

# **NASAA Unethical Business Practices Of Investment Advisers, Investment Adviser Representatives, And Federal Covered Advisers**

## **Model Rule 102(a)(4)-1**

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### **Rule 102(a)(4)-1 Unethical Business Practices Of Investment Advisers, Investment Adviser Representatives, And Federal Covered Advisers**

[Introduction] A person who is an investment adviser, an investment adviser representative or a federal covered 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 advisers to the extent that the conduct alleged is fraudulent, deceptive, or as otherwise permitted by the National Securities Markets Improvement Act of 1996 (Pub. L. No. 104-290). While the extent and nature of this duty varies according to the nature of the relationship between an investment adviser or an investment adviser representative and its clients and the circumstances of each case, an investment adviser, an investment adviser representative or a federal covered adviser shall not engage in unethical business practices, including the following:

- (a) Recommending to a client to whom investment supervisory, management or consulting 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.
- (b) Exercising any discretionary power 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 power 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 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. The rule appropriately forbids an excessive number of transaction orders to be induced by an adviser for a "customer's account."
- (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 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 advisory client, or prospective advisory client, the qualifications of the investment adviser or any employee of the 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.
- (i) Providing a report or recommendation to any advisory client prepared by someone other than the adviser without disclosing that fact. (This prohibition does not apply to a situation where the adviser uses published research reports or statistical analyses to render advice or where an adviser orders such a report in the normal course of providing service.)
- (j) Charging a client an unreasonable advisory fee.
- (k) Failing to disclose to clients in writing before any advice is rendered any material conflict of interest relating to the adviser, or any of its employees which could reasonably be expected to impair the rendering of unbiased and objective advice including:
  - (1.) Compensation arrangements connected with advisory services to clients which are in addition to compensation from such clients for such services; and
  - (2.) Charging a client an advisory fee for rendering advice when a commission for executing securities transactions pursuant to such advice will be received by the adviser or its employees.
- (l) Guaranteeing a client that a specific result will be achieved (gain or no loss) with advice which will be rendered.
- (m) **[Alternative 1]** Publishing, circulating or distributing any advertisement which does not comply with Rule 206(4)-1 under the Investment Advisers Act of 1940.
- (m) **[Alternative 2]** (1.) Except as otherwise provided in subsection (2.), it shall constitute a dishonest or unethical practice within the meaning of [Uniform Act Sec. 102(a)(4)] for any investment adviser or investment adviser representative, directly or indirectly, to use any advertisement that does any one of the following:
  - (i.) Refers to any testimonial of any kind concerning the investment adviser or investment adviser representative or concerning any advice, analysis, report, or other service rendered by such investment adviser or investment adviser representative.
  - (ii.) Refers to past specific recommendations of the investment adviser or investment adviser representative 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 or investment adviser representative 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.

(iii.) 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.

(iv.) 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.

(v.) Represents that the [Administrator] has approved any advertisement.

(vi.) Contains any untrue statement of a material fact, or that is otherwise false or misleading.

(2.) With respect to federal covered advisers, the provisions of this section only apply to the extent permitted by Section 203A of the Investment Advisers Act of 1940.

(3.) 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:

(i.) Any analysis, report, or publication concerning securities.

(ii.) 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.

- (iii.) 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.
  - (iv.) Any other investment advisory service with regard to securities.
- (n) Disclosing the identity, affairs, or investments of any client unless required by law to do so, or unless consented to by the client.
- (o) 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 advisor's action is subject to and does not comply with the requirements of Rule 102e(1)-1. and any subsequent amendments.
- (p) Entering into, extending or renewing any investment advisory contract, unless such contract is in writing and discloses, in substance, the services to be provided, the term of the contract, the advisory fee, the formula for computing the fee, the amount of prepaid fee to be returned in the event of contract termination or non-performance, whether the contract grants discretionary power to the adviser and that no assignment of such contract shall be made by the investment adviser without the consent of the other party to the contract.
- (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) Entering into, extending, or renewing 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.
- (s) To indicate, 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.
- (t) Engaging in any act, practice, or course of business which is fraudulent, deceptive, or manipulative in contrary to the provisions of Section 206(4) of the Investment Advisers Act of 1940, notwithstanding the fact that such investment adviser or investment adviser representative is not registered or required to be registered under Section 203 of the Investment Advisers Act of 1940.
- (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 this act or any rule or regulation thereunder.

The conduct set forth above is not inclusive. Engaging in other conduct such as non-disclosure, incomplete disclosure, or deceptive practices shall be deemed an unethical business practice. The federal statutory and regulatory provisions referenced herein shall apply to investment advisers, investment adviser representatives and federal covered advisers to the extent permitted by the National Securities Markets Improvement Act of 1996 (Pub. L. No. 104-290).