



ADMINISTRATIVE RULES OF MONTANA

6.10.402 FRAUDULENT AND UNETHICAL PRACTICES PROHIBITED BY INVESTMENT ADVISERS, INVESTMENT ADVISER REPRESENTATIVES, AND FEDERAL COVERED ADVISERS

- (1) A person who is a federal covered adviser, investment adviser, or an investment adviser representative is a fiduciary and has a duty to act for the benefit of its clients. The provisions of this rule 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 (PL 104-290). While the extent and nature of this duty varies according to the nature of the relationship between an investment adviser, investment adviser representative, or a federal covered adviser and its clients and the circumstances of each case, an investment adviser, investment adviser representative, or a federal covered adviser shall not engage in unethical business practices, or prohibited, fraudulent, deceptive, or manipulative conduct, including but not limited to the following:
 - (a) Recommending to a client, to whom investment supervisory, management or consulting services are provided, the purchase, sale, or exchange of a 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 adviser;
 - (b) Exercising any discretionary power in placing an order for the purchase or sale of a security for a client without obtaining written discretionary authority from the client within ten 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 if the investment adviser, investment adviser representative or federal covered adviser can directly or indirectly benefit from the number of securities transactions effected in a client'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 instructions of a third party without first having obtained 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, investment adviser representative, or of a federal covered adviser, or a financial institution engaged in the business of loaning funds or securities;

- (g) loaning money or securities to a client unless the investment adviser, investment adviser representative, or federal covered adviser is a financial institution engaged in the business of loaning funds, or the client is an affiliate of the investment adviser, investment adviser representative, or a federal covered adviser;
- (h) misrepresenting to an advisory client, or prospective advisory client, the qualifications of the investment adviser, investment adviser representative, or federal covered adviser, or an employee or affiliate of the investment adviser, investment adviser representative, or federal covered adviser; misrepresenting the nature of the advisory services being offered or fees to be charged for the investment advisory service; or omitting 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 a client prepared by someone other than the investment adviser, investment adviser representative, or federal covered adviser without disclosing that fact. This prohibition does not apply to a situation where the investment adviser, investment adviser representative, or federal covered adviser uses a published research report or statistical analysis to render advice or where an investment adviser, investment adviser representative, or federal covered adviser orders such a report in the normal course of providing service.
- (j) charging a client an advisory fee that is unreasonable in light of the type of services to be provided, the experience and expertise of the investment adviser, investment adviser representative, or federal covered adviser, the sophistication and bargaining power of the client, and whether the investment adviser, investment adviser representative, or federal covered adviser has disclosed that a lower fee for comparable services may be available from other sources;
- (k) failing to disclose to a client in writing before any advice is rendered a material conflict of interest relating to the investment adviser, investment adviser representative, or federal covered 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:
 - (i) compensation arrangements connected with advisory services to a client which are in addition to compensation from the client for the services; and
 - (ii) charging a client an advisory fee for rendering advice when a commission for executing securities transactions pursuant to the advice will be received by the investment adviser, investment adviser representative, or federal covered adviser or its employees or affiliates;
 - (iii) serving as an officer, or in a similar capacity, for any outside company or other entity;
- (l) guaranteeing a client that a specific result will be achieved (gain or no loss) with advice which will be rendered;
- (m) publishing, circulating, or distributing sales material which does not comply with 17 C.F.R. 275.206(4)-1;
- (n) disclosing to a third party the identity, affairs, other financial information, or investment of a client or former client unless:
 - (i) required by law to do so; or

