PROTECTING THE SMALL INVESTOR: COMBATING TRANSNATIONAL RETAIL SECURITIES AND FUTURES FRAUD

INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS

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INTRODUCTION

With the proliferation of modern telecommunication facilities and the internationalization of financial markets and transactions in recent years, regulators face growing challenges in combating transnational retail securities and futures fraud. Boiler rooms (1) increasingly are operating from jurisdictions apart from those where their customers are located ("*target jurisdictions*") (2). Other boiler rooms are establishing operations in multiple jurisdictions, while some employ mail drops, mail and telephone forwarding services or shell corporations in jurisdictions outside the target country to conceal their identities, create false impressions of substantial operations, or otherwise obfuscate their activities (3). In enforcement cases involving transnational boiler room fraud, authorities in target jurisdictions increasingly need and are seeking assistance from foreign regulators.

Regulators also increasingly need the cooperation of foreign regulatory and enforcement authorities in the investigation and prosecution of domestic boiler rooms. For example, even where a boiler room is soliciting customers solely within a particular jurisdiction, it may be offering investments in financial instruments registered or traded in another jurisdiction. It also may divert funds obtained from customers to accounts in other jurisdictions, or be owned or controlled by principals located abroad. In such cases, regulators often must contact their foreign counterparts for assistance in gathering information and evidence abroad.

Part I of the report considers various types of problems and challenges regulators face in the investigation and prosecution of transnational boiler room fraud. Part II reviews various domestic measures countries have adopted to protect customers from boiler room fraud while Part III explores the role of international cooperation in combatting transnational boiler room fraud. Finally, the report identifies additional measures that may assist regulators in their efforts to combat transnational retail securities and futures fraud.

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(1) - In this report, the term "*boiler room*" refers to an enterprise, typically, though not necessarily, unregistered that uses high pressures sales tacticts to solicit unsophiticated customers to invest in securities, futures or option instruments. The sales tactics vary from case to case, but generally involve fraudulent promises of quick and large profits through investments in instruments that are not traded on recognized exchanges, or lack demonstrable indicia of actual value.

(2) - Boiler rooms located outside a target jurisdiction are referred to herein as "*foreign boiler rooms*". The terms "*transnational*" and "*multi-jurisdictional*" also are used in connection with boiler room activities discussed herein, and focus, respectively, on the cross-border aspects of boiler rooms (whether foreign or domestic) and the location or operation of boiler rooms in more than two jurisdictions.

(3) - Of course, many bona fide firms have complex transnational corporate structures. The existence of such a structure is not, in itself, evidence of a fraudulent operation.

I - PROBLEMS AND CHALLENGES FOR REGULATORS IN COMBATING TRANSNATIONAL BOILER ROOM FRAUD

In studying the characteristics of and problems created by transnational boiler room operations, the Working Group has identified a number of challenges that these operations pose to regulators. These include : difficulties in detecting and gathering evidence about the operations of foreign boiler rooms ; concealment of principals of multijurisdictional boiler rooms ; avoidance and evasion of regulation ; use of mail and telephone forwarding services ; dealing in unregulated or fictitious instruments ; boiler room sales techniques and fraudulent misrepresentations ; concealment and expatriation of customer funds ; and recidivist boiler room principals.

A - Difficulties in Detecting And Gathering Evidence About The Operations Of Foreign Boiler Rooms

The division of illegal activities among several countries may make the activities of a foreign boiler room more difficult to detect, particularly since, from a purely domestic point of view, parts of the scheme may appear, or even may be, legal. Thus, for example, a boiler room may settle in a country that does not require authorization and promote products in another country that does not impose restrictions on the type of products that can be offered. In these circumstances, it may be more difficult for the regulators in both jurisdictions to discover the activities of the boiler room. In addition, boiler rooms operating from unregulated jurisdictions may promote financial instruments in regulated jurisdictions, anticipating that a sales campaign can be completed successfully before the regulators become aware of the fraud.

The foreign boiler room also can create formidable factual and evidentiary problems for the regulator in the jurisdiction where the boiler room's intended victims are located. Sheer geographic separation of the regulator from the boiler room may make it quite difficult for the regulator to obtain detailed information about the actual operations of a foreign boiler room. The regulator generally will be unable to exercise its investigative powers to visit, conduct surveillance or otherwise directly examine the foreign location. In the absence of information from the foreign jurisdiction, the local regulator may have to rely upon information and records provided by customers in its territory. This makes it more difficult to assess the size of the boiler room operation, to obtain documentary evidence of the transactions purportedly engaged in by the firm, or to uncover the internal structure and day-to-day management of the firm.

B - Concealment Of Principals of Multijurisdictional Boiler Rooms

Identification of the principals of a multijurisdictional boiler room also can be challenging to a regulator. Sophisticated boiler room principals often avoid direct participation in solicitation of customers, and also may remove themselves from direct involvement in the office through use of managers and employees who may not know the identity or the full scope and nature of the activities of the principals. Furthermore, beneficiaries of these schemes often form their companies as affiliates or subsidiaries of shell corporations located or incorporated in jurisdictions separate from those where operations are actually handled. These shell corporations are often located in jurisdictions where information about the entities and their true principals is not maintained, or, if maintained, may not be made available to regulators because of stringent secrecy requirements. In addition, foreign principals of boiler rooms further conceal their ownership of such shell corporations through use of nominee shareholders, including lawyers, accountants and management companies.

C - Avoidance And Evasion Of Regulation

As discussed below, boiler rooms may target customers in regulated jurisdictions from bases of operation located in unregulated or lightly regulated jurisdictions. They may also evade or exploit registration requirements in jurisdictions with existing securities and futures laws.

1 - Establishing Boiler Room Operations In Unregulated Jurisdictions

Boiler room operators often seek to locate in jurisdictions that have no licensing or other regulatory requirements governing their operations. In this way, they can conduct various types of fraudulent activity, such as marketing misrepresentations and price and market manipulation, with little fear of meaningful oversight or prompt prosecution. Once established in unregulated jurisdictions, these boiler rooms often will target customers located in jurisdictions where securities and futures trading are highly regulated. In many cases, the fraud perpetrated by boiler room operators located in unregulated jurisdictions may not be investigated by the authority in the regulated jurisdiction until a significant number of investors have been defrauded, and complaints have been sent to the regulator, by which time the boiler room may have ceased operations or relocated to a different jurisdiction.

In order to reduce the likelihood of legal action against them in the jurisdictions where they are located, boiler rooms often avoid soliciting local investors. The boiler room operators may assume that the local authority will be less interested in halting the fraud if its residents are not affected. In addition, the local authority may encounter jurisdictional limits on its ability to respond. As a result, the regulatory authority in the target jurisdiction may have difficulties obtaining information from its regulatory counterpart, if any, in the jurisdiction from which the boiler room operations are being conducted.

2 - Establishing Boiler Room Operations In Lightly Regulated Jurisdictions

Securities and futures transactions are only lightly regulated in some jurisdictions due to lack of comprehensive or effective statutes, regulations or sanctions, or to lack of resources for carrying out regulatory and enforcement programs. Such regulation may give the investing public the impression that effective regulations and recourse to regulators exist, when, in fact, protection against boiler room fraud is insufficient.

3 - Evading Registration In Regulated Jurisdictions

Another typical operating method of boiler rooms is to locate in regulated jurisdictions but evade regulation by failing to register with, or obtain a license from, the appropriate regulator. Often such a boiler room attempts to create the impression of legitimacy through false or misleading representations to customers concerning its authorized status, or through the use of a corporate name or logo that appears official or legitimate. When unregistered boiler rooms operate in regulated jurisdictions, they usually are ready to close shop and move locations immediately upon receiving substantial funds from investors or upon detection by a regulatory or criminal agency. By operating in this manner, unregistered boiler rooms may be able to perpetrate a significant fraud without easily being located or traced.

4 - Exploitation of Registration In Regulated Jurisdictions

In yet another operating method, boiler room operators will locate in regulated jurisdictions and will register with the appropriate agency or obtain a license to do business. Then the boiler room will engage in high pressure sales campaigns to unsophisticated investors, using the registration status or license to create an appearance of legitimacy to prospective customers. As noted above with unregistered entities, these registered or licensed boiler rooms, which in the registration process may appear the same as legitimate businesses, may be able to accumulate large sums of money from unsuspecting investors, and quickly move or dissolve their businesses and form new ones under different names, including in the same jurisdiction, before they are detected by regulators.

D - Use of Mail Drop And of Mail And Telephone Forwarding Services

Another fairly common problem is the use by boiler rooms in one jurisdiction of mail drop or mail and telephone forwarding services located in another jurisdiction to facilitate fraudulent schemes. For example, a boiler room operation located in jurisdiction A may offer investments in securities or derivative instruments traded in jurisdiction B (often a jurisdiction with fully developed markets and regulatory structures) to customers in jurisdiction C. To enhance its credibility, the company will include in its solicitation materials references to its offices or headquarters in jurisdiction B. The jurisdiction B "office" may even have a name that is intentionally similar to a well-known registered or authorized financial institution in jurisdiction B. Unknown to the customers in the target jurisdiction, the address in jurisdiction B is a mail drop or telephone forwarding service, simply relaying phone messages and mail for the boiler room, back to jurisdiction A, or even to yet another jurisdiction.

In many cases the mail drop or mail and telephone forwarding services may be unaware of the nature of the business they are facilitating. In the absence of knowing participation by such firms in the fraudulent scheme, or conduct by them otherwise requiring authorization or registration by the local securities or futures regulatory authority, that authority may have difficulty taking effective action against the continued operation of mail drop or mail and telephone forwarding services for such schemes.

E - Dealing In Unregulated Or Fictitious Instruments

One of the tactics used by boiler rooms is the promotion of financial instruments whose worth, if any, cannot be calculated or verified independently. Although the types of instruments may vary, they often represent corporations, entities, or goods that actually do not exist or that exist only in shell form, without value, assets, or bona fide business use or prospects. Boiler room operators often work in concert with promoters of these fictitious or valueless goods and entities, and are aware that the worth of the goods or entities underlying the instruments has not been independently verified or audited. In the case of penny stocks (4) for example, boiler room operators often capitalize on the low value of the instruments, by telling prospective investors that they can be purchased for mere pennies per share (when in truth the stock may be worth nothing) while at the same time fraudulently misrepresenting that their value will increase dramatically.

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(4) - "Penny stocks" generally are low-priced equity securities traded in markets in which there is little current or accurate information about trading, pricing, or the security itself. Penny stocks are generally high-risk investments, often because the issuer may have few or no assets or legitimate business purpose or prospects.

F - Boiler Room Sales Techniques And Fraudulent Misrepresentations

One common characteristic of boiler room operators is the use of "*cold calling.*" Cold calling is a telemarketing tool that involves the making of unsolicited telephone calls to potential customers to sell a product, such as a financial instrument. Names of the persons to be called usually are obtained from telephone directories or from commercially available lists maintained by various organizations. Thus, for example, in a jurisdiction undergoing privatization of government owned companies, there may be lists of investors with relatively little experience in futures or securities investments which become available to a boiler room through a link with a registered entity. By obtaining customer lists, boiler room operators may be able to target specific types of especially vulnerable customers, based on such factors as age, occupation, location, household income, and previous investment history.

In making cold calls, particularly to a targeted group, boiler room operators usually employ high-pressure sales tactics designed to intimidate prospective customers or to appeal to their desire to avoid taxation or make money quickly. They often rely on prepared scripts that employ psychological tools to expose weaknesses in customers or to lull them into parting with their money. Occasionally, using this technique, boiler room operators will attempt to establish a friendly relationship during an initial call to a customer. Then, after one or two more calls, they will solicit the customer to make an investment.

The problem posed by boiler rooms, however, is not simply that they employ high-pressure sales techniques. In fact, boiler room operators typically combine these telemarketing techniques with fraudulent misrepresentations about the nature of the instrument being sold, the company issuing the instrument, the instrument's worth, or the prospects for its success in the secondary markets. For example, the boiler room may set up a series of pre-arranged trades between related parties resulting in a significant short term rise in the price of a company's shares. To bolster the impression of success, the boiler room will issue false or misleading statements overstating the financial situation of the firm. Meanwhile, boiler room principals and insiders will sell as many of their shares as possible to unsuspecting investors using high pressure sales techniques. At some point the manipulation can no longer be maintained, and the boiler room will withdraw from the market, causing the price of the stock to collapse.

During the early part of the scheme, a boiler room often will seek to avoid arousing suspicion on the part of potential customers. To that end, the boiler room may provide false or misleading account statements to customers, thereby leading them to believe that substantial profits have been earned. On occasion, in furtherance of the fraud, these "profits" may even be paid to the customer. Similarly, in some cases, if a customer asks to withdraw his money, the boiler room may comply with the request, using money provided by new investors. Such payments to a few customers early on may permit the boiler room to avoid the risk of early detection of fraud and provide the opportunity to increase the amount of funds taken in by the boiler room from customers.

Boiler rooms also attempt to convey an impression of respectability by using bona fide intermediaries and investment instruments. For example, stock promoted by a boiler room sometimes actually is traded in organized markets, with real orders to buy and sell transmitted through established brokers. In this way, the boiler room may achieve a certain credibility, even without the knowledge of the bona fide intermediaries. Similarly, a boiler room may be promoting a stock through fraudulent means without the knowledge or involvement of the issuer of the stock.

Using these and other techniques, boiler rooms prey on the lack of financial sophistication about the securities and futures markets on the part of the individuals they solicit. As a result, unsuspecting customers often invest substantial sums, even life savings, in worthless instruments, only to suffer a total loss of their investment.

G - Concealment And Expatriation Of Customer Funds

From the perspective of defrauded customers of boiler rooms, the most meaningful outcome is the return of their funds. A securities or futures regulator, however, may face formidable obstacles in attempting to obtain control of assets that have been moved by defendants to locations outside the regulator's jurisdiction. The ease and speed of international financial transactions provide ready avenues for boiler room operators to remove assets from the control of local regulatory authorities and courts. Moreover, the proliferation and convenience of certain international financial centers have made them attractive places to store funds, or through which to channel funds destined for other locations. Ordinary compulsory powers that may be available to a regulatory authority within its own jurisdiction, such as asset freezes and injunctions, generally are ineffective in immobilizing assets located abroad.

In addition, boiler room operators may move funds through institutions in a number of jurisdictions before permitting them to come to rest in a foreign or even a domestic financial institution. Boiler room operators also may hold the funds in multiple accounts, often in the names of aliases or third parties. Regulators may face difficult challenges in attempting to track assets as they move from one jurisdiction to the next. Sometimes the "paper trail" is incomplete or nonexistent. Certain means of transferring funds, for example, may generate insufficient documentation to enable regulators to reconstruct the movement of funds. In some instances, inflexible secrecy laws can add to the difficulties regulators face in tracing and recapturing customer funds diverted by boiler rooms.

H - Recidivist Boiler Room Principals

When a regulator initiates an investigation of a suspected boiler room, consultation with other regulators frequently reveals that the principals already have been involved in schemes in other jurisdictions that resulted in regulatory or criminal investigations or actions. This occurs in part because boiler rooms are often very mobile. They may be limited in size to just a few individuals, equipped with telephones and some mailing lists or other customer directories. In other cases, offices may be scattered among a number of jurisdictions. Once a small-scale boiler room, or part of a multijurisdictional boiler room, is closed down in one jurisdiction, the individuals behind the defunct operation may simply relocate and continue their operations.

Just as international transactions have become easier and faster, so has the ability to travel around the globe. Recidivist boiler room principals, therefore, can be extremely mobile. In addition, boiler room principals frequently use multiple identities or aliases and may possess numerous illegal passports, enabling them to travel without arousing suspicion. Foreign boiler room operators, thus, are often able to evade regulators by moving quickly and quietly from jurisdiction to jurisdiction.

II - REGULATORY RESPONSES TO TRANSNATIONAL RETAIL SECURITIES AND FUTURES FRAUD

The Working Party's study of transnational retail securities and futures fraud included a review of both general regulatory structures and specific measures that have proven effective in combatting boiler rooms. These domestic measures are important not only for market integrity and investor confidence, but also because they provide a solid basis for effective international cooperation for enforcement purposes. Such cooperation is essential to deter the spread of boiler room fraud from one jurisdiction to another, and to permit the effective investigation and prosecution of transnational boiler room operations. The purpose of this section is to describe the types of provisions that one or more jurisdictions have found to be the most appropriate regulatory responses to boiler room fraud. It is not meant to be directing but only to list the measures which could be contemplated by each regulatory authority within the scope of its specific domestic statutory framework.

A - Promoting Regulatory Structures That Discourage Boiler Rooms

Generally, countries do not adopt regulatory provisions merely to prevent boiler room operations. Nonetheless, such requirements are useful for combatting boiler room fraud by those who do business in the futures or securities markets.

1 - Registration Of Intermediaries And Professionals

The primary purposes of registration are to ensure that applicants satisfy the requirements for operating as securities and futures intermediaries and professionals and to identify those organizations and individuals whose activities are subject to review by the governmental regulator and applicable self-regulatory organizations ("*SROs*") (5). Regulatory schemes also usually specify certain circumstances which trigger disqualifications from registration, including many that are based on prior proceedings in which the applicant was found to have violated the law or in which the applicant was enjoined from engaging in certain activities. SROs generally perform extensive background checks to determine whether cause for disqualification exists. More recently, given the increasing internationalization of financial markets, some jurisdictions have extended background checks to include vetting of the names of foreign principals of applicants with foreign regulatory and criminal authorities. Registered firms, moreover, generally are subject to ongoing monitoring by regulators or SROs (e.g. periodic submission of reports, regular inspection of registrants), which is helpful in detecting and deterring use of boiler room tactics by registrants.

2 - Regulation Of Products And Markets

Many member countries have found that regulation of aspects of the offer and sale of securities and futures products may be useful in protecting customers from boiler room fraud. Thus, for example, most members have statutes providing for registration with the competent regulatory authority for securities that are offered to the public. Among other things, this provides potential customers with a source of information about the offered securities other than the firms that are soliciting investment in the securities. In addition, some jurisdictions conduct reviews concerning disclosure about or the merits of the product, or may limit the offer of specific types of products to unsophisticated investors.

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(5) - The term "*self-regulatory organization*" refers to a non-governmental body, often, but not necessarily, a membership organization, that has regulatory, supervisory and disciplinary responsibility for securities or futures intermediaries and professionals, and may act on authority delegated by a governmental body.

Some member countries also regulate the offer and sale of foreign securities and futures products within their territories. Thus, for example, some jurisdictions have published lists of foreign exchanges with respect to which authorized intermediaries are permitted to solicit the public and limit or prohibit the offer and sale of foreign products not traded on exchanges included in such lists. Others have employed special risk disclosure requirements for dealings by their authorized firms in foreign transactions for customers, again, with some variations arising depending upon the type of customer involved. Several member countries use listing standards as a means of excluding risky or fraudulent securities, which can aid in protecting investors against boiler room-type fraud. In addition, some jurisdictions provide rescission rights and private rights of action to help investors avoid losses in cases of fraud. Several Working Party members also have made arrangements with foreign counterparts to permit authorized foreign intermediaries to offer and sell foreign futures or securities to customers in the members' home jurisdictions.

3 - Disclosure Of Information

Some jurisdictions have adopted legislation or regulations requiring disclosure of pre-trade or post-trade market information, such as firm quotations and price and volume information ; anticipated revenue and profits ; and disclosures relating to liquidity or sole market-maker status. Some jurisdictions also require distribution of a monthly account statement detailing activity in a customer's account and providing the estimated market value of the investment at the time of the statement. Such requirements can have the effect of discouraging, or slowing the pace of, boiler room operators.

Some countries have adopted laws and regulations geared towards providing differing levels of regulatory protection to different classes of investors. Such differential regulation recognizes distinctions between inexperienced individual investors and sophisticated institutional investors, with many gradations and variations in between. The effect of being included in different classes of investors may involve, for example, variations in the types of disclosures required to be made to such persons. Thus, retail investors, who are more susceptible to boiler room fraud, may receive more detailed disclosures, with a view to assisting them in avoiding fraudulent investment schemes.

4 - Enforcement Options

Various requirements mentioned above provide an important source of information to prospective customers about securities and futures professionals, and may restrict or prohibit certain intermediaries or individuals from engaging in securities and futures business. They are not, however, sufficient to eliminate boiler room fraud, because the perpetrators of retail securities and futures fraud often are prepared to operate in defiance of statutory and regulatory requirements. For this reason, regulatory authorities generally have a number of enforcement options available to them to fight boiler room fraud.

a - Domestic Enforcement Powers

Many regulatory authorities have the power to conduct investigations and commence administrative or civil proceedings leading to the imposition of a variety of sanctions including fines, limitations on activities, suspensions or revocations of registration, orders to refrain from future violations or to take specified actions, orders to comply with the law, and orders to disgorge profits illegally obtained or provide restitution to wronged customers.
In some jurisdictions, a regulatory authority may seek ex-parte emergency relief, i.e., temporary measures taken without prior notice to the prospective defendant. Such measures may include freezes of the assets of the boiler room and its principals and temporary restraining orders

preventing the destruction of documents and directing the operators to cease violating relevant provisions of law. Given the ease and speed with which skilled boiler room operators can remove and conceal assets and shutter offices, these emergency measures have been invaluable tools to those authorities that possess them.

In some countries, victims of the fraud may commence civil actions seeking remedies or sanctions for fraud. SROs also may impose disciplinary sanctions on their members who fail to comply with applicable rules. Sanctions may include a reprimand, expulsion of a member, suspension of the rights and privileges of a member, fine, temporary or permanent bar from all or some activities, or directive to other members to refuse to do business with the wrongdoer.

b - Prioritizing The Fight Against Boiler Room Fraud

Another approach taken by some members of the Technical Committee has been to make the investigation and prosecution of boiler room fraud an explicit priority. Task forces have been established to focus on the issues and to propose changes in law and regulations to address the boiler room problem. In those jurisdictions where the regulators have devoted resources and efforts to the problem, a noticeable decrease in boiler room fraud has been reported.

c - Public Warnings

Finally, a practice used with increasing frequency by some authorities is the use of public warnings. Some regulatory authorities, for example, issue warnings to the public concerning firms believed to be engaging in unauthorized securities or futures business, or particular investment products, the offer or sale of which may be unlawful. A principal advantage of this practice is its timeliness - an authority may issue a warning prior to completing the lengthy process generally required for a full investigation and prosecution of a particular individual or firm. This kind of measure may be useful in transnational cases, through transmission of the warnings to foreign authorities potentially concerned by the case.

B - Specific Measures To Target Boiler Rooms

1 - Education Of Public

a - Brochures

In order to alert potential investors about the existence of boiler rooms and the risks of investing in their products, some jurisdictions publicly distribute brochures. These brochures often describe the operations of a typical boiler room as well as products favored by boiler rooms, such as penny stocks, and markets favored by boiler rooms, such as those where price and trading information tends to be less accessible or not easily verified by independent means. The brochures also may contain information about market manipulation techniques of boiler rooms, such as price domination and trading among nominee accounts. Some materials instruct investors to obtain important information before investing, such as the background of the firm and its salespeople, and product information, such as firm quotations, interdealer quotations, markups, and resale information. Some brochures also inform the public of the duties of firms to the customer, and of customer rights and remedies. Many brochures provide contact persons at regulatory agencies or SROs to whom customers may complain, or from whom customers may obtain information concerning registrants and their disciplinary history.

These brochures may be distributed in a variety of ways : through mass-mailings by regulators or SROs ; as enclosures with other mail, such as utility bills or bank statements ; or upon request by regulators, SROs, local governmental agencies or other local business or professional organizations. Some jurisdictions have required firms that sell products involving a high degree of risk, such as penny stocks, to distribute, on a pre-trade basis, a standardized risk disclosure document, with printing and distribution costs borne by the firms themselves.

b - Public Access To Computerized Databases

Some regulatory and self-regulatory organizations have established database services to assist customers in learning about firms or financial instruments before they invest. By gaining access to non confidential information contained in these organizations' databases, potential investors readily may obtain public background information on firms, such as registration status or in certain countries disciplinary history.

c - Mass Media

Some regulators use mass media, such as television, radio, and newspapers, to disseminate information about boiler rooms. Using the media, authorities can focus on certain groups that tend to be targets of boiler room operations. Regulators have also issued press releases to inform the public of the details of enforcement actions taken against boiler rooms. For example, regulators can warn potential investors that the inclusion of a particular address in a company's solicitation materials does not necessarily mean the firm is registered or even does business in that location.

