

REQUEST FOR PUBLIC COMMENT

PROPOSED REVISIONS TO NASAA’S DISHONEST OR UNETHICAL BUSINESS PRACTICES OF BROKER-DEALERS AND AGENTS MODEL RULE

September 5, 2023

Deadline for Public Comments: December 4, 2023

The Broker-Dealer Market and Regulatory Policy and Review Project Group and the Broker-Dealer Section Committee (collectively, the “Committees”) of the North American Securities Administrators Association, Inc. (“NASAA”) seek public comment on proposed revisions to NASAA’s model rule on *Dishonest or Unethical Business Practices Of Broker-Dealers And Agents* (the “Business Practices Rule”). The revisions to the Business Practices Rule proposed herein are intended to update the model rule in light of the U.S. Securities and Exchange Commission’s 2019 adoption of Regulation Best Interest, 17 C.F.R. § 240.15l-1 (“Reg BI”), and other developments in the securities industry. In particular, the Committees propose that NASAA amend the Business Practices Rule to:

- (1) acknowledge and incorporate by reference the new federal conduct standard applicable to broker-dealer and agents pursuant to Reg BI;
- (2) define and clarify various obligations or components of this new conduct standard for purposes of state interpretation and enforcement; and
- (3) prohibit misleading uses of the title “advisor” or “adviser.”

Details regarding each of these proposed revisions are set forth below.

Comments on this proposal are due on or before the date specified above. We are only accepting comments by electronic mail. Please email your comments to NASAAComments@nasaa.org, and please cc: Broker-Dealer Market and Regulatory Policy and Review Project Group Chair Amy Kopleton (kopletona@dca.njoag.gov) and Broker-Dealer Section Chair Stephen Bouchard (stephen.bouchard@dc.gov). All comments received in response to this request will be posted to NASAA’s website (www.nasaa.org) without edit or redaction, though inappropriate comments will not be posted. Please do not include any information in your comment letter that you do not wish to become publicly available.

Thank you.

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I. BACKGROUND AND INTRODUCTION

The Business Practices Rule was adopted by the NASAA membership on May 23, 1983, to set high standards of commercial honor and just and equitable principles of trade for broker-dealers and their agents. The Business Practices Rule (or a rule like it) has been adopted by most U.S. NASAA members under authority of their state securities laws to set forth conduct standards the violation of which may result in civil or administrative sanctions (such as fines, censures, denials,

suspensions, bars or revocations of registration, or such other remedies as may be authorized by law).

NASAA recently amended the Business Practices Rule to add failure to pay arbitration awards or other monetary sanctions to the list of sanctionable conduct.¹ But the Business Practices Rule may not fully account for revisions to federal conduct standards for broker-dealers and agents arising out of the adoption of Reg BI by the Securities and Exchange Commission (“SEC”). In addition, the Business Practices Rule does not fully account for other significant changes that have occurred in the financial services industry in recent years, including the blurring of brokerage and advisory service models and the emergence of fintech and other digital investing platforms. To address these shortcomings, the Committees are jointly proposing the following revisions to the Business Practices Rule. (A full text of the Business Practices Rule with the revisions proposed herein is attached as Exhibit A.)

II. REVISION #1

The first proposed revision to the Business Practices Rule – acknowledgement and incorporation of the principles in Reg BI – would be inserted as new Part 1d, placed immediately after the prohibition against unsuitable recommendations. Like the SEC and the Financial Industry Regulatory Authority (“FINRA”), the Committees find value in retaining the existing suitability provision, as the protections emanating from the suitability rule extend further in various respects than Reg BI (e.g., the suitability rule applies to all broker-dealer and agent recommendations whereas Reg BI applies only to recommendations to retail customers). The language proposed for the first revision is to insert the following as new Part 1d:

1d: *When making a recommendation to a retail customer, placing the financial or other interest of the broker-dealer or agent ahead of the interest of the retail customer, recommending an investment strategy or the sale or purchase of any security without a reasonable basis to believe that the recommendation is in the best interest of the retail customer based on the customer’s investment profile and the potential risks, rewards, and costs associated with the recommendation, or otherwise failing to comply with the obligations set forth in Regulation Best Interest, as set forth in rule 17 C.F.R. § 240.15l-1, including, but not limited to 17 C.F.R. § 240.17a-14.*

These obligations would also be extended to agents through a proposed revision to Part 2f of the Business Practices Rule (which cross-references this new Part 1d).

