

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

Amendment and Compilation of Chapter 16-39  
Hawaii Administrative Rules

MM DD, YYYY

1. Chapter 16-39, Hawaii Administrative Rules, entitled, "Securities", is amended and compiled to read as follows:

"HAWAII ADMINISTRATIVE RULES

TITLE 16

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

CHAPTER 39

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Historical Note: These new rules implement the new securities laws that become effective on July 1, 2008. In 2006, the Legislature passed Act 229, which established the new Hawaii Uniform Securities Act in HRS chapter 485A. Act 229 also repealed the old securities laws in HRS chapter 485 on June 30, 2008. Because these old

securities laws are being repealed, their corresponding administrative rules in HAR chapter 16-38 are also repealed. However, this chapter is based substantially upon chapter 16-38. [Eff 6/4/70; am 1/1/71; 7/30/81; am 11/5/81; am and comp 10/12/85; am 4/4/87; am and com 4/14/03; R 6/30/08; comp ]

## SUBCHAPTER 1

### GENERAL PROVISIONS

**§16-39-101 Definitions.** As used in this chapter, and in the forms, instructions, and orders of the commissioner, the following meanings shall apply to the extent that they are not inconsistent with the definitions provided in chapter 485A, HRS.

"Affiliate" means a person who, directly or indirectly, through one or more intermediaries, controls, or is controlled by, or is under common control with another person.

"Amount" means the aggregate dollar value affixed to a share. In the context of capitalization: number of shares multiplied by the par or stated value equals the amount. In the context of an offering: number of shares multiplied by the offering price per unit equals the amount.

"Applicant" means the issuer, broker-dealer, agent, investment adviser, investment adviser representative, or other person executing the application.

"Application" means the form prescribed by the commissioner, and includes any other paper, exhibit, amendment, or document filed pursuant to chapter 485A, HRS, and this chapter in connection with the registration of a security, broker-dealer, agent,

investment adviser, or investment adviser representative.

"Audited financial statements" means financial statements prepared in accordance with generally accepted accounting principles or any standard approved by the PCAOB and examined by independent accountants in accordance with generally accepted auditing standards, accompanied by an opinion of such independent accountants.

"Branch office" means any branch office, sales office, or office of supervisory jurisdiction that is listed on Schedule E to Form BD or on Schedule D to Form ADV; or any location in this State that is held out to the public as a place of business of a broker-dealer, an agent, an investment adviser, an investment adviser representative, or a federal covered investment adviser.

"Broker-dealer services" means the investment banking or securities business as defined by the FINRA.

"CFR" means the Code of Federal Regulations, as amended.

"Commissioner" means the state commissioner of securities.

"Compensation" as used in the definition of "investment adviser" in section 485A-102, HRS, shall include, but not be limited to, a salary, flat fee, any periodic retainer fee, or commissions or other types of monetary remuneration.

"Control" or "controlling person" means possession of the power, authority, or means to engage in the management or policymaking functions of a person, directly or indirectly, through ownership of securities, by contract or otherwise. A person owning at least twenty-five per cent of the outstanding voting securities of another shall be presumed to be a "controlling person" unless and until a determination to the contrary is made by the commissioner based on evidence presented by or on behalf of the person presumed to be controlling.

"CRD" means the Central Registration Depository of FINRA.

"Department" means the state department of commerce and consumer affairs.

"FDIC" means the Federal Deposit Insurance Corporation.

"Financial institution" means any of the following federal and state-chartered banks, savings and loan associations, savings banks, credit unions, and the service corporations of such institutions located in this State.

"Financial statements" means, but is not limited to, the statement of financial condition, statement of income, and statement of changes in stockholders' or owners' equity, or similar statements, as well as all related footnotes and supporting schedules applicable thereto, prepared in accordance with generally accepted accounting principles or any standard approved by the PCAOB.

"FINRA" means the Financial Industry Regulatory Authority.

"HRS" means Hawaii Revised Statutes, as amended.

"IARD" means the Internet-based Investment Adviser Registration Depository operated by FINRA to receive and store filings and collect related fees from investment advisers and investment adviser representatives on behalf of the commissioner.

