

NASAA YEAR IN REVIEW 2004
PROTECTING INVESTORS & RESTORING INTEGRITY



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ABOUT NASAA

Organized in 1919, the North American Securities Administrators Association (NASAA) is the oldest international organization devoted to investor protection. NASAA is a voluntary association whose membership consists of securities administrators in the 50 states, the District of Columbia, Puerto Rico, Canada, and Mexico. In the United States, NASAA is the voice of state securities agencies responsible for efficient capital formation and grassroots investor protection.

NASAA Members have been protecting investors from fraud and abusive sales practices for almost 90 years, beginning with the passage of the first “blue sky” law, in Kansas, in 1911. In the United States, state securities regulation preceded

federal securities laws and the creation of the Securities and Exchange Commission (SEC) and the National Association of Securities Dealers (NASD). The system of state, federal and industry oversight supports securities markets and has helped make them the envy of the world. Within this system, each regulator complements the other, leveraging resources, strengths and expertise.

Investors benefit from grassroots regulation and NASAA Members have a long record of success in protecting investors at the local level. As an investor’s front line of defense, NASAA Members provide residents within their jurisdictions with information about securities firms or individuals selling securities within the state or province. NASAA Members also are quick to respond, even to individual complaints. ■

LEADERSHIP

LETTER

LOOKING FORWARD: Restoring Integrity by Sharing Responsibility

The past year's scandals — whether involving mutual funds, insurance, analyst research, variable annuities, or sales of unsuitable securities — continued to demonstrate the vital role that state and provincial securities regulators serve in protecting the citizens within their jurisdictions. Wrongdoing within various sectors of the financial services industry — and our swift actions in response — resulted in a very eventful 2004 for NASAA members throughout the United States, Canada, and Mexico.

For all the tasks that demand our attention in the year ahead, one calls on regulators and industry alike. Together, we must focus our priorities to help investors regain confidence in our financial markets. And we must also honor our responsibilities to ensure that all investors are treated fairly.

In reviewing 2004 enforcement actions by NASAA Members it is clear that many firms with otherwise good compliance programs appear to have allowed a culture of noncompliance to exist for too long. If not redressed, such a culture will lead to a further erosion of investor confidence. Indeed, investor confidence is always enhanced in an environment of greater transparency and accountability, supported by governmental examinations and enforcement.

The mission of state and provincial securities regulators is to protect investors, and we will continue to fulfill our responsibilities to do all that we can to ensure that financial markets are fair for all and provide for economic growth. Specifically, in 2005, we will:

- continue to monitor the firms and agents, through our registration procedures;
- continue to conduct examinations of firms and review securities offerings to ensure compliance with state and provincial securities laws and regulations; and
- continue to bring enforcement actions against those who would let their own self-interest take precedence over the public interest.

The securities industry is among the most sophisticated in the world and it must not lose sight of the ultimate beneficiary — the capital markets and the investors that rely on them. The industry, led by its senior management, must work to ensure that its employees comply with the law and put their customers' interests ahead of their own.

Looking forward, NASAA will continue to focus on three key aspects of our strategic plan in 2005: training, investor education, and enforcement. NASAA is committed to providing a multitude of training programs for our Membership and their staffs. Providing knowledge and training is our responsibility and we will continue to enhance our training programs as a core goal of the association. In the area of investor education, NASAA will continue its leadership role. Investor education will remain a top priority of both NASAA and its Members throughout 2005.


In the area of enforcement, NASAA and its Members will continue to forge close alliances with other stakeholders in the area of state financial services regulation to work together to advocate our positions on behalf of investors. In the United States, as a matter of sovereignty, the states have a separate and distinct role to serve in protecting investors, a role that Congress recognizes is different from that played by the SEC and membership organizations such as the NASD and New York Stock Exchange. Investors need the protection of state securities regulators. As more investors turn to the market for their financial security, this responsibility is only going to grow.

We have outlined the three key areas of responsibility for 2005 — training, investor education and enforcement. Each of these areas will be emphasized throughout our jurisdictions. NASAA also will continue to reach out to the international regulatory community and advocate the need to develop cooperative information sharing programs, policies and laws as positive steps toward greater enforcement and protection from fraud. In particular, NASAA looks forward to forming closer relationships with our Canadian and Mexican members in these areas.

We are confident that NASAA and its Membership will continue to honor our responsibilities to ensure that all investors are treated fairly; strengthen investor confidence; retain state securities regulatory authority; maintain the position of our markets as the most efficient and respected in the world; and most importantly, take proactive measures to protect investors by putting their interests first.



Franklin L. Widmann
Chief, New Jersey Bureau of Securities
NASAA President, 2004-2005



Ralph A. Lambiasi
Director, Connecticut Division of Securities
NASAA President, 2003-2004



Patricia D. Struck
Administrator, Wisconsin Division of Securities
NASAA President-elect, 2004-2005

CORPORATE OFFICE REPORT

Looking back on 2004, the Corporate Office staff would like to express our sincere appreciation for the opportunity to be part of executing the strategy that the Board of Directors and Membership developed to help the association achieve its goals during the year.

A major challenge in 2004 came in the form of federal preemption provisions included in legislation (H.R. 2179) that were aimed directly at limiting the core mission of our association — protecting investors from investment fraud and abuse. In the end, through much hard work by the Membership, Congress recognized that the work of state securities regulators is essential to protect investors and make the nation's securities markets the most fair and trusted in the world.

Despite this successful outcome on H.R. 2179, we continue to bear in mind the words of the Honorable Paul Sarbanes, the Ranking Member on the Senate Banking Committee. At our Spring Conference, Senator Sarbanes cautioned NASAA Members to remain vigilant and prepared to face attempts to neutralize state regulators who are aggressively protecting investors. "Part of what they're trying to do is seeking to knock out those states that are being fairly aggressive ... in how they seek to protect their investors," he said.

The preemption battle was broader than just the legislative front. Early in 2004, the Office of the Comptroller of the Currency, the arm of the U. S. Treasury Department that regulates national banks, imposed new rules that would significantly weaken the ability of states to enforce laws designed to protect consumers. The new rules expanded existing federal preemptions applicable to national banks and their operating subsidiaries. The potential impact of this action on this country's banking system and all consumers is enormous. The OCC's action raised significant legal and public policy questions of whether one federal regulatory agency, without explicit Congressional authority, can and should preempt laws that were lawfully enacted by state legislatures to protect their citizens.

In December, this question moved from rhetorical to real when State Farm announced plans to defy state licensing requirements and have its agents more aggressively market the deposit and loan products of its State Farm Bank, F.S.B. subsidiary in several states. State Farm based its decision to sell its bank products without meeting state licensing standards on an opinion letter issued by the Office of Thrift Supervision (OTS), the Treasury Department unit that regulates federally-chartered savings banks.

As President Lambiase testified before the Senate Banking Committee in June, "protecting investors and punishing those who would victimize investors with abusive sales practices are fundamental roles of government, be it federal, state, or provincial."

Indeed, the NASAA Membership has a strong and united voice that clearly advocated its need to maintain the authority to regulate at the local level and bring enforcement actions with appropriate remedies against those firms that violate securities laws in their jurisdictions.

The challenges NASAA faced last year also illustrate the importance of maintaining a strong working relationship with regulators, legislators, and, as appropriate, the securities industry itself. We here in the Corporate Office look forward to helping the Membership meet these challenges head on in 2005 and to continue advocating the important role NASAA Members serve in protecting more than 100 million North American investors.

NASAA Corporate Office Staff

NASAA's daily operations are managed by an executive director and a professional staff located in Washington, D.C. NASAA departments include legal, finance, government affairs, communications, investor education, and membership services. The NASAA Corporate Office staff, as of December 31, 2004, is listed below.

EXECUTIVE & ADMINISTRATIVE OFFICE

- John H. Hanley
Executive Director
- John H. Lynch
Deputy Executive Director & Controller
- Benita Carr
*Executive Assistant/Office Administrator/
Benefits Coordinator*
- Brandi Greenleaf
Receptionist

LEGAL

- Rex A. Staples
General Counsel
- Steve Hall
Deputy General Counsel
- Mark Davis
Associate Counsel

GOVERNMENT AFFAIRS

- Deborah Fischione House
Director of Policy
- J.P. Green
Legislative Affairs Manager
- Katie Henke
Government Affairs Assistant

COMMUNICATIONS & INVESTOR EDUCATION

- Bob Webster
Director of Communications
- Jerry Munk
Investor Education Manager

CONFERENCES & EVENTS

- Lonnie Martin
Meetings Manager

SPECIAL REPORT

Protecting Investors & Restoring Integrity

NASAA assists its Members in coordinating enforcement efforts regarding multi-jurisdictional frauds by facilitating the sharing of information and leveraging the resources of our jurisdictions more efficiently. White-collar crime cases encompass a broad range of misconduct that profoundly affects all investors. For instance, it is estimated that securities fraud alone costs investors \$40 billion per year. The ability of regulators and prosecutors to fight crime relies on our ability to effectively leverage the resources of local, state and federal agencies. For example, the investigation of mutual fund trading practices launched by state and federal officials demonstrates both the value-added benefits of state securities regulation and the complementary relationship between state and federal regulators.

"State securities regulators perform an essential role in promoting the goal of investor protection."

Sen. Paul Sarbanes (D-MD)
Ranking Member
Senate Banking Committee



NASAA President Ralph A. Lambiase (CT) welcomes Sen. Paul Sarbanes (D-MD), Ranking Member of the Senate Banking Committee, to NASAA's 2004 Spring Conference.

