the basis of entries in any ledger.
  - (2) General and auxiliary ledgers (or other comparable records) reflecting asset, liability, reserve, capital, income and expense accounts.
  - (3) A memorandum of each order given by the investment adviser for the purchase or sale of any security, of any instruction received by the investment adviser from the client concerning the purchase, sale, receipt or delivery of a particular security, and of any modification or cancellation of any such order or instruction. The memoranda shall show the terms and conditions of the order, instruction, modification or cancellation; shall identify the person connected with the investment adviser who recommended the transaction to the client and the person who placed the order; and shall show the account for which entered, the date of entry, and the bank, broker-dealer by or through whom executed where appropriate. Orders entered pursuant to the exercise of discretionary power shall be so designated.
  - (4) All check books, bank statements, canceled checks and cash reconciliations of the investment adviser.
  - (5) All bills or statements (or copies of), paid or unpaid, relating to the investment adviser's business.
  - (6) All trial balances, financial statements and internal audit working papers relating to the investment adviser's business.
  - (7) Originals of all written communications received and copies of all written communications sent by the investment adviser relating to:
    - (A) any recommendation made or proposed to be made and any advice given or proposed to be given,
    - (B) any receipt, disbursement or delivery of funds or securities, or
    - (C) the placing or execution of any order to purchase or sell any security, provided, however,
      - (i) that the investment adviser shall not be required to keep any unsolicited market letters and other similar communications of general public distribution not prepared by or for the investment adviser, and
      - (ii) that if the investment adviser sends any notice, circular or other advertisement offering any report, analysis, publication or other investment advisory service to more than 10 persons, the investment adviser shall not be required to keep a record of the names and addresses of the persons to whom it was sent; except that if the notice, circular or advertisement is distributed to persons named on any list, the investment adviser shall retain with the copy of the notice, circular or advertisement a memorandum describing the list and its source.

- (8) A list or other record of all accounts which list identifies the accounts in which the investment adviser is vested with any discretionary power with respect to the funds, securities or transactions of any client.
- (9) A copy of all powers of attorney and other evidences of the granting of any discretionary authority by any client to the investment adviser.
- (10) A copy in writing of each agreement entered into by the investment adviser with any client, and all other written agreements otherwise relating to the investment adviser's business as an investment adviser.
- (11) A file containing a copy of each notice, circular, advertisement, newspaper article, investment letter, bulletin, or other communication including by electronic media that the investment adviser circulates or distributes, directly or indirectly, to two or more persons (other than persons connected with the investment adviser), and if the notice, circular, advertisement, newspaper article, investment letter, bulletin, or other communication including by electronic media recommends the purchase or sale of a specific security and does not state the reasons for the recommendation, a memorandum of the investment adviser indicating the reasons for the recommendation.
- (12) (A) A record of every transaction in a security in which the investment adviser or any advisory representative (as hereinafter defined) of the investment adviser has, or by reason of any transaction acquires, any direct or indirect beneficial ownership, except
- (i) transactions effected in any account over which neither the investment adviser nor any advisory representative of the investment adviser has any direct or indirect influence or control; and
  - (ii) transactions in securities which are direct obligations of the United States. The record shall state the title and amount of the security involved; the date and nature of the transaction (i.e. purchase, sale or other acquisition or disposition); the price at which it was effected; and the name of the broker-dealer or bank with or through whom the transaction was effected. The record may also contain a statement declaring that the reporting or recording of any transaction shall not be construed as an admission that the investment adviser or advisory representative has any direct or indirect beneficial ownership in the security. A transaction shall be recorded not later than 10 days after the end of the calendar quarter in which the transaction was effected.
- (B) For purposes of this subsection (12) the following definitions will apply;
- (i) The term "advisory representative" shall mean any partner, officer or director of the investment adviser; any employee who participates in any way in the determination of which recommendations shall be made; any employee who, in connection with his duties, obtains any information concerning which securities are being recommended prior to the effective dissemination of the recommendations; and any of the following persons who obtain information concerning securities recommendations being made by the investment adviser prior to the effective dissemination of the recommendations:
    - a. any person in a control relationship to the investment adviser,
    - b. any affiliated person of a controlling person and
    - c. any affiliated person of an affiliated person.
  - (ii) "Control" shall mean the power to exercise a controlling influence over the management or policies of a company, unless such power is solely the result of an official position with such company. Any person who owns beneficially, either



directly or through one or more controlled companies, more than 25 % of the voting securities of a company shall be presumed to control such company.

(C) An investment adviser shall not be deemed to have violated the provisions of this subsection (12) because of the failure to record securities transactions of any advisory representative if the investment adviser establishes that it instituted adequate procedures and used reasonable diligence to obtain promptly reports of all transactions required to be recorded.

(13) (A) Notwithstanding the provisions of subsection (12) above, where the investment adviser is primarily engaged in a business or businesses other than advising investment advisory clients, a record must be maintained of every transaction in a security in which the investment adviser or any advisory representative (as hereinafter defined) of the investment adviser has, or by reason of any transaction acquires, any direct or indirect beneficial ownership, except

(i) transactions effected in any account over which neither the investment adviser nor any advisory representative of the investment adviser has any direct or indirect influence or control; and

(ii) transactions in securities which are direct obligations of the United States.

The record shall state the title and amount of the security involved; the date and nature of the transaction (i.e. purchase, sale, or other acquisition or disposition); the price at which it was effected; and the name of the broker-dealer or bank with or through whom the transaction was effected. The record may also contain a statement declaring that the reporting or recording of any transaction shall not be construed as an admission that the investment adviser or advisory representative has any direct or indirect beneficial ownership in the security. A transaction shall be recorded not later than 10 days after the end of the calendar quarter in which the transaction was effected.

(B) An investment adviser is "primarily engaged in a business or businesses other than advising investment advisory clients" when, for each of its most recent three fiscal years or for the period of time since organization, whichever is lesser, the investment adviser derived, on an unconsolidated basis, more than 50% of

(i) its total sales and revenues, and

(ii) its income (or loss) before income taxes and extraordinary items, from such other business or businesses.

(C) For purposes of this subsection (13) the following definitions will apply:

(i) The term "advisory representative", when used in connection with a company primarily engaged in a business or businesses other than advising investment advisory clients, shall mean any partner, officer, director or employee of the investment adviser who participates in any way in the determination of which recommendation shall be made, or whose functions or duties relate to the determination of which securities are being recommended prior to the effective dissemination of the recommendations; and any of the following persons, who obtain information concerning securities recommendations being made by the investment adviser prior to the effective dissemination of such the recommendations or of the information concerning the recommendations:

a. any person in a control relationship to the investment adviser,

b. any affiliated person of a controlling person and

c. any affiliated person of an affiliated person.

(ii) "Control" shall mean the power to exercise a controlling influence over the management or policies of a company, unless such power is solely the result of an official position with such company. Any person who owns beneficially, either

directly or through one or more controlled companies, more than 25 percent of the voting securities of a company shall be presumed to control such company.

(D) An investment adviser shall not be deemed to have violated the provisions of this subsection (13) because of the failure to record securities transactions of any advisory representative if the investment adviser establishes that it instituted adequate procedures and used reasonable diligence to obtain promptly reports of all transactions required to be recorded.

(14) A copy of each written statement and each amendment or revision, given or sent to any client or prospective client of the investment adviser in accordance with the provisions of Rule 411(g) of the Act, and a record of the dates that each written statement, and each amendment or revision, was given, or offered to be given, to any client or prospective client who subsequently becomes a client.

(15) For each client that was obtained by the adviser by means of a solicitor to whom a cash fee was paid by the adviser

(A) evidence of a written agreement to which the adviser is a party related to the payment of such fee;

(B) a signed and dated acknowledgment of receipt from the client evidencing the client's receipt of the investment adviser's disclosure statement and a written disclosure statement of the solicitor; and,

(C) a copy of the solicitor's written disclosure statement. The written agreement, acknowledgment and solicitor disclosure statement will be considered to be in compliance if such documents are in compliance with Rule 275.206(4)-3 of the Investment Advisers Act of 1940. For purposes of this rule, the term "solicitor" shall mean any person or entity who, for compensation, acts as an agent of an investment adviser in referring potential clients.

(16) All accounts, books, internal working papers, and any other records or documents that are necessary to form the basis for or demonstrate the calculation of the performance or rate of return of all managed accounts or securities recommendations in any notice, circular, advertisement, newspaper article, investment letter, bulletin, or other communication including but not limited to electronic media that the investment adviser circulates or distributes, directly or indirectly, to two or more persons (other than persons connected with the investment adviser); provided, however, that, with respect to the performance of managed accounts, the retention of all account statements, if they reflect all debits, credits, and other transactions in a client's account for the period of the statement, and all worksheets necessary to demonstrate the calculation of the performance or rate of return of all managed accounts shall be deemed to satisfy the requirements of this paragraph.