2 - Solicitation And Sales Practices

In some jurisdictions, efforts have been made to set regulatory parameters for permissible solicitations relating to investments in securities and futures, whether via telephone or through written materials.

a - Telephone Solicitation

The use of telephone calls to promote or sell financial products is regulated in many countries. Such statutes or regulations generally permit solicitation only subject to certain conditions. These may include :

* a limit on the frequency with which each new customer may be solicited by phone ;
* a requirement that calls may be made only if they have been requested by the potential customer or if, given the circumstances, it is reasonable to infer that the customer is agreeable to receiving the call ;
* a requirement that a risk disclosure statement be signed by the customer before the opening of any account and the performance of any transaction ;
* a requirement that orders received by phone be confirmed in writing along with the data related to the transactions performed ;
* a prohibition or limitation on "cold-calls" directed to unsophisticated investors.

Telephonic solicitation also may be addressed in general legislation, in advertising regulations, or under laws relating to business practices.

b - Written Solicitation

Some securities and futures authorities regulate the advertising practices of licensed firms, requiring firms to submit proposed advertisements to relevant regulatory or self-regulatory authorities prior to distribution. Others require provision of solicitation materials to such authorities only for certain types of securities or futures instruments, or with respect to certain classes of customers. In many countries, however, promotion of securities and futures products through mailings is not regulated as such. The promotion of securities, futures, derivatives or other financial products may be covered, nonetheless, by general regulatory provisions concerning mail solicitation or advertising.

III - OPTIONS FOR INTERNATIONAL COOPERATION

Regulatory authorities who detect transnational boiler room fraud occurring in or targeting their jurisdictions may take advantage of numerous options to assist them in their efforts to combat the fraud. Bilateral or multilateral cooperation between counterpart authorities through formal or informal channels can provide vital information and assistance. In certain cases, consultation and cooperation with criminal authorities, or use of existing criminal powers, also can be effective means to locate and prosecute boiler room operators.

A - Cooperation Between Securities And Futures Regulatory Authorities

When a regulator detects a boiler room in its jurisdiction and has reason to believe the boiler room has operations or contacts in another jurisdiction, or if the regulator detects evidence of boiler room fraud emanating entirely from outside its jurisdiction, it often is necessary to seek the assistance of its foreign counterparts. In this regard, a regulator may choose from a variety of avenues for assistance.

1 - Tools For International Regulatory Assistance And Cooperation

The first step a regulator in a target jurisdiction usually takes is to contact its relevant counterpart as soon as possible after the boiler room fraud is suspected. The initial contact will differ, however, depending on the available channels for the exchange of information and provision of assistance between the affected countries. International assistance and cooperation can be provided to the extent permitted by law either pursuant to a Memorandum of Understanding or other agreements, or on a case by case basis in the absence of more formal channels.

Memoranda of Understanding ("MOUs") and other agreements for mutual assistance and cooperation in enforcement matters (6) are useful tools for combatting international boiler rooms fraud. MOUs are bilateral or multilateral arrangements that are not binding under international law, while treaties and some other types of agreements are binding upon their signatories. They provide an agreed upon means for obtaining quick and effective assistance by relying on each signatory's willingness to use its domestic enforcement powers to assist its counterpart in the investigation or prosecution of illegal securities or futures activity. MOUs and other agreements usually target specific areas in which assistance can be provided, such as fraud and manipulation, which would cover most if not all illegal boiler room operations (7). They usually do not include a dual illegality requirement, i.e. there need not be a violation of law in both signatory countries for administrative assistance to be rendered.

To the extent permitted by the agreement and the law of a requested authority, assistance provided may be voluntary, compulsory, or both. In addition, MOUs and other agreements facilitate the provision of assistance by specifying in advance the exact manner in which requests are to be made and executed ; confidentiality of information obtained (or limits thereto) ; and recognized forms of assistance, such as the voluntary or compulsory production of documents and testimony ; and the comtemplated uses of the information, including criminal, administrative or civil proceedings.

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(6) - Cf. IOSCO Working Party n° 4 Report "*addressing difficulties encountered while negotiating and implementing Memoranda of Understanding*" released by the Technical Committee in July, 1990, and "*IOSCO Principles for MOUs*" released by Technical Committee in July, 1991.

(7) - In many cases, self regulatory organizations ("SROs") in some jurisdictions have entered int cross-border information-sharing and surveillance agreements with their foreign counterparts to detect and prevent market manipulation and fraud. These agreements also can be useful in combatting boiler rooms.

In the absence of MOUs or other international agreements, a regulator in a target jurisdiction also may contact successfully its counterparts in other relevant jurisdictions to obtain information about a boiler room and seek assistance in stopping the fraud. Without a pre-existing arrangement, a requested authority may find it more difficult to exercise its full powers, including its compulsory powers on behalf or another authority. Nevertheless, as a practical matter, many nations provide information and various forms of assistance to combat boiler room fraud, even in the absence of a pre-existing agreement, particularly when fraudulent activity is taking place in the requested authority's territory and the authority has an independent interest in prosecuting it.

2 - *Types Of Assistance*

The international assistance needed by regulators varies with numerous factors, particularly the nature and extent of the boiler room operation. On the one hand, a regulator may seek international assistance although its goal is only domestic prosecution and not large-scale international coordination against the boiler room. On the other hand, bilateral or multilateral investigations may be warranted to combat a large transnational operation. In the latter case, effective coordination becomes essential to the successful prosecution of the company and individuals perpetrating the transnational fraud.

a - Information Gathering And Sharing

Using the available formal or informal channels, the regulator in a target jurisdiction may find it useful to contact its counterpart to learn about a foreign boiler room's operating history, principals, shareholders, sales activities, or other information available to the counterpart. In addition, regulators in target jurisdictions can seek the voluntary or compelled production of information and records from the suspect company by the counterpart regulator. Further, if the authority receiving a request has the legal authority, it may be able to provide assistance using compulsory powers even if it does not perceive the boiler room to be a fraud within its own jurisdiction. In cases where compulsory powers are used, countries often must address confidentiality issues, such as how information obtained by the requested authority exercising such powers may be used by the requestor.

As a practical matter, once notified of a boiler room by a regulator in a target country, the regulatory counterpart may be alerted to the problem in its own jurisdiction and may have an independent interest in the case. In such instances, the regulator receiving a request for assistance may prosecute a fraud in its own jurisdiction, as well as provide assistance to the authority that initially requested it. The rendering of immediate and effective assistance, even in the absence of a perceived fraud in the jurisdiction of the regulator receiving the request, can go far toward combatting transnational boiler room fraud.

Moreover, a regulatory authority may become aware of a boiler room operating in or from its territory which also may affect the interests of a regulator in another jurisdiction. In such cases, the regulator detecting the operation may pass on information to the interested regulator on an unsolicited basis, keeping in mind requirements of confidentiality.

b - Multilateral Coordination

If it has been determined that a boiler room is operating in multiple jurisdictions, and particularly if the boiler room is perceived to be large-scale, it may be appropriate for regulators to take coordinated international action. When confronted with such situations in the past, members of the Working Party have found various ways to make international actions efficient and effective.

One method that has proven effective in combatting large-scale transnational boiler room fraud is periodic meetings between two or more interested jurisdictions. Such meetings can be useful not only for the exchange of information but also for detailed planning of future coordinated actions. The meetings may be ad hoc and small-scale, involving, for example, regulators from

two or three affected jurisdictions that are focusing on a particular aspect of the case. On the other hand, the meetings may be larger, involving regulators from all known jurisdictions affected by the boiler room. An example of such a large-scale meeting can be seen in the conference held in 1989 regarding the Quinn case, a well-known transnational boiler room . Such meetings can result in effective and coordinated planning and action against boiler rooms.

Often as a result of international meetings, countries may go further and take coordinated action against a transnational boiler room, such as searches, asset freezes, injunctive actions, or even criminal prosecution. Simultaneous proceedings or emergency measures, which are carried out by two or more interested jurisdictions, can be highly effective not only in dissolving or terminating the boiler room, but also in apprehending and prosecuting the organizers and promoters and providing restitution to the victims.

B - Criminalization Of Boiler Room Fraud And Cooperative Liaison With Criminal Authorities

The recidivist boiler room operator, often a problem for securities and futures regulators in domestic cases, presents even more challenges to regulators in the transnational context. The most effective means to combat recidivist boiler room operators, whether domestic or international, is to stop the individual wrongdoers, not just their current boiler room operations. In a few jurisdictions, securities and futures regulatory authorities also possess certain criminal investigative and prosecutorial powers. The investigation of crimes and the imposition of criminal sanctions, however, generally are the province of criminal authorities rather than securities and futures regulators. Nonetheless, the experience of various member jurisdictions demonstrates that securities and futures authorities can play a role in bringing the most potent enforcement sanctions to bear against recidivist boiler room operators.

Obtaining criminal sanctions against transnational boiler room principals and liaising or cooperating with criminal authorities in investigating such operations can be critical in detecting and deterring the spread of boiler room fraud from one jurisdiction to another. Criminalization of securities and futures boiler room fraud has been accomplished by member jurisdictions in a variety of ways. Similarly, cooperative liaison with criminal authorities has taken a variety of forms, even including, when permitted by local law, use of mutual legal assistance treaties for criminal matters ("MLATs").

1 - Criminalization Of Unlicensed And Fraudulent Activities

Some jurisdictions have had success deterring boiler room fraud by enacting statutes that criminalize the offer and sale of securities and futures products by firms that have not been authorized to engage in such business. In some jurisdictions that adopted such measures, a noticeable drop in the level of domestic boiler room activity was reported. Other jurisdictions impose criminal penalties, in addition to civil or administrative penalties, for the fraudulent and manipulative practices that are typical tools of the boiler room operator.

Some jurisdictions that impose criminal sanctions for fraudulent boiler room activities also establish a liaison between the relevant criminal and regulatory authorities in the investigation and prosecution of these cases. This liaison may involve various degrees of cooperation according to domestic legal structures. For instance, in one member country, task forces focusing on securities and futures fraud have been formed, linking efforts of the securities and futures regulators with specially designated units at various criminal prosecutorial offices throughout the country.

One of the benefits of this cooperative liaison has been the provision of expertise by the securities and futures regulators to the criminal prosecutorial authorities, who generally are not trained in or familiar with the complex operations that are often typical of securities and futures transactions. In addition, certain legal systems authorize "*strikes*" against boiler room operations, in which seizure of a boiler room premises by criminal authorities is effected at the same time an

order is obtained by the regulator from a civil court, freezing assets of the operation and its principals, and enjoining them from further violative acts. The increasingly common imposition of both criminal and civil sanctions in boiler room fraud cases raises the stakes for those who would engage in this fraud.

2 - *Cooperative Liaison With Foreign Criminal Authorities*

In many instances, foreign criminal authorities can provide very useful information about past and present operating methods of a transnational boiler room and its principals. In most cases, of course, the first and foremost point of governmental contact in another jurisdiction for a securities and futures regulator is its regulatory counterpart in that jurisdiction. However, in jurisdictions in which there is no securities and futures regulatory authority, or in cases where the conduct in question does not fall within the regulatory jurisdiction of such authorities, a criminal authority may provide the only avenue of assistance to a regulator.

In the experience of the members, the assistance that may be provided by such authorities varies very widely. Some criminal authorities may be unable or unwilling to provide assistance. Others, however, will provide publicly available background information on companies and persons, while many are willing to provide, and even to gather, confidential information concerning conduct that may amount to criminal wrongdoing in their own jurisdictions. Indeed, a request from an overseas regulator may bring illegal local conduct to the attention of the criminal authority for the first time. Moreover, information provided by the overseas regulator to the foreign criminal authority may enhance the criminal authority's ability to act quickly and effectively against the boiler room or its principals. Such action, of course, ultimately benefits the regulator and the customers in the jurisdiction targeted by the boiler room.

3 - *Use Of Criminal Mutual Legal Assistance Treaties*

Many member jurisdictions are parties to bilateral mutual legal assistance treaties ("MLATs") providing for cooperation between their national criminal authorities in a wide variety of criminal matters. Many of these MLATs have provisions that are broad enough to cover violative practices that include retail securities and futures fraud. In addition, many of the MLATs provide for assistance in certain ancillary administrative or civil investigations, where the possibility of criminal investigation and sanction exists in the requesting State.

Regulators in some jurisdictions have found that they may be able to seek information or assistance from abroad through MLATs. Where such assistance is available, it can be a very powerful weapon against a transnational boiler room operation. MLATs often provide for ex-parte freezes of assets upon request, thus providing the requesting authority with the possibility of immobilizing illegally obtained funds before they can be dissipated or moved to other jurisdictions. Given the speed and ease of international financial transactions, such a power is particularly desirable in combatting transnational boiler room fraud. It must be recognized, however, that cases in which such assistance has been rendered to a securities and futures regulator under an MLAT have thus far been the exception rather than the rule. In addition, there may be restrictions on use of information obtained under an MLAT in non-criminal matters, which can limit the effectiveness of these agreements in regulatory enforcement cases. Nonetheless, members continue to explore the possibilities of MLATs as mechanisms for gathering information concerning taking action, or supporting taking action, against securities and futures fraud.

OPTIONS FOR THE FUTURE

Based upon its review of existing statutes and regulations relevant to the fight against transnational retail securities and futures fraud, and the range of enforcement powers thus far applied against boiler rooms and their principals, the Working Group believes that a number of options should be considered by the members of IOSCO. Implementation of these measures may take different forms in different jurisdictions, and will depend upon a variety of factors, including the particular legal and regulatory structures in place in each jurisdiction, the scope and nature of the problems of this type of fraud experienced by particular jurisdictions, and the resources available in various jurisdictions to combat such operations.

In order to strengthen efforts against transnational retail securities and futures fraud, the members of IOSCO should consider the following domestic and international cooperative measures :

1. reviewing and enhancing domestic procedures for educating the retail investing public on the dangers of boiler room fraud, through print, telecommunications or other media as may be appropriate in their jurisdictions ;

2. taking steps to heighten the awareness of bona fide professionals and intermediaries and of mail and telephone forwarding services through which boiler room operators may attempt to effect or facilitate fraudulent operations ; and

3. prioritizing cooperation in significant cases involving transnational boiler room fraud, by providing information and enforcement assistance in a timely fashion through MOUs or other bilateral or multilateral information sharing arrangements, so that the fraudulent activities of boiler rooms and their principals may be quickly detected and halted ;

4. encouraging exchange of information between authorities on an unsolicited basis concerning multijurisdictional boiler room operations ;

5. developing enhanced means of cooperation between regulatory and criminal authorities, as appropriate under national law, to deter and punish boiler room fraud more effectively ;

6. examining transnational legal structures that might be developed, either on a bilateral or multilateral basis, to improve or broaden existing procedures to effect timely cross-border freezes of assets of boiler rooms and their principals, including on an emergency basis ;

7. studying the means for improving the enforcement of securities and futures judgments on a cross-border basis, with a view to repatriation and return to customers of funds that have been wrongfully obtained.

Through these and other avenues, the members of IOSCO will be able to combat more effectively transnational retail securities and futures fraud in the increasingly international financial markets they supervise.

APPENDIX

COMPILATION OF ANSWERS GIVEN BY IOSCO TECHNICAL COMMITTEE MEMBERS TO THE QUESTIONNAIRE ON THE LEGISLATION GOVERNING BOILER ROOM ACTIVITIES

COMPILATION OF ANSWERS GIVEN BY IOSCO TECHNICAL COMMITTEE MEMBERS TO THE QUESTIONNAIRE ON THE LEGISLATION COVERING BOILER ROOM ACTIVITIES

Boiler room activities are the subject of the Working Party's current work program involve the cross-border sales of securities, commodities, derivative and other financial products through high pressure sales techniques and/or misleading promotional materials and presentations. As part of the Working Party's evaluation of unilateral, bilateral and multilateral responses to such boiler room activities, it was considerad useful to determine what legislation exists in the country of each member of the Technical Committee with respect to the activities of boiler rooms. It was the purpose, therefore, of the Questionnaire to elicit information about such legislation in the Member countries of the Technical Committee. The following document is the compilation of the answers to the Questionnaire, received from each country. It provides for a detailed review of legislation relevant to boiler room activities.

The following compilation gathers the answers of :

- *AUSTRALIA :*
  the AUSTRALIAN SECURITIES COMMISSION,
- *CANADA-ONTARIO :*
  the ONTARIO SECURITIES COMMISSION,
- *CANADA-QUEBEC :*
  the COMMISSION DES VALEURS MOBILIERES DU QUEBEC,
- *FEDERAL REPUBLIC OF GERMANY :*
  the BUNDESMINISTER DER FINANZEN,
- *FRANCE :*
  the COMMISSION DES OPERATIONS DE BOURSE,
- *HONG-KONG :*
  the SECURITIES AND FUTURES COMMISSION,
- *ITALY :*
  the COMMISSIONE NAZIONALE PER LA SOCIETA E LA BORSA,
- *JAPAN :*
  the MINISTRY OF FINANCE,
- *SPAIN :*
  the COMISION NACIONAL DEL MERCADO DE VALORES,
- *SWEDEN :*
  the FINANCIAL SUPERVISORY AUTHORITY,
- *SWITZERLAND :*
  the FEDERAL DEPARTMENR FOR FOREIGN AFFAIRS,
- *THE NETHERLANDS :*
  the STICHTING TOEZICHT EFFECTENVERKEER
- *UNITED KINGDOM :*
  the DEPARTMENT OF TRADE AND INDUSTRY,
- *UNITED STATES OF AMERICA :*
  * *the SECURITIES AND EXCHANGE COMMISSION,*
  * *the COMMODITY FUTURES TRADING COMMISSION.*

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QUESTION 1

What are, in your country, the existing provisions governing the sale and the promotion of securities, futures, derivative and other financial products to customers ?

Do you have specific provisions governing the promotion or the sale of foreign securities, futures, derivative and other financial products to customers ?

A - SALE AND PROMOTION OF SECURITIES, FUTURES, DERIVATIVE AND OTHER FINANCIAL PRODUCTS

A.1 - In AUSTRALIA, the principal federal laws are :

- *Corporations Act 1989*,
- *Australian Securities Commission Act 1989*,
- *Foreign Acquisitions and Takeovers Act 1975*,
- *Trade Practices Act 1974*.

The *Corporations Act 1989*, together with complementary laws of the States and Territories are collectively referred to as the *Corporation Law*. Complementary State and Territory laws also extend the scope of the *Australian Securities Commission Act 1989* so that the *Corporations Law* is administered uniformly by the Australian Securities Commission.

A.2 - In CANADA, ONTARIO, the sale of securities, futures, derivative and other financial products to customers, within Ontario, is governed by the *Securities Act* (*RSO* 1980, c. 466, as amended). This statute prohibits persons from trading in securities unless they are registered with the Ontario Securities Commission. It also prohibits companies from issuing securities to residents of Ontario without a propectus filed and approved by the Ontario Securities Commission. The *Commodity Futures Act* (*RSO* 1980, c.78, as amended) governs the trading in approved commodity futures contracts and options. Trading in commodity futures contracts and options which are not approved under the *Commodity Future Act* are governed under the *Securities Act*.

A.3 - In CANADA, QUEBEC, the provisions applicable are to be found in the *Québec Securities Act* (*Revised Statutes of Quebec*, Chapter V-1.1).

A.4 - In THE FEDERAL REPUBLIC OF GERMANY, there are, with the exception of the regulations for the distribution of foreign investment shares, no special regulations for the sale and the promotion of foreign securities and financial products.

The legal framework for the sale and promotion of securities and other financial products is provided by the following regulations.

German Banking Law (Kreditwesengesetz - KWG). - In the Federal Republic of Germany, it is first and foremost the credit institutions via which the sale of securities and other financial products to customers takes place. Under Section 1 *KWG*, the purchase and sale of securities on behalf of customers is a banking activity. Of relevance to the contractual relations between the credit institutions and their customers are the regulations of the German Commercial Code (*Handelgesetzbuch)*, particularly those regarding the consignment agreement, and the regulations of the German Civil Code (*Bürgerliches Gesetzbuch)* regarding the purchase contract and the agency contract. The German courts have ruled that the credit institutions have an obligation to provide information to their customers according to the nature of the transactions. Insofar as the credit institutions utilize brochures or other presentational material in selling securities or other financial products, they are responsible for the accuracy and completeness of this information.

Activity of middlemen under Section 34c "Trade Regulation Act". - The purchase of securities and other financial products can also be effected via professional brokers. Under Section 34 C of the *Trade Regulation Act*, the middleman must have a licence from the trade supervisory authority if the object of his business is the professional brokering of German or foreign investment shares, domestic and foreign stocks and bonds of domestic and foreign corporations. On the other hand, the brokering of stock options and futures contracts does not require a licence under Section 34 c of the *Trade Regulations Act*.

As regards the activity of the middlemen pursuant to Section 34 c of the *Trade Regulation Act*, the Federal Minister of Economics has issued a *Decree on Brokers and Builders* containing a number of regulations for the protection of the customers. This places inter alia the following obligations on the investment broker :

- the broker must provide surety for assets of the investor which he receives for the purpose of carrying out the transaction ordered by the investor. He may use such assets only for the specific transaction at hand ;

- the broker must keep the customer's assets separate from his own and from those of his other customers ;

- of particular importance is the broker's obligation to provide information to the customer before accepting the order. The broker must inform the customer in writing in the German language inter alia about the corporation involved, the listing of the shares on the stock exchanges, the existence of an underwriting or stock exchange prospectus, the applicable law and all costs connected with purchase. The investment brokers, just like the credit institutions, are liable under civil law to the investors for the fulfillment of their obligation to provide information and for the accuracy of the prospectus material used.

Sales Prospectus Law and *Sales Prospectus Decree*. - For securities being offered domestically for the first time, since January 1st, 1991, the offerer must publish a sales prospectus three days before the commencement of the subscription period. The contents of the sales prospectus correspond to the listing prospectus if listing of the securities for official trading is to be applied for. In all other cases, the requirements for the contents of the prospectus are somewhat lower. The exact information which must be included on the issuer and the securities is laid down in the *Sales Prospectus Decree*. The *Sale Prospectus Law* further states that the offerer is liable for damages to the investor if the prospectus contains inaccurate or incomplete information. A fine may be imposed by the competent authority for failure to comply with prospectus requirements.

Law on Investment Companies. - This law specifies the obligations which German investment companies must observe in the distribution of shares of the investment funds they manage. At the time the contract is concluded the purchaser of an investment fund share must be given a sales prospectus with the terms of the contract and the last annual report on the fund's assets.

Foreign Investment Law. - The Foreign Investment Law lays down the preconditions and modalities for the distribution of foreign investment shares in the Federal Republic of Germany. Preconditions include that a domestic credit institution or a professionally qualified person is nominated as representative, that the objects of the investment fund are subject to monitoring by a depositary bank and that domestic credit institutions act as paying agents. Exactly as in the distribution of German investment shares, at the time of the conclusion of the contract the purchaser must be given a sales prospectus with the terms of the contract and last annual report. The foreign investment company must notify the distribution of investment shares in advance to the Federal Banking Supervisory Office,

which may, if necessary, object to the commencement of distribution. The supervisory authority may prohibit certain types of promotion in order to prevent abuses. This applies in particular to promotion which is designed in a misleading way to create the impression that the offer is especially advantageous.

Law Regarding Revocation of the Door to Door and Similar Dealings. - This law gives the customer the right to revoke within a week in writing his decision to conclude the contract if the contract was effected by oral negociations at his workplace or at his private residence or after he was unexpectedly approached in public transport or in an area of public passage. The period within which revocation is possible does not begin until the customer has received a written notification of his right of revocation. The *Law on Investment Companies* and the *Foreign Investment Law* provide a written right of revocation by the customer within two weeks for the distribution of investment shares if the oral negociations on the purchase of investment shares were conducted in a place other than at the offerer's permanent business premises.

Stock Exchange Act. - For the distribution of futures contracts it is important to note that under the *Stock Exchange Act*, a private investor can raise objections (known as the gambling plea) to the validity of the transactions at any time until accomplishment of the performance incumbent on him. The bank, however, can render futures contracts relating to securities and other financial instruments binding by informing the customer in writing before conclusion of the transaction in particular about the risks connected with futures transactions. The details of the written notification are set forth at length in the *Stock Exchange Act*.