Continuing Need for Adequate Funding

Given both the important role financial markets play and the growing numbers of individuals turning to the markets for their long-term financial goals, it is imperative that more resources are focused on enforcement. State, federal and provincial prosecutors rely on state securities agencies for expertise and guidance, help and support. To continue delivering this support, NASAA urges state legislatures to increase resources for state securities regulation and enforcement.

Advancing Responsible Regulation

Advancing the interests of state and provincial securities regulation through effective regulation is a fundamental aspect of NASAA's mission. Thus, a significant amount of NASAA's work focuses on representing the interests of state and provincial securities regulators and working in a coordinated and cooperative manner with the U.S. Securities and Exchange Commission, industry self-regulatory organizations such as the NASD and the New York Stock Exchange, and other international regulatory bodies, including the International Organization of Securities Commissions (IOSCO) and the Council of Securities Regulators for the Americas (COSRA).

STATE SECURITIES REGULATORS ENFORCEMENT ACTIVITY (2002/2003 reporting period)

2,941	\$818 million	\$660 million	717.31 years
ENFORCEMENT ACTIONS	MONETARY FINES & PENALTIES	MONEY ORDERED RETURNED TO INVESTORS	YEARS OF INCARCERATION SENTENCED
<i>(Includes administrative, civil, and criminal actions)</i>	<i>(Includes civil and criminal fines and penalties)</i>	<i>(Includes restitution, rescission, and disgorgement)</i>	

NOTES: All data are for the 2002/2003 reporting period; reflected either as calendar year 2002 or most recent fiscal year, July 1, 2002 through June 30, 2003. Totals are preliminary as of May 27, 2004 and are based on responses from 34 of 52 jurisdictions.

SOURCE: North American Securities Administrators Association

"State regulators have a mandate to protect investors that extends beyond enforcement actions and coordination with federal regulators."

Sen. Richard Shelby (R-AL)
Chairman
Senate Banking Committee



Joseph P. Borg, Alabama Securities Commission Director and Chair of NASAA's Enforcement Section, and Senate Banking Committee Chairman Richard Shelby (R-AL) exchange greetings before a Senate hearing examining how state securities regulators protect investors.

Enhancing Coordination and Cooperation

NASAA welcomes the opportunity to continue to work with our regulatory counterparts at the SEC and the SROs to collectively use our resources to protect investors. We also look forward to the continued progress of our ongoing series of discussions with the SEC in 2004 as part of the joint initiative to explore ways to improve coordination and communication. We stand ready to provide insight from our unique perspective to the SEC and SROs as they move forward in their rulemaking processes.

NASAA also is taking steps to reach out to other regulators at both the state and federal levels. For example, in 2004 NASAA successfully joined forces with the National Association of Insurance Commissioners (NAIC) to conduct the first-ever joint training program to benefit state insurance and state securities regulators who want to work together more effectively to solve the persistent problem of securities fraud by insurance agents.

Also in 2004, NASAA accepted an invitation from the U.S. Treasury Department to become a member of the Financial and Banking Information Infrastructure Committee (FBIIC), which is sponsored by the President's Working Group on Financial Markets. As an active FBIIC member, NASAA helps coordinate public-sector efforts to improve the reliability and security of the U.S. financial system. FBIIC also develops procedures and systems to allow federal and state regulators to communicate among themselves and with the private sector during times of crisis. NASAA also serves as a member of the Federal Reserve's Cross-Sector Group and participated in the group's bi-annual meetings, which are hosted by the Federal Reserve and include representatives from the state and federal banking, insurance and securities regulators.

Encouraging Effective Legislation

NASAA, through its Membership, Board-level Federal Legislation Committee, and the Corporate Office staff, actively promotes the interests of state and provincial securities regulators before legislatures. NASAA provides a united voice to advocate for ensuring that state and provincial securities regulators maintain authority essential to keep capital markets safe for all investors. Our members testify before federal, state and provincial legislatures on a variety of initiatives and have been the voice of reasonable and responsible regulation to protect investors in our securities markets. NASAA provides technical information and comments on legislation of concern and interest to its Members.

Protecting Investors' Rights

NASAA plays an important role in representing the membership's position, as *amicus curiae*, in significant legal proceedings that may have a widespread impact upon securities regulators and the rights of investors. Under the direction of the Legal Services Committee chaired by Robert McDonald, of Maryland, NASAA filed 6 amicus briefs in cases pending before the U.S. Supreme Court, the U.S. Court of Appeals, the U.S. Bankruptcy Court and the Maryland Court of Appeals.

- In **SEC v. Mutual Benefits Corp.** NASAA filed an amicus brief in the U.S. Court of Appeals for the Eleventh Circuit in support of the SEC's enforcement action against Mutual Benefits. NASAA argued that MBC's viatical settlements are investment contracts under the Howey test and that investors will be exposed to a heightened risk of fraud and abuse if these investment offerings are not subject to SEC regulation.
- At issue in **Dura Pharmaceuticals v. Broudo**, pending in the U.S. Supreme Court, is what a plaintiff must plead to satisfy the element of loss causation in an action alleging fraud on the market under Section 10(b). NASAA's *amicus brief* argued in support of the Ninth Circuit's ruling that a plaintiff need only allege that the stock price was inflated on the date of purchase as a result of the defendants' misrepresentations, reasoning that "the injury occurs at the time of the transaction" and damages are to be measured at that point.



- In *Wachovia v. Burke*, NASAA filed an *amicus brief* with the U.S. Court of Appeals for the Second Circuit in support of the Connecticut Banking Commissioner on the question of whether the Office of the Comptroller of the Currency (OCC) properly preempted state licensing requirements for mortgage lenders. The brief argues that the preemption was improper.
- At issues in *In Re Simon* is a constitutional challenge to the provision of the Sarbanes-Oxley Act excluding from discharge in bankruptcy claims relating to the violation of state and federal securities laws. The case is pending in the U.S. Bankruptcy Court for the Southern District of Florida. Mark Sendrow, formerly Director of Securities in Arizona, played a leadership role in the enactment of the provision

being challenged, and prepared the *amicus brief* on NASAA's behalf.

- In *Lubin v. Agora, Inc.* in the Maryland Court of Appeals, NASAA's *amicus brief* supported Maryland's position that it has authority to subpoena subscriber information from a newsletter company that appears to be engaged in activities for which it needs to be registered as an investment adviser.
- In *Ropp v. 1717 Capital Management* in the U.S. Court of Appeals for the Third Circuit, NASAA's *amicus brief* supported Delaware's position that an arbitration agreement between an investor and a firm does not preclude a state securities regulator from seeking victim-specific relief, such as restitution, in an enforcement action. ■

SENATE BANKING COMMITTEE EXAMINES ROLE OF STATE SECURITIES REGULATORS IN PROTECTING INVESTORS



NASAA President Lambiase and Enforcement Section Chair Borg testify before the Senate Banking Committee



Investor Juanita Periman (right) tells members of the Senate Banking Committee how Montana securities regulators provided her with invaluable assistance.


On June 2, NASAA President Ralph Lambiase (CT) and Enforcement Section Chair Joe Borg (AL) stressed the importance of state securities regulators in testimony before the Senate Banking Committee. Additional witnesses included New Jersey Attorney General Peter Harvey, on behalf of the National Association of Attorneys General; AARP Board Chairman Charles Leven; and Juanita Periman, a securities fraud victim from Montana.

Both Chairman Richard Shelby (R-AL) and Ranking Member Sarbanes (D-MD) endorsed the mission of state securities regulators and praised their job execution. At one point, Chairman Shelby interrupted a witness to underscore: "and that's why we don't need preemption, isn't it?" He stated that "time and again we have seen the need for vigorous state regulators to pursue investigations and enforcement actions." Ranking Member Sarbanes said state securities regulators "perform an essential role in promoting the goal of investor protection." He added that preemption of state authority would not serve the public interest and praised the efforts of Maryland Securities Commissioner Melanie Lubin.

Senator Jon Corzine (D-NJ) said he believes that cooperation between state and federal regulators is essential and that the "right balance" between federal and state regulators is needed for effectively functioning national markets. Senator Chris Dodd (D-CT) noted Mr. Lambiase's distinguished career in public service, saying he has done a "tremendous job" in protecting investors.

Attorney General Harvey told the panel that since assuming office last year, he has dedicated increased staff and resources to the New Jersey Bureau of Securities, under the direction of Frank Widmann, in order to handle the workload. Mr. Leven added that AARP believes there are demonstrated benefits to the dual system of regulation and to the role and value of state securities regulators.

Ms. Periman praised the work of the Montana Securities Department on her behalf. "I am very grateful that my state securities regulators responded so quickly and successfully to my call," she said. Committee Members all expressed their gratitude to Ms. Periman for traveling from Montana and her willingness to tell her compelling story.



2004 NASAA SECTION REVIEW

Broker-Dealer

OVERVIEW

The NASAA Broker-Dealer Section focuses on issues involving broker-dealers and agents. These issues include qualification and licensing requirements, record-keeping and compliance requirements, continuing education, and practices involving investors. The Section monitors trends involving the broker-dealers and their agents, provides official comments on rule proposals, participates in discussions with industry regarding trends and concerns, and provides guidance to states on trends and issues. Relevant issues include including the applicability of

suitability determinations, required disclosures, account fees, variable annuity sales, arbitration, finders, sales practices and supervision issues. The point-of-sale contact broker-dealers have with investors makes the work of this Section critical in achieving NASAA's mission of investor protection.