(17) A file containing a copy of all written communications received or sent regarding any litigation involving the investment adviser or any investment adviser representative or employee, and regarding any written customer or client complaint.

(18) Written information about each investment advisory client that is the basis for making any recommendation or providing any investment advice to such client.

(19) Written procedures to supervise the activities of employees and investment adviser representatives that are reasonably designed to achieve compliance with applicable securities laws and regulations.

(20) A file containing a copy of each document (other than any notices of general dissemination) that was filed with or received from any state or federal agency or self regulatory organization and that pertains to the registrant or its investment adviser representatives as that term is defined in subsection (a)(12)(B) of this Rule, which file should contain, but is not limited to, all applications, amendments, renewal filings, and correspondence.

(21) Copies, with original signatures of the investment adviser's appropriate signatory and the investment adviser representative, of each initial Form U4 and each amendment to Disclosure

Reporting Pages (DRPs Form U4) must be retained by the investment adviser (filing on behalf of the investment adviser representative) and must be made available for inspection upon regulatory request.

(22) Where the adviser inadvertently held or obtained a client's securities or funds and returned them to the client within three business days or has forwarded third party checks within 24 hours the adviser will be considered as not having custody but shall keep a ledger or other listing of all securities or funds held or obtained, including the following information:

- (A) Issuer;
- (B) Type of security and series;
- (C) Date of issue;
- (D) For debt instruments, the denomination, interest rate and maturity date;
- (E) Certificate number, including alphabetical prefix or suffix;
- (F) Name in which registered;
- (G) Date given to the adviser;
- (H) Date sent to client or sender;
- (I) Form of delivery to client or sender, or copy of the form of delivery to client or sender;  
and
- (J) Mail confirmation number, if applicable, or confirmation by client or sender of the fund's or security's return.

(23) If an investment adviser obtains possession of securities that are acquired from the issuer in a transaction or chain of transactions not involving any public offering that comply with the exception from custody under Rule 411(f)-1(b)(2), the adviser shall keep the following records:

- (A) A record showing the issuer or current transfer agent's name address, phone number and other applicable contract information pertaining to the party responsible for recording client interests in the securities; and
- (B) A copy of any legend, shareholder agreement or other agreement showing that those securities that are transferable only with prior consent of the issuer or holders of the outstanding securities of the issuer.

(b) (1) If an investment adviser has custody, as that term is defined in Rule 411(f)-1(d)(2), the records required to be made and kept under paragraph (a) above shall include:

- (A) A copy of any and all documents executed by the client (including a limited power of attorney) under which the adviser is authorized or permitted to withdraw a client's funds or securities maintained with a custodian upon the adviser's instruction to the custodian.
- (B) A journal or other record showing all purchases, sales, receipts and deliveries of securities (including certificate numbers) for all accounts and all other debits and credits to the accounts.
- (C) A separate ledger account for each client showing all purchases, sales, receipts and deliveries of securities, the date and price of each purchase and sale, and all debits and credits.
- (D) Copies of confirmations of all transactions effected by or for the account of any client.
- (E) A record for each security in which any client has a position, which record shall show the name of each client having any interest in each security, the amount or interest of each client, and the location of each security.
- (F) A copy of each of the client's quarterly account statements, as generated and delivered by the qualified custodian. If the adviser also generates a statement that is delivered to the client, the adviser shall also maintain copies of such statements along with the date such statements were sent to the clients.

(G) If applicable to the adviser's situation, a copy of the special examination report verifying the completion of the examination by an independent certified public accountant and describing the nature and extent of the examination.

(H) A record of any finding by the independent certified public accountant of any material discrepancies found during the examination.

(I) If applicable, evidence of the client's designation of an independent representative.

(2) If an investment adviser has custody because it advises a pooled investment vehicle, the adviser shall also keep the following records:

(A) True, accurate and current account statements;

(B) Where the adviser complies with Rule 411(f)-1(b)(4) the records required to be made and kept shall include:

(i) the date(s) of the audit;

(ii) a copy of the audited financial statements; and

(iii) evidence of the mailing of the audited financial to all limited partners, members or other beneficial owners within 120 days of the end of its fiscal year.

(C) Where the adviser complies with rule 411(f)-1(a)(5) the records required to be made and kept shall include:

(i) A copy of the written agreement with the independent party reviewing all fees and expenses, indicating the responsibilities of the independent third party.

(ii) Copies of all invoices and receipts showing approval by the independent party for payment through the qualified custodian.

(c) Every investment adviser subject to subsection (a) of this Rule who renders any investment supervisory or management service to any client shall, with respect to the portfolio being supervised or managed and to the extent that the information is reasonably available to or obtainable by the investment adviser, make and keep true, accurate and current:

(1) Records showing separately for each client the securities purchased and sold, and the date, amount and price of each purchase and sale.

(2) For each security in which any client has a current position, information from which the investment adviser can promptly furnish the name of each the client, and the current amount or interest of the client.

(d) Any books or records required by this Rule may be maintained by the investment adviser in such manner that the identity of any client to whom the investment adviser renders investment supervisory services is indicated by numerical or alphabetical code or some similar designation.

(e) Every investment adviser subject to subsection (a) of this rule shall preserve the following records in the manner prescribed:

(1) All books and records required to be made under the provisions of paragraph (a) to (c)(1), inclusive, of this Rule (except for books and records required to be made under the provisions of paragraphs (a)(11) and (a)(16) of this Rule), shall be maintained and preserved in an easily accessible place for a period of not less than five years from the end of the fiscal year during which the last entry

was made on record, the first two years in the principal office of the investment adviser.

(2) Partnership articles and any amendments, articles of incorporation, charters, minute books, and stock certificate books of the investment adviser and of any predecessor, shall be maintained in the principal office of the investment adviser and preserved until at least three years after termination of the enterprise.

(3) Books and records required to be made under the provisions of paragraphs (a)(11) and (a)(16) of this Rule shall be maintained and preserved in an easily accessible place for a period of not less than five years, the first two years in the principal office of the investment adviser, from the end of the fiscal year during which the investment adviser last published or otherwise disseminated, directly or indirectly, the notice, circular, advertisement, newspaper article, investment letter, bulletin, or other communication including by electronic media.

(4) Books and records required to be made under the provisions of paragraphs (a)(17)-(22), inclusive, of this Rule shall be maintained and preserved in an easily accessible place for a period of not less than five years from the end of the fiscal year during which the last entry was made on such record, the first two years in the principal office of the investment adviser, or for the time period during which the investment adviser was registered or required to be registered in the state, if less.

(5) Notwithstanding other record preservation requirements of this Rule, the following records or copies shall be required to be maintained at the business location of the investment adviser from which the customer or client is being provided or has been provided with investment advisory services:

(A) records required to be preserved under paragraphs (a)(3),(a)(7)-(10), (a)(14)-(15), (a)(17)-(19), (b) and (c) inclusive, of this Rule, and

(B) the records or copies required under the provision of paragraphs (a)(11) and (a)(16) of this Rule which records or related records identify the name of the investment adviser representative providing investment advice from that business location, or which identify the business locations' physical address, mailing address, electronic mailing address, or telephone number. The records will be maintained for the period described in subsection (e) of this Rule.

(f) An investment adviser subject to subsection (a) of this Rule, before ceasing to conduct or discontinuing business as an investment adviser shall arrange for and be responsible for the preservation of the books and records required to be maintained and preserved under this Rule for the remainder of the period specified in this Rule, and shall notify the [Administrator] in writing of the exact address where the books and records will be maintained during the period.

(g) (1) Pursuant to Rule 411(c)-1(e) the records required to be maintained and preserved may be immediately produced or reproduced, and maintained and preserved for the required time, by an investment adviser on:

(A) Paper or hard copy form, as those records are kept in their original form; or

(B) Micrographic media, including microfilm, microfiche, or any similar medium; or

(C) Electronic storage media, including any digital storage medium or system that meets the terms of this section.

(2) The investment adviser must:

(A) Arrange and index the records in a way that permits easy location, access, and retrieval of any particular record;

(B) Provide promptly any of the following that the [Administrator] (by its examiners or other representatives) may request:

(i) A legible, true, and complete copy of the record in the medium and format in which it is stored;

(ii) A legible, true, and complete printout of the record; and

(iii) Means to access, view, and print the records; and

(C) Separately store, for the time required for preservation of the original record, a duplicate copy of the record on any medium allowed by this section.

(3) In the case of records created or maintained on electronic storage media, the investment adviser must establish and maintain procedures:

(A) To maintain and preserve the records, so as to reasonably safeguard them from loss, alteration, or destruction;

(B) To limit access to the records to properly authorized personnel and the [Administrator] (including its examiners and other representatives); and

(C) To reasonably ensure that any reproduction of a non-electronic original record on electronic storage media is complete, true, and legible when retrieved.