Itinerant Trade. - Under Section 56 of the *Trade Regulation Act*, the distribution of securities and interim certificates in the so-called itinerant trade is not permissible.

A.2 - In FRANCE

1 - SALE OF SECURITIES, FUTURES, DERIVATIVE AND OTHER FINANCIAL PRODUCTS

a - Offer and sale of securities

According to the *1967 Ordinance*, the initial public offering of securities is subject to the elaboration, by the issuer, of a prospectus to be filed with the COB and distributed to the general public (*1967 Ordinance*, Article 6 and Article 7). The information to be included in this document of information are provided for in the *COB Rule n° 88-04*.

If the shares are to be listed on a French Exchange, an application is submitted to the Securities Exchange Council by a brokerage firm, a bank, or any other financial intermediary (*Securities Exchange Council Regulations*, Article 3 § 1.1 ; *Securities Exchange Council General Decision n° 88-2*). The Securities Exchange Council then delivers an authorization to introduce the concerned shares on the exchange (*1988 Securities Law*, Article 7). At this step of the procedure, the COB has the power to veto the authorization of the Council (*1988 Securities Law*, Article 7) in three cases (*COB Rule n° 88-03*) :

- when it considers that such introduction constitutes a risk incompatible with the interests of the investors ;

- when it considers that the financial statements show serious gaps or that the verifications made by the auditors are inadequate ;

- when during the year preceding the introduction, insider dealing transactions have been operated on the securities concerned.

The *1988 Securities Law* provides that the sale of listed securities and of options on such securities can only be performed through a brokerage firm authorized to operate on the relevant Exchange (Article 1 § 1).

The main exceptions to this rule are (Article 1 § 3) :

- when the transaction is concluded directly between two individuals ;

- when the transaction involves a firm and its subsidiary, provided that the former holds more than 20 % of the latter ;

- when the transaction is just a part of a contract different than a pure sale, and is a necessary component of it.

It should also be noted that a recent *COB Rule n° 91-02* incorporated into French law the provisions of two EEC directives on prospectus to be issued for the emission and admission of securities on an official exchange. Company emitting securities and which ask for their admission on a French exchange shall provide the COB with a document of information called "prospectus". The same duty is given to French companies wishing to have their securities listed abroad. Under EEC law, these prospectuses are recognized among EEC countries. The *COB Rule n° 91-02* provides for the contents to be given to these prospectuses.

The sale of non listed securities is governed by *COB Rule n° 92-02* on the offer of securities to the public. This Rule has been homologated by the Ministry of Finance on March 3, 1992. It incorporates into French law the same directives as *Rule n° 91-02*. The difference is that *Rule n° 92-02* governs the offer to the public of non listed securities. This rule provides that a simplified prospectus shall be given to the public. It also provides for the procedure to be followed to file the simplified prospectus with the COB, and the contents to be given to the document.

b - Sale of financial and commodity futures

The sale of futures and that of options on futures can only be performed through a brokerage firm, a commissioner or a bank authorized to operate on the relevant market.

c - Sale of mutual funds shares

French firms responsible for managing mutual funds assets can sell mutual funds shares to the public provided that a document of information approved by the COB and describing the main characteristics of the mutual fund is given to the customer prior to any subscription.

B - PROMOTION OF SECURITIES, FUTURES, DERIVATIVE AND OTHER FINANCIAL PRODUCTS

Before going into details on specific rules governing canvassing activities in France, it is essential to point out that the principle, under French law is that only a limited list of persons are authorized to enter into canvassing activities. These persons all belong to strictly regulated professions. The basic provisions regarding this authorization are to be found in the *Law of December 28, 1966 on usury, loans and certain operations of canvassing and advertising*. These regulated professions may canvass the public through the activities of intermediaries, canvassors, who shall comply with a number of formal requirements in order to actually canvass the public.

It is also to be pointed out that **a number of operations are strictly forbidden** :

- the *law of December 28, 1966 on usury, loans and certain operations of canvassing and advertising* forbids canvassing for funds invested in shares of real estate companies ;

- the *law of January 3, 1972 on canvassing of securities* forbids :

  * peddling for securities (Article 1),
  * canvassing for operations implying certain particular risks, or on securities which are not known (Article 5).

- the *Law of December 23, 1988 on Mutual Funds* also forbids certain investments presenting a too high degree of risk (Article 22, Article 23, Article 35).

a - Promotion of securities

a.1 - DEFINITION OF CANVASSING. - Under the *Law of December 28, 1966 (Article 9)* and the *1972 Law on canvassing of securities (Article 2)*, the canvassing of securities is defined as follows : is considered as canvassing the act of going regularly to the domicile or residency of people, or at their workplace, or in public places, in order to advice for subscribing, buying, selling, exchanging securities, or for participating into such operations ; are also considered canvassing activities offers of services or advice given on a regular basis, towards the same goal, at the domicile or residency of people or at their workplace, through letters, circulars, or by phone.

a.2 - ENTITIES AUTHORIZED TO CANVASS THE PUBLIC. - The canvassing of securities may be made only by brokerage firms, banks, portfolios management firms, and, for certain products, by insurance companies (Article 3).

a.3 - CONDITIONS TO BE FULFILLED BY CANVASSORS. - Each canvassor must be able to present a professional card delivered by the firm which employs him (Article 7), on which it is specified that the firm authorizes him to promote stocks on its behalf. The firm must forward a list of all authorized persons to the Department of Justice (Article 8). The card can be given only to French citizens or to citizens of an EEC member State(*1972 Law on canvassing of securities*, Article 8 § 4 ; *Law of July 10, 1975*, art. 7). The card can be taken back from the canvassor either by his employer or by the Department of Justice, the latter having to provide the reasons for his decision (Article 8). The card mentions the civil status of the canvassor, his adress, the name of his employer, the location of the seat of the

employer, the financial products the canvassor is directed to promote. Modifications brought to these information shall be transmitted to the Department of Justice.

The canvassor may only promote the stocks he was directed to promote by his employer (*1972 Law on canvassing of securities*, Article 9).

The canvassor must provide his clients with a document of information concerning each promoted security (Article 6). This document is elaborated under the responsibility of the firm which promotes the stock and it shall be updated on a regular basis. It is submitted to the COB which can ask for modifications, or even forbid its publication.The document of information shall also mention the identity references of the company promoting the stocks, its adress as well as the denomination of the company which stocks are promoted (*Decree of August 22, 1972*, Article 6).

The promotion of stocks issued but not listed is forbidden (*1972 Law on canvassing of securities*, Article 5).

b - Promotion of commodity and financial futures

b.1 - DEFINITION OF CANVASSING. - The canvassing of commodity and financial futures is defined in the same way as that of securities with, however, one difference : the *1885 Futures Markets Law* encompasses in the definition of canvassing the fact of taking and placing orders on behalf of the public. It is not, as for securities, the mere fact of advertising and counselling.

b.2 - ENTITIES AUTHORIZED TO CANVASS THE PUBLIC. - The canvassing of commodity and financial futures may be performed by brokerage firms, banks, the Caisse des Dépôts et Consignations, authorized commissioners ("commissionaires agréés") and dealers specialized in futures, and operators registered with the CMT (Futures Market Council) (*1885 Futures Markets Law*, Article 8, Article 8 § 1 and Article 11).

b.3 - CONDITIONS TO BE FULFILLED BY CANVASSORS. - Each canvassor shall have a professional card delivered by the firm which employs him. A canvassor cannot operate on behalf of more than one firm (Article 12 § 1). The card lists the type of operations or products that the canvassor is authorized to promote (Article 12 § 2). The firm must provide the Department of Justice with a list of all authorized persons (Article 13 § 1). The card is delivered to the canvassor after one month (Article 13 § 4). During this time, the Department of Justice may oppose the delivery of the card to the canvassor (Article 13 § 5).The card may be given only to French citizens or to citizens of EEC member States (Article 13 § 3). The Department of Justice may deprive the canvassor from his card, provided that this decision is motivated (Article 13 § 5).

The canvassor may collect funds only after the expiration of a seven days period (delay given to the customer for further consideration) following the delivery to the customer to be of a document of information, approved by the COB and describing the functioning of the referred markets and the related risks and obligations (Article 14 § 1 and § 2 ; *Futures Markets Council Decision n° 84-003*). Under the *1885 Futures Markets Law*, the document of information to be provided to the customer is more general than under the *1972 Law on canvassing of securities*. Information is to be given about the futures markets in general, and not only on the products as it would be the case for canvassing of securities. The document of information is thus more general. Actually, it has been elaborated under the auspices of the Futures Markets Council and consists in a general presentation of the market, to which

are attached some technical memos outlining the major characteristics of the products negociated on the concerned markets.

The funds collected should not be given to the canvassors, under any circumstances (Article 14 § 3).

c - Promotion of mutual funds shares

c.1 - ENTITIES AUTHORIZED TO CANVASS THE PUBLIC. - To be allowed to collect funds, a mutual fund must have been registered with the COB (*COB Rule n° 89-02*, Article 5 and Article 8). The information to be provided by mutual funds to be registered with the COB are described in a *COB Instruction on Mutual Funds for the application of COB Rule n° 89-02*.

c.2 - CONDITIONS TO BE FULFILLED BY THE CANVASSORS. - Once the mutual fund is registered, the promotion of its shares is usually authorized provided that the canvassor abides by the following conditions.

The canvassor is forbidden to collect any funds or orders directly (*1972 Law on canvassing of securities*, Article 17).

A document of information, approved by the COB, must be provided to the customer to be (*COB Rule n° 89-02*, Article 32). The *COB Instruction on Mutual Funds* provides for the exact contents of the document of information ("fiche signalétique"). Basically, this document states the characteristics of the fund.

The purchase of shares shall be formalized through the signing of a subscription sheet (*1972 Law on canvassing of securities*, Article 16 § 1) which shall mention, among other things, the opportunity for the customer to cancel his purchase within a 15 day period (Article 16 § 2 and Article 21), and the interdiction made to the canvassor to collect any funds or orders (Article 16 § 2 and Article 17).

d - Promotion of other financial products

The *law of 1966* (Article 9 § 4), setting up a general regime applicable to canvassing, provides that canvassing on all other financial products than those specifically listed (and that we have mentioned above) is also within the scope of its provisions. Thus, this law makes sure that any canvassing is regulated.

The *law of 1983* deals with the promotion of life annuities and of rights upon goods, when the purchaser does not himself manage his property or when the contract provides for the possibility for the buyer to resell or exchange the goods and the reassessment of the capital invested (Article 36 § 1). The law applies to canvassors as well as to persons who collect funds for such activities and those who manage these properties. The law provides that, within the scope of the activities mentioned above, those who perceive funds collected from the customers or produced by the investments, shall be organized in the form of joint-stock companies (Cf. US incorporated companies) and meet the capital minima required by the *1966 Company Law* for public companies (Article 36-1 ; *1966 Company Law* Article 71 : to date, the capital minima required for public companies is 1.500.000 FF). Furthemore, a document of information approved by the COB must be given to the customer prior to the collection of any funds (Article 37 § 1). A *decree of May 2, 1983* provides for the indications to be mentionned in the document of information. The COB examines the document of information within a 30 or 60 day period (for the latter, a motivated decision is needed) and

gives its appreciation. The canvassor shall comply with the observations of the COB. Any change in the conditions of the contracts proposed shall be submitted to the COB for approval. If the conditions of the canvassing do not correspond anymore to those approved by the Commission, injunction may be made to the canvassor to resume his activities.

A.6 - In HONG KONG, the Securities and Futures Commission ("SFC") has regulatory jurisdiction over the following :

(a) dealing in securities in Hong Kong ;
(b) trading in commodity futures contracts in Hong Kong ;
(c) marketing of investment arrangements in relation to property other than securities being advertised and/or offered to the public in Hong Kong.

Three ordinances are relevant to these activities, namely : the *Securities Ordinance*, the *Commodities Trading Ordinance* and the *Protection of Investors Ordinance*.

DEALING IN SECURITIES. - The *Securities Ordinance*, Chapter 333, defines securities to include "foreign securities". The promotion of securities is covered both in the *Securities Ordinance* ("SO")and the *Protection of Investors Ordinance* ("PIO"), Chapter 335. The following provisions are relevant :

- Section 72 of the *SO* which requires dealers to provide certain information to a client in relation to both an offer to acquire, or dispose of, securities of a corporation.

- Section 73 prohibits cold calling by registered dealers.

- Section 74 prohibits hawking of securities by any person.

- Section 4 of the *PIO* prohibits any person from issuing to another person any advertisement, or invitation in relation to the acquisition, disposal, subscription for, or underwriting of securities. The SFC can also authorise the issue of advertisements, and promotional material under this provision.

- Section 3 of the *PIO* makes it an offence for any person who, by any fraudulent or reckless misrepresentation, induces another person to acquire, dispose of, subscribe for, or underwrite securities.

- Section 136 of the *SO* creates an offence for any person to employ any fraudulent or deceptive method in connexion with the sale, or purchase, of securities to another person (general fraud provision).

- Section 135 of the *SO* creates an offence for :

* any person to create a false or misleading appearance of active trading, or a false market, in respect of any security traded on the Stock Exchange of Hong-Kong Limited ;

** to depress, raise, or cause fluctuations in the market price of securities, by conducting transactions involving no change in beneficial ownership ;

*** for circulating, or disseminating information to the effect market activities, which to his knowledge are conducted in contradiction to * above, will affect the price of securities.

- Section 138 of the *SO* creates an offence for any person, for the purpose of inducing the sale of securities of a corporation, to make a false or misleading statement, or omit in a

statement material information, that would render the statement false or misleading, in relation to the operation or the past or the future performance of that corporation.

- *Hong Kong's Companies Ordinance*, Chapter 32, contains requirements concerning the issue of prospectus for both local and overseas companies.

- *Hong Kong's Theft Ordinance* contains various fraud provisions which could, dependent on circumstances, be applicable to boiler rooms operations.

TRADING IN COMMODITY FUTURE CONTRACTS. - The following rules are relevant :

- Section 60 A of the *Commodities Trading Ordinance* ("CTO"), Chapter 250,creates an offence for hawking of futures contracts.

- A futures contract is an investment arrangement in relation to property other than securities. Section 4 of the *PIO* prohibits the issue of an advertisement or invitation in relation to such, unless it has been authorised by the SFC.

- Section 3 of the *PIO* caters for fraudulent or reckless misrepresentations made to induce another person to enter into an investment arrangement.

- Section 62 of the *CTO* creates an offence for any person to intentionally create a false or misleading appearance of active trading in any commodity on a market operated by the Hong Kong Futures Exchange Limited. It further creates an offense for a person to circulate, or disseminate, information to the effect such market activities, which to his knowledge contravene this provision, will affect the price of the futures contract.

- Section 63 is a general fraud provision relating to the purchase or sale of a futures contract.

- Section 64 creates an offence for any person to make a false or misleading statement for the purpose of inducing the purchase or sale of a futures contract.

- *Hong Kong's Theft Ordinance* contains various fraud provisions which could, dependent on the circumstances, be applicable to boiler room operations.

INVESTMENT ARRANGEMENTS. - These are covered by Section 3 and 4 of the *PIO*.

A.7 - In ITALY, public offers of all types of securities, however effected, are governed by Articles 1/18 ff of *Law 216/1974*. These provisions require a person who wishes to offer securities to the public to give advance notice of his intention to the CONSOB, indicating the quantity and features of the securities offered as well as the procedures and time limits foreseen for the operation and to publish a prospectus with information on the organization, assets and liabilities, financial position, profits and losses, and prospects of the offeror and issuer.

From the date of the notification the offeror is subject to the supervision of the CONSOB, which may require the offeror to provide it with information and to publish such information permitting potential investors to arrive at an informed opinion regarding the proposed operation.

Promotional and advertising activities concerning securities are considered as raising funds from the public and are therefore subject to the advance notification and prospectus requirements referred to above. Advertising is allowed once the prospectus as been published provided the rules laid down by the CONSOB in specific regulations are respected. The advertising copy has to be submitted in advance to the CONSOB. Failure comply with the foregoing provisions is a criminal offence and involves the suspension of the advertising.

If the obligations described above have not been fulfilled, the sale of securities and the promotion of securities for the purpose of selling them are subject to penal sanctions.

There are no specific legislative or regulatory provisions in Italy on the promotion or sale of foreign securities since the provisions of the law on the public offer refer to domestic and foreign securities alike.

A.8 - In JAPAN, the *Securities and Exchange Law* governs the sale and the promotion of securities and its derivatives, while the *Financial Futures Trading Law* and *Commodities Exchange Law* govern those of financial futures and commodities respectively. Following answers apply only to sales and promotion of securities because the securities Bureau is in charge only of *Securities and Exchange Law*.

A.9 - In SPAIN, (translation provided), distinction should be made between promotion and sale.

As far as **promotion** is concerned, Article 94 of the *LMV* (*Loi du Marché des Valeurs* / *Stock Exchange Law*) provides that the Ministry of Economy determines cases in which promotion of activities dealt with in this law, will require authorization or any other administrative control by the CNMV (Comision Nacional del Mercado de Valores) and will adopt, in general, specific provisions with which the CNMV will comply. This opportunity has never been used to date. This activity is rather free.

The CNMV will take appropriate measures in order to obtain completion or modification of the promotion concerned which is contrary to the provisions mentioned previously, or, in general, which is contrary to the common rules applicable to advertising : *Loi Générale sur la Publicité* (*General Law on Advertising*) and *Loi de Défense du Consommateur* (*Law on Protection of the Consumer*). There are no direct measures foreseen.

As far as the **sale** is concerned :

Primary market :

It is regulated in Title III of the *LMV*, Articles 25 to 30.
Article 25 provides that the issue of securities does not require any administrative authorization, although the Ministry of Economy may forbid certain issues or decide that they require authorization.

Nonetheless, the issue of securities require fulfillment of the following conditions, provided for in Article 26 :

- communication of the project to the CNMV, according to the formalities set by regulations ;

- submission to the CNMV and registration with the CNMV, of all documents justifying the agreement for issuance, characteristics of the securities, duties of the holders ;

- existence and registration of an audit of the financial sheets of the issuer.

- presentation to the CNMV and registration of the information prospectus of the concerned issue ;

- compliance with certain period of time between communication of the project to the CNMV, registration of the prospectus, and issue of the securities. These time periods are to be provided for in regulations.

Recently, *Royal Decree 291/1992* on Issues and Public Offers which developes Tittle III of the *LMV*, has supposed the application to our legislation of community provisions and specially *Directive 8/298/EEC*, relating to the prospectus of information.

For all these reasons, we consider that fraudulent commercialization of any stock by an hypothetic boiler room, would be an unusual phenomenon.

Secondary market :

* trading on an official exchange is governed by Title IV, Articles 31 to 61.

Pursuant to Article 36, the admission of securities to trading on an official market needs to be done with the participation of at least one stock exchange member.

Article 47 provides that the brokerage houses and dealers authorized to be exchange members are those which take part in the capital of a joint-stock company responsible for the organization and internal functioning of the stock exchange.

Title V of the *LMV*, dealing with the brokerage houses and dealers, stresses that only these entities may be members of an exchange, and perform an activity of trading (Article 70). The quality of member is materialized by the participation into the capital of the joint-stock company which manages the concerned exchange (Article 64).

The process does not guarantee the quality but the transparency of the transmission.

* trading on a non-official exchange :

The Third Additional Provision to the *LMV* provides that the subscription or transfer of securities only requires, for its validity, the intervention of the person in charge of certifying the authenticity of the contract, when the securities are in the form of bearer stocks. This subscription or transfer does not need the intermediary of a brokerage house or a dealer.

As for trading on an official exchange, the process does not guarantee the quality but the transparency of the transmission.

For all these reasons, we consider that the activity of an hypothetic boiler room in Spain should turn towards the promotion and sale of stocks trading on a non-official exchange and besides, issued in a way described as non-Public Offer (those stocks issued without seeking trading on an official exchange or spreading among the public and those issues turned towards the members of the issuer) and also the issues of an amount lower than 500 million pesetas done without any advertising, because those kinds of issues are not subject to the CNMV supervision and the mission of the person in charge of certifying the authenticity of the transfer is not focused on the economic study of the stock subject to transfer.

A.10 - In SWEDEN, the existing provisions governing the sale and the promotion of financial products to customers are to be found essentially in a recent legislation brought into force on August 1, 1991. This legislation is composed of two main sets of provisions : an *Act on the Trade in Financial Instruments* (*SFS* 1991 : 980) and an *Act on Securities Business* which governs the professional supply of certain financial services (*SFS* 1991 : 981). In addition to these two laws, an *Insider Act* entered into force in February 1991 (*SFS* 1991 : 1342).
The government has passed, on March 19, 1992, a bill to the Parliament, on a new stock exchange and clearing legislation. The bill was treated by the Parliament on June 2, 1992 and enacted as "SFS 1992 : 543". This act will enter into force on January 1, 1993.

The difference between the requirements of this new legislation and the former one is mainly that the contents of the new listing particulars are adapted to the minimum rules of the *Council Directive Coordinating The Conditions For Admission Of Securities To Official Stock Exchange List* (79/279 EEC) and that the present monopoly situation of the Stockholm Stock Exchange will be abolished.

The present rules stipulate that at the scrutiny of listing particulars, there should be regarded the economic situation of the issuer, the market conditions of the securities to be listed and the other circumstances of importance for a fair trade.

In order to enable the board of the stock exchange to get properly informed, there are governmental provisions about what should be attached to an application for listing at the Stockholm Stock Exchange.

In the governmental provisions, there are some requirements to the issuer and to the securities due to the listing process. These provisions are completed by the listing rules of the Stock Exchange itself. Thus, there are checks on liquidity and profitability and also on information supply, economic control and monitoring.

According to the governmental provisions, there shall be attached to the application of listing a promise by the applying company to inform about the company in a special form. This form has got to be called a "registration contract". The purpose of this contract is to guarantee a rapid and vast distribution of company information. There are listed a number of different types of decisions and events that are to be submitted to the public.

If the Stockholm Stock Exchange functions as a primary market place, principally the same requirements and the same scrutiny will be directed to foreign issuers as to Swedish ones of securities etc. In the case of the Swedish exchange being a secondary market place, there is no further listing control except for the information to the public by the applicant company. Thus, there are provisions for the foreign securities too.

The major provisions regarding persons authorized to sale or promote securities, futures and other financial products are to be found among the conditions for licensing, a task up to the FSA. In its advisory rules (*FFS* 1991 : 3), the FSA has initially stressed the importance of the fitness and skill of the personel. Concerning the owners, the FSA has, in accordance with the Act, to scrutinize the ability of the applicants from an ethical, economical and skillful point of view.

A.11 - In SWITZERLAND, at the present time, Swiss federal legislation does not contain any specific provision governing the sale and promotion of securities, commodities, derivatives and other financial products (here below securities). Only general provisions of commercial law regulating rights and obligations related to the execution of contracts would apply. With a very few exceptions, this means Swiss legislation is in this matter of civil or penal nature only. Three important cantons regulate the securities dealers (Zurich and Basle

City) or the financial intermediaries (Ticino). Moreover, professional self-regulation plays in this regard also an important role. Different professional associations, active in the financial services industry have asked their members to subscribe to codes of conduct or similar set of professional rules of behaviour. Practices such as high pressure sales or misleading promotional materials are not compatible with these codes of conduct. It is difficult for the federal authorities to make an assessment of the implementation of these rules.

However, a federal draft law on stock exchanges and securities trading is currently before Parliament where debates within committees have started in the summer 1993. The necessity to regulate all suppliers of financial services whose activities are not regulated by a federal law is currently examined.

A.12 - In THE NETHERLANDS, the sale of securities, futures and derivative products and the offering of brokerage and/or portfolio management services in relation to these securities are regulated by the *Supervision of Securities Trading Act (SSTA)*, the *Supervision of Securities Trading Decree (SSTD)*, the Regulations issued by the *Securities Board of the Netherlands (STE)* governing the *Supervision of Securities Trade (RSST)* and the *Exemption Regulation (ER)*.

The *SSTA* contains provisions governing :

- the offering of securities upon issue (Chapter II),
- brokerage services (Chapter III Division 1),
- portfolio management services (Chapter III Division 2).