NASAA's 2003-2004 Broker-Dealer Section was chaired by Illinois Securities Director Tanya Solov; Don Saxon, Director of the Florida Department of Financial Services Office of Financial Regulation, served as Vice Chair. Section Members

included: James O. Nelson II, Mississippi; Matthew J. Neubert, Arizona; Ryan Ushijima, Hawaii. Douglas Brown, of Manitoba, served as the Section's Canadian Liaison.

The Section oversees the activities of six Project Groups, including: Continuing Education (Chair: Don Saxon, Florida); Exams Advisory (Chair: Sheila Cahill, Nebraska); Market and Regulatory Policy and Review (Chair: Rex Staples, Washington); Broker-Dealer Operations (Chair: William Reilly, Florida); Arbitration (Chair: Matthew Nestor, Massachusetts); and Variable Annuities (Chair: James O. Nelson II, Mississippi).

The Section also works closely with the NASAA Board CRD/IARD Steering Committee, chaired by Maryland Securities Commissioner Melanie Senter Lubin.

2004 ACTIVITIES

NASAA Listens Forum on Arbitration

In his inaugural address in Chicago, NASAA 2003-2004 President Lambiase signaled his intention to thoroughly examine the issue of arbitration. This goal was achieved when, under the guidance of Broker-Dealer Section Chair Tanya Solov and Arbitration Project Group Chair Matthew Nestor, NASAA successfully focused national attention on concerns about the securities arbitration process by hosting a NASAA Listens Forum. The Forum, held July 20 at the National Press Club in Washington and broadcast live over the Internet, brought together an audience of nearly 360 regulators, industry representatives, media, policymakers and others for a discussion of whether the current arbitration process is fair to investors. Media coverage in *The Wall Street Journal*, *Dow Jones*, *BNA*, and *The Boston Globe* was positive. Ms. Solov moderated the Forum; panelists included Mr. Nestor, NASD Dispute Resolution President Linda Fienberg, *Business Week* Senior Writer Gary Weiss, Fordham University law professor Constantine Katsoris, former NASD arbitrator John Mark, and attorney Thomas Grady.

Mutual Funds

NASAA's Broker-Dealer Section, along with the Investment Adviser and Corporation Finance sections, played an active



James O. Nelson II, Mississippi's Assistant Secretary of State, Business Regulation & Enforcement, discusses arbitration issues with Linda Fienberg, President of NASD Dispute Resolution at the NASAA Listens Forum.



NASAA Broker-Dealer Section Chair Tanya Solov (IL) and Georgetown University Law Center Professor Jeffrey Bauman at the 2004 Spring Conference.

role in association's efforts to ensure that the interests of mutual fund investors are fully protected. Specifically, through the efforts of the Section, NASAA made a series of recommendations on several new rules proposed by the SEC governing mutual funds. In February, NASAA strongly urged the SEC to require an additional one- or two-page document to be given to investors for discussion of mutual fund breakpoint discounts at the point of sale. NASAA also offered the Membership's perspective on ways to improve the disclosure of mutual fund fees and expenses.

Short Sales

NASAA urged the SEC to move forward with its proposed Regulation SHO, which includes specific rules to address on a near-term basis certain aspects of the short selling issue. NASAA believes these proposed rules are an appropriate and important exercise of the Commission's rulemaking responsibilities with respect to the national marketplace. NASAA's Broker-Dealer Operations Project Group has monitored this issue from the perspective of its impact on small-business issuers, the securities of which are traded in

the over-the-counter market, as well as their public stockholders, who have contended that the trading market for their shares has been adversely affected by manipulative short selling activity. NASAA believes it is critical that existing rules governing short selling be revised to effectively remedy potential trading abuses.

Initial Public Offerings

NASAA Members support proposals aimed at eliminating abuses involving Initial Public Offering (IPO) allocations and believe that additional transparency is needed in the allocation of IPO shares. Through the efforts of both the Broker-Dealer and Corporation Finance Section Committees, NASAA in 2004 supported the NASD's proposed rule governing allocations and distributions of shares in initial public offerings (IPOs). The investing public will benefit from extending fairness and transparency to the IPO allocation and distribution process.

Variable Annuities

Sales of variable annuities have increased dramatically over the past decade. As sales have risen, so too have complaints from investors. In 2004, NASAA, based on the efforts of the Variable Annuity Project Group, urged the NASD to expand its proposed rule on the purchase, sale and exchange of deferred variable annuities to include all variable annuity transactions and to include a provision that specifically addresses the use of hypothetical illustrations in variable annuity transactions. NASAA is encouraging changes in state laws that would allow state insurance regulators to continue to oversee the insurance companies that sell variable annuities while authorizing state securities regulators to investigate complaints about variable annuities and to take action against the companies and individuals who sell them.

Privacy

The privacy of consumer financial information is an important issue for NASAA Members. NASAA and its Members have been instrumental in facilitating compliance with the privacy provisions in the Gramm-Leach-Bliley Act (GLBA), which currently permit states to adopt greater

privacy protections under state law. NASAA believes that the initial privacy notices provided by financial institutions have not been as effective as they could be in educating consumers about how their nonpublic personal information is disclosed. In 2004, NASAA Broker-Dealer Section Chair Tanya Solov (IL), Vice-Chair Don Saxon (FL), and Executive Director John Hanley participated in an interagency working group meeting hosted by the SEC and provided the perspective of state securities regulators on a federal interagency proposal to make privacy notice requirements that financial institutions must meet under GLBA more understandable and useful to consumers.

Exam Modules

In 2004, the Section's Operations Project Group developed a municipal bond and mutual fund submodule within the NASAA Broker-Dealer Examination Module. The Project Group also focused its efforts on training Member jurisdictions on the use of examination modules. In addition, the Section's Exams Advisory Project Group met with industry representatives and test developers in 2004 to draft and review approximately 350 new questions for addition to three exam banks.

Continuing Education

When considering state, federal, and industry cooperation, one of the best examples is the Securities Industry Regulatory Council on Continuing Education. Created in 1995, the Council is comprised of representatives of the securities industry, self-regulatory organizations, the SEC, and NASAA. Our joint efforts have resulted in a national continuing education program that is accepted by all regulatory agencies. In 2004, more than 175,000 financial professionals participated in the continuing education program's computer-based training. This year, the Council instructed the Content Committee, which includes NASAA Members Matthew Neubert, of Arizona, and Bonnie Moore, of Nevada, to emphasize mutual fund sales practices and to stress an awareness of breakpoint discounts available to investors.



Broker-Dealer Training

The Section's annual Broker-Dealer Training Seminar attracted more than 81 NASAA participants. The seminar offered sessions for examiners of all levels of experience, and focused on sales practices, supervision and examination procedures, and variable annuity and mutual fund issues. The Section also presented SEC and Wall Street veteran Theodore A. Levine with its Distinguished Service Award, noting his "commitment to engage in open, meaningful, and honest discussions with state securities regulators." ■

2004 BROKER-DEALER SECTION

SECTION COMMITTEE

Tanya Solov (IL), Chair
Don Saxon (FL), Vice Chair
James O. Nelson (MS)
Matthew Neubert (AZ)
Ryan S. Ushijima (HI)
Douglas Brown (MB), Canadian Liaison

PROJECT GROUPS

Continuing Education

Don Saxon (FL), Chair
Matt Neubert (AZ)
Bonnie Moore (NV)

Exams Advisory

Sheila Cahill (NE), Chair
William Cahill (MA)
Barry Glennon (NH)

Market and Regulatory Policy and Review

Ryan Ushijima (HI), Chair
Kimiko Butcher (MA)
Colleen Monahan (CA)
John Moore (AK)
George Robison (UT)
Bruce Topman (NY)

Operations

William Reilly (FL), Chair
Richard Barry (NJ)
Jackie Drouin (ME)
Carol Gruis (OK)
Alfred Hughes (VA)
Patricia Moy (HI)
Bennette Zivley (TX)

Arbitration

Matthew Nestor (MA), Chair
Leigh Davis-Schmidt (UT)
Angela Kinser (KY)
Andrea Soto (WA)

Variable Annuities

James O. Nelson (MS), Chair
John Cronin (VT)
John Cullen (KY)
William DeLuca (RI)
Dean Soma (HI)

Corporation Finance

OVERVIEW

NASAA Members have long helped facilitate capital formation at the state and local level. NASAA members assist entrepreneurs with their business plans, help them obtain resources to grow their enterprises and create local jobs.

NASAA's 2003-2004 Corporation Finance Section was chaired by Texas Securities Commissioner Denise Voigt Crawford; Jack Herstein, Assistant Director, Nebraska Bureau of Securities, served as Vice-Chair. Section members included: Tim Cox, Maryland; Tim Le Bas, California; Lynn Naefach, Pennsylvania. Anthony Patey, Newfoundland & Labrador, served as the Section's Canadian Liaison.

The Section oversaw the activities of seven Project Groups, including: Corporation Finance Policy (Chair: Tim Cox, Maryland); Direct Participation Programs Policy (Chair: Rebecca J. Alford, Pennsylvania); Franchise and Business Opportunities (Chair: Dale Cantone, Maryland); Non-Profit Debt Offerings (Chair: Steve Wassom, Kansas); Shareholder Rights (Chair: Robert M. Lam, Pennsylvania); Small Business (Chair: Lynn Naefach, Pennsylvania); and Trading and Exchanges (Chair: Randall Schumann, Wisconsin).

2004 ACTIVITIES

NASAA's Corporation Finance Section made significant progress on its goals during 2004. The following is a brief synopsis of the Section's 2004 achievements.

