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ANNEX

INTRODUCTION AND EXECUTIVE SUMMARY

Internet technology is profoundly affecting the evolution of financial services activities. Issuers¹ and financial service providers increasingly sell securities or provide financial services on the Internet. Indeed, the typically “non-physical” or “dematerialized” nature of securities transactions makes the Internet an appealing medium for the financial services industry. At a relatively low cost, the Internet offers unprecedented immediacy, flexibility and interactivity, magnifying the financial services industry’s ability to reach into the retail market.

Investors use the Internet to connect with the financial services industry domestically and globally. As personal computers continue to move into homes and offices, investors are migrating to the Internet to make investment decisions and conduct investment activities. As a communication medium, the Internet provides investors with unparalleled access to financial tools and services worldwide, all at a relatively low cost and with relative ease.

The explosion in Internet use, however, also presents new challenges for securities regulators and self-regulatory organizations (SROs). Electronic communication and interactivity may not fit neatly within the parameters of statutes, regulations and directives originally intended for a telephone- and paper-based environment, thus creating unnecessary regulatory burdens or unintended regulatory gaps. Moreover, the very qualities that make the Internet a valuable tool for investors and the securities industry may render it a convenient tool to perpetrate securities fraud and other violations. The Internet also provides for instantaneous cross-border communication and interactivity, which challenge traditional notions of jurisdiction and territoriality.

In response to these challenges, the Technical Committee of the International Organization of Securities Commissions (IOSCO) created an Internet task force (Task Force) to examine and provide guidance on issues relating to the impact of the Internet on securities regulation. With input from the Technical Committee’s Working Parties 2, 4 and 5, this report addresses the regulatory and enforcement issues posed by securities activities conducted over the Internet. This report identifies those Internet issues that should be addressed by each jurisdiction and provides guidelines on how to approach those issues. It is not the role of IOSCO, however, to provide legal interpretations or set universal standards with respect to the use of the Internet by the financial service industry. These issues must be determined under the domestic statutory schemes of each jurisdiction. This report was approved by the Technical Committee at its meeting in Nairobi, Kenya on September 13, 1998.

¹ In this report, where the context permits, the term “issuer” encompasses all issuers of securities including collective investment schemes (CIS), “financial service provider” encompasses brokers, dealers, investment advisers, underwriters and banks (*i.e.*, universal banks engaged in a securities business), “securities” and “securities markets” refer to the various market sectors and also, where relevant, shall be understood to include the derivatives markets (the same applies to the use of the term “securities regulation.” *See* IOSCO by-laws, Explanatory Memorandum), “investors” encompasses customers and other consumers of financial services, “financial service industry” encompasses issuers and financial service providers, “securities industry” encompasses the financial service industry and markets, and “market participants” encompasses the financial services industry and investors.

Key Principles

Our discussion of the appropriate securities regulatory framework for the Internet, as with any new medium, begins with an examination of the principles of securities regulation. For the purposes of this report, the three fundamental objectives of securities regulation are:

- the protection of investors;
- ensuring that securities markets are fair, efficient and transparent; and
- the reduction of systemic risk.

Against this background, regulators should consider the following principles when formulating policies regarding specific securities activities on the Internet.

1. *The fundamental principles of securities regulation do not change based on the medium.*
2. *Consistent with the fundamental principles of securities regulation, regulators should not unnecessarily impede the legitimate use of the Internet by market participants and markets.*
3. *Regulators should strive for transparency and consistency regarding how their regulations apply in an Internet environment.*
4. *Regulators should cooperate and share information to monitor and police securities activity on the Internet effectively.*
5. *Regulators should recognize that electronic media and the use of such media is likely to evolve.*

Key Recommendations

The key principles described above guide the following recommendations:

A. Application of Domestic Regulatory Requirements to Securities Activities on the Internet

Offers and Advertisements

1. Regulators and SROs should provide guidance to alert market participants and markets as to how their existing registration, licensing and other regulatory requirements apply to offers and advertisements conducted on the Internet and alert them to the possibility that other jurisdictions likewise may impose other requirements.
2. Regulators should amend, or seek to have the relevant authorities or legislative bodies amend, specific requirements when appropriate to accommodate and ensure appropriate regulatory coverage of the Internet environment.
3. General antifraud provisions should apply to all offers and advertisements involving securities or financial services, regardless of the medium and regardless of whether a regulator or SRO is involved in approving the offer or advertisement.
4. Regulators and, where appropriate, SROs should strengthen surveillance of Internet advertising and offerings for unauthorized or fraudulent activities.

Delivery of Disclosure Documents and Other Information

5. Regulators should ensure that issuers who use the Internet to communicate with and send offering material to shareholders and potential investors provide the same disclosure about their operations, financial condition and securities that would be provided in a paper-based medium, so that investors can evaluate the risk and value of investing in the issuer.
6. Regulators should provide guidance for the financial service industry on the use of the Internet to satisfy their obligation to deliver disclosure documents.

In providing guidance, regulators should consider what constitutes delivery and the extent to which electronic delivery provides timely and adequate notice.

In permitting the use of electronic delivery by the financial service industry, regulators should require that investor access to electronic communications be at least as good as that provided by paper delivery.

Regulators should permit the financial service industry to deliver disclosure documents electronically when an investor has given an informed consent to this form of delivery.

Voting in Meetings

7. Subject to investor protection and confidentiality concerns, regulators should explore the possibilities under their company laws to enable issuers, transfer agents, depositories and broker-dealers to make full use of the Internet for the dissemination of voting information and in the proxy voting process as one means to facilitate full participation by shareholders in annual and other meetings of shareholders.

Communications and Customer Orders

8. Regulators should require that financial service providers continue to satisfy suitability and general conduct requirements when transacting business over the Internet.
9. Regulators should require that financial service providers ensure that their computer networks have sufficient operational integrity (security, reliability, capacity, backup systems and alternative means of communication) and that they have adequate personnel to handle Internet communications, including trading instructions.
10. Regulators should consider requiring financial service providers to develop written procedures for the review of incoming and outgoing electronic correspondence between employees and the public relating to the financial service provider's securities business.
11. Regulators should clarify if, and under what circumstances, the use of authentication technologies will be allowed and when manual signatures will be required.

Recordkeeping

12. Recordkeeping requirements applicable to financial service providers should apply to Internet transactions. Regulators need to be satisfied that the key standards of recordkeeping can be met regardless of the technology used (*e.g.*, that certain records be created and maintained; that these records are durable, cannot be altered and are available and accessible to the regulator).
13. Recordkeeping policies and requirements should address e-mail communications that relate to the securities business of a financial service provider.

B. Exercise of Regulatory Authority over Cross-Border Securities Activities on the Internet

14. Regulators should provide guidance on the circumstances under which they will exercise regulatory authority over Internet offers.
15. If an issuer's or financial service provider's offer or sales activities over the Internet occur within a regulator's jurisdiction, or if the issuer's or financial service provider's offshore activities, in fact, have a significant effect upon residents or markets in the regulator's jurisdiction, a regulator may impose its regulatory requirements (*e.g.*, licensing and registration requirements) on such activities.
16. Regulators should examine the following factors in determining whether to assert regulatory authority over an offer of securities or financial services on the Internet.

Factors that may support the assertion of regulatory authority include:

It is evident that information is targeted to residents of the regulator's jurisdiction.

The issuer or financial service provider accepts purchases from or provides services to residents of the regulator's jurisdiction (unless made pursuant to an exemption or under circumstances that may exclude a public offering).

The issuer or financial service provider uses e-mail or other media to "push" the information to residents of the regulator's jurisdiction.

Factors that may support a decision not to assert regulatory authority include:

The issuer or financial service provider clearly states to whom the Internet offer is directed, rather than appearing to extend the offer into any jurisdiction.

The Web site contains a statement listing those jurisdictions in which the issuer or financial service provider has been (or has not been) authorized to offer or sell its securities or services.

The issuer or financial service provider takes precautions that are reasonably designed to prevent sales to residents in the regulator's jurisdiction.

C. Use of the Internet to Foster Investor Education and Transparency

17. Regulators and SROs should include use of the Internet in educating investors and providing guidance to the securities industry.
18. Regulators and SROs should educate investors about securities fraud on the Internet by providing information about possible fraudulent activities. For example, regulators and SROs could use their Web sites to post warnings regarding false or misleading

offerings or advertisements.

19. Regulators, SROs, and organized markets should consider using their Web sites to provide current and potential investors with access to information about their organizations, including current laws, regulations, by-laws and governance procedures.
20. Regulators, SROs, and organized markets should facilitate investor access to corporate and market information by developing electronic databases for reports and legally required disclosure documents, and making the information publicly available on their Web sites.

D. Use of the Internet to Enhance Cooperation in Enforcement Matters

21. Regulators or other authorities in their jurisdictions should have the authority to gather and share information regarding activities that occur over the Internet that appear questionable or that have been prosecuted in their jurisdictions.
22. Regulators and SROs should strengthen surveillance of Internet activities by routinely monitoring for unauthorized or fraudulent activities.
23. Regulators and SROs should have staff sufficiently trained in current techniques for conducting surveillance on the Internet.
24. Regulators should assist one another by exchanging details about techniques for monitoring Internet advertising, offers of securities or financial services that may contain false or misleading information, and by sharing expertise with regulators who have limited experience in this area.

Structure of the Report

The report is divided into four parts and an annex.

Part I describes the general characteristics of the Internet, specifically those characteristics that distinguish it from traditional methods of communication.

Part II examines the current uses of the Internet by market participants and markets and, where relevant, describes the regulatory concerns posed by those uses.

Part III reviews the current regulatory responses to these issues. In addition, the current Internet use by securities regulators is described.

Part IV specifically addresses the key principles mentioned above and sets forth recommendations and guidelines for securities regulators.

The annex contains a list of significant Internet-related statements of certain jurisdictions and

uniform resource locators where the full text of these statements may be obtained. IOSCO jurisdictions are encouraged to contribute to the annex and update it upon publication of notable Internet-related statements.

PART I: CHARACTERISTICS OF THE INTERNET

The term "Internet" generally refers to an informal, worldwide network of computers linking millions of users. Although the information disseminated over the Internet may be no different from the information disseminated by telephone and fax machine, the Internet provides several new methods of communication.

Each of these new methods of communication provides for ease, immediacy and low cost in the dissemination of information, "interactivity," hyperlinks, decentralization, anonymity and flexibility. These characteristics, discussed below, present new opportunities for the securities industry and raise new challenges and concerns for securities regulators. The purpose of this section is not to provide a comprehensive statement of the constantly evolving characteristics of the Internet, but rather to set the context for the discussion of regulatory issues that follows.

A. Widespread and Instantaneous Communication

The Internet provides for several different methods of communication. Generally, communications are sent through the Internet via the World Wide Web (Web), electronic bulletin boards, e-mail and personal broadcast networks. A common characteristic of these methods is the widespread and almost instantaneous communication with other users. The Internet is accessible by any person who has a personal computer and an account with an Internet service provider. It is currently estimated that the Internet is used worldwide by approximately 130 million people.²

A widely publicized mechanism to distribute information on the Internet is the Web. The Web is a vast network of sites which are collections of Web pages stored on a single computer. Web pages are graphical, audio and textual presentations of information that can be revised and updated. A single entity or individual typically controls the information that appears on a Web site. The mere posting of information on a Web site potentially makes it available worldwide. While access to Web sites can be restricted through the use of technologies that, for example, require passwords or identification, the majority of Web sites currently are freely accessible.

Web sites have many applications in the financial services industry. They permit individuals and entities to distribute information about securities to a wide audience. They also can be used to dispense investment advice, to make offers for the purchase or sale of securities, and to effect transactions. Visitors to a Web site can analyze the information and use the interactive features of the Web site, but generally speaking, cannot modify the existing Web site information.³

A second mechanism used to distribute information on the Internet is electronic bulletin

² For current statistics on regional and global Internet use see (visited Sept. 8, 1998) <http://www.nua.ie/surveys/how_many_online/index.html>.

³ The information can be copied from one Web site, posted to another site, and then altered. In this way, Internet users may be misled into thinking that they are viewing an authentic Web site, when they are actually viewing a counterfeit. This possibility raises issues of security and authentication, discussed later in this report.

boards, also referred to as newsgroups (*i.e.*, bulletin boards about particular topics) or message boards. As its name implies, an electronic bulletin board is analogous to its physical counterpart, and is accessible to any member of the public with a personal computer and Internet access. A “chat room” is a form of bulletin board that enables users to communicate with each other one-on-one or in a group, on a real-time basis.

A third mechanism used to distribute information over the Internet is electronic mail (e-mail). An e-mail is an electronic message, similar to a letter or a fax, that is directed to a particular addressee. E-mail messages, like mass mailings, can be sent to vast numbers of addressees. The contents of an e-mail message, in principle, are available only to the particular addressees. However, there are several ways for e-mail messages to be read or altered by someone other than the intended recipient.

A fourth mechanism used to distribute information over the Internet is “File Transfer Protocol” (FTP). FTP allows files (not messages) to be sent from one computer to another. FTP is particularly useful for software distribution and the “downloading” of files containing public domain software and computer programs.

A fifth mechanism used to distribute information over the Internet is the personal broadcast network. When using this technology, consumers download computer “tuners,” similar to radio or television station tuners, free of charge. Providers of information then pay a fee to transmit information to anyone who has activated a tuner. A similar form of technology, called “push media,” allows information to be distributed to viewers automatically, without any need for the viewer to contact a particular Web site or bulletin board system. Rather, the information is “pushed” at individuals while they are on-line or while logging on to their computers, regardless of where they are located.

B. Low Cost

Dissemination of information over the Internet is inexpensive and can reach a broad audience, domestic or international, in seconds. Downloading the necessary software programs from the Internet can provide the tools to produce Web sites quickly and easily. Basic access costs normally are comprised of the telecommunication cost involved in connecting to a local Internet service provider and a fee charged by the provider. No special equipment is required, other than browser software and a modem connection to an Internet service provider, which have become standard features of many personal computers.

The Internet provides an ideal environment for issuers and financial service providers to access a worldwide customer base, and to provide potential investors with large quantities of detailed information quickly and inexpensively. These low costs contribute to the enormous amount of information that is available to investors (some of which may be stale or unreliable). The low costs and broad access associated with use of the Internet also make it an attractive medium for persons contemplating misleading, fraudulent or manipulative schemes.

C. Interactivity

The Internet provides its users with an interactive form of communication. Graphical, audio and written communication media are combined on the Internet to create credible and captivating Web sites and messages, which may become increasingly interactive as technologies such as voice recognition and virtual reality are improved. Interactive presentations that contain, for example, options to pay electronically or send in trading orders, allow investors to effectuate investment decisions instantly. Such an environment, however, could increase the temptation for impulsive, immediate and less reflective investment decisions by investors and could accelerate market overreactions in non-transparent markets that are susceptible to manipulation.