The definition of the concept "securities" in the *SSTA* is wide in comparison with other countries (*SSTA* Chapter 1 Section 1 (a)).

The *SSTA* applies when securities, brokerage services or portfolio management services are offered in or from the Netherlands to natural or legal entities who are not members of a restricted circle. A restricted circle. A restricted circle can only be assumed when :

- the group approached is restricted in number and specified ; and

- a certain relation between the firm that offers securities, brokerage services or portfolio management services and the members of the group exists apart from the financial relation ; and

- in the promotion material, it is clearly stated that the acceptance of the offer is reserved to the members of the above mentioned group.

When securities, which are not admitted to the listing of an official national securities exchange (the Amsterdam Stock Exchange, the European Options Exchange and the Financial Futures Market and Agrarian Futures Exchange Amsterdam (Exchanges)), are offered upon issue beyond a restricted circle, a prospectus concerning the offer has to be made generally available. The prospectus has to satisfy the requirements in the *SSTD* (Section 2), with the exception of the prospectus which has been approved by the competent authority of an other member state at least six monts before the date on which the offer of securities upon issue is to be made and which has been drawn up in accordance with Section 8 or 12 of Directive (89/298/EEC). The requirements are further elaborated in the RSST.

When securities are offered upon issue which are admitted to the listing of the Exchanges, the regulations of these Exchanges do apply. With regard to the requirements for a prospectus, the *SSTD* does not differ substancially from these regulations.

Furthermore, the prohibition will not apply to the offering of securities exempted by the ER. An exemption is applicable if :

1. the securities are solely offered to professionals ;

2. the securities are offered in denominations of at least one hundred thousand quilders ;

3. the offer concerns Euro-securities ;

4. the offer relates to debts certificates which have an initial maturity not exceeding one year and are issued by a credit institution ;

5. the offer relates to securities which are issued by a public authority of a member state ;

6. the securities are offered free of charge ;

7. the offer is solely made to persons outside the Netherlands.

The exemptions are subject to restrictions provided for in the ER. The ER also provides for conditions attached to exemptions.

A.13 - In the UNITED KINGDOM, all these activities are within the scope of the *Financial Services Act of 1986* (*FSA*) which makes it a criminal offence to carry on such activities (and other investment business) without authorization (Section 3). The *FSA* also makes it a criminal offence to issue misleading statements or engage in misleading practices (Section 47) and to breach restrictions on advertising (Section 57). The *FSA* also prohibits the making of unsollicited calls (Section 56) except to the extent allowed under regulations made by the Securities and Investment Board (SIB).

The *FSA* requires all firms to be subject to conduct of business rules. SIB has introduced a three-tier approach to the regulation of investment business in the UK. The *Core Rules*, together with 10 Principles, provide the central framework. The *Core Rules* will apply to all firms authorised by the 4 Self-Regulating Organisations (SROs) and SIB. They will be supplemented by "third-tier" rules and guidance. The *Core Rules* for the conduct of investment business cover, inter alia, independence, advertising and marketing, customer relations, dealing for customers, market integrity and administration.

UK Recognised Investment Exchanges must meet the requirements of Schedule 4 of the *FSA* including rules and practices which ensure that business conducted by means of its facilities is conducted in an orderly manner and so as to afford proper protection to investors. An authorised firm trading in securities off-exchange will normally have to provide its regulator with details of the transactions. Generally, in relation to derivatives, contingent liability transactions for private customers must be made on a recognised or designated investment exchange.

A.14 - In THE UNITED STATES

A.14.1 - Answer of the SEC

THE OFFERS AND SALES OF SECURITIES GENERALLY. - Offers and sales of securities in the US must be registered under the *Securities Act of 1933* ("*1933 Act*"), unless an exemption

from registration is available. The term "securities" is broadly defined, and would include certain derivative and other financial products. However, futures and certain related financial products are subject to the jurisdiction of the Commodities Futures Trading Commission.

The *1933 Act* and the rules and regulations thereunder prohibit sales of, or written or oral offers to sell, a security prior to the filing of a registration statement with the SEC. During this period, no activities may be undertaken by the issuer that might have the effect of creating investor interest in the securities to be offered. After the registration statement has been filed, oral offers to sell the securities may be made or indications of interest in buying the securities may be solicited, subject to certain limitations. Securities may be sold without registration in a private placement (i.e. a non-public offering, as defined by rules), but general solicitations of interest in the securities, and general advertising relating to the private placement are not permitted.

The offer and sale of investment company securities, such as mutual fund shares, is governed by the *Investment Company Act of 1940* ("*1940 Act*") and the *1933 Act*.

Those who provide advice with respect to securities are generally subject to regulation under the *Investment Advisers Act of 1940* ("*Advisers Act*").

The anti-fraud and anti-manipulation provisions of the federal securities laws apply generally to the offer, purchase or sale of securities, without distinguishing whether the securities are foreign or domestic. Section 10(b) of the *Securities Exchange Act of 1934* ("*1934 Act*"), prohibits the use of "any manipulative or deceptive device or contrivance" in connection with the purchase or sale of any security. It is a broad "catch-all" provision that empowers the SEC to prescribe rules that it deems necessary and appropriate in the public interest and for the protection of investors. Section 17 (a) of the *1933 Act* prohibits fraudulent transactions with respect to the offer or sale of securities.

Rule 10 b-5, which was promulgated pursuant to Section 10 (b) of the *1934 Act*, makes it unlawful, in connection with the purchase or sale of any security, to : (a) employ any device or scheme to defraud ; (b) make a materially false statement or misleading omission ; or (c) engage in any act, practice, or course of business that would operate as a fraud or deceit on others. The SEC relies upon this section to prohibit insider trading and certain other fraudulent or manipulative practices.

A principal purpose of the *1934 Act* is to prevent the manipulation of a security's price. Generally, manipulation is an activity which has as its purpose the deliberate raising, lowering or pegging of a security's price. In essence, a manipulation is an intentional interference with the free forces of supply and demand. Section 9 (a) (1) prohibits the use of "wash sales" and "matched orders" for the purpose of creating a false or misleading appearance of active trading in any security registered on a national security exchange. Section 9 (a) (2) contains a general prohibition of manipulation of securities registered on a national securities exchange. Section 9 (a) (3) prohibits brokers or dealers (or anyone else seeking to buy or sell a security) from inducing the purchase or sale of any security registered on a national securities exchange by circulating or disseminating information to the effect that certain trading activity is occuring or will occur that will cause its price to rise or fall.

Section 9 (a) (5) prohibits the receipt of consideration from a broker-dealer or from any person to induce the purchase or sale of any security registered on a national securities exchange by the circulation or dissemination of information that certain trading is occuring or will occur that will cause the price of the security to rise or fall.

Section 9 (a) (4) prohibits brokers or dealers (or anyone else seeking to buy or sell a security) from knowingly making any false or misleading statement of material fact regarding a security registered on a national securities exchange for the purpose of inducing the purchase of the security.

Section 9 (a) (6) prohibits any person from effecting, either directly or indirectly, with one or more other persons, any series of transactions for the purchase and/or sale of any security registered on a national securities exchange for the purpose of pegging, fixing, or stabilizing the price of such security in contravention of the rules and regulations adopted by the SEC for the protection of investors. The only rule adopted by the SEC under this provision is *Rule 10 b-7*.

Section 15 (c) (1) prohibits a broker-dealer from effecting any transaction in, or inducing, or attempting to induce, the purchase or sale of any security, otherwise than on a national securities exchange, by means of any manipulative, deceptive or other fraudulent device or contrivance. Section 15 (c) (2) prohibits a broker-dealer from making fictitious quotations. The SEC must define by rules and regulations those devices or contrivances that it deems manipulative, deceptive, or otherwise fraudulent, and such quotations as are fictitious. These statutory provisions and the rules promulgated thereunder apply to the over-the-counter securities markets only.

The SEC has promulgated a number of rules pursuant to the authority granted in Sections 15 (c) (1) and (2). Rule 15 c 1-2 is a general anti-fraud provision that defines the term "manipulative, deceptive, or other fraudulent device or contrivance" as any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person and any untrue statement or omission of a material fact, which statement is made with knowledge or reasonable grounds to believe that it is untrue or misleading. The other rules promulgated under Sections 15 (c) (1) and (2) prohibit a variety of specific fraudulent or manipulative acts.

All self-regulatory organizations ("SROs"), including the New York Stock Exchange, Inc. ("NYSE") and the National Association of Securities Dealers Association, Inc ("NASD"), have adopted various rules which prohibit manipulative, deceptive, or otherwise fraudulent conduct, or conduct inconsistent with just and equitable principles of trade.

THE OFFERS AND SALES OF "PENNY STOCKS". - The United States Congress passed a new federal securities law, the *Securities Enforcement Remedies and Penny Stock Reform Act of 1990*, which, in part, creates a new regulatory scheme for penny stocks ("*Remedies and Penny Stock Act*"). "Penny stock" is a term used to refer to low priced equity securities traded in the over-the-counter market in the United States. These securities may be listed on foreign exchanges as well. The *Remedies and Penny Stock Act* addresses five main areas. In connection with broadening enforcement remedies available to the SEC generally, the *Remedies and Penny Stock Act* allows the SEC to sanction and prohibit future penny-stock activity by both associated persons of a broker-dealer and all other persons participating in an offering of a penny-stock. Second, the SEC is obligated to facilitate the establishment of automated quotation systems for penny stocks which will collect, and make available to the public, transaction and quotation information. Third, the SEC must prescribe special rules for blank check companies issuing penny stocks. Fourth, the SEC is given broad rulemaking authority to regulate penny stocks. Fifth, the SEC must adopt specific disclosure rules regarding penny stocks. These rules require, among other things, that broker-dealers selling penny stocks provide customers with the following :

- a risk disclosure document describing the risks of the penny stock market and making disciplinary information access ;

- information on the broker-dealer's bid-ask prices, if reliable ;

- information on the broker-dealer's compensation in the trade ;
- information on the salesperson's compensation in the trade ;

- information on the salesperson's compensation in the trade ;

- monthly statements giving the current market value of penny stocks held in a customer's account.

The SEC recently proposed a serie of rules on these topics. These rules have received public comments and are now being revised with a view towards final adoption. Amendments also have been made to Rule 15 c 2-11 of the 1934 Act to increase and clarify the obligations of markets makers in penny stocks. Further changes to these duties also have been proposed for public comment.

The collective effect of the major legislative and SEC rulemaking initiatives related to penny stocks is significant in two respects. When fully implemented the proposed rules will put into place a regulatory framework for penny stocks similar to exchange listed securities. In addition, these initiatives will provide investors with significant new disclosures about who they are dealing with, the market risk and what proportions of their investment dollar actually gets invested.

A.14.2 - Answer of the CFTC

The *Commodity Exchange Act (CEA)*, the CFTC's enabling legislation, establishes the fundamental regulatory framework for the sale and promotion of commodity futures and option contracts in the United States [1]. The *CEA* gives the CFTC exclusive jurisdiction with respect to accounts, agreements (including any transaction that is of the character of an option), and transactions involving contracts of sale of a commodity for future delivery, traded or executed on a contract market designated pursuant to the *CEA* or any other board of trade, exchange or market in the United States [2].

Section 4 (a) of the *CEA* requires that all domestic futures transactions be conducted on or subject to the rules of a board of trade that has been designated as a contract market by the CFTC [3].

Section 4 (b) of the *CEA* is the fundamental provision prohibiting fraud in connection with the offer or sale of futures contracts [4]. It prohibits cheating and defrauding, willfully making false reports or causing false records to be entered for any person, willfully deceiving or attempting to deceive any person, bucketing of the orders of any person, or filling such orders by offset against the orders of any other person, and willfully and knowingly, without the person's prior consent, taking the opposite side of a person's order [5]. In addition, Section 4(o) of the *CEA* specifically prohibits commodity trading advisors ("CTAs"), commodity pools operators ("CPOs") and their associated persons ("APs") from employing any device, scheme or artifice to defraud any client or participant, prospective or otherwise, and from engaging in any transaction, practice or course of business that operates as a fraud or deceit upon such client or participant [6].

With respect to options, the *CEA* prohibits offering to enter into, entering into, or confirming the execution of any option transaction involving any commodity regulated under the *CEA* in a manner contrary to any order, rule or regulation of the CFTC prohibiting any such transaction or allowing any such transaction under such terms and conditions as the CFTC shall prescribe [7]. The CFTC has promulgated rules governing the offer and sale of domestic commodity options, and, in particular, domestic exchange-traded commodity options, which prohibit, among other things, fraud in connection with entering into, offering to enter into or confirming the execution of such options, including cheating or defrauding or attempting to cheat or defraud any person, making false reports or statements to any person, deceiving or attempting to deceive any persons by any means whatsoever [8].

In addition to the prohibitions against fraud in connection with domestic futures and options products, the CFTC's regulations place significant emphasis upon disclosure of the risks associated with trading futures and options contracts. A risk disclosure statement, in the form specified in CFTC regulations, must be provided by certain registrants to each customer, and a customer account may not be opened unless the registrant has received an acknowledgement, signed and dated by the customer that such statement has been received and understood [9]. Disclosure requirements are also imposed with respect to trading in option contracts [10].

Parts 32 and 33 of the CFTC's regulations also prohibit, in relevant part, persons required to be registered from expressly or impliedly representing that CFTC has approved any commodity option transaction or that compliance by such persons with the provisions of either Part 32 or 33 constitutes a guarantee of fulfillment of any commodity option transaction [11]. Similarly, the CFTC's regulations prohibit CPOs, CTAs, and their principals or agents from representing that such CPOs or CTAs have been sponsored, recommended or approved, or that their abilities or qualifications have in any respect been passed upon, by the CFTC or the US government or any agency thereof [12].

B - SPECIFIC RULES APPLYING TO THE PROMOTION AND SALE OF FOREIGN PRODUCTS

B.1 - In AUSTRALIA, dealing in foreign securities, futures, options or other financial products are regulated in the same terms as domestic securities.

The issue of, or trading in, foreign securities and of non-existent foreign securities is governed to the extent that invitations or offers in respect of the securities are made in, or into, Australia. Supervision does not depend on listing, manipulation, or residential status. All promotion of foreign securities within Australia is governed : brokers and advisers promoting or trading in the securities are required to be licensed locally and they, and any other persons dealing with the securities, are governed by provisions regulating the form of invitations, offers etc.

Since any person trading in the securities in Australia is required to be licensed as a broker or adviser and to comply with provisions regulating the form of offers, no distinction needs to be made as to whether non residents are located in the country of product or a third country.

As with national futures contracts, foreign futures contracts are required to be traded on approved futures exchanges. Activities conducted in Australia which result in a futures contract being made in another country are subject to Australian regulation. As well, a person located in Australia who trades on a foreign futures exchange directly (i.e. by electronic connection with the exchange) would be subject to Australian regulation. In that connection, there are, in addition to approved futures exchanges located in Australia, 32 overseas futures exchanges which are "recognised" as exchanges on which Australia futures brokers are permitted to trade.

B.2 - In CANADA, ONTARIO, the *Securities Act* governs the sale of any securities to residents of Ontario, whether the securities originate within Ontario or elsewhere (see answer to Question 1-A).

B.3 - In CANADA, QUEBEC, the existing provisions governing the sale of securities are as follows.

Section 11 of the *Act* states :

> "*Every person intending to make a distribution of securities shall prepare a prospectus and obtain a receipt therefore from the Commission. The application for a receipt must be accompanied with the document prescribed by Regulation*".

This is the main condition. Section 11 of the *Act* applies equally to the promotion on the sale of foreign securities or other financial products in Québec.

AUTHORIZED PERSONS. - There is also Section 148 of the *Act* which requires dealers and advisers to be registered as such with the Commission before they can legally sell or promote securities.

DOCUMENTS TO THE PUBLIC. - Section 29 of the *Act* states that *"a dealer who receives an order to subscribe for or purchase a security offered in a distribution made in accordance with this chapter shall send to the applicant a copy of the prospectus and any amendement thereto..."*.

B.4 - In THE FEDERAL REPUBLIC OF GERMANY, see answer to Question 1 A.

B.5 - In FRANCE

a - Promotion and sale of foreign securities, futures and derivative products

The *1972 Law on canvassing of securities* forbids the promotion of foreign securities or mutual funds on the French territory when the issuance or sale of such products in France is submitted to prior consent and that this consent has not been given. This authorization is to be given by the Ministry of Finance.

The *decree of March 9, 1989* provides that such an authorization is required for issuance or introduction on the French territory of foreign securities but that exception is made to this rule :

- for securities issued by citizens of EEC Member States, by EEC institutions, and by other international organizations of which France is a member ;

- for loans benefitting from the warranty of the French State ;

- for stocks which will be assimilated to already existing stocks listed on a French exchange ;

- for securities issued by citizens of OECD.

As far as non EEC countries are concerned, exemptions imply a condition of reciprocity.

The *Law of 1989 on security and transparency of the financial market* (Article 32) modified article 18 of the *1885 Futures Markets Law*, which now provides that the French public may be sollicited under whatever form, directly or indirectly, to perform operations on foreign securities, futures or other financial products, only if the exchange concerned has been recognized according to certain conditions provided for in a decree.

This *decree, dated October 25, 1990*, provides that in order to be recognized, a foreign exchange shall fulfill two conditions (Article 1) :

- the rules regarding the protection of investors, the security and control of the transactions shall be equivalent to those existing in France ;

- French brokers shall be fairly treated on this exchange.

The decree also provides that the list of the recognized exchanges is drawn by the Minister of Finance, after consultation of the COB (Article 2).

Finally, the decree states (Article 3) that persons located outside the French territory are authorized to canvass the French public for products traded on recognized foreign markets provided that :

- they are registered with the market authorities of their home country ;

- the rules to which they shall comply (proficiency, respectability, solvency) are equivalent to those applicable in France.

A *COB Rule n° 90-10* has been approved by the Minister of Finance on September 20, 1991. It provides for the conditions to be fulfilled for the commercialization in France of foreign securities, futures or other financial products. The information to be given to the public shall be accurate, precise and honest (Article 1). The products proposed shall be adapted to the public canvassed, and the COB may forbid the commercialization of a product on which the risk has not been adequately announced (Article 2). This Rule also provides for the information to be given to the public in the document of information and for a 7 days period for further consideration (Article 3). Finally, this Rule provides for some compulsory contents of any advertising material (Article 4).

An *Arrêté of September 20, 1991* contains the list of recognized markets.

b - Promotion and sale of foreign mutual funds shares

b.1 - MUTUAL FUNDS FROM EEC MEMBER STATES. - Mutual funds originating from EEC Member States and which abide by the provisions of *EEC Directive n° 85-611 of December 20, 1985 on Coordinated Mutual Funds* do not have to comply with the French registration procedures. They shall notify to the COB their intention to canvass the public and provide the French authorities with a certificate of compliance with the Directive, issued by the relevant authorities of their home country. Provided that there is no refusal from the COB within a 2 month delay, the mutual fund may be introduced on the French territory (*COB Rule 89-2*, Article 9). They shall comply with the rules governing mutual funds in France. A *COB Instruction* provides for the information to be given to its services by the mutual funds concerned.

b.2 - NON COORDINATED MUTUAL FUNDS FROM EEC COUNTRIES. -Mutual funds from EEC countries, taking advantage of the above referenced Directive while they are not coordinated, shall provide the public with a translation into French of the document of information approved by the authority of their home country, or with any document in French approved by the COB, prior to any subscription by the public. Canvassing shall then comply with the same rules as those applicable to French mutual funds (*COB Rule 89-2*, Article 38).

b.3 - MUTUAL FUNDS FROM THIRD STATES. - Mutual funds originating from non EEC countries shall apply with the COB for an authorization prior to performing any sale or promotion to French customers.

B.6 - In **HONG KONG**, there are no specific provisions governing the promotion or the sale of foreign financial products. (see answer to Question 1 : the *Securities Ordinance* (Chapter 333) defines securities to include foreign securities).

B.7 - In ITALY, there are no specific legislative or regulatory provisions on the promotion or sale of foreign securities since the provisions of the law on the raising of funds from the public refer to domestic and foreign securities alike.

B.8 - In JAPAN, there is no specific legislation governing the promotion and sale of foreign securities. Insofar as foreign securities fall under the definition of securities within the structure of the *Securities and Exchange Law*, those would be under the regulation of the *Securities and Exchange Law*.

B.9 - In SPAIN, (translation provided), there are no specific provisions regarding the promotion and sale of foreign financial products. According to Article 3 of the LMV, provisions of this law apply to all securities which are either issued, negociated or commercialized within the territory of Spain. Similarly, Article 10.3 of the Civil Code provides that the issue of securities refers to the law of the place where it occured.

B.10 - In SWEDEN, there are no specific provisions governing the promotion or the sale of foreign financial products (see answer to Question 1 A. Update in fine for new provisions).

B.11 - In SWITZERLAND, see A.

B.12 - In THE NETHERLANDS, there are no specific provisions governing the sale of foreign securities. The *Supervision of Securities Transaction Act (SSTA)* applies when securities are offered in or from the Netherlands, without regard to the "nationality" of the security concerned.

B.13 - In the UNITED KINGDOM, the *Financial Services Act* contains certain restrictions on the promotion of foreign life insurance in the UK. For other types of investment business, the key factor is the location of the investment business (and hence whether or not the firm doing it requires authorisation) rather than the origin of the product. UK private customers are protected in relation to overseas firms by the restrictions on advertising and unsollicited calls. Private customers are forewarned in relation to unregulated overseas business carried on by UK authorised firms through a prescribed disclosure requirement provided by the relevant firm.

B.14 - In THE UNITED STATES

B.14.1 - Answers of the SEC

Offers and sales of foreign securities in the United States are subject to the registration requirements of the *1933 Act* to the same extent as securities of domestic issuers. Separate registration forms are available for use by foreign issuers, and certain accomodations have been made to foreign issuers in several categories of required disclosure (e.g., management

remuneration, segment reporting and related party transactions) and in the use of home country financial statements with reconcilitation to US generally accepted accounting principles. The provisions of the *1933 Act* relating to sales of, or written or oral offers to sell, securities, apply to foreign as well as domestic securities.

[With respect to the registration of brokers and dealers, including those located outside of the US and/or selling foreign financial products, see Working Party n° 7 "Collated Summary of Responses to Common Framework of Anaysis", May 21, 1990 (WP7 Summary"), pp. 25-26].

Mutual funds. - Any investment company that proposes to use the mails or any means or instrumentality of interstate commerce ("US jurisdictional means") in connection with a public offering of its securities must comply with all the provisions of the 1933 and 1940 Actsof US jurisdictional means in connection with a public offering of its securities is required to register with the SEC under the *1933 Act* and the *1940 Act* unless excepted or exempted from registration. Specifically, the investment company must register under the *1940 Act*, while the shares it offers to the public must be registered under the *1933 Act*.

Advisers Act. - A registered investment adviser that gives advice about foreign securities is subject to the same regulation as other registered investment advisers.

B.14.2 - Answer of the CFTC

Yes. Section 4 (b) of the *CEA* permits the CFTC to adopt certain rules and regulations imposing requirements regarding the offer and sale in the United States of futures contracts that are traded on or subject to the rules of a board of trade, exchange or market located outside the United States [13]. The requirements of Section 4 (c) (b) of the *CEA* noted above concerning transactions in options also apply with equal force to transactions involving foreign options [14]. The CFTC has promulgated rules concerning the offer or sale of foreign futures and option contracts, which are found in Part 30 of the CFTC regulations [15]. In particular, Part 30 expressly prohibits fraud in connection with foreign futures or option transactions [16]. In addition, risk disclosure statements regarding foreign futures and option transactions, in the form approved by the CFTC, are required to be delivered to customers by FCMs, IBs, CPOs and CTAs, and by those proceeding under the alternative procedures for non-domestic persons in Part 30 [17]. The CFTC consistently has included such a requirement in its exemptive orders under Part 30 [18].

(1) - 7 USC § 1 et seq. The CEA does not govern or apply to transactions in foreign currency, security warrants, security rights, resales of installment loan contracts, repurchase options, government securities, or mortgages and mortgage purchase commitments, unless such transactions involve the sale thereof for future delivery conducted on a board of trade. 7 USC § 2 (A) (1). In this regard, note that the CFTC has reaffirmed its view that this provision is not applicable when such transactions involve members of the general public. 50 Fed Reg 42963 (October 23, 1985). In addition, forward contracts are excluded from the definition of "future delivery" in the CEA. 7 USC § 2 (A) (1).

