

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

[Adopted 9/17/2008; Amended 11/06/17, 5/19/2019, 05/16/2022]

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

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

- (a) Recommending to a client to whom investment advisory services are provided the purchase, sale or exchange of any security without reasonable grounds to believe that the recommendation is suitable for the client on the basis of information furnished by the client after reasonable inquiry concerning the client's investment objectives, financial situation and needs, and any other information known by the investment adviser, investment adviser representative or federal covered investment adviser.
- (b) Exercising any discretionary authority in placing an order for the purchase or sale of securities for a client without obtaining written discretionary authority from the client within ten (10) business days after the date of the first transaction placed pursuant to oral discretionary authority, unless the discretionary authority relates solely to the price at which, or the time when, an order involving a definite amount of a specified security shall be executed, or both.
- (c) Inducing trading in a client's account that is excessive in size or frequency in view of the financial resources, investment objectives and character of the account.¹
- (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.

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

- (f) Borrowing money or securities from a client unless the client is a broker-dealer, an affiliate of the investment adviser or a financial institution engaged in the business of loaning funds.
- (g) Loaning money or securities to a client unless the investment adviser is a financial institution engaged in the business of loaning funds or the client is an affiliate of the investment adviser.
- (h) Misrepresenting to any client, or prospective client, the qualifications of the investment adviser, investment adviser representative, federal covered investment adviser, or any employee, or person affiliated with the investment adviser, investment adviser representative or federal covered investment adviser, or misrepresenting the nature of the advisory services being offered or fees to be charged for such service, or to omit to state a material fact necessary to make the statements made regarding qualifications, services or fees, in light of the circumstances under which they are made, not misleading.
- (i) Providing a report or recommendation to any client prepared by someone other than the investment adviser, investment adviser representative or federal covered investment adviser without disclosing that fact. This prohibition does not apply to a situation where the investment adviser, investment adviser representative or federal covered investment adviser uses published research reports or statistical analyses to render advice or where an investment adviser, investment adviser representative or federal covered investment adviser orders such a report in the normal course of providing service.
- (j) Charging a client an unreasonable fee.
- (k) Failing to disclose to clients in writing before any advice is rendered any material conflict of interest relating to the investment adviser, investment adviser representative or federal covered investment adviser, or any of its employees, or affiliated persons which could reasonably be expected to impair the rendering of unbiased and objective advice including but not limited to:
 - (1) Compensation arrangements connected with investment advisory services to clients which are in addition to compensation from such clients for such services; and
 - (2) Charging a client an investment advisory fee for rendering investment advice when compensation for effecting securities transactions pursuant to such advice will be received by the investment adviser, investment adviser representative or federal covered investment adviser or its employees, or affiliated persons.
- (l) While acting as principal for its own advisory account, to knowingly sell any security to or purchase any security from a client, or while acting as broker-dealer for a person other than the client, to knowingly effect any sale or purchase of any security for the account of the client, without disclosing to the client in writing before the completion of the transaction the capacity in which it is acting and obtaining the consent of the client to the transaction.

- (1) The prohibitions of this subsection shall not apply to any transaction with a customer of a broker-dealer if the broker-dealer is not acting as an investment adviser in relation to the transaction.²
- (2) The prohibitions of this subsection shall not apply to any transaction with a customer of a broker-dealer if the broker-dealer acts as an investment adviser solely:
 - (A) by means of publicly distributed written materials or publicly made oral statements;
 - (B) by means of written materials or oral statements not purporting to meet the objectives or needs of specific individuals or accounts;
 - (C) through the issuance of statistical information containing no expressions of opinion as to the investment merits of a particular security; or
 - (D) any combination of the foregoing services.³
- (3) Publicly distributed written materials or publicly made oral statements shall disclose that, if the purchaser of the advisory communication uses the investment adviser's services in connection with the sale or purchase of a security which is a subject of the communication, the investment adviser may act as principal for its own account or as agent for another person. Compliance by the investment adviser with the foregoing disclosure requirement shall not relieve it of any other disclosure obligations under the Act.⁴
- (4) Definitions for purposes of this Rule,
 - (A) "Publicly distributed written materials" means written materials which are distributed to 35 or more persons who pay for those materials.
 - (B) "Publicly made oral statements" means oral statements made simultaneously to 35 or more persons who pay for access to those statements.
- (m) The prohibitions of this Rule shall not apply to an investment adviser effecting an agency cross transaction for an advisory client provided the following conditions are met:⁵
 - (1) The advisory client executes a written consent prospectively authorizing the investment adviser to effect agency cross transactions for such client;
 - (2) Before obtaining such written consent from the client, the investment adviser makes full written disclosure to the client that, with respect to agency cross transactions, the investment adviser will act as broker-dealer for, receive

² Note: 1956 Act § 102(a)(3) not included in 2002 Act.

