S U N R I S E R E V I E W

FINANCIAL PLANNERS

Submitted by
The Colorado Department of Regulatory Agencies
June 1991

STATE OF COLORADO

DEPARTMENT OF REGULATORY AGENCIES
Office of the Executive Director
Steven V. Berson, Executive Director

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Roy Romer
Governor

May 15, 1991

The Honorable Bob Schaffer
Joint Sunrise/Sunset Review Committee Chairman
Room 348, State Capitol Building
Denver, Colorado 80203

Dear Senator Schaffer:

We have completed our evaluation of the sunrise application for licensure of financial planners and are pleased to submit this written report which will be the basis for my office's oral testimony before the Sunrise and Sunset Review Committee. The report is submitted pursuant to section 24-34-104.1, Colorado Revised Statutes, 1988 Repl. Vol., (the "Sunrise Act") which provides that the Department of Regulatory Agencies shall conduct an analysis and evaluation of proposed regulation to determine whether the public needs and would benefit from the regulation.

The report discusses the question of whether there is a need for the regulation in order to protect the public from potential harm, whether regulation would serve to mitigate the potential harm and whether the public can be adequately protected by other means in a more cost effective manner.

Sincerely,

Steven V. Berson
Executive Director

SVB/pf
Attachment

1991 SUNRISE REVIEW OF FINANCIAL PLANNERS

PART I

INTRODUCTION

The Department of Regulatory Agencies has completed its evaluation of the application for regulation submitted by the Colorado Investment Advisers Act Committee. The applicants seek additional state regulation of persons who hold themselves out as financial planners or who give advice and direction with respect to specific purchases of securities in return for compensation. Pursuant to the Colorado Sunrise Act, C.R.S. 24-4-104.1, the applicants must prove the benefit to the public of their proposal for regulation according to the following criteria:

1. Whether the unregulated practice of the occupation or profession clearly harms or endangers the health, safety or welfare of the public, whether the potential for harm is easily recognizable and not remote or dependent on tenuous argument;

2. Whether the public needs, and can be reasonably expected to benefit from, an assurance of initial and continuing professional or occupational competence;

3. Whether the public can be adequately protected by other means in a more cost-effective manner.

METHODOLOGY

The author of this report was greatly aided by the effort of the Securities Law Review Committee of the Colorado Bar Association. Under the leadership of David Johnson of the law firm of Sherman and Howard, the committee has been engaged for many months in research and discussion of a proposal for strengthened regulation in this area. In addition, numerous interested persons and organizations were invited to participate in the discussions of the committee. Attempts were made to accommodate the views of those persons and groups in this proposal for regulation.

SUMMARY OF FINDINGS AND RECOMMENDATIONS

FINDINGS

1. The term "financial planner" is a general and imprecise term which is used by many different persons and organizations to describe different financial services offered to different types

of consumers. In its most generic sense, the term financial planner describes one who gives general advice to a client on how to handle money in return for some sort of fee or commission.

2. The term "financial planner" carries with it the implication that the planner is a counselor to the client who will assist the client in setting and achieving financial goals. Thus, a trust relationship is implied.

3. Financial planning services are provided by unlicensed persons as well as licensed professionals, such as lawyers, certified public accountants, insurance professionals and securities brokers and dealers. Financial planners who are unlicensed make up a minority of all financial planners.

4. Although financial planners are often lumped together with investment advisers who manage the money only of wealthy persons and firms, it is important to distinguish between the two groups. For purposes of this report and the proposed legislation it contains, investment advisers who are money managers are deemed to have a sophisticated clientele familiar with the investment process, while the clients of investment advisers who call themselves financial planners include consumers of more modest means who may not be familiar with the investment process.

5. There are several significant private associations of financial planners that have been active in attempting to upgrade the status of the profession, including the Institute of Certified Financial Planners (ICFP), a Denver-based national professional association, the International Association for Financial Planning, (IAFP), and the National Association for Personal Financial Advisers, (NAPFA), based in Chicago, Illinois.

6. Financial Planning has been a growth industry during the last decade, with current estimates of the numbers of financial planners ranging from 250,000 to 400,000. The estimates vary widely because of the different definitions of the term "financial planner" used by researchers.

7. All but seven states and the District of Columbia have chosen to regulate financial planners. The most common regulatory system adopted by the states involves the requirement that persons who advise their clients to make certain investments must register with the state as an "investment adviser." These state laws generally closely parallel the existing federal law, the Investment Adviser Act of 1940. States with no investment adviser regulation at all are Arizona, Colorado, the District of Columbia, Iowa, Massachusetts, Ohio, Vermont and Wyoming.

8. Available information indicates that the citizens of the state of Colorado would benefit from increased regulation of financial planners who give specific investment advice to their clients by

the imposition of a Colorado investment adviser registration requirement administered through the Colorado Division of Securities.

RECOMMENDATIONS

Recommendation 1: The General Assembly should implement increased regulation of those financial planners giving specific investment advice to their clients in return for compensation.

Recommendation 2: It is not recommended that the term "financial planner" be regulated or restricted due to its imprecise nature and the generality of the services offered by persons using that or related titles.

Recommendation 3: The best vehicle for instituting increased regulation in this area is the proposed Colorado Investment Advisers Act found in Appendix A of this report, based on its successful use in other states and its coordination with existing federal law.

Recommendation 4: This new regulatory system should be located in the most appropriate state government agency, which is the Colorado Division of Securities.

APPLICATION FOR REGULATION

PART 2

The application for regulation of financial planners in Colorado was submitted by the Colorado Investment Advisers Act Committee. This committee consists of individuals and representatives of interested groups who are concerned with the lack of regulation of financial planners in Colorado. The applicants point out that "there is no one organizational sponsor or self-regulatory organization that is representing an unregulated occupational group with respect to this application."

The applicants also cite the work of the Securities Law Review Committee of the Colorado Bar Association as being instrumental in laying the

ground work for the submission of this application. It should be noted, however, that the Colorado Bar Association "has taken no position with respect to the proposed legislation", at least at the time this report was released, and is not a member of the applicant group.

According to the applicants, Colorado associations and organizations that are likely to have some members give investment advice in their work include the following:

* Certified Financial Planner licensees of the International Board of Standards and Practices for Certified Financial Planners, Inc.. (IBCFP)

* Institute of Certified Financial Planners

* Colorado Society of Certified Public Accountants

* Investment Advisers registered with the Securities and Exchange Commission

* Persons registered with the National Association of Securities Dealers

* Trust officers with Colorado banks, savings and loans and other financial institutions

* American Society of Chartered Financial Consultants and Certified Life Underwriters

* Colorado Bar Association members

* Association for Investment Management and Research (Chartered Financial Analysts)

* International Association of Financial Planners

* Colorado Association of Life Underwriters

* Independent Insurance Agents of Colorado

* Licensed Real Estate Brokers and Salespersons.

DEFINITION OF TERMS

Since there is no regulation of financial planners in the state of Colorado, the term "financial planner" includes anyone who offers investment advice to a client in return for compensation. All groups, persons and professions indicated above, therefore, may be involved in the performance of financial planning. For example, CPAs take the position that giving this kind of financial advice has been part of their profession since its inception.

Insurance agents, attorneys and securities professionals may become financial planners, by circumstance or design, in the performance of their professions. Persons holding designations such as "certified planner" and other similar designations, are attempting to delineate a clear role for persons using the term "financial planner" based on published guidelines and ethical responsibilities and premised on providing clients with a wide scope of information and assistance as part of a process of preparing and implementing a financial plan.

Because the performance of financial planning services crosses the boundaries between many well established professions, and because the harm posed to consumers is most clearly related to the performance of some, but not all, of the services provided by these persons, it is both more convenient and more useful to define a financial planner as a person who is included in the term "investment adviser." The definition of the term "investment adviser" is well established in federal law in the Investment Advisers Act of 1940:

> "Investment adviser means any person who, for compensation, engages in the business of advising others, either directly or through publications, writings or electronic means, as to the value of securities or as to the advisability of investing in securities or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities. Investment adviser includes a financial planner or other person who, as an integral component of other financially related services, provides investment advisory services to others for compensation and as a part of a regular business or who is held as providing investment advisory services to others for compensation."

The definition of investment adviser, which includes the term "financial planner," focuses on the services provided by those persons which are related specifically to the giving of advice about investing in securities. The key to the definition is that it <u>excludes persons who give general investment advice</u> and focuses on persons who make recommendations for investments or investment related purchases of securities.

Examples of such purchases include insurance policies, mutual funds, stocks and limited partnerships. Due to the wide diversity of persons and firms rendering financial advice in the United States today, it is important for the purposes of this report to focus, as the above definition does, on the rendering of specific investment advice in return for compensation. This is the thread which ties together the different persons and organizations offering services which involve both a demonstrated and potential harm to consumers in Colorado.

APPLICATION FOR REGULATION

The basic elements of the regulatory scheme that the applicants have requested are as follows:

1. Registration of all persons in Colorado who fit the definition of "investment adviser" which is patterned after the Investment Advisers Act of 1940.

2. Registration of all persons who act as representatives of investment advisers and, therefore, are directly involved in giving investment advice to consumers.

3. An examination requirement for those persons listed in numbers one and two above, who do not meet minimum experience requirements. (Such a requirement might be a minimum of five years experience in the business.)

4. The establishment of a fee for each license and exam.

5. The establishment of a record keeping requirement.

6. The establishment of a disclosure requirement in order to provide consumers with basic information regarding the experiential background of the investment adviser/financial planner as well as details regarding compensation.

7. Specific enforcement authority vested in a Colorado regulatory body. This enforcement would be separate from, but could be exercised jointly with the Securities and Exchange Commission.

8. Establishment of the regulatory program in the Colorado Division of Securities.

The basic elements of this proposal parallel investment adviser laws found in most states and at the federal level. In order to understand the impact of this proposal, it is necessary to look more closely at the development of the profession of financial planning.

DESCRIPTION OF FINANCIAL PLANNING PRACTICE

> "Financial planning has emerged as a buzz word of the 1980's. As no legal definition of the term exists, it is applied almost indiscriminately to a wide array of services. These services are provided by 'planners' with equally diverse qualifications. Because of financial planning's relatively recent emergence as a major industry, very little is known about those calling

themselves financial planners - - how many there are, how they do business. For consumers, the result is at best confusion and at worst great financial risk."

> "Financial Planning Abuses: A Growing Problem," a report of the Consumer Federation of America, July, 1987.

One of the reasons for confusion among the public with respect to financial planning in the United States today is summed up by Richard Gould in a recent article in Trusts and Estates:

> "Financial planning at this point is not so much an industry as the convergence of several industries in pursuit of a market. Life insurance agents, stock brokers, bankers, accountants, investment advisers, estate planning attorneys and a host of opportunists have come together, with widely different backgrounds and motives, under one professional banner: 'financial planner.'"

Indeed, it has only been within the last decade or so that financial services were provided other than through clearly segmented kinds of service companies, such as insurance companies, realty companies, banks and brokerage houses. Each sold a well defined product. But as financial services have become consolidated with individual companies offering the variety of investment instruments, new types of companies and individuals have emerged which offer an array of financial services and financial investment instruments. By offering financial planning services, it has become possible to attract new clients who can then serve as an investor pool when it comes time to implement the financial plan.

In addition, the use of financial planning services has become generalized to a broad segment of the population. Traditionally, financial planning and investment advice was mainly the realm of the wealthy. Today, millions of persons are interested in financial planning in order to fund their children's education, to buy a home and to provide for financial security in retirement. These persons represent a vast new market for financial planners/investment advisers and do not fit the traditional definition of sophisticated or accredited investors. This group of persons, in particular, may be at risk in following the advice of unscrupulous financial planners and can ill afford to take significant losses.