The text in Part 1d is similar to language adopted in Ohio in 2021 to update its state regulations in light of Reg BI.²

III. REVISION SET #2

The second set of revisions are presented as subparts 1 through 8 under Part 1d. Each subpart attempts to define, clarify, or simply emphasize an obligation or component of Reg BI that is

¹ The current text of the Business Practices Rule with these May 16, 2022, amendments is available at <https://www.nasaa.org/wp-content/uploads/2022/07/1956-Act-and-2002-Act-Broker-Dealer-Dishonest-or-Unethical-Practices-Rule-20220516.pdf>.

² See Ohio Admin. Code § 1301:6-3-19(A)(6).

functionally incorporated via the first revision. These subparts include definitions and interpretations drawn directly from SEC guidance in its Adopting Release for Reg BI³ (but not expressly included within the text of the SEC’s rule) as well as definitions and interpretations intended to fill certain gaps in SEC guidance. The language set forth in the second set of revisions was written to align with the principles of Reg BI and incorporate SEC’s related interpretive guidance .. Where adopted, these subparts would also extend to agents through the proposed revision to Part 2f of the Business Practices Rule, which cross-references the new Part 1d.

It is important to note that the various subparts within the second revision are presented as a menu of provisions that NASAA members can use to define, clarify, or emphasize the obligations and components of Reg BI that matter most to each jurisdiction. Members may desire definition and clarity that is best achieved by adopting one, some, or all of the subparts set forth in this revision set. This approach provides flexibility while also promoting uniformity through standardized options. Each of these eight subparts is discussed separately below.

(a) Subpart 1d(1): Compliance and Disclosure

1d(1): *The obligations set forth in this section cannot be satisfied through disclosure alone.*

Subpart 1d(1) is straightforward and incorporates SEC guidance from the Adopting Release (and repeated elsewhere) directly into the text of the model rule. Based on examination findings the Committees believe it is necessary to emphasize and elevate this guidance into the text of the rule as many firms are relying too heavily on disclosure as their primary or sole means of complying with the care and conflict of interest obligations under Reg BI.⁴

(b) Subpart 1d(2): Conflicts of Interest

1d(2): *To ensure the broker-dealer or agent does not place the financial or other interest of the broker-dealer or agent ahead of the interest of the retail customer, the broker-dealer or agent must make all reasonable efforts to avoid or eliminate conflicts of interest. Conflicts of interest that cannot reasonably be avoided or eliminated must be disclosed and mitigated;*

- a. For purposes of this paragraph, mitigating a conflict of interest means neutralizing or reducing the potential for harm or adverse impact of the conflict to the retail customer.*
- b. The broker-dealer or agent will be presumed to have placed its financial interest ahead of the interest of the retail customer where the broker-dealer or agent participates in (i) sales contests; (ii) sales quotas; (iii) bonuses, or (iv) any other non-cash compensation based on the sales of*

³ See Regulation Best Interest; The Broker-Dealer Standard of Conduct, SEC Rel. No. 34-86031 (Jun. 5, 2019), available at <https://www.sec.gov/rules/final/2019/34-86031.pdf>.

⁴ NASAA National Examination Initiative Phase II (A) Report and Findings of NASAA’s Regulation Best Interest Implementation Committee (Nov. 2021) (“NASAA Reg BI Phase II(A) Report”), https://www.nasaa.org/wp-content/uploads/2021/11/NASAA-Reg-BI-Phase-II-A-Report-November-2021_FINAL.pdf; NASAA National Examination Initiative Phase II (B) Report and Findings of NASAA’s Broker-Dealer Section (Sept. 2023) (“NASAA Reg BI Phase II(B) Report”)

specific securities or specific types of securities within a limited period of time, or rewards the broker-dealer or agent with additional cash or non-cash compensation beyond the sales commission as the result of that recommendation.

Subpart 1d(2) provides definition and clarity regarding broker-dealer and agent conflict of interest obligations. The subpart specifically defines “mitigating” in the text of the revised rule, consistent with SEC guidance in the Adopting Release.⁵ Additionally, this subpart reconciles SEC guidance seeking to address the cumulative impact occasioned by a multiplicity of conflicts that collectively steer recommendations in a firm’s financial favor and does not address the continued use of “manufactured conflicts.” The latter are conflicts that firms and product sponsors voluntarily and self-servingly inject into transactions to incentivize retail sales.