D. Hyperlinks

The Internet allows Web site sponsors, bulletin boards and newsgroups to establish electronic links, known as “hypertext” or “hyperlinks,” which allow for the interconnection of information and materials within (internal hyperlinks) and between (external hyperlinks) Web sites.⁴ A person accessing a specific Web site typically sees the home page first. The Web site’s home page is analogous to the cover page and table of contents of a book. The home page may contain internal hyperlinks to additional information on that Web site, or external hyperlinks to information on other Web sites. Hyperlinks allow viewers to move quickly and easily through documents to find the desired information and create proximity between information sources that is not available in the paper context. It is this rapid, cross-referencing mechanism that provides readers with a unique and valuable information-gathering tool.

Because hyperlinks can send a reader to a page in the middle of a document or Web site, the information may be provided out of context and without necessary cautionary or explanatory language. The improper use of hyperlinks is of concern to regulators because a hyperlink can give the appearance of legitimacy to otherwise non-legitimate information. For example, a Web site containing a non-legitimate or unauthorized offering of securities could contain a hyperlink to a regulator’s home page. The mere existence of the link could be construed to imply that the regulator has reviewed or approved the offering when, in fact, it has not. In addition, issues may arise such as whether hyperlinks from one site to another would constitute an implied endorsement of the material contained on the site to which a link is made.

E. Decentralization

The Internet is an “open” network without a central location from which the Internet emanates or from which it can be controlled. It is a highly decentralized system, comprised of millions of computers and sub-systems. This is in contrast to proprietary networks and commercial on-line networks, which are “closed” systems owned and operated by an entity that is responsible for maintaining and controlling its network.⁵

When a message is sent over the Internet, it is broken into small pieces and put into units

⁴ Alexander C. Gavis, *Hyperlinks in Mutual Fund Advertising*, Wallstreetlawyer.com, January 1998, at 1, 1.

⁵ In proprietary and commercial on-line networks, members typically pay a monthly fee to access the network. France’s Minitel and the United States’ America OnLine are examples of commercial, proprietary networks. Although these networks are extremely large (each with millions of members), they are distinguished, in part, from the Internet because they are centrally managed and controlled. Certain Internet networks that restrict access through the use of encryption technology or passwords are, in effect, “closed” networks.

called “packets,” all taking different routes before reassembling at the final destination. Because it is difficult to maintain the same capacity and quality level in all parts of the network, there is a risk of connection delays and failures. For instance, some Internet service providers may not have enough computing capacity or telephone lines to process large numbers of access requests.⁶ This may cause connection delays or failures, potentially resulting in some investors receiving information before others and opportunities for abuse. These risks, while posing significant logistical and technological challenges, may be remedied by improved communication technologies and greater system resources.

Security of customer orders and communications is of great concern to investors, regulators and the securities industry. The Internet’s open architecture, diverse routing, and lack of central control make it far more vulnerable to abuse by “crackers”⁷ than is the case with restricted access proprietary systems, which are often constructed with security in mind.

Encryption technology,⁸ however, is increasingly being used to ensure security of communication over the Internet. Many Web browsers contain generally reliable encryption technology that allow for recognition of digital signatures. For high risk or high value transactions, however, commercially available encryption technology may not be sufficient to guarantee a secure communication channel. To prevent intrusion of computer viruses and other unauthorized access, various measures can be taken, such as refusal of access without proper identification codes and passwords, and the use of firewalls.⁹

F. Anonymity

The Internet has several “anonymizing” tools that allow users to conduct Internet

⁶ Most Internet users are connected with the network through a server computer or a local Internet service provider using public telecommunication lines. Long distance telecommunication networks globally connect the computers of the Internet service providers. Communication between users is carried out through chains of server computers of the Internet service providers.

⁷ A cracker is an individual who attempts to access computer systems, e-mails and other private information without authorization and usually for illegal purposes. Conversely, “hackers” are persons who have an intimate understanding of the internal workings of a computer system or network and enjoy accomplishing difficult tasks. The term “hacker” is often misused in a pejorative context, where “cracker” would be the correct term. See Glee Harrah Cady & Pat McGregor, *Mastering the Internet* 805-06, 815 (1995).

⁸ Public-key cryptography is a security technology that is currently being used and developed for authentication purposes. In a public-key system, a user has software that generates two related keys, a public key and a private key, both of which are necessary to authenticate a transmission and to “unlock” messages encrypted by the corresponding key. For example, the user would keep its private key secure, but send the public key to persons from which it would like to receive messages. The messages are sent to the user, encrypted by the public key, and only its private key can decrypt them. See Daniel J. Greenwood & Ray A. Campbell, *Electronic Commerce Legislation: From Written on Paper and Signed in Ink to Electronic Records and Online Authentication*, 53 Bus. Law. 307, 310-16 (1997).

⁹ A firewall is a computer system that works as a barrier between the Internet and an internal network. Firewalls verify the source and destination of each message. Messages without proper identification and passwords are not allowed to penetrate the firewall, and are thus denied access to the internal network. Cady & McGregor, *supra*, at 536-537.

activities with privacy. Specifically, these anonymizers allow users to conceal their identities and countries of citizenship or residence. For example, users can access an anonymous “remailer” site that will obscure their identities by providing them with pseudonyms. Users can download software from the Internet, called an “anonymizer,” that acts as a middleman, masking the identities of the senders and the sources of information.

Anonymity is an attractive feature of the Internet for users who may wish to conduct business in privacy. However, anonymizers can be used for illegitimate reasons. For example, crackers use the anonymizers to “spoof” or impersonate others, as well as to alter or falsify e-mail messages en route to their final destinations.¹⁰ In addition, money can be transmitted electronically and anonymously on the Internet, making it difficult to track both its location and that of the investor. Anonymity, however, is neither an automatic feature of Internet activity, nor is it complete. The necessity of proving the authenticity and integrity of messages requires the use of digital signatures, which are incompatible with anonymity. In addition, most of the existing protocols for the electronic payment of money conceal the identity of the payer, but not that of the receiver.

Because the Internet relies on electronic networks and communications, its use generally creates an electronic audit trail, which can assist in tracking illegitimate transactions. It is possible, however, for anonymizing tools to strip the identifying information from the message, making it more difficult to follow the trail.

G. Flexibility

The Internet is a flexible medium for members of the securities industry, due to their ability to control the content of their Web sites. Unlike television and newspaper advertisements, information on Web sites can be easily and inexpensively erased or updated within minutes. New functions and services can be easily added. While the transient nature of information on a Web site provides enormous cost savings for market participants, it poses regulatory and evidentiary issues for securities regulators (see Part IV). For example, evidence of false or misleading statements on a Web site can be quickly erased or changed creating difficulties for regulators attempting to build an investigation.

¹⁰ There are several ways for messages to be intercepted en route to their destinations. For example, “spy” programs exist that monitor keystrokes of the senders, allowing a cracker to use the typed message to create a false posting that appears to come from the sender. A deceitful system administrator might read e-mail while it is stored prior to being sent, and use it later on for impersonation purposes. Also, a user with access to mail-routing computers can intercept e-mails, alter them, and send them on.

PART II: CURRENT INTERNET USE BY THE SECURITIES INDUSTRY

The Internet has presented the securities industry with opportunities for increased efficiencies, information flow and trading volume. Indeed, more and more market participants and markets are turning to the Internet to conduct securities activities. This section describes the current uses of the Internet by market participants and markets and, where relevant, examines the attendant regulatory issues.

A. Market Participants

(1) Investors

The Internet provides an unprecedented amount of information to individual investors. Investors use the Internet for obtaining research, market data, and the latest news reports as well as to communicate information quickly through the use of e-mail and message boards. Retail investors are increasingly using the Internet to open and maintain accounts on-line and to place trading orders.¹¹

By accessing many regulators' Web sites, investors may be able to obtain financial information about public issuers, review disciplinary histories of financial service providers, receive general warnings of security frauds, and lodge complaints. Investors also access Web sites that provide educational information. For example, many on-line services offer tutorials on trading strategies or collective investment scheme investing. Investors also are able to chart historical data, monitor portfolios, and receive notices of price moves.

Investors use the Internet to communicate with each other. They use chat rooms and newsgroups to discuss investment strategies and startup companies. Chat rooms and newsgroups, however, can also be places where fraud, manipulations and other illegal schemes are carried out.

(2) Issuers

Many issuers are using the Internet to communicate directly with their shareholders, potential investors and analysts. Disseminating corporate information is one of the more popular uses of issuer Web sites. Indeed, issuers frequently post financial information, product information, transfer agent information, security price history, ratings information, and expected earnings release dates on their Web sites.

Issuers who use the Internet enjoy faster, less expensive, and more widespread dissemination of information. This can have the effect of providing small investors with similar access to information as large investors, and with new avenues to obtain information from and communicate with company management. The Internet may assist smaller issuers in raising capital more efficiently by giving them better access to potential investors.

¹¹ Most jurisdictions, however, require that manual signatures be obtained to open accounts and conduct certain securities activities. This has resulted in the practice of broker-dealers sending out paper account-opening documentation following an on-line request from a customer.

(a) Public Offerings

Issuers are using the Internet to assist them in the public offering process. For example, issuers use the Internet to make information more broadly available to investors in the form of electronic “roadshows.” Roadshows are traditional marketing activities in which company management meets with investors to explain the company’s prospects and answer questions in connection with a forthcoming offering. These meetings have been limited both with respect to location and number of participants. Providing access to the roadshows over the Internet, both on a real-time and recorded basis, could serve to broaden the number and nature of investors who participate.

Where permitted, issuers also are making offerings of securities to the public directly through their Web sites without intermediation by broker-dealers. Many public companies are making direct offerings to their shareholders and other investors through their direct stock purchase plans, which provide a vehicle for investors to purchase securities. Until recently, an investor had to determine which public companies offered direct stock purchase plans and then call each company individually to learn the details of and enroll in its plan. The Internet has made this process easier, by providing on-line direct stock purchase plan directories. This easy access to information appears to be fueling the growth of direct stock purchase plans.

A growing number of public companies are implementing “self-service” employee benefit systems, including those that offer company securities as a part of the benefits package. These systems allow employees to access information regarding their company benefits through various media. Employers may use “intranets”¹² to assist their employees in managing their accounts.

These direct offerings conducted over the Internet raise certain regulatory issues. For example, while the offering may be exempt in one jurisdiction, registration of the offering may be required in others. Additionally, although prospectuses often are required, because financial intermediaries might not be involved in the offering, the entire burden may be on the investor to evaluate the information and to deal directly with the issuer.

(b) Disclosure and Communication

In some jurisdictions, issuers are permitted and are using the Internet to disseminate prospectuses and financial information to potential investors. In many jurisdictions, requirements focus on preventing premature or inappropriate disclosure, while in other jurisdictions the requirements focus on establishing minimum standards of disclosure. In some cases, certain information must be delivered to the investor, while in other cases the information need only be filed with the regulator or exchange and made public, so that the investing public has access to it. Issuers also are using the Internet to meet their obligation to deliver annual reports and proxy statements to those shareholders that have agreed to receive this information electronically.

The use of the Internet to communicate with investors, especially during the securities

¹² An intranet is a closed version of the Internet, for example, where only company employees have access. An intranet may allow employees to access their benefits information and conduct transactions on their home or office computers.

offering process, presents the issue of whether all of the material on a Web site must comply with the prospectus requirements (including material that is connected by hyperlinks). For example, regulators must consider whether the entity or person controlling a Web site (controller) that contains a prospectus, might be held responsible for the content of another Web site merely because it is linked to the controller's Web site. In addition, the ability of the controller of the Web site to erase or update information on the site presents prospectus compliance issues.

Issuers in some jurisdictions use Web sites and e-mail to allow shareholders to "attend," in real-time, annual meetings through their personal computers. Shareholders are able to ask questions by e-mail during the meeting. Web sites are also used in proxy contests allowing participants to communicate their views by posting proxy materials, press releases and letters. Shareholder disagreements can also be posted on-line. Increasingly, shareholders are able to vote by proxy over the Internet.

(c) Private Offerings

Private offerings of securities in virtually all jurisdictions are exempt from registration requirements. These exemptions may place limits on the manner of offering, the number and types of purchasers and offerees, the resale of the purchased securities, and the amount of money to be raised during a specific time period. Generally speaking, general solicitation or advertising is limited or not permitted in a private offering. Widespread availability of the offering materials over the Internet could create a conflict with private placement requirements. To address these limitations on solicitation, issuers and financial service providers have limited the access to their posted offering materials with the use of password technology. Qualified investors are given a password, which enables them to view private placements over the Internet.

(3) Financial Service Providers

Within the securities industry, financial service providers have most actively used the Internet for marketing and advertising purposes, for presenting information on portfolio analysis and market information, and for communicating with and receiving orders from potential investors and customers. Most major securities firms have Web sites containing information ranging from general corporate information to account opening documents. Capital market analyses, economic data, research information, real-time or delayed information on share and derivative prices, and information on special subjects, are also offered.

Financial service providers are able to send a variety of information to a large number of individuals over the Internet without having to rely on traditional mass media such as newspaper or mailings. This substantially reduces costs. By cutting costs through the use of the Internet, broker-dealers have started to offer reduced commission rates.

The lowest commissions currently are being offered by the new generation of electronic brokers. Electronic brokers are either extensions of existing brokers, who view the Internet as another channel through which they can provide their clients with access to a variety of services, or they are purely Web-based, officeless brokerages that take advantage of low overhead costs. The explosive growth of electronic brokers has provided investors with worldwide access to a

variety of financial services. This essentially borderless environment requires securities regulators to determine when and how their regulations will apply to these activities.

(a) Advertising

The Internet is becoming an important means for financial service providers to advertise their financial services and products. This can be accomplished effectively on their Web sites or by e-mail, in place of conventional direct-mail advertising. Advertising on the Internet may be especially effective for a multi-service company that may hyperlink to the Web sites of its subsidiaries and affiliates, providing investors access to information about the full range of financial services offered by the parent company. Investors can thus enjoy “one stop shopping” by gaining access to a single Web site. Financial service providers also advertise by paying for space on other Web sites (*e.g.*, Web sites of search engine companies).

Advertising through the Internet raises regulatory concerns. For example, an on-line financial service provider that offers multiple financial services (such as banking, securities and insurance services) on its Web site (or through a series of hyperlinked sites) may be subject to different regulatory regimes. A hyperlink to a foreign affiliate’s Web site may prompt the regulator of the parent company to assert regulatory authority over the affiliate’s activities. Likewise, the same hyperlink between parent and affiliate may prompt the regulator of the affiliate to assert regulatory authority over the parent’s activities on the Internet.