(2) - 7 USC § 4 (a) (1). The CEA does not apply to and the CFTC has no jurisdiction to designate a board of trade as a contract market for any option on one or more securities, including any group or index of such securities, or any interest therein or based on the value thereof. 7 USC § 2 a. The CFTC does have jurisdiction, however, and may designate, absent objection from the SEC, a board of trade with respect to any contract of sale (or option on such contract) for future delivery of any group or index of securities (or any interest therein or based upon the value thereof). 7 USC § 2 a. The CEA also prohibits contracts of sale (or options on such contracts) for future delivery of any security, or interest therein or based upon the value thereof, except an exempted security under relevant US securities laws. Id. The CFTC also has jurisdiction over options on foreign currencies other than those traded on a national securities exchange. 7 USC § 6 c (f). The CFTC must consult with the US Department of the Treasury and with the Board of Governors of the Federal Reserve System in the case of an application from an exchange for designation of a contract market with respect to transactions for future delivery of any security issued or guaranteed by the United States or any agency thereof. 7 USC § 4 a.

(3) - 7 USC § 6 (a).

(4) - 7 USC § 6 (b).

(5) - 7 USC § 6 (b).

(6) - 7 USC § 6 (o).

(7) - 7 USC § 6(c)(b).

(8) - 17 CFR § 32.9 (commodity option transactions in interstate commerce generally) and 17 CFR § 33.10 (commodity options traded on domestic exchanges). Note that Part 32 also generally prohibits options on certain agricultural products. 17 CFR § 32.2.

(9) - 17 CFR §§ 1.55 (futures commission merchants ("FCMs") and introducing brokers ("IBs"), 4.21 (CPOs), and 4.31 (CTAs).

(10) - 17 CFR §§ 32.5, 33.7.

(11) - 17 CFR §§ 32.8, 33.9.

(12) - 17 CFR § 4.16.

(13) - 7 USC § 6 (b).

(14) - 7 USC § 6 (c) (b).

(15) - 17 CFR §§ 30.1 et seq.

(16) - 17 CFR § 30.9.

(17) - 17 CFR §§ 30.5, 30.6.

(18) - 17 CFR § 30.10. See e.g. Order Under CFTC Rule 30.10 Exempting Firms Designated by the Sydney Futures Exchange Ltd., No 7 1988 ; 53 Fed Reg 44856. One of the elements of a comparable regulatory scheme identified by the CFTC is minimum sales practice standards, including disclosure of the risks of futures and options transactions, and, in particular, the risk of transations undertaken outside the jurisdiction of domestic law. See Appendix A - Part 30 - CFTC Interpretative Statement With Respect to the Commission's Exemptive Authority Under Section 30.10 of Its Rules.

QUESTION 2

Do these activities require authorization by or registration with a supervisory authority ?

2.1 - In AUSTRALIA, these activities do require registration.

2.2 - In CANADA, ONTARIO, the *Securities Act* prohibits persons from trading in securities unless they are registered with the Ontario Securities Commission (see answer to question 1).

2.3 - In CANADA, QUEBEC, the activities of distribution of any securities in Québec require the preparation of a prospectus which has to be approved by the Commission des Valeurs Mobilières du Québec (CVMQ) by means of a visa and a person exercising the activities of a broker in Québec must be registered as such with the same Commission.

2.4 - In THE FEDERAL REPUBLIC OF GERMANY, the German credit institutions are subject to licensing and regular monitoring by the Federal Banking Supervisory Office in their dealings in securities with their customers. Middlemen who professionally broker the purchase of investment shares, stocks and bonds of corporations need a permit from the trade supervisory authority.

2.5 - In FRANCE, any person who proposes securities, futures, or derivative products on behalf of a bank, broker, portfolio manager, commissioner or mutual fund has to be declared by his employer to the French Department of Justice (*1972 Law on canvassing of securities*, Article 8 ; *1885 Futures Markets Law*, Article 13).

The firms themselves have to be registered with the competent supervisory authority :

- the Banking Comity for the banks (*1984 Banking Law*, Article 15 § 1),

- the Stock Exchange Council - CBV - (*1988 Securities Markets Law*, Article 4) or the Futures Exchange Council - CMT - (*1885 Futures Markets Law*, Article 8 and Article 8-1) for the brokers,

- the COB for the portfolio managers (*1989 Law on security and transparency of the financial market*, Article 23) and mutual funds (*1988 Law on Mutual Funds*, Article 24).

2.6 - In HONG KONG, the activities do not require authorization as such, except that :

(a) Certain advertisements in relation to securities, and advertisements promoting investment arrangements, can only be issued subject to authorization by the SFC. A failure to obtain such an authorization would result in a breach of section 4 of the *PIO*.

(b) To market unit trusts and mutual funds requires the SFC's authorisation under Section 15 of the *SO*. Promotion of unauthorised trusts/funds would be in breach of Section 4 of the *PIO*.

(c) Any prospectus issued under the *Companies Ordinance* must be registered with Hong Kong's Registar of Companies.

However, persons who perform such activities in Hong-Kong do require registration, brief details of which are as follows :

(a) Securities. - A person (either an individual or corporation) who carries on a business of :

- dealing in securities in Hong-Kong,

- acts as an investment adviser in Hong-Kong,

must be registered with the SFC. Also, any person acting as a representative must be registered.

Certain persons can apply for exempt dealer, and investment dealer status, in very restricted circumstances. These would never apply to boiler room operations.

(b) Commodities. - A person

- who carries on a business of trading in commodity futures contracts,

- acts as a commodity trading adviser,

must be registered with the SFC. Also, any person acting as a representative must be registered.

2.7 - In ITALY, only securities investment firms authorized in accordance with Articles 1 and 2 of *Law 1/1991*, credit institutions authorized in conformity with Article 16 of the same law, the Community banks and securities firms subject to mutual recognition under articles 13 and 14.l.1.131/92 and alos authorized no Community banks may engage in the underwriting and distribution of securities with or without firm commitment underwriting or standby commitments to issuers, taking orders to buy or sell securities, advisory services, raising funds from the public by means of activities that may also be promotional in nature and carried on in a place different from the legal head office or principal administrative establishment of the issuer, offeror or person marketing the investment.

When raising funds from the public by way of door-to-door methods, securities investment firms and credit institutions must use only the services of financial salesmen regulated in accordance with the provision of Article 5 of *Law 1/1991*.

2.8 - In JAPAN, Article 28 of the *Securities and Exchange Law* prescribes that no person other than a joint stock corporation licensed by the Minister of Finance shall engage in the securities business.

2.9 - In SPAIN, (translation provided), as far as the primary market is concerned, both the promotion and the bringing into circulation of securities which are considered as public offer, require verification by and registration with the CNMV, its authorization being also necessary in certain cases. In that sense, conditions provided for in Article 26 of the *LMV* apply to all issues, whether they are to be traded on an official exchange or not.

As far as the general procedure of registration is concerned, it is as follows.

SCOPE. - The procedure applies to all new issues of securities of set or varying price, aimed at collecting funds from private investors residing on the territory.

MATERIALS SUBJECT TO REGISTRATION REQUIREMENTS. - Before any securities be offered to the public, a preliminary condition is that it should be registered with the CNMV. Every time the issue has the characteristics of a public offer, the above condition is independent from the trading or not on an official exchange.

The official registration of an issue of securities requires the presentation of the following documents :

- communication of the project of issue,
- documents justifying agreement on the issue and the characteristics of securities,
- report on the audit of the statements of accounts of the issuer,
- prospectus of information on the issue and the issuer.

Once these documents are registered with the CNMV, they are at the disposal of the public for consultation and information.

PROCESS AND DELAYS. - The issuer shall send the documents to the CNMV enough in advance. In this view, the issuer will have to pay attention to the 10 days delay before the opening of the subscription, delay necessary for fufilling the publicity formalities in the BOE (Bulletin Officiel de l'Etat/State Official Register) and in one national newspaper, at least.

Once the issuer has completed these information duties, the CNMV has a one month delay past which, absent any objections addressed to the CNMV, the registration will be considered done.

As far as the contents of the registered documents are concerned :

COMMUNICATION OF THE PROJECT OF ISSUE. -

a - Condition of registration according to the nature of the issuer. Registration will not be necessary for issues performed by the State, the Autonomous Communities and International Organizations to which Spain is a participant. As for other issuers, they need to officialy register with the CNMV.

b - The project should respect certain caracteristics and contain certain documents or information.

RELEVANT DOCUMENTS TO BE PROVIDED. -

a - Condition of registration according to the nature of the issuer. Same as above.

b - The project should respect certain caracteristics and contain certain documents or information.

AUDITS. -

a - Condition of registration according to the nature of the issuer. Same as above.

b - The project should respect certain caracteristics and contain certain documents or information.

PROSPECTUS OF INFORMATION. -

a - Condition of registration according to the nature of the issuer. Same as above, but for International Organizations to which Spain is a participant, provisions of an Order of the Minister of Economy of February 3, 1987 are also applicable.

b - The characteristics of the information should be incorporated in the prospectus.

c - Publicity and diffusion of the prospectus : the prospectus is the basic document for the publicity of the issue. In annex to the prospectus, the following information should be provided :

- the publication which will be made in the newspapers and in the BOE, containing the main characteristics of the project;

- a presentation of the type of advertising used to call the attention of the public on the operation. The issuer may not advertise for the promotion of the operation before registration of all information documents with the CNMV.

Any advertising , made through any means, shall be based on the information contained in the prospectus of information and will have to be presented in such a way that it does not deceive about the characteristics of the issue or of the situation of the issuer.

Any advertising concerning the operation, shall indicate that the prospectus of information has been registered with the CNMV and also the place where the prospectus may be obtained for free.

The prospectus of information, registered with the CNMV shall be put at the disposal of the potential subscribers, at least in the offices of the issuer and in those of the intermediaries taking part in the placing of the issue.

d - Information contained in the prospectus shall follow the structure provided for in the *Ministerial Order of November 17, 1981*.

e - Informative contents of each chapter of the prospectus: in all cases of prior registration of the prospectus, the contents of its chapters shall follow that provided in the Order mentioned above.

Nevertheless, certain contents mentioned in this Order shall be changed according to the new provisions of the *LMV*.

As far as the secondary market is concerned, a distinction should be made between ordinary and special operations.

Ordinary operations. -

Ordinary operations are transfers of securities within a sale of securities, in cases where the concerned securities are or are not traded on an official exchange.

a - SALE.- This type of operations does not require, in itself, any authorization by a supervisory authority, since it may be performed only by certain entities, as was mentioned in the answer to question 1. All these operations need to be archived and every receiver of an order shall have a copy of them together with their incidences (Article 2 of the *Royal Decree 1849/80*). A project of *Circulaire sur les Registres Obligatoires et Normes avec la Clientèle (Circular on Compulsory Registries and Standards in Relation With Customers)*, which should be approved soon, provides that entities receiving and executing orders of the clients for the buying and selling of securities, shall keep a register which shall contain, apart from the information contained in the orders received, the identification of the person giving the order and the intermediaries which took part in the operations, as well as all incidences of the operation.

The CNMV has access to these operations since, pursuant to Article 85 of the *LMV*, it may require from legal and natural persons, any information that it considers necessary concerning the matters dealt with in this law.

b - PUBLICITY.- The publicity of the ordinary operations is made through the Bulletin Officiel de Cotation (Official Quote) which the Commerce Exchanges publish every day of session.

Special Operations. -

Special operations are the following : Takeovers, Public Offer of Sale, Admission to trading, Applications off market, Notation.

As far as takeovers are concerned, this operation is governed by Article 60 of the *LMV* and regulated by the *Royal Decree 1197/1991*. The authorization as the promotion for such operation is provided for in Chapter II "Preparation and authorization of the Offer" of said decree.

Public Offers of Sales are dealt with in Article 61 of the *LMV* and are subject to all provisions regarding new issues of securities, Title III of the *LMV*, developped recently by *Royal Decree 291/1992*. Consequently, all that has been explained above concerning the primary market is applicable to the promotion and authorization of a public offers sales.

Admission to trading on an official secondary market, mentioned in Article 32 of the *LMV*, requires prior verification by the CNMV and shall fulfill the conditions set forth in Article 26 of the *LMV* on the issue of securities. The process of authorization for such admission, as well as the publicity to be given to it, are those explained above for the primary market.

Applications off market, governed by *Royal Decree 1416/1991* do not require authorization and are allowed whenever they fulfill the conditions set forth in Article 2 of said decree. The publication of the details of this operation is done by the company managing the exchange before the pre-opening session of the next day following the application.

Article 36 of the *LMV* refers, in its paragraph d -, to operations of buying and selling in which the compulsory participation of a member of the exchange consists in taking note of the conditions of the contract concluded between those who are not members of the exchange. Notation is not subject to authorization, unless it fulfill some conditions contained in *Royal Decree 1416/1991*. Regarding the publication, once the communication is received, the company managing the exchange publishes it.

2.10 - In SWEDEN, these activities require the authorization by and the registration with the Financial Supervisory Authority of Sweden. By this authorization, the following business activities are licensed :

- trade in financial instruments on behalf of another person but in one's own name ;

- brokering of contracts between buyers and sellers of financial instruments or otherwise assistance in transactions concerning such instruments ;

- trade in financial instruments for one's own account ;

- management of financial instruments belonging to another person ;

- certifying or other form of assistance at stock issues or offers for buying or selling of financial instruments for free trade.

2.11 - In SWITZERLAND, having no specific provisions for the sale and promotion of securities implies that no existing supervisory authority delivers authorizations or carries out any registration at the federal level.

2.12 - In THE NETHERLANDS, under the SSTA, brokerage and portfolio management activities need authorization by the Securities Board of The Netherlands (STE). The issue of Securities does not need authorization of the STE.

Furthermore, the STE keeps a register listing the brokers and portfolio managers who are entitled to offer or perform services pursuant to a license or exemption (section 15, SSTA).

2.13 - In the UNITED KINGDOM, these activities require authorisation and registration.

2.14 - In the UNITED STATES

2.14.1 - Answer of the SEC

Yes. The *1934 Act* provides a comprehensive statutory scheme for the regulation of US broker-dealers. One important aspect of that regulatory scheme provides for broker-dealer registration. Section 15 (a) of the *1934 Act* makes it unlawful for any "broker" or "dealer" to use the mails (or any other means of interstate commerce) to transact a business in securities unless such broker or dealer registers with the SEC. Generally speaking, a broker is defined

as one who acts in an agency capacity, while a dealer is defined as one who acts in a principal capacity. Banks are specifically excluded from the coverage of these definitions. Section 15 (a) also contains two statutory exemption from registration. These exemptions apply to : 1) broker-dealers whose business is solely intra-state (e.g. whose business takes place only within the boundaries of one State), and 2) natural persons who work for a broker-dealer. (Such "associated persons" register only with the national securities exchange or association of which their employer is a member).

Section 15 (a) also excludes certain specified types of securities transactions from its scope. Business in commercial paper transactions, bankers' acceptances, or commercial bills does not, by itself, require broker-dealer registration. In addition, business in certain "exempted securities" (which is defined in Section 3 (a) (12) of the *1934 Act*) does not require registration under Section 15 (a), although registration may be required under other *1934 Act* provisions (see following paragraph).

MUTUAL FUNDS. - Any investment company that proposes to make use of US jurisdictional means in connection with a public offering of its securities is required to register with the SEC under the *1933 Act* and the *1940 Act* unless excepted or exempted from registration. Specifically, the investment company must register under the *1940 Act*, while the shares it offers to the public must be registered under the *1933 Act*.

A foreign investment company that proposes to make use of US jurisdictional means in connection with a public offering may not offer or sell its securities without obtaining an SEC order under Section 7 (d) of the *1940 Act* allowing the company to register and to make such an offering. In this regard, a foreign investment company that uses US jurisdictional means in connection even with a private offering of its shares that results in more than 100 beneficial owners of the fund's shares who are resident in the US also would be required to obtain an SEC order under Section 7 (d).

ADVISERS ACT. - The *Advisers Act* generally prohibits any investment adviser, unless registered with the SEC, from using US jurisdictional means in connection with its business as an investment adviser. Section 202 (a) (11) of the *Advisers Act*, in relevant part, defines an investment adviser as "any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities...".
See also the answer to question 1 above.

2.14.2 - Answer of the CFTC

Yes. The *CEA* requires persons who act in the capacity of FCMs, IBs, CTAs, CPOs, and APs of such persons with respect to domestic futures or option contracts to register in the appropriate category with the CFTC. Similarly, persons who engage in the offer and sale of foreign futures or option contracts to US customers in the capacity of FCMs, IBs, CPOs or CTAs, or APs of such persons must also register [19]. Alternative procedures may be available to IBs, CPOs and CTAs located outside the United States [20]. In addition, foreign firms may apply for exemption from registration under the procedures and principles set forth in part 30 [21].

(19) - 17 CFR § 30-4.
(20) - 17 CFR § 30-5.
(21) - 17 CFR § 30-10.

QUESTION 3

If they do, what are the requirements to be met ?

3.1 - In AUSTRALIA, offerings of new securities require lodgement and registration of a prospectus with the Australian Securities Commission.

Secondary offerings of securities must be accompanied by a prospectus or be made through listing on an approved securities exchange.

Futures contracts must be traded on approved futures exchange.

Securities and futures brokers must be members of approved exchanges and their representatives and non-broker dealers and investment and futures advisers must be licensed.

3.2 - In CANADA, ONTARIO, applications for registration of persons who trade in securities are reviewed for honesty, financial integrity and educational qualifications. Prospectuses filed with the Commission by companies wishing to distribute securities are reviewed to ensure that they contain full, true and plain diclosure concerning the company, its principals and the securities being offered. This disclosure includes audited financial statements and full disclosure of the use of proceeds from the distribution of securities including the payment of sales commissions and underwriting fees.

3.3 - In CANADA, QUEBEC, the requirements to be a broker are as follows.

NATIONALITY. - Section 203 of the *Regulation* states that "*a securities dealer or adviser must have a principal establishement in Québec, under the direction of a person who is an officer residing in Québec*". And, according to Section 204 of *the Regulation* "*an applicant who applies for registration as a representative of a dealer or an adviser (...) must be resident in Québec*".

AGE. - According to Section 204 of the *Regulation*, "*an applicant who applies for registration as a representative of a dealer or an adviser must be at least 18 years old...*".

EDUCATION. - And finally, "*he must have successfully completed the courses that would in the opinion of the Commission give him an adequate professional training*" (Section 205 of the Regulation).

3.4 - In THE FEDERAL REPUBLIC OF GERMANY, the licensing of credit institutions depends on the usual preconditions of sufficient equity capital and the reliability and professional qualification of the management. Under Section 34 c of the *Trade Regulation Act*, the trade supervisory authority may not grant a permit for middlemen who broker investment shares, stocks and bonds of corporations if the applicant does not possess the necessary reliability for the trade or if his finances are not in order.

3.5 - In FRANCE, the persons employed by banks, brokers, portfolio managers, commissioners or mutual funds wishing to promote financial products shall be French citizens or citizens of an EEC Member State, and aged of more than 18 years. They shall not be barred from performing banking activities (*1885 Futures Markets Law*, Article 13 ; *1972 Law on canvassing of securities*, Article 8).

The firms themselves have to abide by many requirements ranging from prudential ratios, to capital adequacy thresholds and professional rules. Nevertheless, these requirements are not directly linked to this specific activity.

3.6 - In HONG KONG, pursuant to Section 23 of the *Securities and Futures Commission Ordinance (SFCO)*, the Commission shall refuse to register a person as a dealer, adviser or representative unless they are considered fit and proper. In considering fitness and properness, the SFC will take into account such matters as a person's :

- financial status,
- his educational or other qualifications, or experience, having regard to the nature of the function to be performed,
- his ability to perform such functions efficiently, honestly and fairly,
- his reputation, character, financial integrity and reliability.

In addition, the *SFCO* empowers the SFC, in considering the fitness and properness of a corporate applicant, to look through to the fitness and properness of the substantial shareholders, directors and officers of the company and of other companies in the same group. The SFC has established "fit and proper criteria" and these are used to assess all applicants for registration in whatever capacity.

In regard to registration as dealers, there are additional requirements that must be met by applicants, namely :

SECURITIES DEALERS. - An individual applicant must demonstrate that :

- He has sufficient qualification or experience in dealing in securities [experience required is 3 years experience in dealing in securities in Hong-Kong or on any stock exchange recognized by the SFC ; or he has passed an examination approved for this purpose by the SFC.
- He is able to demonstrate a net capital in his business of not less than HK $ 1 million.

A corporate applicant must :

- be a registered company in Hong-Kong (this would include both local companies and overseas companies registered under the provisions of *HK's Companies Ordinance*) ; and

- have every director , who actively participates in or is directly responsible for the supervision of the dealing business, registered as a dealer ;

- be able to demonstrate a net capital in its business of not less than HK $ 5 million.

COMMODITIES DEALERS. - Currently, there are no capital adequacy requirements for commodities dealers although these are likely to be introduced in the near future. To become a dealer, an applicant, corporate or individual must :

- either be a member of the Hong Kong Futures Exchange Limited ; or
- of any other exchange specified in the *CTO*. In the case of a corporation seeking registration, it can be a wholly owned subsidiary of a member of such overseas exchange.

In addition, a corporation may not carry on a business as a dealer unless every director or employee who is responsible for the company's business of trading in commodity futures contracts is registered as a dealer.

3.7 - In ITALY, operators have to be specifically authorized in order to engage in the activities listed above.

Securities investment firms have to be listed in a special register kept by the CONSOB.

The law requires securities investment firms to comply with capital adequacy requirements and their directors and controllers to satisfy requirements regarding their professional competence and good reputation.

In the case of credit institutions, authorization to engage in securities business is in addition to that required to engage in credit business and is granted in accordance with the conditions and procedures laid down by the Bank of Italy.

3.8 - In JAPAN, criteria of licensing and reasons for rejecting licenses are prescribed in the *Securities and Exchange Law*, as follows :

- CRITERIA FOR LICENSING. -

Article 31.

1 - That the applicant for licenses shall have financial resources sufficiently large to conduct the business applied for on a sound basis and the prospect of its profitability shall be reasonably hopeful.

2 - That judging from the personel composition, the applicant shall have sufficient knowledge and experience to perform the service of the business fairly and precisely, and that he enjoys a good social standing.

3 - That the securities business for which the license is applied shall be necessary and appropriate in light of the given state of securities trading, the number of existing securities corporations and their business offices, and other economic conditions of the area in which the applicant may be engaged in the securities business.

- REASONS FOR REJECTING LICENSES. -

Article 32.

1 - In case the applicant is not a stock corporation, the amount of whose stated capital is such or more than as prescribed by *Cabinet Order* as necessary and appropriate in the public interest or for the protection of investors, in view of the concerned kind of license, type of business and location of business office.

2 - In case the applicant is a corporation which had been fined under the provisions of the *Securities and Exchange Law* and for which a period of five years has not elapsed since the execution was completed or exempted.

3 - In case the applicant is a corporation for which, in accordance with the provisions of Paragraph 1 of Article 35, all of its licenses or a license of the same kind as that applied for, had been cancelled and a period of five years has not elapsed since the date of such cancellation.

4 - In case the applicant is a corporation, anyone of whose directors or statutory auditors falls under a bankrupt and has not been rehabilitated.

3.9 - In SPAIN, see question 2.

3.10 - In SWEDEN, the Financial Supervisory Authority has, in the beginning of July 1991, edited its advising rules concerning how to apply for license to do securities business in accordance with the law (1991 : 981) [*Act on Securities Business*.]. Briefly speaking, the requirements concerning the persons active in the firm there are within the licensing procedure questions of ownership, company statutes, company name, company finances including capital adequacy, management of deposits of clients and in connection with ethical aspects even two points concerning criminal activity and court processes.

Another main area of the advisory rules about authorization comprehends the performance of planning business : which persons will be responsible for each business branch and organisation unit, enforcement activities, commissions and other fees, international trade, risk management and so on.

3.11 - In SWITZERLAND, see answer to question 2.