NASAA’s Phase II(A) Reg BI Report establishes that layered and manufactured conflicts, which are a lucrative source of extra compensation for firms and agents, are not inherent to the broker-dealer business model.⁶ Rather, the conflicts appear concentrated in recommendations involving certain products or investment strategies.⁷ The NASAA Phase II(A) Report also indicates that many firms are exploiting the gaps and lack of clarity within the SEC’s guidance to sidestep meaningful reductions in conflicts that are mandated by the text of the rule, leaving retail customers vulnerably exposed.⁸ The continued layering of compensation conflicts, in particular, exacerbates rather than mitigates the potential for customer harm, as each incentive affirmatively places firm and agent financial interests incrementally ahead of the interests of their retail customers.

NASAA’s Phase II(B) Reg BI Report identified that although certain firms had procedures that generally acknowledged the conflict of interest obligation, the procedures failed to address how the firms identify conflicts and certain firms’ procedures were not reasonably designed to mitigate conflicts.

To address these issues, Subpart 1d(2) clarifies that a broker-dealer “must make all reasonable efforts to avoid or eliminate conflicts of interest” and “will be presumed to have placed its financial interest ahead of the interest of the retail customer where the broker-dealer or agent participates in sales contests, sales quotas, bonuses, and non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited period of time, or rewards the broker-dealer or agent with additional cash or non-cash compensation beyond the sales commission as the result of that recommendation.” The subpart preserves sales commissions, the compensation model that is inherent to the broker-dealer model (and consequently cannot be avoided or eliminated altogether, but which can be mitigated). This would include both upfront and trailing sales commission, as they are ingrained forms of compensation depending on the product, but as always, must be disclosed to investors and mitigated in their effect. Many, if not all, layered compensation conflicts can be avoided and eliminated entirely, *e.g.*, by not holding sales contests, establishing sales quotas, or permitting issuers and sponsors to provide unnecessary extra benefits.

⁵ See Adopting Release at 326 (“affirmatively reduce the potential effect of these conflicts of interest such that they do not taint the recommendation”); *see also id.* at 330 (“policies and procedures must be reasonably designed to reduce the potential effect such conflicts may have on a recommendation given to a retail customer”); 57 n.123, 319 (“reasonably reduce”); 320 (“modify practices to reduce”).

⁶ NASAA Reg BI Phase IIA Report at 14-16.

⁷ *Id.* at 16.

⁸ *Id.* at 16-18.

Under the proposed revision, firms are not prohibited from receiving other extra forms of compensation, but firms will need to rebut the presumption that they are placing their financial interests ahead of their customers when they affirmatively choose to engage in these conflicts. Scrutiny would be heightened where the conflicts tend to steer agents toward more costly, more remunerative, and riskier investments. To the extent firms can rebut that presumption, the subpart emphasizes that those conflicts must be disclosed and mitigated consistent with SEC guidance.

(c) Subpart 1d(3): Care, Skill, and Diligence

1d(3): To ensure the recommendation is “in the best interest of the retail customer” for purposes of this subsection, the broker-dealer or agent must use the care, skill, and diligence that a person acting in a like capacity and familiar with such matters would use, taking into consideration all of the relevant facts and circumstances.

- a. *The relevant facts and circumstances include:*
 1. *The risks, costs, and conflicts of interest related to the recommendation made and any related investment advice given to the retail customer;*
 2. *Securities and investment strategies that can achieve the retail customer’s investment objectives with less risk or less costs;*
 3. *The customer’s age, education, other investments, debt, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance; and,*
 4. *Any other relevant information*
- b. *To satisfy this care obligation, a broker-dealer or agent shall make reasonable inquiry regarding lower-cost and lower-risk securities and investment strategies that are reasonably available to the broker-dealer or agent, as well as products or services available if the agent is also [licensed/registered] in other capacities such as an investment adviser representative or insurance agent.*

Subpart 1d(3) emphasizes and clarifies key aspects of broker-dealer and agent duties of care. The subpart codifies a simplified form of the SEC’s lengthy guidance directing firms to consider lower-cost and lower-risk securities and strategies when they consider reasonably available alternatives. The Committees believe this guidance needs to be simplified, emphasized, and elevated to the text of the NASAA model rule because many firms are not giving due consideration to lower-cost and lower-risk alternatives.⁹ With respect to the universe of lower-cost and lower-risk alternatives, the Committees propose consideration of securities and investment strategies “that are reasonably available to the broker-dealer or agent, as well as products or services available if the agent is also [licensed/registered] in other capacities such as an investment adviser representative or insurance agent.”