Additionally, the use of hyperlinks also raises concerns over the content and placement of disclosure information. For example, investors may not be able to distinguish between products and services that are offered by the parent company (*e.g.*, a bank) and its subsidiary or affiliates (*e.g.*, a broker-dealer). Additionally, misleading or fraudulent advertisements posted on the Internet can be viewed by a large number of investors, potentially magnifying the adverse impact of the fraud. Moreover, because of its flexibility and cost-effectiveness, the contents of advertisements over the Internet may be altered rapidly. This poses challenges for regulators in their role of ensuring that the advertising material meets relevant requirements. Additional regulatory concerns regarding disclosure and compensation are raised when a financial service provider places advertisements on other Web sites.

(b) Providing Investment Information and Investment Advice

The Internet enables investors to access an increasing amount of information related to investments, as financial service providers are actively disseminating a variety of information through the Internet. Some financial service providers post research reports on their Web pages and make them accessible only by customers who have certain passwords. Some circulate the equivalent of financial newsletters over the Internet and charge subscription fees.

These activities raise concerns for regulators. For example, a financial service provider’s duty to satisfy customer suitability (know your customer) and general conduct requirements when providing advice over the Internet may become more difficult as communications with customers become more attenuated (*i.e.*, less face-to-face or voice interaction). Further, investment information provided over the Internet may be made to appear legitimate, especially if there were

a hyperlink to something that is legitimate (*e.g.*, a regulator's Web site). Finally, financial service providers must have sufficient records of electronic activities to ensure that both they and their regulators have the ability to monitor the provision of on-line investment advice.

(c) Underwriting

The Internet is being used for underwriting purposes. Some broker-dealers are using their Web sites to conduct offerings of securities that they underwrite. Web sites are being used in a variety of ways to promote offerings.¹³ In addition, discount and on-line brokerage firms are now forming "e-syndicates" through which initial public securities offerings (IPOs) are distributed. The larger on-line brokerage firms have joined with traditional underwriters willing to offer them limited allocations of IPOs.

(d) Communicating with Investors

Investors may communicate with financial service providers through Web sites or by e-mail over the Internet to obtain specific information, open up an account, get information on transaction fees or send trading instructions. Likewise, financial service providers use e-mail as a means of communicating with their customers by sending customized investment advice, or even personal messages. The large volume of e-mail communications raises issues of adequate supervision of employee communications with customers and systems capacity. These electronic communications also raise recordkeeping issues. In addition, special care must be taken by financial service providers to ensure the authenticity and integrity of e-mail communications with their customers.

While the use of the Internet provides customers with many benefits, it also removes direct contact between the financial service provider and its customers. In an Internet transaction today, the financial service provider and customer may neither meet in person nor speak on the telephone. To ensure that investors can make well-informed decisions, financial service providers in many jurisdictions are obliged to provide material information and make appropriate disclosure about risks inherent in investments, according to their customer's investment experience and objectives. Without face-to-face or voice interaction, it may be more difficult for financial service providers to obtain enough information about a customer to meet suitability or other eligibility obligations.

(e) Customer Orders

Broker-dealers, are increasingly allowing investors to communicate trading instructions over the Internet. Although institutional investors sometimes deliver orders by e-mail, the main growth in the use of the Internet for sending orders is in the retail sector. Electronic broker-dealers are rapidly emerging in jurisdictions throughout the world.

Orders are placed over the Internet to a broker-dealer, which in turn sends the trade to the exchange floor through its own or the exchange's order routing system. This process could be

¹³ For example, see IPONET (visited Sept. 8, 1998) <<http://www.e-iponet.com>>.

automated in an electronic market. At present, however, orders are not transmitted directly by the customer via the Internet to the trading floor of an exchange or to an electronic market (*i.e.*, through the trading system of a member firm) in any jurisdiction.

In addition, when opening an account or accepting an order, broker-dealers may be required to identify the customer. This is especially important for preventing money laundering activities. Broker-dealers can comply with this requirement by confirming the identity of prospective customers by means other than the Internet (*e.g.*, face-to-face contact, or correspondence through ordinary mail), rather than completing the account opening procedure over the Internet. It is more likely, however, that where this possibility exists broker-dealers will verify the identity of the person who sent an order or opened an account over the Internet through the use of electronic verification services offered by certificate authorities.¹⁴

Broker-dealers often are unwilling to accept and execute customer orders unless payment is assured. Accordingly, many broker-dealers require an arrangement that assures payment from customers or limits the risks to which they are exposed (*e.g.*, margin requirements, advance payments, setting limits on transaction sizes, agreement on automatic withdrawals from customers' accounts). Finally, the capacity and reliability of a financial service provider's interface with the Internet and backup systems may become an issue when trading volume increases. During times of high volume, customers may be unable to access the financial service provider's Web site to place orders.

To address the security issues that arise when customer orders and communications are sent over the Internet, some financial service providers are adopting and developing security policies (including hiring independent computer security specialists) to enhance the security of their Internet-based systems. Regulators also are interested in seeing that financial service providers are vigilant in maintaining the security of their systems. However, internal compliance issues may arise when encryption technology is used in outgoing messages from financial service providers, since compliance officers may not be able to see the contents of the encrypted e-mail messages sent out by sales persons.

(f) Recordkeeping

The use of e-mail by financial service providers to communicate with investors, employees and other financial service providers raises the issue of how financial service providers can comply with recordkeeping obligations (*i.e.*, the creation and maintenance of required records and communications) and whether recordkeeping rules should be amended.

B. Markets

(1) Conventional Exchanges and Regulated Trading Markets

At present, conventional securities exchanges are using the Internet primarily as a tool for disseminating a variety of information to the public and for advertising their products and

¹⁴ Certificate authorities serve as trusted third parties that can authenticate the identity of each participant in a transaction and issue encrypted digital tokens of such identity in the form of public and private keys.

services. Some provide comprehensive information on their organizational structure and history. Many already have set up their own Web sites and provide market information (in some cases including real time quotes), trading rules and regulations. Some have two-way communication by e-mail to direct questions to staff about exchange rules and fees. Information on individual security prices, trading volume, contract terms, trading mechanisms, margin requirements and exchange rules are in some cases dealt with through a general description, and in other cases through comprehensive information. Some exchanges' Web sites contain a list of exchange members.

Some exchanges provide information on the listed companies, either in total or in specific market segments. These databases could include information about a company's head office, management, shareholders and financial condition. Only a few exchanges use the Internet to provide access to information filed with the exchanges by listed companies.

Some exchanges also offer educational information on trading strategies in order to educate investors about how to invest generally, as well as to provide specific information on special instruments, such as the risks associated with warrants and options. Some exchanges also allow simulated trading on the Internet.

In addition to communicating with the public, exchanges and other market infrastructure providers are exploring using the Internet for communicating with their members. It also would be possible for exchanges to use the Internet as part of their market infrastructure. For example, an exchange could provide links between broker-dealers and the exchange for order transmission, trade execution, and clearance and settlement. At least one exchange is developing an order routing facility that would allow members and member firms to enter orders through the Internet. Most exchanges already have developed sophisticated closed trading systems, using dedicated lines, for their operations. For exchanges with conventional closed membership structures, these systems are an efficient and secure way of providing access, since access to the system's central computer is limited to members.¹⁵ As security features continue to develop, Internet systems may become as secure as traditional closed systems.

(2) Organized Over-the-Counter Markets

The organized over-the-counter (OTC) markets typically serve as vehicles for broker-dealers to trade equity-type securities. These broker-dealers sometimes use computer screens provided by information vendors and other proprietary trading systems to communicate among themselves. The organized OTC markets, with central supervisory organizations that regulate their day-to-day operations, use the Internet primarily as a way to disseminate price quotations, other market data and investor education materials to the broker-dealers that trade in these organized OTC markets, to other market participants, and to the general public. Broker-dealers may eventually use the Internet to disseminate quote information, for order entry and execution, and for other types of communication among market participants. At this stage, however, market participants using electronic communication systems conduct their trading on proprietary trading

¹⁵ One of the major advantages of an Internet-based system may be its flexibility. However, even without using the Internet, many securities exchanges have flexible computer systems based on open architecture that allow member firms to connect their own in-house trading systems directly to the network provided by the exchange.

networks rather than the Internet.

(3) New Trading Facilities

(a) Use of the Internet by Alternative Trading Systems

Alternative trading systems (ATSs)¹⁶ have been developing outside conventional securities markets and are now multiplying. They provide investors with additional proprietary electronic trading facilities for securities that are traded principally on securities exchanges or other organized markets. Some ATSs have price discovery functions, others serve as matching systems, and still others serve as crossing systems using prices already established in organized markets such as securities exchanges (*e.g.*, closing price). Investors using ATSs may be able to lower their transaction costs.

The ATSs that currently exist are closed systems, however, and are not generally accessible to the public through the Internet. For emerging ATSs, the Internet could be used to increase order flow by providing new participants with easier access to their trading systems.

(b) Electronic Bulletin Boards

Although issuer and third-party bulletin boards operate in some markets, these mechanisms do not appear to have a significant amount of activity. An issuer bulletin board is essentially a forum for posting information and advertising offers of securities to prospective investors.¹⁷ A third-party bulletin board is similar to an issuer bulletin board, except that it is established and maintained by someone other than the issuer. Transactions on issuer and third party bulletin boards are effected wholly independent of the system.¹⁸

These systems have the potential to decrease transaction costs and improve transparency by disseminating information to potential investors. They also may be an effective means of facilitating transactions in emerging company securities, which often do not have liquid markets.¹⁹ Although investors can save brokerage commissions and avoid the spread between

¹⁶ For purposes of this report, the term “alternative trading systems” encompasses proprietary trading systems.

¹⁷ For example, a securities transaction on an issuer bulletin board is often carried out in the following way. A prospective buyer or seller posts a message on the bulletin board. Normally, investors are required to input an indication of interest to purchase or sell the security at a certain price, trading amount and contact information (*i.e.*, e-mail address, telephone number). Then, another investor who sees the information on the bulletin board contacts the buyer or seller. The two parties negotiate over the Internet or phone and, when the terms are agreed upon, they exchange funds and securities independently of the issuer and its transfer agent. The appropriate documentation is then submitted to the issuer’s transfer agent in order to transfer record ownership from the seller to the buyer.

¹⁸ To avoid triggering various regulatory requirements, the issuer or third party system does not play any role in effecting the transactions and does not receive compensation for creating or maintaining the system. Additionally, the issuer does not participate in any purchase or sale negotiations, does not provide advice as to whether an investor should buy or sell the security, and does not receive, transfer or hold funds or securities as part of its operation of the system. The issuer is required to keep records of all quotes entered into the system and make them available upon request to the regulator and any market on which the securities are listed.

¹⁹ These securities generally are not traded actively in an organized market (securities exchanges or organized

market makers' bids and asks when they trade directly through a bulletin board system,²⁰ they still have to pay costs associated with settling transactions and transferring record ownership. These costs can exceed traditional transaction charges. Moreover, when financial intermediaries are not involved in the transaction, investors are exposed to additional liquidity, credit and transactional risks.

The use of electronic bulletin boards raises a number of issues. The transactions between buyers and sellers using electronic bulletin boards are not governed by established market rules ensuring transparency (unlike the transactions carried out under the rulings and control of an exchange). Reliable arrangements for trade confirmation, delivery of the securities and secure payment are indispensable for the smooth functioning of any trading system. Such arrangements may not be provided in the absence of a financial intermediary.

(4) Clearance and Settlement

While the clearance and settlement of securities transactions still occur mostly in closed, dedicated systems, the Internet soon will be used to facilitate this function.²¹ Smaller clearing firms in particular may find clearing over the Internet to be more cost effective than clearing over dedicated systems. As technological advances make electronic payments over the Internet as, or even perhaps more, safe than traditional payment methods, investors will be able to settle transactions by transferring cash to a broker-dealer's account, or by using credit cards or an Internet-based banking service.

OTC markets) and often do not satisfy the listing requirements of those markets.

²⁰ Currently, issuers operate most electronic bulletin board systems on the Internet. Broker-dealers, as third parties, can operate a similar system for facilitating trades of illiquid small securities. A system operated by a broker-dealer could be regarded as an alternative trading system rather than a third-party bulletin board.

²¹ The National Securities Clearing Corporation (NSCC), a U.S. clearing agency, has announced plans to use the Internet to transmit information between itself and certain members. *See* NSCC Important Notice A 4715, *Launch of PC Web Direct - an Internet Application* (visited Sept. 8, 1998) <<http://www.nsccl.com/impnot/notices/notice1998/a4715.htm>>.

PART III: REGULATORY APPROACHES TO THE INTERNET

Securities regulators, like securities markets and market participants, also realize the benefits of the Internet and using it in innovative ways. They are not only responding to the regulatory issues raised in Part II, but also are making use of the Internet to enhance their own regulatory effectiveness.

Securities regulators are addressing the growth of securities transactions on the Internet with statements, rules and interpretations, specifically adopted in response to the use of the Internet by the securities industry. Part III briefly summarizes these developments, and describes how regulators use the Internet for their own purposes. The annex provides a list of published, Internet-related guidance from certain jurisdictions.²² All IOSCO jurisdictions are encouraged to contribute to the annex and update it when they publish significant Internet-related statements.

A. Published Statements

(1) Delivery and Disclosure Issues

In most jurisdictions, the securities laws require certain information to be delivered to investors. For regulators, the key issue is how electronic delivery of information should be seen as meeting those delivery requirements.

Many regulators have already adopted the general principle, endorsed by this report, that access to electronically delivered information should be at least as good as that provided by postal mail. What these regulators focus on is whether there has been effective delivery. Some regulators have stated that electronic delivery can be an acceptable alternative to paper delivery, and provided guidelines. Regulators seek to assure that investors receive electronic information on at least an equal or better basis than information received in paper form. Also, because access to the Internet is not yet universal, regulators have insisted that investors retain the option of requesting paper delivery.

(2) Recordkeeping

The securities regulatory framework requires the retention of certain records. Recognizing the growth in use of electronic records, some regulators have published statements seeking to ensure that these records are retained, not able to be altered, and accessible by regulators, regardless of the medium. Some regulators have already provided guidance to the securities industry about their policies with respect to the retention of e-mail communications.

(3) Registration and Other Regulatory Requirements

Many regulatory systems contain a range of exemptions from, and modifications of, the underlying regulatory requirements that persons must register or be authorized to carry on the business of operating an exchange, a brokerage firm or an investment advisory business. These

²² This report and the annex will be posted on IOSCO's Web site at <<http://www.iosco.org>>.

existing exemptions, which are often subject to conditions, frequently apply to private offerings or offerings to sophisticated investors. Some regulators have clarified whether and how these exemptions apply in the Internet context.

