



State of Wisconsin


LEGISLATIVE REFERENCE BUREAU

RESEARCH APPENDIX - **PLEASE DO NOT REMOVE FROM DRAFTING FILE**

Date Transfer Requested: 02/14/2008 (Per: ARG)





Appendix A ... Part 13 of 23

 The 2007 drafting file for LRB-1109/2

has been transferred to the drafting file for

2007 LRB-3866 (SB 483)

 This cover sheet, the final request sheet, and the final version of the 2007 draft were copied on yellow paper, and returned to the original 2007 drafting file.

 The attached 2007 draft was incorporated into the new 2007 draft listed above. For research purposes, this cover sheet and the complete drafting file were transferred, as a separate appendix, to the 2007 drafting file. If introduced this section will be scanned and added, as a separate appendix, to the electronic drafting file folder.

[ARTICLE] 5

FRAUD AND LIABILITIES

SECTION 501. GENERAL FRAUD. It is unlawful for a person, in connection with the offer, sale, or purchase of a security, directly or indirectly:

(1) to employ a device, scheme, or artifice to defraud;

(2) to make an untrue statement of a material fact or to omit to state a material fact necessary in order to make the statement made, in the light of the circumstances under which it is made, not misleading; or

(3) to engage in an act, practice, or course of business that operates or would operate as a fraud or deceit upon another person.

Official Comments

Prior Provisions: 1956 Act Section 101; RUSA Section 501.

1. Section 501, which was Section 101 in the 1956 Act, was modeled on Rule 10b-5 adopted under the Securities Exchange Act of 1934 and on Section 17(a) of the Securities Act of 1933. There has been significant later case development interpreting Rule 10b-5, Section 17(a), and Section 101 of the 1956 Act. Section 501 is not identical to either Rule 10b-5 or Section 17(a).

2. There are no exemptions from Section 501.

3. Section 501 applies to any securities offer, sale or purchase, including offers, sales, or purchases involving registered, exempt, or federal covered securities. It would also apply to a rescission offer under Section 510.

4. The possible consequences of violating Section 501 are many. These include denial, suspension, or revocation of securities registration under Section 306; denial, revocation, suspension, withdrawal, restriction, condition or limitation of a broker-dealer, agent, investment adviser, or investment adviser representative registration under Section 412; criminal prosecution under Section 508; civil enforcement proceedings under Sections 603; and

administrative proceedings under 604.

5. Because Section 501, like Rule 10b-5, reaches market manipulation, see 8 Louis Loss & Joel Seligman, *Securities Regulation* Ch.10.D (3d ed. 1991), this Act does not include the RUSA market manipulation Section 502, which had no counterpart in the 1956 Act.

6. The culpability required to be pled or proved under Section 501 is addressed in the relevant enforcement context. See, e.g., Section 508, criminal penalties, where "willfulness" must be proven; Section 509, civil liabilities, which includes a reasonable care defense; or civil and administrative enforcement actions under Sections 603 and 604, where no culpability is required to be pled or proven.

7. There is no private cause of action, express or implied, under Section 501. Section 509(m) expressly provides that only Section 509 provides a private cause of action for conduct that could violate Section 501.

SECTION 502. PROHIBITED CONDUCT IN PROVIDING INVESTMENT

ADVICE.

(a) [**Fraud in providing investment advice.**] It is unlawful for a person that advises others for compensation, either directly or indirectly or through publications or writings, as to the value of securities or the advisability of investing in, purchasing, or selling securities or that, for compensation and as part of a regular business, issues or promulgates analyses or reports relating to securities:

(1) to employ a device, scheme, or artifice to defraud another person; or

(2) to engage in an act, practice, or course of business that operates or would operate as a fraud or deceit upon another person.

(b) [**Rules defining fraud.**] A rule adopted under this [Act] may define an act, practice, or course of business of an investment adviser or an investment adviser representative, other than a supervised person of a federal covered investment adviser, as fraudulent, deceptive, or

manipulative, and prescribe means reasonably designed to prevent investment advisers and investment adviser representatives, other than supervised persons of a federal covered investment adviser, from engaging in acts, practices, and courses of business defined as fraudulent, deceptive, or manipulative.

(c) **[Rules specifying contents of advisory contract.]** A rule adopted under this [Act] may specify the contents of an investment advisory contract entered into, extended, or renewed by an investment adviser.

Official Comments

Prior Provisions: 1956 Act Section 102(a); RUSA Section 503.

1. Section 502(a) applies to any person that commits fraud in providing investment advice. Section 502(b) is not limited to persons registered as investment advisers or investment adviser representatives.

2. A person can violate both Section 501 and Section 502 if the person violates Section 502 in connection with the offer, purchase, or sale of a security.

3. The rulemaking authority under Sections 502(b) and (c) would provide the basis for existing NASAA rules concerning investment advisers, to the extent these rules are not preempted by the National Securities Markets Improvement Act of 1996.

4. Under Section 203A(b)(2) of the Investment Advisers Act States retain their authority to investigate and bring enforcement actions with respect to fraud or deceit against a federal covered investment adviser or a person associated with a federal covered investment adviser. Under Section 502(a), which applies to any person, a State could bring an enforcement action against a federal covered investment adviser, including a federal covered investment adviser excluded from the definition of investment adviser in Section 102(15)(E).

5. There is no private cause of action, express or implied, under Section 502. Section 509(m) expressly provides that only Section 509 provides for a private cause of action for prohibited conduct in providing investment advice that could violate Section 502.

SECTION 503. EVIDENTIARY BURDEN.

(a) **[Civil.]** In a civil action or administrative proceeding under this [Act], a person claiming an exemption, exception, preemption, or exclusion has the burden to prove the applicability of the claim.

(b) **[Criminal.]** In a criminal proceeding under this [Act], a person claiming an exemption, exception, preemption, or exclusion has the burden of going forward with evidence of the claim.

Official Comment

Prior Provisions: 1956 Act Section 402(d); RUSA Section 608.

1. As specified in Section 503(a), in a civil or administrative action, the person claiming an exemption, exception, preemption, or exclusion has the burden of persuasion.

2. In contrast, in a criminal action under Section 503(b), the prosecutor is required to prove each element of a crime "beyond a reasonable doubt." The defendant only has the burden of producing evidence of an exemption, exception, preemption, or exclusion. Some court decisions have characterized this burden as an affirmative defense. See, e.g., *United States ex. rel. Schott v. Teahan*, 365 F.2d 191, 195 (6th Cir. 1966) (Ohio blue sky law constitutionally shifts burden of production to defendant); *Commonwealth v. David*, 309 N.E.2d 484, 488 (Mass. 1974) (exemption is an affirmative defense); *State v. Frost*, 387 N.E.2d 235, 238-239 (Ohio 1979) (it is not unconstitutional to require the burden of proof as an affirmative defense to prove a securities law exemption); *State v. Andersen*, 773 A.2d 328 (Conn. 2001) (an exemption from registration is an affirmative defense to the charge of selling unregistered securities).

SECTION 504. FILING OF SALES AND ADVERTISING LITERATURE.

(a) **[Filing requirement.]** Except as otherwise provided in subsection (b), a rule adopted or order issued under this [Act] may require the filing of a prospectus, pamphlet, circular, form letter, advertisement, sales literature, or other advertising record relating to a security or investment advice, addressed or intended for distribution to prospective investors, including clients or prospective clients of a person registered or required to be registered as an investment

adviser under this [Act].

(b) **[Excluded communications.]** This section does not apply to sales and advertising literature specified in subsection (a) which relates to a federal covered security, a federal covered investment adviser, or a security or transaction exempted by Section 201, 202, or 203 except as required pursuant to Section 201(7).

Official Comments

Prior Provisions: 1956 Act Section 403; RUSA Section 405.

1. The prospectuses, pamphlets, circulars, form letters, advertisements, sales literature or advertising communications, include material disseminated electronically or available on a web site.

2. The administrator may bring a civil enforcement action in a court under Section 603 or institute administrative enforcement under Section 604 to prevent publication, circulation or use of any materials required by the administrator to be filed under Section 504 that have not been filed.

3. Section 504(b) is meant to refer to the communications described in Section 504(a).

SECTION 505. MISLEADING FILINGS. It is unlawful for a person to make or cause to be made, in a record that is used in an action or proceeding or filed under this [Act], a statement that, at the time and in the light of the circumstances under which it is made, is false or misleading in a material respect, or, in connection with the statement, to omit to state a material fact necessary to make the statement made, in the light of the circumstances under which it was made, not false or misleading.

Official Comment

Prior Provisions: 1956 Act Section 404; RUSA Section 504.

The definition of "materiality" in *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976) ("an omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote") has generally been followed in both federal and state securities law. See 4 Louis Loss & Joel Seligman, *Securities Regulation* 2071-2105 (3d ed. rev. 2000).

SECTION 506. MISREPRESENTATIONS CONCERNING REGISTRATION OR EXEMPTION. The filing of an application for registration, a registration statement, a notice filing under this [Act], the registration of a person, the notice filing by a person, or the registration of a security under this [Act] does not constitute a finding by the administrator that a record filed under this [Act] is true, complete, and not misleading. The filing or registration or the availability of an exemption, exception, preemption, or exclusion for a security or a transaction does not mean that the administrator has passed upon the merits or qualifications of, or recommended or given approval to, a person, security, or transaction. It is unlawful to make, or cause to be made, to a purchaser, customer, client, or prospective customer or client a representation inconsistent with this section.