Mutual Fund 12b-1 Fees

The Corporation Finance Section, with the assistance of the Investment Adviser Section successfully focused national attention on concerns about mutual fund 12b-1 plans and their resulting fees at a NASAA Listens Forum in New York. The forum, which was also webcast live over the Internet, brought together an audience of more than 200 regulators, industry representatives, attorneys, media, and others for a balanced discussion of whether Rule 12b-1 continues to meet its intended purpose given the evolution and growth of the mutual fund industry. Section Chair Crawford moderated a panel of regulatory and industry experts,



Corporation Finance Section Chair Denise Voigt Crawford (TX) and Section Vice Chair Jack Herstein (NE) at the NASAA Membership Meeting at the 2004 Annual Conference.

including Investment Adviser Section Chair Struck; Vanguard Group founder and former CEO John Bogle; Stuart J. Kaswell, Partner, Dechert LLP; Elizabeth Krentzman, General Counsel, Investment Company Institute; and Richard M. Phillips, Senior Partner and Head of Securities, Kirkpatrick & Lockhart. The Forum attracted national media coverage, including articles in *The Wall Street Journal*. Following the Forum, the California Department of Corporations issued an investor alert cautioning the state's investors to be aware of 12b-1 fees that may have an adverse impact on their mutual fund portfolio.

Toronto Venture Exchange

The NASAA Membership adopted a Section recommendation that expanded the existing NASAA Model Secondary Market Trading Exemption for Qualifying Canadian Securities to include the Toronto Venture Exchange (TSX). The scope of the exemption relates solely to secondary market transactions and does not expand exemption status to primary offerings or to any offers or sales of newly issued securities by a qualifying issuer, as does an exchange-listing type of exemption.



NASAA Corporation Finance Section Chair Denise Voigt Crawford (TX) shares a conversation with Vanguard founder and former CEO John Bogle before the start of the NASAA Listens Forum in New York.

Shell Companies

In an effort to protect investors, NASAA, based on the work of its Corporation Finance Policy Project Group, urged the SEC to limit the use of Form S-8 and Form 8-K by shell companies. NASAA Members have seen a steady stream of fraud and misconduct in the distribution and manipulation of shares of shell companies. NASAA believes SEC rules are particularly appropriate in this area because transactions resulting, directly or indirectly, in the issuance of securities, and involving a merger, acquisition, share exchange, or other combination, are almost universally exempt from registration or notice filings at the state level. Issues raised in the SEC's shell company proposal have been addressed in large part in Canada through rules of the provincial securities commissions and exchange policies. NASAA urged the SEC to carefully analyze whether its proposal will be implemented in a manner that is complementary to the Canadian regime.

Guidelines for Cover Legends

In an effort by NASAA to keep its statements of policy, guidelines, and other publications current and consistent with the ever-changing statutory and regulatory environment, the Corporation Finance Policy Project Group conducted a top-to-bottom review of its corporation finance-related publications. In its first year, the Project Group completed a review of nine guidelines and statements of policy. The Project Group identified six guidelines and statements of policy as obsolete and outdated and recommended that they be revoked. The Group also updated the Uniform Disclosure Guidelines - Legends, which are intended to assist issuers and attorneys in writing uniform cover legends. NASAA expects the updated guidelines will lessen the regulatory burden on issuers and harmonize and reduce the number of deficiency comments issued by examiners.

Direct Participation Programs

The Direct Participation Programs Policy Project Group organized NASAA's 2004 comments supporting an NASD proposal to include trail commissions within the limitations on compensation for the sale of commodity Direct Participation Programs (DPPs). Since 1982, these commissions have been excluded from the limitation on underwriting compensation. NASAA believes that uncapped trail commissions result in very high selling compensation in commodity pool offerings, putting the compensation payable for such offerings far out of line with that payable for other types of offerings. NASAA also urged NASD to scrutinize sales contests of DPPs carefully.

Franchise Issues

The Section's Franchise and Business Opportunities Project Group focused much of its effort in 2004 on reviewing the Federal Trade Commission's staff report proposing revisions to the FTC's franchise rule. The report proposes that the FTC adopt a new, national franchise disclosure standard based in large part on the Uniform Franchise Offering Circular Guidelines adopted by NASAA in 1993. Working in conjunction with the FTC, the Project Group also took steps to educate prospective franchisees about franchise sales brokers.

Corporate Governance

NASAA generally supports measures proposed to strengthen corporate governance standards as a positive step toward protecting investors and helping restore their confidence. Enforcement actions brought by NASAA Members and the SEC underscore the fact that the structures of many mutual fund boards are inadequate to effectively oversee fund management. Based on the work of the Shareholder Rights Project Group, NASAA supported SEC efforts to enhance the ability of fund boards of directors to manage conflicts of interest that arise between the fund adviser and the fund, noting that the SEC proposal is consistent with standards for fund management that recently have been adopted by the administrators of several large state pension funds. In a separate comment letter, also based on the efforts of the Shareholder Rights Project

Group, NASAA urged the SEC to examine its proxy rules with a view toward providing long-term security holders with meaningful input into the selection of company directors.

Church Extension Fund Securities

The Section's Non-Profit Project Group recommended, and the Membership agreed, to replace the existing NASAA Statement of Policy Regarding Church Extension Fund Securities. The new statement of policy, which includes extensive technical updates and enhancements to financial standards and disclosure provisions, will facilitate a reasonable level of investor protection without inhibiting capital formation by Church Extension Funds and will also promote more uniformity among NASAA members that require either registration or an exemption filing for securities of non-profit organizations.

Training

The Corporation Finance Section conducted two training seminars in 2004, including sessions devoted to franchise examiner training and corporate financing issues. In June, the annual Franchise & Business Opportunity Training Seminar attracted 35 NASAA participants. In July, 78 NASAA participants attended the annual Corporation Finance Training Seminar, where Philip Rutledge, formerly with the Pennsylvania Securities Commission, was presented with the Corporation Finance Section's Distinguished Service Award. ■

2004 CORPORATION FINANCE SECTION

SECTION COMMITTEE

Denise Voigt Crawford (TX), Chair
Jack Herstein (NE), Vice Chair
Timothy F. Cox (MD)
Tim Le Bas (CA)
Lynn Naefach (PA)

PROJECT GROUPS

Corporation Finance Policy

Tim Cox (MD), Chair
Bill Beatty (WA)
Sylvia Miller (IN)
Gayle Oshima (CA)
Don A. Raschke (TX)

Direct Participation Programs Policy

Rebecca J. Alford (PA), Chair
Peter Cassidy (MA)
Mark Heuerman (OH)
Patricia Louterback (TX)
Michael McManus (DC)
Susan Baker Toth (AZ)

Franchise and Business Opportunities

Dale Cantone (MD), Chair
Martin Cordell (WA)
Henry Lew (CA)
Steve Maxey (VA)
Joseph Punturo (NY)
Brian Stern (RI)

Non-Profit Debt Offerings

Steve Wassom (KS), Chair
Elvin Farr (AZ)
Karen D. Wildmo (MI)

Shareholder Rights

Robert M. Lam (PA), Chair
Mark Connolly (NH)
Gina Gombar (MA)
Wayne Howell (GA)
Tim Le Bas (CA)
Patricia Struck (WI)
David Weaver (TX)

Small Business

Mike Stevenson (WA), Chair
Brenda Benham (BC)
George Close (FL)
Russel Taulli (TX)

Trading and Exchanges

Randall Schumann (WI), Chair
Rosetta Gagliardi (PQ)
Robin Golivesky (GA)
Robert Hudson (BC)
Henry Withers (CO)

Enforcement

OVERVIEW

NASAA Members have compiled an impressive record in bringing enforcement actions, including criminal prosecutions. Enforcement against fraud is the essence of what state and provincial securities regulators do -- to protect investors and to appropriately sanction and punish those who would harm or defraud investors. NASAA assists its Members in coordinating enforcement efforts regarding multi-state frauds by facilitating the sharing of information and leveraging the resources of the states more efficiently. NASAA's Enforcement Section acts as a point of contact for other federal agencies and the self-regulatory organizations, such as the SEC, the FBI, the Postal Inspectors, the NASD, and the NYSE; and helps identify new fraud trends.

NASAA's 2003-2004 Enforcement Section was chaired by Alabama Securities Director Joseph P. Borg; James B. Ropp, Delaware Securities Commissioner, served as Vice Chair. Section members included: Virginia Jo Dunlap, California; Richard Gerber, Pennsylvania; David Massey, North Carolina; and Glenda Campbell, Alberta, served as the Section's Canadian Liaison.

The Section oversaw the activities of seven Project Groups, including: Attorney/Investigator Training (Chair: Peter Jamison, Delaware); Enforcement Database (Chair: A. Duane Fry, Georgia); Internet Enforcement (Chair: Colin McCann, Ontario); Litigation Forum (Chair: Doug Ommen, Missouri); Special Project Development & Coordination (Chair: Zachary Ortenzio, Pennsylvania); Unregistered Securities Products/Unregistered Persons (Chair: Michael Byrne, Pennsylvania); and Viaticals (Chair: Wiley Kannarr, Kansas).