"Independent accountants" means independent certified public accountants. The concept of independence shall be defined by rules promulgated by the American Institute of Certified Public Accountants.

"Investment Advisers Act" means the Investment Advisers Act of 1940, as amended.

"Investment Company Act" means the Investment Company Act of 1940, as amended.

"NASAA" means the North American Securities Administrators Association.

"Networking arrangement" means a contractual or other arrangement between a broker-dealer and a financial institution pursuant to which the broker-dealer conducts broker-dealer services on the premises of the financial institution where retail deposits are taken.



"Officer" means a president, vice president, secretary, treasurer, or any other person performing similar functions with respect to any organization, whether incorporated or unincorporated.

"Opinion of independent accountants" means audited financial statements shall be accompanied by an opinion of an independent accountant. The opinion letter shall be dated, shall be signed, shall identify without detailed enumeration the financial statements covered by the opinion, shall state that the examination was conducted in accordance with generally accepted auditing standards and shall express the independent accountant's opinion as to the fairness or unfairness of the financial statements in accordance with generally accepted accounting principles or any standard approved by the PCAOB or the independent accountant's inability to express such an opinion.

"Organization" means a corporation, partnership, trust, association, joint venture, syndicate, limited liability company, and any other form of business entity.

"OTC" means over-the-counter.

"Partnership" means a general partnership, limited partnership, or a limited liability partnership.

"PCAOB" means the Public Company Accounting Oversight Board.

"Predecessor" means a person, a major portion of whose business, assets, or control has been acquired by another.

"Promoter" means a person who, acting alone or in conjunction with others, takes the initiative in founding, organizing, or incorporating the business or enterprise of an issuer.

"Prospectus" means a document meeting the applicable requirements of chapter 485A, HRS, and this chapter.

"Public offering" means the offering of any security for sale to the general public, including, but not limited to:

- (1) By advertisement in any newspaper, magazine, periodical, or other publication, or by

means of a prospectus, offering circular, pamphlet, brochure, dodger, or addressed or unaddressed written or printed communication intended for public distribution or information, including through electronic media; or

- (2) By general solicitation by billboard, window display, website posting, or use of phonographic or other recording, radio, television, or any public demonstration or explanation by any similar device.

"Registrant" means an applicant whose registration of securities has become effective or whose registration as a broker-dealer, agent, investment adviser, or investment adviser representative has been approved under this chapter and chapter 485A, HRS.

"Registration statement" means the application to register securities that is filed with the commissioner.

"SCOR" means small company offering registration.

"SEC" means the United States Securities and Exchange Commission.

"Securities Act" means the Securities Act of 1933, as amended.

"Securities Exchange Act" means the Securities Exchange Act of 1934, as amended.

"Share" means a share of stock or unit of investment or interest in a corporation, limited partnership, limited liability company, or other unincorporated person, or a share or unit of a security.

"SRO" means self-regulatory organization.

"State" means the State of Hawaii.

"Subsidiary" means an affiliate controlled by another person.

"Underwriter" means a broker-dealer who participates in the distribution of a security, in connection with a public offering, either as a purchaser with a view to offer for resale, or one who undertakes to offer or sell, directly or indirectly, for an issuer. [Eff 6/30/08; comp ]

(Auth: HRS §485A-606) (Imp: HRS §§485A-102, 485A-202)

**§16-39-102 Filing.** (a) Unless otherwise specified, a document is considered filed on the first business day it is received in the office of the commissioner.

(b) All communications shall be addressed to: Commissioner of Securities, Business Registration Division, Department of Commerce and Consumer Affairs, P.O. Box 40, Honolulu, Hawaii 96810; or delivered to: 335 Merchant Street, Room 203, Honolulu, Hawaii 96813.

(c) The office of the commissioner shall be open for the transaction of business between the hours of 7:45 a.m. and 4:30 p.m. on weekdays, excluding state holidays.

(d) All documents, forms, statements, exhibits, etc. filed with the commissioner under chapter 485A, HRS, and this chapter shall be in the English language.