Official Comment

Prior Provisions: 1956 Act Section 405; RUSA Section 505.

This Section follows the 1956 Act and RUSA, as well as state securities statutes generally, in providing that a misrepresentation concerning registration or an exemption is unlawful.

SECTION 507. QUALIFIED IMMUNITY. A broker-dealer, agent, investment adviser, federal covered investment adviser, or investment adviser representative is not liable to another broker-dealer, agent, investment adviser, federal covered investment adviser, or investment

adviser representative for defamation relating to a statement that is contained in a record required by the administrator, or designee of the administrator, the Securities and Exchange Commission, or a self-regulatory organization, unless the person knew, or should have known at the time that the statement was made, that it was false in a material respect or the person acted in reckless disregard of the statement's truth or falsity.

Official Comments

Source of Law: National Association of Securities Dealers, Inc. Proposal Relating to Qualified Immunity in Arbitration Proceedings for Statements Made in Forms U-4 and U-5.

1. In 1994 The Securities and Exchange Commission Division of Market Regulation published *The Large Firm Project: A Review of Hiring, Retention, and Supervisory Practices* (1994), which found that a small number of "rogue brokers" were responsible for a significant proportion of customer disciplinary complaints. These brokers in some instances moved from one broker-dealer firm to another, it was explained, without full and complete disclosure of disciplinary problems by the broker-dealer, because of broker-dealer firms' fear of state law defamation claims. See also GAO, *Actions Needed to Better Protect Investors against Unscrupulous Brokers* 3 (1994); Testimony of SEC Chairman Arthur Levitt Concerning the Large Firm Project, Subcomm. on Telecommunications & Fin., House Comm. on Energy & Commerce (Sept. 14, 1994), *reprinted in* 1994-1995 Fed. Sec. L. Rep. (CCH) ¶185,433 (1994).

2. In 1998, the National Association of Securities Dealers proposed qualified immunity for statements made in Forms U-4 and U-5 to address this problem. This proposal was reprinted in Securities Exchange Act Release 39,892, 66 SEC Dock. 2473 (1998). This proposal was limited to arbitration proceedings. It was not acted on by the Securities and Exchange Commission.

3. An alternative approach would be a standard providing for absolute immunity. See generally Anne Wright, *Form U-5 Defamation*, 52 Wash. & Lee L. Rev. 1299 (1995); *Acciaro v. Millennium Sec. Corp.*, 83 F. Supp. 2d 413 (S.D.N.Y. 2000) (discussing both New York qualified and absolute immunity cases).

4. Securities administrators or self-regulatory organizations generally are subject to absolute or qualified immunity for actions of their employees within the course of their official duties. See 10 Louis Loss & Joel Seligman, *Securities Regulation* 4818-4821 (3d ed. rev. 1996).

5. As is generally the law "truth is a complete defense to a defamation action." *Andrews v. Prudential Sec., Inc.*, 160 F.3d 304, 308 (6th Cir. 1998).

6. An agent who has been the subject of a Form U-5, Uniform Termination Notice for Securities Industry Registration, may respond to specified adverse disclosures and have her or his responses reprinted on the published version of Form U-5.

7. Through September 2002 no state had adopted an immunity provision in its securities statute. No state has rejected immunity in this context by judicial decision. A number of states have adopted qualified immunity by judicial decision. See, e.g., *Eaton Vance Distrib., Inc. v. Ulrich*, 692 So.2d 915 (Fla. Dist. Ct. App. 1997); *Bavarati v. Josephal, Lyon & Ross, Inc.*, 28 F.3d 704 (7th Cir. 1994) (Illinois); *Andrews v. Prudential Sec., Inc.*, 160 F.3d 304 (6th Cir. 1998) (Michigan); *Prudential Sec., Inc. v. Dalton*, 929 F. Supp. 1411 (N.D. Okla. 1996) (Oklahoma); *Glennon v. Dean Witter Reynolds Inc.*, 83 F.3d 132 (6th Cir. 1996) (Tennessee).

SECTION 508. CRIMINAL PENALTIES.

(a) **[Criminal penalties.]** A person that willfully violates this [Act], or a rule adopted or order issued under this [Act], except Section 504 or the notice filing requirements of Section 302 or 405, or that willfully violates Section 505 knowing the statement made to be false or misleading in a material respect, upon conviction, shall be fined not more than \$[] or imprisoned not more than [] years, or both. An individual convicted of violating a rule or order under this [Act] may be fined, but may not be imprisoned, if the individual did not have knowledge of the rule or order.

(b) **[Criminal reference not required.]** The [Attorney General or the proper prosecuting attorney] with or without a reference from the administrator, may institute criminal proceedings under this [Act].

(c) **[No limitation on other criminal enforcement.]** This [Act] does not limit the power of this State to punish a person for conduct that constitutes a crime under other laws of this State.

Official Comments

Prior Provisions: 1956 Act Section 409; RUSA Section 604; Securities Exchange Act of 1934 Section 32(a).

1. This Section follows the 1956 Act and the federal securities laws in imposing criminal penalties for any willful violation of the Act. RUSA Section 604 distinguished between felonies and misdemeanors, limiting willful violations of cease and desist orders to a misdemeanor.

2. The term "willfully" has the same meaning in Section 508 as it did in the 1956 Act. All that is required is proof that a person acted intentionally in the sense that the person was aware of what he or she was doing. Proof of evil motive or intent to violate the law or knowledge that the law was being violated is not required.

3. The final sentence of Section 508(a) is based on Section 32(a) of the Securities Exchange Act of 1934, which provides: "[N]o person shall be subject to imprisonment under this section in violation of any rule or regulation if he proves that he had no knowledge of such rule or regulation." The "no knowledge" clause in Section 508(a) is relevant only to sentencing. The person convicted has the burden of persuasion to prove no knowledge at sentencing. Because this does not impose a burden on the defendant to disprove the elements of a crime, Section 32(a) of the Securities Exchange Act of 1934 has been held not to raise a constitutional problem. *United States v. Mandel*, 296 F. Supp. 1038, 1040 (S.D.N.Y. 1969).

4. The appropriate state prosecutor under Section 508(b) may decide whether to bring a criminal action under this statute, another statute, or, when applicable, common law. In certain states the administrator has full or limited criminal enforcement powers.

5. This section does not specify maximum dollar amounts for criminal fines, maximum terms for imprisonment, nor the years of limitation, but does provide for each state to specify appropriate magnitudes for criminal fines or maximum terms for imprisonment.

6. The definition of willfulness in Comment 2 to Section 508 has been followed by most courts. See, e.g., *State v. Hodge*, 460 P.2d 596, 604 (Kan. 1969) ("No specific intent is necessary to constitute the offense where one violates the securities act except the intent to do the act denounced by the statute"); *State v. Nagel*, 279 N.W.2d 911, 915 (S.D. 1979) ("[I]t is widely understood that the legislature may forbid the doing of an act and make its commission a crime without regard to the intent or knowledge of the doer"); *State v. Fries*, 337 N.W.2d 398, 405 (Neb. 1983) (proof of a specific intent, evil motive, or knowledge that the law was being violated is not required to sustain a criminal conviction under a state's blue sky law); *People v. Riley*, 708 P.2d 1359, 1362 (Colo. 1985) ("A person acts 'knowingly' or 'willfully' with respect to conduct . . . when he is aware that his conduct . . . exists"); *State v. Larsen*, 865 P.2d 1355, 1358 (Utah 1993) (willful implies a willingness to commit the act, not an intent to violate the law or to injure another or acquire any advantage); *State v. Montgomery*, 17 P.3d 292, 294 (Idaho 2001) (bad faith is not required for a violation of a state securities act; willful implies "simply a purpose or willingness to commit the act or make the omission referred to"); *State v. Dumke*, 901 S.W.2d 100, 102 (Mo. Ct. App. 1995) (*mens rea* not required); *State v. Mueller*, 549 N.W.2d 455, 460 (Wis. Ct. App. 1996) (willfulness does not require proof that the defendant acted with intent to defraud or knowledge that the law was violated); *United States v. Lilley*, 291 F. Supp.

989, 993 (S.D. Tex. 1968) (“no knowledge” clause in federal statute not available to defendant claiming lack of knowledge of particular SEC rule).

SECTION 509. CIVIL LIABILITY.

(a) **[Securities Litigation Uniform Standards Act.]** Enforcement of civil liability under this section is subject to the Securities Litigation Uniform Standards Act of 1998.

(b) **[Liability of seller to purchaser.]** A person is liable to the purchaser if the person sells a security in violation of Section 301 or, by means of an untrue statement of a material fact or an omission to state a material fact necessary in order to make the statement made, in light of the circumstances under which it is made, not misleading, the purchaser not knowing the untruth or omission and the seller not sustaining the burden of proof that the seller did not know and, in the exercise of reasonable care, could not have known of the untruth or omission. An action under this subsection is governed by the following:

(1) The purchaser may maintain an action to recover the consideration paid for the security, less the amount of any income received on the security, and interest [at the legal rate of interest] from the date of the purchase, costs, and reasonable attorneys' fees determined by the court, upon the tender of the security, or for actual damages as provided in paragraph (3).

(2) The tender referred to in paragraph (1) may be made any time before entry of judgment. Tender requires only notice in a record of ownership of the security and willingness to exchange the security for the amount specified. A purchaser that no longer owns the security may recover actual damages as provided in paragraph (3).