2004 ACTIVITIES

Investment Banking/Research Analyst Settlement

On August 26, NASAA, the California Department of Corporations, the SEC, NASD, and NYSE, announced the settlement of investigations of conflict of interest allegations between investment banking and research analysts at Deutsche Bank Securities and Thomas Weisel

Partners. These settlements are tied to the April 2003 Global Settlement that other investment banks reached with the SEC, state securities regulators, NASD, and the NYSE. Under the settlement agreement, Deutsche Bank and Thomas Weisel will pay a combined total of \$67.5 million in fines and disgorgement and \$27.5 million to fund independent research. In addition, Deutsche Bank will pay \$5 million to fund and promote investor education.

California was the lead state participating in both investigations. The District of Columbia and Maryland securities regulators assisted California on the Deutsche Bank investigation. Model settlement agreements have been finalized and the NASAA Board of Directors has recommended them to the states.

Operation Roaming Charge

In October, U.S. Attorney General John Ashcroft acknowledged the role of NASAA members in the most extensive multinational enforcement operation ever directed at telemarketing fraud schemes. "Operation Roaming Charge," spearheaded by the U.S. Department of Justice, led to the arrest of more than 135 individuals worldwide. Special thanks go to Idaho and Virginia, which submitted cases included in the operation's case summary. To date, more than 190 U.S. and Canadian search warrants have been executed as part of the operation and 70 individuals have been convicted in the United States. In addition, state attorneys general have brought 279 criminal, civil and regulatory actions against illegal telemarketing operations. The ongoing action uncovered every major category of telemarketing fraud.



NASAA Enforcement Section Chair Joseph P. Borg (AL), Section Vice Chair James B. Ropp (DE) and Section Member Virginia Jo Dunlap (CA) at the Enforcement Section Forum during the 2004 NASAA Annual Conference.

Internet Enforcement

The Internet continues to play a greater role in investment research and transactions in North America. To help protect investors from Internet-based fraud, NASAA's Internet Enforcement Project Group prepared a resource package to educate investigators on current techniques and procedures for investigating cyberfraud. Members of the project group also served as panelists in discussions of Internet investment fraud at the Economic Crime Summits of the National White Collar Crime Center (NW3C).

Viaticals

NASAA's Viaticals Project Group monitored the progress of a task force created in the aftermath of actions by the SEC and the Florida Department of Financial Services-Office of Insurance Regulation against Mutual Benefits Corporation. State and federal regulators shut down Mutual Benefits Corporation, of Fort Lauderdale, Florida, in 2004 after lengthy investigations by the Florida Office of Insurance Regulation and the SEC. Florida's Office of Statewide Prosecution has charged the company with racketeering and 15 counts of investor fraud, saying the company lured tens of thousands of investors into an elaborate Ponzi scheme that raised more than \$1 billion. A task force of members of NASAA met with receiver Roberto Martinez and is coordinating the collection and distribution of records relating to Mutual Benefits.

Public Outreach

The Enforcement Section, in conjunction with the Corporate Office, continued to take proactive steps to inform the public about new trends in investment fraud with the annual release of the NASAA Top 10 List of scams, schemes and scandals. NASAA President Lambiase was joined by Section Chair Borg in a news conference to announce the 2004 list and to announce that NASAA created an interactive Fraud Center on its website to help inform investors about investment fraud. The following ranking of NASAA's Top 10 scams, schemes and scandals for 2004 is based on the order of prevalence and seriousness as identified by state securities regulators: 1) Ponzi Schemes, 2) Senior Investment Fraud, 3) Promissory



The Enforcement Section Forum at the 2004 NASAA Annual Conference attracted a large audience of NASAA Members and industry representatives.

Notes, 4) Unscrupulous Broker/Dealer Representatives, 5) Affinity Fraud, 6) Insurance Agent Securities Fraud, 7) Prime Bank/High-Yield Investment Schemes, 8) Internet Fraud, 9) Mutual Fund Business Practices, 10) Variable Annuities.

Enforcement Outreach & Training

NASAA took steps in 2004 to reach out to other regulators at both the state and federal levels on issues of common interest. For example, in May, NASAA successfully joined forces with the National Association of Insurance Commissioners to conduct the first-ever joint training program to benefit state insurance and state securities regulators who want to work together more effectively to solve the persistent problem of securities fraud by insurance agents. NASAA's annual Winter Enforcement Conference attracted nearly 160 NASAA participants for a two-day session featuring panel discussions on mutual fund sales practices, hedge funds, and ethics; the increasing use of technology in enforcement cases; and emerging trends in fraudulent activities. Alabama Congressman Artur Davis and *USA Today* columnist John Waggoner addressed the welcoming and keynote luncheons. The Section also presented Massachusetts Secretary of the Commonwealth William Galvin and Massachusetts Securities Division Director Matthew Nestor with the NASAA Annual Enforcement Award. The Section's Attorney Investigator Training, attended by 145 NASAA participants, offered a two-day seminar covering the fundamentals of securities enforcement. ■

2004 ENFORCEMENT SECTION

SECTION COMMITTEE

Joseph Borg (AL), Chair
 James Ropp (DE), Vice Chair
 Virginia Jo Dunlap (CA)
 Richard Gerber (PA)
 David Massey (NC)
 Glenda Campbell (AB), Canadian Liaison

PROJECT GROUPS

Attorney/Investigator Training

Peter Jamison (DE), Chair
 T. Webster Brenner (MD)
 Daniel Clarke (OK)
 William Harmening (IL)
 Tracy Meyers (SC)
 Susan Schoaps (OR)
 Jamie Sharp (CO)

Enforcement Database

A. Duane Fry (GA), Chair
 James Burns (ID)
 Rodney Griess (NE)
 Charles Kaiser (OK)
 Patricia Moy (HI)
 Baldemar Quintanilla (TX)

Internet Enforcement

Colin McCann (ON), Chair
 Robert Brunner (OR)
 David Cohen (WI)
 Joseph Punturo (NY)
 Alfred Rusch (DC)

Litigation Forum

Doug Ommen (MO), Chair
 Chris Biggs (KS)
 Joe Brady (MS)
 Jim Joven (IN)
 Randy McNeill (AL)
 Jeffrey Spill (NH)
 Mary Beth Taylor (VA)
 Doug Brown (MB)

Special Project Development & Coordination

Zachary Ortenzio (PA), Chair
 Terry Bolte (CO)
 Ricky Locklar (AL)
 David Ruhnke (KS)
 Sharon Sloan (NM)

Unregistered Securities Products/Unregistered Persons

Michael Byrne (PA), Chair
 Asdrubal Aponte (PR)
 Bruce Kohl (NM)
 Robert Koppin (IA)
 Constance Melton (TX)
 Allan Russ (NC)
 Caroline Smith (OR)

Viaticals

Wiley Kannarr (KS), Chair
 Lucy Cardwell (MD)
 Maliaka Bass EssamelDin (TN)
 John Michael Foley (AL)
 Joseph Oman (TX)
 James Openshaw (CA)

Zones

Zone 7 (Western)
 David Tatman (OR), Chair
Zone 1 (Northeast)
 David Briden (RI)
Zone 2 (Southeast)
 Dale Clements (TN)
Zone 3 (Mid-Atlantic)
 Katharine Weiskittel (MD)
Zone 4 (Central)
 Sonya Lester (IA)
Zone 5 (South/Central)
 David Grauer (TX)
Zone 6 (Mountain)
 Karen Powell (MT)
Zone 8 (Canadian)
 Brian Butler (ON)

Investment Adviser

OVERVIEW

The primary goal of NASAA's Investment Adviser Section is to help NASAA Members protect investors by making the regulation of small investment advisers more manageable. Through careful licensing and on-site examinations, NASAA Members protect investors from malfeasance ranging from overreaching sales practices to outright fraud. NASAA Members believe it is critical that information about investment advisers be readily accessible to the investing public, industry, and regulators. NASAA members have made much progress in streamlining the regulatory process for investment advisers. Recognizing that good compliance programs have costs associated with them, especially for small firms that make up the majority of the industry, NASAA Members remain committed to keeping these costs as low as possible while continuing to protect the interests of investors.

NASAA's 2003-2004 Investment Adviser Section was chaired by Wisconsin Securities Administrator Patricia D. Struck; Theodore A. Miles, Director of the District of Columbia Securities Bureau, served as Vice Chair. Section members included: Colleen Keefe, Kentucky; Kristina Kneip, Washington; Ron Thomas, Virginia; and Barbara Shourounis, Saskatchewan, served as the Section's Canadian Liaison.

The Section oversaw the activities of five Project Groups, including: Operations (Chair: Michael Huggs, Mississippi); Outreach (Chair: Theodore Miles, District of Columbia); Regulatory Policy and Review (Chair: Kristina Kneip, Washington); Zones (Chair, Colleen, Keefe, Kentucky) and Training (Chair: Richard White, Florida).

The Section also works closely with the NASAA Board CRD/IARD Steering Committee, chaired by Maryland Securities Commissioner Melanie Senter Lubin.

2004 ACTIVITIES

Investment Adviser Regulation

NASAA has consistently encouraged the SEC to minimize investor and industry confusion by clarifying all issues tied to the incidental practice of advisory services. In 2004,

NASAA submitted comments on an SEC proposal that would permit brokerage firms to charge asset-based fees to their customers without automatically meeting the definition of investment adviser. The proposed rule would, among other provisions, exempt certain broker-dealers offering investment advice to clients from registration under the Investment Advisers Act, provided that any advice offered is on a non-discretionary basis and is solely incidental to brokerage services provided, and disclosure is made to the clients that their accounts are brokerage accounts. NASAA also believes agents of broker-dealers marketing wrap fee programs should register as investment adviser representatives.