⁹ NASAA Reg BI Phase II(A) Report at 9-11 and NASAA Reg BI Phase II(B) Report at 3-6, 8, 16.

If the agent is also registered as an investment adviser representative or insurance agent, the agent would need to consider products that are available through those channels as well.

(d) Subpart 1d(4): Costs

1d(4): *For purposes of this subsection, “costs” include the sum total of all potential fees and costs based on the anticipated holding period for the security or investment strategy that is recommended by the broker-dealer or agent.*

- a. *“Costs” include but are not limited to account fees, commissions, other transactional costs such as markups and markdowns, costs arising from tax considerations, costs associated with payment for order flow and cash sweep programs, and other indirect costs that could be borne by the retail customer.*
- b. *When applicable, “costs” also include fees associated with the investment products that are available through the account, such as the internal expenses of funds, management fees, distribution and servicing fees, including any front-end and back-end fees.*
- c. *To the extent that certain “costs,” such as distribution and servicing fees and transactional costs, depend on the retail customer’s anticipated investment horizon, the broker-dealer or agent is to consider the potential impact of those costs on the customer’s account based on an understanding of that horizon.*

Subpart 1d(4) codifies SEC guidance from the Reg BI Adopting Release and the SEC’s more recent Staff Bulletin construing Reg BI in the context of account recommendations.¹⁰ The Committees believe this guidance should be emphasized and elevated to the text of the rule because many firms have expressed confusion about the term “costs” and other firms are not giving due consideration to or providing full and fair disclosure about total costs when making recommendations to retail customers.¹¹ Further, more recent examinations by NASAA members found that some firms had not established procedures addressing how costs should be considered when making recommendations.¹²

(e) Subpart 1d(5): Recommendations

Subpart 1d(5) is a provision that attempts to clarify what qualifies as a “recommendation” subject to the model rule. A “recommendation” is a well-established concept with sufficient elasticity to accommodate technological advancements within the industry.¹³

1d(5): *The obligations set forth in this section do not apply to unsolicited transactions that a broker-dealer or agent execute for a customer in a self-*

¹⁰ SEC Staff Bulletin: Standards of Conduct for Broker-Dealers and Investment Advisers Account Recommendations for Retail Investors (Mar. 29, 2022), <https://www.sec.gov/tm/iabd-staff-bulletin>.

¹¹ NASAA Reg BI Phase II(A) Report at 12-13.

¹² NASAA Reg BI Phase II(B) Report at 10-11, 16.

¹³ See NASD Notice to Members 01-23 (Apr. 2001) (outlining recommendations as a call to action in a case by-case inquiry); Frequently Asked Questions on Regulation Best Interest, SEC (Jan. 10, 2020) (discussing permitted communications with new and existing clients and the “call to action” framework).

directed or nondiscretionary account. If the broker-dealer or agent utilized any means, method or mechanism to feature or promote an account type, specific security or investment strategy to a retail customer, whether directly or through a third-party, then that transaction will not be deemed an unsolicited transaction, but rather will be deemed a recommendation to which all of the foregoing obligations set forth in this subsection apply.

This subpart codifies SEC guidance that Reg BI does not apply to unsolicited transactions, but clarifies that this exclusion does not apply “[i]f the broker-dealer or agent utilized any means, method or mechanism to feature or promote an account type, specific security or investment strategy to a retail customer, whether directly or through a third-party....” With the advent of fintech and proliferation of sophisticated algorithmic digital engagement practices that feed on and cater to the unique personal attributes of individual retail investors, especially vulnerable unsophisticated investors, securities regulators are updating their guidance about what qualifies as a recommendation for purposes of Reg BI.¹⁴ Subpart 1d(5) specifies that the requisite “call to action” occurs and a “recommendation” is made where “broker-dealer or agent utilized any means, method or mechanism to feature or promote an account type, specific security, or investment strategy to a retail customer, whether directly or through a third-party....” The subpart is intended to provide greater regulatory certainty regarding a key term.