(4) Cross-Border Internet Offers

Internet communications that are not limited to a specific group of viewers (including communications through Web sites and bulletin boards) challenge the premise upon which many jurisdictions' securities regulations are based -- that when an offer is presented to residents of a jurisdiction, that offer, and the person who made that offer, may be subject to regulation. Several regulators have issued statements on their approach to cross-border offers, advertising and other material on the Internet.

There is no consensus among IOSCO members as to when Internet communications constitute an offer of securities or financial services. Indeed, securities regulators employ various approaches when analyzing whether a communication is an offer and, if so, whether the offer is being made to residents within their respective jurisdictions.

For example, some regulators do not consider information contained on a Web site to be an offer unless it contains both detailed information and a means to subscribe. Others consider less detailed information to be an offer, but do not consider the offer to be made in their jurisdiction unless such information is targeted at their residents. Some regulators consider an offer to be made in their jurisdiction simply if it can be viewed by their residents. Regulators in this latter group, however, generally will not exercise regulatory authority over the issuer or financial service provider unless there is evidence that the offer is targeted at their residents in some way.

Other regulators focus on whether the receipt of an offer over the Internet by one of their residents was volitional. Under this approach, if a viewer "pulls" the information from the Internet, such as by finding it on the Web site of an unauthorized issuer or financial service provider, the information would not constitute an offer. In contrast, if the information were "pushed" at the viewer, such as by e-mail, the information may be viewed as an offer.

While there is no single approach used by all task force members, they generally agree that the following activities would most likely be subject to the regulatory requirements (such as licensing or prospectus requirements) in their jurisdictions:

- ◆ An offer of securities or financial services is targeted or directed at their residents, *i.e.*, "pushed" at a resident in a particular jurisdiction.
- ◆ Even if the offer is not "pushed," there is sufficient information about the product or service to constitute an "offer" under local law, and the offer reasonably can be construed on some objective basis as being targeted at residents in a particular jurisdiction.
- ◆ Regardless of how the offer is presented, the level of regulatory interest may be

affected if the offer in fact generates significant sales from residents in a particular jurisdiction.

Regardless of the applicability of a jurisdiction's regulatory requirements, many jurisdictions are likely to assert authority over fraud or manipulation activities that place their residents at risk.

These approaches are not mutually exclusive. Also, this list does not contain all approaches used by regulators in determining whether an offer of securities or financial services has been made to residents in their jurisdictions. Part IV draws those approaches together and recommends some factors that regulators should take into account in addressing this critical issue.

B. Internet Uses by Regulators

(1) Investor Education

The Internet holds the promise of many benefits for investors, including improving their investment literacy. Accordingly, it is not surprising that a large number of regulators have established a significant presence on the Internet.

In addition to promoting the regulators' aims and objectives generally, the regulators' Web sites are intended specifically as investor education sites. They sometimes include advice on the relevant risks of investments in securities and derivatives, as well as specific warnings to investors about how to avoid becoming a victim of a fraudulent scheme.

Most regulators communicate with investors via e-mail. For example, some regulators have created complaint centers that the public can use to submit information electronically about potential violations. Users can complete an on-line complaint form describing the alleged violative conduct.

(2) Regulatory Matters

(a) Issuer Filings

In most jurisdictions, an issuer offering securities to the public is required to file or lodge certain information about the securities and the issuer with a regulator. Although these filings have traditionally been made in a paper form, some jurisdictions have introduced electronic filing systems in order to lower costs of the filings and to make it easier for the public to access the information disclosed in the filings.

(b) Rules, Notices and Announcements

Most regulators provide a general overview of their functions and organizational structure, relevant laws and publications, press releases, annual reports, bibliographical information and

special reports on their Internet Web sites. Also, in many cases, regulators' Web sites contain formal statements and letters to the industry dealing with current issues.

(c) Systematic Surveillance of Internet Communications and Enforcement Issues

The ease by which information can be disseminated over the Internet makes it an ideal environment where securities fraud can flourish. Regulators can use the Internet as a source of information to look for suspicious offers and market and price manipulation. Increasingly, regulators are conducting routine surveillance activities on the Internet. Further, since some Internet users are self-policing, regulators are provided with a great amount of detail about alleged securities illegalities on the Internet.

PART IV: KEY RECOMMENDATIONS

Domestically, regulators must determine whether their current regulatory framework adequately addresses use of the Internet by their respective markets, issuers and financial service providers. Internationally, the borderless nature of the Internet necessarily requires regulators to be alert to the securities activities of foreign entities taking place over the Internet.

Part IV discusses the general approaches that regulatory agencies should take in relation to the Internet, beginning with a discussion of key principles and followed by key recommendations.

Key Principles

Our discussion of the appropriate securities regulatory framework for the Internet, or any new medium, begins with an examination of the principles of securities regulation.²³ For the purposes of this report, the three fundamental objectives of securities regulation are:

- the protection of investors;
- ensuring that securities markets are fair, efficient and transparent; and
- the reduction of systemic risk.

Against this background, regulators should consider the following principles when formulating policies regarding specific securities activities on the Internet.

1. *The fundamental principles of securities regulation do not change based on the medium.*

Although the Internet provides a new and alternative medium for securities business, it raises many of the same policy issues as more traditional paper- and telephone-based securities activities. Hence, the use of the Internet for securities transactions should be subject to regulation that promotes the fundamental objectives of protecting investors, ensuring market fairness, efficiency and transparency, and reducing systemic risk.

Moreover, the existing regulatory framework that has been developed to protect investors can generally be adapted to securities transactions over the Internet while keeping in mind the fundamental principles of securities regulation. Nevertheless, regulators should undertake to review their existing laws and rules for incompatibilities with legitimate financial activities taking place over the Internet. They also should seek to ensure appropriate coverage of Internet securities activity (*i.e.*, to ensure that there are not legislative or regulatory gaps).

²³ See IOSCO Consultation Document, Objectives and Principles of Securities Regulation. (May 1998) <<http://www.iosco.org/documents-consult/1998-objectives.html>>.

2. *Consistent with the fundamental principles of securities regulation, regulators should not unnecessarily impede the legitimate use of the Internet by market participants and markets.*

Electronic communication technology such as the Internet provides numerous potential benefits to market participants and markets. The technology permits these entities to disseminate information to more people at a faster and more cost-effective rate than traditional distribution methods. Electronic distribution of information has the potential, at the same time, to enhance investors' ability to access, research and analyze information about an offer of securities and financial services and to provide access to a broader range of products. This, in turn, has the potential to make securities markets more transparent and efficient. Because of these potential benefits, securities regulators should resist imposing any more restrictions on the use of the Internet than are necessary to promote the fundamental objectives of securities regulation in their jurisdictions.

In addition, consistent with statements set forth in the U.S. White House Framework for Global Electronic Commerce and the Bonn Declaration,²⁴ the private sector leads and should continue to lead in Internet development and innovation. The private sector is in the best position to provide innovation, expanded services and broader participation in a market-driven environment. Regulators should also encourage the securities industry to adopt appropriate standards and encourage self policing with respect to their activities conducted over the Internet.

3. *Regulators should strive for transparency and consistency regarding how their regulations apply in an Internet environment.*

Although Internet communications are not easily confined within national borders, national regulators remain responsible for protecting investors in their jurisdictions. Each regulator must determine generally under what circumstances Internet securities transactions, wherever originating, may be made available to investors in their jurisdictions.

The securities industry is looking to securities regulators to clarify positions and to set parameters for the industry's Internet activities. Indeed, regulatory uncertainty, inconsistency and conflict prevent the full use and development of the Internet. Regulators should provide guidance on how they intend to apply their regulations to the Internet. Guidance on how market participants may lawfully use the Internet is necessary to facilitate the full potential of the Internet for the benefit of securities markets and to ensure that investors receive the full measure of benefits and protections contemplated by existing laws in an electronic environment.

²⁴ The U.S. Framework's strategy is to guide government support for the evolution of electronic commerce and to promote global efforts to preserve the Internet as a medium in which competition and consumer choice, rather than regulation, will shape the marketplace. See *A Framework for Global Electronic Commerce* (July 1, 1997) <www.whitehouse.gov/WH/New/Commerce/index.html>.

The Federal Republic of Germany and the European Commission held a European Ministerial Conference to broaden the common understanding of the use of Global Information Networks, to identify barriers to their use, to discuss possible solutions and to undertake an open dialogue on further possibilities for European and international cooperation. See Ministerial Conference Bonn, *Global Information Networks: Realising the Potential*, (July 6-8, 1997) <<http://www2.echo.lu/bonn/final.html>>.

The regulatory relationship between a securities market participant and its regulator in a particular jurisdiction provides a powerful tool that, if applied by regulators around the world, can help to achieve the aim of promoting transparency and protecting investors. Regulators should take what action they can domestically with respect to those market participants that they license or authorize, to encourage them to abide by the recommendations set out below.

Moreover, market participants will benefit from consistent regulatory regimes that are applicable to Internet securities activities. Regulators should work together to develop a principled approach to reducing the potential for regulatory conflicts so that market participants can understand, in advance, the regulatory requirements to which their activities will be subject. Any approach should, however, acknowledge that each regulator must retain the discretion to exercise regulatory authority and impose its own regulations on activities that have an impact on market participants and markets inside that regulator's jurisdiction.

4. *Regulators should cooperate and share information to monitor and police securities activity on the Internet effectively.*

The Internet is an international medium. Activities undertaken in a single jurisdiction can be accessed and have implications in multiple, geographically and regulatorily different jurisdictions. Enhanced cooperation among regulators is necessary to monitor and police effectively activities by the securities industry on the Internet. Such cooperation will permit the Internet to evolve as a medium for use by the securities industry.

5. *Regulators should recognize that electronic media and the use of such media is likely to evolve.*

In drafting regulatory requirements with respect to the Internet, regulators should recognize that the technology is likely to evolve, therefore requiring flexible regulatory approaches and requirements. Some of the regulatory concerns presented by the current limitations on technology will be resolved by further developments. On the other hand, new issues and concerns may arise.

Key Recommendations

The key principles described above guide the following recommendations:

A. Application of Domestic Regulatory Requirements to Securities Activities on the Internet

Offers and Advertisements

1. *Regulators and SROs should provide guidance to alert market participants and markets as to how their existing registration, licensing and other regulatory requirements apply to offers and advertisements conducted on the Internet and alert them to the possibility that other jurisdictions likewise may impose other requirements.*

The Internet provides ready and direct access to large numbers of potential investors. Internet users may appreciate this access but may not always be aware that communications over the Internet create legal and regulatory obligations. Offers of securities or financial services and other forms of advertising on the Internet may trigger registration, prospectus and licensing requirements in much the same fashion as other communications media. In addition, the open nature of the Internet could make it inappropriate for users of this medium to rely on regulatory exemptions based on the offer being made only to sophisticated investors or to a limited number of persons, absent special procedures to restrict access to the offering materials.

2. *Regulators should amend, or seek to have the relevant authorities or legislative bodies amend, specific requirements when appropriate to accommodate and ensure appropriate regulatory coverage of the Internet environment.*
3. *General antifraud provisions should apply to all offers and advertisements involving securities or financial services, regardless of the medium and regardless of whether a regulator or SRO is involved in approving the offer or advertisement.*
4. *Regulators and, where appropriate, SROs should strengthen surveillance of Internet advertising and offerings for unauthorized or fraudulent activities.*

Delivery of Disclosure Documents and Other Information

5. *Regulators should ensure that issuers who use the Internet to communicate with and send offering material to shareholders and potential investors provide the same disclosure about their operations, financial condition and securities that would be provided in a paper-based medium, so that investors can evaluate the risk and value of investing in the issuer.*

Adequate and accurate information is at the heart of the securities regulatory framework. Therefore, disclosure and dissemination requirements are crucial elements of securities regulation worldwide. Regulators and SROs can best protect investors by requiring that issuers who are using the Internet to communicate with shareholders and potential investors continue to provide

full and accurate disclosure about their operations, financial condition and securities so that investors can evaluate the risk and value of investing in the issuer.

6. *Regulators should provide guidance for the financial service industry on the use of the Internet to satisfy their obligation to deliver disclosure documents.*

To enable the use of developing technologies, regulators should provide guidance for the financial service industry on the use of the Internet to satisfy their obligation to deliver disclosure documents. For example, issuers and their underwriters should be able to use Web site prospectuses to satisfy delivery obligations in public offerings if done in a manner that ensures that investors receive information similar to what they would receive on paper. Under similar circumstances, a financial service provider should be able to use its Web site or e-mail to provide account information and trade confirmations to its customers. The following are non-exclusive factors to assist in formulating policies on electronic delivery.

In providing guidance, regulators should consider what constitutes delivery and the extent to which electronic delivery provides timely and adequate notice.

Postal mail delivery typically makes an investor aware that new information exists. Investors, however, may not have notice that required information is available on a Web site. Therefore, a Web site posting of a document by itself should not be deemed to constitute adequate notice. Separate notice that information is available on a Web site should be required unless issuers and financial service providers can show that delivery has been effected.

In permitting the use of electronic delivery by the financial service industry, regulators should require that access to electronic communications be at least as good as that provided by paper delivery.

In light of the wide disparity in investor abilities to use electronic media, access to an electronic medium should not be so burdensome that access is effectively denied. For as long as the applicable delivery requirements dictate, investors should have the ability to retain, or have access to, the electronic document. In addition, regulators and SROs should consider possible differences in the quality and content of the electronic document that the investor will be able to print at home compared with what the investor would receive in the mail.

Regulators should permit the financial service industry to deliver disclosure documents electronically when an investor has given an informed consent to this form of delivery.

Information posted on an Internet Web site could be considered to be delivered in satisfaction of regulatory delivery requirements after an investor has given an informed consent to receive the information on that basis. For a consent to be considered “informed,” it should specify the medium of delivery and the period during which the consent is effective. The consent should also specify the information that will be delivered electronically. Investors should be informed of any potential costs associated with Web site delivery.

Voting in Meetings

7. *Subject to investor protection and confidentiality concerns, regulators should explore the possibilities under their company laws to enable issuers, transfer agents, depositories and broker-dealers to make full use of the Internet for the dissemination of voting information and in the proxy voting process as one means to facilitate full participation by shareholders in annual and other meetings of shareholders.*

Two of the areas where the Internet has the potential to improve communications between issuers and their shareholders are the dissemination of proxy material relating to shareholder meetings and proxy voting. As the capital markets have internationalized, the shareholder bases of companies accessing those markets have become global. Procedures for disseminating information regarding matters to be voted upon and for voting by proxy, however, have not kept pace. The legal requirements or practices of many jurisdictions do not require or permit dissemination of materials sufficiently in advance of a meeting for non-resident shareholders to receive the materials and return a completed proxy form in time for the meeting. Moreover, non-resident holders will normally not be registered owners of their securities and will instead own through one or more layers of broker-dealer nominees and depositories.