(h) For purposes of this Rule, "investment supervisory services" means the giving of continuous advice as to the investment of funds on the basis of the individual needs of each client; and "discretionary power" shall not include discretion as to the price at which or the time when a transaction is or is to be effected, if, before the order is given by the investment adviser, the client has directed or approved the purchase or sale of a definite amount of the particular security.

(i) Any book or other record made, kept, maintained and preserved in compliance with Rules 17a-3 and 17a-4 under the Securities Exchange Act of 1934, which is substantially the same as the book or other record required to be made, kept, maintained and preserved under this Rule, shall be deemed to be made, kept, maintained and preserved in compliance with this Rule.

(j) Every investment adviser registered [licensed] or required to be registered [licensed] in this state and that has its principal place of business in a state other than this state shall be exempt from the requirements of this section, provided the investment adviser is registered or licensed in such state and is in compliance with such state's recordkeeping requirements.

**Rule USA 2002 411(c)-1 Recordkeeping Requirements [ALTERNATIVE 2]** (*Language for states which incorporate by reference Rule 204-2 of the Investment Advisers Act of 1940*)

(a) Every investment adviser registered [licensed] or required to be registered [licensed] under this Act shall make and keep true, accurate and current the following books, ledgers and records:

(1) Those books and records required to be maintained and preserved in compliance with Rule 204-2 of the Investment Advisers Act of 1940 (17 C.F.R. 275.204-2 (1996)), notwithstanding the

fact that the investment adviser is not registered or required to be registered under the Investment Advisers Act of 1940.

- (2) All trial balances, financial statements prepared in accordance with generally accepted accounting principles, and internal audit working papers relating to the investment adviser's business as an investment adviser. For purposes of this subsection, "financial statements" means balance sheets, income statements, cash flow statements and net worth computations as required by Rule 202(d)-1.
- (3) A list or other record of all accounts with respect to the funds, securities, or transactions of any client.
- (4) A copy in writing of each agreement entered into by the investment adviser with any client.
- (5) A file containing a copy of each record required by Rule 204-2(11) of the Investment Advisers Act of 1940 including any communication by electronic media that the investment adviser circulates or distributes, directly or indirectly, to two or more persons (other than persons connected with the investment adviser)
- (6) A copy of each written statement and each amendment or revision given or sent to any client or prospective client of the investment adviser in accordance with the provisions of Rule 411(g) of the Act and a record of the dates that each written statement, and each amendment or revision was given or offered to be given to any client or prospective client who subsequently becomes a client.
- (7) For each client that was obtained by the adviser by means of a solicitor to whom a cash fee was paid by the adviser, records required by Rule 206(4)-3 of the Investment Advisers Act of 1940, notwithstanding the fact that the investment adviser is not registered or required to be registered under the Investment Advisers Act of 1940.
- (8) All records required by Rule 204-2(16) of the Investment Advisers Act of 1940 including but not limited to electronic media that the investment adviser circulates or distributes, directly or indirectly, to two or more persons (other than persons connected with the investment adviser).
- (9) A file containing a copy of all written communications received or sent regarding any litigation involving the investment adviser or any investment adviser representative or employee, and regarding any written customer or client complaint.
- (10) Written information about each investment advisory client that is the basis for making any recommendation or providing any investment advice to such client.
- (11) Written procedures to supervise the activities of employees and investment adviser representatives that are reasonably designed to achieve compliance with applicable securities laws and regulations.
- (12) A file containing a copy of each document (other than any notices of general dissemination) that was filed with or received from any state or federal agency or self regulatory organization and that pertains to the registrant or its investment adviser representatives which file should contain, but is not limited to, all applications, amendments, renewal filings, and correspondence.

(13) For investment advisers who have custody, as that term is defined in Rule 411(f)-1(d)(2), of client funds or securities, all records and evidence of compliance required by Rule 206(4)-2 under the Investment Advisers Act of 1940.

(b) Every investment adviser subject to subsection (a) of this rule shall preserve for the period described in subsection (e) of this Rule the following records in the manner prescribed:

(1) Books and records required to be made under the provisions of paragraph (a)(1) of this Rule shall be maintained and preserved in an easily accessible place for a period of not less than five years from the end of the fiscal year during which the last entry was made on such record, the first two years in the principal office of the investment adviser.

(2) Books and records required to be made under the provisions of paragraphs (a)(2)-(a)(13), inclusive, of this Rule shall be maintained and preserved in an easily accessible place for a period of not less than five years from the end of the fiscal year during which the last entry was made on such record, the first two years in the principal office of the investment adviser, or for the time period during which the investment adviser was registered or required to be registered in the state, if less.

(3) Notwithstanding other record preservation requirements of this Rule, the following records or copies shall be required to be maintained at the business location of the investment adviser from which the customer or client is being provided or has been provided with investment advisory services:

(A) records required to be preserved under

i. paragraphs (a)(3), (a)(7)-(10), (a)(14)-(15), (b) and (c) inclusive, of SEC Rule 204-2 of the Investment Advisers Act of 1940.

ii. paragraphs (a)(9)-(11) of this Rule; and

(B) the records or copies required under the provision of paragraphs (a)(11) and (a)(16) of this Rule which records or related records identify the name of the investment adviser representative providing investment advice from that business location, or which identify the business locations' physical address, mailing address, electronic mailing address, or telephone number.

(c) To the extent that the U.S. Securities and Exchange Commission promulgates changes to the above-referenced rules of the Investment Advisers Act of 1940, investment advisers in compliance with such rules as amended shall not be subject to enforcement action by the [Administrator] for violation of this Rule to the extent that the violation results solely from the investment adviser's compliance with the amended rule.

(d) Every investment adviser that has its principal place of business in a state other than this state shall be exempt from the requirements of this section, provided the investment adviser is registered or licensed in such state and is in compliance with the state's recordkeeping requirements.

(e) Every investment adviser subject to subsection (a) of this rule shall preserve the following records in the manner prescribed:

(1) All books and records required to be made under the provisions of paragraph (a) to (c)(1), inclusive, of this Rule (except for books and records required to be made under the provisions of paragraphs (a)(11) and (a)(16) of this Rule), shall be maintained and preserved in an easily accessible place for a period of not less than five years from the end of the fiscal year during which the last entry was made on record, the first two years in the principal office of the investment adviser.

(2) Partnership articles and any amendments, articles of incorporation, charters, minute books, and stock certificate books of the investment adviser and of any predecessor, shall be maintained in the principal office of the investment adviser and preserved until at least three years after termination of



the enterprise.

(3) Books and records required to be made under the provisions of paragraphs (a)(11) and (a)(16) of this Rule shall be maintained and preserved in an easily accessible place for a period of not less than five years, the first two years in the principal office of the investment adviser, from the end of the fiscal year during which the investment adviser last published or otherwise disseminated, directly or indirectly, the notice, circular, advertisement, newspaper article, investment letter, bulletin, or other communication including by electronic media.

(4) Books and records required to be made under the provisions of paragraphs (a)(17)-(22), inclusive, of this Rule shall be maintained and preserved in an easily accessible place for a period of not less than five years from the end of the fiscal year during which the last entry was made on such record, the first two years in the principal office of the investment adviser, or for the time period during which the investment adviser was registered or required to be registered in the state, if less.

(5) Notwithstanding other record preservation requirements of this Rule, the following records or copies shall be required to be maintained at the business location of the investment adviser from which the customer or client is being provided or has been provided with investment advisory services:

(A) records required to be preserved under paragraphs (a)(3),(a)(7)-(10), (a)(14)-(15), (a)(17)-(19), (b) and (c) inclusive, of this Rule, and

(B) the records or copies required under the provision of paragraphs (a)(11) and (a)(16) of this Rule which records or related records identify the name of the investment adviser representative providing investment advice from that business location, or which identify the business locations' physical address, mailing address, electronic mailing address, or telephone number. The records will be maintained for the period described in subsection (e) of this Rule.

*56 Act cross reference 203(a)-2*

**NASAA Bonding Requirements for Investment Advisers**  
**Model Rule USA 2002 411(e)-1**  
*Adopted 9/17/2008; Amended 9/11/2011*

**Rule USA 2002 411(e)-1 Bonding Requirements for Certain Investment Advisers**

(a) Any bond required by this Rule shall be issued by a company qualified to do business in this state in the form determined by the [Administrator] and shall be subject to the claims of all clients of such investment adviser regardless of the client's state of residence.

(1) Every investment adviser registered [licensed] or required to be registered [licensed] under the Act having custody of or discretionary authority over client funds or securities shall be bonded in an amount determined by the [Administrator] based upon the number of clients and the total assets under management of the investment adviser.

(2) Every investment adviser registered [licensed] or required to be registered [licensed] under the Act who has custody or discretion of client funds or securities who does not meet the minimum net worth standard in Rule 411(a)-1(a) and (b) shall be bonded in the amount of the net worth deficiency rounded up to the nearest \$5,000.

