



Dora
Department of Regulatory Agencies

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Colorado Division of Securities
Department of Regulatory Agencies

The Switch
General Guidance and Instruction for Investment
Advisers that will be switching from the
Securities and Exchange Commission to the
State of Colorado

On November 21, 2011 the Colorado Division of Securities (“Division”) announced the Colorado Switch Program for investment advisers that will be switching from the regulatory authority of the Securities and Exchange Commission (“SEC”) to the regulatory authority of the Division as required by The Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) For full text of the announcement please visit the Division’s website or use the following link:

http://www.dora.state.co.us/securities/pdf_forms/publicnotices/Colo_Switch_Announcement.pdf

As noted in the November 21, 2011 release, the Colorado Switch Program has been developed to assist the advisers in fulfilling the requirement to switch in an efficient and timely fashion consistent with Colorado’s securities laws and regulations that protect the marketplace and investing public. The Program’s Key Aspects and Timeline are as follows:

Key Aspects:

- The Program is designed to not overburden the investment adviser or its agents.
- The Program respects the adviser’s time and the adviser’s responsibilities to their clients.



- The Program recognizes that the advisers who will be switching to state oversight have been regulated by the SEC and that there are differences between state and federal regulation. As such, the adviser will be responsible for making the necessary changes to their application documents and policies/procedures to ensure their compliance under Colorado's securities laws and regulations.
- By participating in the Program the adviser is committing to work with the Division both before and after the approval date to ensure compliance with Colorado's securities laws and regulations.
- Participation in the Program will ensure the adviser's timely approval with the Division.
- There will be no fees associated or assessed by the Division in connection with the Program.

Timeline:

- November 21, 2011 – Colorado Switch Program announcement.
- November 28, 2011 – This release provides further general guidance and instruction for advisers that will be switching from the SEC to the Division of the changes that they will be required to make to their application documents and policies or procedures prior to the approval date to be in compliance with Colorado's securities laws and regulations (discussed below).
- December 2, 2011 through December 19, 2011 – The Division is hosting a number of Workshop/Seminars entitled "The Switch." We invite and encourage the switching advisers and industry participants to sign up for one of these 2-hour sessions. We will cover the material disseminated in this release and answer questions you may have. For dates, times, and sign up directions please visit the Division's website or use the following link:

http://www.dora.state.co.us/securities/pdf_forms/publicnotices/Switch_Seminar_Workshop_Announcement.pdf

- January 3 through January 31, 2012 – The switching advisers file their Annual Updating Amendment, notify the SEC that they are no longer eligible to remain with the SEC and apply to the State of Colorado (discussed below).
- February 1 through February 29, 2012 – The advisers send to the Division other required documents (discussed below).
- June 14, 2012 – The Division will approve the advisers and will notify them that they are approved and are eligible to withdraw from SEC registration.
- June 15 through June 28, 2012 – The switching advisers will file a partial Form ADV-W to terminate their registration with the SEC.
- June 28, 2012 – Switch Program Completed.

The Division's ongoing proactive licensure examination process is designed to look for consistency in your application documents along with the required disclosures. The vast majority of deficiencies that occur in field examinations occur in the inconsistencies in the Form ADV Part 1A-1B, Form ADV Part 2A-2B, the advisory agreements or other documents, and what the adviser is actually doing. Our ongoing process is designed to eliminate these inconsistencies at time of licensure. This proactive approach provides consistency in the marketplace for the advisers and the investing community, and makes the field examination program more efficient.

Key to Colorado's Switch Program is the responsibility of the switching advisers to make the necessary changes to your application documents and policies or procedures to ensure consistency and compliance with Colorado's securities laws and regulations. The following information highlights a number of key issues that advisers are likely to encounter and provides you guidance and instruction:

- As an SEC registered investment adviser you are required to utilize and upload to the Investment Adviser Registration Depository ("IARD") system your current Form ADV Part 2A (Items 1-18). As a licensed investment adviser in Colorado, you will be required to amend your Form ADV Part 2A to include Item 19, and upload all appropriate Form ADV Part 2B's for each investment adviser representative. In the spring of 2011, the Division provided guidance to state licensed advisers regarding how to approach and maintain the Form ADV Part 2A-2B. For that guidance please visit the Division's website or use the following link:

http://www.dora.state.co.us/securities/pdf_forms/publicnotices/adv_part-2a-2b_recap.pdf

- Conflicts of interest may exist in the investment adviser community. Key is how you disclose and handle the conflict. Your Form ADV Part 2A-2B should disclose all conflicts of interest. Each conflict of interest should be addressed in three parts:
 - State the conflict (i.e., we buy and sell securities that we also recommend to clients).
 - State that it is a conflict; not that it is a potential, possible, might be, or maybe (i.e., this represents a conflict of interest).
 - Mitigate the conflict.
(For further guidance please visit the Division's website or use the above mentioned link)
- The federal definition of an investment adviser representative is different than the Colorado definition. Colorado law, Section 11-51-201 (9.6), C.R.S., provides:

“(a) "Investment adviser representative" with respect to an investment adviser means an individual who has a place of business in this state; who is a partner, officer, or director of an investment adviser; who occupies a status similar to or performs functions similar to those of a partner, officer, or director for an investment adviser; or who is employed or otherwise associated with an investment adviser who:

- (I) Makes recommendation or otherwise renders advice to clients regarding securities;
- (II) Manages securities accounts or portfolios for clients;
- (III) Determines which recommendation or advice regarding securities should be given to clients; or
- (IV) Supervises employees of, or persons otherwise associated with, an investment adviser or federal covered adviser who perform any of the duties specified in this paragraph (a).”