(3) Actual damages in an action arising under this subsection are the amount that would be recoverable upon a tender less the value of the security when the purchaser disposed

of it, and interest [at the legal rate of interest] from the date of the purchase, costs, and reasonable attorneys' fees determined by the court.

(c) [**Liability of purchaser to seller.**] A person is liable to the seller if the person buys a security by means of an untrue statement of a material fact or omission to state a material fact necessary in order to make the statement made, in light of the circumstances under which it is made, not misleading, the seller not knowing of the untruth or omission, and the purchaser not sustaining the burden of proof that the purchaser did not know, and in the exercise of reasonable care, could not have known of the untruth or omission. An action under this subsection is governed by the following:

(1) The seller may maintain an action to recover the security, and any income received on the security, costs, and reasonable attorneys' fees determined by the court, upon the tender of the purchase price, or for actual damages as provided in paragraph (3).

(2) The tender referred to in paragraph (1) may be made any time before entry of judgment. Tender requires only notice in a record of the present ability to pay the amount tendered and willingness to take delivery of the security for the amount specified. If the purchaser no longer owns the security, the seller may recover actual damages as provided in paragraph (3).

(3) Actual damages in an action arising under this subsection are the difference between the price at which the security was sold and the value the security would have had at the time of the sale in the absence of the purchaser's conduct causing liability, and interest [at the legal rate of interest] from the date of the sale of the security, costs, and reasonable attorneys' fees determined by the court.

(d) [**Liability of unregistered broker-dealer and agent.**] A person acting as a broker-dealer or agent that sells or buys a security in violation of Section 401(a), 402(a), or 506 is liable to the customer. The customer, if a purchaser, may maintain an action for recovery of actual damages as specified in subsections (b)(1) through (3), or, if a seller, for a remedy as specified in subsections (c)(1) through (3).

(e) [**Liability of unregistered investment adviser and investment adviser representative.**] A person acting as an investment adviser or investment adviser representative that provides investment advice for compensation in violation of Section 403(a), 404(a), or 506 is liable to the client. The client may maintain an action to recover the consideration paid for the advice, interest [at the legal rate of interest] from the date of payment, costs, and reasonable attorneys' fees determined by the court.

(f) [**Liability for investment advice.**] A person that receives directly or indirectly any consideration for providing investment advice to another person and that employs a device, scheme, or artifice to defraud the other person or engages in an act, practice, or course of business that operates or would operate as a fraud or deceit on the other person, is liable to the other person. An action under this subsection is governed by the following:

(1) The person defrauded may maintain an action to recover the consideration paid for the advice and the amount of any actual damages caused by the fraudulent conduct, interest [at the legal rate of interest] from the date of the fraudulent conduct, costs, and reasonable attorneys' fees determined by the court, less the amount of any income received as a result of the fraudulent conduct.

(2) This subsection does not apply to a broker-dealer or its agents if the investment

advice provided is solely incidental to transacting business as a broker-dealer and no special compensation is received for the investment advice.

(g) [**Joint and several liability.**] The following persons are liable jointly and severally with and to the same extent as persons liable under subsections (b) through (f):

(1) a person that directly or indirectly controls a person liable under subsections (b) through (f), unless the controlling person sustains the burden of proof that the person did not know, and in the exercise of reasonable care could not have known, of the existence of conduct by reason of which the liability is alleged to exist;

(2) an individual who is a managing partner, executive officer, or director of a person liable under subsections (b) through (f), including an individual having a similar status or performing similar functions, unless the individual sustains the burden of proof that the individual did not know and, in the exercise of reasonable care could not have known, of the existence of conduct by reason of which the liability is alleged to exist;

(3) an individual who is an employee of or associated with a person liable under subsections (b) through (f) and who materially aids the conduct giving rise to the liability, unless the individual sustains the burden of proof that the individual did not know and, in the exercise of reasonable care could not have known, of the existence of conduct by reason of which the liability is alleged to exist; and

(4) a person that is a broker-dealer, agent, investment adviser, or investment adviser representative that materially aids the conduct giving rise to the liability under subsections (b) through (f), unless the person sustains the burden of proof that the person did not know and, in the exercise of reasonable care could not have known, of the existence of conduct by reason of

which liability is alleged to exist.

(h) **[Right of contribution.]** A person liable under this section has a right of contribution as in cases of contract against any other person liable under this section for the same conduct.

(i) **[Survival of cause of action.]** A cause of action under this section survives the death of an individual who might have been a plaintiff or defendant.

(j) **[Statute of limitations.]** A person may not obtain relief:

(1) under subsection (b) for violation of Section 301, or under subsection (d) or (e), unless the action is instituted within one year after the violation occurred; or

(2) under subsection (b), other than for violation of Section 301, or under subsection (c) or (f), unless the action is instituted within the earlier of two years after discovery of the facts constituting the violation and five years after the violation.

(k) **[No enforcement of violative contract.]** A person that has made, or has engaged in the performance of, a contract in violation of this [Act] or a rule adopted or order issued under this [Act], or that has acquired a purported right under the contract with knowledge of conduct by reason of which its making or performance was in violation of this [Act], may not base an action on the contract.

(l) **[No contractual waiver.]** A condition, stipulation, or provision binding a person purchasing or selling a security or receiving investment advice to waive compliance with this [Act] or a rule adopted or order issued under this [Act] is void.

(m) **[Survival of other rights or remedies.]** The rights and remedies provided by this [Act] are in addition to any other rights or remedies that may exist, but this [Act] does not create a cause of action not specified in this section or Section 411(e).

Official Comments

Prior Provisions: 1956 Act Section 410; RUSA Sections 605-607, 609, 802.

1. Under Section 509 violations of two or more sections can be proven, but the remedy is limited either to rescission or actual damages. Actual damages means compensatory damages. Punitive or "double" damages are not provided by this section which also is the standard under Section 28(a) of the Securities Exchange Act of 1934. See 9 Louis Loss & Joel Seligman, Securities Regulation 4408-4427 (3d ed. rev. 1992).

2. The Securities Litigation Uniform Standards Act of 1998 cited in Section 509(a) modifies the entire Section 509.

3. As with Section 12(a)(2) of the Securities Act of 1933, Section 509(b) contains a type of privity requirement in that the purchaser is required to bring an action against the seller. Section 509(b) is broader than Section 12(a)(2) in that it will reach all sales in violation of Section 301, not just sales "by means of a prospectus" as is the law under Section 12(a)(2). See *Gustafson v. Alloyd Co., Inc.*, 513 U.S. 561 (1995).

4. Unlike the current standards on implied rights of action under Rule 10b-5, neither causation nor reliance has been held to be an element of a private cause of action under the precursor to Section 509(b). See *Gerhard W. Gohler, IRA v. Wood*, 919 P.2d 561 (Utah 1996); *Ritch v. Robinson-Humphrey Co.*, 748 So. 2d 861 (Ala. 1999); *Kaufman v. I-Stat Corp.*, 754 A.2d 1188 (N.J. 2000).

5. The measure of damages in Section 509(b)(3) is that contemplated by Section 12 of the Securities of 1933. See 9 Louis Loss and Joel Seligman, Securities Regulations 4242-4246 (3d ed. 1992). The measure of damages in Section 509(c)(3), however, is that contemplated by Rule 10b-5. See 9 id. 4408-4427. In providing for damages as an alternative to rescission, Section 509(b)(3) follows the 1956 Act and is an improvement upon many earlier state provisions, which conditioned the plaintiff's right of recovery on his or her being in a position to make a good tender. A plaintiff is not given the right under this type of statutory formula to retain stock and also seek damages.

6. Sections 509(e) and (f) are based on a proposed NASAA amendment to the Uniform Securities Act adopted in order "to establish civil liability for individuals who willfully violate Section 102 dealing with fraudulent practices pertaining to advisory activities." Neither provision is intended to limit other state law claims for providing investment advice.

7. Broker-dealer employees, including research analysts, who receive no special compensation from third parties for investment advice would not be liable under Section 509(f).

8. The control liability provision in Section 509(g)(1) is modeled on that in the 1956 Act. On the meaning of "control," see 4 Louis Loss & Joel Seligman, Securities Regulations 1703-1727 (3d ed. rev. 2000).

9. The defense of lack of knowledge in Sections 509(g) is also modeled on the 1956 Act.

10. Under Section 509(g)(2) partners, officers, and directors are liable, subject to the defense afforded by that subsection, without proof that they aided in the sale. In Section 509(g)(2), the term "partner" is intended to be limited to partners with management responsibilities, rather than a partner with a passive investment.

11. Under 509(g)(4), the performance by a clearing broker of the clearing broker's contractual functions – even though necessary to the processing of a transaction – without more would not constitute material aid or result in liability under this subsection. See, e.g., *Ross v. Bolton*, 904 F.2d 819 (2d Cir. 1990).

12. The "reasonable attorneys' fees" specified in Section 509 are permissive, not mandatory. See, e.g., *Andrews v. Blue*, 489 F.2d 367, 377 (10th Cir. 1973), (Colorado statute).

13. The contribution provision in Section 509(h) is a safeguard to avoid the common law principle that prohibited contribution among joint tortfeasors.

14. The statute of limitations in Section 509(j) is a hybrid of the 1956 Act and federal securities law approaches. The 1956 Act Section 410(p) provided that: "No person may sue under this section more than two years after the contract of sale." Under this provision, the state courts generally decline to extend a statute of limitations period on grounds of fraudulent concealment or equitable tolling.