(f) Subpart 1d(6): Retail Customer

1d(6): *For the purposes of this section, the term “retail customer” shall include current and prospective customers and clients, but shall not include:*

- a. A bank, savings and loan association, insurance company, trust company, or registered investment company;*
- b. A broker-dealer registered with a state securities regulator;*
- c. An investment adviser registered with the SEC under Section 203 of the Investment Advisers Act of 1940 or with a state securities regulator; or*
- d. Any other institutional buyer, as defined in [state rule citation].*

Subpart 1d(6) defines and clarifies the term “retail customer” by excluding various classes of institutional investors, consistent with SEC guidance regarding the scope of the term for purposes of Reg BI. The subpart is also intended to provide greater regulatory certainty regarding a key term.

(g) Subparts 1d(7) and 1d(8): Savings Clauses

1d(7): *Nothing in this section shall be construed to apply to a person acting in the capacity of a fiduciary to an employee benefit plan, its participants, or its beneficiaries, as those terms are defined in the Employee Retirement*

¹⁴ E.g., SEC Release Nos. 34-92766; IA-5833, Request for Comment on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches; Information and Comments on Investment Adviser Use of Technology, (Aug. 27, 2021) at 31-32 & n.31, <https://www.sec.gov/rules/other/2021/34-92766.pdf> (“The use of a DEP by a broker-dealer may, depending on the relevant facts and circumstances, constitute a recommendation for purposes of Reg BI.”).

Subpart 1d(7) clarifies that the principles incorporated into the Business Practices Rule, as further defined or clarified by each jurisdiction, do not apply to or supplant the fiduciary duties that apply in ERISA plan recommendations.

1d(8): *Nothing in this section shall be construed to establish any requirements for capital, custody, margin, financial responsibility, making and keeping of records, bonding, or financial or operational reporting for any broker-dealer or agent that differ from, or are in addition to, the requirements established under 15 U.S.C. § 78o(i).*

Subpart 1d(8) is an explicit savings clause respecting the recordkeeping, bonding, and financial or operational reporting limitations imposed on state securities regulations by the National Securities Markets Improvement Act of 1996, 15 U.S.C. § 78o(i).

IV. REVISION #3

The third revision to the Business Practices Rule is a prohibition against misleading use of the professional title “advisor” or “adviser.” This revision appears as new Part 1e in the Business Practices Rule and reads as follows:

1e: *Using a title, purported credential, or professional designation containing any variant of the terms “advisor” or “adviser” without licensure as either an investment adviser or an investment adviser representative, unless otherwise permitted by law.*

This subpart codifies SEC guidance that discourages broker-dealers and agents from misleading investors regarding the professional capacity in which their services are provided.¹⁵ The Committees find the addition helpful to ameliorate investor confusion stemming from the blurring of brokerage and advisory services. The Committees believe it is a deceptive and unethical practice for broker-dealers to mislead investors into believing the broker-dealers are acting in a fiduciary capacity with an ongoing duty of loyalty through misuse of the “advisor” and “adviser” title. As noted in NASAA’s Phase II(A) Report:

Using the title in that manner blurs the lines between these two business models and gives investors a false impression regarding the capacity in which a firm or agent is operating. In 2018, many firms allowed their agents/ reps to use the ‘adviser’ and ‘advisor’ titles of trust while operating in a broker-dealer capacity: 29% of firms allowed agents/ reps to use ‘advisor’ or ‘adviser’ title while acting in broker-dealer capacity and 46% of those firms (13% of the total) had no prerequisites for using such title, such as requiring IAR registration. In 2021, the percentage of Reg BI firms using (or allowing their brokers to use) the title without dual licensure dropped to 7%.¹⁶

Further, NASAA members have found more recently that firms continue to permit the use of the

¹⁵ Adopting Release at 156-57.

¹⁶ NASAA Reg BI Phase II(A) Report at 18.

term “adviser” in instances where the firm and/or its agents are not licensed or registered as an investment adviser or investment adviser representative.¹⁷

The prohibition is extended to agents through the proposed revision to Part 2f of the Business Practices Rule. Also, it is recognized that certain jurisdictions’ laws permit the use of the term “advisor” or “adviser” in other circumstances. As such the subpart provides “unless otherwise permitted by law,” within the context permitted under those laws.