According to statistics compiled by the International Association for Financial Planning, 13% of all Americans now use financial planners and that number is increasing steadily. The Securities and Exchange Commission estimates that investment advisers registered with the

Commission manage total assets in excess of $4.6 trillion. This represents a change from $450 billion under management in 1981, or an increase of ten fold. In addition, the numbers of registered investment advisers has risen steeply according to the S.E.C. Between October, 1980 and October, 1987, the number of RIAs had risen from 4,580 to 12,700, or an increase of 173%. Today the G.A.O reports there are 14,000 registered investment advisers. These numbers are even more impressive since S.E.C. figures reflect only the number of firms and not the number of individuals registered to offer investment services. . Financial planning trade associations have also reported sharp increases in their membership in the last ten years.

Another new aspect to this industry is the predominance of, and reliance on, advertising to attract new customers. According to James C. Meyer, former president of the North American Securities Administrators' Association:

> "The aggressive advertising and promotion of the financial planning concept has led to some uncertainty among the public as to what financial planning is and what a financial planner does. That uncertainty has allowed numerous individuals in the financial services profession, as well as out-and-out con men, to mislead the public by claiming to be financial planners, when in fact, they have neither the credentials nor the professional expertise necessary to provide that service. There are many honest, skilled people doing excellent work today as financial planners. Reputable financial planners provide a service that can be of use to thousands - if not millions - of Americans. But it is equally apparent that this industry can also provide "deep cover" for a substantial number of swindlers, con artists and abusive or unethical promoters."

Mr.. Meyer goes on to outline several common frauds or abuses which have emerged in the financial planning industry. The nature of these problems is a result of the special and sensitive relationship which is formed between a financial planner and a client.

First of all, current federal registration of investment advisers under the Securities and Exchange Commission requires investment advisers to register but does not require any applicant to satisfy any formal minimum standards. Therefore, anyone can register to be an investment adviser by filling out the S.E.C.'s form ADV and paying the $150.00 fee. Once the application is accepted, and applications are almost never denied, the applicant may truthfully represent him or herself as an investment adviser registered with the Securities and Exchange Commission. The only further oversight the S.E.C exercises over investment advisers is through infrequent inspections.

According to S.E.C. and G.A.O. statistics, the first inspection by S.E.C. of a newly registered investment adviser usually does not occur until an average of three years after registration, if at all. If deficiencies are noted, follow-up inspections are possible but infrequent. Thus, the problem of unqualified or inexperienced financial planners/investment advisers is a real one. On one hand, a well qualified financial planner needs a wide ranging knowledge of law, taxes, insurance, pensions, real estate and various other investment instruments. In fact, federal regulation not only does not require such wide ranging knowledge, but requires no knowledge at all. The potential impact of this standard, as clearly pointed out by the G.A.O. is:

> "The 1940 Act may be doing more harm than good by giving investors the illusion that S.E.C. registered advisers have 'seal of approval'."

The second generally recognized problem in the industry is that financial planners/investment advisers are easily susceptible to being "product driven." Many of these persons come to the business of giving financial advice from one background, such as securities, insurance or real estate. Since very few financial planners simply plan and very few financial advisers simply advise, the implementation recommendations they make are often slanted toward the products with which they are most familiar.

In addition, persons marketing financial investment products are very aggressive. It is common that such marketing includes special prizes, commissions or bonuses to the sellers of the product. Since most financial planners and investment advisers earn the majority of their compensation through commissions, it is natural for those persons to incline toward recommending that their clients purchase the financial instrument which offers the planner or adviser the greatest reward.

S.E.C. investigations bear out the concern in this area. For example, recent inspections of active planners showed that 85% of them were affiliated with an organization that sold financial products. In every case, the time spent on developing a financial plan was dwarfed by the amount of time spent in selling the client products for the purpose of "implementing" the financial plan.

Further, according to statistics gathered by the National Association of Financial Planners, 64% of the average planner's gross revenue comes from commissions. It is clear then that there is a strong influence at work in favor of selling the client the products which the planner/adviser is most familiar with and from which the planner/adviser may receive the most benefit.

Thirdly, disclosure continues to be a problem. The federal and state securities laws have always been based largely on the concept of disclosure. It has been and continues to be believed that a client who

receives full disclosure of all relevant facts related to an investment purchase would best be able to make a rational decision about whether to proceed with the transaction.

According to the S.E.C., disclosures currently required under the federal act are "not routinely provided." According to S.E.C. inspection data, while 85% of planners/advisers actually sell products to clients, only 37% informed prospective clients of their sales function. Often, even when disclosures are made, the disclosure brochures are more in the vein of cleverly planned advertising than anything else.

Fourthly, the financial planning/investment adviser field has become notorious as a cover for confidence men. Clearly, part of the problem is, and will always be, simple greed. Persons who are attracted to an investment based on the promise of uncommon rates of return are most often easy prey.

The abuses take many, often intricate forms. For example, investment firms and professionals often find themselves susceptible to "moonlighting" abuses by employees or related persons.

According to NASA's Meyer:

> "A moonlighter may capitalize on his employment relationship with an established brokerage, insurance or realty firm as a lure to attract customers to the planning or advisory business. Borrowing on the credibility of an affiliation from an established firm, moonlighters can convince customers of their financial expertise or business acumen. The existing employment relationship may then be used to sell products recommended to a planning or advisory customer. Operating off the premises of the employing firm, the planning or advisory services of a moonlighter may not be detected by the day-to-day supervisory oversight of the employing firm."

The common result of the problems outlined above is that the client suffers a financial loss. At worst, all or substantially all of the money invested is lost. At best, the investment is simply unsuitable to the needs of the investor and does not result in greater financial security.

DISCUSSION OF HARM

According to data recently compiled by the International Board of Standards and Practices for Certified Planners, Inc.., it appears that there are currently about 3,435 financial planners in Colorado. This number includes 438 persons and firms who are registered with the Securities and Exchange Commission as investment advisers and who have

indicated on their registration form that they hold themselves out as providing financial planning or some similarly termed services to clients.

Since 1989, more than 30 cases of financial planner abuse of clients has been discernible in Colorado, according to the IBCFP. Research both on the number of financial planner/investment advisers and the number of abuses continues to be difficult since there is no specific regulation in Colorado for financial planners or investment advisers and, therefore, no central location to capture all the relevant information. However, of all the problems and cases which have appeared in this field, both in Colorado and across the country, one of the most notable is the recent case of Englewood investment advisor, James D. Donahue, who has been accused of fraud in the recent loss of more than $100 million in client funds.

THE DONAHUE CASE

On August 23, 1990, Donahue, via video tape, announced to hundreds of his clients gathered in a ballroom of a Denver hotel that he had lost practically all of their money. Although the exact amount of the losses was not announced, Donahue stated:

> "At the request of many individual investors to keep the extent of their participation confidential, the total dollar loss will be disclosed through correspondence and through final accounting, and not at this semi-public meeting. The loss is extensive and it involved almost all of the total assets of the fund."

Donahue's fund was known as Hedged-Investment Associates, (HIA), which was the general partner of more than 20 limited partnerships, all sharing a common portfolio managed exclusively by Donahue. At the end of June, 1990, accounts managed by HIA showed a balance of more than $268 million. If interest which was claimed by Donahue to have been earned on these investments is included in the value of the partnership, more than $303 million was involved. However, since Donahue was the keeper of the books for HIA and since he has admitted inflating the numbers over many years, all that is known for sure today is that the partnership is worth less than $2 million, according to the trustee in bankruptcy.

As is the case with many investment advisers/financial planners, Donahue's fame as a financial czar became known largely by word of mouth. In addition, Donahue was a gifted salesman who was able to sell many investors, both average consumer types and large pension funds, on his financial acumen. For years, Donahue claimed that his clients earned at least a 15% rate of return. The periodic reports sent to clients, without any auditing support, showed consistently high rates of return

even when the rest of the nation's financial system was convulsing, such as happened in October, 1987.

More than 1,500 investors have apparently lost all of the money they placed with Donahue. This includes some well-known persons such as former Secretary of the Interior James Watt. Other notable clients claiming significant losses include:

Weyerhaeuser Pension Fund (about $25 million in losses)

Paradigm Partners (about $15 million in losses)

Union Texas Petroleum Corp. (about $8 million in losses) and

Grosvenor Capital Management (about $12 million in losses).

It should be pointed out, however, that Donahue's clients were not limited to the wealthy. Numerous individuals and even groups of persons affiliated with certain churches were persuaded to invest with Donahue. For example, members of two church congregations, one in Englewood and one in Detroit, consisting of a group of about 150 families in all, invested their savings with Donahue. In January, 1990, Donahue accepted for investment the entire reserves of the governing body of the Evangelical Presbyterian Church, amounting to approximately $100,000. As Donahue's name spread, his employees, friends and friends of friends often approached him with sums of money they had scraped together, often by taking all of their savings and mortgaging their homes. Thus, when Donahue announced that all of this money had been lost, primarily in transactions, "involving United Airlines stock option positions", a wide variety of persons were hurt.

Ironically, Donahue was completely open with his clients about his lack of registration with the S.E.C. and the lack of independent audits of his financial activities. The closest Donahue came to preparing a financial report for his clients was in August, 1989, when his secretary's husband prepared an "Accountant's Report", which Donahue apparently used in confirming his financial activities with his clients. Donahue's companies were not required to register with the Securities and Exchange Commission under the Investment Company Act of 1940 because his investors were split into numerous limited partnerships. Since that law provides that money managers with 100 or more investors have to register as mutual funds, Donahue's business format was not covered. In addition, Donahue simply claimed that dealing with the federal government was expensive and time consuming.

In this case, the losses were finally uncovered when representatives of Weyerhaeuser and Paradigm Partners became concerned and paid an unexpected personal visit to Donahue on August 13, 1990. After his announced losses to shareholders on August 23, 1990, Donahue has

subsequently been silent with respect to his activities. Numerous lawsuits are pending against James Donahue both in federal court and state courts in Colorado. As previously indicated, Donahue's firm is in bankruptcy. The charges against Donahue include breach of contract, breach of fiduciary responsibility and fraud.

One of the most disturbing aspects of the Donahue case is the willingness of Donahue's investors to place their funds under his management and control with virtually no information about his financial dealings. Although it is questionable whether any regulatory system could help people so willing to part with their money, the lack of effective regulation certainly assisted in creating a situation where abuse of investor funds was a simple proposition. A review of other cases of consumer harm shows a similar pattern.

OTHER CASES OF HARM

As previously indicated, there is no single repository for complaints against investment advisers or financial planners in the State of Colorado. However, a recent research report update on complaints regarding Colorado financial planners dated March, 1991, and compiled by the International Board of Standards and Practices for Certified Financial Planners, Inc.., provides some information regarding Colorado cases. Among those groups or agencies reporting financial planner/investment adviser complaints were the following:

1. National Association of Securities Dealers: - 5-6 complaints per year.

   Type of complaints: suitability of investments, mainly concerning limited partnerships; advertising mutual funds without disclosures. These complaints are referred to the Securities and Exchange Commission.

2. Colorado Division of Securities: 10 cases since 1989. Case histories reprinted on the following pages.

3. International Board of Standards and Practices for Certified Financial Planners: 6 cases since 1989. See case histories reprinted on following pages.

4. Colorado Better Business Bureaus: Denver: 5 cases since 1989. Fort Collins: 26 cases in 1987-88 (information for '89 and '90 not available). Pueblo: 4 cases in 1989.

5. Colorado courts: El Paso and Teller Counties: 2 cases since 1989. Jefferson County: 1 case. Larimer County: 2 cases. Pueblo County: 1 case. Weld County: 6 cases.

