

18 NCAC 06A .1706 RECORD-KEEPING REQUIREMENTS FOR INVESTMENT ADVISERS

(a) Except as otherwise provided in Paragraph (j) of this Rule, every investment adviser registered or required to be registered under the Act shall make and keep true, accurate and current the following books, ledgers and records:

- (1) A journal or journals, including cash receipts and disbursements records, and any other records of original entry forming the basis of entries in any ledger;
- (2) General and auxiliary ledgers (or other comparable records) reflecting asset, liability, reserve, capital, income and expense accounts;
- (3) A memorandum of each order given by the investment adviser for the purchase or sale of any security, of any instruction received by the investment adviser from the client concerning the purchase, sale, receipt or delivery of a particular security, and of any modification or cancellation of any such order or instruction. Such memoranda shall show the terms and conditions of the order, instruction, modification or cancellation; shall identify the person connected with the investment adviser who recommended the transaction to the client and the person who placed such order; and shall show the account for which entered, the date of entry, and the bank or dealer by or through whom executed where appropriate. Orders entered pursuant to the exercise of discretionary power shall be so designated;
- (4) All check books, bank statements, canceled checks and cash reconciliations of the investment adviser;
- (5) All bills or statements (or copies thereof), paid or unpaid, relating to the business of the investment adviser as such;
- (6) All trial balances, financial statements, and internal audit working papers relating to the business of such investment adviser;
- (7) Originals of all written communications received and copies of all written communications sent by such investment adviser relating to:
 - (A) Any recommendation made or proposed to be made and any advice given or proposed to be given,
 - (B) Any receipt, disbursement or delivery of funds or securities, or
 - (C) The placing or execution of any order to purchase or sell any security; provided, however,
 - (i) that the investment adviser shall not be required to keep any unsolicited market letters and other similar communications of general public distribution not prepared by or for the investment adviser, and
 - (ii) that if the investment adviser sends any notice, circular or other advertisement offering any report, analysis, publication or other investment advisory service to more than ten persons, the investment adviser shall not be required to keep a record of the names and addresses of the persons to whom it was sent; except that if such notice, circular or advertisement is distributed to persons named on any list, the investment adviser shall retain with the copy of such notice, circular or advertisement a memorandum describing the list and the source thereof;
- (8) A list or other record of all accounts in which the investment adviser is vested with any discretionary power with respect to the funds, securities or transactions of any client;
- (9) All powers of attorney and other evidences of the granting of any discretionary authority by any client to the investment adviser, or copies thereof;
- (10) All written agreements (or copies thereof) entered into by the investment adviser with any client or otherwise relating to the business of such investment adviser as such;
- (11) A copy of each notice, circular, advertisement, newspaper article, investment letter, bulletin or other communication recommending the purchase or sale of a specific security, which the investment adviser circulates or distributes, directly or indirectly, to ten or more persons (other than clients receiving investment supervisory services or persons connected with such investment adviser), and if such notice, circular, advertisement, newspaper article, investment letter, bulletin or other communication does not state the reasons for such recommendation, a memorandum of the investment adviser indicating the reasons thereof;
- (12) The following records:
 - (A) A record of every transaction in a security in which the investment adviser or any advisory representative of such investment adviser has, or by reason of such transaction acquires, any direct or indirect beneficial ownership, except:

- (i) Transactions effected in any account over which neither the investment adviser nor any advisory representative of the investment adviser has any direct or indirect influence or control; and
 - (ii) Transactions in securities which are direct obligations of the United States
Such record shall state the title and amount of the security involved; the date and nature of the transaction (i.e., purchase, sale or other acquisition or disposition); the price at which it was effected; and the name of the dealer or bank with or through whom the transaction was effected.
Such record may also contain a statement declaring that the reporting or recording of any such transaction shall not be construed as an admission that the investment adviser or advisory representative has any direct or indirect beneficial ownership in the security. A transaction shall be recorded not later than 10 days after the end of the calendar quarter in which the transaction was effected.
 - (B) For purposes of this Subparagraph (a)(12), the term "advisory representative" shall mean any partner, officer or director of the investment adviser; any employee who makes any recommendation, who participates in the determination of which recommendation shall be made, or whose functions or duties relate to the determination of which recommendation shall be made; any employee who, in connection with his duties (other than clerical, ministerial or administrative duties), obtains any information concerning which securities are being recommended prior to the effective dissemination of such recommendations or of the information concerning such recommendations; and any of the following persons who obtain information concerning securities recommendations being made by such investment adviser prior to the effective dissemination of such recommendations or of the information concerning such recommendations:
 - (i) any person in a control relationship to the investment adviser,
 - (ii) any affiliated person of such controlling person, and
 - (iii) any affiliated person of such affiliated person."Control" shall have the same meaning as that set forth in Section 2(a)(9) of the Investment Company Act of 1940, as amended.
 - (C) An investment adviser shall not be deemed to have violated the provisions of this Subparagraph (a)(12) because of his failure to record securities transactions of any advisory representative if he establishes that he instituted adequate procedures and used reasonable diligence to obtain promptly reports of all transactions required to be recorded;
- (13) Records required of investment advisers primarily engaged in other businesses:
- (A) Notwithstanding the provisions of Subparagraph (a)(12) in this Rule, where the investment adviser is primarily engaged in a business or businesses other than advising registered investment companies or other advisory clients, a record must be maintained of every transaction in a security in which the investment adviser or any advisory representative of such investment adviser has, or by reason of such transaction acquires, any direct or indirect beneficial ownership, except:
 - (i) Transactions effected in any account over which neither the investment adviser nor any advisory representative of the investment adviser has any direct or indirect influence or control; and
 - (ii) Transactions in securities which are direct obligations of the United States
Such record shall state the title and amount of the security involved; the date and nature of the transaction (i.e., purchase, sale or other acquisition or disposition); the price at which it was effected; and the name of the dealer or bank with or through whom the transaction was effected. Such record may also contain a statement declaring that the reporting or recording of any such transaction shall not be construed as an admission that the investment adviser or advisory representative has any direct or indirect beneficial ownership in the security. A transaction shall be recorded not later than 10 days after the end of the calendar quarter in which the transaction was effected.
 - (B) An investment adviser is "primarily engaged in a business or businesses other than advising registered investment companies or other advisory clients" when, for each of its three most recent fiscal years or for the period of time since organization, whichever is

lesser, the investment adviser derived, on an unconsolidated basis, more than 50 percent of:

- (i) its total sales and revenues; and
 - (ii) its income (or loss) before income taxes and extraordinary items;
- from such other business or businesses.

(C) For purposes of this Subparagraph (13), the term "advisory representative", when used in connection with a company primarily engaged in a business or businesses other than advising registered investment companies or other advisory clients, shall mean any partner, officer, director or employee of the investment adviser who makes any recommendation, who participates in the determination of which recommendation shall be made, or whose functions or duties relate to the determination of which recommendation shall be made, or who, in connection with his duties (other than clerical, ministerial or administrative duties), obtains any information concerning which securities are being recommended prior to the effective dissemination of such recommendations or of the information concerning such recommendations; and any of the following persons who obtain information concerning securities recommendations being made by such investment adviser prior to the effective dissemination of such recommendations or of the information concerning such recommendations:

- (i) any person in a control relationship to the investment adviser,
- (ii) any affiliated person of such controlling person, and
- (iii) any affiliated person of such affiliated person.

"Control" shall have the same meaning as that set forth in Section 2(a)(9) of the Investment Company Act of 1940, as amended (see G.S. 78A-2(10)).

(D) An investment adviser shall not be deemed to have violated the provisions of this Subparagraph (13) because of his failure to record securities transactions of any advisory representative if he establishes that he instituted adequate procedures and used reasonable diligence to obtain promptly reports of all transactions required to be recorded;

(14) A copy of the following:

- (A) A copy of each written statement and each amendment or revision thereof, given or sent to any client or prospective client of such investment adviser in accordance with the provisions of Rule .1707;
- (B) any summary of material changes that is required by Part 2 of Form ADV but is not contained in the written statement; and
- (C) a record of the dates that each written statement, and each amendment or revision thereof, was given, or offered to be given, to any client or prospective client who subsequently becomes a client.

(15) A memorandum describing any legal or disciplinary event listed in Schedule D of Form ADV or in any Form U-4 relating to any of the investment adviser's investment adviser representatives and presumed to be material, if the event involved the investment adviser or any of its investment adviser representatives or supervised persons and is not disclosed in the written statements described in Paragraph (a)(14)(A) of this Section. The memorandum must explain the investment adviser's determination that the presumption of materiality is overcome, and must discuss the factors described in those items.

(16) For each client that was obtained by the adviser by means of a solicitor to whom a cash fee was paid by the adviser:

- (A) evidence of a written agreement to which the adviser is a party related to the payment of such fee;
- (B) a signed and dated acknowledgement of receipt from the client evidencing the client's receipt of the investment adviser's disclosure statement and a written disclosure statement of the solicitor; and
- (C) a copy of the solicitor's written disclosure statement.

The written agreement, acknowledgment and solicitor disclosure statement will be considered to be in compliance with Rule .1717. For purposes of this Rule, the term "solicitor" shall mean any person or entity who, for compensation, acts as an agent of an investment adviser in referring potential clients.