- (ii) consented to by the client;
- (o) taking action, directly or indirectly, with respect to those securities or funds in which a client has a beneficial interest, if the investment adviser, investment adviser representative, or federal covered adviser has custody or possession of the securities or funds when the investment adviser's, investment adviser representative's, or federal covered adviser's action is subject to, and does not comply with, the requirements of 17 C.F.R. 275.206(4)-2, or the investment adviser, investment adviser representative, or federal covered adviser is exempt from these requirements by virtue of 17 C.F.R. 275.206(4)-2(b);
- (p) entering into, extending, or renewing an investment advisory contract, other than a contract for impersonal services, unless the 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 or the manner of calculation of the prepaid fee to be returned in the event of contract termination or nonperformance, and whether the contract grants discretionary power to the investment adviser, investment adviser representative, or federal covered adviser or its representative, and that no assignment of such contract shall be made by the investment adviser, investment adviser representative, or federal covered adviser without the consent of the other party;
- (q) failing to disclose to a client or prospective client each material fact with respect to:
 - (i) the financial condition of the investment adviser, investment adviser representative, or federal covered adviser that is reasonably likely to impair the ability of the investment adviser, investment adviser representative, or federal covered adviser to meet contractual commitments to a client, if the investment adviser, investment adviser representative, or federal covered adviser has express or implied discretionary authority or custody over the client's funds or securities or requires prepayment of advisory fees of more than \$500 from the client, six months or more in advance; or
 - (ii) a legal or disciplinary action that is material to an evaluation of the investment adviser's, investment adviser representative's, or federal covered adviser's integrity or ability to meet contractual commitments to a client;
- (r) 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;
- (s) entering into, extending, or renewing any advisory contract contrary to the provisions of section 205 of the Investment Advisers Act of 1940. This provision is adopted and incorporated, and applies to all advisers registered or required to be registered under the Securities Act of Montana, notwithstanding the fact that such investment adviser is not registered or required to be registered under section 203 of the Investment Advisers Act of 1940. Section 205 establishes standards for investment advisory contracts entered into by the adviser and may be obtained from the Commissioner of Securities, 840 Helena Avenue, Helena, MT 59601;
- (t) 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, which is adopted and incorporated notwithstanding the fact that such investment adviser is not registered or required to be registered under section 203 of the

Investment Advisers Act of 1940. Section 215 of the Investment Advisers Act of 1940 establishes standards for the validity of advisory contracts, and may be obtained from the Commissioner of Securities, 840 Helena Avenue, Helena, MT 59601;

- (u) engaging in any act, practice, or course of business which is fraudulent, deceptive, or manipulative, or contrary to the provisions of section 206(4) of the Investment Advisers Act of 1940, 15 U.S.C. 80b-6(4), which is adopted and incorporated by this reference, notwithstanding the fact that such investment adviser, investment adviser representative, or federal covered adviser is not registered or required to be registered under section 203 of the Investment Advisers Act of 1940, 15 U.S.C. 80b-3. Section 206(4) of the Investment Advisers Act of 1940, 15 U.S.C. 80b-6(4) establishes prohibited practices in the investment advisory business, and may be obtained from the CSI, 840 Helena Avenue, Helena, MT 59601;
- (v) engaging in conduct or any act, indirectly through any other person, which would be unlawful for such person to do directly under the provisions of the Securities Act of Montana or any rule or regulation thereunder; and
- (w) accessing a client's account by using the client's own unique identifying information, except where:
 - (i) the investment adviser, investment adviser representative, or federal covered adviser does not know, or have access to, the client's passwords;
 - (ii) there is an agreement between a data aggregation software company and the custodian(s)/online account platform which permits some form of "back-door" access; and
 - (iii) the data is in a read-only format;
- (x) 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 the investment adviser, investment adviser representative, or federal covered adviser is acting and obtaining the consent of the client to the transaction.
 - (i) the prohibitions of this rule shall not apply to any transaction with a customer of a broker-dealer if the broker-dealer is not acting as an investment adviser, investment adviser representative, or federal covered adviser in relation to the transaction.
 - (ii) the prohibitions of this subsection shall not apply to any transaction with a customer of a broker-dealer if the broker-dealer acts as investment adviser, investment adviser representative, or federal covered 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) by any combination of the foregoing services.