6. U. S. District Court: 2 cases since 1989.

STATE OF COLORADO

CASE HISTORIES

The following case histories are reprinted from the files of the Colorado Division of Securities.

Donald Thomas and Seeger Financial Corporation

Seeger operated in Colorado Springs. Between 1983 and 1986, he and his sister raised $2.4 million from approximately 151 investors through the offer and sale of various "investment contract" securities involving mostly real estate and related investments. Seeger held himself as a virtual supermarket of investments, ranging from real estate to bridge loans to IRA'S, to even something called "plywood banking". He portrayed himself as a master of all these investments and strategies.

No one involved was registered as a broker, dealer, principal or representative. Following action taken by the Securities Division in Denver District Court, Seeger and his operation were enjoined from violation of the registration and anti-fraud provisions of the Colorado Securities Act of 1981. He filed for protection under federal bankruptcy laws. He then stipulated to permanent injunction. Soon after, he commenced another securities under an alias. The Securities Division sought to have him held in contempt. He was sentenced to 30 days in jail, but appealed. On appeal, the case was remanded for rehearing. Seeger was again held in contempt and again sentenced. The Seeger matter was also referred to the attention of the Colorado Attorney General for consideration of criminal prosecution of criminal prosecution. Multiple charges were filed against him in El Paso County. Seeger pled guilty to three counts and was sentenced to six years in prison. Seeger is currently in jail on the contempt sentence, although he is appealing that, and has indicated his intention to appeal his sentence in the criminal case. Both matters remain pending.

R. Donald Jackson

Jackson was registered with the Securities and Exchange Commission as an investment advisor. He held himself out as a financial planner. He served as a salesman for a colossal fraud called RaTek, a real estate venture. More than $8 million was lost. He subsequently sold other investments to his RaTek investors in the attempt to recoup their losses, according to him. Jackson stipulated to a permanent injunction and agreed to repay $80,000 to this second tier of investors. Only $5,000 was repaid.

The Division then discovered that, acting as a financial planner, Jackson solicited approximately $40,000 from 155 investors in the offer and sale

of "self liquidating loans". The Division sought to have him held in contempt of the permanent injunction against unregistered activity and fraud. He was found in contempt and sentenced to 120 days in jail. He appealed.

During the pendency of the appeal, he was arrested and convicted of federal charges stemming from his fraudulent sale of telephone access codes. He was found guilty and sent to federal prison . Based on the state court advisor injunction, the Securities and Exchange Commission revoked his investment advisor registration. Just before his release from prison, the Colorado Court of Appeals upheld his contempt conviction, in principle, but remanded the case on procedural grounds. On rehearing, Jackson's 120 day sentence was reinstated. Jackson is serving that time or has just recently completed the sentence.

Ronald Haves Ross

Ross is a public accountant (though not a CPA) and has held himself out to be a "financial planner". In a criminal complaint filed by the Arapahoe County District Attorney in March of 1989, Ross is charged with defrauding 15 Colorado investors out of approximately $400,000 by selling five different investment programs involving Arabian horses in violation of the Colorado Securities Act of 1981. The investments were taken between 1983 and 1989. The charges are pending.

Equivest Financial Services

Between approximately 1984 and 1986, Ray Werner, John Hill and Equivest, holding themselves out to be investment counselors and advisors, took investments from approximately 50 persons of over $1.2 million to be placed in various investments including mortgages, consumer note pools, etc. The Securities Division filed an injunctive action against them. Hill and Equivest consented to the entry of a permanent injunction and judgment of $1.3 million. Werner and his wife sought protection under federal bankruptcy law. Hill filed bankruptcy subsequently. Hearing is pending before the bankruptcy court.

Brian Flanders, et al

Developing an advisory relationship with various insurance clients, Flanders took approximately $600,000 from 20 investors between 1984 and 1987. These investments were to be used for mortgages or real estate. The Securities Division filed an injunctive action against the defendants. They stipulated to preliminary injunction and to the appointment of a receiver. Flanders subsequently stipulated to a contempt order after using estate proceeds in a manner contrary to the court's order. Further action is pending.

Jan Guadina and North American Mortgage

Gaudina, through North American Mortage in Boulder, offered and sold real estate related trust deed investments totalling approximately $4 million

to 150 investors over a seven year period from approximately 1980 to 1987. The Securities Division filed an injunctive action against Gaudina and his many companies, alleging in part that the operations were nothing but a large Ponzi Scheme. Gaudina stipulated to a preliminary injunction after filing for protection under federal bankruptcy laws. The Division sought and the bankruptcy court appointed a trustee over Gaudina's affairs. Gaudina was subsequently held in contempt of the state district court's injunctive order for using proceeds of the estate contrary to court mandate. Trial on the permanent injunction is scheduled soon.

Larry Lowry

Lowry is an ex-CPA who raised approximately $2 million from 177 investors by selling real estate limited partnerships. Lowry was indicted in El Paso County on 109 counts of unregistered dealer and anti-fraud violations.

Anonymous Case #1

Acting as a "financial consultant", the subject solicited close to $32,000 from one investor in 1983 to be invested in an oil and gas well. The proceeds were shifted from the oil and gas well to real estate to an electronics company, but in the end were simply dissipated.

Anonymous Case #2

The subject solicited almost $550,000 from approximately 11 investors between February and August, 1987 to be pooled and invested in U.S. Government bonds. Injunctive action against the subject is pending.

Anonymous Case #3

The subject was registered with the SEC as an investment advisor. Between 1982 and 1987, the subject advised clients to invest in several different programs. The subject also sold approximately $400,000 in promissory notes and mortgage bonds issued by the subject's own mortgage investment company to 36 investors. For each recommendation, the subject received commissions. In 1988, the subject moved to another state and filed bankruptcy. Approximately $1 million was taken from 30 investors in one related case, and $2.6 million was taken from approximately 140 in another. All of the activity occurred between 1983 and 1986. The subject is presently registered with the SEC as an investment advisor and resides in another state.

FINANCIAL PLANNER COMPLAINTS - PROFESSIONAL ASSOCIATION

The following case histories are taken from the files of the International Board of Standards and Practices for Certified Financial Planners, Inc.. (IBCFP); Denver, Colorado office.

1989

Contact:	Investigator
No. of Complaints:	Approximately 5
Comments	Since March , 1987 there have been approximately 5 complaints on Certified Financial Planner registrants in Colorado.

June 1989 through December 1990:

Contact:	Investigator
Number of Complaints:	1
Comments:	1987 - 1 complaint 1988 - 1 complaint 1989 - 3 complaints 1990 - 1 complaint

FINANCIAL PLANNER COMPLAINTS - COLORADO

By the International Board of Standards and Practices
of Certified Financial Planners, Inc..

Anonymous Case History #1:

The client brought a complaint to the IBCFP as the result of a failed investment. The client felt the investments were of poor quality and that the CFP registrant failed to make timely responses to his inquiries and concerns.

Code of Ethics: Section IV (B) (1) (c); Section III (A)

Mitigation: Evidence showed that the client was an experienced investor and that the client accepted all risks involved with the investments. The Respondent had no control over the investment's success or failure. The Respondent was a sole practitioner, and when he became ill and unavailable to his clients, he made no arrangements to communicate this to his clients.

Letter of Admonition.

Anonymous Case History #2:

Client complained that the CFP Respondent failed to disclose the various companies he was associated with; that they were told one fee and charged another; that the properties they bought from him were faulty and in need of repair; and that as a financial advisor he would have been able to detect the over building that was occurring in that city.

Code of Ethics: Section I (B) (3), Section I (B) (3) (e), Section I (B) (5) (e) and Section III (B) (5)

Mitigation: The CFP Respondent supplied the IBCFP with documents and information indicating that the Complainant worked with someone other than the CFP Respondent and that the CFP Respondent was merely the owner of the firm. Still, there was no proof of gross negligence on the part of the financial planner, the CFP Respondent and/or the firm. The Complainant failed to supply the IBCFP with requested supporting documents that might have substantiated the allegations.

Dismissed.

Anonymous Case History #3:

The clients complained that the CFP Respondent failed to contact them in over three (3) years regarding their financial plan. The clients state that the CFP Respondent failed to notify them when he changed companies. As a result, clients state it took several trips to the former firm of the CFP Respondent in order to straighten out and update their accounts. Additionally, the clients state that as a result of their being ignored for over three (3) years, a $10,000 investment had plunged to a worth of $750 without them being aware of such a loss.

Code of Ethics: Section IV (B) (1) (c)

Mitigation: The clients had received monthly and quarterly statements from the CFP Respondent's firm regarding their investments. The clients stated that they did not understand the monthly and quarterly statements, but failed to call the CFP Respondent for help. CFP Respondent stated that he sent several letters to the clients and had contacted them on several occasions to update and review their plan. CFP Respondent supplied documentation supporting this claim.

Dismissed.

Anonymous Case History #4:

Clients complained that CFP Respondent borrowed money from them when the CFP knew that he was insolvent and unable to repay those borrowed monies. Additionally, the clients complained that CFP Respondent failed to disclose to the clients the nature of his compensation. Additionally, the clients complained that almost all of the investments that CFP Respondent recommended failed.

Code of Ethics: Section I (A) and Section I (B) (1) (a)

Aggravation: CFP Respondent admitted to borrowing approximately $100,000 from clients and family in an attempt to recoup losses on behalf of other clients in a failed mortgage investment. CFP Respondent denied ever stating that he was a fee only planner, but admitted that he could understand how clients could get the impression that he was fee only. CFP Respondent placed his clients in multiple limited partnership investments which had a high risk quotient and

ultimately proved to be extremely poor investments. Although CFP Respondent testified that the investments had been approved by his broker/dealer and that his clients qualified for the investment, it was considered extremely poor practice to suggest to clients with limited investment capital that they place the bulk of that capital in high risk investments such as real estate limited partnerships in a depressed economy.

Revoked.

Anonymous Case History #5:

Client complained that CFP Respondent recommended investments to him which were unsuitable in light of his financial condition and were riskier than the client's stated objectives.

Code of Ethics: Section II, III and IV

Mitigation: The acts occurred prior to the Respondent receiving his CFP designation, and the client received civil redress for his economic injury and is no longer interested in pursuing the IBCFP complaint. Without the client complaint, there is little chance of substantiating these allegations.

Anonymous Case History #6:

Client complained that CFP Respondent recommended and placed the client in inappropriate investments in the form of an insurance policy as an investment vehicle when that insurance policy accounted for 80% of the client's resources and left the client in a severe short cash position. Additionally, the client stated that the CFP Respondent was engaged to supply the client with "future value" computations to support the client's claim for a workman's compensation award, resulting from the death of the client's spouse. The client stated that the CFP Respondent failed to appear and/or cancelled all five (5) scheduled meetings with the client's attorney and ultimately failed to appear at the meetings negotiating the workman's compensation settlement.

Code of Ethics: Sections II (A) and III (A)

Aggravation: CFP Respondent failed to show that the investments he recommended for the client were justifiable, especially regarding new tax laws which effected the insurance policies. Additionally, the CFP Respondent was unable to justify his failing to appear and/or cancelling the scheduled workman's compensation settlement meetings.

Three year suspension.

CASE STUDIES OF HARM ACROSS THE UNITED STATES

Aside from the foregoing cases of financial planner abuse which have been documented in Colorado, the North American Securities Administrators Association has released a report entitled The NASSA Survey of Fraud and Abuse in the Financial Planning Industry. Numbers of cases of consumer harm from the 30 states surveyed are highlighted. This survey of recent state enforcement actions shows a significant increase in the activities of state regulators in pursuing violators of state securities laws. According to NASSA, investor losses from illegal activity amount to some $400,000,000 as of July, 1990. The NASSA report shows that the cases of abuse in the financial planning industry that have occurred in Colorado are not uncommon across the country.