3.12 - In THE NETHERLANDS, it is prohibited to offer brokerage services or portfolio management services in or from The Netherlands beyond a restricted circle without a license. A license will be granted by the Securities Board of The Netherlands if the applicant complies with the requirements in respect of : a) expertise and integrity, b) capital adequacy, c) organization and d) information to be supplied to the public. The requirements are provided for in the *Supervision of Securities Trading Decree* (Section 6 and Section 10), and further elaborated in the RSST.

The prohibition will not apply to brokers and portfolio managers, who are member of the Exchanges, insofar the services are offered with regard to securities which are admitted to the listing of the Exchanges. The members of the Exchanges are subject to the regulations of these Exchanges and directly supervised by them (Section 8 and Section 12. *SSTA*). The requirements for a license as a broker or a portfolio manager do not differ substantially from the regulations of the Exchanges.

Furthermore, the prohibition will not apply to brokers and portfolio managers exempted by the ER. For brokerage activities the following exemptions are applicable :

1. credit institutions which are not member of an Exchange ;

2. members of a securities exchange within the European Communities, in so far as the offering or performing of brokerage services relates to the trade in securities which are admitted to the official listing on the relevant exchange ;

3. natural or legal persons who introduce clients to an investment firm which is entered in the register kept by the STE ;

4. natural or legal persons who introduce clients to an investment firm which is member of an Exchange ;

5. natural or legal persons offering their services to professionals ;

6. private venture capital companies, in so far as the offering relates to shares in the issued capital of the relevant private venture capital company.

The exemptions mentioned under 3, 5 and 6 also apply if the activities offered concern portfolio management activities.

The exemptions are subject to restrictions provided for in the ER. The ER also provides for conditions attached to exemptions.

3.13 - In the UNITED KINGDOM, successful applicants have to be "fit and proper" *i.e.*, honest, competent and solvent and to be able and willing to comply with the regulator's rules.

3.14 - In the UNITED STATES

3.14.1 - Answer of the SEC

In order to register in the US, **broker-dealers** must meet capital requirements set by the SEC and operational requirements of the relevant SROs. Broker-dealers and the people "associated" with them, may be disqualified based on past conduct, such as violations of the securities laws of the US or foreign countries. In addition, associated persons must pass tests for competence that are given by the SROs. (See also WP7 Summary pp. 195-196).

MUTUAL FUNDS. - An **investment company** must file with the SEC a "notification of registration" and a registration statement on a prescribed form. Once registered, an investment company may not offer or sell its shares unless it does so in compliance with the provisions of the *1933 and 1940 Acts*. The requirements of the *1940 Act* with respect to the structure and operation of an investment company are too detailed to list here. The SEC has compiled, and will provide on request, an "*Investment Company Registration Package*", which contains a copy of the *1940 Act* and other useful information.

Before ordering that a **foreign investment company** can register, the SEC is required, under Section 7 (d) to make a finding that the registration would be consistent with the public interest and the protection of investors and that it would be both "legally and practically feasible effectively to enforce" the provisions of the *1940 Act* against the foreign investment company if the order were granted. In effect, the SEC must find that investors in the foreign investment company have the same protections as investors in domestic investment companies.

ADVISERS ACT. - There are no special requirements (minimum capital, formal training...) that must be met in order to register as an **investment adviser**. The adviser must file a registration form and pay a one-time fee of $ 150. The form requests information about the nature of the adviser's business, any disciplinary information, and other relevant disclosures (such as the business and educational background of the advisers).

3.14.2 - Answer of the CFTC

CFTC registration requirements are adressed in detail at pages 172-176 of the "Collated Summary of Responses to Common Framework of Analysis and Cross Regulatory Summary Chart", prepared by IOSCO Working Party Number 7 in June 1990 ("Collated Summary").

QUESTION 4

Are authorized/registered firms subject to ongoing monitoring of their marketing and sales practices ?

4.1 - In AUSTRALIA, there is such a monitoring. It is conducted by the self-regulatory organisations. The Australian Securities Commission has commenced a national programme of licence holder surveillance.

4.2 - In CANADA, ONTARIO, registered dealers which are members of the Investment Dealers Association of Canada or The Toronto Stock Exchange, are subject to regular audit and compliance checks by those SROs. All firms must file with the Ontario Securities Commission annual financial questionnaires. Complaints from customers are investigated by the SROs and by the OSC. The market surveillance departments of the OSC and The Toronto Stock Exchange monitor trading in securities on The Toronto Stock Exchange and the over-the-counter market.

4.3 - In CANADA, QUEBEC, the Québec Securities Commission, the Montréal Stock Exchange and the Investment Dealers' Association all monitor the activities of registered brokers and salesmen which are also subjected to regular inspections by them.

POWERS OF SECURITIES AUTHORITIES. -

(a) - QUEBEC SECURITIES COMMISSION. - Section 11 of the *Act*, as we said previously, provides that "*every person intending to make a distribution of securities shall prepare a prospectus and obtain a receipt therefor from the Commission*".

Section 13 prescribes that "*a prospectus must contain the information and certificates prescribed by Regulation*".

And according to Section 15 of the *Act*, "*the Commission shall refuse to issue a receipt if it believes*", for instance "*the prospectus does not conform to this Act or to the Regulation there under...*".

"*When a material change occurs in relation to the information presented in the prospectus*", the amendement made there into requires a receipt from the Commission (Section 25 and 27 of the *Act*). Section 196 of the *Act* provides that a person is guilty of a penal offence who in different kinds of prospectuses makes a misrepresentation that is likely to affect the value or the market price of a security. Section 271 of the *Act* provides that the Commission may order a registrant to submit any advertising document before using it.

(b) - MONTREAL STOCK EXCHANGE. - Section 9452 of the Montreal Stock Exchange Regulation (MSER) provides for immediate disclosure of material information. There must be a public disclosure of any material information (Section 9453 MSER) followed by cease tradings if necessary (Section 8456 MSER).

Regulation provides also a provision for disclosure of conflicting interests that may arise with a client (Section 4052 MSER).

(c) - INVESTMENT DEALERS'S ASSOCIATION (IDA). - According to Section 2 of the Investment Dealer's Association (IDA) the objects of the Association shall be, among other things :

"*To encourage through self-discipline and self-regulation a high standard of business conduct among members and their partners, directors, officers and employees and to adopt, and enforce compliance with, such practices and requirements as may be necessary and desirable to guard*

against conduct contrary to the interest of members, their clients or the public..." The IDA has established some basic managment and accounting rules (for instance status XXXIX, XIX, VI, XXXV, etc) aimed to the service of all members and that could be, in some cases, the basis for disciplinary action (status XIX).

By-law n° 19 provides that each member shall be responsible for all acts and omissions of all officers and employees of the member.

4.4 - In THE FEDERAL REPUBLIC OF GERMANY, credit institutions which deal in securities with customers are subject under the *German Banking Law* to an annual audit into the orderly transaction of their securities business.

Middlemen who are licensed pursuant to Section 34c of the *Trade Regulations Act* to broker investment shares, stocks and bonds are audited once a year by an auditor. The audit also covers the obligations of the middlemen to his customers laid down in the decree on brokers and builders.

The trade supervisory authority uses the auditor's report to check whether the investment broker is still reliable and takes measures needed to protect the investors (warning to observe regulations, imposing a fine, or, as a last resort, revocation of the trading license).

4.5 - In FRANCE, the supervisory authorities may check if the firms which are within the scope of their jurisdiction abide by the professional rules they are submitted to.

Furthermore, within the scope of its general duty to protect savings invested in financial products, the COB may decide to conduct an investigation on the marketing practices of a firm if it has reasons to suspect that securities, futures, derivative or other financial products have been proposed to customers in violation of one of the provisions mentioned in the answer to question 1. The COB also has a general duty to monitor the information given by listed companies. The COB may ask these companies to modify or correct some information they provided the public with. It may also bring to the attention of the public the observation adressed to one of these companies, or any information it deems necessary to provide the public with (*1967 Ordinance*, Article 3). A similar monitoring power over information given on foreign products is also given to the COB (*COB Rule n° 90-10* Article 5).

4.6 - In HONG KONG, the accounting procedures pertaining to marketing and sales are subject to routine compliance checks. However, there is no direct monitoring of their marketing and sales practices.

4.7 - In ITALY, in the exercise of their securities business, securities investment firms and credit institutions are subject to the supervision of the CONSOB for matters concerning information requirements and transparency and to that of the Bank of Italy for matters concerning monetary stability.

On the specific question of offering securities to the public, Article 1/18 (4) of *Law 216/1974* provides that, for as long as the offer is in force, the offerer must comply with the requirements laid down in the same law in Articles 1/3 (b and c) concerning the publication of information and the CONSOB's right to information and Article 1/4 concerning the transmission to the CONSOB of annual and half-year reports and the notification of proposed changes in the company's memorandum of association, bond issues and mergers, etc.

As regards the control of selling activities, the power granted to the CONSOB to carry out on-site inspections is especially important. Such on-site controls serve both to verify the propriety of the activity of the intermediary and its behaviour towards customers and to verify that the financial product actually offered corresponds to that described in the prospectus.

4.8 - In JAPAN, these activities are subject to monitoring of the Ministry of Finance, self-regulatory organizations such as the Japan Securities Dealers Association and stock exchanges, concerning their marketing and sales practices.

4.9 - In SPAIN (translation provided), on the primary market, entities who wish to promote and put into circulation securities within the framework of a public offer, either through admission to trading on an exchange or not, are subject to a supervision of these operations.

As far as the secondary market is concerned, distinction should be made between ordinary and special operations.

As far as ordinary operations require the participation of a dealer or brokerage house member of the exchange, or of the one who certifies the authenticity in case of transfer of securities, these operations are subject to the supervision of the CNMV.

As far as special operations are concerned, the conditions under which they are performed (see above) imply supervision by the CNMV.

Concerning other market activities, article 71 of the *LMV* provides for a list of activities that may be performed by dealers or brokerage houses, if they are member of an exchange. Article 76 provides for exceptions, since it lists other entities which may perform activities of Article 71. The concerned activities may not be performed regularly by entities or persons other than these. A *Royal Decree 276/89* provides that there is regular activity when activities of article 71 go hand in hand with commercial actions, advertising, in view of creating relations with the customers.

Royal Decree 276/89 provides that natural and legal persons may represent dealers and brokerage houses within the scope of their activity. However, it should be noted that the operations performed by these persons will be made on behalf of the one they represent and will be included in the accounting of the latter, with no delay, according to the dates, and in conformity with the *Circular 7/89*.

For all these reasons, persons or entities which may perform all or part of activities of article 71 are authorized, registered, and subject to the supervision of the CNMV.

As far as marketing activities are concerned, article 71 of the *LMV* does not contain any specific provisions. Therefore, pursuant to article 73, the government has the opportunity to regulate, for all matters not governed by the law regarding activities of article 71. Article 94 provides that the Minister of Economy will determine cases in which advertising of such activities should be subject to authorization or to any other administrative control, by the CNMV, and will approve the special standards which should be respected. This opportunity has not been used to date.

4.10 - In SWEDEN, authorized firms are subject to ongoing monitoring as follows :

- such firm has to inform the Authority about the firm and its business in the manner demanded by the Authority ;

- the Authority has to supervise that a proper development of the securities market be forwarded ;

- the Authority is mandated to cancel decisions by firms not in accordance with law or other regulations and may ultimately prohibit the further business of a firm ;

- the Authority may as well take actions against a firm lacking license.

4.11 - In SWITZERLAND, the only authorized/registered firms subject to administrative law at the federal level are banks or banklike financial companies. Even though the *Federal Banking Law (FBL)* does not contain any provision regulating specifically the sale and promotion of securities, banks have to comply with a general clause of "irreprochable management" (Article 3 of the *FBL*) which will prevent them from applying high pressure sales techniques or misleading promotional materials.

4.12 - In THE NETHERLANDS, institutions of which securities have been issued should ensure that information on their business activities is made generally available (Section 5 *SSTD*). The *SSTD* provides for a specification of this information.

Financial firms which have been granted a license are obliged to observe the requirements laid down in the *SSTD* (Section 7 and 11 *SSTA*). These requirements imply, for example, that the financial firms have to act in the best interests of their customers and the integrity of the market. These principles are implemented by more detailed regulations in the *RSST*. Licensees shall report, for example, on changes in the management and structure of the company. They also have to report on their solvency position. They are subjected to periodic inspections by the STE. In these inspections, the STE also pays attention to the rules of conduct. Apart from these inspections, the STE is empowered to investigate or order an investigation on the activities of brokers, portfolio managers and applicants for a licence.

Financial firms who are member of the Exchanges are obliged to observe the rules issued by the Exchanges. The objective of these rules is to guarantee the protection of the interests of the customers and the integrity of the market.

4.13 - In the UNITED KINGDOM, authorized firms are subject to on-going monitoring of their marketing and sales practices through compliance visits or, for instance, when a complaint has been made, special investigations.

4.14 - In the UNITED STATES

4.14.1 - Answer of the SEC

Yes. The SROs and the SEC regularly monitor the marketing and sales practices of registered broker-dealers. The SEC is authorized to investigate or examine all the activities of registered brokers and dealers, including their marketing and sales practices and the

procedures employed by brokers and dealers to supervise the conduct of their associated persons in the marketing and sales of securities.

MUTUAL FUNDS. - The SEC has the authority to investigate or examine the activities of registered investment companies and registered investment advisers including their marketing and sales practices. In addition, the advertising materials of investment companies and their underwriters and dealers are generally filed with, and reviewed by, the NASD. Further, the *1940 Act* requires that a registered investment company file with the SEC certain periodic and other reports that are required to be sent to shareholders.

4.14.2 - Answer of the CFTC

Yes. The CFTC oversees the monitoring of sales practices (including marketing practices) of registrants by ensuring that futures self-regulatory organizations (the US futures exchanges and the National Futures Association [NFA]) have rules to ensure proper sales practices of their members.

In addition, the exchanges and NFA have affirmative obligations under the CEA and the CFTC's regulations to conduct ongoing monitoring of their members' sales practices [22].

(22) - These requirements are detailed at page 218 of the Collated Summary.

QUESTION 5

What provisions are there governing :

a - the promotion of securities, futures, derivative or other financial products (including foreign products) through telephone calls ?

b - the promotion of securities, futures, derivative or other financial products (including foreign products) through mailing ?

c - the publication of financial advice ?

d - the use of yearbooks, datafiles or directories, or the purchase of mailing lists to contact customers ?

a - promotion of securities, futures, derivative or other financial products (including foreign products) through telephone calls

5.(a).1 - In AUSTRALIA, invitations and offers to subscribe for or purchase securities are, when made by telephone, governed by the general rules relating to hawking of securities. Dealing in securities or futures contracts by electronic connection with a securities or futures exchange is treated as dealing on a market of that exchange. The *Corporations Law* prohibits the promotion of securities by telephone where the promotion does not relate to the availability of a prospectus or where it relates to proposed securities of a corporation not yet formed.

The Commission may require a person not to publish, by telephone, matter in respect of futures contracts where the Commission considers that the person's past conduct makes it desirable that such matter should be first approved by the Commission.

In addition, securities and futures exchanges would limit the manner and frequency with which exchange members solicit new business from the public by telephone.

5.(a).2 - In CANADA, ONTARIO, registered dealers are permitted to make telephone calls to persons at their residence but the Commission may by Order suspend, cancel, restrict or impose terms and conditions upon this right.

5.(a).3 - In CANADA, QUEBEC, Section 5 of the *Securities Act* provides that "solicitation" by a broker includes the activities of a person "who regularly uses the telephone" to propose to persons to purchase or dispose of securities or to offer them advice.

Consequently, all those activities are included in the general section of *the Act* and of the Regulations adopted in virtue of it and are thus governed by the general rules dealing with distribution and broker activities.

5.(a).4 - In THE FEDERAL REPUBLIC OF GERMANY, under Section 1 of the *Law against Unfair Competition*, unsolicited telephone calls promoting securities and other financial products to private customers are in principle anticompetitive. In the business sphere as well, telephone calls for promotional purposes are permissible only if the businessman requested the call or if in the circumstances it is reasonable to assume that the businessman is agreeable to a promotional call. Depending on the situation, the unsolicited transmission of promotional letters by telefax may also be classed as anticompetitive.

5.(a).5 - In FRANCE, the general provisions governing the sale and promotion of financial products (see Question 1) apply to the sale and promotion of these products through telephone calls. No specific rules have been adopted in this respect. However, it should be pointed out that the *Law of December 28, 1966 on usury, loans and certain operations of canvassing and advertising* (Article 9 in fine), as well as the *1972 Law on canvassing of securities* (Article 2 § 3) expressly mention phone calls. The *1885 Futures Markets Law* encompasses all communication means.

5.(a).6 - In HONG KONG,

as far as securities are concerned :

(i) cold calling by registered dealers (see Question 1 (a), A (b))
(ii) hawking of securities (see Question 1 (a) and A (c))
(iii) issuing an invitation (which includes telephone calls) to acquire, dispose of, subscribe for or underwrite securities (see Question 1 (a), A (d)). [Note : this provision, in general, does not apply to registered persons, except those offering unauthorized mutual funds or unit trusts]. (iv) fraudulently or recklessly inducing persons to invest money in securities (see Question 1 (a), A (e)).

as far as commodities are concerned :

(i) hawking of futures contracts (see Question 1 (a), B (a))
(ii) fraudulently or recklessly inducing persons to invest in futures contracts (investment arrangement) (see Question 1 (c), B (b))
(iii) issuing an invitation (which includes telephone calls) to take part in any investment arrangement in respect of property other than securities (see Question 1 (a) B (b)).

As far as other products are concerned, identical to commodities (i) and (ii) above.

5.(a).7 - In ITALY, the offer of securities and the promotion of securities with a view to a subsequent offer, whether by way of telephone calls, letters, press or TV advertisements, are considered a "raising funds from the public" and are therefore subject to the provisions of Articles 1/18 ff of *Law 216/1974* as described above.

5.(a).8 - In JAPAN, solicitation of sales/purchase of securities is regarded as part of securities business, which is subject to general rules of the *Securities and Exchange Law*.

5.(a).9 - In SPAIN, (translation provided) there is no specific legislation. The only provision related to this matter is contained in a project of *Circular on Compulsory Registries and Standards in Relations with Customers*, which should be adopted soon, and provides that for orders received by phone, there should be written confirmation with the data of the operation. This *Circular* states that any written means of instantaneous transmission such as telex, fax, telegram etc, are accepted for confirmation of the order.

5.(a).10 - In SWEDEN, the promotion through telephone calls is not especially provided for.

5.(a).11 - In SWITZERLAND, there are no specific provisions in order to prevent malpractice through the cases stated in (a), (b), (c) and (d).

5.(a).12 - In THE NETHERLANDS, securities institutions may not approach or cause to be approached by telephone or in person a third party with whom it has not yet

concluded a securities transaction or who is not yet a client in some other capacity unless that person has explicitly given prior written consent and provided that consent has not been revoked by registered letter (Section 9 *RSST*).

5.(a).13 - In the UNITED KINGDOM, the relevant provisions are Section 3 of the *FSA*, and the *Financial Services (Unsollicited Calls) Regulations 1987*.

5.(a).14 - In the UNITED STATES

5.(a).14.1 - Answer of the SEC

In response to the widespread incidence of fraud and misconduct by broker-dealers engaged in broad scale "cold calling", to members of the public for the purpose of selling certain penny stocks, the SEC adopted *Rule 15 c 2-6 under the 1934 Act*. "Cold calling" refers to the practice of telephoning persons who are not previous customers and attempting to sell such persons securities. This Rule became effective on January 1, 1990.

Reliance on boiler room - style operations which engage in cold calling to sell penny stocks has been a frequent problem. The names of prospective investors usually are secured from a telephone directory or a commercially purchased membership list. The broker-dealer and salesperson often are located in a region or community distant from the prospective investor. Fraudulent price predictions and misstatements about the issuer commonly are made. The provisions of *Rule 15 c 2-6* are intended to address unsuitable purchases and unauthorized purchases by investors as the result of high pressure telephone sales and to allow investors the opportunity to reflect, investigate and consult before making a purchase of a speculative security.

Rule 15 c 2-6 requires a broker-dealer to fulfill three obligations before selling a security subject to the rule. First, the broker-dealer must obtain information on the financial situation, investment experience, and investment objectives of a prospective customer. Second, based on this information, the broker-dealer must determine that the recommended security is suitable for that particular person and that the investor can reasonably be expected to evaluate the risks of purchasing the security. These findings must be put into writing and sent to the investor for signature verification. Finally, the broker-dealer must obtain written customer agreements from the investor for the first three securities purchases of different issuers and set forth the identity and quantity of securities to be purchased.

Not all penny stocks or investors are covered by *Rule 15 c 2-6*, although the SEC is now solliciting public comment on broadening its application. The rule does not apply to existing customers who have traded securities with the firm for one year or more or who already have purchased three securities covered by the Rule. Securities on NASDAQ or exchange listed, with net tangible assets greater than $ 2 million, or priced at $ 5 or more, also are excluded.

MUTUAL FUNDS. - The promotion of investment companies securities through telephone calls is generally subject to the advertising and other restrictions under the *1940 Act* with respect to communications with shareholders or other members of the public, and to restrictions under the *1933 and 1934 Acts*. The same is true with respect to pre-recorded telephone services that allow shareholders or others to obtain information about a fund.

ADVISERS ACT. - Any person that provides investment advice over the telephone, including a person who calls clients or prospective clients, and including a person who provides a live "hotline" through which prospective investors may obtain advice about securities, is subject to the general anti-fraud provisions of Section 206 of the *Advisers Act*, unless that person is able to rely on an exclusion or exemption from the definition of "investment adviser" under the Act. Section 206 is applicable to both registered and unregistered investment advisers.

5.(a).14.2 - Answer of the CFTC

There is no *CEA* provision or CFTC regulation that explicitely addresses promotion of futures or option products by telephone. Fraudulent conduct engaged in through telephonic means is covered by the anti-fraud provisions of the *CEA* and the CFTC regulations thereunder referred to in the answer to question 1. In addition, as noted above, domestic futures or option trading accounts may not be opened in the absence of receipt by the registrant of the prescribed risk disclosure statement signed by the customer [23]. Criminal provisions prohibiting the use of interstate telephone wires for fraudulent purposes also apply to such conduct.

b - promotion of securities, futures, derivatives or other financial products (including foreign products) through mailing

5.(b).1 - In **AUSTRALIA**, invitations and offers of securities made by post are treated as hawking of securities. Since futures contracts can be traded only on an approved futures exchange, they may not be traded by post.

The *Corporations Law* prohibits the promotion of securities through the post where the promotion is not, and does not relate to the availability of, a prospectus, or where it relates to proposed securities in a corporation not yet formed.

The Commission may require a person not to publish, by mail, matter in respect of futures contracts where the Commission considers that the person's past conduct makes it desirable that such matter should be first approved by the Commission.

In addition, securities and futures exchanges would limit the manner and frequency with which exchange members solicit new business from the public by mail.

5.(b).2 - In **CANADA, ONTARIO**, the promotion of securities through mailing is permitted but there are restrictions on the contents of the advertising material which is mailed.There are specific restrictions on the type of material that may be mailed during the waiting period while the Commission reviews the prospectus before granting approval. When selling securities, persons are prohibited from making representations that they will resell or repurchase the security or that they will refund all or any of the purchase price of the security. They are also prohibited from giving an undertaking relating to the future value or price of the security being sold. They are also prohibited from stating that a security will be listed on a stock exchange. A dealer who sells a security as principal is required to disclose that fact to the purchaser. The Commission may require a registered dealer to submit all advertising to the Commission for approval before distributing it and may prohibit the distribution of advertising by a registered dealer.

The Canadian Securities Administrators have issued a draft policy governing the advertisement of securities in considerable detail. This policy has not yet been finalized.

5.(b).3 - In **CANADA, QUEBEC**, it is also included in the definition of "*solicitation*".

Consequently, all those activities are included in the general section of *the Act* and of the Regulations adopted in virtue of it and are thus governed by the general rules dealing with distribution and broker activities.

5.(b).4 - In **THE FEDERAL REPUBLIC OF GERMANY**, promoting the sale of securities and financial products by mail is permitted in principle. Disguising such promotional mail as private mail could, however, be in violation of Section 1 of the *Law Against Unfair Competition*.