- (iii) publicly distributed written materials or publicly made oral statements shall disclose that, if the purchaser of the advisory communications uses the investment adviser's, investment adviser representative's, or federal covered adviser's services in connection with the sale or purchase of a security which is a subject of the communication, the investment adviser, investment adviser representative, or federal covered adviser may act as principal for its own account or as agent for another person. Compliance by the investment adviser, investment adviser representative, or federal covered adviser with the foregoing disclosure requirement shall not relieve it of any other disclosure obligations under 15 U.S. C. § 206(3);
- (iv) definitions for purposes of (x):
 - (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.
- (y) the prohibitions of this rule shall not apply to an investment adviser, investment adviser representative, or federal covered adviser effecting an agency cross transaction for an advisory client provided the following conditions are met:
 - (i) the advisory client executes a written consent prospectively authorizing the investment adviser, investment adviser representative, or federal covered adviser to effect agency cross transactions for such client;
 - (ii) before obtaining such written consent from the client, the investment adviser, investment adviser representative, or federal covered adviser makes full written disclosure to the client that, with respect to agency cross transactions, the investment adviser, investment adviser representative, or federal covered adviser will act as broker-dealer for, receive commissions from, and have a potentially conflicting division of loyalties and responsibilities regarding both parties to the transactions;
 - (iii) at or before the completion of each agency cross transaction, the investment adviser, investment adviser representative, or federal covered 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, investment adviser representative, or federal covered adviser received or will receive in connection with the transaction. In the case of a purchase, if the investment adviser, investment adviser representative, or federal covered adviser was not participating in a distribution, or, in the case of a sale, if the investment adviser, investment adviser representative, or federal covered adviser was not participating in a tender offer, the written confirmation may state whether the investment adviser, investment adviser representative, or federal covered adviser has been receiving or will receive any other remuneration and that the investment adviser, investment adviser

representative, or federal covered adviser will furnish the source and amount of such remuneration to the client upon the client's written request;

- (iv) at least annually, and with or as part of any written statement or summary of the account from the investment adviser, investment adviser representative, or federal covered adviser, the investment adviser, investment adviser representative, or federal covered 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, investment adviser representative, or federal covered adviser received or will receive in connection with agency cross transactions for the client during the period.
- (v) each written disclosure and confirmation required by this rule must include a conspicuous statement that the client may revoke the written consent required under (x)(i) of this rule at any time by providing written notice to the investment adviser, investment adviser representative, or federal covered adviser.
- (vi) no agency cross transaction may be effected in which the same investment adviser, investment adviser representative, or federal covered adviser recommended the transaction to both any seller and any purchaser.
- (vii) for purposes of this rule, "agency cross transaction for an advisory client" means a transaction in which a person acts as an investment adviser, investment adviser representative, or federal covered adviser in relation to a transaction in which the investment adviser, investment adviser representative, or federal covered adviser, or any person controlling, controlled by, or under common control with such investment adviser, investment adviser representative, or federal covered adviser, acts as a broker-dealer for both the advisory client and another person on the other side of the transaction. When acting in this capacity the person is required to be registered as a broker-dealer in this state unless excluded from the definition.
- (viii) nothing in this rule shall be construed to relieve an investment adviser, investment adviser representative, or federal covered adviser from acting in the best interests of the client, including fulfilling their duty with respect to the best price and execution for the particular transaction for the client nor shall it relieve any investment adviser, investment adviser representative, or federal covered adviser of any other disclosure obligations imposed by the Act.
- (z) 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.
- (aa) 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.
- (bb) taking any action, directly or indirectly, with respect to those securities or funds in which any client has a beneficial interest, where the investment adviser, investment adviser

representative, or federal covered adviser has custody or possession of such securities or funds when the action of the investment adviser, investment adviser representative, or federal covered adviser, is subject to and does not comply with the requirements of ARM 6.10.508; and

- (cc) engaging in other conduct such as nondisclosure, incomplete disclosure, or deceptive practices.

Authorizing statute(s): 30-10-107, MCA

Implementing statute(s): 30-10-201, 30-10-301, MCA

History: NEW, 1989 MAR p. 221, Eff. 1/27/89; AMD, 1998 MAR p. 2527, Eff. 12/18/98; AMD, 1999 MAR p. 56, Eff. 1/15/99; TRANS and AMD, from ARM 6.10.127, 2008 MAR p. 2046, Eff. 9/26/08; AMD, 2020 MAR p. 1874, Eff. 10/24/20.