STRUCTURE OF REGULATORY PROPOSAL

In order to respond to the numerous incidents of abuse in the financial planning industry, the applicants propose that Colorado adopt the Colorado Investment Advisers Act (Appendix A). The proposed Act has been written with dual objectives. First, the proposal would allow the Colorado Securities Commissioner to track investment advisers and their representatives doing business in Colorado and to regulate them through a strengthened system of civil and criminal penalties. Second, the proposal would coordinate Colorado's law in this area with the federal Investment Advisers Act of 1940 and similar laws which have been adopted in 43 other states. It is generally agreed that the Securities and Exchange Commission cannot effectively regulate this profession without the active and coordinated assistance of the several states. In this way, Colorado would be empowered to track investment advisers and their activities, provide information to consumers and coordinate enforcement with the SEC. In addition, the law would include a new disclosure requirement which would give investors better information to use in selecting an investment adviser. With these goals in mind, the following is a summary of the proposal.

SUMMARY OF PROPOSAL

INVESTMENT ADVISERS REGISTERED UNDER THE FEDERAL INVESTMENT ADVISERS ACT OF 1940.

Note: These persons are often called "money managers". They generally serve institutions and wealthier individuals. Many of these persons require that their clients generally be "accredited investors", a term common in securities law which connotes persons of a high level of wealth or financial sophistication requiring less regulatory protection.

1. Require a Colorado license for firms. Application would be based on the federal securities Form ADV which is already required to be filed with the SEC by this group. Applications would also include a consent to service of process. State would collect an annual fee to fund Division of Securities.

2. Require Colorado license for individuals who provide investment advisory services directly to firm's clients. Each individual would file an application, together with a consent to service of process and pay an annual fee. Individuals with specified experience would be excused from the examination requirement, while those without experience would be required to pass a standardized examination. Several possible national examinations for this purpose exist or are being prepared (e.g. NASD Examination for Brokers, Series 65).

3. Require record keeping only as required under federal act.

4. Require no disclosures to clients beyond those already required by the federal act (Form ADV, Part 2), provided that clients are "accredited investors". Accredited investors are generally institutional investors with more than $5 million in assets, or individuals earning more than $200,000 per year or having a net worth in excess of $1 million.

ALL OTHER INVESTMENT ADVISERS - FINANCIAL PLANNERS

5. Apply Items 1 through 4 above.

6. Require individuals who apply for licenses as investment adviser representatives to pass standard examination, assuming they lack specified experience.

7. Require disclosure, on form to be prescribed by Securities Commissioner, to existing and prospective clients who do not meet client criteria mentioned in No. 4 above. Such disclosures would include (a) qualifications, (b) method of compensation, and (c) if required by the Commissioner, information about past violations of the securities laws.

8. Require disclosure of conflicts of interest as now required for federal act registrants.

ENFORCEMENT PROVISIONS (APPLICABLE TO ALL)

9. Authorize Securities Commissioner to conduct inspections and investigations, to deny, suspend or revoke licenses for specific violations and to file court enforcement actions.

10. Provide for private remedies, civil and criminal penalties against firms and individuals for fraud, failure to make required disclosures to clients, or failure to comply with licensing requirements.

Exemptions from regulation:

The term "Investment Adviser" does not include:

(a) A depository institution;

(b) A lawyer, accountant, engineer, or teacher whose providing of investment advisory services is solely incidental to the practice of such person's profession;

(c) A broker-dealer whose providing of investment advisory services is solely incidental to the conduct of such person's business as broker-dealer and who receives no special compensation for such services;

(d) A publisher of any bona fide newspaper, news magazine, or business or financial publication with a regular and paid circulation; a publisher of any securities advisory newsletter with a regular and paid circulation which does not provide advice to subscribers on their specific investment situations; or any author of material included in any such newspaper, magazine, publication, or newsletter who does not otherwise come within the definition of investment adviser;

(e) A person who provides investment advisory services solely while acting as an investment banker or business broker on behalf of one or more of the parties to, and in connection with, a transaction or proposed transaction for the transfer of a controlling interest in a business enterprise; or

(f) Any other person or class of persons the securities commissioner designates by rule or order.

CONCLUSION

The applicants have met the burden set out in the sunrise statute which requires a clear showing of harm to the public as a result of the unregulated practice of the profession in question. Further, a well established and effective mechanism for regulation already exists in the Colorado Division of Securities. The public can be expected to realize a significant level of protection from the efforts of the Securities Commissioner and his staff, who are already engaged in prosecuting Colorado securities violations. Finally, the imposition of registration and testing requirements is not a burden which is unfamiliar to the profession.

The rise of consolidated financial service firms in the United States is a relatively new phenomenon which offers many benefits to consumers. At the same time, government needs to keep pace with these developments by reviewing and adjusting the laws which regulate such activity. The proposed Colorado Investment Advisers Act would significantly strengthen the laws protecting Colorado consumers who utilize the services offered by investment advisers and financial planners.

APPENDIX A

COLORADO INVESTMENT ADVISERS ACT (Proposed)

COLORADO INVESTMENT ADVISERS ACT (Proposed)
(May 15, 1991)

THE PROPOSED COLORADO INVESTMENT ADVISERS ACT HAS BEEN PREPARED BY THE COLORADO SECURITIES LAW REVIEW COMMITTEE OF THE COLORADO BAR ASSOCIATION. THE COMMITTEE IS SUBMITTING THE PROPOSED ACT TO THE COLORADO BAR ASSOCIATION FOR CONSIDERATION. **THE COLORADO BAR ASSOCIATION HAS TAKEN NO ACTION WITH RESPECT TO THE PROPOSED ACT AND THUS NEITHER SUPPORTS NOR ENDORSES THE PROPOSED ACT.**

SUMMARY

The proposed Colorado Investment Advisers Act (the "Act") is based upon the Uniform Securities Act (1985) with 1988 amendments but contains various modifications. A similar approach was followed for the Colorado Securities Act of 1990. The Act would be administered by the Colorado Securities Commissioner.

The Act concerns investment advisers, who are defined in substantially the same manner as in the federal Investment Advisers Act of 1940. The definition refers to a person who for compensation engages in the business of advising others as to securities. The definition includes a financial planner who provides investment advisory services to others for compensation and as part of a regular business or who is held out as providing investment advisory services to others for compensation. Investment adviser does not include a lawyer or accountant who provides investment advisory services solely incidental to the person's practice; the definition also excludes a broker-dealer or its sales representative who provides advisory services solely incidental to the person's business and receives no special compensation for such services.

Under the Act, an investment adviser and its representative who provide services in Colorado would be required to be licensed by the Commissioner. Investment advisers exempt from the licensing requirement include any person who deals solely with broker-dealers or with financial or institutional investors, as well as any out-of-state adviser whose business during any twelve consecutive months is with not more than five persons in Colorado.

The Act would authorize the Commissioner to require an examination of an individual who applies for a license as an investment adviser representative. In addition to other possible exemptions by rule of the Commissioner, the Act authorizes an exemption from examinations for individuals who are associated with nationally recognized, non-profit organizations that maintain suitable standards.

A key element of the Act is mandated disclosures for clients. All clients must be furnished the same type of information which is required under the federal Investment Advisers Act of 1940. In addition, the Colorado Act would require specific, simplified disclosures to consumer clients with regard to (a) any monetary or other compensation derived directly or indirectly as a result of a transaction, (b) the education and background of the investment adviser representative and (c) (if the Commissioner requires disclosure as a condition of a license) orders, violations or other grounds which would have allowed the Commissioner to deny, suspend or revoke a license. Consumer clients are all persons other than accredited investors. (Accredited investors are generally institutional investors, pension plans with more than $5 million in assets, and individuals with a net worth of more than $1 million or income of more than $200,000 per year.) The Act thus addresses for consumer clients a particular concern with the conflict of interest which exists when an adviser or planner receives selling commissions or similar compensation for recommended transactions in securities.

In order to enforce the Act, the Colorado Securities Commissioner would have investigative authority and may seek injunctions, in a manner following the Colorado Securities Act. The Act would also create private remedies for licensing violations and untrue or misleading statements in connection with the solicitation of business from prospective or existing clients.

COLORADO INVESTMENT ADVISERS ACT (PROPOSED)

It is proposed that a new Article [#] of Title 11, Colorado Revised Statutes, be enacted to read as follows:

Article [#]--Investment Advisers

Part 1
Short Title, Purpose, and Scope

11-[#]-101. Short title and purpose. (1) This article shall be known and may be cited as the "Colorado Investment Advisers Act".

(2) The purposes of this article are to protect clients who use investment advisory services and maintain public confidence in investment advisers while avoiding unreasonable burdens on investment advisers and their representatives. This article is remedial in nature and is to be broadly construed to effectuate its purposes.

(3) The provisions of this article and rules made under this article shall be coordinated with the federal acts and statutes to which references are made in this article and rules and regulations promulgated under those federal acts and statutes, to the extent coordination is consistent with both the purposes and the provisions of this article.

11-[#]-102. Scope of article. (1) Sections 11-[#]-301, 11-[#]-308, 11-[#]-401, and 11-51-403 apply to persons who provide investment advisory services in this state.

(2) For the purpose of this section, a person provides investment advisory services in this state, whether or not such person is then present in this state, when the person providing the investment advisory services resides in this state or the person receiving the investment advisory services resides or is present in this state. A person providing investment advisory services is deemed to reside in this state if such person maintains a place of business [or a principal residence] in this state.

Part 2
Definitions

11-[#]-201. Definitions. As used in this article, unless the context otherwise requires:

(1) "Bank" shall have the same meaning as provided in section 11-51-201(1), C.R.S.

(2) "Broker-dealer" shall have the same meaning as provided in section 11-51-201(2), C.R.S.

(3) "Commodity futures trading commission" shall have the same meaning as provided in section 11-51-201(4), C.R.S.

(4) "Consumer client" means any person who is a client or prospective client of an investment adviser for investment advisory services other than a person who is, or who the investment adviser reasonably believes to be, an accredited investor as such term is defined in section 2(15) of the federal "Securities Act of 1933" and regulations thereunder.

(5) "Depository institution" shall have the same meaning as provided in section 11-51-201(5), C.R.S.

(6) "Financial or institutional investor" shall have the same meaning as provided in section 11-51-201(6), C.R.S.

(7) "Fraud", "deceit", and "defraud" are not limited to common-law deceit.

(8) "Fraudulent conduct" means, for the purposes of section 11-[#]-311, conduct within this state which constitutes a willful violation of section 11-[#]-401 or section 11-51-501, C.R.S., or conduct outside this state which would constitute a willful violation of section 11-[#]-401 or section 11-51-501, C.R.S., if it had occurred within this state.

(9) "Investment adviser" means any person who, for compensation, engages in the business of advising others, either directly or through publications, writings or electronic means, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as a part of a regular business, issues or promulgates analyses or reports concerning securities. "Investment adviser" includes a financial planner or other person who, as an integral component of other financially related services, provides investment advisory services to others for compensation and as a part of a regular business or who is held out as providing investment advisory services to others for compensation. "Investment adviser" does not include:

(a) An investment adviser representative;

(b) A depository institution;

(c) A lawyer, accountant, engineer, or teacher whose providing of investment advisory services is solely incidental to the practice of such person's profession;

(d) A broker-dealer or sales representative whose providing of investment advisory services is solely incidental to the conduct of such person's business as a broker-dealer or sales representative and who receives no special compensation for such services;

(e) A publisher of any bona fide newspaper, magazine, or business or financial publication with a regular and paid circulation; a publisher of any securities advisory newsletter with a regular and paid circulation which does not provide advice to subscribers on their

specific investment situations; or any author of material included in any such newspaper, magazine, publication, or newsletter who does not otherwise come within the definition of investment adviser;

(f) - A person who provides investment advisory services solely while acting as an investment banker or business broker on behalf of one or more of the parties to, and in connection with, a transaction or proposed transaction for the transfer of a controlling interest in a business enterprise; or

(g) Any other person or class of persons the securities commissioner designates by rule or order.