The Internet offers an opportunity to greatly improve the proxy voting process. Regulators should explore, or seek to encourage relevant authorities to explore, the possibilities under local company law to encourage issuers, transfer agents, depositories and broker-dealers to make full use of electronic dissemination of voting information and electronic voting procedures to facilitate full participation by all shareholders in annual and other meetings of shareholders.

Equally, the use of the Internet for voting purposes raises investor protection, confidentiality and insider dealing concerns. Regulators should ensure that investors have equal access to voting and are not therefore prejudiced by an electronic proxy voting procedure, and that any electronic proxy voting system is appropriately secure.

Subject to those concerns being adequately addressed, regulators should review or encourage review of the laws of their jurisdictions that govern the validity of proxies with a view towards the elimination, by the appropriate bodies, of any obstacles to the use of the Internet for proxy voting. For example, legal requirements calling for a manually executed proxy should be reviewed with a view to permit other forms of verification and authentication.

Communications and Customer Orders

8. *Regulators should require that financial service providers continue to satisfy suitability and general conduct requirements when transacting business over the Internet.*

Internet communications do not eliminate the need for financial service providers to comply with suitability obligations. Regulators should provide guidance to assist financial service providers in meeting these obligations. Financial service providers operating in an electronic environment will need to ensure that they have sufficient, verifiable information about investors, whether through on-line questionnaires or otherwise, and to ensure that they are providing suitable advice and are otherwise meeting general conduct requirements.

9. *Regulators should require that financial service providers ensure that their computer networks have sufficient operational integrity (security, reliability, capacity, backup systems and alternative means of communication) and that they have adequate personnel to handle Internet communications, including trading instructions.*

Financial service providers may be unable to process their transaction volume without disruption if their computer networks do not have adequate capacity or if they lack adequate personnel. In the event of a disruption, financial service providers should have alternative methods of communication available (e.g., telephone, fax) to handle customer trading requests. In addition, financial service providers should be encouraged to explain the risks of Internet communications and trading to their customers, and take steps to protect confidential customer information transmitted on such open networks.

10. *Regulators should consider requiring financial service providers to develop written procedures for the review of incoming and outgoing electronic correspondence between employees and the public relating to the financial service provider's securities business.*

The benefits of electronic communication to financial service providers are accompanied by the requirement that they adequately supervise such communications. Financial service providers should have written procedures in place to deal with the electronic communications relating to their securities business.

11. *Regulators should clarify if, and under what circumstances, the use of authentication technologies will be allowed and when manual signatures will be required.*

The use of authentication technologies (e.g., digital signatures) may allow the financial services industry to effect securities transactions in a secure manner. Regulators, however, should determine which situations and transactions should require manual signatures.

Recordkeeping

12. *Recordkeeping requirements applicable to financial service providers should apply to Internet transactions. Regulators need to be satisfied that the key standards of recordkeeping can be met regardless of the technology used (e.g., that certain records be created and maintained; that these records are durable, cannot be altered and are available and accessible to the regulator).*

Rules that apply to a financial service provider's recordkeeping should apply to Internet transactions. Because Internet transactions are in electronic format, the issues of how to store and retrieve such records are different than in a paper-based environment. Some jurisdictions currently allow for electronic storage of electronic and paper-based transactions provided that the technology meets certain regulatory criteria and allows for the establishment of an audit trail. Regulators should permit the use of any type of technology that meets the standards set forth by the regulator.

13. *Recordkeeping policies and requirements should address e-mail communications that relate to the securities business of a financial service provider.*

B. Exercise of Regulatory Authority over Cross-Border Securities Activities on the Internet

Because the Internet generally recognizes no geographic boundaries, it presents jurisdictional challenges for regulators. One approach would be for regulators to require registration or licensing for all Internet offers of securities or investment services that their residents could access. As a practical matter, however, such an approach by regulators is not feasible and would hinder some of the Internet's most promising innovations and applications by market participants and markets. Reaching consensus on a universal approach to the question of when a Web site communication will be considered to be an offer of securities or services taking place within a particular jurisdiction is unlikely, because that determination must be based on the particular circumstances and the laws of each jurisdiction.

Issues relevant to determining the circumstances in which regulators might exercise regulatory authority over particular offers of securities or financial services made over the Internet are discussed below. In formulating recommendations, it is assumed that the contents of a Web site based in one jurisdiction can under specified circumstances constitute an offer according to the rules and definitions of each jurisdiction from which the Web site can be viewed. The following are non-exclusive factors to guide regulators in setting policies as to the circumstances in which a regulator should exercise regulatory authority over an offer originating in another jurisdiction.

14. *Regulators should provide guidance on the circumstances under which they will exercise regulatory authority over Internet offers.*

Regulators should determine under what circumstances Internet securities transactions may be made available to residents in their jurisdictions. That responsibility should not be delegated to the foreign jurisdiction in which the Internet offer originates.

15. *If an issuer's or financial service provider's offer or sales activities over the Internet occur within a regulator's jurisdiction, or if the issuer's or financial service provider's offshore activities, in fact, have a significant effect upon residents or markets in the regulator's jurisdiction, a regulator may impose its regulatory requirements (e.g., licensing and registration requirements) on such activities.*

16. *Regulators should examine the following factors in determining whether to assert regulatory authority over an offer of securities of financial services on the Internet.*

While not all jurisdictions would necessarily rely on the same factors (and some may

consider additional factors), the following list describes some circumstances under which a regulator should consider exercising regulatory authority over an Internet offer. It is important to note that these factors are not determinative or exhaustive. The presence or absence of any one or more factors should not dictate that a regulator should assert or decline to assert regulatory authority.

Factors that may support assertion of regulatory authority include:

It is evident that information is targeted to residents of the regulator's jurisdiction (indications of targeting may include an established local distribution network in the jurisdiction, concurrent advertising or publicity using other media in the jurisdiction, or prices denominated in local currency or communications written in local language, when that currency or language is not commonly used on a global basis).

The issuer or financial service provider accepts purchases from or provides services to residents of the regulator's jurisdiction (unless made pursuant to an exemption or under circumstances that may exclude a public offering).

The issuer or financial service provider uses e-mail or other media to “push” the information to residents of the regulator’s jurisdiction.

Factors that may support a decision not to assert regulatory authority include:

The issuer or financial service provider clearly states to whom the Internet offer is directed, rather than appearing to extend the offer into any jurisdiction.

The Web site contains a statement listing the jurisdictions in which the issuer or financial service provider has been (or has not been) authorized to offer or sell its securities or services.²⁵

The issuer or financial service provider takes precautions that are reasonably designed to prevent sales to residents in the regulator’s jurisdiction. For example, the issuer or financial service provider could screen the address and other residency information provided by persons responding to the Internet offer. A significant amount of unauthorized sales would indicate the absence of reasonable precautions.

These factors should guide regulators in interpreting their own laws in the context of Internet offers of securities and financial services. Markets and market participants, on the other hand, can rely only upon the laws and interpretations of each jurisdiction as authoritative on these issues.

²⁵ The disclaimer should be prominently displayed. A disclaimer that states something to the effect of, “This offer is not being made in any jurisdiction in which the offer would or could be illegal,” should not be considered a sufficiently clear statement.

In any event, it should be understood that the regulator may take enforcement action whenever fraudulent or manipulative Internet securities activities have placed the residents in the regulator's jurisdiction at risk.

C. Use of the Internet to Foster Investor Education and Transparency

17. *Regulators and SROs should include use of the Internet in educating investors and providing guidance to the securities industry.*
18. *Regulators and SROs should educate investors about securities fraud on the Internet by providing information about possible fraudulent activities.*

Investor education and investor protection assists regulators and SROs in preventing securities fraud. Although regulators and SROs must continue to work to identify and fight securities fraud and other illegal activity, an effective system of investor education is an important defense against securities fraud. This remains the case when the Internet is used for illegal activities, since it becomes even more difficult for regulators to monitor all securities related messages distributed over the Internet.

The Internet has the potential to reach large numbers of individual investors, who may be particularly vulnerable to illegal activity. Regulators and SROs can improve market integrity by educating investors about securities fraud on the Internet. Regulators and SROs should provide investors with information about possible fraudulent activities through means that could include posting:

notices alerting investors to improper conduct on the Internet. These notices can also be posted on bulletin boards used by investors.

investment information on the Internet, including questions that investors should ask themselves and their financial advisers before investing.

notices of decisions taken by regulators and other authorities with respect to securities activities.

on-line warnings of the risks related to the transmission of credit card numbers and other sensitive financial information on the Internet.

There is also a degree of self-policing among Internet users, many of whom resent having the Internet used for illegal purposes. These individuals seek to protect the integrity of the Internet by investigating suspicious matters and reporting potential abuses to regulators. This practice should be encouraged by regulators as it is a useful source of information about Internet-related fraud. Regulators traditionally have relied on tips from investors to detect information on securities fraud and the Internet is a necessary and effective tool to expand that practice.

In addition, regulators and SROs can establish interactive systems allowing investors to confirm the regulatory status of a particular person or entity with the regulator of that jurisdiction,

or provide a phone number or Web site address where an investor could obtain such information.²⁶ Regulators and SROs also can publish their e-mail addresses to allow investors and members of the securities industry to transmit comments and questions.

19. *Regulators, SROs, and organized markets should consider using their Web sites to provide current and potential investors with access to information about their organizations, including current laws, regulations, by-laws and governance procedures.*

Increasingly, market participants are using the Internet as a research tool to facilitate due diligence reviews of markets in which they wish to participate.

20. *Regulators, SROs, and organized markets should facilitate investor access to corporate and market information by developing electronic databases for reports and legally required disclosure documents, and making the information publicly available on their Web sites.*

Ready access to offering and disclosure documents can form the core of the body of corporate information on which investors worldwide can base their investment decisions. Transparency could also be enhanced by the provision by exchanges of transactional data, such as trading prices and volume, either on a real time or delayed basis.

When regulators and exchanges provide investors with Internet access to information or offering documents filed with them, this access should not be viewed as indicative of an attempt by the filing entity to make offers in jurisdictions where the offer is unauthorized.

D. Use of the Internet to Enhance Cooperation in Enforcement Matters

21. *Regulators or other authorities in their jurisdictions should have the authority to gather and share information regarding activities that occur over the Internet that appear questionable or that have been prosecuted in their jurisdictions.*

Perpetrators of Internet securities fraud can easily move both the location of their Internet sites and the target location of their fraudulent scheme from one jurisdiction to another when they encounter difficulties in a particular jurisdiction. In addition, these perpetrators can send the same message to multiple jurisdictions simultaneously. As a result, regulators or other authorities should seek out opportunities to leverage their efforts by sharing information on transactions that they view as questionable and by cooperating generally regarding potential securities violations occurring on the Internet.

Just as importantly, regulators can share information on successfully concluded prosecutions of Internet-related securities fraud (*e.g.*, by posting notices on their Web sites). This sharing of information has multiple benefits. First, it may decrease the chance that the same individuals will successfully perpetrate the same fraud in another jurisdiction. Second, it may

²⁶ Confirming the regulatory status of a person or entity should not imply that the regulatory authority has in any way approved the merits of the offer or securities or services, or that the regulatory authority makes any assertion about the quality of the offer.

alert other regulators to the types of Internet fraud they are likely to encounter.

22. *Regulators and SROs should strengthen surveillance of Internet activities by routinely monitoring for unauthorized or fraudulent activities.*

Surveillance is especially important in areas on the Internet where manipulations or fraud frequently occur (e.g., newsgroups).

23. *Regulators and SROs should have staff sufficiently trained in current techniques for conducting surveillance on the Internet.*

Regulators and SROs need to learn new methods for conducting surveillance and must become familiar with Internet-specific methods for locating and sharing information. Because of the particular techniques available to Internet users, identifying and locating the persons responsible for securities fraud can be especially difficult. Internet users can hide their identities through a veil of anonymity that may be more difficult for regulators to pierce than when more traditional methods of communication are used. For example, regulators and SROs may find it more difficult to identify a person engaged in a market manipulation through an Internet bulletin board than in a more traditional manipulation. Regulators and other authorities in their jurisdiction should consider whether they can obtain, when necessary, information from the Internet access providers about the identity of persons using the services for illegal purposes.

24. *Regulators should assist one another by exchanging details about techniques for monitoring Internet advertising, offers of securities or financial services that may contain false or misleading information, and by sharing expertise with regulators who have limited experience in this area.*

Regulators will be best able to deal with the rapidly increasing need for investigating and taking action against fraud and other misconduct on the Internet if they are willing to share relevant information and experience with one another. In addition, regulators should make available to their counterparts information about techniques for monitoring Internet offers of securities or financial services that may contain false or misleading information.

The Internet presents a particular challenge for regulators that have limited technical expertise. This challenge is exacerbated by the changing nature of Internet-related technology. A great deal of hardware and software, especially information processing tools, considered state of the art a few years ago, is now considered outdated if not obsolete. It is in jurisdictions in which technical expertise is limited that perpetrators of securities fraud may be most successful, since their chances of detection may be lower. To address this concern, regulators could assist one another by devising training programs and by sharing expertise and experience in methods of recognizing fraud perpetrated on the Internet.

ANNEX

Australia

Australian Securities and Investment Commission (ASIC)
(Formerly known as the Australian Securities Commission (ASC))

Policy Statement 107, Electronic prospectuses

Focuses on electronic prospectuses issued on the Internet or other computer networks, CD-ROM and floppy disk. In essence, the ASIC considers that electronic prospectuses can be allowed in cases where the policy underlying the prospectus provisions in the Corporations Law can be satisfied.

<http://www.asic.gov.au/page-321.html>

Policy Statement 118, Investment advisory services: media, computer software and Internet advice

Sets out guidelines in relation to a person providing investment advice on the Internet.

Policy Statement 100, Stock Markets

Includes regulatory requirements for the conduct of electronic bulletin boards.

Information Package On Electronic Commerce

The Australian Securities Commission (ASIC's predecessor) released a package of materials in May 1996 for industry consultation comprising:

- (a) a background Information Paper on electronic commerce in the financial services industry;
- (b) a Concept Paper containing a draft statement of principles on electronic communications under the Corporations Law; and
- (c) some Frequently Asked Questions on the application of the Law to the provision of investment information on the Internet.

ASIC response to the Parliamentary Joint Committee on Corporations and Securities - Inquiry into global electronic capital raising and share trading
(September 1997)

The paper discusses a wide range of issues including security and authenticity, equity and access issues, investment advice, trading and settlement systems, jurisdictional problems with disclosure, and foreign acquisitions and takeovers.