5.(b).5 - In **FRANCE**, the general provisions governing the sale and promotion of financial products (see Question 1) apply to the sale and promotion of these products through mailing. No specific rules have been adopted in this respect. However, it should be pointed out that the *Law of December 28, 1966 on usury, loans and certain operations of canvassing and advertising* (Article 9 in fine), as well as the *1972 Law on canvassing of securities* (Article 2 § 3) expressly mention advertising by mail. The *1885 Futures Markets Law* encompasses all communication means.

5.(b).6 - In **HONG KONG**, as far as **securities** are concerned

(i) the issues of an offer by a dealer that does not comply with Section 72 of *SO* (see Question 1 (a), A (a)) ;

as far as **securities, futures contracts, investment arrangements** are concerned

(ii) Section 3 of *PIO* would cater for the issue of documents containing a fraudulent or wreckless misrepresentation to induce another person to invest in these products ;

- Section 4 of *PIO* would cater for the unauthorized issue of documents relating to investment in these products.

5.(b).7 - In **ITALY**, see 5.(a).7.

5.(b).8 - In **JAPAN**, solicitation of sales/purchase of securities is regarded as part of securities business, which is subject to general rules of the *Securities and Exchange Law*.

5.(b).9 - In **SPAIN**, (translation provided) there is no specific legislation. The only provision related to this matter is contained in a project of *Circular on Compulsory Registries and Standards In Relations With Customers*, which should be adopted soon, and provides that for orders received by phone, there should be written confirmation with the data of the operation.This *Circular* states that any written means of instantaneous transmission such as telex, fax, telegram etc, are accepted for confirmation of the order.

5.(b).10 - In **SWEDEN**, the promotion through mailing is not especially provided for.

5.(b).11 - In **SWITZERLAND**, see 5.(a).11.

5.(b).12 - In **THE NETHERLANDS**, there are no specific provisions governing the promotion of securities through mailing. Advertisement or documents in which the offering of securities upon issue is promoted have to make mention where and when a prospectus concerning the offer will be generally available. Before the advertisement and documents are published, the STE has to be provided with a copy. It should be noted that Section 31 b of the *STA* applies when misleading promotion material is used in order to promote securities.

5.(b).13 - In the UNITED KINGDOM, the relevant provisions are Section 3 and Section 57 of the *FSA* . If the firm is authorised , conduct of business rules will also apply.

5.(b).14 - In the UNITED STATES

5.(b).14.1 - Answer of the SEC

The anti-fraud and manipulation rules (see above) apply to all promotions of securities through the means of interstate commerce, such as by telephone, and by the mails. The SROs also have rules governing the nature of advertisements and promotional litterature by broker-dealers. For example, the NASD's rules require that all communications with the public should provide a "sound basis for evaluating the facts in regard to any particular security...", should not omit "material facts" ; or should not contain "exaggerated, unwarranted or misleading claims".

MUTUAL FUNDS. - The promotion or advertisement of investment company securities through the mail or through other media is subject to restrictions under both the *1933 and the 1940 Acts*. An investment company may use three forms of sales litterature. First, the *1933 Act* permits an investment company to send any type of sales material if the material follows or is sent with a full prospectus and is not misleading. Second, *Rule 134 under the 1933 Act* permits investment companies to use advertisements that contain only specified types of information and no performance data ("tombstone ads"). Finally, *Rule 482 under the 1933 Act* allows investment companies to advertise using any information that is also contained in the full prospectus provided that investors can obtain a full prospectus before investing. Investment companies are not permitted to advertise projected future performance and the advertising of past performance data is allowed only under certain conditions set forth in *Rule 34b-1 under the 1940 Act and Rule 482 under the 1933 Act*.

The *1933 and 1940 Acts* require that purchasers of investment company shares must be provided a prospectus containing information about a fund's investment policies and objectives, investment risks, and expenses. Investment companies are required to submit prospectuses, as well as updates to those prospectuses, for the SEC staff's review. Section 5 of the *1933 Act* provides that the prospectus must be delivered to the purchaser before, or together with, delivery of the security or the confirmation of purchase.

ADVISERS ACT. - An investment adviser that provides advice through the mail would generally be subject to the same requirements, including the anti-fraud provisions under Section 206 of the *Advisers Act*, as any other investment adviser. Rule 206 (4)-1 specifically adresses advertisements by investment advisers. See, however, our response below to Question 5 (c) regarding publishers of financial advice.

5.(b).14.2 - Answer of the CFTC

There is no *CEA* provision or CFTC regulation that explicitly addresses promotion of futures or option products through mailing. Fraudulent conduct engaged in through the mails is covered by the anti-fraud provisions of the *CEA* and the CFTC regulations thereunder referred to in the answer to question 1. Criminal provisions prohibiting the use of the mail for fraudulent purposes also apply to such conduct. In addition, NFA requires that all its members have written supervisory procedures for review of all promotional materials [24]. The CFTC requires, moreover, that, as a precondition to designation as a contract market in options, an exchange adopts rules requiring each FCM that offers or sells such options to submit all promotional material to its designated self regulatory organization for review [25].

c - *publication of financial advice*

5.(c).1 - In AUSTRALIA, investment and futures advisers are licensed. Unlicensed advice is prohibited except when given by solicitors and accountants as incidental to the ordinary course of their business or when given to the general public in media publications by disinterested journalists.

5.(c).2 - In CANADA, ONTARIO, advisers must be registered with the Ontario Securities Commission. When a registered adviser recommends a specific security in any advertising or publication, he is required to conspicuously disclose a full and complete statement of any financial or other interest that he may have directly or indirectly in the securities being recommended.

5.(c).3 - In CANADA, QUEBEC, Section 5 of the *Securities Act* provides that an "adviser" is a person who advises others through "printed materials".

Consequently, all those activities are included in the general section of *the Act* and of the Regulations adopted in virtue of it and are thus governed by the general rules dealing with distribution and broker activities.

5.(c).4 - In THE FEDERAL REPUBLIC OF GERMANY, the publication of financial advice is subject to no special regulations.

5.(c).5 - In FRANCE, the *law of December 28, 1966* (Article 10) and the *Decree of 1968* forbid marketing and advertising with the view to collect funds from the public, when this marketing or advertising includes false or misleading information. The *Decree* also provides that people who would like to advertise for financial products in France from a foreign country shall, prior to any advertisement, designate a representative located on the French territory (Article 2).

This does not prevent journalists from writing newspapers articles that would include recommendations to buy or sell financial products provided they abide by the general rules of their profession.

Furthermore, advertising for securities and mutual funds shares remains governed by the *1972 Law on canvassing of securities*, and the general provisions included in this text apply to the publication of financial advice related to such products.

5.(c).6 - In HONG KONG, a person who for remuneration issues or circulates analyses or reports in respect of securities or futures contracts must be registered as an adviser. Both advisers and registered dealers can, in general, issue financial advice, being exempt from the provisions of the *PIO*, to their clients. Persons registered under the *SO* are, with a few exceptions, exempt from the provisions of Section 4 of the *PIO*. Persons registered under the *CTO* do not have a similar exemption. Subject to certain exceptions contained in Section 4 of the *PIO*, invitations or documents relating to offers of securities,

futures contracts or investment arrangements, have to be authorized by the SFC. Any person failing to obtain such authorisation commits an offence under Section 4 of the *PIO*. In general, financial advice contained in any newspaper, journal, magazine, or other periodical which has general and regular circulation, is exempt from the provisions of the *PIO*.

5.(c).7 - In **ITALY**, see 5.(a).7.

5.(c).8 - In **JAPAN**, the publication of financial advice is governed by the *Law for Regulating Securities Investment Advisory Business*, if it is based upon an investment management contract with a client. In addition, in case a securities firm publishes financial advice, it is subject to the advertisement rules of Japan Securities Dealers Association.

5.(c).9 - In **SPAIN**, (translation provided) this activity is free. However, pursuant to article 77 of the *LMV*, the Government has the opportunity to provide for conditions under which these activities of advising and information on matters relating to stock exchange should be performed. So long as the government does not use this opportunity, these activities will remain free : they will not require any authorization and they will be opened to all persons. Nevertheless, persons or entities performing these activities remain subject to the rules of conduct and to the supervision, inspection and sanction regime of the CNMV. Due to the absence of obligation to communicate financial advice or letters made, to the CNMV, there is no control over these publications.

5.(c).10 - In **SWEDEN**, there is specific legislation since the 1987 crash, regarding derivative instruments, and, in that context, also the publication of financial advice.

In the beginning of 1988 and after an intensive work with many spot investigations at the trading and back-office units of both banks and securities firms, the former Bank Inspection Board issued advisory rules (BFFS 1988 : 7) concerning derivative instruments. In these rules the BIB stressed the importance of clear contract documents, collateral requirements, risk management and good transactions information such as settlement notes. And as the knowledge of how to trade in these instruments was bad in the market, the BIB underlined the responsibility of the securities firms to inform their customers and to educate their own personel. Since that time, the experience of the FSA is that fairly few derivative transactions have caused processes in court. Recently, a district court has charged a bank with the responsibility of customers losses due to insufficient financial advice. Furthermore, the FSA has experienced that self regulation by the dealers organisation itself has not yet become a realistic alternative. That is why an updated version of the 1988 issue is necessary now, especially concentrated upon distribution of information, time allocation of business transactions and risk management.

5.(c).11 - In **SWITZERLAND**, see 5.(a).11.

5.(c).12 - In **THE NETHERLANDS**, there are no specific provisions. However, it should be noted that Section 31 b of the *SSTA* applies when misleading promotion material is used in order to promote securities.

5.(c).13 - In the UNITED KINGDOM, the relevant provisions are Section 3 and Section 57 of the *FSA* . If the firm is authorized , conduct of business rules will also apply.

5.(c).14 - In the UNITED STATES

5.(c).14.1 - Answer of the SEC

MUTUAL FUNDS : response (b) above.

ADVISERS ACT : An investment adviser that provides disinterested advice that is disseminated through a bona fide publication of general and regular circulation may rely on the "publisher's exclusion" from the definition of investment adviser in Section 202 (a) (11) (D) of the *Advisers Act* and is therefore not subject to the requirements under that Act. Under the US Supreme Court's decision in *Lowe v. SEC* (472 *US* 181 [1985]), an investment advisory publication does not fall within the publisher's exclusion if it is issued only occasionally in response to episodic market activity ; if it is issued primarily to "tout" particular securities issues or to list securities that are "sure to go up" in value, or if it is "distributed as an incident to personalized investment services".

Publishers of investment advice who receive compensation from issuers of securities in connection with specific recommendations, or who have any personal economic interest in such issuers and intend to reap personal gain from influencing the market price of any of their securities would be subject to the anti fraud provisions of the *Advisers Act* and the *1933 Act*.

Persons who provide financial information through "on-line" computerized services also may be able to rely on the publisher's exclusion from the *Advisers Act*. In addition, the staff has stated that financial information provided through computerized services would not be considered "analyses or reports concerning securities" for purposes of the definition of "investment adviser" under the following conditions : 1) the information provided is readily available in its raw state ; 2) the categories of information are not highly selective ; and 3) the information is not organized or presented in a manner that suggests the purchase, holding or sale of any security. If, however, an "on-line" computerized service provides advice concerning securities that is based upon the specific investment objectives and needs of the particular subscriber, such tailoring could take the service outside the scope of the publisher's exclusion and outside the staff's position on analyses and reports concerning securities.

5.(c).14.2 - Answer of the CFTC

As noted above, the CEA requires persons acting in the capacity of CTAs to register. The *CEA* defines CTA to mean any person who, for compensation or profit, engages in the business of advising others, either directly or thorugh publications, writings or electronic media, as to the value of or the advisability of trading in any contract of sale of a futures or option contract [26]. However, this category does not include, among others, news reporters, columnists or editors, or publishers or producers of print or electronic data of general and regular dissemination [27]. Whether publication of particular materials containing advice about futures or options trading constitutes engaging in the activity requiring registration depends upon the facts involved in that particular case.

d - use of yearbooks, datafiles or directories, purchase of mailing lists to contact customers

5.(d).1 - In AUSTRALIA, there are no specific provisions.

5.(d).2 - In CANADA, ONTARIO, there are no specific provisions regarding this matter.

5.(d).3 - In CANADA, QUEBEC, there are no specific provisions in *the Act* dealing with this kind of material.

Consequently, all those activities are included in the general section of *the Act* and of the Regulations adopted in virtue of it and are thus governed by the general rules dealing with distribution and broker activities.

5.(d).4 - In THE FEDERAL REPUBLIC OF GERMANY, the use of generally available data and the purchase of mailing lists is permitted.

5.(d).5 - In FRANCE, no specific rules apply to the use of datafiles, yearbooks, directories... to promote financial products. Nevertheless, people using such means shall comply with the general rules governing the use of files, as provided in the *Law of January 6, 1978*. This includes the right for the concerned customers, or people in general, to be informed on the data contained in the files, to amend them, or to oppose to them or to their communication to a third party.

5.(d).6 - In HONG KONG, there is no law applicable to this matter.

5.(d).7 - In ITALY, there are no specific provisions.

5.(d).8 - In JAPAN, this question is not governed by any specific provisions.

5.(d).9 - In SPAIN, there is no specific legislation.

5.(d).10 - In SWEDEN, the use of EDP registers to contact customers is supervised by a special governmental inspectorate.

5.(d).11 - In SWITZERLAND, see 5.(a).11.

5.(d).12 - In THE NETHERLANDS, there are no specific provisions governing these activities provided for in the *SSTA*, *SSTD* or *RSST*. However, we would like to stress that the general prohibition mentioned under 5 a also applies to security firms using purchased mailing lists in order to approach persons by telephone, as long as a business relations between this security and the approached person does not exist.

Furthermore, the purchase of mailing lists may be subject to privacy legislation as Act on the Protection of Privacy.

5.(d).13 - In the UNITED KINGDOM, data files are subject to the *Data Protection Act 1984*. There are no provisions directly governing the use of yearbooks, directories or mailing lists, but any firm which uses such sources to contact potential customers will - by that contract - come within the *FSA* provisions referred to above.

5.(d).14 - In the UNITED STATES

5.(d).14.1 - Answer of the SEC

There are no special provisions under the US federal securities laws governing the use of such directories or lists.

5.(d).14.2 - Answer of the CFTC

There are no provisions of the *CEA* or of the *CFTC's regulations* thereunder that explicitly address these matters. Fraudulent conduct engaged in through these means is covered by the anti-fraud provisions of the *CEA* and the *CFTC regulations* thereunder referred to in the answer to Question 1.

(23) - 17 CFR §§ 1.55, 33.7.
(24) - NFA Rule 2.29 (d).
(25) - 17 CFR § 33.4 (b).
(26) - 7 USC § 2 (A) (1).
(27) - 7 USC § 2 (A) (1).

QUESTION 6

What sanction (professional, administrative, civil, criminal...), il any, can be imposed on those who commit fraud ?

6.1 - In AUSTRALIA, the sanctions are as follows :

- disciplinary measures in respect of, or expulsion from, membership of a securities or futures exchange ;

- cancellation of, or imposition of conditions on, a dealer's licence ;

- banning or disqualification from future licensing as a dealer, dealer's representative or adviser ;

- imposition of civil liability for misleading or deceptive conduct, false or misleading statements and omissions in relation to prospectuses and securities, market manipulation and rigging, fraudulent inducement to deal, insider trading etc ;

- imposition of a non-civil offence penalty involving a fine or, for natural persons, a fine, imprisonment, or both ;

- disqualification from appointment to or continuance in office as an officer of a corporation.

6.2 - In CANADA, ONTARIO, under the *Canadian Criminal Code*, persons can be charged with fraud affecting the public market, fraudulent manipulation of stock exchange transactions, issuing false prospectus and paying or receiving secret commissions. If convicted they are liable to a term of imprisonment not exceeding five or ten years depending on the charge. Persons also can be charged under the *Securities Act* with trading in securities without registration, distributing securities without a prospectus and filing documents such as a prospectus or press releases with the Commission which contain misrepresentations. The maximum penalty if convicted is a jail term of two years and a fine of $ 1 million. In addition, the Ontario Securities Commission has the power to make orders prohibiting trading in securities issued by a company and to prohibit named persons from trading in securities. It can also revoke or suspend the registration of any person. In addition, a superior court in Ontario may issue an order requiring persons to comply with the *Securities Act*. If that order is violated, proceeding may be taken for contempt.

6.3 - In CANADA, QUEBEC, Section 197 of the *Securities Act* provides that every person is guilty of an offence who makes a misrepresentation in respect of a transaction of a security, in any document or information filed with the Commission or one of its agents and in any document forwarded or record kept by any person pursuant to the *Securities Act*. General accusation in the field of fraud can also be laid in virtue of the *Criminal Code*.

Sanctions are as follows :

(a) - THE CRIMINAL CODE. - The *Criminal Code of Canada* holds a few provisions that relate to stock or public market.

Section 380 (2) of the *Code* provides a term of emprisonment not exceeding ten years for everyone who, by deceit, falsehood or other fraudulent means, with intent to defraud, affects the public market price of stocks, shares, merchandise or anything that is offered for sale to the public.

Section 381 makes it a indictable offence to make use of the mails for the purpose of transmitting or delivering letters or circulars concerning schemes devised or intented to deceive or defraud the public.

Section 382 of the *Code* provides a term of imprisonment not exceeding five years for everyone who, through the facility of a stock exchange, curb market or other market, with intent to create a false or misleading appearance of active public trading in a security.

And Section 384 targets brokers reducing stock by selling for their own account. The section holds also a term of imprisonment not exceeding five years.

(b) - THE QUEBEC SECURITIES ACT. - The *Quebec Securities Act* provides two types of sanctions. First, there are prohibitions and penalties which are of penal nature. Section 202 of the Act states that every person who contravenes a provision of the Act is guilty of an offence and is liable, in the case of a natural person, to a fine of 500 $ to 25.000 $. These offences are namely : use of privileged information (Section 187 Act), representative who is not registered (Section 149) and multiple transactions (Section 193), short sales (Section 194), etc.

There is also a wide range of civil actions available to the public (Section 214 to 232). And the Commission can intervene, among other things, in action for recovery (Section 229, 230 and 233). The *Act* provides also administrative measures. According to Section 276, the Commission is responsible for the administration of this *Act* and has the duty to protect investors against unfair, improper and fraudulent practices (Section 276 (2)) and to regulate the information that must be disclosed to security holders and the public (Section 276 (3)).

Thus, the Commission has jurisdiction to decide on all matters related to its "*function*". However, "*the Commission shall exercise the discretion conferred on it in accordance with the public interest*" (Section 316).

The Commission may take any measure that it thinks fit for the protection of investors. For instance, it may order the person who is or is about to be under investigation not to dispose of the funds, securities or other assets in his possession (Section 249) ("*freeze order*"). Finally, the Commission may order a person to cease carrying on business as an adviser (Section 266). It may also proceed by an injunction against a delinquant (Section 268).

Under Section 153 of the Act may revoke or suspend the right granted by Registration or impose restrictions or conditions on their exercise when a registrant fails to comply with the *Act* or *Regulation*. Under Section 273; it may also reprimand registrant or a self-regulatory organization.

(c) - THE MONTREAL STOCK EXCHANGE. - The disciplinary committee of the MSE disposes of a wide range of sanctions against delinquant members. It goes from a single reprimand to the expulsion of a member (Section 4105 of the Regulation).

It provides also some measures for the revocation of a registration. It can also impose on a member the obligation to take one course or more given by the Canadian Securities Institute.

(d) - INVESTMENT DEALER'S ASSOCIATION. - According to by-law n° 19, the applicable business conduct committee has the discretionnary power to impose upon the member a range of penalties that goes from a reprimand to the expulsion of a member, passing by a fine note exceeding 100.000 $ per offense or the suspension of the rights and privileges of a member.

By-law n° 20 holds measures of publicity in the interest of the public and the good reputation of the Association.

6.4 - In THE FEDERAL REPUBLIC OF GERMANY, in cases of fraud, the banking supervisory authority can take the necessary measures against the credit institutions, taking into account the principle of commensurability.

If a middleman is unreliable, the trade supervisory authority can revoke the license granted pursuant to Section 34 c if this is necessary to prevent imminent harm to the general public.

As regards civil law, the offerer of securities and other financial products bears liability if the information in the prospectus is inaccurate or if he fails to meet his obligations to inform the customer in connection with the investment contract. Over and above that, in the case of criminal fraud there is liability in tort under civil law according to the *German Civil Code*.

The following offences are punishable under criminal law :

- under Section 88 *Stock Exchange Act*, the manipulation of stock exchange or market prices of securities, subscription rights or goods by inaccurately stating or failing to disclose circumstances important for evaluation or by other deceptive means is punishable by up to three years imprisonment or a fine ;

- under Section 89 *Stock Exchange Act*, the gainful enticement of others to stock exchange speculation, in particular to futures contracts and options on such contracts, by taking advantage of their inexperience is punishable by up to three years imprisonment or a fine ;

- under Section 264 of the *Penal Code*, the use of inaccurate or incomplete prospectuses or other representations for the distribution of securities, subscription rights or shares in enterprises is punishable by up to three years imprisonment or a fine.

6.5 - In FRANCE, the sanctions are to be distinguished among professional sanctions, administrative sanctions, civil sanctions and criminal sanctions.

6.5.(a) - PROFESSIONAL SANCTIONS

6.5.(a).1 - PROFESSIONAL SANCTIONS PRONOUNCED BY THE FUTURES EXCHANGE COUNCIL. - A professional proceeding may be initiated by the Futures Exchange Council (CMT) against any of its members, if the latter has violated the provisions regarding the sale or the promotion of financial or commodity futures contracts to customers, which are included in the *1885 Futures Markets Law*. The sanctions may be a blame, a temporary or definitive bar from all or part of activity, or a fine up to 200.000 FF (Article 15, Article 17, Article 17 bis).

6.5.(a).2 - PROFESSIONAL SANCTIONS PRONOUNCED BY THE MUTUAL FUNDS COUNCIL. - A professional proceeding may also be initiated by the Mutual Funds Council , for any violation of the laws and regulations governing this activity. The sanctions are a blame, a temporary or definitive bar from activity and a fine up to 5.000.000 FF (*1988 Law on Mutual Funds*, Article 33-1, Article 33-4).

6.5.(a).3 - PROFESSIONAL SANCTION INITIATED BY THE COMMISSION DES OPERATIONS DE BOURSE. - The COB may ask the President of the Tribunal de Grande Instance (High Court) to bar a person from activity, temporarily, when this person is involved in a case investigated by the COB (*1967 Ordinance*, Article 8-1 § 1). It is to be

noted here that the COB has the initiative to ask the judge to pronounce such sanctions but it cannot pronounce these sanctions itself.

6.5.(b) - ADMINISTRATIVE SANCTIONS

The COB may pronounce injunctions to resume activities contrary to its rules (*1967 Ordinance*, Article 9-1). The COB may also ask in court that an injunction is given to a person to comply with some laws or regulations, or to resume violations to these rules (*1967 Ordinance*, Article 12-2). Here again the authority of a judge is required.

The COB may impose administrative sanctions against the persons who have violated its own rules. The sanction is a fine up to 10.000.000 FF or, when profits have been obtained out of the violation, up to 10 times the amount of the referred profits (*1967 Ordinance*, Article 9-2). Currently, three main COB Rules govern or somehow interfere with the promotion of financial products : *Rule n° 88-04* on information to be provided by public companies ; *Rule n° 89-02* on mutual funds ; *Rule n° 90-10* on commercialization of securities, futures and other financial products negociated on a foreign market.

6.5.(c) - CIVIL SANCTIONS

The COB has no power to initiate civil proceedings against fraudsters. Nevertheless, any interested party who would consider itself as defrauded could initiate such action and seek to obtain relief.

In this view, it is very interesting to point out the liability regime applicable to canvassing activities. The canvassor is an independent person in relation to the entity for which he performs the canvassing. It is neither an employee, nor an agent. There is no subordination link, neither a link of principal and agent. Thus, the liability for damage caused by a canvassor should not follow the rules of that applicable to labor or agency contracts. However, under the *1972 Law on canvassing of securities (Article 11)*, the liability regime provided for in Article 1384 of the French Civil Code regarding the liability of the principal for the damage caused by his agents is deemed applicable to canvassing activities (the principal being the entity for which the canvassing is carried out, and the agent being the canvassor). The same liability regime is provided for in *Article 14 of the 1885 Law on Futures Markets*.