(10) "Investment adviser representative" means any individual who is a partner, officer, or director of an investment adviser, who occupies a similar status with or performs similar functions for an investment adviser, or who is employed by or otherwise associated with an investment adviser and, in each case, who provides investment advisory services directly to clients on behalf of the investment adviser. "Investment adviser representative" does not include a sales representative whose providing of investment advisory services is solely incidental to the conduct of such person's business as a sales representative and who receives no special compensation for such services.

(11) "Investment advisory services" means the providing of advice, either directly or through publications, writings, or electronic means, as to the value of securities or the advisability of investing in, purchasing, or selling securities or, as a part of a regular business, issuing or promulgating analyses or reports concerning securities.

(12) "Issuer" shall have the same meaning as provided in section 11-51-201(10), C.R.S.

(13) "Person" [shall have the same meaning as provided in section 11-51-201(12), C.R.S.] means an individual, a corporation, a partnership, an association, an estate, a joint-stock company, a trust [where the interests of the beneficiaries are evidenced by a security], an unincorporated organization, a government, a governmental subdivision or agency, or any other legal entity.

(14) "Sales representative" shall have the same meaning as provided in section 11-51-201(14), C.R.S.

(15) "Securities and exchange commission" shall have the same meaning as provided in section 11-51-201(15), C.R.S.

(16) "Securities commissioner" means the commissioner of securities appointed pursuant to section 11-51-701, C.R.S.

(17) "Security" shall have the same meaning as provided in section 11-51-201(17), C.R.S.

(18) "State" means any state, territory, or possession of the United States, the District of Columbia, or Puerto Rico.

11-[#]-202. References to federal statutes. (1) Each reference in this article, either explicitly or by cross-reference to another section of the Colorado Revised Statutes, to a federal act or statute means, unless the context otherwise requires, that act or statute as in effect on **[a chosen date preceding the introduction of this bill]**, together with all rules and regulations under such act or statute as in effect on that date, except as subsequent amendments may become applicable under this article pursuant to subsection (2) of this section.

(2) (a) Whenever an amendment to any federal act or statute to which reference is made in this article is enacted with an effective date on or after **[the date inserted in subsection (1)]**, or whenever an amendment to any rule or regulation under any such federal act or statute is promulgated with an effective date on or after such date, the securities commissioner shall determine whether giving effect to such amendment is inconsistent with the purposes of this article set forth in section 11-[#]-101(2), any other provision of this article, or any rule under this article. If the securities commissioner determines that an inconsistency exists, the securities commissioner shall commence rulemaking proceedings for the purpose of making, amending, or rescinding such rules under this article as may be appropriate to carry out the policy stated in section 11-[#]-101(3). If no rulemaking proceeding with respect to such amendment is commenced within ninety days after the effective date of such amendment (or within ninety days after the effective date of this article as set forth in section 11-[#]-701, if later), such amendment shall apply to this article and the rules under this article. If a rulemaking proceeding with respect to such amendment is commenced within ninety days after the effective date of such amendment (or within ninety days after the effective date of this article as set forth in section 11-[#]-701, if later), such amendment shall not apply to this article or any rule under this article except as may be provided by rule upon completion of such rulemaking proceeding.

(b) No provision of this article imposing any liability upon a person or providing a basis for any sanction against a person applies to any act done or omitted by such person in good faith and in conformity with the provisions of this article and the rules under this article, as in effect prior to the effective date of any amendment to any federal act or statute to which reference is made in this article or any amendment to any rule or regulation under any such federal act or statute, during the period commencing upon the effective date of such amendment and ending on the date determined by the following:

(I) If no rulemaking proceeding with respect to such amendment is commenced under this subsection (2) within ninety days after its effective date (or within ninety days after the effective date of this article as set forth in section 11-[#]-701, if later), ending on the ninetieth day after such effective date; or

(II) If such a rulemaking proceeding is commenced within such period of ninety days, ending upon completion of such rulemaking proceeding.

Part 3
Licensing and Regulation of Investment Advisers and Investment Adviser Representatives

11-[#]-301. Licensing requirements. (1) A person shall not transact business in this state as an investment adviser or investment adviser representative unless licensed or exempt from licensing under section 11-[#]-302.

(2) An investment adviser shall not employ or otherwise engage an individual to act as an investment adviser representative in this state unless the investment adviser representative is licensed or exempt from licensing under section 11-[#]-302.

(3) An investment adviser shall not employ or otherwise engage a person to participate in any activity in this state contrary to an order by the securities commissioner applicable to that person under section 11-[#]-311. An investment adviser does not violate this subsection (3) if the investment adviser sustains the burden of proof that it did not know and in the exercise of reasonable care could not have known of the order. Upon request from an investment adviser and for good cause shown, the securities commissioner may waive the prohibition of this subsection (3) with respect to a person subject to an order under section 11-[#]-311.

11-[#]-302. Exempt investment advisers and investment adviser representatives. (1) The following investment advisers are exempt from the license requirement of section 11-[#]-301(1):

(a) An investment adviser whose business in this state as an investment adviser is exclusively with the following:

(I) Other investment advisers;

(II) Broker-dealers;

(III) Financial or institutional investors;

(IV) Individuals who are existing clients of the investment adviser and whose principal places of residence are not in this state, if the investment adviser is registered as an investment adviser under the federal "Investment Advisers Act of 1940" and has no place of business in this state; and

(V) During any twelve consecutive months, not more than five persons in this state, excluding persons described in subparagraphs (I) through (IV) of this paragraph (a), provided that the investment adviser has no place of business in this state, and

(b) Other investment advisers the securities commissioner by rule or order exempts.

(2) The following investment adviser representatives are exempt from the license requirement of section 11-[#]-301(1):

(a) An investment adviser representative acting only on behalf of investment advisers exempt under subsection (1) of this section; and

(b) Other investment adviser representatives the securities commissioner by rule or order exempts.

11-[#]-303. Application for license. (1) An applicant for a license as an investment adviser or investment adviser representative shall file with the securities commissioner an application for a license and the consent to service of process required by section 11-[#]-605. The application must contain the information and be in the form the securities commissioner by rule requires. If the information contained in an application is inaccurate or incomplete in any material respect when the application is filed or becomes inaccurate or incomplete in any material respect as a result of any subsequent event, the applicant shall promptly file an amendment to the application to cure the inaccuracy or omission. The securities commissioner may require an applicant to submit additional information which is material to an understanding of information about the applicant available to the securities commissioner in the application or otherwise and an application shall be incomplete until all additional information required by the securities commissioner has been submitted.

(2) The application requirements of subsection (1) of this section are satisfied by an applicant for a license as an investment adviser who has filed and maintains complete and current registration information with the securities and exchange commission pursuant to the federal "Investment Advisers Act of 1940", or with a self-regulatory organization registered with the securities and exchange commission under a federal statute dealing with the regulation of investment advisers, if the same information is filed with the securities commissioner and the consent to service of process required by section 11-[#]-605 is provided to the securities commissioner. Any additional information the securities commissioner may require pursuant to subsection (1) of this section from such an investment adviser must be material to an understanding of the information about the investment adviser filed and maintained with the securities and exchange commission or with such a self-regulatory organization.

11-[#]-304. License fees. (1) An applicant for a license as an investment adviser or investment adviser representative shall pay an initial fee and a licensed person shall pay an annual license fee which shall be determined and collected pursuant to section 11-[#]-606.

(2) If an initial license fee is not paid within ninety days after the application is filed, the securities commissioner may deem the application to be withdrawn.

(3) (a) If an annual license fee is not paid within thirty days after the securities commissioner sends a written notice that the fee was not paid when due, the amount of the annual license fee will be double the amount originally payable. In the case of an investment adviser representative, written notice will be deemed sent to the investment adviser representative when the notice is sent to an investment adviser for whom the investment adviser representative is licensed to act.

(b) If an annual license fee is not paid within sixty days after the securities commissioner sends the written notice described in paragraph (a) of this subsection (3), the securities commissioner may by order summarily suspend the license. The securities commissioner shall send a copy of the order to the investment adviser whose license has been summarily suspended, or, in the case of an investment adviser representative whose license has been summarily suspended, to an investment adviser for whom the investment adviser representative has been licensed to act. If the annual license fee is not paid within thirty days after the effective date of the summary suspension, the securities commissioner may by order summarily revoke the license on the grounds that the license has been abandoned.

(4) If an application is denied or withdrawn, or a license is abandoned, revoked, suspended, or withdrawn, the securities commissioner shall retain all fees paid.

11-[#]-305. Examinations. (1) Except as provided in subsection (2) of this section, the securities commissioner may by rule require a written examination of an individual who applies for a license as an investment adviser representative or, in the case of a sole proprietor, as an investment adviser to determine whether the applicant has a satisfactory level of knowledge about federal and state securities laws applicable to investment advisers and investment adviser representatives. Any examination may be administered by the securities commissioner or any person the securities commissioner may designate. The securities commissioner may by rule exempt designated classes of individuals from any written examination requirement.

(2) No examination shall be required of any individual who is a member in good standing of, is certified by, or is otherwise associated with an organization as the securities commissioner may determine by rule. Any such determination must be based upon findings of fact that such organization is nationally recognized, is not operated for profit, and maintains satisfactory standards and procedures to assure that each such individual has a satisfactory level of knowledge about federal and state securities laws applicable to investment advisers and investment adviser representatives.

11-[#]-306. General provisions. (1) (a) Unless a proceeding under section 11-[#]-311 is instituted the license of an investment adviser or investment adviser representative becomes effective upon the last to occur of the following:

(I) The passage of thirty days after the filing of the application or, if any amendment is filed before the license becomes effective, the passage of thirty days after the filing of the latest amendment, provided that the application, including all amendments, if any, was complete at the commencement of the thirty day period;

(II) The examination requirement under section 11-[#]-305 is satisfied;

(III) In the case of an investment adviser, the requirements of section 11-[#]-307(4) are satisfied; and

(IV) The required fee has been paid.

(b) The securities commissioner may authorize an earlier effective date of licensing.

(2) The securities commissioner may, by rule or order, waive or reduce any of the requirements of this section and sections 11-[#]-305 and 11-[#]-307 with respect to any person or class of persons and, in connection with the waiver or reduction of any requirement, may limit or impose conditions on the investment advisory services that such person or class of persons may provide in this state.

(3) The license of an investment adviser representative is effective only with respect to actions taken for an investment adviser for whom the investment adviser representative is licensed to act.

(4) A person may not act at any one time as an investment adviser representative for more than one investment adviser, unless the investment advisers for whom the investment adviser representative acts are affiliated by direct or indirect common control or the securities commissioner by rule or by order authorizes such person to act for more than one investment adviser.

(5) If a licensed investment adviser representative ceases to be employed or otherwise engaged by an investment adviser or ceases to act as an investment adviser representative, the investment adviser for whom such investment adviser representative is licensed to act shall promptly notify the securities commissioner.

(6) The license of an investment adviser or investment adviser representative is effective until terminated by revocation or withdrawal.

11-[#]-307. Operating requirements. (1) The securities commissioner may by rule require licensed investment advisers who are not registered under the federal "Investment Advisers Act of 1940" to make and maintain specified records and to preserve such records for five years or such other period as may be specified.