(b) For purposes of this Rule, "custody" is defined in Rule 411(f)-1(d)(2).

(c) An investment adviser that has its principal place of business in a state other than this state shall be exempt from the requirements of subsection (a) of this section, provided that the investment adviser is registered or licensed as an investment adviser in the state where it has its principal place of business and is in compliance with such state's requirements relating to bonding.

*56 Act cross reference to 202(e)-1*

**NASAA Custody Requirements for Investment Advisers**  
**Model Rule USA 2002 411(f)-(1)**  
*Adopted 9/17/2008; Amended 9/11/2011*

**Rule USA 2002 411(f)-(1) Custody Requirements for Investment Advisers**

(a) **Safekeeping required.** It is unlawful and deemed to be a fraudulent, deceptive, or manipulative act, practice, or course of business for an investment adviser, registered or required to be registered, to have custody of client funds or securities unless:

- (1) **Notice to [Administrator].** The investment adviser notifies the [Administrator] promptly in writing that the investment adviser has or may have custody. Such notification is required to be given on Form ADV;
- (2) **Qualified Custodian.** A qualified custodian maintains those funds and securities:
  - (A) in a separate account for each client under that client's name; or
  - (B) in accounts that contain only the investment adviser's clients' funds and securities, under the investment adviser's name as agent or trustee for the clients, or, in the case of a pooled investment vehicle that the investment adviser manages, in the name of the pooled investment vehicle
- (3) **Notice to clients.** If an investment adviser opens an account with a qualified custodian on its client's behalf, under the client's name, under the name of the investment adviser as agent, or under the name of a pooled investment vehicle, the investment adviser must notify the client in writing of the qualified custodian's name, address, and the manner in which the funds or securities are maintained, promptly when the account is opened and following any changes to this information. If the investment adviser sends account statements to a client to which the investment adviser is required to provide this notice, the investment adviser must include in the notification provided to that client and in any subsequent account statement the investment adviser sends that client a statement urging the client to compare the account statements from the custodian with those from the investment adviser.
- (4) **Account Statements.** The investment adviser has a reasonable basis, after due inquiry, for believing that the qualified custodian sends an account statement, at least quarterly, to each client for which it maintains funds or securities, identifying the amount of funds and of each security in the account at the end of the period and setting forth all transactions in the account during that period.
- (5) **Special rule for limited partnerships and limited liability companies.**  
**[ALTERNATIVE ONE]** *Without gatekeeper requirement.*  
If the investment adviser or a related person is a general partner of a limited partnership (or managing member of a limited liability company, or holds a comparable position for another type of pooled investment vehicle), the account statements required under

paragraph (a)(4) of this rule must be sent to each limited partner (or member or other beneficial owner).

**[ALTERNATIVE TWO]** *With additional gatekeeper requirement.*

If the investment adviser or a related person is a general partner of a limited partnership (or managing member of a limited liability company, or holds a comparable position for another type of pooled investment vehicle),

(A) the account statements required under paragraph (a)(4) of this rule must be sent to each limited partner (or member or other beneficial owner), and

(B) the investment adviser must:

- (i) enter into a written agreement with an independent party who is obliged to act in the best interest of the limited partners, members, or other beneficial owners to review all fees, expenses and capital withdrawals from the pooled accounts;
- (ii) send all invoices or receipts to the independent party, detailing the amount of the fee, expenses or capital withdrawal and the method of calculation such that the independent party can:
  - (a) determine that the payment is in accordance with the pooled investment vehicle standards (generally the partnership agreement or membership agreement) and
  - (b) forward, to the qualified custodian, approval for payment of the invoice with a copy to the investment adviser.

(6) **Independent Verification.** The client funds and securities of which the investment adviser has custody are verified by actual examination at least once during each calendar year, by an independent certified public accountant, pursuant to a written agreement between the investment adviser and the independent certified public accountant, at a time that is chosen by the independent certified public accountant without prior notice or announcement to the investment adviser and that is irregular from year to year. The written agreement must provide for the first examination to occur within six months of becoming subject to this paragraph, except that, if the investment adviser maintains client funds or securities pursuant to this rule as a qualified custodian, the agreement must provide for the first examination to occur no later than six months after obtaining the internal control report. The written agreement must require the independent certified public accountant to:

- (A) file a certificate on Form ADV-E with the [Administrator] within 120 days of the time chosen by the independent certified public accountant in paragraph (a)(6) of this rule, stating that it has examined the funds and securities and describing the nature and extent of the examination.
- (B) notify the [Administrator] within one business day of the finding of any material discrepancies during the course of the examination, by means of a facsimile transmission or electronic mail, followed by first class mail, directed to the attention of the [Administrator]; and
- (C) file within four business days of the resignation or dismissal from, or other termination of, the engagement, or removing itself or being removed from consideration for being reappointed, Form ADV-E accompanied by a statement that includes:
  - (i) the date of such resignation, dismissal, removal, or other termination, and the name, address, and contact information of the independent certified public accountant; and
  - (ii) an explanation of any problems relating to examination scope or procedure that contributed to such resignation, dismissal, removal, or other termination.

(7) **Investment advisers acting as qualified custodians.** If the investment adviser maintains, or if the investment adviser has custody because a related person maintains, client funds or securities pursuant to this rule as a qualified custodian in connection with advisory services the investment adviser provides to clients:

- (A) The independent certified public accountant the investment adviser retains to perform the independent verification required by paragraph (a)(6) of this rule must be registered with, and subject to regular inspection as of the commencement of the professional engagement period, and as of each calendar year-end, by, the Public Company Accounting Oversight Board in accordance with its rules; and
- (B) The investment adviser must obtain, or receive from its related person, within six months of becoming subject to this paragraph and thereafter no less frequently than once each calendar year a written internal control report prepared by an independent certified public accountant:
  - (i) The internal control report must include an opinion of an independent certified public accountant as to whether controls have been placed in operation as of

a specific date, and are suitably designed and are operating effectively to meet control objectives relating to custodial services, including the safeguarding of funds and securities held by either the investment adviser or a related person on behalf of the investment advisers clients, during the year;

- (ii) The independent certified public accountant must verify that the funds and securities are reconciled to a custodian other than the investment adviser or the investment advisers related person; and
- (iii) The independent certified public accountant must be registered with, and subject to regular inspection as of the commencement of the professional engagement period, and as of each calendar year-end, by, the Public Company Accounting Oversight Board in accordance with its rules.

(8) **Independent representatives.** A client may designate an independent representative to receive, on his behalf, notices and account statements as required under paragraphs (a)(3) and (a)(4) of this rule.

(b) **Exceptions.**

(1) **Shares of mutual funds.** With respect to shares of an open-end company as defined in Section 5(a)(1) of the Investment Company Act of 1940 (“mutual fund”), the investment adviser may use the mutual fund’s transfer agent in lieu of a qualified custodian for purposes of complying with paragraph (a) of this rule;

(2) **Certain privately offered securities.**

(A) The investment adviser is not required to comply with paragraph (a)(2) of this rule with respect to securities that are:

- (i) acquired from the issuer in a transaction or chain of transactions not involving any public offering;
- (ii) uncertificated and ownership thereof is recorded only on the books of the issuer or its transfer agent in the name of the client; and
- (iii) transferable only with prior consent of the issuer or holders of the outstanding securities of the issuer.

(B) Notwithstanding paragraph (b)(2)(A) of this rule, the provisions of this paragraph (b)(2) are available with respect to securities held for the account of a limited partnership (or limited liability company, or

other type of pooled investment vehicle) only if the limited partnership is audited, and the audited financial statements are distributed, as described in paragraph (b)(4) of this rule and the investment adviser notifies the [Administrator] in writing that the investment adviser intends to provide audited financial statements, as described above. Such notification is required to be provided on Form ADV.

(3) **Fee Deduction.** Notwithstanding paragraph (a)(6) of this rule, an investment adviser is not required to obtain an independent verification of client funds and securities maintained by a qualified custodian if all of the following are met:

(A) The investment adviser has custody of the funds and securities solely as a consequence of its authority to make withdrawals from client accounts to pay its advisory fee;

(B) The investment adviser has written authorization from the client to deduct advisory fees from the account held with the qualified custodian;

(C) Each time a fee is directly deducted from a client account, the investment adviser concurrently:

(i) sends the qualified custodian [sends the independent party designated pursuant to section (a)(5)(B)(ii)] an invoice or statement of the amount of the fee to be deducted from the client's account; and

*If the administrator has adopted the gatekeeper requirements of sub. (a)(5) Alternative Two, this subsection should refer to the bracketed language with regard to only sending the invoice to the independent party, not directly to the custodian, who will upon approval forward the invoice to the custodian for action.*

(ii) sends the client an invoice or statement itemizing the fee. Itemization includes the formula used to calculate the fee, the amount of assets under management the fee is based on, and the time period covered by the fee.