Hedge Funds

NASAA Members are increasingly engaged in an ever-rising number of investigations and enforcement actions regarding hedge funds, their managers, and advisers. The expansion of the hedge fund industry's scope and its increasing flow of assets supports the proposition for additional regulatory oversight and monitoring of hedge fund advisers and their affiliates. For that reason, NASAA in 2004 supported the SEC's rule to require hedge fund advisers to register under the Investment Advisers Act of 1940. NASAA also supports raising the threshold for state registration of hedge fund and investment advisers from \$25 million to \$50 million in assets.



Patricia Struck (WI), Chair of NASAA's Investment Adviser Section and 2004-2005 President-elect, addresses the Membership at the 2004 Annual Conference.

Mutual Funds

The Investment Adviser Section, along with the Broker-Dealer and Corporation Finance Sections, played an active role in NASAA's efforts to ensure that the interests of mutual fund investors are fully protected. Specifically, Section members assisted with the preparation of a series of comment letters to the SEC regarding several mutual fund rules, including: disclosure requirements of mutual fund portfolio managers; requirements addressing how a fund's board of directors evaluates, approves and recommends an investment advisory contract to shareholders for approval; and rules that further enhance the independence and effectiveness of chief compliance officers of investment companies and investment advisers. NASAA also commended the SEC for adopting rules under the Investment Company Act of 1940 and the Investment Advisers Act of 1940 that require each investment company and investment adviser registered with the Commission to adopt and implement written policies and procedures to aid in the prevention of federal securities law violations.

IA Sweep and Best Practices

The Section's IA Operations and IA Zones project groups, developed a series of best practices in an effort to help investment advisers develop compliance programs that will minimize the potential for regulatory violations. The best practices, announced at the NASAA Annual Conference in September, were developed after a nationwide sweep of investment advisers by state examiners in 26 states revealed

a significant number of problem areas. Overall, the examinations found 588 deficiencies in 15 compliance areas. The greatest number of deficiencies identified in the sweep involved registration and the two most common registration deficiencies involved inaccurate disclosures on the Form ADV and failing to annually offer an updated Form ADV to clients. Based on the sweep results, NASAA proposed a series of 10 "Best Practices" to help advisers develop compliance practices and procedures.



Melanie Senter Lubin (right), Maryland Securities Commissioner and Chair of the NASAA CRD/IARD Steering Committee, makes a point during the Ombudsman Meeting at the 2004 Annual Conference as Fred Joseph (CO) looks on.

Codes of Ethics

NASAA Members have a long history of taking proactive measures to keep investment advisers from committing unethical business practices and to hold them accountable for violations of their fiduciary obligations to their clients. NASAA, through the Investment Adviser Section, voiced support in 2004 for the SEC's amendment to the Investment Advisers Act of 1940 to require advisers to adopt and enforce a Code of Ethics applicable to supervised persons as a best practice, but noted concern that a regulatory mandate of a written Code of Ethics is not the most appropriate method for ensuring compliance with the existing fiduciary duties of investment advisers. NASAA Members remain concerned that advisers may characterize the Code of Ethics as an official imprimatur from regulators that a firm has been recognized as meeting a higher standard of conduct. By itself, the creation of a Code of Ethics amounts to a cosmetic method of addressing the real problem: conflicts of interest and unethical business practices.

CRD/IARD Forms and Process

Form ADV

Under the Direction of the NASAA Board CRD/IARD Steering Committee, NASAA and SEC staff continued in 2004 to revise Part II of Form ADV and facilitate its filing and public disclosure through the Investment Adviser Registration Depository (IARD) and Investment Adviser Public Disclosure system (IAPD).

These much-needed revisions, which include the addition of investment adviser brochure information and the electronic filing of Part II, are priorities for NASAA.

Model Custody Rules

Based on a recommendation from the Investment Adviser Regulatory Policy and Review Project Group, and approval by the NASAA Board of Directors, the Membership voted to approve amendments to the NASAA Model Custody Rules for Advisers. The amendments were necessary following the 2003 approval of SEC amendments to the custody rule under the Investment Advisers Act of 1940. Because changes to the federal rules are not automatically applicable to non-federally registered investment advisers, changes in NASAA model rules were necessary to provide an element of uniformity between the regulation of federal and state registered investment advisers, while continuing to protect investors.

Examinations

The Section focused considerable attention in 2004 on training staff members from NASAA jurisdictions on the use of new modules for examinations of investment advisers. The Section's Investment Adviser Operations Project Group modified the performance reporting module and instructions to reflect new AIMR reporting standards as well as to make the module more user-friendly. The group also created an "exam builder" page within the examination

modules designed to help examiners prepare, organize, and navigate through the examination modules. Following adoption at the 2004 Spring Conference of the NASAA Model Custody Rule for Advisers, the Sections' Investment Adviser Operations Project Group began modifying the custody module to track the rule.

Investment Adviser Training

The Section also continued to prepare resources to help NASAA Members inform investment advisers within their jurisdictions on what they need to know to comply with state or provincial laws and to train staff members from a number of jurisdictions on the use of new modules for examinations of investment advisers. The Investment Adviser Training Group held the annual Investment Adviser Training Workshop, attracting 128 NASAA participants from 41 jurisdictions. During the training, Maryland Securities Commissioner Melanie Senter Lubin was presented with the Investment Adviser Section's Distinguished Service Award for consistently demonstrating "an unparalleled level of service in advancing the interests of investor protection, notably as the primary author of Form ADV Part 2 and as NASAA's architect of IARD." ■

2004 SECTION AND PROJECT GROUP LIST

SECTION COMMITTEE

Patricia D. Struck (WI), Chair
Theodore A. Miles (DC), Vice Chair
Colleen Keefe (KY)
Kristina L. Kneip (WA)
Ronald Thomas (VA)
Rick White (FL)
Barbara Shourounis, (SK), Canadian Liaison

PROJECT GROUPS

Operations

Michael Huggs (MS), Chair
Phi Duong (TX)
Alisa Goldberg (FL)
Dale Laswell (OR)
Barbara Olson (WI)
John Reese (VT)
David Swafford (CO)
Audrey Thrift (VA)

Outreach

Theodore Miles (DC), Chair
Rosemarie Mares (NM)
Dora Meija (CA)
William Stone (KY)
Henry Tanji (HI)
Richard Unangst (AZ)

Regulatory Policy & Review

Kenneth Hojnacki (WI), Chair
Jay Knight (DC)
Edwin Reed (AL)
Paul M. Schwartz (PA)
David Smith (AR)
Jackie Van Cura (NE)
Jean-Richard Beauboeuf (MI)

Training

Richard White (FL), Chair
Carmen Bishop (KY)
J.B. Cassidy (CO)
Kerri Dixon (MA)
David Finnigan (IL)
William Ruff (WI)
Richard Squires (NF)
Gina DeCamp (WA)

Investor Education

OVERVIEW

NASAA Members have a long tradition of protecting investors through financial education. Most state and provincial securities regulators have established investor education programs within their agencies. The result is an effective network of dedicated professionals delivering financial education at the grassroots level. NASAA Members have traditionally been a highly effective resource in the pursuit of greater financial literacy, delivering the message of financial education on a daily basis and coordinating efforts with each other to share and leverage resources. The Investor Education Section, along with a network of professionals from across the NASAA Membership, develops, coordinates, delivers, and supports financial education initiatives used by securities regulators in their on-going efforts to improve the level of financial literacy in their jurisdictions. The Section also supports and participates in a variety of national financial education programs to increase financial literacy, such as the American Savings Education Council, the Investor Protection Trust, Jump\$tart Coalition for Financial Literacy, and Financial Literacy 2010.

NASAA's 2003-2004 Investor Education Section was chaired by North Dakota Securities Commissioner Karen Tyler; Fred Joseph, Colorado Securities Commissioner, served as Vice Chair. Section members included: Glen Gainer, West Virginia; Karen Terhune, Ohio; Terri Williams, Ontario; and Adrienne Salvail-Lopez, British Columbia, served as the Section's Canadian Liaison.

The Section oversaw the activities of five Project Groups, including: Affinity and Ethnic-Based Outreach (Chair: Fred Joseph, Colorado); Coordination (Chair: Karen Terhune, Ohio); Online Trading Awareness (Chair: Diane Young-Spitzer); Senior Outreach (Chair: Robyn Goodman, California); and Youth Outreach (Chair: Diane Kambeitz, North Dakota).

2004 ACTIVITIES

National Financial Education Strategy

Established under the Fair and Accurate Credit Transactions



Karen Tyler, North Dakota Securities Commissioner and Chair of NASAA's Investor Education Section, stresses the importance of financial education during the Investor Education Section Forum at the 2004 NASAA Annual Meeting.

Act of 2003, the Financial Literacy and Education Commission (FLEC) includes representatives of 20 federal agencies and seeks to create a national strategy to improve financial education and literacy in the United States. NASAA Members share FLEC's concerns about the current level of financial literacy in the United States and are committed to pursuing constructive and proactive solutions.

In 2004, NASAA Investor Education Chair Tyler testified before the FLEC to address the many ways state securities regulators deliver investor education. NASAA 2004-2005 President Widmann also submitted written comments to the committee concerning FLEC's national strategy and urged the FLEC to address two key issues as it formulated its national strategy: prevention of financial fraud and development of basic money management and savings skills. While developing a national financial strategy is a bold undertaking, NASAA believes there are abundant resources currently available, including educational materials, monies available through grants and other programs, and numerous dedicated individuals now working to deliver financial education to the public.