(2) The securities commissioner may by rule require licensed investment advisers who are registered under the federal "Investment Advisers Act of 1940" to make, maintain, and preserve specified records, but no rule made by the securities commissioner under this subsection (2) shall require any investment adviser to make, maintain, or preserve any records other than the following:

(a) Records required to be made, maintained, and preserved under the federal "Investment Advisers Act of 1940"; and

(b) Records required to show compliance by the investment adviser with the requirement, to the extent applicable, of section 11-[#]-308.

(3) Every licensed investment adviser and every licensed investment adviser representative shall file with the securities commissioner such information as may be necessary to correct any information in its application for license which is or has become inaccurate in any material respect. The requirements of this subsection (3) may be satisfied by an investment adviser who is registered as an investment adviser under the federal "Investment Advisers Act of 1940" by filing with the securities commissioner all of the information the investment adviser is required to file with the securities and exchange commission in connection with such registration.

(4) Every licensed investment adviser shall at all times have in its employment one or more individuals who have passed the written examination required under section 11-[#]-305(1), who are exempt from any written examination requirement pursuant to section 11[#]-305(2), or for whom the written examination requirement has been waived by the securities commissioner.

(5) If an investment adviser at any time knows, or has reason to know, that it is not in compliance with any provision of this section or any rule made by the securities commissioner under this section, the investment adviser shall promptly notify the securities commissioner of all relevant facts.

11-[#]-308. Mandatory disclosure. (1) (a) Every investment adviser who is licensed or required to be licensed under this article shall furnish each client who receives investment advisory services and each prospective client with a written disclosure statement which contains such information from the application (including any amendments) of the investment adviser required to be filed pursuant to section 11-[#]-303 and from the filings required to be made by the investment adviser pursuant to section 11-[#]-307(3) as the securities commissioner may by rule specify, provided that the information required by any such rule shall be about the same matters and in no greater detail than the information that investment advisers who are registered under the federal "Investment Advisers Act of 1940" are required to disclose or offer to disclose in writing to their clients.

(b) An investment adviser shall deliver the disclosure statement required by this subsection (1) to a client or prospective client at such time prior to entering into any contract

with the client or prospective client for investment advisory services, and in such manner, as the securities commissioner may by rule specify. An investment adviser shall also annually, without charge, deliver or offer in writing to deliver upon written request to each of its clients for investment advisory services the disclosure statement required by this subsection (1), in such manner as the securities commissioner may by rule specify.

(c) In the case of an investment adviser registered under the federal "Investment Advisers Act of 1940," the requirements for delivery of or an offer to deliver a disclosure statement under this subsection (1) are satisfied by the delivery of or offer to deliver a written disclosure statement to the client or prospective client in compliance with the federal "Investment Advisers Act of 1940" and the regulations of the securities and exchange commission thereunder.

(2) (a) In addition to the disclosure statement required by subsection (1) of this section, each investment adviser who is licensed or required to be licensed under this article shall furnish each consumer client a written disclosure statement which shall contain the following:

(I) In regard to each transaction in securities, the source and amount, or method of determining the amount, of all monetary and other compensation which the investment adviser or any investment adviser representative of the investment adviser reasonably expects to derive, directly or indirectly, as a result of the transaction;

(II) Such information concerning the education and background of each investment adviser representative who will provide investment advisory services to the consumer client as the securities commissioner may by rule specify; and

(III) Any finding of the securities commissioner required to be disclosed in accordance with section 11-[#]-311(2).

(b) Each disclosure statement required by subparagraph (a)(I) of this subsection (2) shall be delivered to the consumer client prior to the incurrence by the consumer client of any obligation in the transaction. The disclosure statements required by subparagraphs (a)(II) and (a)(III) of this subsection (2) shall be furnished to the consumer client at the same times as the disclosure statements required by subsection (1) of this section. In the case of any monetary or other compensation which is not contingent upon completion of a transaction (such as a fixed amount fee) or which is uniformly applied to any class of transactions (such as a fixed percentage fee), an investment adviser may satisfy the requirements of subparagraph (a)(I) of this subsection (2) by including such required disclosure in the disclosure statements required by subsection (1) of this section. Any disclosure statement required by this subsection (2) may be combined with a disclosure statement required by subsection (1) of this section if the requirements of this subsection (2) are satisfied.

(c) The duty to deliver a disclosure statement required by subparagraph (a)(I) of this subsection (2) shall not apply to:

(I) Any transaction in a security described in section 11-51-307(1)(f), C.R.S. if the investment adviser is also acting as a broker-dealer or a sales representative of a broker-dealer and the consumer client pays no more than the usual and customary broker's commission; or

(II) Any transaction in a security issued by an investment company registered under the federal "Investment Company Act of 1940" if the investment adviser, as a broker-dealer, sales representative or otherwise, receives no more than the compensation described in the current prospectus of the investment company filed under the federal "Securities Act of 1933".

(3) The securities commissioner may by rule allow the omission of any information otherwise required to be contained in a disclosure statement under subsection (1) or (2) of this section. The securities commissioner may by rule exempt any class of investment advisers from the requirements, in whole or in part, of subsection (1) or (2) of this section.

(4) Insofar as this section or any rule made under this section requires disclosure, the rules made and forms prescribed by the securities commissioner, when such rules and forms apply to investment advisers registered under the federal "Investment Advisers Act of 1940," shall be compatible with the requirements under the federal "Investment Advisers Act of 1940" in order to minimize any additional burden and expense of those investment advisers.

11-[#]-309. Licensing of successor firms. (1) A licensed investment adviser may file an application for a license on behalf of a successor, whether or not the successor is in existence. If an investment adviser succeeds to and continues the business of a licensed investment adviser and the successor files an application for a license within thirty days after the succession, the license of the predecessor remains effective as the license of the successor for sixty days after the succession. An application filed pursuant to this subsection (1) must satisfy all requirements of an application provided in this article.

(2) If a successor is licensed pursuant to subsection (1) of this section, the license of each investment adviser representative licensed to act for the predecessor shall remain effective as a license to act for the successor without a separate filing or payment of a separate fee.

11-[#]-310. Access to records. (1) The securities commissioner, in a manner reasonable under the circumstances, may examine, without notice, the records, within or without this state, of a licensed investment adviser which are required to be made and maintained pursuant to this article in order to determine compliance with this article. A licensed investment adviser may maintain such records in any form of data storage if the records are readily accessible to the securities commissioner in legible form.

(2) The securities commissioner, in a manner reasonable under the circumstances, may copy records required to be made and maintained under this article or require a licensed

investment adviser, at the expense of the investment adviser, to copy such records and provide copies to the securities commissioner.

(3) The securities commissioner, in a manner reasonable under the circumstances, may examine, without notice, the records, within or without this state, of a licensed investment adviser representative which are made and maintained by the investment adviser representative in the normal course of business in order to determine compliance with this article.

(4) The securities commissioner, in a manner reasonable under the circumstances, may copy records made and maintained by a licensed investment adviser representative in the normal course of business or require a licensed investment adviser representative, at the investment adviser representative's expense, to copy such records and provide copies to the securities commissioner.

11-[#]-311. Denial, suspension, or revocation. (1) The securities commissioner may by order deny an application for a license, suspend or revoke a license, censure a licensed person, limit or impose conditions on the investment advisory services that a licensed person may provide in this state, and bar a person from association with any licensed investment adviser in the conduct of its business in this state in such capacities and for such period as the order specifies. These sanctions may be imposed only if the securities commissioner makes a finding, in addition to the findings required by section 11-[#]-603(2), that the applicant or licensed person or, in the case of an investment adviser, a partner, officer, director, person occupying a similar status or performing similar functions, or person directly or indirectly controlling the investment adviser;

(a) Has filed an application for a license with the securities commissioner which, as of the effective date of the license or as of any date after filing in the case of an order denying effectiveness, was false or misleading as a result of an untrue statement of a material fact or an omission to state a material fact, unless the applicant sustains the burden of proof that the applicant did not know and in the exercise of reasonable care could not have known of the untruth or omission;

(b) Has willfully violated or willfully failed to comply with any provision of this article or any rule made or any order issued under this article, except any rule which is subject to the additional findings required by paragraph (h) of this subsection (1);

(c) Within the past ten years, has entered a plea of guilty or nolo contendere to, or has been convicted of, any felony, any misdemeanor involving a breach of fiduciary duty or fraud, or any misdemeanor in connection with a purchase or sale of a security or in connection with the providing of investment advisory services;

(d) Has been found in a final decree issued by a court of competent jurisdiction within the past five years, in an action instituted by the securities commissioner, the securities agency or administrator of another state or a Canadian province or territory, the securities

and exchange commission, or the commodity futures trading commission, to have violated any securities registration or any broker-dealer, investment adviser, or similar license requirement or to have engaged in fraudulent conduct;

(e) Is currently the subject of a temporary or permanent injunction issued by a court of competent jurisdiction within the past five years in an action instituted by the securities commissioner, the securities and exchange commission, or the commodity futures trading commission, which injunction was issued with the consent of such person;

(f) Is currently the subject of an order of the securities commissioner denying, suspending, or revoking the person's license as an investment adviser or investment adviser representative, or the person's license as a broker-dealer or sales representative under section 11-51-401 et. seq., C.R.S., or barring the person from association with any licensed investment adviser or with any broker-dealer licensed under section 11-51-401 et. seq., C.R.S.;

(g) Is currently the subject of any of the following orders issued within the past five years:

(I) An order by the securities agency or administrator of another state or a Canadian province or territory, entered after notice and opportunity for hearing and based upon fraudulent conduct, denying or revoking the person's license as an investment adviser, investment adviser representative, broker-dealer, sales representative, or the substantial equivalent of those terms, or suspending or barring the right of the person to be associated with an investment adviser or a broker-dealer; or

(II) An order by the securities and exchange commission, entered after notice and opportunity for hearing, denying, suspending, or revoking the person's registration as an investment adviser under the federal "Investment Advisers Act of 1940" or the person's registration as a broker-dealer under the federal "Securities Exchange Act of 1934" or suspending or barring the right of the person to be associated with an investment adviser or a broker-dealer;

(h) Has willfully engaged in a course of conduct involving the violation of one or more rules made by the securities commissioner which prohibit unfair and dishonest dealings by an investment adviser or investment adviser representative, including any rule that may be made to define conduct prohibited by section 11-[#]-401, provided that each such rule is based upon a finding, in addition to the findings required by section 11-51-603(2), which finding itself must be based on information provided by investment advisers and investment adviser representatives at a hearing on the proposed rule, that licensed investment advisers and investment adviser representatives who will be required to comply with the rule generally agree that the conduct prohibited by the rule does not meet prevailing standards of fair and honest dealing within the securities industry and that it is reasonable to expect the rule will prevent or deter such conduct;

(i) Is not in compliance with section 11-[#]-307(4);

(j) Has failed reasonably to supervise, with a view to preventing violations of this article, another person who is subject to the person's supervision and who commits such a violation, but for the purpose of this paragraph (j) no person shall be deemed to have failed to supervise another person if there existed established procedures, and a system for applying such procedures, which would reasonably be expected to prevent and detect, insofar as practicable, any such violation by such other person and such person reasonably discharged the duties and obligations incumbent upon such person by reason of such procedures and system without reasonable cause to believe that such procedures and system were not being complied with; or

(k) Has ceased to do business as an investment adviser or investment adviser representative.

(2) In any case where the securities commissioner makes a final finding entitling the securities commissioner to impose any sanction under subsection (1) of this section, the securities commissioner may, in addition to imposing any other conditions as provided in subsection (1), require that the licensed person, whether an investment adviser or an investment adviser representative, disclose to each consumer client either a summary or complete description of that finding, as the securities commissioner may order.