(e) Only originally executed forms or exhibits shall be filed, unless otherwise authorized by the commissioner.

(f) Unless otherwise provided by statute or rule, in computing any period of time prescribed or allowed by this chapter, the day of the act, event, or default after which the designated period of time is to run, shall not be included. The last day of the period so computed shall be included unless it is a Saturday, Sunday, or legal holiday in the State, in which event the period runs until the next day which is neither a Saturday, Sunday, nor a holiday. Intermediate Saturdays, Sundays, and holidays shall not be included in a computation when the period of time prescribed or allowed is seven days or less. A half holiday shall not be considered a holiday for the purpose of these computations. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§80-1, 485A-606)

**§16-39-103 Fees.** (a) The following fees shall be submitted with an initial or renewal application, or notice filing:

- (1) The fee for filing a notice of transaction involving the offer or sale of a security by an issuer to an accredited investor shall be \$200;
- (2) The fee for filing a report of the value of the federal covered securities sold or offered under section 485A-302, HRS, shall be \$50;
- (3) The fee for an initial notice filing for investment company securities shall be \$200 per portfolio or series. The annual fee to renew such notice filing shall be \$50 per portfolio or series;
- (4) The notice filing fee for a transaction under the Securities Act, Regulation D, 17 CFR Section 230.505, shall be \$100;
- (5) The notice filing fee for a federal covered security issued under the Securities Act, Regulation D, 17 CFR Section 230.506, shall be \$100;
- (6) The fee for registration of securities by qualification shall be one tenth of one per cent of the aggregate offering price of the securities to be offered in the State with a minimum fee of \$250 and a maximum fee of \$2,500. The annual fee to renew a registration by qualification shall be \$250;
- (7) The application fee for registration of a broker-dealer shall be \$200. The annual fee to renew a broker-dealer's registration shall be \$200;
- (8) The application fee for registration of a securities agent shall be \$50. The annual fee to renew an agent's registration shall be \$50. The fee for a transfer of registration as an agent shall be \$50;

- (9) The application fee for registration of an investment adviser shall be \$100. The annual fee to renew an investment adviser's registration shall be \$100;
  - (10) The application fee for registration of an investment adviser representative shall be \$50. The annual fee to renew an investment adviser representative's registration shall be \$50;
  - (11) The notice filing fee for a federal covered investment adviser required to file a notice shall be \$100 per calendar year. The annual fee to renew a federal covered investment adviser's notice filing shall be \$100; and
  - (12) The filing fee for any exempt transaction granted under subchapter 2 shall be \$100.
- (b) The fee for copies of documents filed in the office of the commissioner shall be twenty-five cents per page. [Eff 6/30/08; comp ] (Auth: HRS §§485A-303, 485A-606) (Imp: HRS §§92-24, 92-28, 485A-302, 485A-304, 485A-406)

**§16-39-104 Forms.** (a) The following forms shall be used by persons submitting an initial or renewal application, or notice filing to the commissioner:

- Form ADV: shall be used by an investment adviser to request registration or to renew a registration, and by a federal covered investment adviser to submit a required notice filing;
- Form ADV-H: shall be used by an investment adviser to request a temporary or continuing hardship exemption;
- Form ADV-W: shall be used by an investment adviser to terminate a registration, or by a federal covered investment adviser to terminate a notice filing;

Form BD: shall be used by a broker-dealer or issuer to request registration;

Form BD-W: shall be used by a broker-dealer or issuer to terminate a registration;

Form D: shall be used by issuers of securities to satisfy the requirements of section 16-39-203 or section 485A-202(15)(D), HRS;

Form NF: shall be used by an investment company to comply with the notice filing requirements under section 16-39-221;

Form U-1: shall be filed by an issuer seeking registration of its securities by qualification;

Form U-2: shall be used to satisfy any requirement under chapter 485A, HRS, that a consent to service of process be filed with the commissioner; provided that in lieu of filing a Form U-2, the commissioner shall accept an originally executed Form ADV, Form BD, or Form U-4 that has been filed with the commissioner or with the CRD;

Form U-2A: shall be used by any person required under chapter 485A, HRS, to file a corporate resolution with the department;

Form U-4: shall be used by an agent or investment adviser representative to request registration or to request a transfer of registration from one broker-dealer, issuer, investment adviser, or federal covered investment adviser to another;

Form U-5: shall be used to terminate the registration of an agent or investment adviser representative;

Form U-7: shall be used by issuers seeking registration of a SCOR offering.