ASIC Information Sheets:

[INFO 230] Investing on the Internet

[INFO 245] Good advice

Contact information for the Australian Securities and Investments Commission, and some of these documents, are available through the Australian Securities and Investments Commission homepage, at:

<http://www.asic.gov.au/>

E-mail: infoline@asic.gov.au

You may also contact the ASIC at one of their national offices:

National Office, Melbourne
Level 20,
485 Latrobe Street, Melbourne
Melbourne Vic 3000
GPO Box 5179AA
Melbourne Vic 3001
DX 423 Melbourne
phone: 61 3 9280 3200
fax: 61 3 9280 3355

or

National Office, Sydney
Level 18,
135 King St
Sydney NSW 2000
GPO Box 4866
Sydney NSW 1042
DX 653 Sydney
phone: 61 2 9911 2000
fax: 61 2 9911 2030

Canada

Ontario Securities Commission (OSC)

Commission des valeurs mobilières du Québec (CVMQ)

British Columbia Securities Commission (BCSC)

Toronto Stock Exchange (TSE)

Delivery of Documents by Issuers using Electronic Media Concept Proposal

Canadian Securities Administrators Request for Comments 11-401

Ontario Securities Commission Bulletin (1997) 20 OSCB 3075

Request for comments regarding electronic delivery of information by issuers to investors and potential investors under Canadian Securities legislation, and other related issues.

http://www.osc.gov.on.ca/en/Regulation/Rulemaking/Notices/csanotices/csa_list.html

(French version)

Transmission de documents par les émetteurs au moyen des médias électroniques - Propositions d'un régime

Autorités canadiennes en valeurs mobilières - Avis de consultation 11-401

B.C.V.M.Q. Vol. XXVIII, June 20, 1997, n° 24 pages 1-4

Trading Securities and Providing Advice Respecting Securities on the Internet

British Columbia Securities Commission Weekly Summary Edition Number 97:10 pp. 1-4.

Notice reminding securities market participants that B.C. Securities Act registration and disclosure requirements apply to persons using Internet as any other medium of communication.

Proposed Electronic Communications Disclosure Guidelines

Toronto Stock Exchange.

This document reviews a number of issues that a company must consider when it goes on-line. The Policy states that information that is disclosed electronically should be viewed as an extension of its formal corporate disclosure record. Guidelines cover subjects like designing a web site, establishing an internal e-mail

policy, and disseminating information over the Internet by listed companies.

http://www.tse.com/mregs/pdf/web_proposed.pdf
(Adobe Acrobat is required to view this document.)

Contact information:

OSC

Suite 800, Box 55
20 Queen Street West
Toronto, ON M5H 3S8
Canada
Reception: (416) 597-0681
Fax: (416) 593-8122
Inquiries: (416) 593-8314
Publications: (416) 593-8117
<http://www.osc.gov.ca>
E-mail: inquiries@osc.gov.on.ca

CVMQ

C.P. 246, Tour de la Bourse
800, square Victoria
17e étage
Montréal, Québec H4Z 1G
Canada
Tel: (514) 873-5326
Fax.: (514) 873-3090
<http://WWW.CVMQ.COM/english/>
E-mail: info@cvmq.com

BCSC

Suite 200, 865 Hornby Street
Vancouver, BC V6Z 2H4
Canada
Tel: (604) 899-6500
Fax: (604) 899-6506
<http://www.bsc.bc.ca/>
E-mail: inquiries@bcsc.bc.ca

TSE

Toronto Stock Exchange
Marketing and Communication

The Exchange Tower

2 First Canadian Place

Toronto, ON M5X 1J2

Canada

Tel: (416) 947-4700

Fax: (416) 947-4662

<http://www.tse.com>

E-mail: info@tse.com

France

Commission des Opérations de Bourse (COB)

No specific Internet regulation has been adopted yet by the COB, though a lot of issues raised by Internet are already covered by the COB securities regulation.

Two recommendations dealing with the Minitel electronic network provide a framework which applies already to various issues raised by the Internet.

The Minitel network operated by the French national public telephone company presents some similarities with Internet though the network only covers France. Minitel has an average of twenty million users.

The COB recommendations adopted on the Minitel in 1987 and in 1993 stressed the application of the already existing COB requirements of accurate and properly updated financial information to this new medium.

Recommendations N° 87 - 01 and N° 93-01, summary of key provisions

Accountability of the site promoter for disclosed information. Obligation to state name of publisher.

Update of information: Clear mention must be given of the last update of the displayed information. Automatic update procedure must be in place to avoid errors or neglect. Time of origin of quotes and other market data must be specified (date and exact time).

Origin of information: Obligation to state the exact origin of third party releases. Clear distinction must be made between financial analyses and original data. Issuers must indicate reference to filings made with the COB (when applicable) for every financial operation mentioned on their site. In that case, indication must be given on the means to obtain this document at no cost.

No Minitel-only disclosure for issuers: No market-sensitive information shall be displayed on Minitel before disclosure by public release. Conversely all market sensitive information disclosed by public release must be mentioned on the Minitel site of the issuer. If the release is displayed in a summarized version, reference of the complete version must be given.

No anonymous chat room on a Minitel site of an issuer for fear it could be used abusively by issuer to provide transaction advice on its securities.

Recordkeeping: electronic or paper records of information must be kept up to 6 month

after display on Minitel site

Also, based on Rule N°96-03 Section III Art. 24, the COB has authority over Collective Investment Schemes to control their information documents before they release it to them, to their customers or to the general public. This applies to electronic transmissions as well as to printed material.

Contact information:

COB

17 Place de la Bourse

75082 Paris cedex 02

Tel : 33 1 53 45 60 00

Fax : 33 1 53 45 61 00

<http://www.cob.fr/eng/index.asp>

E-mail : rel-pub@cob.fr

Documentation Center Tel. : 33 1 53 45 62 00

Public Relations Department Tel. : 33 1 53 45 60 25

Information regarding the Minitel Web site is available at <http://www.minitel.fr>

Germany

Bundesaufsichtsamt für den Wertpapierhandel (BAWe)

(Federal Securities Supervisory Office)

Bundesaufsichtsamt für das Kreditwesen (BAKred)

(Federal Banking Supervisory Office)

In Germany the system of securities supervision follows the functional approach. Accordingly, the BAWe is responsible for market surveillance and supervision of the rules of conduct, whereas the BAKred is responsible for licensing and solvency of financial institutions, including the licensing of collective investment schemes. The statements of both authorities are set out below:

BAWe

The BAWe has issued the following general statements as guidance with regard to the use of the Internet in the financial sector:

Annual Verifications of Credit Institutions, p. 10 of the Annual Report for 1997

The BAWe has stated that in its annual audits of firms under its supervision with regard to compliance with the rules of conduct, it would look into the use of the Internet by these institutions. Of particular interest would be whether orders can be placed over the Internet, whether the rules of conduct are thereby complied with and what security measures are being taken.

(available on Internet homepage of the BAWe <http://www.bawe.de>, "Jahresberichte," "Jahresbericht 1997 ," as download version in German)

Public Offerings over the Internet, p. 14 et seq. of the Annual Report for 1997

In 1997, the first public placement of securities over the Internet took place which directly addressed German private investors. The BAWe states that in respect of a public offering of securities over the Internet in Germany the ordinary prospectus requirements (*e.g.*, with regard to depositing with the BAWe and publication) apply for the issuer/offeror in the same way as for public offerings in Germany made in any other (electronic or print) medium.

An offer is regarded as a public offer if it is directed via the media at the general public or an unlimited number of investors. An offer is not regarded as a public offer in Germany if it is addressed only to a limited number of specific German (private or institutional) investors, all of which are known to the issuer/offeror in person. In the view of the BAWe, an offer over the Internet is deemed a public offer in Germany if either German investors are expressly targeted by the offer, or if German investors are not expressly excluded from the offer.

(Available on Internet homepage of the BAWe <http://www.bawe.de>,

"Jahresberichte," "Jahresbericht 1997," as download version in German.)

Rules and Principles for Investor Protection, p. 10 of the Annual Report for 1996

The BAWe has stated that the general rules and principles for investor protection apply also with regard to offers of investment services on the Internet; the protection of investors must be ensured irrespective of the medium used. In particular, the ordinary legal requirements with regard to rules of conduct and organisation/compliance apply irrespective of the kind of (electronic or print) medium used.

(Available on Internet homepage of the BAWe <http://www.bawe.de>, "Jahresberichte," "Jahresbericht 1996," as download version in German.)

Public Offers on the Internet, p. 12 et seq. of the Annual Report for 1996

The BAWe has stated that with regard to public offerings, irrespective of the medium used (newspaper advertisements, mailings, structured sales [*Strukturvertrieb*], telephone or Internet) the usual prospectus requirements (*e.g.*, with regard to depositing with the BAWe and publication) apply. The fact that some of these offerings are labelled as "Private Placements" does not change this view, if, in fact, these offers are addressed to the general public and therefore constitute public offers under German law.

(Available on Internet homepage of the BAWe <http://www.bawe.de>, "Jahresberichte," "Jahresbericht 1996," as download version in German.)

BAKred

The BAKred has issued the following general statement with regard to the use of the Internet in the financial sector:

Guideline: "Marketing of Foreign Collective Investment Schemes on the Internet" of 2 June 1998

The pronouncement deals with the question as to when marketing of foreign funds over the Internet would constitute an illegal offer in Germany. The provisions of the Foreign Investment Act (*Auslandinvestment-Gesetz*) prohibit a foreign Collective Investment Scheme to market its shares in Germany without prior notification of the BAKred. The BAKred sets out its approach with regard to marketing of foreign funds on the Internet, but points out that it states only its current practice which still needs to be tested in practice and may be adjusted for the actual case.

(Available on Internet homepage of the BAKred)

<http://www.bakred.de/#Aktuelles>, as a download version bilingual in German and English.)

The BAKred will not consider Internet sites in a foreign language that are clearly not directed towards German investors (*e.g.*, no German addresses or special information, disclaimers) as a public offering or an advertisement in Germany, whereas Internet sites in German language will generally be considered a public offering in Germany. Exceptions might, however, be possible for sites clearly only directed towards investors in other German speaking nations. Unsolicited e-mails to a bulk of recipients in Germany will be considered by the BAKred a public offering in Germany, even if the e-mails, because of their language and content, appear not to be aimed at German investors. If an e-mail is sent to a bulletin board/ newsgroup, the BAKred states that it will need to look at the content of the mail and the target group of the board/newsgroup.

For advertisements the general rules of the Foreign Investment Act are stated to apply. If shares can be ordered on-line, the rules of the Foreign Investment Act have to be followed, *e.g.*, the investor must be offered the prospectus and the last reports before completing the sale. The BAKred considers it to be sufficient if the investor has the possibility to download the prospectus and the reports, unless the investor explicitly requests to receive the fund documents in paper form.

Customer Identification Rules:

No. 10 respectively no. 12 of the Guidelines of the BAKred concerning measures to be taken by credit institutions or financial services institutions to combat and prevent money laundering of 30 March 1998 respectively 30 December 1997

In view of the growing use of new technologies in banking business (homebanking, telebanking as well as internetbanking), the BAKred has drawn up special regulations concerning customer identification when establishing business relationships in direct banking. For this purpose the Guidelines concerning "measures to be taken by credit institutions to combat and prevent money laundering" were revised with effect from 1 January 1997 (see Annex 7). The former method of verifying the customer's identity by sending account opening documentation by registered mail with personal acknowledgement of receipt has been replaced by a specific postal identification procedure developed by Deutsche Post AG in cooperation with BAKred, in which the identity of customers is established on behalf of the relevant credit institution and in accordance with the requirements applying to banks by counter service on the premises of Deutsche Post AG or in the course of mail delivery (PostIdent Service). In addition to the employees of Deutsche Post AG, notaries public and other banks are authorised a.o. to establish identity on behalf of the institution obliged to identify the customer. An identical regulation was included in the Guidelines of the BAKred

concerning measures to be taken by financial services institutions to combat and prevent money laundering of 30 December 1997.

(Available on Internet homepage of the BAKred <http://www.bakred.de>, as download versions in German.)

Contact information:

BAWe

Lurgiallee 12

D-60439 Frankfurt am Main

Germany

Tel: 49 69 95 95 2 0

Fax: 49 69 95 95 2 123

http://www.bawe.de/english/frame_e.htm

E-Mail: mail@bawe.de

BAKred

Gardeschützenweg 71- 101

D- 12203 Berlin

Germany

Tel: 49 30 84 36 0

Fax: 49 30 84 36 1550

<http://www.bakred.de>

Italy

Commissione Nazionale per le Società e la Borsa (CONSOB)

On June 14, 1998, the CONSOB issued a Communication (DIS/RM/96006769), stating that advertising messages on the Internet of collective investment schemes should include in each page a warning to the reader on the necessity of reading the prospectus.

As far as the distribution of collective investment schemes prospectuses on the Internet is concerned, the CONSOB held the view (Communication DAL/RM/96008280 of September 9, 1996) that the content of prospectuses should be the same as the one filed with the CONSOB and on the condition that no advertising activity is carried out.

Furthermore, article 32 of Legislative Decree 58 of February 24, 1998, deals with telemarketing techniques. These shall mean techniques of contacting customers, other than advertising, which do not involve the simultaneous physical presence of the customer and the offeror or a person appointed by the offeror.

The CONSOB issued a regulation on the telemarketing of financial instruments and investment services (resolution 11522 of July 1, 1998.) This regulation applies both to cases in which authorized intermediaries and clients can interact immediately and cases in which the documentation given to clients is aimed to enter into a contract

The above-mentioned regulation provides, *inter alia*, that telemarketing techniques should be immediately interrupted by authorized intermediaries when investors object to their use. Information and clarification due to investors shall be addressed to them in a clear and understandable way and in conformity with the technique adopted.

Authorized intermediaries may transmit by telemarketing techniques, documents which must be provided to investors in hard form, provided that these techniques allow investors to acquire the documents in hard form. Authorized intermediaries should use financial salesmen promoting and placing by investors when issuing techniques that allow immediate interaction and individual communication. The presence of financial salesmen is not compulsory when the initiative has been taken by the investor, provided that this initiative has not been prompted by messages addressed only to this investor.

Communication No. DI/98063298 - Authorized intermediaries may receive orders from clients through the Internet, within the framework under the negotiation service provision. This is consistent with article 60, para. 1, of CONSOB Regulation No. 11522 of 1998, according to which authorized intermediaries, when orders are received, must give investors a paper-based confirmation. When orders are received

through the Internet, however, the confirmation may be sent throughout the Internet, provided investors are able to acquire the document in paper form.