V. REQUEST FOR PUBLIC COMMENT

The Committees request public comment on these proposed revisions to the Business Practices Rule. Clean copies of the Business Practices Rule as it would be revised, plus redlines showing these proposed revisions against the current text of the Business Practices Rule are attached hereto.

¹⁷ NASAA Reg BI Phase II(B) Report at 11-12, 16.

Exhibit A

DISHONEST OR UNETHICAL BUSINESS PRACTICES OF BROKER-DEALERS AND AGENTS

[Adopted May 23, 1983; Amended May 16, 2022; Amended [date]]

[HIGH STANDARDS AND JUST PRINCIPLES.] Each broker-dealer and agent shall observe high standards of commercial honor and just and equitable principles of trade in the conduct of their business. Acts and practices, including but not limited to the following, are considered contrary to such standards and may constitute grounds for denial, suspension or revocation of registration or such other action authorized by statute.

1. BROKER-DEALERS

- a. Engaging in a pattern of unreasonable and unjustifiable delays in the delivery of securities purchased by any of its customers and/or in the payment upon request of free credit balances reflecting completed transactions of any of its customers;
- b. Inducing trading in a customer's account which is excessive in size or frequency in view of the financial resources and character of the account;
- c. Recommending to a customer the purchase, sale or exchange of any security without reasonable grounds to believe that such transaction or recommendation is suitable for the customer based upon reasonable inquiry concerning the customer's investment objectives, financial situation and needs, and any other relevant information known by the broker-dealer;

d. When making a recommendation to a retail customer, placing the financial or other interest of the broker-dealer or agent ahead of the interest of the retail customer, recommending an investment strategy or the sale or purchase of any security without a reasonable basis to believe that the recommendation is in the best interest of the retail customer based on the customer's investment profile and the potential risks, rewards, and costs associated with the recommendation, or otherwise failing to comply with the obligations set forth in Regulation Best Interest, as set forth in rule 17 C.F.R. § 240.15/-1, including, but not limited to 17 C.F.R. § 240.17a-14.

(1) The obligations set forth in this section cannot be satisfied through disclosure alone;

(2) To ensure the broker-dealer or agent does not “place the financial or other interest of the broker-dealer or agent ahead of the interest of the retail customer,” the broker-dealer or agent must make all reasonable efforts to avoid or eliminate conflicts of interest. Conflicts of interest that cannot reasonably be avoided or eliminated must be disclosed and mitigated;

- a. For purposes of this paragraph, mitigating a conflict of interest means neutralizing or reducing the potential for harm or adverse impact of the conflict to the retail customer.

b. The broker-dealer or agent will be presumed to have placed its financial interest ahead of the interest of the retail customer where the broker-dealer or agent participates in (i) sales contests; (ii) sales quotas; (iii) bonuses; or (iv) any other non-cash compensation that are based on the sales of specific securities or specific types of securities within a limited period of time, or rewards the broker-dealer or agent with additional cash or non-cash compensation beyond the sales commission as the result of that recommendation.

(3) To ensure the recommendation is “in the best interest of the retail customer” for purposes of this subsection, the broker-dealer or agent must use the care, skill, and diligence that a person acting in a like capacity and familiar with such matters would use, taking into consideration all of the relevant facts and circumstances.

a. The relevant facts and circumstances include:

1. The risks, costs, and conflicts of interest related to the recommendation made and any related investment advice given to the retail customer;

2. Securities and investment strategies that can achieve the retail customer’s investment objectives with less risk or less costs;

3. The customer’s age, education, other investments, debt, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs, risk tolerance; and

4. Any other relevant information.

b. To satisfy this care obligation, a broker-dealer or agent shall make reasonable inquiry regarding lower-cost and lower-risk securities and investment strategies that are reasonably available to the broker-dealer or agent, as well as products or services available if the agent is also [licensed/registered] in other capacities such as an investment adviser representative or insurance agent.

(4) For purposes of this subsection, “costs” include the sum total of all potential fees and costs based on the anticipated holding period for the security or investment strategy that is recommended by the broker-dealer or agent.

a. “Costs” include but are not limited to account fees, commissions, other transactional costs such as markups and markdowns, costs arising from tax considerations, costs associated with payment for order flow and cash sweep programs, and other indirect costs that could be borne by the retail customer.

b. When applicable, “costs” also include fees associated with the investment products that are available through the account, such as the internal expenses of funds, management fees, distribution and servicing fees, including any front-end and back-end fees.

c. To the extent that certain “costs,” such as distribution and servicing fees and transactional costs, depend on the retail customer’s anticipated investment

horizon, the broker-dealer or agent is to consider the potential impact of those costs on the customer's account based on an understanding of that horizon.