Model Accredited

Investor Form: shall be used by an issuer offering or selling securities to accredited investors to submit a notice filing;

(b) Broker-dealers that are registered under the Securities Exchange Act may file Forms BD, BD-W, U-4, and U-5 with the commissioner through the CRD.

(c) Investment advisers and federal covered investment advisers may, to the extent permitted by the IARD, file Forms ADV, ADV-W, U-4, and U-5 with the commissioner through the CRD.

(d) Every applicant or registrant that has filed any of the forms listed in subsection (a) with the commissioner shall promptly file with the commissioner any and all amendments necessary to keep the information previously reported on the forms current and accurate. If the form being amended was filed with the commissioner through the CRD, any amendment to the form may also be filed through the CRD. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §485A-606)

**§16-39-105 Action on documents submitted to the commissioner; extension.** (a) The commissioner shall accept or deny documents submitted to the commissioner within forty-five calendar days after the date the documents were submitted.

(b) An application for registration as a broker-dealer, agent, investment adviser, or investment adviser representative shall become effective at noon on the forty-fifth day after a completed application is filed unless:

- (1) Otherwise provided by state or federal law; or
- (2) An earlier effective date is specified by rule or order.

(c) To be complete, the document shall consist of the appropriate form described in section 16-39-104, together with any additional documents or information and fees required under this chapter or chapter 485A, HRS, or requested by the commissioner.

(d) The commissioner shall notify an applicant within forty-five calendar days of an application being received if the application is not complete and shall provide the applicant a list of the documents, information, and fees that must be filed in order to have the application deemed complete. An applicant shall have an additional forty-five calendar days from the receipt of the commissioner's letter within which to complete the pending document. If the document has not been completed within this time, it may be denied by the commissioner pursuant to section 485A-412, HRS, or be withdrawn by the applicant. [Eff 6/30/08; comp ] (Auth: HRS §§26-9, 91-13.5, 485A-606) (Imp: HRS §91-13.5)

**§16-39-106 Fines and penalties.** Any fines and penalties imposed under chapter 485A, HRS, or this chapter shall be deposited into the compliance resolution fund. [Eff 6/30/08; comp ] (Auth: HRS §§26-9, 485A-606) (Imp: HRS §§485A-508, 485A-602, 485A-603, 485A-604)

## SUBCHAPTER 2

### EXEMPT TRANSACTIONS AND NOTICE FILING REQUIREMENTS FOR FEDERAL COVERED SECURITIES

#### A. Exempt Transactions



**§16-39-201 Limitation on issuers and offerors.**

(a) Nothing in this subchapter shall relieve, or be construed as in any way relieving, issuers or persons acting on their behalf from the anti-fraud provisions of chapter 485A, HRS.

(b) In view of the objective of this subchapter and the purpose and policies underlying chapter 485A, HRS, the exemptions are not available to any issuer or persons acting on their behalf with respect to any transaction which, although in technical compliance with this subchapter, is part of a plan or scheme to evade registration or the conditions or limitations explicitly stated in chapter 485A, HRS, or this chapter. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-202, 485A-203)

**§16-39-202 Exemptions.**

(a) Any offer or sale of securities offered or sold in compliance with the Securities Act, Regulation D, 17 CFR sections 230.501, 230.502, 230.503, and 230.505 and complies with the conditions and limitations of this subchapter, shall be exempted under section 485A-203, HRS.