(D) The investment adviser notifies the [Administrator] in writing that the investment adviser intends to use the safeguards provided above. Such notification is required to be given on Form ADV.

*The bracketed language in (C)(i) is to be used when the administrator adopts ALTERNATIVE TWO of sub. (a)(5).*

(4) **Limited partnerships subject to annual audit.** An investment adviser is not required to comply with paragraphs (a)(3) and (a)(4) and shall be deemed to have complied with paragraph (a)(6) of this rule with respect to the account of a limited partnership (or

limited liability company, or another type of pooled investment vehicle) if each of the following conditions are met:

- (A) The adviser sends to all limited partners (or members or other beneficial owners) at least quarterly, a statement showing:
  - (i) the total amount of all additions to and withdrawals from the fund as a whole as well as the opening and closing value of the fund at the end of the quarter based on the custodian's records;
  - (ii) a listing of all long and short positions on the closing date of the statement in accordance with FASB Rule ASC 946-210-50;
  - (iii) the total amount of additions to and withdrawals from the fund by the investor as well as the total value of the investor's interest in the fund at the end of the quarter.

*The listing in sub. (ii) follows FASB rule ASC 946-210-50-6 whereby, long and short positions representing more than 5% of the net assets of the fund must be reported as outlined in this subsection of the FASB rule. All provisions of subsection 50-6 apply to the position disclosure required on the quarterly customer statement.*

- (B) At least annually the fund is subject to an audit and distributes its audited financial statements prepared in accordance with generally accepted accounting principles to all limited partners (or members or other beneficial owners) [and the Administrator] within 120 days of the end of its fiscal year;
- (C) The audit is performed by an independent certified public accountant that is registered with, and subject to regular inspection as of the commencement of the professional engagement period, and as of each calendar year-end, by, the Public Company Accounting Oversight Board in accordance with its rules;
- (D) Upon liquidation, the adviser distributes the fund's final audited financial statements prepared in accordance with generally accepted accounting principles to all limited partners (or members or other beneficial owners) and the Administrator promptly after the completion of such audit;
- (E) The written agreement with the independent certified public accountant must require the independent certified public accountant to, upon resignation or dismissal from, or other termination of, the engagement, or upon removing itself or being removed from consideration for being



reappointed, notify the [Administrator] within four business days accompanied by a statement that includes:

- (i) The date of such resignation, dismissal, removal, or other termination, and the name, address, and contact information of the independent certified public accountant; and
- (ii) An explanation of any problems relating to audit scope or procedure that contributed to such resignation, dismissal, removal, or other termination.

(F) The investment adviser must also notify the [Administrator] in writing that the investment adviser intends to employ the use of the statement delivery and audit safeguards described above. Such notification is required to be given on Form ADV.

(5) **Registered Investment Companies.** The investment adviser is not required to comply with this rule with respect to the account of an investment company registered under the Investment Company Act of 1940.

**(c) Delivery to Related Persons.** Sending an account statement under paragraph (a)(5) of this rule or distributing audited financial statements under paragraph (b)(4) of this rule shall not satisfy the requirements of this rule if such account statements or financial statements are sent solely to limited partners (or members or other beneficial owners) that themselves are limited partnerships (or limited liability companies, or another type of pooled investment vehicle) and are related persons of the investment adviser.

**(d) Definitions.** For purposes of the rule:

(1) “Control” means the power, directly or indirectly, to direct the management or policies of a person whether through ownership of securities, by contract, or otherwise. Control includes:

(A) Each of the investment adviser’s officers, partners, or directors exercising executive responsibility (or persons having similar status or functions) is presumed to control the investment adviser;

(B) A person is presumed to control a corporation if the person:

- (i) directly or indirectly has the right to vote 25 percent or more of a class of the corporation’s voting securities; or
- (ii) has the power to sell or direct the sale of 25 percent or more of a class of the corporation’s voting securities;

(C) A person is presumed to control a partnership if the person has the right to receive upon dissolution, or has contributed, 25 percent or more of the capital of the partnership;

(D) A person is presumed to control a limited liability company if the person:

- (i) directly or indirectly has the right to vote 25 percent or more of a class of the interests of the limited liability company;
- (ii) has the right to receive upon dissolution, or has contributed, 25 percent or more of the capital of the limited liability company;
- (iii) is an elected manager of the limited liability company; or

(E) A person is presumed to control a trust if the person is a trustee or managing agent of the trust.

(2) “Custody” means holding directly or indirectly, client funds or securities, or having any authority to obtain possession of them [or has the ability to appropriate them]. The investment adviser has custody if a related person holds, directly or indirectly, client funds or securities, or has any authority to obtain possession of them, in connection with advisory services the investment adviser provides to clients.

(A) Custody includes:

- (i) Possession of client funds or securities unless the investment adviser receives them inadvertently and returns them to the sender promptly but in any case within three business days of receiving them;
- (ii) Any arrangement (including a general partner of attorney) under which the investment adviser is authorized or permitted to withdraw client funds or securities maintained with a custodian upon the investment adviser’s instruction to the custodian; and
- (iii) Any capacity (such as general partner of a limited partnership, managing member of a limited liability company or a comparable position for another type of pooled investment vehicle, or trustee of a trust) that gives the investment adviser or its supervised person legal ownership of or access to client funds or securities.

- (B) Receipt of checks drawn by clients and made payable to third parties will not meet the definition of custody if forwarded to the third party within 3 business days of receipt and the investment adviser maintains the records required under Rule 411(c)-1(a)(22);
- (3) “Independent certified public accountant” means a certified public accountant that meets the standards of independence described in rule 2-01(b) and (c) of Regulation S-X (17 CFR 210.2-01(b) and (c)).
- [(4) “Independent party” means a person that:
  - (A) is engaged by the investment adviser to act as a gatekeeper for the payment of fees, expenses and capital withdrawals from the pooled investment;
  - (B) does not control and is not controlled by and is not under common control with the investment adviser; and
  - (C) does not have, and has not had within the part two years, a material business relationship with the investment adviser.
  - (D) Shall not negotiate or agree to have material business relations or commonly controlled relations with an investment adviser for a period of two years after serving as the person engaged in an independent party agreement.]
- (5) “Independent representative” means a person who:
  - (A) acts as agent for an advisory client, including in the case of a pooled investment vehicle, for limited partners or a limited partnership, members of a limited liability company, or other beneficial owners of another type of pooled investment vehicle and by law or contract is obliged to act in the best interest of the advisory client or the limited partners, members, or other beneficial owners;
  - (B) does not control, is not controlled by, and is not under common control with investment adviser; and
  - (C) does not have, and has not had within the past two years, a material business relationship with the investment adviser.
- (6) “Qualified custodian” means the following:
  - (A) A bank or savings association that has deposits insured by the Federal Deposit Insurance Corporation under the Federal Deposit Insurance Act;
  - (B) A broker-dealer registered in this jurisdiction and with the SEC holding the client assets in customer accounts;

- (C) A registered futures commission merchant registered under Section 4f(a) of the Commodity Exchange Act, holding the client assets in customer accounts, but only with respect to clients' funds and security futures, or other securities incidental to transactions in contracts for the purchase or sale of a commodity for future delivery and options thereon; and
- (D) A foreign financial institution that customarily holds financial assets for its customers, provided that the foreign financial institution keeps the advisory clients' assets in customer accounts segregated from its proprietary assets.

(7) "Related person" means any person, directly or indirectly, controlling or controlled by the investment adviser, and any person that is under common control with the investment adviser.

*56 Act cross reference 102(e)1-1*

**NASAA Brochure Rule Requirements for Investment Advisers**  
**Model Rule USA 2002 411(g)**  
*Adopted 9/17/2008; Amended 9/11/2011*

**Rule USA 2002 411(g) Investment Adviser Brochure Rule**

- (a) **GENERAL REQUIREMENTS.** Unless otherwise provided in this rule, an investment adviser, registered or required to be registered pursuant to Section 403 of the Act shall, in accordance with the provisions of this section, furnish each advisory client and prospective advisory client with:
- (1) a brochure which may be a copy of Part 2A of its Form ADV or written documents containing the information required by Part 2A of Form ADV;
  - (2) a copy of its Part 2B brochure supplement for each individual
    - (A) providing investment advice and having direct contact with clients in this state; or
    - (B) exercising discretion over assets of clients in this state, even if no direct contact is involved;
  - (3) a copy of its Part 2A Appendix 1 wrap fee brochure if the investment adviser sponsors or participates in a wrap fee account;
  - (4) a summary of material changes, which may be included in FORM ADV Part 2 or given as a separate document; and
  - (5) such other information as the [Administrator] may require.
  - (6) The brochure must comply with the language, organizational format and filing requirements specified in the Instructions to Form ADV Part 2.