(5) The obligations set forth in this section do not apply to unsolicited transactions that a broker-dealer or agent execute for a customer in a self-directed or nondiscretionary account. If the broker-dealer or agent utilized any means, method or mechanism to feature or promote an account type, specific security or investment strategy to a retail customer, whether directly or through a third-party, then that transaction will not be deemed an unsolicited transaction, but rather will be deemed a recommendation to which all of the foregoing obligations set forth in this subsection apply.

(6) For the purposes of this section, the term "retail customer" shall include current and prospective customers and clients, but shall not include:

a. A bank, savings and loan association, insurance company, trust company, or registered investment company;

b. A broker-dealer registered with a state securities regulator;

c. An investment adviser registered with the SEC under Section 203 of the Investment Advisers Act of 1940 or with a state securities regulator; or

d. Any other institutional buyer, as defined in [state rule citation].

(7) Nothing in this section shall be construed to apply to a person acting in the capacity of a fiduciary to an employee benefit plan, its participants, or its beneficiaries, as those terms are defined in the Employee Retirement Income Security Act (ERISA), 29 U.S.C. §§ 1001 et seq.

(8) Nothing in this section shall be construed to establish any requirements for capital, custody, margin, financial responsibility, making and keeping of records, bonding, or financial or operational reporting for any broker-dealer or agent that differ from, or are in addition to, the requirements established under 15 U.S.C. § 78o(i).

e. Using a title, purported credential, or professional designation containing any variant of the terms "adviser" or "advisor" without licensure as either an investment adviser or an investment adviser representative, unless otherwise permitted by law.

d.f. Executing a transaction on behalf of a customer without authorization to do so;

e.g. Exercising any discretionary power in effecting a transaction for a customer's account without first obtaining written discretionary authority from the customer, unless the discretionary power relates solely to the time and/or price for the executing of orders;

f.h. Executing any transaction in a margin account without securing from the customer a properly executed written margin agreement promptly after the initial transaction in the account;

g.i. Failing to segregate customers' free securities or securities held in safekeeping;

h.j. Hypothecating a customer's securities without having a lien thereon unless the broker-

dealer secures from the customer a properly executed written consent promptly after the initial transaction, except as permitted by Rules of the Securities and Exchange Commission;

i.k. Entering into a transaction with or for a customer at a price not reasonably related to the current market price of the security or receiving an unreasonable commission or profit;

j.l. Failing to furnish to a customer purchasing securities in an offering, no later than the due date of confirmation of the transaction, either a final prospectus or a preliminary prospectus and an additional document, which together include all information set forth in the final prospectus;

k.m. Charging unreasonable and inequitable fees for services performed, including miscellaneous services such as collection of monies due for principal, dividends or interest, exchange or transfer of securities, appraisals, safekeeping, or custody of securities and other services related to its securities business;

l.n. Offering to buy from or sell to any person any security at a stated price unless such broker-dealer is prepared to purchase or sell, as the case may be, at such price and under such conditions as are stated at the time of such offer to buy or sell;

m.o. Representing that a security is being offered to a customer “at the market” or a price relevant to the market price unless such broker-dealer knows or has reasonable grounds to believe that a market for such security exists other than that made, created or controlled by such broker-dealer, or by any such person for whom he is acting or with whom he is associated in such distribution, or any person controlled by, controlling or under common control with such broker-dealer;

n.p. Effecting any transaction in, or inducing the purchase or sale of, any security by means of any manipulative, deceptive or fraudulent device, practice, plan, program, design or contrivance, which may include but not be limited to;