6.5.(d) - CRIMINAL SANCTIONS

Criminal sanctions can be sought against persons who have :

- sold or promoted securities without being authorized to do so, or in violation of the legal provisions governing this activity (*Securities Markets Law of January 22, 1988*, Article2 ; *Law on canvassing of securities of January 3, 1972*, Article 8, Article 10, Article 33) ;

- promoted financial or commodity futures without being authorized to do so, or in violation of the legal provisions governing this activity (*Futures Markets Law of March 28, 1885* Article 16) ;

- promoted any other financial product (except mutual fund shares) without being authorized to do so, or in violation of the legal provisions governing this activity (*Law of December 28, 1966 on usury, loans, and certain operations of canvassing and advertising*, Article 15)

The sanctions are a prison term up to 5 years and/or a fine up to 2.500.000 FF.

Furthermore, general sanctions, such as those provided for fraud (Article 405 of the *Criminal Code*), abuse to customers proxies or confidence (Article 408 of the *Criminal Code*) may also ne sought against the fraudsters. It should be noted that for the application of these sanctions, the fact that the company issued shares in the public is an aggravating circumstance.

The judge may also decide to withdraw the professional card to a canvassor.

6.6 - In **HONG KONG**, there are various criminal sanctions contained in the *SO*, *CTO*, *PIO* and the *Theft Ordinance* for breaches of the Sections referred to.

In the *SO*, (Section 144) the SFC can make application to the Court to restrain certain illegal activities and to declare a contract relating to securities void or voidable. This provision has been used to close down boiler room operations.

If registered persons are involved, disciplinary action can be considered which could lead to the registered person being revoked (Section 36 of the *CTO* ; Section 56 of the *SO*).

In the *SO* (Section 141)and Section 8 of the *PIO*, (Section 8) there are "action in tort" provisions whereby an aggrieved person can seek compensation by way of damages when certain antifraud provisions have been breached.

There are powers of intervention that are exercisable by the Commission against registered persons who have committed offences contrary to the provisions of *SO*, *CTO*, *PIO* and *SFCO*, including

- restriction of business,
- restriction of dealing with assets,
- maintenance of assets,
- winding up orders,
- receiving orders.

Futures contracts entered into with an unregistered person may be rescinded by any other party to the contract, who, upon so doing, shall be entitled to recovery of any money or other thing he may have paid or delivered, under the contract.

6.7 - In **ITALY**, violations of the provisions on the public offer regarding the obligation to notify the CONSOB in advance and publish a prospectus are criminal offences punishable with a fine of between a quarter and a half of the total value of the operation.

Failure to comply with the instructions or requests of the CONSOB is also a criminal offence punishable with a prison sentence up to three months or a fine between 2 and 40 million lire.

The CONSOB is empowered to forbid the carrying out of an operation in the event of the proposer failing to comply with the provisions regarding the advance notification of the CONSOB and the publication of a prospectus.

Law 1/1991 provides additional penal, administrative and civil sanctions in the event of intermediaries violating other legislative and regulatory provisions.

Article 5 of Law 1/1991 also provides for financial salesman to be subject to the administrative sanctions of suspension or cancellation from the register.

6.8 - In JAPAN, the following sanctions may be imposed on a securities company or on its employees.

ADMINISTRATIVE SANCTION. - In case a securities company provides a customer with false information or acts so as to cause misunderstanding, the Minister of Finance imposes an administrative sanction (withdrawal of license or suspension of business) based upon Articles 35 and 50 of the *Securities and Exchange Law*. In such case, the Japan Securities Dealers Association (JSDA) also imposes a sanction on the member company (fine, suspension of membership, expulsion...).

CIVIL SANCTION. - In case a securities company unlawfully causes damage to its customers, it must compensate for the damage, pursuant to Article 709 of the *Civil Law*.

CRIMINAL SANCTION. - In case an act of an employee of the company constitutes a fraud as defined by Article 246 of the *Criminal Law*, imprisonment not exceeding 10 years may be imposed on him.

6.9 - In SPAIN, (translation provided) there are three possible types of sanction.

ADMINISTRATIVE SANCTIONS. -

On the primary market, is sanctionned as *very serious offence* the issue of securities or their placing (article 99.n *LMV*) and the operation of a public offer of sale (article 99.o *LMV*), without prior supervision by the CNMV, or in contradiction with the conditions which had been imposed. On the secondary market, is sanctionned as *very serious offence* the trading of securities without authorization (article 99.q *LMV*) and as *serious offence* the illegal advertising or the advertising contrary to general legislation on the matter (article 100.l *LMV*) and the non-compliance with the principle of priority given to the customer (article 100.n *LMV*). Administrative sanctions applicable according to the serious character of the offences fall under the following categories :

a - *Very Serious :*

1 - Fine of an amount which should not be inferior to the benefit obtained by the operations or omissions constituting the offence, neither superior to 5 times the said benefit, or, in case this criteria is not applicable, up to 5 % of the shareholders' equity if it is a company, or up to 5 million pesetas, if it is not so.

2 - Suspension or limitation of the operations or activities of the person during a period of time not superior to 5 years.

3 - Suspension of the quality of member of the official secondary market for a period of time not superior to 5 years.

4 - Withdrawal of the authorization when the concerned person is a dealer or a brokerage house, Investment companies or "Entités de Gestion dans le Marché de la Dette Publique"(Managing Entity on the Public Debt Market).

b - *Serious :*

1 - Public sanction, published in the BOE.

2 - Fine of an amount equal to the gross benefit obtained by the operations or omission constituting the offence, or if the criteria is not applicable, up to 2 % of the shareholders' equity if it is a company, or up to 2 million pesetas, if it is not no.

3 - Suspension or limitation of the operations or activities of the person on the official secondary market, for a period of time not exceeding 1 year.

4 - Suspension of the quality of member of the official secondary market for a period of time not superior to 1 year.

CRIMINAL SANCTIONS. -

The provisions relating to swindle and breach of trust may be applicable. The sanctions for such offence are imprisonment, according to the gravity of the facts, from 1 month up to 12 years, and also other sanctions such as suspension from all official functions, profession, business and from voting right for a period of time. It should be kept in mind that the person condemned will also have to compensate for the damage caused by the offence.

CIVIL SANCTIONS. -

Natural or legal persons who have been defrauded may, independently from any other administrative or criminal action, bring an action before a civil court in order to obtain the restitution of their property and assets, as well as damages.

6.10 - In SWEDEN, this question is not within the jurisdiction of the Financial Supervisory Authority. When confronted to such question the Authority passes it over to a decision by a prosecutor. The sanctions that can be imposed on fraudsters in Sweden are regulated in a special chapter of law within the criminal code. Generally speaking, the

sanction caused by fraud is up to two years imprisonment. There are, however, two more degrees mentioned in the law, that is to say, fraudulent behaviour causing either a fine or up to six months imprisonment, and if the fraud is very severe, the penalty is from six months up to six years of imprisonment.

There is also the possibility of professional sanction by prohibition or restriction of being active as for instance a lawyer, a chartered accountant or any such licensed professional. Both the stock exchange in connection with the listing procedure and the FSA when authorizing have to regard facts of fraud. Finally, there is in Sweden a special act (1986 : 436) on prohibition of doing business. Such prohibition will be the consequence if anybody is found guilty of a serious criminal action.

6.11 - In SWITZERLAND, beside institutions subject to the FBL and members of associations subject to professional sanctions, any sanctions related to the sale or promotion of securities, would be of civil or penal nature. Two ways to initiate a prosecution against fraudsters would roughly be possible for the present cases, namely :

- the victim(s) of an offence evoquing deceit or swindling according to the nature of the fraud ;

- (a) competitor(s) of the fraudster evoquing unfair competition.

6.12 - In THE NETHERLANDS, administrative sanctions (withdrawing a dispensation or a license) may be imposed by the STE pursuant to the *SSTA*.

Criminal sanctions may be imposed by the court pursuant to the *SSTA* and the *Economic Offenses Act*. Professional sanctions can be imposed by the Exchanges pursuant to their regulations.

It should be noted that, besides these sanctions, the Minister of Finance is empowered to withdraw or alter the ER.

6.13 - In the UNITED KINGDOM, if a firm which is authorised is found to have abused that authorisation and to have conducted fraudulent business, it will have its right to conduct investment business temporarily or permanently withdrawn. Depending on the nature of the offence, it may also be subject to prosecution under Section 47 of the *FSA*, under the *Companies Securities (Insider Dealing) Act of 1985* or the *Theft Acts of 1968/1978*. It may also be subject to civil claims for restitution under Section 61 or Section 62 of the *FSA*.

An unauthorised firm is open to civil and criminal legal proceedings even if not fraudulent. Where there is fraud as well as "technical" illegality, the fraudster is also open to prosecution under Section 47 of the *FSA* or the *Theft Acts*. It may also be subject to a restitution order under Section 6 of the *FSA*.

6.14 -In the UNITED STATES,

6.14.1 - Answer of the SEC

The SEC has broad authority to investigate possible violations of the federal securities law and to obtain appropriate remedies through administrative proceedings and civil litigation. In

addition, willful violations of the federal securities laws can be prosecuted criminally, in which case criminal fines and prison sentences can be imposed.

Enforcement actions initiated by the SEC generally are preceded by an examination pursuant to the SEC's inspection powers or by an investigation. Under its inspection powers, the SEC is authorized to conduct examinations of regulated entities, including broker-dealers, municipal securities dealers, investment advisers, investment companies, transfer agents and self-regulatory organizations. The SEC's investigations may be conducted either informally or formally. Informal investigations are conducted on a voluntary basis, with the SEC requesting persons with relevant information to cooperate by providing documents and testifying before SEC staff. The federal securities laws also empower the SEC to conduct formal investigations, in which the SEC has the authority to issue subpoenas that compel the production of books and records and the appearance of witness to testify. Both types of investigations are generally conducted on a confidential, nonpublic basis.

The SEC's primary enforcement mechanism for addressing violative conduct is the injunctive action filed in the federal court. In these civil actions, the SEC is authorized to seek temporary restraining orders and preliminary injunctions as well as permanent injunctions against any person who is violating or about to violate any provision of the federal securities laws. A federal court injunction will prohibit future violations, and, once an injunction has been imposed, conduct that violates the injunction will be punishable by either civil or criminal contempt, and violators will be subject to fines or imprisonment. In addition to seeking such orders, the SEC often seeks other equitable relief such as an accounting and disgorgement of illegal profits, rescission, or restitution. Also, when seeking temporary restraining orders, the SEC often requests a freeze order to prevent concealment of assets or dissipation of the profits of illegal conduct. The SEC is specifically authorized to seek civil penalties in connection with insider trading violations.

Several types of administrative proceedings may be instituted by the SEC. The SEC may institute administrative proceedings against regulated entities to impose sanctions including censures, limitations on activities, and suspension or revocation of registration. The SEC may impose similar sanctions on persons associated with such entities and persons affiliated with investment companies.

Administrative proceedings may be instituted against the issuers as well. For example, Section 8 (d) of the *1933 Act* enables the SEC to institute proceedings to suspend the effectiveness of a registration statement that contains false and misleading statements. Administrative proceedings pursuant to Section 15 (c) (4) of the *1934 Act* may be instituted against any person who fails to comply, and any person who is a cause of failure to comply, with reporting, beneficial ownership, proxy, and tender offer requirements. Respondents may be ordered to comply or effect compliance with the relevant provisions. Pursuant to Rule 2 (e) of the *SEC's Rules of Practice*, administrative proceedings may be instituted against persons who appear or practice before the SEC, such as accountants and attorneys ; the sanctions that may be imposed in these proceedings include suspensions and bars.

The SEC also is authorized to refer matters to other federal, state or local authorities or self regulatory organizations such as the NYSE or the NASD. The SEC often provides substantial assistance to criminal authorities, such as the Departement of Justice, for the criminal prosecution of securities violations.

The *Remedies and Penny Stocks Act* created new judicial and administrative remedies for violations of the federal securities laws in four areas : (1) cease-and-desist authority ; (2) officer and/or director bars or suspensions ; (3) general fining authority ; and (4) expanded sanctioning authority over persons involved in penny stock offerings and imposed new duties on broker-dealer firms participating in such offerings. These new powers not only expand the types of remedies available to the SEC but also give the SEC greater flexibility to tailor remedies to fit particular conduct and violators. These changes should enhance the effectiveness of the SEC's enforcement actions, particularly their deterrent effect.

Specifically, the *Remedies and Penny Stock Act* amends the US federal securities laws to provide de SEC with authority to issue orders against any person to require a respondent to cease-and-desist from committing or causing a violation of the federal securities laws. These orders can be issued on either a temporary or permanent basis. In addition, the SEC can order the respondent to refrain from future violations, to take specified action in order to comply with the law, to make an accounting, and to disgorge ill-gotten gains, including interest. The SEC can enforce both temporary and permanent cease-and-desist orders in federal court and may ask the court to impose civil money penalties on violators who fail to comply with such an order.

Under its new authority, the SEC also can ask a federal court to bar or suspend individual defendants from serving as an officer and/or director of any publicly held company. However, the court may impose a bar only if the defendant has violated scienter-based provisions and has engaged in conduct that demonstrates substancial unfitness to serve as an officer or director. This remedy is not available in SEC administrative proceedings.

The *Remedies and Penny Stock Act* also confers upon the SEC and the federal courts general fining authority if such a penalty would be in the public interest. In general, the SEC can impose a monetary penalty on regulated entities and associated persons if the respondent has : willfully violated the federal securities laws ; willfully aided, abetted, counseled, commanded, induced or procured such a violation by any other person ; willfully made or caused materially false statements or omissions in applications for registration or reports filed with the SEC ; or failed reasonably to supervise a violator. The *Remedies and Penny Stock Act* establishes a three tiers of maximum penalty amounts, according to the type of violation and the extent of harm.

A federal district court may impose substantially similar money penalties. The courts, however, have the option to impose a fine equal to the amount of the violator's gross pecuniary gain, even if that amount exceeds the maximum dollar amount otherwise specified in the *Remedies and Penny Stock Act*.

Last, the *Remedies and Penny Stock Act* expands the SEC's authority to sanction persons who engage in penny stock offerings who previously were excluded from the SEC's jurisdiction. Promoters, finders, consultants, agents or other persons who engage in activities with a broker, dealer or issuer in connection with the issuance of or trading in any penny stock or, in connection with the purchase or sale of any penny stock, now can be barred or suspended from participating in future penny stock sales. The Act also makes it unlawful for any broker or dealer to permit a person subject to such an order from doing so if the broker or dealer reasonably should have known of the order.

MUTUAL FUNDS. - Section 9 of the *1940 Act* authorized the SEC, after notice and opportunity for a hearing, to enter a permanent or temporary order enjoining any person from violating any provision of the *1940 Act* or from acting in certain capacities for a registered investment company. With respect to such orders, the SEC is also authorized, under certain conditions, to impose civil penalties and to enter an order requiring an accounting and disgorgement, including reasonable interest.

Section 36 (a) of the *1940 Act* authorizes the SEC to bring an action in a US district court seeking that the court enjoin certain persons from a breach of fiduciary duty involving personal misconduct in respect of any investment company. The court may enjoin such a person from acting in certain capacities with respect to the investment company and award injunctive or other appropriate relief against such a person. Section 36 (b) authorizes the SEC, or any security holder of a registered investment company on behalf of the investment company, to bring an action against the investment adviser of the fund, or against certain other affiliated persons, for breach of fiduciary duty in respect of compensation received by that person.

Section 42 of the *1940 Act* authorizes the SEC to bring an action in a US district court seeking to enjoin acts or practices in violation of the Act and to enforce compliance with the Act. In addition, Section 42 authorizes the SEC to bring an action in a US district court seeking to impose a civil penalty for violations of the Act or of any cease-and-desist order issued by the SEC under Section 9 (f) of the Act. Finally, Section 42 authorizes the SEC to transmit evidence of *1940 Act* violations to the US Department of Justice which may institute appropriate criminal proceedings under the *1940 Act*.

ADVISERS ACT. - The SEC is authorized, after notice and opportunity for a hearing, to enter an order that censures, or places limitations on the activities of, persons who violate the federal securities laws or who fall within other categories set out in Section 203 of the *Advisers Act*. In connection with such an order, the SEC may also impose civil penalties or enter an order requiring an accounting and disgorgement. The SEC is further authorized, after notice and opportunity for a hearing, to bring an action in US district court to enjoin any person from violating the *Advisers Act*, to enforce compliance with the Act, and to seek that the court impose civil penalties. The SEC is also authorized to transmit evidence of *Advisers Act* violations to the US Department of Justice which may institute appropriate criminal proceedings.

6.14.2 - Answer of the CFTC

The CFTC has a wide range of administrative sanctions available for such violations, including imposition of civil monetary penalties of up to $ 100,000 per violation, entry of cease or desist orders, prohibition on trading in US futures and options markets, and, in the case of a registered person, revocation or suspension of registration [28]. The CFTC also may bring injunctive actions in the courts of the United States against such persons, and may obtain orders enjoining further violations of the *CEA*, disgorgement of illegally obtained assets and restitution to wronged customers [29]. Finally, members of self-regulatory organizations, including NFA and the exchanges, who engage in fraudulent conduct are subject to disciplinary action by the relevant self-regulatory organization, including fines and suspension of or expulsion from membership, and directives to other members to refuse to do business with them. Violations of the anti-fraud provisions of the *CEA* are felonies, and are punishable, in the case of individuals, by fines up to $ 100,000 and imprisonment of five years, or both, and in other cases, by fines of up to $ 500,000 and imprisonment for five years, or both [30].

(28) - 7 USC §§ 9, 13 b.
(29) - 7 USC § 13 a-1.
(30) - 7 USC § 13.

QUESTION 7

Which is the competent authority in charge of investigating alleged violations ?

7.1 - In AUSTRALIA, the competent authorities are :

- the Australian Securities Commission,
- the Commonwealth Director of Public Prosecution,
- the Australian Federal Police.

7.2 - In CANADA, ONTARIO, the competent investigating authotities are : the Ontario Securities Commission, the Royal Canadian Mounted Police, the Commercial Crime Unit, the Ontario Provincial Police, the Anti-Rackets Squad.

7.3 - In CANADA, QUEBEC, the Commission des Valeurs Mobilières du Québec is the competent authority to investigate alleged violations of the *Securities Act*, while the Section of Economic Crimes of the "Sûreté du Québec" will have the authority to investigate in the field of securities in the case of violations of the *Criminal Code*.

7.4 - In THE FEDERAL REPUBLIC OF GERMANY, if it is supected that criminal acts have been committed, it is first and foremost the prosecuting authorities who conduct the investigations. This does not rule out the possibility that in urgent cases, the banking and trade supervisory authorities may conduct their own investigations.

7.5 - In FRANCE, within the scope of its duty to protect savings invested in securities and other financial products, the Commission des Opérations de Bourse may conduct an investigation on alleged violations of securities and futures laws and regulations, including those related to the promotion of financial products.

In certain limited instances, and within the scope of their respective jurisdiction, the Banking Commission, the Stock Exchange Council and the Futures Exchange Council may undertake certain investigations.

Last, the Judge may deem necessary to investigate alleged offenses.

7.6 - In HONG KONG, in the first instance, the competent authority in charge of investigating alleged violations is the Securities and Futures Commission. If matters are serious and may result in a prosecution on indictment (the SFC can only prosecute summarily), the matter would have to be referred to the Royal Hong Kong Police via the Attorney General. In those instances which only relate to offences under the Theft Ordinance e.g. the sale of non existent products or when a blatant misrepresentation is involved, this would solely be a matter for the Police.

7.7 - In ITALY, the authority responsible for ensuring the transparency of the market and compliance with the requirements regarding the disclosure of information to the public is the CONSOB, which informs the law enforcement authorities in the event of presumed violations of criminal law.

In addition, *Law 1/1991* provides that the Chairman of the CONSOB may issue an urgent order to suspend, as a precautionary measure for a period of not more than sixty days, a securities investment firm from exercising the activities with regard to whose performance by the firm there is presumptive evidence of irregularities or breaches of the law or of regulations or orders issued by the supervisory authorities. Such measures have to be approved by the Minister of the Treasury. When there is presumptive evidence of serious irregularities or serious breaches of the law or of regulations or orders issued by the supervisory authorities in the management of a securities investment firm, and whenever this is required to safeguard investors, the CONSOB, after consulting the Bank of Italy, may temporarily suspend the firm's listing in the register for all the activities it exercises. In the event of an ascertained irregularity or ascertained breach of the law or of regulations or orders issued by the supervisory authorities, the Minister of the Treasury, acting on a proposal from the CONSOB or the Bank of Italy, may suspend a securities investment firm from exercising the activities in whose performance by the firm the irregularity or breach has been ascertained. When serious irregularities are ascertained in the management of a securities investment firm, the Minister of the Treasury provides for the CONSOB to suspend the firm's registration. If the ascertained irregularities or breaches threaten the stability of the markets or the protection of investors, the Ministry of the Treasury provides for the CONSOB to cancel the firm's registration.

The suspension or revocation of authorization are also applicable to the credit institutions.

7.8 - In JAPAN, if the sanction to be imposed is 1) Administrative : the authority in charge of investigating is the Securities Bureau of the Ministry of Finance and, insofar as the sanction by the Japan Securities Dealers Association is concerned, JSDA may conduct investigation ; 2) Civil : the Ministry of Finance is not concerned because it is a matter of private law ; 3) Criminal : the public prosecutor.

7.9 - In SPAIN, (translation provided) investigations in view of administrative sanctions are carried out by the CNMV. When a criminal investigation is initiated the proofs will be brought by the parties and the police.

7.10 - In SWEDEN, the competent investigating authority about criminal cases is the police when the general prosecutor has taken preliminary actions. In certain matters, special investigations might be effected by, for instance, tax authorities. Violations e.g. against capital adequacy requirements, margin requirements and other regulating directives are investigated by the Supervisory Authority and, if necessary, suitable actions are taken.

7.11 - In SWITZERLAND, competent authorities are all cantonal prosecutors for offences of penal nature, and judges for civil cases.

7.12 - In THE NETHERLANDS, the competent authorities in charge of investigating alleged violations are the Securities Board of The Netherlands (STE), at request of the STE, the Economic Investigation Service and, by order of the STE the Compliance Divisions of the Exchanges. Furthermore, the Compliance Divisions of the Exchanges can investigate their members on their own initiative. The competent authority in charge of investigating criminal violations is the Economic Control Board.

7.13 - In the UNITED KINGDOM, if the firm concerned is authorised, it is the responsibility of his FSA regulator (SRO or Recognised Professional Body ["RPB"] or SIB) to investigate his behaviour and to liaise with the appropriate prosecuting authority. SIB, or in certain circumstances, DTI, is responsible for investigating allegations of unauthorised trading. DTI is responsible for investigating allegations of offences under Section 47 of the *FSA*. The police are responsible for the *Theft Acts*.

7.14 - In the UNITED STATES,

7.14.1 - Answer of the SEC

CIVIL.- The SEC has broad civil authority to investigate violations of all the matters described above. SROs also are empowered to conduct civil investigations for violations of their rules. State securities regulators also are authorized by State law to investigate and prosecute civil violations of State securities laws.

CRIMINAL.- The United States Department of Justice, with the assistance of the Federal Bureau of Investigation, the US Postal Service and possibly other investigatory authorities, are competent to investigate and prosecute criminal violations involving securities. Such investigations would cover potential criminal violations of the federal anti-fraud and anti-manipulation statutes, the use of interstate commerce to carry out frauds (such as the use of telephones and the mails), and false statements to the SEC. Criminal prosecutions of cases involving possible violations of State securities laws are handled by State attorneys general, local prosecutors and police.

7.14.2 - Answer of the CFTC

The CFTC is the US governmental authority charged with investigation of possible violations of the *CEA* and the CFTC rules and regulations thereunder, and with civil and administrative enforcement of the provisions of the *CEA*. In addition, as noted, violations of certain provisions of the *CEA*, including the anti-fraud provisions are also criminal violations [31]. Criminal investigatory and prosecutorial authority resides with the US Department of Justice. The CFTC often cooperates closely with the Department of Justice in criminal investigations involving violations of the anti-fraud provisions of the *CEA*, and may refer matters that come to its attention to the Department of Justice.

(31) - 7 USC §13.