Before the July 2002 enactment of the Sarbanes-Oxley Act, Rule 10b-5 of the Securities Exchange Act as construed by the United States Supreme Court in *Lampf, Pleva, Lipkind, Preps & Petigrew v. Gilbertson*, 501 U.S. 350 (1991), prohibited equitable tolling under the federal securities law one year after discovery and three years after the act formula. See generally 10 Louis Loss & Joel Seligman, *Securities Regulation* 4505-4525 (3d. ed. rev. 1996). The Sarbanes-Oxley Act added 28 U.S.C. §1658(b) which provides

... a private right of action that involves a claim of fraud, deceit, manipulation, or contrivance in contravention of a regulatory requirement concerning the securities laws, as defined in section 3(a)(47) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(47)), may be brought not later than the earlier of ---

(1) 2 years after the discovery of the facts constituting the violation; or

(2) 5 years after such violation.

Section 509(j)(1), as with the 1956 Act, is a unitary statute of repose, requiring an action to be commenced within one year after a violation occurred. It is not intended that equitable tolling be permitted.

Section 509(j)(2), in contrast, generally follows the federal securities law model. An action must be brought within the earlier of two years after discovery or five years after the violation. As with federal courts construing the statute of limitations under Rule 10b-5, it is intended that the plaintiff's right to proceed is limited to two years after actual discovery "or after such discovery should have been made by the exercise of reasonable diligence" (inquiry notice), see, e.g., *Law v. Medco Research, Inc.*, 113 F.3d 781 (7th Cir. 1997), or five years after the violation.

The rationale for replicating the basic federal statute of limitations in this Act is to discourage forum shopping. If the statute of limitations applicable to Rule 10b-5 were to be changed in the future, identical changes should be made in Section 509(j)(2).

15. Section 509(k) is similar to Section 29(b) of the Securities Exchange Act and is intended to apply only to actions to enforce illegal contracts. See Louis Loss, *Commentary on the Uniform Securities Act 150* (1976).

16. Section 509(m) follows the 1956 Act.

17. Section 509 and Section 411(e) provide the exclusive private causes of action under this Act.

SECTION 510. RESCISSION OFFERS. A purchaser, seller, or recipient of investment advice may not maintain an action under Section 509 if:

(1) The purchaser, seller, or recipient of investment advice receives in a record, before the action is instituted:

(A) an offer stating the respect in which liability under Section 509 may have arisen and fairly advising the purchaser, seller, or recipient of investment advice of that person's rights in connection with the offer, and any financial or other information necessary to correct all material misrepresentations or omissions in the information that was required by this [Act] to be furnished to that person at the time of the purchase, sale, or investment advice;

(B) if the basis for relief under this section may have been a violation of Section

509(b), an offer to repurchase the security for cash, payable on delivery of the security, equal to the consideration paid, and interest [at the legal rate of interest] from the date of the purchase, less the amount of any income received on the security, or, if the purchaser no longer owns the security, an offer to pay the purchaser upon acceptance of the offer damages in an amount that would be recoverable upon a tender, less the value of the security when the purchaser disposed of it, and interest [at the legal rate of interest] from the date of the purchase in cash equal to the damages computed in the manner provided in this subsection;

(C) if the basis for relief under this section may have been a violation of Section 509(c), an offer to tender the security, on payment by the seller of an amount equal to the purchase price paid, less income received on the security by the purchaser and interest [at the legal rate of interest] from the date of the sale; or if the purchaser no longer owns the security, an offer to pay the seller upon acceptance of the offer, in cash, damages in the amount of the difference between the price at which the security was purchased and the value the security would have had at the time of the purchase in the absence of the purchaser's conduct that may have caused liability and interest [at the legal rate of interest] from the date of the sale;

(D) if the basis for relief under this section may have been a violation of Section 509(d); and if the customer is a purchaser, an offer to pay as specified in subparagraph (B); or, if the customer is a seller, an offer to tender or to pay as specified in subparagraph (C);

(E) if the basis for relief under this section may have been a violation of Section 509(e), an offer to reimburse in cash the consideration paid for the advice and interest [at the legal rate of interest] from the date of payment; or

(F) if the basis for relief under this section may have been a violation of Section

509(f), an offer to reimburse in cash the consideration paid for the advice, the amount of any actual damages that may have been caused by the conduct, and interest [at the legal rate of interest] from the date of the violation causing the loss;

(2) the offer under paragraph 1 states that it must be accepted by the purchaser, seller, or recipient of investment advice within 30 days after the date of its receipt by the purchaser, seller, or recipient of investment advice or any shorter period, of not less than three days, that the administrator, by order, specifies;

(3) the offeror has the present ability to pay the amount offered or to tender the security under paragraph (1);

(4) the offer under paragraph (1) is delivered to the purchaser, seller, or recipient of investment advice, or sent in a manner that ensures receipt by the purchaser, seller, or recipient of investment advice; and

(5) the purchaser, seller, or recipient of investment advice that accepts the offer under paragraph (1) in a record within the period specified under paragraph (2) is paid in accordance with the terms of the offer.

Official Comments

Prior Provisions: 1956 Act Section 410(e); RUSA Section 607.

1. A rescission offer must meet the specific requirements of Section 510 for civil liability under Section 509 to be extinguished. Cf. *Binder v. Gordian Sec., Inc.*, 742 F. Supp. 663, 666 (N.D. Ga. 1990). See generally Rowe, *Rescission Offers under Federal and State Securities Law*, 12 J. Corp. L. 383 (1987).

2. A rescission offer that does not comply with Section 510 is subject to civil liability, administrative enforcement, or criminal penalties under this Act. A rescission offer, for example, could violate Section 501, the general fraud provision.

3. The administrator may publish a form that would comply with Section 510, but the

form would not be the only one that could be used by the parties.

4. A valid rescission offer will be exempt from securities registration. See Section 202(19).

5. If a state chooses to add a notice or filing provision, it could provide this provision in Section 510(6), which would state:

(6) The offer [or a notice] is required to be filed with the administrator 10 business days before the offering and conform in form and content with a rule prescribed by the administrator.

[ARTICLE] 6

ADMINISTRATION AND JUDICIAL REVIEW

SECTION 601. ADMINISTRATION.

(a) **[Administration.]** The administrator shall administer this [Act] [insert any related provisions on such matters as method of selection, salary, term of office, selection and remuneration of personnel, and annual reports to the legislature or governor that are appropriate to the particular State].

(b) **[Unlawful use of records or information.]** It is unlawful for the administrator or an officer, employee, or designee of the administrator to use for personal benefit or the benefit of others records or other information obtained by or filed with the administrator that are not public under Section 607(b). This [Act] does not authorize the administrator or an officer, employee, or designee of the administrator to disclose the record or information, except in accordance with Section 602, 607(c), or 608.

(c) **[No privilege or exemption created or diminished.]** This [Act] does not create or diminish a privilege or exemption that exists at common law, by statute or rule, or otherwise.

(d) **[Investor education.]** The administrator may develop and implement investor education initiatives to inform the public about investing in securities, with particular emphasis on the prevention and detection of securities fraud. In developing and implementing these initiatives, the administrator may collaborate with public and nonprofit organizations with an interest in investor education. The administrator may accept a grant or donation from a person that is not affiliated with the securities industry or from a nonprofit organization, regardless of whether the organization is affiliated with the securities industry, to develop and implement

1 (4) INVESTOR EDUCATION. The administrator may develop and implement
 2 investor education initiatives to inform the public about investing in securities, with
 3 particular emphasis on the prevention and detection of securities fraud. In
 4 developing and implementing these initiatives, the administrator may collaborate
 5 with public and nonprofit organizations with an interest in investor education. The
 6 administrator may accept a grant or donation from a person that is not affiliated with
 7 the securities industry or from a nonprofit organization, regardless of whether the
 8 organization is affiliated with the securities industry, to develop and implement
 9 investor education initiatives. This subsection does not authorize the administrator
 10 to require participation or monetary contributions of a registrant in an investor
 11 education program.

12 (5) THE SECURITIES INVESTOR EDUCATION AND TRAINING FUND. The Securities
 13 Investor Education and Training Fund is created to provide funds for the purposes
 14 specified in sub. (4). All monies collected from civil penalties imposed under s.
 15 551.604 shall be credited to the appropriation under s. 20.144 (1) (i).

***NOTE: I need to figure this out. Maybe d-note re common school fund. Probably
 revise sub. (5) and amend s. 20.144 (1) (i) if needed. Add note here that forfeitures through
 court must go to common school fund, by constitution. So this is limited to administrative
 assessments. Copy

16 MERGE PROVISION BELOW WITH ONE ABOVE -

17 SECTION 2. 551.605 (2) of the statutes is amended to read:

18 551.605 (2) INVESTOR EDUCATION. All moneys collected from the administrative
 19 assessment under sub. (1) shall be credited to the appropriation under s. 20.144 (1)
 20 (i). Subject to s. 20.144 (1) (i), the division shall use moneys credited to that
 21 appropriation to provide information to residents of this state about investments in
 22 securities to help investors and potential investors evaluate their investment
 23 decisions, protect themselves from unfair, inequitable or fraudulent offerings, choose

investor education initiatives. This subsection does not authorize the administrator to require participation or monetary contributions of a registrant in an investor education program.