³ Note: 1956 Rule 102(f)-2(b) not included in 2002 Act.

⁴ Note: 1956 Rule 102(f)-2(c).

⁵ Note: 1956 Rule 102(f)-1.

commissions from and have a potentially conflicting division of loyalties and responsibilities regarding both parties to the transactions;

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

such person is required to be registered [licensed] as a broker-dealer in this state unless excluded from the definition.

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

- (4) Represents that any report, analysis, or other service will be furnished for free or without charge, unless such report, analysis, or other service actually is or will be furnished entirely free and without any direct or indirect condition or obligation.
- (5) Represents that the [Administrator] has approved any advertisement.
- (6) Contains any untrue statement of a material fact, or that is otherwise false or misleading.
- (7) For the purposes of this section, the term “advertisement” shall include any notice, circular, letter, or other written communication addressed to more than one person, or any notice or other announcement in any electronic or paper publication, by radio or television, or by any medium, that offers any one of the following:
 - (A) Any analysis, report, or publication concerning securities.
 - (B) Any analysis, report, or publication that is to be used in making any determination as to when to buy or sell any security or which security to buy or sell.
 - (C) Any graph, chart, formula, or other device to be used in making any determination as to when to buy or sell any security, or which security to buy or sell.
 - (D) Any other investment advisory service with regard to securities.
- (p) Making, in the solicitation of clients, any untrue statement of a material fact, or omitting to state a material fact necessary in order to make the statement made, in light of the circumstances under which they are made, not misleading.⁶
- (q) Failing to establish, maintain, and enforce written policies and procedures reasonably designed to prevent the misuse of material nonpublic information contrary to the provisions of Section 204A of the Investment Advisers Act of 1940.
- (r) Disclosing the identity, investments, or other financial information of any client or former client unless required by law to do so, or unless consented to by the client.
- (s) Taking any action, directly or indirectly, with respect to those securities or funds in which any client has any beneficial interest, where the investment adviser has custody or possession of such securities or funds when the action of the investment adviser or investment adviser representative is subject to and does not comply with the requirements of Rule 411(f)-1.
- (t) Engaging in any act, practice, or course of business which is fraudulent, deceptive, manipulative or unethical.

⁶ Note: 1956 Act § 102(b).

- (u) Engaging in conduct or any act, indirectly or through or by any other person, which would be unlawful for such person to do directly under the provisions of the Act or any rule or regulation thereunder.
- (v) Accessing a client's account by using the client's own unique identifying information (such as username and password).*
- (w) Failing to establish, maintain, and enforce a required policy or procedure.
- (x) Failing to pay and fully satisfy any final judgment or arbitration award resulting from an investment-related, client or customer-initiated arbitration or court proceeding, unless alternative payment arrangements are agreed to between the client and the investment adviser or investment adviser representative or 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.
- (y) Attempting to avoid payment of any final judgment or arbitration award resulting from an investment-related, client or customer-initiated arbitration or court proceeding, unless alternative payment arrangements are agreed to between the client and the investment adviser or investment adviser representative or 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.
- (z) Failing to pay and fully satisfy any fine, civil penalty, order of restitution, order of disgorgement, or similar monetary payment obligation imposed upon the investment adviser or investment adviser representative by the Securities and Exchange Commission, the securities or other financial services regulator of any state or province, or any self-regulatory organization.

* This rule amendment is not intended to apply to data aggregation software where: (a) the investment adviser does not know, or have access to, the client's password(s); (b) there is an agreement between the data aggregation software company and the custodian(s)/online account platform which permits this "back-door" access; and (c) the data is read-only (*i.e.*, the investment adviser can only view the information and cannot effectuate any changes to the client's underlying account(s)).