- (1) Effecting any transaction in a security which involves no change in the beneficial ownership thereof;
- (2) Entering an order or orders for the purchase or sale of any security with the knowledge that an order or orders of substantially the same size, at substantially the same time and substantially the same price, for the sale of any such security, has been or will be entered by or for the same or different parties for the purpose of creating a false or misleading appearance of active trading in the security or a false or misleading appearance with respect to the market for the security; provided, however, nothing in this subsection shall prohibit a broker-dealer from entering bona fide agency cross transactions for its customers;
- (3) Effecting, alone or with one or more other persons, a series of transactions in any security creating actual or apparent active trading in such security or raising or depressing the price of such security, for the purpose of inducing the purchase or sale of such security by others;

o.q. Guaranteeing a customer against loss in any securities account of such customer carried

by the broker-dealer or in any securities transaction effected by the broker-dealer or in any securities transaction effected by the broker-dealer with or for such customer;

p.r. Publishing or circulating, or causing to be published or circulated, any notice, circular, advertisement, newspaper article, investment service, or communication of any kind which purports to report any transaction as a purchase or sale of any security unless such broker-dealer believes that such transaction was a bona fide purchase or sale of such security; or which purports to quote the bid price or asked price for any security, unless such broker-dealer believes that such quotation represents a bona fide bid for, or offer of, such security;

q.s. Using any advertising or sales presentation in such a fashion as to be deceptive or misleading. An example of such practice would be a distribution of any nonfactual data, material or presentation based on conjecture, unfounded or unrealistic claims or assertions in any brochure, flyer, or display by words, pictures, graphs or otherwise designed to supplement, detract from, supersede or defeat the purpose or effect of any prospectus or disclosure; or

r.t. Failing to disclose that the broker-dealer is controlled by, controlling, affiliated with or under common control with the issuer of any security before entering into any contract with or for a customer for the purchase or sale of such security, the existence of such control to such customer, and if such disclosure is not made in writing, it shall be supplemented by the giving or sending of written disclosure at or before the completion of the transaction;

s.u. Failing to make a bona fide public offering of all of the securities allotted to a broker-dealer for distribution, whether acquired as an underwriter, a selling group member, or from a member participating in the distribution as an underwriter or selling group member; or

t.v. Failure or refusal to furnish a customer, upon reasonable request, information to which he is entitled, or to respond to a formal written request or complaint.

u.w. Failing to pay and fully satisfy any final judgment or arbitration award, resulting from an investment-related, customer-initiated arbitration or court proceeding, unless alternative payment arrangements are agreed to between the customer and the broker-dealer or broker-dealer agent, in writing, and the broker-dealer or broker-dealer agent complies with the terms of the alternative payment arrangement.

v.x. Attempting to avoid payment of any final judgment or arbitration award resulting from an investment-related, customer-initiated arbitration or court proceeding, unless alternative payment arrangements are agreed to between the customer and the broker-dealer or broker-dealer agent, in writing, and the broker-dealer or broker-dealer agent complies with the terms of the alternative payment arrangements.

w.y. Failing to pay and fully satisfy any fine, civil penalty, order of restitution, order of disgorgement, or similar monetary payment obligation imposed upon the broker-dealer or agent by the Securities and Exchange Commission, the securities or other financial services regulator of any state or province, or any self-regulatory organization.

2. AGENTS

a. Engaging in the practice of lending or borrowing money or securities from a customer, or acting as a custodian for money, securities or an executed stock power of a customer;

- b. Effecting securities transactions not recorded on the regular books or records of the broker- dealer which the agent represents, unless the transactions are authorized in writing by the broker-dealer prior to execution of the transaction;
- c. Establishing or maintaining an account containing fictitious information in order to execute transactions which would otherwise be prohibited;
- d. Sharing directly or indirectly in profits or losses in the account of any customer without the written authorization of the customer and the broker-dealer which the agent represents;
- e. Dividing or otherwise splitting the agent's commissions, profits or other compensation from the purchase or sale of securities with any person not also registered as an agent for the same broker-dealer, or for a broker-dealer under direct or indirect common control; or
- f. Engaging in conduct specified in Subsection 1.b, c, d, e, f, [g](#), [h](#), [i](#), [j](#), [k](#), [l](#), [m](#), [n](#), [o](#), [p](#), [q](#), [r](#), [s](#), [t](#), [u](#), [v](#), [w](#), [x](#) or [y](#).

[CONDUCT NOT INCLUSIVE.] The conduct set forth above is not inclusive. Engaging in other conduct such as forgery, embezzlement, nondisclosure, incomplete disclosure or misstatement of material facts, or manipulative or deceptive practices shall also be grounds for denial, suspension or revocation of registration.