(e) **[The Securities Investor Education and Training Fund.]** The Securities Investor Education and Training Fund is created to provide funds for the purposes specified in subsection (d). [All monies received by the State by reason of civil penalties pursuant to this [Act] shall be deposited in the Securities Investor Education and Training Fund. The State may insert any other provision concerning appropriations to support this fund as well as procedures for its operations.]

Official Comments

Prior Provisions: 1956 Act Section 406; RUSA Sections 701-702.

1. Section 601(b) should be read with Section 607. Section 601(b) prohibits the administrator or the administrator's officers and employees from using for personal benefit records or information that Section 607(b) specifies do not constitute public records. Section 601(b) is not intended to limit the operation of Section 607(a). Neither Section 601(b) nor 607(b) is intended to impede the ability of the agencies specified in Section 608(a) from sharing records or other information in connection with an examination or an investigation.

2. Section 601(c) makes clear that nothing in this Act alters the availability of evidentiary privileges. That question is left to the general law of the particular state.

3. Sections 601(d) and (e) were adopted in recognition of the importance of investor education. An increasing number of jurisdictions are earmarking specific funds for this purpose. The lack of financial acumen among public investors, seniors, and students continues to be demonstrated in recent industry and regulatory studies. The importance of investor financial literacy is increasingly crucial given the decades long shift from defined benefit retirement plans toward defined contribution plans where employees are left to direct their own retirement accounts.

SECTION 602. INVESTIGATIONS AND SUBPOENAS.

(a) **[Authority to investigate.]** The administrator may:

(1) conduct public or private investigations within or outside of this State which the administrator considers necessary or appropriate to determine whether a person has violated, is

violating, or is about to violate this [Act] or a rule adopted or order issued under this [Act], or to aid in the enforcement of this [Act] or in the adoption of rules and forms under this [Act];

(2) require or permit a person to testify, file a statement, or produce a record, under oath or otherwise as the administrator determines, as to all the facts and circumstances concerning a matter to be investigated or about which an action or proceeding is to be instituted; and

(3) publish a record concerning an action, proceeding, or an investigation under, or a violation of, this [Act] or a rule adopted or order issued under this [Act] if the administrator determines it is necessary or appropriate in the public interest and for the protection of investors.

(b) **[Administrator powers to investigate.]** For the purpose of an investigation under this [Act], the administrator or its designated officer may administer oaths and affirmations, subpoena witnesses, seek compulsion of attendance, take evidence, require the filing of statements, and require the production of any records that the administrator considers relevant or material to the investigation.

(c) **[Procedure and remedies for noncompliance.]** If a person does not appear or refuses to testify, file a statement, produce records, or otherwise does not obey a subpoena as required by the administrator under this [Act], the administrator [may refer the matter to the Attorney General or the proper attorney, who] may apply to [insert name of the appropriate court] or a court of another State to enforce compliance. The court may:

- (1) hold the person in contempt;
- (2) order the person to appear before the administrator;
- (3) order the person to testify about the matter under investigation or in question;
- (4) order the production of records;

(5) grant injunctive relief, including restricting or prohibiting the offer or sale of securities or the providing of investment advice;

(6) impose a civil penalty of not less than \$[] and not greater than \$[] for each violation; and

(7) grant any other necessary or appropriate relief.

(d) [**Application for relief.**] This section does not preclude a person from applying to [insert name of appropriate court] or a court of another State for relief from a request to appear, testify, file a statement, produce records, or obey a subpoena.

(e) [**Use immunity procedure.**] An individual is not excused from attending, testifying, filing a statement, producing a record or other evidence, or obeying a subpoena of the administrator under this [Act] or in an action or proceeding instituted by the administrator under this [Act] on the ground that the required testimony, statement, record, or other evidence, directly or indirectly, may tend to incriminate the individual or subject the individual to a criminal fine, penalty, or forfeiture. If the individual refuses to testify, file a statement, or produce a record or other evidence on the basis of the individual's privilege against self-incrimination, the administrator may apply [to the name of the appropriate court] to compel the testimony, the filing of the statement, the production of the record, or the giving of other evidence. The testimony, record, or other evidence compelled under such an order may not be used, directly or indirectly, against the individual in a criminal case, except in a prosecution for perjury or contempt or otherwise failing to comply with the order.

(f) [**Assistance to securities regulator of another jurisdiction.**] At the request of the securities regulator of another State or a foreign jurisdiction, the administrator may provide assistance if the requesting regulator states that it is conducting an investigation to determine

whether a person has violated, is violating, or is about to violate a law or rule of the other State or foreign jurisdiction relating to securities matters that the requesting regulator administers or enforces. The administrator may provide the assistance by using the authority to investigate and the powers conferred by this section as the administrator determines is necessary or appropriate. The assistance may be provided without regard to whether the conduct described in the request would also constitute a violation of this [Act] or other law of this State if occurring in this State. In deciding whether to provide the assistance, the administrator may consider whether the requesting regulator is permitted and has agreed to provide assistance reciprocally within its State or foreign jurisdiction to the administrator on securities matters when requested; whether compliance with the request would violate or prejudice the public policy of this State; and the availability of resources and employees of the administrator to carry out the request for assistance.

Official Comments

Prior Provisions: 1956 Act Section 407; RUSA Section 601.

1. Sections 602 (a) and (b) follow the 1956 Act, which was modeled generally on Sections 21(a) through (d) of the Securities Exchange Act of 1934 as it then read.

2. Standards for issuance of subpoenas have been generally established in federal and state securities law. See, e.g., 10 Louis Loss & Joel Seligman, *Securities Regulation* 4917-4937 (3d ed. rev. 1996) (discussing *Oklahoma Press Pub. Co. v. Walling*, 327 U.S. 186 (1946) and other cases). The scope of subpoena enforcement in each state is a general matter for judicial determination. Under Section 602, an individual subpoenaed to testify by the administrator is not compelled to testify within the meaning of these sections simply by service of a subpoena. Under Section 602(b) the individual can be subpoenaed and compelled to attend. Once in attendance an individual can assert an evidentiary privilege or exemption, see Section 601(c), including the Fifth Amendment privilege against self-incrimination. If an individual refuses to testify or give evidence, the administrator may apply (or have the appropriate State attorney apply) to the appropriate court for the relief specified in Section 602(c). If the individual invokes the privilege against self-incrimination, Section 602(d) allows the administrator to apply to the appropriate court to compel testimony under the "use immunity" provision barring the record compelled or other evidence obtained from being used in a criminal case. See *People v.*

District Co. of Arapahoe County, 894 P.2d 739 (Colo. 1995). The phrase "directly or indirectly" in Section 602(e) is intended to include testimony, other evidence, or other information derived from immunized testimony, statements, records, or evidence.

3. Section 602 is intended to apply generally to securities offers and sales under Article 3 and broker-dealer and investment adviser activity under Article 4, when there is noncompliance with the first sentence of Section 602(c). This subsection does not limit the powers of an administrator under other provisions of this Act.

4. A court may quash a subpoena for good cause under Section 602(d). The court may decline to enforce a subpoena that is arbitrary, capricious, or oppressive.

5. Where appropriate under Section 602(f), an administrator could move to authorize admission of a requesting state's attorney under existing *pro hac vice* rules.

6. Section 602(f) is consistent with the Securities Litigation Uniform Standard Act of 1998 which provides in Section 102(e):

The Securities and Exchange Commission, in consultation with State securities commissions (or any agencies or offices performing like functions), shall seek to encourage the adoption of State laws providing for reciprocal enforcement by State securities commissions of subpoenas issued by another State securities commission seeking to compel persons to attend, testify in, or produce documents or records in connection with an action or investigation by a State securities commission of an alleged violation of State securities laws.

7. There are limitations on financial institutions being subject to visitorial powers by State officials, such as those affecting national banks contained in 12 U.S.C. 484 and 12 C.F.R. Sec. 7.4000. Law outside this Act may place similar limits on state chartered financial institutions being subjected to visitorial powers. This Act does not negate these limitations.

SECTION 603. CIVIL ENFORCEMENT.

(a) **[Civil action instituted by administrator.]** If the administrator believes that a person has engaged, is engaging, or is about to engage in an act, practice, or course of business constituting a violation of this [Act] or a rule adopted or order issued under this [Act] or that a person has, is, or is about to engage in an act, practice, or course of business that materially aids a violation of this [Act] or a rule adopted or order issued under this [Act], the administrator may maintain an action in the [insert the name of the court] to enjoin the act, practice, or course of business and to enforce compliance with this [Act] or a rule adopted or order issued under this [Act].

(b) **[Relief available.]** In an action under this section and on a proper showing, the court may:

(1) issue a permanent or temporary injunction, restraining order, or declaratory judgment;

(2) order other appropriate or ancillary relief, which may include:

(A) an asset freeze, accounting, writ of attachment, writ of general or specific execution, and appointment of a receiver or conservator, that may be the administrator, for the defendant or the defendant's assets;

(B) ordering the administrator to take charge and control of a defendant's property, including investment accounts and accounts in a depository institution, rents, and profits; to collect debts; and to acquire and dispose of property;

(C) imposing a civil penalty up to \$[] for a single violation or up to \$[] for more than one violation; an order of rescission, restitution, or disgorgement directed to a person that has engaged in an act, practice, or course of business constituting a violation of this [Act] or the predecessor act or a rule adopted or order issued under this [Act] or the predecessor act; and

(D) ordering the payment of prejudgment and postjudgment interest; or

(3) order such other relief as the court considers appropriate.

(c) **[No bond required.]** The administrator may not be required to post a bond in an action or proceeding under this [Act].