Individuals at your firm who meet this definition need to be licensed as investment adviser representatives. For those individuals, you will need to submit a Form U4 application for them to be licensed in Colorado and meet minimum qualifications.

- Advisers who deduct fees directly from their client’s accounts must be in compliance with Colorado Rule 51-4.10 (IA) B.2 regarding custody and safekeeping requirements. Colorado’s rule, the North American Securities Administrators Association (NASAA) model rule, and the language contained in Form ADV Part 1B, Item 2.I.(1)(a)(b) and (c) are consistent regarding the withdrawal of fees directly from customer accounts. However, this is different than the custody rules for the SEC. By complying with Colorado’s custody and safekeeping rule, you will be deemed to have constructive custody rather than full custody and, therefore, not have to comply with our full custody rules as prescribed in Section 11-51-407(5), C.R.S.
- Advisers or their related persons that have custody because of their position as a general partner, managing member, or their association or affiliation with a Pooled Investment Vehicle, must comply with Colorado Rule 51-4.10 (IA) B.3 regarding custody and safekeeping requirements. Colorado’s rule, elements of the NASAA model rule, and the language contained in Form ADV Part 1B, Item 2.I.(2)(a) are consistent in content. However, this is different than the custody rules for the SEC. By complying with Colorado’s custody and safekeeping rule regarding this activity, you will be deemed to have constructive custody rather than full custody and, therefore, not have to comply with our full custody rules as prescribed in Section 11-51-407(5), C.R.S.
- It is the Division’s position that binding arbitration clauses are inconsistent with the adviser’s fiduciary duties to the clients, and are for that reason inappropriate. At best these clauses cause confusion and can be considered to be misleading. The Division is not opposed to arbitration clauses for investment advisers, however, they should be denoted to be voluntary, they should not have terms such as final and binding, or have language that indicates that the client is waiving their rights to any other judicial forum.

Any voluntary arbitration clause should state clearly that it does not constitute a waiver of the client's rights under the Investment Advisers Act or similar state statutes or rules.

- Indemnification clauses may be couched in terms that are inconsistent with the adviser's fiduciary duties. Quite often the Division will find within indemnification clauses inappropriate qualifying words such as gross, willful, or intentional. You should remove any qualifying words from any indemnification clause that is inconsistent with your fiduciary duties such as gross, willful, or intentional.
- The Division is requesting that you file your Annual Updating Amendment between January 3 and January 31, 2012.
 - When you file this amendment you will be presented with the option to:
 - "Submit an Amendment" or "Apply ... with one or more States".
 - When you click the Amendment box, your option for "Annual" or "Other-Than" presents itself.
 - It is then that you may check all the boxes as in the screen
 - "Submit an Amendment", and
 - "Annual Updating Amendment for Fiscal Year ended December ...", and
 - "Apply ... with one or more States".
 - By filing in this methodology you will be fulfilling your Annual Updating Amendment requirement, and your application to the state. All of the appropriate sections of the ADV will then be opened, including Part 1B which will be blank for you to fill out. You are required to submit ADV Part 1B. ADV Part 1B is part of the Form ADV that state licensed or registered investment advisers are required to submit that you have not been required to submit as an SEC registrant, and
 - During this amendment you should mark Item 2.A.(13) which states the you are no longer eligible to remain registered with the SEC, and
 - When you file this amendment make sure that all the information on the IARD is current and correct including affirming your assets under management, and
 - You may upload you revised Form ADV Part 2A-2B as part of this amendment or you may submit it subsequently as an Other Than Annual Updating Amendment. The upload instructions are available through the link mentioned in the ADV Part 2A-2B section above.
- February 1 through February 29, 2012 – The advisers are to send to the Division other required documents:
 - If your business model includes separately managed accounts, financial planning, or consulting arrangements, please send to the Division a copy of the advisory agreement(s) or contract(s) that you utilize or intend to utilize. Unlike the SEC, which allows for oral agreements, Colorado requires that agreements or contracts must be in writing. Our Dishonest and Unethical Rule 51-4.8(1A) P prohibits an investment adviser or investment adviser representative from "Entering into,

extending, or renewing any investment advisory contract, unless such contract is in writing...”

- If your business model includes a pooled investment vehicle, please send to the Division all documents related to the pool such as, but not limited to, the Preliminary Prospectus Memorandum, Subscription Agreement, Limited Partnership Agreement, and a copy of the Independent 3rd Party Agreement.
- You may send the other required documents in paper form or electronic form in a non-writable compact disc to:

The Switch
Colorado Division of Securities
1560 Broadway, Suite 900
Denver, CO 80202

- The Division may request additional documents.

If you have any questions, we invite you to register for one of our upcoming Seminar/Workshops mentioned above, or you may contact me by email @ david.swafford@dora.state.co.us.

On behalf of the Commissioner and the Staff, we thank you in advance for your work and efforts and look forward to a successful culmination to this project.

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