(3) The securities commissioner may not begin a proceeding under this section against any person more than ninety days after a license has been issued to that person on the basis of a fact or transaction which the person shows was known to the securities commissioner when the license was issued or when any prior license of the same class was issued to that person if such prior license was not revoked on the basis, in whole or in part, of such fact or transaction.

(4) For good cause shown the securities commissioner may waive or modify an order previously made under this section as it applies to any person with the consent of that person.

11-[#]-312. Abandonment of license. If a licensed person has died or ceased to exist as a legal entity, has been adjudicated incompetent, or cannot be located by the securities commissioner after a reasonable search, the securities commissioner may by order summarily revoke the license on the grounds that the license has been abandoned.

11-[#]-313. Withdrawal. (1) An application for a license may be withdrawn without prejudice by the applicant upon written notice to the securities commissioner before the license becomes effective unless a proceeding under section 11-[#]-311 to deny the license is pending.

(2) Withdrawal from licensing as an investment adviser or investment adviser representative becomes effective thirty days after receipt by the securities commissioner of an

application to withdraw, or at such earlier time as the securities commissioner may allow, unless:

(a) A proceeding under section 11-[#]-311 against the licensed person is pending when the application is filed or is instituted within thirty days thereafter; or

(b) Additional information regarding the application is required by the securities commissioner within thirty days after the application is filed.

(3) If a proceeding is pending or instituted under subsection (2) of this section, withdrawal becomes effective at the time and upon the conditions the securities commissioner by order determines. If additional information is requested, withdrawal is effective thirty days after the additional information is received by the securities commissioner. If no proceeding is pending or instituted under subsection (2) of this section and withdrawal becomes effective, the securities commissioner may institute a proceeding under section 11-[#]-311 within one year after withdrawal became effective and enter an order as of the last date on which licensing was effective.

Part 4
Fraud and Other Prohibited Conduct

11-[#]-401. Fraud and other prohibited conduct. (1) It is unlawful for any investment adviser or investment adviser representative, directly or indirectly;

(a) To employ any device, scheme, or artifice to defraud any client or prospective client;

(b) In any disclosure statement delivered to any client or prospective client as required by section 11-[#]-308, to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading; or

(c) To engage in any transaction, act, practice, or course of business which operates or would operate as a fraud or deceit upon any client or prospective client or which is fraudulent, deceptive, or manipulative.

(2) It is unlawful for any investment adviser or investment adviser representative who is licensed or required to be licensed under this article, acting as principal for such investment adviser's or investment adviser representative's own account, knowingly to sell any security to a client or purchase any security from a client, or acting on behalf of a person other than such client knowingly to effect any sale or purchase of any security for the account of such client, without disclosing to such client in writing, before the completion of such transaction, the capacity in which such investment adviser or investment adviser representative is acting and without obtaining the consent of the client to such transaction.

The prohibitions of this subsection (2) shall not apply to any transaction with a customer of a broker-dealer if such broker-dealer is not acting as an investment adviser in relation to such transaction.

(3) (a) Except as provided in paragraph (b) of this subsection (3), it is unlawful for any investment adviser who is licensed or required to be licensed under this article and who has custody or possession of any funds or securities in which any client of such investment adviser has any beneficial interest to do any act or take any action, directly or indirectly, with respect to any such funds or securities, unless:

(I) All such securities of each client are segregated, marked to identify the particular client who has the beneficial interest therein, and held in safekeeping in some place reasonably free from risk of destruction or other loss;

(II) (A) All such funds of clients are deposited in one or more bank accounts which contain only clients' funds;

(B) Each such account is maintained in the name of the investment adviser as agent or trustee for such clients; and

(C) The investment adviser maintains a separate record for each such account which shows the name and address of the bank where such account is maintained, the dates and amounts of deposits in and withdrawals from such account, and the exact amount of each client's beneficial interest in such account;

(III) The investment adviser, immediately after accepting custody or possession of such funds or securities from any client, notifies the client in writing of the place and manner in which such funds and securities will be maintained, and thereafter, if and when there is any change in the place or manner in which such funds or securities are being maintained, gives the client written notice of the change;

(IV) The investment adviser sends to each client, not less frequently than once every three months, an itemized statement showing the funds and securities in the custody or possession of the investment adviser at the end of such period, and all debits, credits and transactions in such client's account during such period; and

(V) All such funds and securities of clients are verified by actual examination at least once during each calendar year by an independent public accountant at a time chosen by such accountant without prior notice to the investment adviser. A certificate of such accountant stating that an examination of such funds and securities has been made, and describing the nature and extent of the examination, shall be filed with the securities commissioner promptly after each examination.

(b) Paragraph (a) of this subsection (3) does not apply to any investment adviser who:

(I) Is registered as an investment adviser under the federal "Investment Advisers Act of 1940" and is in compliance with the requirements under that act, including rules made by the securities and exchange commission under that act, relating to the safekeeping of funds and securities of clients; or

(II) Is registered as a broker-dealer under the federal "Securities Exchange Act of 1934" and either:

(A) Is subject to and in compliance with the requirements under that act, including rules made by the securities and exchange commission under that act, relating to the financial responsibility and related practices of broker-dealers who have custody or possession of funds or securities of customers; or

(B) Is a member of a national securities exchange whose members are exempt from the requirements described in sub-subparagraph (A) of this paragraph (II) and is subject to and in compliance with the rules and settled practices of such exchange with respect to the financial responsibility and related practices of members who have custody or possession of funds or securities of customers.

(4) Nothing in this section shall relieve any investment adviser or any investment adviser representative of any liability under section 11-51-501, C.R.S., or any other law.

11-[#]-402. Misleading filings. It is unlawful for any investment adviser or any investment adviser representative to make or cause to be made, in any document filed with the securities commissioner or in any proceeding under this article, any statement which such investment adviser or investment adviser representative knows or has reasonable grounds to know is, at the time and in the light of the circumstances under which it is made, false or misleading in any material respect.

11-[#]-403. Unlawful representation concerning a license or exemption. (1) Neither the fact that an application for a license has been filed nor the fact that a person is effectively licensed constitutes a finding by the securities commissioner that any document filed under this article is true, complete, and not misleading. No such fact, nor the fact that an exemption or exception is available for an investment adviser or an investment adviser representative, means that the securities commissioner has passed in any way upon the merits or qualifications of, or has recommended or given approval to, any investment adviser or investment adviser representative.

(2) It is unlawful to make, or cause to be made, to any existing or prospective client any representation inconsistent with subsection (1) of this section.

Part 5
Enforcement and Civil Liability

11-[#]-501. Investigations and subpoenas. (1) The securities commissioner may make such public or private investigations within or outside of this state as the securities commissioner deems necessary to determine whether any person has violated or is about to violate any provision of this article or any rule or order under this article or to aid in the enforcement of this article or in the prescribing of rules and forms under this article, may require or permit any person to file a statement as to all the facts and circumstances concerning the matter to be investigated, and may publish information concerning any violation of this article or any rule or order under this article.

(2) For the purpose of any investigation or proceeding under this article, the securities commissioner or any officer designated by the securities commissioner may administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence, and require the production of any books, papers, correspondence, memoranda, agreements, or other documents or records which the securities commissioner deems relevant or material to the inquiry.

(3) In case of contumacy by, or refusal to obey a subpoena issued to, any person, the district court of the city and county of Denver, upon application by the securities commissioner, may issue to the person an order requiring that person to appear before the securities commissioner, or the officer designated by the securities commissioner, to produce documentary evidence if so ordered or to give evidence touching the matter under investigation or in question. Failure to obey the order of the court may be punished by the court as a contempt of court.

(4) No person is excused from attending and testifying or from producing any document or record before the securities commissioner, or in obedience to the subpoena of the securities commissioner or any officer designated by the securities commissioner, or in any proceeding instituted by the securities commissioner on the ground that the testimony or evidence, documentary or otherwise, required of that person may tend to incriminate that person or subject that person to a penalty or forfeiture; but no document, evidence, or other information compelled under order of the district court of the city and county of Denver, or any information directly or indirectly derived from such document, evidence or other information, may be used against an individual so compelled in any criminal case; except that the individual testifying is not exempt from prosecution and punishment for perjury in the first or second degree or contempt committed in testifying.

(5) Information in the possession of, filed with, or obtained by the securities commissioner in connection with a private investigation under this section shall be confidential. No such information may be disclosed by the securities commissioner or any of the officers or employees of the division of securities except after authorization in writing by the securities commissioner or any designee of such commissioner that disclosure of information in the case is necessary or appropriate in connection with a particular investigation or proceeding under

this article or for any law enforcement purpose. The absence of written authorization pursuant to this subsection (5) shall not be proof of the lack of authorization in fact and shall not constitute grounds for the exclusion of any such information as evidence in any proceeding. No provision of this article either creates or derogates from any privilege which exists at common law or otherwise when documentary or other evidence is sought under a subpoena directed to the securities commissioner or any of the officers or employees of the division of securities.

11-[#]-502. Enforcement by injunction. (1) Whenever it appears to the securities commissioner upon sufficient evidence satisfactory to the securities commissioner that any person has engaged in or is about to engage in any act or practice constituting a violation of any provision of this article or of any rule or order under this article, the securities commissioner may apply to the district court of the city and county of Denver to temporarily restrain or preliminarily or permanently enjoin the act or practice in question and to enforce compliance with this article or any rule or order under this article. If the action is against an investment adviser or an investment adviser representative and the court finds that the investment adviser or investment adviser representative has committed a violation of section 11-[#]-401, in addition to any other relief the court may enter an order imposing such conditions on the investment adviser or investment adviser representative as the court deems appropriate. In any such action, the securities commissioner shall not be required to plead or prove irreparable injury or the inadequacy of the remedy at law. Under no circumstances shall the court require the securities commissioner to post a bond.

(2) The securities commissioner may include in any action authorized by subsection (1) of this section, relating to any violation of section 11-[#]-301, 11-[#]-308, or 11-[#]-401, a claim for damages under section 11-[#]-504 or restitution, disgorgement, or other equitable relief on behalf of some or all of the persons injured by the act or practice constituting the subject matter of the action, if the applicable scienter standard of section 11-[#]-504 is met.

11-[#]-503. Criminal penalties. (1) Any person who willfully violates the provisions of section 11-[#]-401(1) commits a class 3 felony and shall be punished as provided in section 18-1-105, C.R.S.

(2) Any person who willfully violates any of the provisions of this article, except section 11-515.-401(1), commits a class 6 felony and shall be punished as provided in section 18-1-105, C.R.S.

(3) The securities commissioner may refer such evidence as is available to the securities commissioner under authority of this article concerning any violation which constitutes the commission of any felony or misdemeanor, including any violation of subsection (1) or (2) of this section, to the attorney general or the proper district attorney, who may, with or without such a reference, prosecute the appropriate criminal proceedings under this article or otherwise as authorized by law, or the securities commissioner may refer such evidence to the proper United States attorney.

(4) Nothing in this article limits the power of the state to punish any person for any conduct which constitutes a crime by statute.

(5) No person shall be prosecuted, tried, or punished for any criminal violation of this article unless the indictment, information, complaint, or action for the same is found or instituted within five years after the commission of the offense.

11-[#]-504. Civil liabilities. (1) Any person who violates section 11-[#]-301(1) is liable to each person to whom investment advisory services are provided in violation of that section in an amount equal to the greater of:

(a) One thousand dollars; or

(b) The value of all benefits derived, directly or indirectly, by the person who commits the violation from the relationship or dealings with the other person prior to such time as the violation may be cured, together with interest at the statutory rate from the date of receipt, costs, and reasonable attorney fees.