(b) This section shall not provide an exemption for any offer or sale of securities offered or sold in compliance with the Securities Act, Regulation D, 17 CFR section 230.504. [Eff 6/30/08; comp

] (Auth: HRS §§485A-203, 485A-606) (Imp: HRS §§485A-202, 485A-203)

**§16-39-203 Notice filing.**

(a) For issuers offering or selling securities in compliance with the Securities Act, Regulation D, 17 CFR section 230.505, a notice filing shall be made no later than fifteen calendar days after the first sale is made in this State. The notice filing shall consist of:

- (1) One signed copy of the Form D currently updated, and the appendix thereto;

- (2) An executed consent to service of process (Form U-2); and
- (3) The filing fee set forth in section 16-39-103.

(b) Upon written request of the commissioner, the issuer shall provide copies of information furnished in tangible form, including by electronic transmission, by the issuer to offerees.

(c) Amendments. During the period of the offering, the issuer shall take steps necessary to ensure that all material information contained in the notice filing remains current and accurate. [Eff 6/30/08; comp ] (Auth: HRS §§485A-203, 485A-606) (Imp: HRS §§485A-202, 485A-203)

**§16-39-204 Application for residential cooperative corporations.** The information required for filing shall be as prescribed in the application form, together with other information as the commissioner may require. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-201, 485A-202)

**§16-39-205 Disqualification.** (a) Any person who is disqualified by the SEC from using any provision of the Securities Act, Regulation D, 17 CFR section 230.507, shall not qualify for any of the exemptions under this subchapter.

(b) Any disqualification caused by this section shall be automatically rescinded if the federal or state agency which created the basis for disqualification determines upon a showing of good cause that it is not necessary under the circumstances that the exemptions be denied. [Eff 6/30/08; comp ] (Auth: HRS §§485A-203, 485A-606) (Imp: HRS §§485A-202, 485A-203)

B. Notice Filing [~~For~~] for Federal Covered Securities

**§16-39-220 Notice filing for investment company securities.** (a) Pursuant to section 485A-302, HRS, for a federal covered security that is issued by an investment company registered under the Investment Company Act, the notice filing shall include:

- (1) A Form NF or a copy of the issuer's federal registration statement;
- (2) A consent to service of process (Form U-2); and
- (3) The filing fee set forth in section 16-39-103.

(b) Except as otherwise provided in chapter 485A, HRS, and this chapter, a notice filing shall be effective commencing upon the later of its receipt by the commissioner or the effectiveness of the offering with the SEC, and continuing until two months after the issuer's fiscal year end. A notice filing may be renewed prior to its expiration by filing with the commissioner:

- (1) A current Form NF or a copy of the issuer's most recent federal registration statement; and
- (2) The renewal fee set forth in section 16-39-103.

(c) A renewed notice filing shall take effect upon the expiration of the previous notice filing.

(d) The initial notice filing by a unit investment trust shall be effective indefinitely.

[Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §485A-302)

**§16-39-221 Notice filing for transactions under the Securities Act, Regulation D, 17 CFR section 230.506.** For a federal covered security issued under the Securities Act, Regulation D, 17 CFR section 230.506, a notice filing shall be filed with the

commissioner no later than fifteen calendar days after the first sale is made in this State. The notice filing shall consist of:

- (1) One copy of the Form D currently updated, and the appendix thereto;
- (2) A consent to service of process (Form U-2); and
- (3) The filing fee set forth in section 16-39-103. [Eff 6/30/08; comp ]  
(Auth: HRS §485A-606) (Imp: HRS §485A-302)

### SUBCHAPTER 3

#### REGISTRATION OF SECURITIES

##### A. Registration of Securities, Prospectus

**§16-39-301 Registration of securities.** (a) In addition to the requirements of section 485A-303, HRS, a registration statement to register securities by qualification shall contain the following:

- (1) A Form U-1 and accompanying documents (including subscription agreement);
- (2) Two copies of the prospectus, including financial statements;
- (3) All exhibits filed with the SEC in connection with the registration statements;
- (4) The filing fee set forth in section 16-39-103; and
- (5) Any additional information or documents requested by the commissioner.