- (17) Copies, with original signatures of the investment adviser's appropriate signatory and the investment adviser representative, of each initial Form U-4 and each amendment to Disclosure Reporting Pages (DRPs U-4) must be retained by the investment adviser (filing on behalf of the investment adviser representative) and must be made available for inspection upon regulatory request.
- (b) If an investment adviser subject to Paragraph (a) of this Rule has custody or possession of securities or funds of any client, the records required to be made and kept under Paragraph (a) of this Rule shall also include:
- (1) A journal or other record showing all purchases, sales, receipts and deliveries of securities (including certificate numbers) for such accounts and all other debits and credits to such accounts;
 - (2) A separate ledger account for each such client showing all purchases, sales, receipts and deliveries of securities, the date and price of each such purchase and sale, and all debits and credits;
 - (3) Copies of confirmations of all transactions effected by or for the account of any such client; and
 - (4) A record for each security in which any such client has a position, which record shall show the name of each such client having any interest in each security, the amount or interest of each such client, and the locations of each such security.
- (c) Every investment adviser subject to Paragraph (a) of this Rule who renders any investment supervisory or management service to any client shall, with respect to the portfolio being supervised or managed and to the extent that the information is reasonably available to or obtainable by the investment adviser, make and keep true, accurate and current:
- (1) Records showing separately for each such client the securities purchased and sold, and the date, amount and price of each such purchase and sale; and
 - (2) For each security in which any such client has a current position, information from which the investment adviser can promptly furnish the name of each such client, and the current amount or interest of such client.
- (d) Any books or records required by this Rule may be maintained by the investment adviser in such manner that the identity of any client to whom such investment adviser renders investment supervisory services is indicated by numerical or alphabetical code or some similar designation.
- (e) Duration requirement for maintenance of records:
- (1) All books and records required to be made under the provisions of Paragraphs (a) to (c)(1), inclusive, of this Rule shall be maintained and preserved in an easily accessible place for a period of not less than five years from the end of the fiscal year during which the last entry was made on such record, the first two years in the principal office of the investment adviser.
 - (2) Partnership articles and any amendments thereto, articles of incorporation, charters, minute books, and stock certificate books of the investment adviser and of any predecessor, shall be maintained in the principal office of the investment adviser and preserved until at least three years after termination of the enterprise.
- (f) An investment adviser subject to Paragraph (a) of this Rule, before ceasing to conduct or discontinuing business as an investment adviser, shall arrange for and be responsible for the preservation of the books and records required to be maintained and preserved under this Rule for the remainder of the period specified in this Rule, and shall notify the administrator in writing of the full address where such books and records will be maintained during such period.
- (g) Preservation and maintenance of records:
- (1) The records required to be maintained and preserved pursuant to this Rule may be immediately produced or reproduced by photograph on film or, as provided in Subparagraph (g)(2) of this Rule, on magnetic disk, tape or other computer storage medium, and be maintained and preserved for the required time in that form. If records are produced or reproduced by photographic film or computer storage medium, the investment adviser shall:
 - (A) arrange the records and index the films or computer storage medium so as to permit the immediate location of any particular record;
 - (B) be ready at all times to provide, and promptly provide, any facsimile enlargement of film or computer printout or copy of the computer storage medium which the administrator by its examiners or other representatives may request;
 - (C) store separately from the original one other copy of the film or computer storage medium for the time required;

- (D) with respect to records stored on a computer storage medium, maintain procedures for maintenance and preservation of, and access to, records from loss, alteration, or destruction; and
 - (E) with respect to records stored on photographic film, at all times have available for the administrator's examination of its records pursuant to Section 78C-18(e) of the Act, facilities for immediate, legible projection of the film and for producing legible facsimile enlargements.
- (2) Pursuant to Subparagraph (g)(1) of this Rule an adviser may maintain and preserve on computer tape or disk or other computer storage medium records which, in the ordinary course of the adviser's business, are created by the adviser on electronic media or are received by the adviser solely on electronic media or by electronic data transmission.
- (h) For purposes of this Rule, "investment supervisory services" means the giving of continuous advice as to the investment of funds on the basis of the individual needs of each client.
- (i) Every registered investment adviser shall maintain within this state, in a readily accessible location, all records required by this Rule. A written request for the waiver of the provisions of this Section may be made to the administrator to permit any registered investment adviser to maintain any of the records required by this Rule in some place other than the State of North Carolina. In determining whether or not the provisions of this Rule shall be waived, the administrator may consider, among other things, whether the main office of the investment adviser is in a place outside the State of North Carolina or whether the investment adviser uses all or some of the bookkeeping facilities of some other investment adviser whose main office is outside the State of North Carolina.
- (j) Every investment adviser that has its principal place of business in a state other than this state shall be exempt from the requirements of this section, provided the investment adviser is licensed in such state and is in compliance with such state's record keeping requirements, if any.

*History Note: Authority G.S. 78C-18(a); 78C-18(b); 78C-18(e); 78C-30(a);
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Temporary Amendment Eff. January 14, 2002;
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