*Administrators should note that the SEC's Instructions for Part 2A of Form ADV exclude a change in advisory fee from its interpretation of "material change" such that it would not trigger an other than annual amendment of Form ADV Part 2A. The Administrator may wish to include a note or additional rule subsection to clarify fee changes constitute material changes requiring an update to all parts of Form ADV.*

(b) **DELIVERY.**

- (1) **INITIAL DELIVERY.** An investment adviser, except as provided in subsection (b)(3), shall deliver the Part 2A brochure and any brochure supplements required by this section to a prospective advisory client:
  - (A) Not less than 48 hours prior to entering into any advisory contract with such client or prospective client; or
  - (B) At the time of entering into any such contract, if the advisory client has a right to terminate the contract without penalty within five business days after entering into the contract.
- (2) **ANNUAL DELIVERY.** An investment adviser, except as provided in subsection (b)(3), must:
  - (A) Deliver within 120 days of the end of its fiscal year a free, updated brochure and related brochure supplements which include or are accompanied by a summary of material changes; or
  - (B) Deliver a summary of material changes that includes an offer to provide a copy of the updated brochure and supplements and information on how the client may obtain a copy of the brochures and supplements.

*Advisers do not have to deliver a summary of material changes or a brochure to clients if no material changes have taken place since the last summary and brochure delivery.*

- (3) Delivery of the brochure and related brochure supplements required by subsections (b)(1) and (2) need not be made to:
  - (A) clients who receive only impersonal advice and who pay less than \$500 in fees per year; or
  - (B) An investment company registered under the Investment Company Act of 1940; or
  - (C) A business development company as defined in the Investment Company Act of 1940 and whose advisory contract meets the requirements of section 15c of that Act.
- (4) Delivery of the brochure and related supplements may be made electronically if the investment adviser:
  - (A) in the case of an initial delivery to a potential client, obtains a verification that a readable copy of the brochure and supplements were received by the client;
  - (B) in the case of other than initial deliveries, obtains each client's prior consent to provide the brochure and supplements electronically;
  - (C) prepares the electronically delivered brochure and supplements in the format prescribed in sub. (a) and instructions to Form ADV Part 2;
  - (D) delivers the brochure and supplements in a format that can be retained by the client in either electronic or paper form;
  - (E) establishes procedures to supervise personnel transmitting the brochure and supplements and prevent violations of this rule.
- (c) OTHER DISCLOSURES. Nothing in this rule shall relieve any investment adviser from any obligation pursuant to any provision of the Act or the rules and regulations thereunder or other federal or state law to disclose any information to its advisory clients or prospective advisory clients not specifically required by this rule.
- (d) DEFINITIONS. For the purpose of this rule:
  - (1) "contract for impersonal advisory services" means any contract relating solely to the provision of investment advisory services:
    - (A) by means of written material or oral statements which do not purport to meet the objectives or needs of specific individuals or accounts;
    - (B) through the issuance of statistical information containing no expression of opinion as to the investment merits of a particular security; or
    - (C) any combination of the foregoing services.
  - (2) "entering into," in reference to an advisory contract, does not include an extension or renewal without material change of any such contract which is in effect immediately prior to such extension or renewal.

*56 Act cross reference to 203(b)-1*

**NASAA EXAMINATION REQUIREMENTS FOR INVESTMENT ADVISERS AND  
INVESTMENT ADVISER REPRESENTATIVES**  
**Model Rule USA 2002 412(e)-1**  
*Adopted 9/17/2008*

**Rule USA 2002 412(e)-1 Examination Requirements**

- (a) Unless otherwise waived by the [Administrator], an investment adviser or an investment adviser representative shall take and pass within the two year period immediately preceding the date of the application:
  - (1) the Uniform Investment Adviser State Law Examination (S65); or
  - (2) the Uniform Combined State Law Examination (S66) and the General Securities Representative Examination (S7).
- (b) If the investment adviser is an entity, then a supervisory or control individual shall take and pass the examination(s) as required in subsection (a) of this Rule.
- (c) Any person who has been registered as an investment adviser or an investment adviser representative in any state requiring the licensing, registration or qualification of investment advisers or investment adviser representatives within the two year period immediately preceding the date of filing an application shall not be required to comply with the examination requirement set forth in subsection (a) of this Rule.
- (d) Compliance with subsections (a) and (b) is waived if the applicant has been awarded any of the following designations and at the time of filing an application is current and in good standing:
  - (1) Certified Financial Planner (CFP) awarded by the Certified Financial Planners Board of Standards.
  - (2) Chartered Financial Consultant (ChFC) or Masters of Science and Financial Services (MSFS) awarded by the American College, Bryn Mawr, Pennsylvania.
  - (3) Chartered Financial Analyst (CFA) awarded by the Institute of Chartered Financial Analysts.
  - (4) Personal Financial Specialist (PFS) awarded by the American Institute of Certified Public Accountants.
  - (5) Chartered Investment Counselor (CIC) awarded by the Investment Adviser Association.
- (e) An applicant who has taken and passed the Uniform Investment Adviser State Law Examination (S65) within 2 years prior to the date the application is filed with the [Administrator] or at any time if the applicant has been registered or licensed as an investment adviser, investment adviser representative [or securities agent] within the 2 years prior to the date the application is filed with the [Administrator], shall not be required to take and pass the Uniform Investment Adviser State Law Examination again.
- (f) An applicant who is an agent for a broker-dealer/investment adviser and who is not required by the agent's home jurisdiction to make a separate filing on CRD as an investment adviser representative but who has previously met the examination requirement in subsection (a) of this Rule necessary to provide advisory services on behalf of the broker-dealer/investment adviser, shall not be required to take and pass the Uniform Investment Adviser State Law Examination (S65) again.
- (g) [Persons deemed to be investment adviser representatives only because they solicit, offer or negotiate for the sale of or sell investment advisory services in this state shall not be required to take and pass the examinations in subsection (a) of this Rule.]

**NASAA Prohibited Conduct of Investment Advisers, Investment Adviser Representatives  
and Federal Covered Investment Advisers**  
**Model Rule USA 2002 502(b)**  
*Adopted 9/17/2008*

**Rule USA 2002 502(b) Prohibited Conduct in Providing Investment Advice**

A person who is an investment adviser, an investment adviser representative or a federal covered investment adviser is a fiduciary and has a duty to act primarily for the benefit of its clients. The provisions of this subsection apply to federal covered investment advisers to the extent that the conduct alleged is fraudulent, deceptive, or as otherwise permitted by the National Securities Markets Improvement Act of 1996. While the extent and nature of this duty varies according to the nature of the relationship between an investment adviser, an investment adviser representative or a federal covered investment adviser and its clients and the circumstances of each case, an investment adviser, an investment adviser representative or a federal covered investment adviser shall not engage in prohibited fraudulent, deceptive, or manipulative conduct, including but not limited to the following:

- (a) Recommending to a client to whom investment advisory services are provided the purchase, sale or exchange of any security without reasonable grounds to believe that the recommendation is suitable for the client on the basis of information furnished by the client after reasonable inquiry concerning the client's investment objectives, financial situation and needs, and any other information known by the investment adviser, investment adviser representative or federal covered investment adviser.
- (b) Exercising any discretionary authority in placing an order for the purchase or sale of securities for a client without obtaining written discretionary authority from the client within ten (10) business days after the date of the first transaction placed pursuant to oral discretionary authority, unless the discretionary authority relates solely to the price at which, or the time when, an order involving a definite amount of a specified security shall be executed, or both.
- (c) Inducing trading in a client's account that is excessive in size or frequency in view of the financial resources, investment objectives and character of the account.<sup>1</sup>
- (d) Placing an order to purchase or sell a security for the account of a client without authority to do so.
- (e) Placing an order to purchase or sell a security for the account of a client upon instruction of a third party without first having obtained a written third-party trading authorization from the client.
- (f) Borrowing money or securities from a client unless the client is a broker-dealer, an affiliate of the investment adviser or a financial institution engaged in the business of loaning funds.
- (g) Loaning money or securities to a client unless the investment adviser is a financial institution engaged in the business of loaning funds or the client is an affiliate of the investment adviser.
- (h) Misrepresenting to any client, or prospective client, the qualifications of the investment adviser, investment adviser representative, federal covered investment adviser, or any employee, or person affiliated with the investment adviser, investment adviser representative or federal covered investment adviser, or misrepresenting the nature of the advisory services being offered or fees to be charged for such service, or to omit to state a material fact necessary to make the statements made regarding qualifications, services or fees, in light of the circumstances under which they are made, not misleading.

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<sup>1</sup> The rule appropriately forbids an excessive number of transaction orders to be induced by an adviser for a "customer's account" in light of the fact that an investment adviser or an investment adviser representative in such situations can directly benefit from the number of securities transactions effected in a client's account.