Senior Outreach

NASAA Members are deeply concerned that millions of seniors in North America face a perfect storm for investment fraud. State and provincial securities regulators

NASAA YEAR IN REVIEW 2004

are committed to providing resources to help older investors better educate and protect themselves against investment fraud. In 2004, NASAA members continued to raise awareness of the dangers of investment fraud among seniors and continued to enhance the Senior Investor Resource Center on the NASAA website. NASAA's Senior Outreach Project Group also developed a tool kit and resource guide to help promote anti-fraud education programs using volunteers and peer educators in member jurisdictions. In March 2004, NASAA Broker-Dealer Section Chair Tanya Solov (IL) testified before the Senate Special Committee on Aging that seniors are facing increasing risks of Internet investment exploitation.

Online Trading Awareness

With millions of investors turning to the Internet to buy and sell investments, NASAA members remain concerned that they have proper resources and tools to protect themselves from online investment scams. In 2004, NASAA's Online Trading Awareness Project Group developed "Teens and Online Investing," a brochure designed to attract the attention and educate an increasingly large segment of the population drawn to the Internet. The group also took steps to enhance the Investing Online Resource Center website.

Youth Outreach

As part of a continuing effort to improve the level of youth financial literacy in our jurisdictions, NASAA's Investor Education Section's Youth Outreach Project Group has developed a Teacher Training Event blueprint to provide a comprehensive, step-by-step system for developing and delivering a teacher training event that offers K-through-12 teachers the knowledge, resources, and tools they need to efficiently and effectively integrate personal finance education into their classroom curriculums. Based on the project group's recommendation, NASAA also joined with the Jump\$tart Coalition for Financial Literacy in supporting the Financial Literacy for Youth Month and trained teachers to use the Financial Literacy 2010 five-unit curriculum, "Personal Finance for the Economics Classroom," which teaches students economic concepts and the importance of saving and investing.

Public Outreach

Under the direction of the NASAA Board Communications Committee, NASAA took several steps to enhance the association's delivery of key messages and outreach to the public in 2004.

NASAA was mentioned or quoted in more than 1,500 articles in publications throughout the world, including: The New York Times, Wall Street Journal, Washington Post, USA Today, BusinessWeek, the International Herald Tribune, the China Daily, and the Toronto Globe and Mail.

The Committee also oversaw the redesign of the NASAA website (www.nasaa.org) and the development and distribution of NASAA's advocacy brochure, Putting Investors First.



NASAA's newly redesigned and enhanced website offers users more resources and improved navigation.

Ethnic and Affinity Outreach

NASAA Members are acutely aware of the diversity in their communities and work hard to develop materials and programs accessible to all of our residents, and in languages from Spanish to Cantonese. There is much work being done to ensure that those of our citizens most in need can find the help they need to make the critical first steps toward financial literacy. In 2004, the Section's Ethnic and Affinity Outreach project group continued to explore methods to expand the use of multilingual resources in NASAA member jurisdictions.

Investor Education Coordination

In an effort to enhance the delivery of investor education materials to the public, NASAA's Investor Education Coordination Project Group served as a clearinghouse for information on investor education initiatives within NASAA jurisdictions. Group members also continued to enhance NASAA's library of educational materials from Member jurisdictions and expanded the library to include online publications. The group also continued efforts to develop a "Securities 101" kit to help NASAA members increase awareness within the law enforcement community of securities products and scams.

2004 Investor Education Training Seminar

The Section's 2004 Investor Education Training Seminar attracted 85 NASAA participants for a two-day session of panel discussions on subjects ranging from survey-based research, partnerships with non-profits, to steps and tips on completing grant applications. Attendees also shared ideas, experiences and materials during interactive sessions focused on new programs, and the Senior Outreach Project Group unveiled its comprehensive package of materials designed to help other jurisdictions implement programs modeled after California's Seniors Against Investment Fraud initiative. NASAA President Widmann, in an address to attendees, emphasized the importance of investor education to NASAA and its Members. ■

2004 SECTION AND PROJECT GROUP LIST

SECTION COMMITTEE

Karen Tyler (ND), Chair
 Fred J. Joseph (CO), Vice Chair
 Glen B. Gainer (WV)
 Karen L. Terhune (OH)
 Terri Williams (ON)
 Adrienne Salvail-Lopez (BC), Canadian Liaison

PROJECT GROUPS

Affinity and Ethnic-Based Outreach

Susan Powell (NF), Chair
 Fred Joseph (CO)
 Ron Claiborne (DC)
 Katholene Palmero (MO)
 Ethel Zoe Rossi (AR)

Coordination

Karen Terhune (OH), Chair
 Elizabeth Block (NY)
 Tryllis Hallford (GA)
 Daniel Lord (AL)
 Perry Quinton (ON)
 Angela Cichocki (KS)

Online Trading Awareness

Diane Young-Spitzer (MA), Chair
 Amanda Blanks (VA)
 Beverly Simcoe (NM)
 Katharine Weiskittel (MD)
 Bill Wilkerson (MS)
 Anthony Wong (BC)

Senior Outreach

Robyn Goodman (CA), Chair
 Elizabeth Flynn (MA)
 Scott Kirby (NH)
 Christina Kotsalos (PA)
 Pam Ruckel (NV)
 Lisa Tolar (AL)

Youth Outreach

Diane Kambeitz (ND), Chair
 Felipe Cruz (PR)
 JoAnn Kocurek (TX)
 Vickie Moseley (IL)
 Justin Southern (WV)

TRAINING & CONFERENCES

TRAINING OVERVIEW

Educating and training our members is a vital part of NASAA's mission. In 2004, NASAA hosted 10 training seminars, which attracted 881 participants. In addition to the joint NASAA/NAIC training seminar, other NASAA training seminars included sessions devoted to broker-dealer, investment adviser, franchise, corporation finance, investor education, electronic examination module, CRD/IARD, attorney/investigator and joint regulatory issues. NASAA's emphasis on training helps promote uniformity by ensuring that state examiners, investigators and prosecutors are schooled in the current problem areas so that they can more effectively regulate the securities industry and serve investors.



NASAA Board Member Craig Goettsch (IA) makes a point during the 2004 Spring Conference as Tanya Solov (IL) and James Joven (IN) look on.



NASAA Member (left to right) Rhonda Reeves (LA), and Board Members Christine A. Bruenn (ME) and Donald Murray (MB) at the 2004 Spring Conference Membership Meeting.

CONFERENCE OVERVIEWS

2004 Spring Conference Report

NASAA's Spring Conference, held in Washington, DC, began with welcoming remarks by Washington Mayor Anthony Williams, who offered his appreciation of the importance of securities regulation and enforcement at the state/provincial level. Maryland Securities Commissioner Melanie Lubin, introduced keynote speaker Senator Paul Sarbanes (MD), the Ranking Member on the Senate Banking Committee, who pledged to defend state securities regulators from attempts to preempt their regulatory authority. "I am opposed to efforts that would back state regulators out of the system," he said. "I also concur that there is no reason to make radical changes in a system that has worked well for decades." Noting that there is no preemption legislation pending in the Senate, Sarbanes added: "We'll do our best to ensure that none gets approved if it's presented."

The luncheon was followed by two panel discussions. The first, a review of functional regulation of financial services, was moderated by Don Saxon (FL), Vice Chair of NASAA's Broker-Dealer Section, and featured panelists from the U.S. Treasury Department, U.K. Financial Services Authority, Federal Reserve Board, and the Financial Services Roundtable. The second panel discussion focused on the relationship between ethics and business. Moderator Tanya Solov (IL), Chair of NASAA's Broker-Dealer Section, noted that recent corporate scandals have exposed an erosion of ethical standards.



Don Saxon (FL), Vice Chair of NASAA's Broker-Dealer Section, and U.S. Treasury Department Assistant Secretary for Financial Institutions Wayne Abernathy (right), participate in a panel discussion on functional regulation at the 2004 NASAA Spring Conference.

2004 Annual Conference Report

NASAA's 87th Annual Conference, chaired by Arizona Director of Securities Matthew Neubert, brought more than 430 regulators and industry representatives to Scottsdale, Arizona, between September 30 and October 2. Following opening remarks from Conference Chair Neubert and Arizona Corporation Commission Chairman Marc Spitzer, Wall Street veteran Joseph Grano made a strong case for the importance of restoring investor confidence in our markets. Grano, the former UBS/PaineWebber Chairman & CEO and now head of Centurion Holdings, also briefed the audience on current security issues related to his role as Chairman of the Homeland Security Advisory Council. The opening day's program also featured a panel discussion moderated by Tanya Solov (IL) examining hybrid investment



NASAA Board Member Scott Borchert (MN) opens a panel discussion examining the current status of state financial services regulation at the 2004 Annual Conference.

NASAA YEAR IN REVIEW 2004



NASAA's Membership includes representatives from Canada, Mexico and Puerto Rico; above, Omar A. Martinez Villada, of Mexico's Comision Nacional Bancaria y de Valores, addresses NASAA Members during the 2004 Annual Conference.



NASAA President Ralph Lambiase (right) and keynote speaker Joseph Grano, former Chairman and CEO of UBS/PaineWebber at the 2004 NASAA Annual Conference.



NASAA 2004-2005 President Franklin L. Widmann (NJ) delivers the President's Remarks during the 2004 Annual Conference and outlines three key areas - training, investor education, and enforcement - that NASAA will emphasize in 2005.

products. Among the panelists were Jim Nelson (MS) and Elizabeth Jetton, President of the Financial Planning Association.