Official Comments

Prior Provisions: 1956 Act Section 408; RUSA Section 603

1. Section 408 of the 1956 Act was limited to injunctions. This Section follows RUSA in broadening the civil remedies available when the administrator believes that a violation has occurred. A primary purpose of a broad range of potential sanctions is to enable administrators to better tailor appropriate sanctions to particular misconduct.

2. The administrator alternatively may proceed to seek administrative enforcement under Section 604; to deny, suspend, or revoke a securities registration under Section 306; or to deny, suspend, revoke, or take other action against a broker-dealer, agent, investment adviser, or investment adviser representative registration under Section 412.

3. Constitutional due process considerations can also be addressed by rulemaking or incorporation of the applicable administrative procedure act provisions of each jurisdiction. The term "upon a proper showing" has a settled meaning in the federal securities laws. See, e.g., Securities Act of 1933 Section 20(b).

4. As with Sections 509(g)(3) and (4), materially aid in Section 603(a) does not include ministerial or clerical acts.

SECTION 604. ADMINISTRATIVE ENFORCEMENT.

(a) **[Issuance of an order or notice.]** If the administrator determines that a person has engaged, is engaging, or is about to engage in an act, practice, or course of business constituting a violation of this [Act] or a rule adopted or order issued under this [Act] or that a person has materially aided, is materially aiding, or is about to materially aid an act, practice, or course of business constituting a violation of this [Act] or a rule adopted or order issued under this [Act], the administrator may:

(1) issue an order directing the person to cease and desist from engaging in the act, practice, or course of business or to take other action necessary or appropriate to comply with this [Act];

(2) issue an order denying, suspending, revoking, or conditioning the exemptions for a broker-dealer under Section 401(b)(1)(D) or (F) or an investment adviser under Section 403(b)(1)(C); or

(3) issue an order under Section 204.

(b) [**Summary process.**] An order under subsection (a) is effective on the date of issuance. Upon issuance of the order, the administrator shall promptly serve each person subject to the order with a copy of the order and a notice that the order has been entered. The order must include a statement whether the administrator will seek a civil penalty or costs of the investigation, a statement of the reasons for the order, and notice that, within 15 days after receipt of a request in a record from the person, the matter will be scheduled for a hearing. If a person subject to the order does not request a hearing and none is ordered by the administrator within 30 days after the date of service of the order, the order becomes final as to that person by operation of law. If a hearing is requested or ordered, the administrator, after notice of and opportunity for hearing to each person subject to the order, may modify or vacate the order or extend it until final determination.

(c) [**Procedure for final order.**] If a hearing is requested or ordered pursuant to subsection (b), a hearing must be held [pursuant to the state administrative procedure act]. A final order may not be issued unless the administrator makes findings of fact and conclusions of law in a record [in accordance with the state administrative procedure act]. The final order may make final, vacate, or modify the order issued under subsection (a).

(d) [**Civil penalty.**] In a final order under subsection (c), the administrator may impose a civil penalty up to \$[] for a single violation or up to \$[] for more than one violation.

(e) [**Costs.**] In a final order, the administrator may charge the actual cost of an investigation or proceeding for a violation of this [Act] or a rule adopted or order issued under this [Act].

(f) [**Filing of certified final order with court; effect of filing.**] If a petition for judicial review of a final order is not filed in accordance with Section 609, the administrator may file a certified copy of the final order with the clerk of a court of competent jurisdiction. The order so filed has the same effect as a judgment of the court and may be recorded, enforced, or satisfied in the same manner as a judgment of the court.

(g) [**Enforcement by court; further civil penalty.**] If a person does not comply with an order under this section, the administrator may petition a court of competent jurisdiction to enforce the order. The court may not require the administrator to post a bond in an action or proceeding under this section. If the court finds, after service and opportunity for hearing, that the person was not in compliance with the order, the court may adjudge the person in civil contempt of the order. The court may impose a further civil penalty against the person for contempt in an amount not less than \$[] but not greater than \$[] for each violation and may grant any other relief the court determines is just and proper in the circumstances.

Official Comments

Prior Provisions: RUSA Sections 602, 712.

1. Section 604, unlike Section 603, may be initiated by the administrator without prior judicial process or a prior hearing. The section, among other matters, empowers the administrator to act summarily in appropriate circumstances.

2. Sections 603 and 604 are intended to be available to the administrator against persons

not subject to stop orders under Section 306 or proceedings against registered broker-dealers, agents, investment advisers, or investment adviser representatives under Section 412. All persons or securities not subject to Section 306 or 412 will be subject to Sections 603 and 604. A person must be covered by either (1) Sections 306 or 412 or (2) Sections 603 or 604.

3. Service of an order or notice under this Section is not effective unless made in accordance with Section 611.

SECTION 605. RULES, FORMS, ORDERS, INTERPRETATIVE OPINIONS, AND HEARINGS.

(a) **[Issuance and adoption of forms, orders, and rules.]** The administrator may:

(1) issue forms and orders and, after notice and comment, may adopt and amend rules necessary or appropriate to carry out this [Act] and may repeal rules, including rules and forms governing registration statements, applications, notice filings, reports, and other records;

(2) by rule, define terms, whether or not used in this [Act], but those definitions may not be inconsistent with this [Act]; and

(3) by rule, classify securities, persons, and transactions and adopt different requirements for different classes.

(b) **[Findings and cooperation.]** Under this [Act], a rule or form may not be adopted or amended, or an order issued or amended, unless the administrator finds that the rule, form, order, or amendment is necessary or appropriate in the public interest or for the protection of investors and is consistent with the purposes intended by this [Act]. In adopting, amending, and repealing rules and forms, Section 608 applies in order to achieve uniformity among the States and coordination with federal laws in the form and content of registration statements, applications, reports, and other records, including the adoption of uniform rules, forms, and

procedures.

(c) [**Financial statements.**] Subject to Section 15(h) of the Securities Exchange Act and Section 222 of the Investment Advisers Act of 1940, the administrator may require that a financial statement filed under this [Act] be prepared in accordance with generally accepted accounting principles in the United States and comply with other requirements specified by rule adopted or order issued under this [Act]. A rule adopted or order issued under this [Act] may establish:

(1) subject to Section 15(h) of the Securities Exchange Act and Section 222 of the Investment Advisers Act of 1940, the form and content of financial statements required under this [Act];

(2) whether unconsolidated financial statements must be filed; and

(3) whether required financial statements must be audited by an independent certified public accountant.

(d) [**Interpretative opinions.**] The administrator may provide interpretative opinions or issue determinations that the administrator will not institute a proceeding or an action under this [Act] against a specified person for engaging in a specified act, practice, or course of business if the determination is consistent with this [Act]. A rule adopted or order issued under this [Act] may establish a reasonable charge for interpretative opinions or determinations that the administrator will not institute an action or a proceeding under this [Act].

(e) [**Effect of compliance.**] A penalty under this [Act] may not be imposed for, and liability does not arise from conduct that is engaged in or omitted in good faith believing it conforms to a rule, form, or order of the administrator under this [Act].

(f) [**Presumption for public hearings.**] A hearing in an administrative proceeding under this [Act] must be conducted in public unless the administrator for good cause consistent with this [Act] determines that the hearing will not be so conducted.

Official Comments

Prior Provisions: 1956 Act Section 412; RUSA Sections 705, 707.

1. It is anticipated that the administrator will propose amendments or make rules under Section 605(a) to remain coordinate with relevant federal law, as well as appropriate rules of the National Association of Securities Dealers, and to achieve uniformity among the States.
2. Uniform forms such as Form B-D, U-4, U-5, and NF are today common in the securities industry and are authorized by Section 605(b).
3. Section 605(c) refers to generally accepted accounting principles in the United States which currently are promulgated by the Financial Accounting Standards Board and the Securities and Exchange Commission.
4. It is anticipated that the states will employ websites, e-mail or other electronic means to provide notice of proposed rulemaking or adoption of new rules, rule amendments, forms or form amendments, statements of policy or interpretations adopted by the administrator, and issuance of orders to registrants and others who have provided a current e-mail or similar address and expressed an interest in receiving such notice.
5. Section 605(e) does not apply to staff no action or interpretative opinions, but does apply to rules, forms, orders, statements of policy or interpretations adopted by the administrator.

SECTION 606. ADMINISTRATIVE FILES AND OPINIONS.

(a) **[Public register of filings.]** The administrator shall maintain, or designate a person to maintain, a register of applications for registration of securities; registration statements; notice filings; applications for registration of broker-dealers, agents, investment advisers, and investment adviser representatives; notice filings by federal covered investment advisers that are or have been effective under this [Act] or the predecessor act; notices of claims of exemption from registration or notice filing requirements contained in a record; orders issued under this [Act] or the predecessor act; and interpretative opinions or no action determinations issued under this [Act].

(b) **[Public availability.]** The administrator shall make all rules, forms, interpretative opinions, and orders available to the public.

(c) **[Copies of public records.]** The administrator shall furnish a copy of a record that is a public record or a certification that the public record does not exist to a person that so requests. A rule adopted under this [Act] may establish a reasonable charge for furnishing the record or certification. A copy of the record certified or a certificate by the administrator of a record's nonexistence is prima facie evidence of a record or its nonexistence.

Official Comments

Prior Provisions: 1956 Act Section 413; RUSA Section 709.

1. "Record" is defined in Section 102(25).
2. Compliance with a state records law will typically satisfy the requirements of Section 606(a).