- (i) Providing a report or recommendation to any client prepared by someone other than the investment adviser, investment adviser representative or federal covered investment adviser without disclosing that fact. This prohibition does not apply to a situation where the investment adviser, investment adviser representative or federal covered investment adviser uses published research reports or statistical analyses to render advice or where an investment adviser, investment adviser representative or federal covered investment adviser orders such a report in the normal course of providing service.
- (j) Charging a client an unreasonable fee.
- (k) Failing to disclose to clients in writing before any advice is rendered any material conflict of interest relating to the investment adviser, investment adviser representative or federal covered investment adviser, or any of its employees, or affiliated persons which could reasonably be expected to impair the rendering of unbiased and objective advice including but not limited to:
  - (1) Compensation arrangements connected with investment advisory services to clients which are in addition to compensation from such clients for such services; and
  - (2) Charging a client an investment advisory fee for rendering investment advice when compensation for effecting securities transactions pursuant to such advice will be received by the investment adviser, investment adviser representative or federal covered investment adviser or its employees, or affiliated persons.
- (l) While acting as principal for its own advisory account, to knowingly sell any security to or purchase any security from a client, or while acting as broker-dealer for a person other than the client, to knowingly effect any sale or purchase of any security for the account of the client, without disclosing to the client in writing before the completion of the transaction the capacity in which it is acting and obtaining the consent of the client to the transaction.
  - (1) The prohibitions of this subsection shall not apply to any transaction with a customer of a broker-dealer if the broker-dealer is not acting as an investment adviser in relation to the transaction.<sup>2</sup>
  - (2) The prohibitions of this subsection shall not apply to any transaction with a customer of a broker-dealer if the broker-dealer acts as an investment adviser solely:
    - (A) by means of publicly distributed written materials or publicly made oral statements;
    - (B) by means of written materials or oral statements not purporting to meet the objectives or needs of specific individuals or accounts;
    - (C) through the issuance of statistical information containing no expressions of opinion as to the investment merits of a particular security; or
    - (D) any combination of the foregoing services.<sup>3</sup>
  - (3) Publicly distributed written materials or publicly made oral statements shall disclose that, if the purchaser of the advisory communication uses the investment adviser's services in connection with the sale or purchase of a security which is a subject of the communication, the investment adviser may act as principal for its own account or as agent for another person. Compliance by the investment adviser with the foregoing disclosure requirement shall not relieve it of any other disclosure obligations under the Act.<sup>4</sup>
  - (4) Definitions for purposes of this Rule,
    - (A) "Publicly distributed written materials" means written materials which are distributed to 35 or more persons who pay for those materials.

<sup>2</sup> Note: 1956 Act § 102(a)(3) not included in 2002 Act

<sup>3</sup> Note: 1956 Rule 102(f)-2(b) not included in 2002 Act

<sup>4</sup> Note: 1956 Rule 102(f)-2(c)

(B) “Publicly made oral statements” means oral statements made simultaneously to 35 or more persons who pay for access to those statements.

(m) The prohibitions of this Rule shall not apply to an investment adviser effecting an agency cross transaction for an advisory client provided the following conditions are met:<sup>5</sup>

- (1) The advisory client executes a written consent prospectively authorizing the investment adviser to effect agency cross transactions for such client;
- (2) Before obtaining such written consent from the client, the investment adviser makes full written disclosure to the client that, with respect to agency cross transactions, the investment adviser will act as broker-dealer for, receive commissions from and have a potentially conflicting division of loyalties and responsibilities regarding both parties to the transactions;
- (3) At or before the completion of each agency cross transaction, the investment adviser or any other person relying on this rule sends the client a written confirmation. The written confirmation shall include:
  - (A) A statement of the nature of the transaction;
  - (B) The date the transaction took place;
  - (C) An offer to furnish, upon request, the time when the transaction took place; and
  - (D) The source and amount of any other remuneration the investment adviser received or will receive in connection with the transaction. In the case of a purchase, if the investment adviser was not participating in a distribution, or, in the case of a sale, if the investment adviser was not participating in a tender offer, the written confirmation may state whether the investment adviser has been receiving or will receive any other remuneration and that the investment adviser will furnish the source and amount of such remuneration to the client upon the client’s written request;
- (4) At least annually, and with or as part of any written statement or summary of the account from the investment adviser, the investment adviser or any other person relying on this rule sends each client a written disclosure statement identifying:
  - (A) The total number of agency cross transactions during the period for the client since the date of the last such statement or summary; and
  - (B) The total amount of all commissions or other remuneration the investment adviser received or will receive in connection with agency cross transactions for the client during the period.
- (5) Each written disclosure and confirmation required by this rule must include a conspicuous statement that the client may revoke the written consent required under subsection (m)(1) of this rule at any time by providing written notice to the investment adviser.
- (6) No agency cross transaction may be effected in which the same investment adviser recommended the transaction to both any seller and any purchaser.
- (7) For purposes of this rule, “agency cross transaction for an advisory client” means a transaction in which a person acts as an investment adviser in relation to a transaction in which the investment adviser, or any person controlling, controlled by, or under common control with such investment adviser, including an investment adviser representative, acts as a broker-dealer for both the advisory client and another person on the other side of the transaction. When acting in such capacity such person is required to be registered [licensed] as a broker-dealer in this state unless excluded from the definition.

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<sup>5</sup> Note: 1956 Rule 102(f)-1

- (8) Nothing in this rule shall be construed to relieve an investment adviser or investment adviser representative from acting in the best interests of the client, including fulfilling his duty with respect to the best price and execution for the particular transaction for the client nor shall it relieve any investment adviser or investment adviser representative of any other disclosure obligations imposed by the Act.
- (n) Guaranteeing a client that a specific result will be achieved with advice rendered.
- (o) **[Alternative 1]** Publishing, circulating or distributing any advertisement which does not comply with Rule 206(4)-1 under the Investment Advisers Act of 1940.
- (o) **[Alternative 2]** Publishing, circulating or distributing any advertisement which directly or indirectly does any one of the following:
- (1) Refers to any testimonial of any kind concerning the investment adviser, investment adviser representative or federal covered investment adviser, or concerning any advice, analysis, report, or other service rendered by such investment adviser or investment adviser representative.
  - (2) Refers to past specific recommendations of the investment adviser, investment adviser representative or federal covered investment adviser that were or would have been profitable to any person; except that an investment adviser or investment adviser representative may furnish or offer to furnish a list of all recommendations made by the investment adviser, investment adviser representative or federal covered investment adviser within the immediately preceding period of not less than one year if the advertisement or list also includes both of the following:
    - (A) The name of each security recommended, the date and nature of each recommendation, the market price at that time, the price at which the recommendation was to be acted upon, and the most recently available market price of each such security.
    - (B) A legend on the first page in prominent print or type that states that the reader should not assume that recommendations made in the future will be profitable or will equal the performance of the securities in the list.
  - (3) Represents that any graph, chart, formula, or other device being offered can in and of itself be used to determine which securities to buy or sell, or when to buy or sell them; or which represents, directly or indirectly, that any graph, chart, formula, or other device being offered will assist any person in making that person's own decisions as to which securities to buy or sell, or when to buy or sell them, without prominently disclosing in such advertisement the limitations thereof and the difficulties with respect to its use.
  - (4) Represents that any report, analysis, or other service will be furnished for free or without charge, unless such report, analysis, or other service actually is or will be furnished entirely free and without any direct or indirect condition or obligation.
  - (5) Represents that the [Administrator] has approved any advertisement.
  - (6) Contains any untrue statement of a material fact, or that is otherwise false or misleading.
  - (7) For the purposes of this section, the term "advertisement" shall include any notice, circular, letter, or other written communication addressed to more than one person, or any notice or other announcement in any electronic or paper publication, by radio or television, or by any medium, that offers any one of the following:
    - (A) Any analysis, report, or publication concerning securities.

- (B) Any analysis, report, or publication that is to be used in making any determination as to when to buy or sell any security or which security to buy or sell.
  - (C) Any graph, chart, formula, or other device to be used in making any determination as to when to buy or sell any security, or which security to buy or sell.
  - (D) Any other investment advisory service with regard to securities.
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- (p) Making, in the solicitation of clients, any untrue statement of a material fact, or omitting to state a material fact necessary in order to make the statement made, in light of the circumstances under which they are made, not misleading.<sup>6</sup>
  - (q) Failing to establish, maintain, and enforce written policies and procedures reasonably designed to prevent the misuse of material nonpublic information contrary to the provisions of Section 204A of the Investment Advisers Act of 1940.
  - (r) Disclosing the identity, investments, or other financial information of any client or former client unless required by law to do so, or unless consented to by the client.
  - (s) Taking any action, directly or indirectly, with respect to those securities or funds in which any client has any beneficial interest, where the investment adviser has custody or possession of such securities or funds when the action of the investment adviser or investment adviser representative is subject to and does not comply with the requirements of Rule 411(f)-1.
  - (t) Engaging in any act, practice, or course of business which is fraudulent, deceptive, manipulative or unethical.
  - (u) Engaging in conduct or any act, indirectly or through or by any other person, which would be unlawful for such person to do directly under the provisions of the Act or any rule or regulation thereunder.