(b) An application filed with the SEC under the Securities Act, Regulation A, 17 CFR sections 230.251 to 230.262, may be filed with the commissioner by qualification. Notwithstanding the requirements of the SEC, however, the prospectus or offering circular

used in connection with an offering of securities under Regulation A of the SEC shall contain the financial statements prescribed by section 485A-303(b), HRS. [Eff 6/30/08; comp ]  
(Auth: HRS §485A-606) (Imp: HRS §§485A-301, 485A-303, 485A-304)

**§16-39-302 Prospectus.** (a) The prospectus of any security that is subject to registration under section 485A-303, HRS, or this chapter may be printed, mimeographed, lithographed, or typewritten, or prepared by any similar process in clearly legible copies.

(b) Every subscription agreement concerning the registration of a security by qualification shall contain a statement by the purchaser that the purchaser has received a copy of the security's prospectus.

(c) Interstate offerings shall contain the information required by the application form together with the following:

- (1) How the public offering price was established;
- (2) Whether there has been a public market for the securities;
- (3) The terms and conditions of the escrow agreement; and
- (4) Business history of the officers and directors.

(d) Intrastate offerings shall contain the same information as interstate offerings, plus the following:

- (1) That the offering is only to bona fide residents of this State;
- (2) That during the public offering, no securities may be transferred to a nonresident of this State;
- (3) That in case of a sale to a nonresident, the issuer may rescind the sale and refund the purchase price; and

(4) In an offering of interest-bearing securities, what reserves or sinking fund shall be provided to pay for the securities as they become due, or whether no reserves shall be provided.

(e) The prospectus shall be prepared in substantially the following form and shall contain the information required under chapter 485A, HRS, this chapter, and any additional information required by the commissioner. (The following specimen form has been prepared for use in connection with a speculative intrastate offering and may therefore be modified to the extent the provisions are inapplicable.)

(1) Cover page:

"PROSPECTUS  
(Date)

(NAME OF ISSUER)  
(Address)

Incorporated under the laws of the State of Hawaii (Date) \_\_\_\_\_ Shares of Common Stock of the Par Value of \$ \_\_\_\_\_ Per Share.

	Offering Price	Sales Commissions	Net Proceeds To Issuer*
Per Share	\$ _____	\$ _____	\$ _____
Aggregate	\$ _____	\$ _____	\$ _____

\*Before deducting expenses estimated not to exceed \$ \_\_\_\_\_ to be borne by the issuer.

THE SECURITY(IES) DESCRIBED IN THIS PROSPECTUS ARE SPECULATIVE. NEITHER THIS PROSPECTUS NOR THE

SECURITIES DESCRIBED HEREIN HAVE BEEN APPROVED OR DISAPPROVED BY THE COMMISSIONER OF SECURITIES OF THE STATE OF HAWAII, NOR HAS THE COMMISSIONER PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. THIS OFFERING IS MADE ONLY TO BONA FIDE RESIDENTS OF THE STATE OF HAWAII.

To be sold by \_\_\_\_\_";

(2) Business.

- (A) State the history, showing capitalization, mergers, change of names, etc., general character and location of issuer's business, properties, branch offices, stores, plants, outlets, etc., and similar information concerning its predecessors, affiliates, and subsidiaries. There should also be a statement as to the length of time the issuer has been in business;
- (B) Describe the physical properties, equipment, claims, patents, or patent applications, etc., and nature of title or interest therein;
- (C) If the issuer leases its plant, office, or other physical properties, disclose briefly the terms of the lease and relationship of the lessor to any officer, director, promoter, or stockholder of the issuer;
- (D) State the nature of present or proposed products or services, the principal market therefor;
- (E) Set forth the general competitive conditions in the industry or business in which the issuer is, or proposes to be, engaged, and any particular risks or hazards to which it might be subjected; and