SECTION 607. PUBLIC RECORDS; CONFIDENTIALITY.

(a) **[Presumption of public records.]** Except as otherwise provided in subsection (b), records obtained by the administrator or filed under this [Act], including a record contained in or filed with a registration statement, application, notice filing, or report, are public records and are available for public examination.

(b) **[Nonpublic records.]** The following records are not public records and are not available for public examination under subsection (a):

(1) a record obtained by the administrator in connection with an audit or inspection under Section 411(d) or an investigation under Section 602;

(2) a part of a record filed in connection with a registration statement under Sections 301 and 303 through 305 or a record under Section 411(d) that contains trade secrets or confidential information if the person filing the registration statement or report has asserted a claim of confidentiality or privilege that is authorized by law;

(3) a record that is not required to be provided to the administrator or filed under this [Act] and is provided to the administrator only on the condition that the record will not be subject to public examination or disclosure;

(4) a nonpublic record received from a person specified in Section 608(a); [and]

(5) any social security number, residential address, and residential telephone number contained in a record that is filed[; and

(6) a record obtained by the administrator through a designee of the administrator that a rule or order under this [Act] determines has been:

(A) expunged from the administrator's records by the designee; or

(B) determined to be nonpublic or nondisclosable by that designee if the

administrator finds the determination to be in the public interest and for the protection of investors].

(c) [**Administrator discretion to disclose.**] If disclosure is for the purpose of a civil, administrative, or criminal investigation, action, or proceeding or to a person specified in Section 608(a), the administrator may disclose a record obtained in connection with an audit or inspection under Section 411(d) or a record obtained in connection with an investigation under Section 602.

Official Comments

Prior Provisions: RUSA Section 703; SEC Rule Section 200.80(b)(4); Securities Exchange Act of 1934 Sections 24(d) and (e).

1. Section 607(a) reflects the extensive development of freedom of information and open records laws since the 1956 Act was adopted.

2. Section 607(b) may insulate from public disclosure records or other information that may be available under a state freedom of information or open records act. Unless the state freedom of information or open records act implements a constitutional provision, this Act as the later and more specific enactment should control as a matter of statutory construction. A state may amend its freedom of information act, open records act or this section to eliminate any inconsistencies.

3. Records and other information obtained by an administrator in connection with an audit or inspection under subsection 411(d) or an investigation under Section 602 may be made public in the enforcement action, even if records and other information would otherwise be subject to subsection 607(b)(1).

4. An administrator may orally disclose information under Section 607(c) to a person specified in Section 608(a) for the purposes specified in Section 607(c).

SECTION 608. UNIFORMITY AND COOPERATION WITH OTHER AGENCIES.

(a) **[Objective of uniformity.]** The administrator shall, in its discretion, cooperate, coordinate, consult, and, subject to Section 607, share records and information with the securities regulator of another State, Canada, a Canadian province or territory, a foreign jurisdiction, the Securities and Exchange Commission, the United States Department of Justice, the Commodity Futures Trading Commission, the Federal Trade Commission, the Securities Investor Protection Corporation, a self-regulatory organization, a national or international organization of securities regulators, a federal or state banking and insurance regulator, and a governmental law enforcement agency to effectuate greater uniformity in securities matters among the federal government, self-regulatory organizations, States, and foreign governments.

(b) **[Policies to consider.]** In cooperating, coordinating, consulting, and sharing records and information under this section and in acting by rule, order, or waiver under this [Act], the administrator shall, in its discretion, take into consideration in carrying out the public interest the following general policies:

- (1) maximizing effectiveness of regulation for the protection of investors;
- (2) maximizing uniformity in federal and state regulatory standards; and
- (3) minimizing burdens on the business of capital formation, without adversely affecting essentials of investor protection.

(c) **[Subjects for cooperation.]** The cooperation, coordination, consultation, and sharing of records and information authorized by this section includes:

- (1) establishing or employing one or more designees as a central depository for registration and notice filings under this [Act] and for records required or allowed to be maintained under this [Act];
- (2) developing and maintaining uniform forms;

- (3) conducting a joint examination or investigation;
- (4) holding a joint administrative hearing;
- (5) instituting and prosecuting a joint civil or administrative proceeding;
- (6) sharing and exchanging personnel;
- (7) coordinating registrations under Sections 301 and 401 through 404 and exemptions under Section 203;
- (8) sharing and exchanging records, subject to Section 607;
- (9) formulating rules, statements of policy, guidelines, forms, and interpretative opinions and releases;
- (10) formulating common systems and procedures;
- (11) notifying the public of proposed rules, forms, statements of policy, and guidelines;
- (12) attending conferences and other meetings among securities regulators, which may include representatives of governmental and private sector organizations involved in capital formation, deemed necessary or appropriate to promote or achieve uniformity; and
- (13) developing and maintaining a uniform exemption from registration for small issuers, and taking other steps to reduce the burden of raising investment capital by small businesses.

Official Comments

Prior Provisions: 1956 Act Section 415; RUSA Sections 704 and 803; 19(c) of the Securities Act of 1933.

1. Uniformity of regulation among the states and coordination with the Securities and Exchange Commission is a principal objective of this Act. Section 608 is intended to encourage such cooperation to the maximum extent appropriate. Operative phrases such as "shall, in its discretion" in Sections 608(a) and (b) are intended to be precisely coordinate with the directive

that Congress gave to the Securities and Exchange Commission in Section 19(c) of the Securities Act of 1933.

2. The goals of uniformity among the states and coordination with related federal regulation, including self regulatory organizations, may be enhanced by greater use of information technology systems such as the Web-CRD, the Investment Adviser Registration Depository (IARD), or the Securities and Exchange Commission Electronic Data Gathering, Analysis and Retrieval System (EDGAR). These types of techniques are consistent with a potential system of "one stop filing" of all federal and state forms that is encouraged by this Act.

3. This Act is intended, to the extent practicable, to be revenue neutral in its impact on existing state laws.

4. Section 608(c) lists some joint or coordinated efforts which might be undertaken. Other appropriate cooperative activities are also encouraged.

5. Court decisions interpreting the securities laws have construed these acts to achieve "broad protection to investors," a remedial approach that "embodies a flexible rather than a static principle, one that is capable of adaption to meet the countless and variable schemes devised by those who seek to use the money of others on the promise of profits." SEC v. W.J. Howey Co, 328 U.S. 293, 299, 301 (1946).

SECTION 609. JUDICIAL REVIEW.

(a) **[Judicial review of orders.]** A final order issued by the administrator under this [Act] is subject to judicial review in accordance with [the state administrative procedure act].

[(b) **[Judicial review of rules.]** A rule adopted under this [Act] is subject to judicial review in accordance with [the state administrative procedure act].]

Official Comments

Prior Provisions: 1956 Act Section 411; RUSA Section 711(b).

1. The 1956 Act Section 411 specified procedures for judicial review of orders, in part modeled on Section 12 of the Model Administrative Procedure Act, 54 Handbook of National Conference of Commissioners on Uniform State Laws 334 (1944) and partly on Section 25 of the Securities Exchange Act.

2. A rule adopted under this Act may be subject to judicial review in accordance with the

state administrative procedure act.

3. In those states in which judicial review of rules is permitted, a state may choose to add Section 609(b). In those states in which judicial review of rules is not permitted, Section 609(b) should be deleted.

SECTION 610. JURISDICTION.

(a) [**Sales and offers to sell.**] Sections 301, 302, 401(a), 402(a), 403(a), 404(a), 501, 506, 509, and 510 do not apply to a person that sells or offers to sell a security unless the offer to sell or the sale is made in this State or the offer to purchase or the purchase is made and accepted in this State.

(b) [**Purchases and offers to purchase.**] Sections 401(a), 402(a), 403(a), 404(a), 501, 506, 509, and 510 do not apply to a person that purchases or offers to purchase a security unless the offer to purchase or the purchase is made in this State or the offer to sell or the sale is made and accepted in this State.

(c) [**Offers in this State.**] For the purpose of this section, an offer to sell or to purchase a security is made in this State, whether or not either party is then present in this State, if the offer:

(1) originates from within this State; or

(2) is directed by the offeror to a place in this State and received at the place to which it is directed.

(d) [**Acceptances in this State.**] For the purpose of this section, an offer to purchase or to sell is accepted in this State, whether or not either party is then present in this State, if the acceptance:

(1) is communicated to the offeror in this State and the offeree reasonably believes

the offeror to be present in this State and the acceptance is received at the place in this State to which it is directed; and

(2) has not previously been communicated to the offeror, orally or in a record, outside this State.

(e) **[Publications, radio, television, or electronic communications.]** An offer to sell or to purchase is not made in this State when a publisher circulates or there is circulated on the publisher's behalf in this State a bona fide newspaper or other publication of general, regular, and paid circulation that is not published in this State, or that is published in this State but has had more than two thirds of its circulation outside this State during the previous 12 months or when a radio or television program or other electronic communication originating outside this State is received in this State. A radio or television program, or other electronic communication is considered as having originated in this State if either the broadcast studio or the originating source of transmission is located in this State, unless:

(1) the program or communication is syndicated and distributed from outside this State for redistribution to the general public in this State;

(2) the program or communication is supplied by a radio, television, or other electronic network with the electronic signal originating from outside this State for redistribution to the general public in this State;

(3) the program or communication is an electronic communication that originates outside this State and is captured for redistribution to the general public in this State by a community antenna or cable, radio, cable television, or other electronic system; or

(4) the program or communication consists of an electronic communication that originates in this State, but which is not intended for distribution to the general public in this

State.