Contact information:

CONSOB

Via Isonzo 19/D

00198 Roma

ITALY

Tel.: ++39 06 8477381

Fax: ++39 06 8477763

E-mail: c.biancheri@consob.it

http://www.consob.it/english/en_index.htm

United Kingdom

**Financial Services Authority (FSA)
Securities and Futures Authority Limited (SFA)
Investment Management Regulatory Organisation (IMRO)
Personal Investment Authority (PIA)**

Unauthorised Investment Advertising over the Internet

The FSA issued a Guidance Release in May 1998 entitled “The Treatment of Material on Overseas World Wide Web Sites Accessible in the UK but Not Intended for Investors in the UK”.

The Guidance states that material that fits the definition of an “investment advertisement” in the Financial Services Act 1986 which can be pulled up on a screen in the UK is likely to be in breach of the advertising provisions of the Act if it has not been approved by a person who is “authorised” under the Financial Services Act 1986. Such a breach is a criminal offence. The Guidance details factors that the FSA will take into account, in such cases, when deciding whether to take enforcement action

The factors include:

the extent to which the underlying investment or investment service was available to UK investors who may respond to the advertisement;

whether steps had been taken to deny UK investors access to the investment service;

the extent to which the advertisement was directed at persons in the UK (including, the presence of disclaimers; whether they reflected what was done in practice; whether the content was such that it was geared towards a UK audience; and whether the site was promoted in the UK);

the extent to which positive steps had been taken to limit access the web site.

FSA Guidance Release 2/98 May 1998. The full text of the Guidance Release is available at:

<http://www.fsa.gov.uk/pubs/guider.htm#1998>
(Adobe Acrobat is required to read .pdf file)

Treatment of Internet Service and Site Providers (letter issued in December 1995)

This explains how Internet Service and Site Providers could be seen in certain circumstances to be issuing or causing the issue of the investment advertisements they carry on behalf of those financial services companies for whom they provide Internet access or server capacity. Also how Internet Service and Site Providers could be seen to be carrying on investment business where, for instance, they provide a facility which is part of the arrangements whereby a person purchases investments.

A summary of the letter is available at <http://www.fsa.gov.uk/enf/els5.htm>

Guidance to Persons/Firms Regulated under the Financial Services Act 1986

Guidance on the applicability of SFA, IMRO, and PIA conduct of business rules to firms authorised by these organisations in the UK in respect of investment business and the issuing of investment advertisements over the Internet. Other matters dealt with include record keeping and the use of e-mail between firms and customers.

SFA - Board Notice 416 (25 April 1997)

The Guidance deals with the applicability of existing conduct of business rules (CBRs) in the following areas:

Advertising Rules (Rule 5-9(1)-(7) ☐ availability of exclusions in respect of the ability to control access to material/services. Also need for and placement of warnings/disclaimers);

Record Keeping (Rule 5-54 and Appendix 18 ☐ electronic records permissible, subject to it being possible to produce a hard copy promptly);

E-mail (can be used to send customer agreements, contact notes and periodic valuations need to verify delivery);

Identifying the regulator (placement and applicable material).

IMRO - Notice (7 May 1997)

The Guidance deals with the applicability of existing conduct of business rules (CBRs) in the following areas:

Unregulated Collective Investment Schemes (need for compliance with restrictions in section 76 of the Financial Services Act);

Advertising Code (Rule 1.(1) - requirement to be fair and not misleading);

Identifying the regulator (Rule 1.(1)(b) ☐ placement and applicable material);

Direct Offer advertisements (information required and relevance of Key Features Document (Rule 1.3(1)(c)));

Packaged products: Key Features (no need for full Key Features document in Direct Offer advertisement);

Exclusions of Liability (relevance of Rule 2.5(1)(a) avoiding excluding or limiting liability in respect of Regulated Business);

Contents of Customer Agreements (where Rule 2.4(1) to (3) is applicable to a Customer Agreement provided over the Internet it must be provided in the same sequence as required in an agreement presented in hard copy);

Customer Signatures (needed in hard copy where Customer Agreement Rules require it - not needed for unit trust dealings nor in respect of overseas customers);

Use of E-mail (need to verify delivery etc);

Record Keeping (need to comply with Chapter IV requirements Rule 1.6(2) already allows electronic records to be kept which have to be capable of production in hard copy within a day).

PIA - Guidance (22 August 1997)

The Guidance deals with the applicability of existing conduct of business rules (CBRs) in the following areas:

Identifying the Regulator (placement and applicable material);

Advertising design content and format (appropriate of warning/disclaimers and sequence of pages);

Direct Offer (Adopted LAUTRO Rule L6.18 applies - provides that direct offer or off page advertising must be contained in a printed document Rule being reviewed);

Key Features (need for potential investors to view Key Features document before access to any application form);

Advertisement Appraisal (need for compliance approval and retention of advertisement layout etc);

Use of E-mail (need for compliance with status disclosure and advertising rules);

Advice (as with other media, need for “fact find” when provided electronically);

Record keeping (Rule 5.1.3 applies ☐ this includes need for material to be produced on their premises in paper form).

The full text of the SFA, IMRO and PIA Guidance is available direct from those organisations (see below for contact details).

Contact Information:

FSA

25 The North Colonnade
Canary Wharf
London, E14 5HS
Tel: 011 44 171 676 1000 (main Switchboard)
Tel: 011 44 845 606 1234 (FSA Public Enquiries Office)
Fax: 011 44 171 676 1099
email: enquiries@fsa.gov.uk

SFA

Cottons Centre
Cottons Lane
London, SE1 2QB
Tel: 011 44 171 378 9000
Tel: 011 44 171 676 3286 (Marketing and Publications Department)
Fax: 011 44 171 403 7569
[http:// www.sfa.org.uk](http://www.sfa.org.uk)
e-mail: c.dell@fsa.gov.uk

IMRO

5th Floor, Lloyds Chambers
1 Portsoken Street
London, E1 8BT
Tel: 011 44 171 390 5000
Fax: 011 44 171 680 0550
<http://www.imro.co.uk>

PIA

1 Canada Square
Canary Wharf
London, E14 4AB
Tel: 011 44 171 538 8860

United States

Commodity Futures Trading Commission

Concept Release on the Placement of a Foreign Board of Trade's Computer Terminals in the United States

63 Fed. Reg. 39779 (July 24, 1998) (request for comment)

The Commission requested comment on how to address issues related to the placement by foreign boards of trade of computer terminals in the United States that would be used for the purpose of facilitating the trading of products available through those boards of trade. Issues upon which comment is requested include how to define "computer terminal" in this context and how the Internet currently is being used and will be used in the future for transmission and/or execution of orders through foreign boards of trade.

<http://www.cftc.gov/foia/fedreg98/980724a.htm>

or

<http://www.cftc.gov/foia/fedreg98/980724a.pdf>

(Adobe Acrobat is required to view this document)

Applications of Futurecom for Designations as a Contract Market in Technology Stock Index Futures and Options

63 Fed. Reg. 34367 (June 24, 1998) (notice of availability of terms and conditions of proposed commodity futures and option contracts)

The Commission requested public comment on an application by an electronic exchange for designation as a contract market for the Internet-based trading of technology stock index futures and option contracts and a request for approval of trading rules and rules of government that the exchange submitted to meet the requirements for a board of trade seeking designations as a contract market.

<http://www.cftc.gov/foia/fedreg98/980624b.htm>

<http://www.cftc.gov/foia/fedreg98/980624b.pdf>

(Adobe Acrobat is required to view this document)

Recordkeeping

63 Fed. Reg. 30668 (June 5, 1998) (proposed rules)

The Commission's proposed rule amendments would shift the Commission's approach to recordkeeping technology from the current specification of a particular class of optical disk or micrographic media to a more generic, performance-based approach to the definition of permissible technology. In addition, the Commission proposed to expand the category of required records for which an affected person may employ micrographic or electronic storage media to meet recordkeeping obligations imposed by the Commodity Exchange Act and Commission regulations. The Commission also proposed to eliminate the current requirement that paper records eligible for transfer to micrographic or electronic storage media be maintained in hard copy for two years.

<http://www.cftc.gov/foia/fedreg98/980605a.htm>

or

<http://www.cftc.gov/foia/fedreg98/980605a.pdf>

(Adobe

Acrobat is required to view this document)

63 Fed. Reg. 42600 (August 10, 1998) (extension of comment period)

<http://www.cftc.gov/foia/fedreg98/980810a.htm>

or

<http://www.cftc.gov/foia/fedreg98/980810a.pdf>

(Adobe

Acrobat is required to view this document)

Application of FutureCom, LTD. as a Contract Market in Live Cattle Futures and Options

62 Fed. Reg. 62566 (November 24, 1997) (notice of application)

The Commission determined to again publish the proposal for public comment upon the receipt of additional materials and information in support of the application.

— <http://www.cftc.gov/foia/fedreg97/971124A.HTM>

63 Fed. Reg. 1959 (January 13, 1998) (extension of comment period)

— <http://www.cftc.gov/foia/fedreg97/980113A.HTM>

Interpretation Regarding Use of Electronic Media by Commodity Pool Operators and Commodity Trading Advisors for Delivery of Disclosure Documents and Other Materials

62 Fed. Reg. 39104 (July 22, 1997) (final interpretation; final rules)

<http://www.cftc.gov/foia/fedreg97/970722A.HTM>

The Commission published its views on issues relating to: (1) the electronic delivery of Disclosure Documents and modifications of Disclosure Documents by commodity pool operators (CPOs) and commodity trading advisors (CTAs); (2) the distribution of monthly or quarterly statements by CPOs; and (3) the delivery of “term sheets” by CPOs (solely to “accredited investors”). The Commission also discussed recordkeeping requirements in the context of electronic media and adopted technical amendments to its rules governing the form of documents distributed by CPOs and CTAs and the requirement that CPOs and CTAs obtain signed acknowledgments when Disclosure Documents are delivered.

CFTC Letter No. 97-63 (July 15, 1997) (interpretative letter)

Commission staff determined that a news wire service that wished to provide a listing of daily estimated rates of return and information on the net asset values of publicly offered commodity pools would be excluded from the definition of “commodity trading advisor” (CTA) in Section 1a(5) of the Commodity Exchange Act and therefore would not be subject to Commission registration requirements applicable to CTAs. The listing would be accessible free of charge on the Internet to members of the public. The news service represented that it would offer the listing in a manner that was solely incidental to its general financial reporting services. The information contained in the listing would be calculated by the pools’ commodity pool operators (CPOs), any calculations would be done in a manner consistent with Commission rules, and only data from pools operated by registered CPOs would be used. The news service would not charge listed CPOs a fee for such listing. The news service also affirmed that it would print certain disclaimers in connection with the listing, including statements that the information contained therein may be estimated and was not independently verified. Commission staff emphasized that the CPOs remained subject to all applicable regulations and could be subject to enforcement action if they submitted false or misleading information to the news service.

Alternative Method of Compliance with Requirements for Delivery and Retention of Monthly, Confirmation and Purchase-and-Sale Statements

62 Fed. Reg. 31507 (June 10, 1997) (advisory)

The Commission issued guidance concerning the delivery and retention of certain statements by futures commission merchants.

— <http://www.cftc.gov/foia/fedreg97/970610A.HTM>

62 Fed. Reg. 34165 (June 17, 1997) (correction)

— <http://www.cftc.gov/foia/fedreg97/970617A.HTM>

62 Fed. Reg. 34165 (June 25, 1997) (correction)

— <http://www.cftc.gov/foia/fedreg97/970625A.HTM>

Electronic Filing of Disclosure Documents with the Commission

62 Fed. Reg. 18265 (April 15, 1997) (final rule)

The Commission adopted an optional permanent program for the electronic filing of commodity pool operator and commodity trading advisor Disclosure Documents with the Commission. The Commission also adopted certain technical amendments to codify the permanent electronic filing program.

— <http://www.cftc.gov/foia/fedreg97/970415A.HTM>

Financial Reports of Futures Commission Merchants, Introducing Brokers and Leverage Transaction Merchants

62 Fed. Reg. 10441 (March 7, 1997) (final rules)

— <http://www.cftc.gov/foia/fedreg97/970307C.HTM>

Selected Financial Data for Futures Commission Merchants

The Commission permitted the electronic filing of certain financial reports by futures commission merchants (FCMs), introducing brokers and leverage transaction merchants, using a personal identification number to make the requisite oath or affirmation attesting that, to the best knowledge and belief of the individual making such oath or affirmation, the information contained in the financial report is true and correct. The Commission has instituted a pilot program to allow FCMs to file these reports electronically, using software initially developed by two futures exchanges. The Commission publishes selected data from the reports in April and October of each year, using data from the most recent financial report received just before publication. This summary is available on the Commission's Internet Web site in both html and excel spreadsheet formats for viewing or downloading.

— <http://www.cftc.gov/tm/fcm-9703.htm>

CFTC Letter No. 97-10 (February 27, 1997) (exemptive letter)

Commission staff stated that it would exempt the commodity pool operators (CPOs) of certain publicly offered commodity pools from the requirement that they deliver a copy of the pool's most recent Annual Report at the same time as the Disclosure Document is delivered to a prospective participant. In lieu of delivering the Annual Report with the Disclosure Document, the CPOs would make the Annual Report available upon request prior to sale and such information would be readily accessible as an exhibit to the Form 10-K posted on the Internet Web site of the Securities and Exchange Commission through its EDGAR system. The relief was conditioned upon: (1) inclusion in the monthly Account Statement delivered within the Disclosure Document of any material information required to be contained in the Annual Report; (2) disclosed availability of net asset value per unit as of the close of the previous business day from the CPO or broker; (3) availability of a paper copy of the most recent Annual Report upon request; (4) delivery of the most recent Annual Report within 21 days of a participant's purchase of units; and (5) right to redeem at least as frequently as monthly.

Applications of Futurecom as a Contract Market in Live Cattle Futures and Options

62 Fed. Reg. 4730 (January 31, 1997) (notice of availability of the terms and conditions of proposed commodity futures and option contracts)

The Commission requested public comment on an application by an electronic exchange for designation as a contract market for the Internet-based trading of cash-settled live cattle futures and option contracts and a request for approval of trading rules, rules of government and other materials that the exchange submitted to meet the requirements for a board of trade seeking initial designation as a contract market.

<http://www.cftc.gov/foia/fedreg97/970131B.HTM>

Use of Electronic Media by Commodity Pool Operators and Commodity Trading Advisors

61 Fed. Reg. 44009 (August 27, 1996) (proposed rule)

The Commission proposed technical changes to its rules requiring the filing and distribution of Disclosure Documents by commodity pool operators and commodity trading advisors in order to clarify certain rule provisions that were premised upon the filing and distribution of paper documents.