(2) Any person who provides investment advisory services to another person but fails to furnish a disclosure statement required by section 11-[#]-308 to the other person, and any person who recklessly, knowingly or with an intent to defraud provides investment advisory services to another person in violation of section 11-[#]-401(1), is liable to such other person for such legal or equitable relief that the court deems appropriate, including rescission, the value of all benefits derived directly or indirectly by the person providing such investment advisory services, actual damages, interest at the statutory rate, costs, and reasonable attorney fees.

(3) Any person who violates section 11-[#]-401(2) or (3) is liable to each person to whom disclosures are not made or from whom consent is not obtained as required by section 11-[#]-401(2) or whose funds or securities are not maintained as required by section 11-[#]-401(3) in an amount equal to the greater of:

(a) Actual damages together with interest at the statutory rate, costs, and reasonable attorney fees; or

(b) The value of all benefits derived, directly or indirectly, by the person who commits the violation from the relationship or dealings with the other person, together with interest at the statutory rate from the date of receipt, costs, and reasonable attorney fees.

(4) (a) Every person who, directly or indirectly, controls a person liable under subsection (1), (2), or (3) of this section is liable jointly and severally with and to the same extent as such controlled person, unless the controlling person sustains the burden of proof that such person did not know, and in the exercise of reasonable care could not have known, of the existence of the facts by reason of which the liability is alleged to exist.

(b) Any person who knows that another person liable under subsection (2) of this section is engaged in conduct which constitutes a violation of section 11-[#]-401(1) and who gives substantial assistance to such conduct is jointly and severally liable to the same extent as such other person.

(5) Every cause of action under this article survives the death of any individual who might have been a plaintiff or defendant.

(6) No person may sue under subsection (1) of this section, or under subsection (4) of this section as it relates to subsection (1), more than two years after the violation. No person may sue under subsection (2) or (3) of this section, or under subsection (4) as it relates to subsection (2) or (3), more than three years after the discovery of the facts giving rise to a cause of action under subsection (2), (3) or (4) of this section or after such discovery should have been made by the exercise of reasonable diligence and in no event more than five years after the violation.

(7) No person who has made or engaged in the performance of any contract in violation of any provision of this article or any rule or order under this article or who has acquired any purported right under any such contract with knowledge of the facts by reason of which its making or performance was in violation may base any suit on the contract.

(8) Any condition, stipulation, or provision binding any person who is provided investment advisory services to waive compliance with any provision of this article or any rule or order under this article is void.

(9) The rights and remedies provided by this article may be pleaded and proved in the alternative and are in addition to any other rights or remedies that may exist at law or in equity, but this article does not create any cause of action not specified in this section or section 11-[#]-502.

(10) Any person liable under this section may seek and obtain contribution from other persons liable under this section, directly or indirectly, for the same violation. Contribution shall be awarded by the court in accordance with the actual relative culpabilities of the various persons so liable.

11-[#]-505. Burden of proof. In any proceeding under this article, the burden of proving an exemption or an exception from a definition is upon the person claiming it.

11-[#]-506. Conduct of proceedings. Any administrative proceeding under this article shall be conducted pursuant to the provisions of section 24-4-105, C.R.S. The securities commissioner shall refer the conduct of all hearings to an administrative law judge appointed pursuant to part 10 of article 30 of title 24, C.R.S. Every hearing in an administrative proceeding shall be public unless the securities commissioner, in the securities commissioner's

discretion, grants a request joined in by all the respondents that the hearing be conducted privately.

11-[#]-507. Judicial review of orders. (1) Any person aggrieved by a final order of the securities commissioner may obtain a review of the order in the district court of the city and county of Denver pursuant to the provisions of section 24-4-106, C.R.S.

(2) The commencement of proceedings under subsection (1) of this section does not, unless specifically ordered by the court, operate as a stay of the securities commissioner's order.

Part 6
Administration and Fees

11-[#]-601. Division of securities. The division of securities created by section 11-51-701, C.R.S., shall be responsible for the administration of the provisions of this article. Nothing in this article shall affect the application to the division of securities of the provisions of section 24-34-104, C.R.S.

11-[#]-602. Administration of article. (1) The securities commissioner is hereby empowered to administer and enforce all provisions of this article and to provide the division of securities with such books, records, files, and printing and other supplies and employ such officers and clerical and other assistance as may be necessary in the securities commissioner's discretion to perform the duties required of the securities commissioner under this article.

(2) It is unlawful for the securities commissioner or any of the officers or employees of the division of securities to use for personal benefit any information which is filed with or obtained by the securities commissioner and which is not made public. No provision of this article authorizes the securities commissioner or any of such officers or employees to disclose any such information except among themselves or when necessary or appropriate in a proceeding or investigation under this article. No provision of this article either creates or derogates from any privilege which exists at common law or otherwise when documentary or other evidence is sought under a subpoena directed to the securities commissioner or any of the officers or employees of the division of securities.

(3) The securities commissioner may enter into an arrangement, agreement, or other working relationship with federal, other state, and self-regulatory authorities whereby public documents may be initially filed and maintained in a central registration depository or with other agencies or authorities. It is the intent of this subsection (3) that the securities commissioner be provided with the power to reduce the duplication of filings, reduce administrative costs, and in conjunction with other states and with federal authorities establish uniform procedures, forms, and administration to be used by this state and by such other states and by such federal authorities.

(4) The securities commissioner may delegate to any officer of the division of securities any power, duty, authority, or function created by this article and vested in the securities commissioner, but nothing in this subsection (4) shall authorize the securities commissioner to delegate to any officer the securities commissioner's authority to make rules, institute proceedings or actions under section 11-[#]-311 or 11-[#]-502, refer evidence under section 11-[#]-503(3), or exercise the authority created by this section, section 11-51-603(1) or (2), or section 11-51-606(3)(a) or (3)(b).

11-51-603. Rules, forms, and orders. (1) The securities commissioner may, from time to time, make, amend, and rescind such rules, forms, and orders as are necessary to carry out the provisions of this article, including rules and forms governing applications and reports and defining any terms, whether or not used in this article, insofar as the definitions are not inconsistent with the provisions of this article. For the purpose of rules and forms, the securities commissioner may classify securities, persons, and matters within the securities commissioner's jurisdiction and prescribe different requirements for different classes.

(2) No rule, form, or order may be made, amended, or rescinded unless the securities commissioner finds that the action is necessary or appropriate in the public interest and is consistent with the purposes and provisions of this article. In prescribing rules and forms, the securities commissioner may cooperate with the securities and exchange commission with a view to effectuating the policy of this article to achieve maximum uniformity in the form and content of applications and reports wherever practicable.

(3) No provision of this article imposing any liability upon a person or providing a basis for any sanction against a person applies to any act done or omitted in good faith and in conformity with any rule, form, or order of the securities commissioner, notwithstanding that the rule, form, or order may later be amended or rescinded or be determined by any judicial or other authority to be invalid for any reason.

11-51-604. Interpretive opinions. The securities commissioner may honor requests from interested persons for confirmation of the applicability of particular exemptions from licensing under section 11-[#]-302 or for other interpretive opinions regarding any provision of this article. Any person making such a request shall pay an opinion fee, which shall be determined and collected pursuant to section 11-[#]-606 and which shall not refundable. In response to any request for a confirmation or other interpretive opinion received under this section, the securities commissioner may waive any condition imposed under this article as it applies to the person making such request.

11-51-605. Consent to service of process. (1) An applicant for licensing under this article shall file with the securities commissioner, in such form as the securities commissioner by rule prescribes, an irrevocable consent appointing the securities commissioner or the successor in office of the securities commissioner to be the attorney for said person to receive service of any lawful process in any noncriminal suit, action, or proceeding against such person, or the successor, executor, or administrator of such person, arising under this article

or any rule or order under this article after the consent has been filed with the same force and validity as if served personally on the person filing the consent.

(2) A person who has filed a consent in compliance with subsection (1) of this section in connection with a previous application for licensing need not file an additional consent, but the securities commissioner may request, and in response to such request such person shall provide, verification of such previous consent.

(3) Service upon any person who has filed a consent pursuant to subsection (1) of this section may be made by leaving a copy of the process in the office of the securities commissioner, but it is not effective unless the plaintiff, who may be the securities commissioner in a suit, action, or proceeding instituted by the securities commissioner, forthwith sends a notice of the service and a copy of the process by registered mail to the defendant or respondent at the last address on file with the securities commissioner and unless the plaintiff's affidavit of compliance with this subsection (3) is filed in the case on or before the return day of the process, if any, or within such further time as the court allows.

(4) The methods of service of process provided for in this section are in addition to other methods of service of process provided for by law, including section 13-1-124, C.R.S. Any violation of this article shall be deemed to constitute the transaction of business within this state for the purpose of section 13-1-124, C.R.S.

11-51-606. Collection of fees. (1) A fee payable under this article shall be deemed paid when the securities commissioner receives the payment.

(2) (a) The securities commissioner shall transmit all fees collected under this article to the state treasurer, who shall credit the same to the division of securities cash fund created by section 11-51-707, C.R.S. All moneys credited to the division of securities cash fund shall be used as provided in this section, section 11-51-707, and any other provisions in the Colorado Revised Statutes which provide for funds to be credited to such cash fund and shall not be deposited in or transferred to the general fund of this state or any other fund.

(b) All fees collected under this article shall be combined with and administered as a single cash fund with the fees collected under article 51 of title 11, C.R.S., and fees, if any, collected under any other provisions of the Colorado Revised Statutes which provide for funds to be credited to such cash fund. The provisions of section 11-51-606 with respect to the budget requests, appropriations, expenditures and unexpended funds of the division shall apply additionally to the administration of this article.

(3) The division shall set the amount of each fee which it is authorized by law to collect under this article, reflecting both direct and indirect costs. Such fees for a fiscal year may be adjusted by the securities commissioner no more often than twice during that fiscal year.

6-51-607. Administrative files. (1) A document is filed when it is received by the securities commissioner.

(2) The securities commissioner shall keep a register of all applications for licenses and all licenses which are or have ever been effective under this article and all orders which have been entered under this article. The register shall be open for public inspection.

(3) The information contained in or filed with any application or report may be made available to the public under article 72 of title 24, C.R.S.

(4) Upon request and at such reasonable charges as the securities commissioner prescribes, the securities commissioner shall furnish to any person photostatic or other copies of any entry in the register or any document which is a matter of public record and may certify their authenticity; and the securities commissioner may also provide certification of the absence of any entry in the register or the absence of any document or other record from division files which are of public record. In any action, proceeding or prosecution under this article, any copy so certified, or any certification by the securities commissioner as to the absence of any such entry, document or record from division files, is prima facie evidence of the contents of the entry, document, or record so certified, or of the absence of the entry, document or record which is the subject of such certification.

Part 7
Effective Date

11-[#]-701. (1) This article shall be effective on and after **[an effective date to be specified]**, except:

(a) Section 11-[#]-603, concerning the rule-making authority of the securities commissioner, section 11-[#]-604, concerning the issuance of interpretive opinions, and section 11-[#]-606, concerning the setting of fees, shall take effect upon passage of this act; and

(b) An application for a license may be filed with the securities commissioner and all other requirements for obtaining a license may be satisfied prior to **[the effective date specified above]** and, if all the conditions listed in section 11-[#]-306(1)(a), including the passage of thirty days as provided in subparagraph (I) of that section, are satisfied as of **[the effective date specified above]** the license shall become effective on **[the effective date specified above]**.

(2) Nothing in this article limits the authority of the securities commissioner or any hearing officer, administrative law judge, or court to consider any event or circumstance which shall have occurred or existed prior to **[the effective date specified above]** in connection with any proceeding or action under section 11-[#]-311.