The second day began with a panel discussion moderated by Scott Borchert (MN) exploring the status of state financial services regulation. Panelists included Craig Goettsch (IA); legislator Donna Stone, who appeared on behalf of the National Conference of State Legislatures (NCSL); and Kevin Lavender, Tennessee Commissioner of Financial Institutions, who appeared on behalf of the Conference of State Bank Supervisors (CSBS). A second morning panel, moderated by Karen Tyler (ND) and including Assistant Treasury Secretary Wayne Abernathy, discussed current trends in financial education. Friday's keynote speaker, CNN Financial Editor Myron Kandel, offered an overview of the evolution of financial journalism.

The conference's closing day began with a panel discussion of cooperative international enforcement efforts moderated by Joe Borg (AL), followed by the Presidential Address of 2004-2005 NASAA President Frank Widmann (NJ). In his speech, President Widmann called upon regulators and the securities industry to continue to work together to restore market integrity. "Together, we must

honor our responsibilities to ensure that all investors are treated fairly," he said. At the NASAA Business Meeting on October 2, Mr. Widmann officially succeeded Ralph Lambiase (CT) as President. Mr. Lambiase will continue to serve on the 2004-2005 Board as Past President.

Mark your calendars now for our 88th Annual Conference, which will be held next September 11-14 at the Hilton Minneapolis. ■

NASAA LISTS

NASAA ORGANIZATION

The following pages contain several NASAA directories, including listings of:

- 2003-2004 Board of Directors
- 2004-2005 Board of Directors
- 2003-2004 Board Committees and Project Groups
- 2004-2005 Board Committees and Project Groups
- 2004-2005 Sections & Project Groups
- 2004 NASAA Awards



NASAA's Board of Directors, Section Chairs and Vice Chairs at the 2004 Spring Conference. Front row l-r: Joseph Borg (AL), Denise Voigt Crawford (TX), Franklin L. Widmann (NJ), Ralph A. Lambiase (CT), Christine A. Bruenn (ME), Deborah A. Bortner (WA), Craig A. Goettsch (IA). Second row l-r: Karen Tyler (ND), Tanya Solov (IL), Patricia Struck (WI), Melanie Senter Lubin (MD), James B. Ropp (DE), Don Saxon (FL), Robert Lam (PA), Donald Murray (MB), Daphne Smith (TN), Scott Borchert (MN), Fred Joseph (CO), Phillips B. Keller (VT), Jack E. Herstein (NE), Anthony Taggart (UT), John H. Hanley (NASAA). Not pictured: Theodore Miles (DC).

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President-Elect

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Maine
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Secretary

Craig A. Goettsch
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Treasurer

Scott P. Borchert
Minnesota
Director

Deborah A. Bortner
Washington
Director
(to April 2004)

Anthony W. Patey
Newfoundland and Labrador
Director
(to April 2004)

Donald G. Murray
Manitoba
Director
(from April 2004)

S. Anthony Taggart
Utah
Director

Robert M. Lam
Pennsylvania
Ombudsman

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Alabama
Director
(from January 2005)

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Maryland
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(from November 2004 to January 2005)

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Manitoba
Director

James O. Nelson II
Mississippi
Director

James B. Ropp
Delaware
Director

Ryan S. Ushijima
Hawaii
Director
(to October 2004)

Robert M. Lam
Pennsylvania
(Ombudsman)

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Communications

Daphne Smith (TN), Chair
Joseph Borg (AL)
Denise Voigt Crawford (TX)
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Patricia Struck (WI)
Karen Tyler (ND)

NASAA Corporate Governance

Ryan Ushijima (HI), Chair
Scott Borchert (MN)
Craig Goettsch (IA)
Patricia McKenna (MD)
James Joven (IN)
Michael Stevenson (WA)

CRD/IARD Steering

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Phillips Keller (VT), Vice-Chair
Pamela Epting (FL)
Alan Ford (KS)
Colleen Keefe (KY) [IA Section Liaison]
Sandy MacDonald (ON)
Don Saxon (FL) [BD Section Liaison]
Chester Thompson (WV)

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Kelvin Blake (MD), IA Vice-Chair
Larry Burton (TN)
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Rodney Griess (NE)
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International

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Felipe Cruz (PR)
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Ryan Ushijima (HI)

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Irving Faight (OK)
Denise Voigt Crawford (TX)
Toni Clithero (VT)

Federal Legislation

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Rick Fleming (KS)
Melanie Senter Lubin (MD)
Michael Vargon (NM)

Finance & Audit

Patricia McKenna (MD), Chair
Richard Morris (CO)
Ann Rankin (VA)

Standards, Certification and Training

Scott Borchert (MN), Chair
Janet Holmes (ON), Canadian Liaison

Investigators Sub-Group

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Carmen Bishop (KY)
Mark Klamrznynski (AZ)
Suzanne Sarason (WA)

Examiners Sub-Group

Felipe Cruz (PR)
Kelvin Blake (MD)
Susan Edwards (OK)
Terri Orton (NM)
David Risley (IN)

Technology Planning & Coordination Project Group

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Chad Harlan (KY)
Charles Kaiser (OK)
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Jim Nix (IL)
John Reese (VT)

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Fred Joseph (CO), Chair
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Phillips Keller (VT)
Theodore Miles (DC)
James Ropp (DE)
Don Saxon (FL)

Uniform Securities Act

Craig Goettsch (IA), Chair
Joseph Borg (AL)
Michael Stevenson (WA)

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Theodore Miles (DC)
Tanya Solov (IL)

NASAA Corporate Governance

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Craig Goettsch (IA)
James Joven (IN)
Ralph Lambiasi (CT)
Patricia McKenna (MD)
Michael Stevenson (WA)

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James Nelson (MS), Vice Chair
Kelvin Blake (MD)
Christine Bruenn (ME)
Pamela Epting (FL)
Alan Ford (KS)
Colleen Keefe (KY) [IA Section Liaison]
Don Saxon (FL) [BD Section Liaison]
Chester Thompson (WV)

CRD/IARD Forms and Process

Pamela Epting (FL), Chair
Alan Ford (KS), Vice-Chair (BD Issues)
Kelvin Blake (MD), Vice-Chair (IA Issues)
Larry Burton (TN)
Patricia Goracke (CA)
Rodney Griess (NE)
Susan Largman (NJ)
Sheryl Lemon (CO)
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Federal Legislation

James Ropp (DE), Chair
Rick Fleming (KS)
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Tom Michlovic (PA)
Michael Vargon (NM)
David Weaver (TX)

Finance & Audit

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Ann Rankin (VA)
Marion Renoll (PA)

International

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Felipe Cruz (PR)
Irving Faught (OK)
Don Saxon (FL)

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Robert McDonald (MD), Chair
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Toni Clithero (VT)
Denise Voigt Crawford (TX)
Irving Faught (OK)

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Carmen Bishop (KY)
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Charles Kaiser (OK)
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Michael Stevenson (WA)

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Scott Borchert (MN)
Craig Goettsch (IA)
Patricia Struck (WI)

Zone Assignments

North East: Ralph Lambiasi (CT)
South East: James Nelson (MS)
Mid-Atlantic: James Ropp (DE)
Central: Patricia Struck (WI)
South Central: Melanie Lubin (MD)
Mountain: Karen Tyler (ND)
Western: Fred Joseph (CO)
Canadian: Donald Murray (MB)

2004-2005 SECTIONS & PROJECT GROUPS

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 Tanya Durkee (VT)
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 Jeffrey Spill (NH)
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 Ricky Locklar (AL)
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NASAA YEAR IN REVIEW 2004

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 Zone 3 (Mid-Atlantic) Katharine Weiskittel (MD)
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 Phi Duong (TX)
 Alisa Goldberg (FL)
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 David Swafford (CO)
 Audrey Thrift (VA)

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 Rosemarie Mares-Ulibarri (NM)
 Henry Tanji (HI)
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 Jay Knight (DC)
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 David Smith (AR)
 Jackie Van Cura (NE)

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 Karen Terhune (OH)
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 Marcelle Groves (CT)
 Dan Lord (AL)
 Ethel Zoe Rossi (AR)

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 Elizabeth Block (NY)
 Tryllis Hallford (GA)
 Perry Quinton (ON)
 Debbie Whipple (NJ)

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 Amanda Blanks (VA)
 Katharine Weiskittel (MD)
 Bill Wilkerson (MS)
 Anthony Wong (BC)

Senior Outreach

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 Shad Balch (CA)
 Elizabeth Flynn (MA)
 Christina Kotsalos (PA)
 Pam Ruckel (NV)

Youth Outreach

Justin Southern (WV), Chair
 Terri Alexon (AZ)
 Stephanie Beck (IN)
 JoAnn Kocurek (TX)
 Vickie Moseley (IL)
 Ty Nohara (HI)

2004 NASAA AWARDS

Blue Sky Cube

Ralph A. Lambiase (CT)

Outstanding Service Awards

Scott Borchert (MN)
 Deborah Bortner (WA)
 Craig Goettsch (IA)
 Anthony Patey (NL)
 Daphne Smith (TN)

Distinguished Service Awards

Kristina Kneip (WA)
 Phil Rutledge (PA)
 John Veator (NASAA Corporate Office)

NASAA 2004 Enforcement Award

William Galvin (MA)
 Matthew Nestor (MA)

NASAA Broker-Dealer Section Distinguished Service Award

Theodore A. Levine (Industry)

NASAA Corporation Finance Section Distinguished Service Award

Philip Rutledge (PA)

NASAA Investment Adviser Section Distinguished Service Award

Melanie Senter Lubin (MD)



NASAA

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