<http://www.cftc.gov/foia/fedreg97/960827a.htm>

Interpretation Regarding Use of Electronic Media by Commodity Pool Operators and Commodity Trading Advisors

61 Fed. Reg. 42146 (August 14, 1996) (interpretation; solicitation of comment)

<http://www.cftc.gov/foia/fedreg97/960814a.htm>

The Commission published its views with respect to the use of electronic media for the transmission and delivery of Disclosure Documents, reports and other information by commodity pool operators (CPOs), commodity trading advisors (CTAs) and associated persons thereof. The Commission also announced a pilot program for the electronic filing of CPO and CTA Disclosure Documents with the Commission.

61 Fed. Reg. 54731 (October 22, 1996) (extension of comment period and effective date of interpretation)

<http://www.cftc.gov/foia/fedreg97/961022a.htm>

61 Fed. Reg. 65940 (December 16, 1996) (delay of effective date of interpretation)

<http://www.cftc.gov/foia/fedreg97/961216a.htm>

CFTC Letter No. 93-66 (June 18, 1993) (no-action letter)

Commission staff issued a no-action position in connection with the operation of a non-profit electronic market by university faculty for academic research and experimental purposes. The market was composed of three submarkets, known as the "Political Market," the "Earnings Market" and the "Economic Indicator Market," which each permitted trading in various contracts primarily by students, faculty and staff at participating universities who either had local access from personal computers or terminals on university networks or remote access via the Internet and telephone dial-up lines. Commission staff stated that it would not recommend that the Commission take any enforcement action in connection with the operation of the Political Market or the Economic Indicator Market based solely upon their operators not seeking designation as contract markets, not registering under the Commodity Exchange Act (Act) or otherwise complying with the Act or Commission regulations. This relief was subject to, among other things, the operators independently confirming whether or not participation by persons or institutions was permitted by state law. As it appeared that the Earnings Market contracts could be viewed as in the nature of options on securities, which could be subject to the jurisdiction of the Securities and Exchange Commission (SEC), staff forwarded information regarding the market to the SEC.

Information is available upon request from the CFTC's Reading Room, located in Room 4072 at

the Commission's principal office at Three Lafayette Centre, 1155 21st Street, NW, Washington, D.C. 20581. The telephone number is (202) 418-5025. Copies may be made at 15 cents per page.

Contact Information:

CFTC

Headquarters Office

Three Lafayette Centre

1155 21st Street, NW

Washington DC 20581

Tel: (202) 418-5000

Tel: (202) 418-5080 (Office of Public Affairs)

<http://www.cftc.gov>

E-mail: opa@cftc.gov

U. S. Securities and Exchange Commission (SEC)

Amendment to Investment Adviser Recordkeeping Rule; Investment Advisers Act Release No. 952; 50 Fed. Reg. 2542 (Jan. 17, 1985)

Use of Magnetic Tape, Disk, or Other Computer Storage Medium; Investment Company Act Release No. 15410; 51 Fed. Reg. 42207 (Nov. 24, 1986)

Use of Electronic Media for Delivery Purposes; Interpretation; Solicitation of Comments; Securities Act Release No. 7233, Exchange Act Release No. 36345; Investment Company Act Release No. 21399; 60 Fed. Reg. 53458 (Oct. 13, 1995)

<http://www.sec.gov/rules/concept/33-7233.txt>

Use of Electronic Media by Broker-Dealers, Transfer Agents, and Investment Advisers for Delivery of Information; Interpretation; Solicitation of Comments; Additional Examples Under the Securities Act of 1933, Exchange Act Release No. 37182, Investment Company Act Release No. 21945; 62 Fed. Reg. 24644 (May 15, 1996)

<http://www.sec.gov/rules/concept/33-7288.txt>

Use of Electronic Media for Delivery Purposes; Securities Act Release No. 7289, Exchange Act Release No. 37183; Investment Company Act Release No. 21946; 61 Fed. Reg. 24652 (May 15, 1996)

<http://www.sec.gov/rules/final/33-7289.txt>

Reporting Requirements for Brokers or Dealers Under the Securities Exchange Act of 1934; Exchange Act Release No. 38245; 62 Fed. Reg. 6469 (Feb. 12, 1997)

<http://www.sec.gov/rules/final/34-38245.txt>

Rulemaking for the EDGAR System; Securities Act Release No. 7427, Exchange Act Release No. 38798, Trust Indenture Act Release No. 2355, Investment Company Act Release No. 22730; 62 Fed. Reg. 36450 (July 8, 1997)

<http://www.sec.gov/rules/final/33-7427.txt>

Interpretation; Statement of the Commission Regarding Use of Internet Web Sites to Offer Securities, Solicit Securities Transactions, or Advertise Investment Services Offshore. March 23, 1998. Release No. 33-7516. 17 CFR Parts 231, 241, 271, 276 (Release Nos. 33-7516, 34-39779, IA-1710, IC-23071) International Series Release No. 1125

<http://www.sec.gov/rules/concept/33-7516.htm>

Selected Staff Interpretive, Advice and No-Action Letters Addressing Internet Technology

Oppenheimer Management Corporation (Aug. 28, 1995)

The staff stated that it would not recommend enforcement action to the Commission if the Oppenheimer investment advisers and investment companies were to maintain and preserve required records on optical disk or comparable imaging technology that may be developed in the future.

Spring Street Brewing Company (Mar. 22, 1996)

The staff suggested certain modifications to an electronic bulletin board on the Internet to enable the bulletin board to comply with the federal securities laws and reduce the possibility of market manipulation.

Munder Capital Management (May 17, 1996)

The staff stated that it would not recommend enforcement action to the Commission with respect to a registered investment adviser that made portfolio information about its mutual funds available on the Internet.

Real Goods Trading Corporation (June 24, 1996)

The staff stated that it would not recommend enforcement action to the Commission if Real Goods, without registering as a broker-dealer, an exchange or an investment adviser, operated an Internet bulletin board on which interested buyers and sellers could post indications of interest in Real Goods' securities. The staff required, among other things, that Real Goods have no involvement in any transactions other than the posting of interested buyers, sellers and quotes.

IPONet (July 26, 1996)

The staff indicated that the use of an Internet-based system to pre-qualify accredited and sophisticated investors to whom Regulation D offering materials for offerings posted after the pre-qualification would later be made accessible would not constitute general solicitation or general advertising. The staff also stated that indications of interest to be accepted by an electronic coupon meet the requirements applicable to paper cards or coupons.

PerfectData Corporation (Aug. 5, 1996)

The staff stated that it would not recommend enforcement action to the Commission if PerfectData operated an Internet bulletin board on which interested buyers and sellers could post indications of interest in PerfectData's securities, without PerfectData registering as a broker-dealer, an exchange or an investment adviser.

Angel Capital Electronic Network (Oct. 25, 1996)

The staff stated that it would not recommend enforcement action to the Commission if several universities and non-profit entities operated a service on a web site (the "Network"), without registering as broker-dealers, without the Network registering as a broker-dealer or exchange, and without the Network and the Network operators registering as investment advisers. The service would allow accredited investors to access a password-controlled listing of small corporate offerings and to download offering materials.

The Flamemaster Corporation (Oct. 29, 1996)

The staff stated that it would not recommend enforcement action to the Commission if Flamemaster, without registering as a broker-dealer, an exchange or an investment adviser, operated an Internet bulletin board on which interested buyers and sellers could post indications of interest in Flamemaster's securities.

Charles Schwab & Co., Inc. (Nov. 27, 1996)

The staff stated that it would not recommend enforcement action to the Commission if Charles Schwab & Co., Inc., a registered broker-dealer, paid certain Internet on-line service providers a nominal, flat fee for routing orders sent by the broker-dealer's customers, without those on-line services registering as broker-dealers.

ITT Corporation (Dec. 6, 1996)

The staff confirmed that identification of ITT's web site in a prospectus and a statement that ITT's filings are available on its web site will not, by itself, incorporate by reference information from the web site into the registration statement that is not otherwise incorporated.

Baltimore Gas and Electric Company (Jan. 6, 1997)

The staff confirmed that identification of Baltimore Gas and Electric's (BG&E) web site in a prospectus and a statement that BG&E filings are available on its web site will not, by itself, incorporate by reference information from the web site into the registration statement that is not otherwise incorporated.

Private Financial Network (Mar. 12, 1997)

The staff stated that it would not recommend enforcement action to the Commission if Private Financial Network (PFN), a subsidiary of a joint venture between NBC and Microsoft, transmitted live or delayed roadshow presentations by satellite, telephone and cable to PFN subscribers' computer or television monitors.

The Securities Transfer Association, Inc. (Oct. 24, 1997)

The staff stated that it would not recommend enforcement action to the Commission if, in reliance on an opinion of counsel that registration under the Securities Act is not required, a bank or issuer uses its Internet Web site in connection with an open-market stock purchase plan (Plan) as described in the request and without compliance with the Securities Act's registration provisions.

Lamp Technologies, Inc. (May 29, 1998)

The staff stated that it would not recommend enforcement action to the Commission if certain information about unregistered investment companies were available on Lamp's web site, operated as described in a previous no-action letter, Lamp Technologies, Inc. (May 29, 1997), with some modifications. Lamp proposed to eliminate the requirements that investors had to pay a set subscription fee and have an investment portfolio of at least \$2 million. The staff agreed that these modifications would not alter the position taken in the earlier letter. The staff also clarified that its prior position would not be affected if the private funds were structured as entities other than limited partnerships.

Charles Schwab & Co., Inc. (July 7, 1997)

The staff agreed that customer purchase or sale orders placed directly with Schwab or its sub-designee may be deemed to have been received by the relevant fund for purposes of Rule 22c-1 under the Investment Company Act at the time that Schwab or its sub-designee accepts the order.

Net Roadshow, Inc. (July 30, 1997)

The staff stated that, subject to certain conditions, it would not recommend enforcement action to the Commission if Net Roadshow, Inc. transmitted delayed roadshow presentations over the Internet.

Internet Capital Corporation (ICC) (Dec. 24, 1997)

The staff stated that it would not recommend enforcement action under Exchange Act Section 15(a) if ICC establishes and operates the described Internet web site without registering as a broker-dealer under Exchange Act Section 15(b).

Internet Capital Corporation (ICC) (Jan. 13, 1998)

The staff agreed not to recommend enforcement action to the Commission if a company, without registering as an investment adviser, established and operated a passive bulletin board on a web

site to facilitate the trading of securities of unaffiliated companies. The staff relied on representations that neither the company nor any affiliate would give advice regarding the merits or shortcomings of any particular trade.

Net Roadshow, Inc. (Jan. 30, 1998)

The staff stated that it would not recommend enforcement action to the Commission if Net Roadshow transmits road shows over its Internet Web site solely to "qualified institutional buyers" (QIBS) on behalf of a QIB (or person acting on its behalf) that purchases securities from an issuer for resale to other QIBS under Rule 144A ("Seller").

StockPower, Inc. (Mar. 26, 1998)

The staff stated that it would not recommend enforcement action against StockPower, Inc. for failing to register as a broker-dealer if StockPower, Inc. makes available "payment software" and related services that would allow new investors or existing shareholders of particular issuers to purchase through the Internet the issuers' shares directly through a dividend reinvestment and stock purchase plan. The payment software enables individuals to interact electronically with participating bank transfer agents, rather than using regular mail or the telephone.

Charles Schwab & Co., Inc. (July 17, 1998)

Schwab was granted relief to provide its customers, through Schwab's Web site, with industry consensus recommendations, consensus earnings estimates and historical earnings data compiled by Standard & Poor's and First Call Individual Investor Services (Providers) without requiring the Providers to register as brokers or dealers.

Please submit all requests in writing to::

Affairs, Stop 3-11

<http://www.sec.gov>
publicinfo@sec.gov

Tel: (202)942-0020

Fax: (202) 942-9654

Washington, DC 20549

SEC
Office of Public
450 5th Street, N.W.

E-mail:

Selected SRO Statements, Rules and Guidance

National Association of Securities Dealer (NASD)

NASD Internet Guide for Registered Representatives

<http://www.nasdr.com/4040.htm>

NASD Notice to Members 96-50 (July 1996)

<http://www.nasdr.com/2611/26119650.htm>

NASD Notice of Members 96-82 (Dec. 1996)

<http://www.nasdr.com/pdf-text/9682.ntm.txt>

or

<http://www.nasdr.com/pdf-text/9682.ntm.pdf>

(Adobe Acrobat is required to read this document.)

NASD Notice to Members 95-74, and NASD Notice to Members 95-80; Exchange Act Release No. 36076 (Aug. 9, 1995), 60 Fed. Reg. 4220 (Aug. 15, 1995).

Self-Regulatory Organizations; Order Approving Proposed Rule Change and Notice of Filing and Order Granting Accelerated Approval to Amendment No.1 to Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to Supervision and Record Retention Rules; Exchange Act Release No. 39510; 62 Fed. Reg. 24147 (December 31, 1997)

http://www.nasdr.com/pdf-text/approval_9724.txt

The SEC approved amendments to the NASD's rules to broaden the definitions of advertisement and sales literature to address the increasing use of electronic media.

The NASD rules also encourage issuers to consider technological methods to communicate interim earnings reports in a timely and less costly manner to both registered and beneficial shareholders.

[Notices published prior to 1996 are not currently available electronically, but may be in print version by calling the NASD's MediaSource at (301) 590-6142]

NASD Rule 2210 (Communications with the Public)

http://www.nasdr.com/conrule_2210.htm

NASD Rule 2310 (Recommendations to Customers [Suitability])

http://www.nasdr.com/conrule_2310.htm

NASD Rule 3010 (Supervision)

http://www.nasdr.com/conrule_3010.htm

NASD Rule 3110 (Books and Records)

http://www.nasdr.com/conrule_3110.htm

The NASD's rules were amended to require a registered principal to approve all advertising and sales literature items prior to use or filing with the NASD.

Contact Information:

NASD
Street, NW
DC 20006-1500

1735 K
Washington,

Tel: (202) 728-8000

Tel: (301) 590-6500 (Inquiries)

Fax: (202) 293-6260

E-mail: iielistsrv@nasd.com (Office of Internet & Investor Education)

[www.http://www.nasd.com](http://www.nasd.com)

Relations -

Condon: 202-728-8379; E-mail: condonn@nasd.com

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NYSE Information Memo 98-03, New Rules - Supervision and Review of

f:\myfiles\projects\internet\final.doc

Communications with the Public (Jan. 14, 1998).

<http://www.nyse.com/public/invprot/5c/5c1/1998/im9803.htm>

or

<http://www.nyse.com/public/invprot/5c/5c1/1998/im9803.pdf>

(Adobe Acrobat is required to view this document)

NYSE Rule 342 (Offices - Approval, Supervision and Control)

NYSE Rule 440 (Books and Records)

NYSE Rule 472 (Communications with the Public)

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