*56 Act cross reference 102(a)(4)-1*

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<sup>6</sup> Note: 1956 Act § 102(b)

**NASAA Contents of Investment Advisory Contract**  
**Model Rule USA 2002 502(c)**  
*Adopted 9/17/2008*

**Rule USA 2002 502(c) Contents of an Investment Advisory Contract**

[Introduction] The provisions of this subsection apply to federal covered investment advisers to the extent that the conduct alleged is fraudulent, deceptive, or as otherwise permitted by the National Securities Markets Improvement Act of 1996.

- (a) It is unlawful for any investment adviser, investment adviser representative, or federal covered investment adviser to enter into, extend, or renew any investment advisory contract unless it provides in writing:
  - (1) the services to be provided, the term of the contract, the investment advisory fee, the formula for computing the fee, the amount of prepaid fee to be returned in the event of termination or non-performance of the contract, and any grant of discretionary power to the investment adviser, investment adviser representative, or federal covered investment adviser;
  - (2) that no direct or indirect assignment or transfer of the contract may be made by the investment adviser, investment adviser representative or federal covered investment adviser without the consent of the client or other party to the contract;
  - (3) that the investment adviser, investment adviser representative or federal covered investment adviser shall not be compensated on the basis of a share of capital gains upon or capital appreciation of the funds or any portion of the funds of the client;
  - (4) that the investment adviser, investment adviser representative or federal covered investment adviser, if a partnership, shall notify the client or other party to the investment contract of any change in the membership of the partnership within a reasonable time after the change.
  
- (b) It is unlawful for any investment adviser, investment adviser representative, or federal covered investment adviser to:
  - (1) include in an advisory contract, any condition, stipulation, or provisions binding any person to waive compliance with any provision of this act or of the Investment Advisers Act of 1940, or any other practice contrary to the provisions of Section 215 of the Investment Advisers Act of 1940; or
  - (2) enter into, extend or renew any advisory contract contrary to the provisions of Section 205 of the Investment Advisers Act of 1940. This provision shall apply to all advisers and investment adviser representatives registered or required to be registered under this Act, notwithstanding whether such adviser or representative would be exempt from federal registration pursuant to Section 203(b) of the Investment Advisers Act of 1940.
  
- (c) Notwithstanding subsection (a)(3) of this rule, an investment adviser may enter into, extend or renew an investment advisory contract which provides for compensation to the investment adviser on the basis of a share of capital gains upon or capital appreciation of the funds, or any portion of the funds, of the client if the conditions in subsections (c)(1) through (c)(4) of this rule are met.
  - (1) The client entering into the contract must be:

- (A) a natural person or a company who, immediately after entering into the contract, has at least \$ 750,000 under the management of the investment adviser; or
  - (B) a person who the investment adviser and its investment adviser representatives reasonably believe, immediately before entering into the contract, is a natural person or a company whose net worth, at the time the contract is entered into, exceeds \$1,500,000. The net worth of a natural person may include assets held jointly with that person's spouse.
- (2) The compensation paid to the investment adviser with respect to the performance of any securities over a given period must be based on a formula with the following characteristics:
- (A) In the case of securities for which market quotations are readily available within the meaning of Rule 2a-4(a)(1) under the Investment Company Act of 1940 (Definition of "Current Net Asset Value" for Use in Computing Periodically the Current Price of Redeemable Security), the formula must include the realized capital losses and unrealized capital depreciation of the securities over the period;
  - (B) In the case of securities for which market quotations are not readily available within the meaning of Rule 2a-4(a)(1) under the Investment Company Act of 1940, the formula must include:
    - (i) The realized capital losses of securities over the period; and
    - (ii) If the unrealized capital appreciation of the securities over the period is included, the unrealized capital depreciation of the securities over the period; and
  - (C) The formula must provide that any compensation paid to the investment adviser under this rule is based on the gains less the losses (computed in accordance with subsections (A) and (B) of this subsection) in the client's account for a period of not less than one year.
- (3) Before entering into the advisory contract and in addition to the requirements of Form ADV, the investment adviser must disclose in writing to the client or the client's independent agent all material information concerning the proposed advisory arrangement, including the following:
- (A) That the fee arrangement may create an incentive for the investment adviser to make investments that are riskier or more speculative than would be the case in the absence of a performance fee;
  - (B) Where relevant, that the investment adviser may receive increased compensation with regard to unrealized appreciation as well as realized gains in the client's account;
  - (C) The periods which will be used to measure investment performance throughout the contract and their significance in the computation of the fee;
  - (D) The nature of any index which will be used as a comparative measure of investment performance, the significance of the index, and the reason the investment adviser believes that the index is appropriate; and
  - (E) Where the investment adviser's compensation is based in part on the unrealized appreciation of securities for which market quotations are not readily available within the meaning of Rule 2a-4(a)(1) under the Investment Company Act of 1940, how the securities will be valued and the extent to which the valuation will be independently determined.
- (4) The investment adviser (and any investment adviser representative) who enters into the contract must reasonably believe, immediately before entering into the contract that the contract represents an arm's length arrangement between the parties and that the client (or in the case of a client which is a company as defined in subsection (f)(4) of this rule, the person representing

the company), alone or together with the client's independent agent, understands the proposed method of compensation and its risks. The representative of a company may be a partner, director, officer or an employee of the company or the trustee, where the company is a trust, or any other person designated by the company or trustee, but must satisfy the definition of client's independent agent set forth in subsection (f)(3) of this rule.

- (d) Any person entering into or performing an investment advisory contract under this rule is not relieved of any obligations under Rule 502(b) or any other applicable provision of the Act or any rule or order thereunder.
- (e) Nothing in this rule shall relieve a client's independent agent from any obligation to the client under applicable law.
- (f) The following definitions apply for purposes of this rule:
  - (1) "Affiliate" shall have the same definition as in Section 2(a)(3) of the Investment Company Act of 1940.
  - (2) "Assignment," as used in subparagraph (a)(2) of this Rule, includes, but is not limited to, any transaction or event that results in any change to the individuals or entities with the power, directly or indirectly, to direct the management or policies of, or to vote more than 50 percent of any class of voting securities of, the investment adviser or federal covered investment adviser as compared to the individuals or entities who had such power as of the date when the contract was first entered into, extended or renewed.
  - (3) "Client's independent agent" means any person who agrees to act as an investment advisory client's agent in connection with the contract, but does not include:
    - (A) the investment adviser relying on this rule;
    - (B) an affiliated person of the investment adviser or an affiliated person of an affiliated person of the investment adviser including an investment adviser representative;
    - (C) an interested person of the investment adviser;
    - (D) a person who receives, directly or indirectly, any compensation in connection with the contract from the investment adviser, an affiliated person of the investment adviser, an affiliated person of an affiliated person of the investment adviser or an interested person of the investment adviser; or
    - (E) a person with any material relationship between himself (or an affiliated person of that person) and the investment adviser (or an affiliated person of the investment adviser) that exists, or has existed at any time during the past two years.
  - (4) "Company" means a corporation, partnership, association, joint stock company, trust, or any organized group of persons, whether incorporated or not; or any receiver, trustee in a case under title 11 of the United States Code, or similar official or any liquidating agent for any of the foregoing, in his capacity as such. "Company" shall not include:
    - (A) A company required to be registered under the Investment Company Act of 1940 but which is not so registered;
    - (B) A private investment company (for purposes of this subparagraph (B), a private investment company is a company which would be defined as an investment company under Section 3(a) of the Investment Company Act of 1940 but for the exception from that definition provided by Section 3(c)(1) of that act);
    - (C) An investment company registered under the Investment Company Act of 1940; or

- (D) A business development company as defined in Section 202(a)(22) of the Investment Advisers Act of 1940, unless each of the equity owners of any such company, other than the investment adviser entering into the contract, is a natural person or a company within the meaning of subsection (f)(4) of this rule.
- (5) “Interested person” means:
  - (A) Any member of the immediate family of any natural person who is an affiliated person of the investment adviser;
  - (B) Any person who knowingly has any direct or indirect beneficial interest in, or who is designated as trustee, executor, or guardian of any legal interest in, any security issued by the investment adviser or by a controlling person of the investment adviser if that beneficial or legal interest exceeds:
    - (i) one tenth of one percent of any class of outstanding securities of the investment adviser or a controlling person of the investment adviser; or
    - (ii) five percent of the total assets of the person seeking to act as the client’s independent agent; or
  - (C) Any person or partner or employee of any person who, at any time since the beginning of the last two years, has acted as legal counsel for the investment adviser.