(f) **[Investment advice and misrepresentations.]** Sections 403(a), 404(a), 405(a), 502, 505, and 506 apply to a person if the person engages in an act, practice, or course of business instrumental in effecting prohibited or actionable conduct in this State, whether or not either party is then present in this State.

Official Comments

Source of Law: 1956 Act Section 414; RUSA Section 801.

1. Section 610 defines the application of the Act to interstate or international transactions when only some of the elements of a violation occur in this State. This Section applies to all types of proceedings specified by the Act – administrative, civil, and criminal. The law is now settled that a person may violate the law of a particular state without ever being within the state or performing each act necessary to violate the law within that state.

2. Section 610 generally follows Section 414 of the 1956 Act, but has been modernized to reflect the development of the Internet and other electronic communications after 1956.

3. Section 610 can be illustrated in the context of a civil action under Section 509(b) by a purchaser in State A against a seller in State B:

Section 610(a) would apply when an “offer to sell is made in this State.”

Section 610(c) provides that an offer which originates in State B and is directed to State A is made in both states. The securities act of State A would apply under Section 610(c)(2). The act of State B would apply also, under Section 610(c)(1). The intent is to prevent a seller in State B from using that state as a base of operations for defrauding person in other states.

Section 610(e) addresses offers made through publications, radio, television, or electronic communications. The subsection provides a series of safe harbors for advertisements in newspapers, magazines, radio, television, or electronic media that either originate outside State A or that originate in State A but are directed outside the state to the general public. With respect to bona fide newspapers or other publications of general, regular, and paid circulation, the safe harbor requires that more than two thirds of its circulation be outside State A. With respect to radio, television, or other electronic communications, safe harbors are specified in Sections 610(e)(1) through (4).

Section 610(d), however, provides that a person in State A who makes an offer to purchase as a result of communication described in Section 610(e) may cause the act to be

applicable if the offeror accepts the offer "in this State." Section 610(d) defines when an offer is accepted "in this State."

If a selling broker-dealer in State B solely sends a confirmation into State A, or the purchaser in State A sends a check from within State A, the act will not apply unless, under Section 610(d), the confirmation or delivery constitutes the seller's acceptance of the purchaser's offer to buy in State A.

The applicability of the act to purchaser is addressed by Section 610(b) which is the converse of Section 610(a). Under Section 509(c) there can be liability of purchasers to sellers.

Section 610(f) is a new provision that specifies jurisdictions in cases involving investment advice and misrepresentations.

4. Under subsection 202(20) certain out-of-state offers or sales are exempt from securities registration.

5. The phrase "other electronic means" is coextensive with computer or other information technology permitted by subsections 102(8), 102(25).

6. Under Section 610 the administrator may adopt interpretative rules or orders to specify when particular uses of new electronic communications, including the Internet, involve an offer to sell or to purchase a security, acceptance of an order to purchase or sell a security, or an act or practice involving prohibited conduct, within a State, whether or not a purchaser, seller, or other party is then present in the State. The NASAA Interpretive Order Concerning Broker-Dealers, Agents, and Investment Adviser Representatives Using the Internet for General Dissemination of Information for Products and Services (Apr. 23, 1997) is an illustration of an interpretative order that would be in compliance with the administrator's authority under Section 610. Under this Order, broker-dealers, agents, investment advisers, and investment adviser representatives who distribute information on available products and services through communications on the Internet generally to anyone having access to the Internet such as postings on a bulletin board or home page shall not be deemed to be transacting business in a State if specified conditions are satisfied including a legend clearly stating that the broker-dealer, agent, investment adviser, or investment adviser representative may transact business in that State only if first registered, excluded or exempted from applicable registration requirements.

SECTION 611. SERVICE OF PROCESS.

(a) [**Signed consent to service of process.**] A consent to service of process complying with Section 611 required by this [Act] must be signed and filed in the form required by a rule or order under this [Act]. A consent appointing the administrator the person's agent for service

of process in a noncriminal action or proceeding against the person, or the person's successor or personal representative under this [Act] or a rule adopted or order issued under this [Act] after the consent is filed, has the same force and validity as if the service were made personally on the person filing the consent. A person that has filed a consent complying with this subsection in connection with a previous application for registration or notice filing need not file an additional consent.

(b) [**Conduct constituting appointment of agent for service.**] If a person, including a nonresident of this State, engages in an act, practice, or course of business prohibited or made actionable by this [Act] or a rule adopted or order issued under this [Act] and the person has not filed a consent to service of process under subsection (a), the act, practice, or course of business constitutes the appointment of the administrator as the person's agent for service of process in a noncriminal action or proceeding against the person or the person's successor or personal representative.

(c) [**Procedure for service of process.**] Service under subsection (a) or (b) may be made by providing a copy of the process to the office of the administrator, but it is not effective unless:

(1) the plaintiff, which may be the administrator, promptly sends notice of the service and a copy of the process, return receipt requested, to the defendant or respondent at the address set forth in the consent to service of process or, if a consent to service of process has not been filed, at the last known address, or takes other reasonable steps to give notice; and

(2) the plaintiff files an affidavit of compliance with this subsection in the action or proceeding on or before the return day of the process, if any, or within the time that the court, or the administrator in a proceeding before the administrator, allows.

(d) [Service in administrative proceedings or civil actions by administrator.]

Service pursuant to subsection (c) may be used in a proceeding before the administrator or by the administrator in a civil action in which the administrator is the moving party.

(e) [Opportunity to defend.] If process is served under subsection (c), the court, or the administrator in a proceeding before the administrator, shall order continuances as are necessary or appropriate to afford the defendant or respondent reasonable opportunity to defend.

Official Comments

Prior Provisions: 1956 Act Sections 414(g) and (h); RUSA Section 708.

1. Section 611 follows the 1956 Act and RUSA in providing for a signed consent to service of process in Section 611(a); a substituted service of process in Section 611(b); and process and opportunity to defend in Sections 611(c) through (e).

2. An issuer is not required to file a consent to service of process unless it proposes to offer a security in this State through someone acting on an agency basis. Since the civil liability provisions of Section 509(b) apply only in a suit by a purchaser against a seller, the issuer in a firm commitment underwriting is civilly liable only to the underwriter, who, in turn, may be liable to the dealer, who, in turn, may be liable to the purchaser. In contrast, in a best efforts underwriting, when the security is sold on an agency basis and title passes directly to the purchaser, the issuer can be liable to the purchaser.

3. Section 611(b) generally follows Section 414(h) of the 1956 Act and Section 708(c) of RUSA. The intent is to provide for substituted service of process when a seller in one state directs an offer into a second state either in violation of the laws of the second state or fraudulently. Under Section 611(b) the purchaser may sue the seller in the purchaser's state and then bring an action on the judgment in the seller's state. The constitutionality of this type of statute has long been sustained.

4. This section was originally based on the type of nonresident motorist statute whose constitutionality was sustained in *Hess v. Pawlowski*, 274 U.S. 352 (1927) and subsequently in other contexts. See, e.g., *International Shoe Co. v. State of Wash.*, 326 U.S. 310 (1945); *Travelers Health Ass'n v. Commonwealth of Va.*, 339 U.S. 643 (1950).

SECTION 612. SEVERABILITY CLAUSE. If any provision of this [Act] or its

application to any person or circumstances is held invalid, the invalidity does not affect other provisions or applications of this [Act] that can be given effect without the invalid provision or application, and to this end the provisions of this [Act] are severable.

Official Comments

Prior Provisions: 1956 Act Section 417; RUSA Section 805.

[ARTICLE] 7

TRANSITION

SECTION 701. EFFECTIVE DATE. This [Act] takes effect on [insert date, which should be at least 60 days after enactment].

SECTION 702. REPEALS. The following act is repealed:

[Insert name of former State securities act].

SECTION 703. APPLICATION OF ACT TO EXISTING PROCEEDING AND EXISTING RIGHTS AND DUTIES.

(a) **[Applicability of predecessor act to pending proceedings and existing rights.]** The predecessor act exclusively governs all actions or proceedings that are pending on the effective date of this [Act] or may be instituted on the basis of conduct occurring before the effective date of this [Act], but a civil action may not be maintained to enforce any liability under the predecessor act unless instituted within any period of limitation that applied when the cause of action accrued or within five years after the effective date of this [Act], whichever is earlier.

(b) **[Continued effectiveness under predecessor act.]** All effective registrations under the predecessor act, all administrative orders relating to the registrations, rules, statements of policy, interpretative opinions, declaratory rulings, no action determinations, and conditions imposed on the registrations under the predecessor act remain in effect while they would have remained in effect if this [Act] had not been enacted. They are considered to have been filed, issued, or imposed under this [Act], but are exclusively governed by the predecessor act.

(c) **[Applicability of predecessor act to offers or sales.]** The predecessor act exclusively applies to an offer or sale made within one year after the effective date of this [Act] pursuant to an offering made in good faith before the effective date of this [Act] on the basis of an exemption available under the predecessor act.

Official Comments

Prior Provisions: 1956 Act Section 418; RUSA Section 807.

Prior law governs all suits, actions, prosecutions, or proceedings which are pending or may be initiated on the basis of facts or circumstances occurring before the effective date of a State blue sky statute. See *Hilton v. Mumaw*, 522 F.2d 588, 600 (9th Cir. 1975).