- (F) Describe the issuer's employee relations by setting forth the number of employees and whether any of them are covered by collective bargaining agreements and, if so, approximately how many are so covered, when the agreements expire, and whether collective bargaining is on a company or industry wide basis. Also describe whether the issuer has experienced any work stoppages in recent years;
- (3) Use of proceeds. Outline the estimated monetary proceeds to be received by the issuer from the offering; the purposes for which the proceeds are to be used by the issuer; the estimated amount to be used for each purpose; the order or priority in which the proceeds will be used for the purposes stated; the amount of funds to be raised from other sources to achieve the purposes stated; the sources of those funds; and, if a part of the proceeds is to be used to acquire property (including goodwill) other than in the ordinary course of business, the names and addresses of the vendors, the purchase price, the names of any persons who have received commissions in connection with the acquisition, and the amounts of the commissions and other expenses in connection with the acquisition;
- (4) Method of offering. If the securities are to be offered through a broker-dealer, state the name and address of the broker-dealer, with a statement of any material relationship between the issuer and the broker-dealer. State whether the securities are to be offered for cash only or whether the securities may be paid for in installments and, if so, the specific terms and conditions. If a minimum purchase is required, it should also be disclosed. State briefly the commission to be paid to



the broker-dealer, including cash, securities, contracts, options, or any other consideration. If the securities are to be sold by the issuer, it should also be stated that the offering shall be done by securities agents duly registered with the commissioner. If the proceeds of the offering are to be placed in escrow, state the terms and conditions of the escrow; and state the other terms prescribed by the commissioner for the certification by the escrow agent to the commissioner when the amount specified in the escrow agreement has been met in the specified time and the conditions whereby the funds shall be released to the subscribers by the escrow agent. State also that during the public offering, no securities may be transferred to a nonresident and that in case of a sale to a nonresident, the issuer shall rescind the sale and refund the purchase price;

- (5) Speculative features of the offering. Explain generally the speculative features of the offering and any special conditions that may affect the success or failure of the enterprise or the investor's interest therein. State how the public offering price was established and whether there has been a public market for the shares. In a speculative offering, the front cover shall contain a clear and conspicuous statement that the securities are speculative. If the officers, directors, or promoters are receiving or have received salaries, fees, or other compensation from the issuer, indicate the amounts, how paid, and services rendered;
- (6) Description of securities. Outline briefly as follows:
  - (A) In the case of shares, the par or stated value, if any; the rate of dividend, if fixed, whether cumulative

- or noncumulative and any restrictions on dividend payments; the preference, if any; and if convertible, the conversion rate; the restrictions, if any, on the transfer of the securities;
- (B) In the case of debt securities, the rate of interest; the date of maturity or, if the issue matures serially, a brief indication of the serial maturities; if the issue is redeemable before maturity, a brief statement of the redemption date or dates and price or prices; if payment of principal or interest is contingent, an indication of the contingency; a brief indication of the priority of the issue; and if convertible, the conversion rate; and
  - (C) In the case of any other kind of security, appropriate information of a comparable character;
- (7) Management and control. With respect to each director and officer of the issuer, and other person having a similar status or performing similar functions, the person's name, address, and principal occupation for the previous five years; the amount of securities of the issuer held by the person as of the thirtieth day before the filing of the registration statement; the amount of the securities covered by the registration statement to which the person has indicated an intention to subscribe; and a description of any material interest of the person in any material transaction with the issuer or a significant subsidiary effected within the previous three years or proposed to be effected. With respect to a promoter, if the issuer was organized within the previous three years, the information or records specified above, any amount paid to the promoter within that period or intended to

- be paid to the promoter, and the consideration for the payment;
- (8) Interests of management. Provide a description of all direct or indirect interests, by security holdings or otherwise, of each officer and director of the issuer and, if the issuer was organized within the last three years, of each promoter of the issuer:
    - (A) In the issuer or its affiliates; and
    - (B) In any material transactions within the past two years or in any material proposed transactions to which the issuer or any of its predecessors or affiliates was or is to be a party, stating the cost to those persons of any property or services for which payment by or for the account of the issuer has been or is to be made;
  - (9) Ownership. With respect to a person owning of record or owning beneficially, if known, ten per cent or more of the outstanding shares or any class or equity security of the issuer, the information specified in paragraph (7) other than the person's occupation;
  - (10) Options and warrants. A description of any stock options or other security options outstanding, or to be created in connection with the offering, including the names of the holders thereof, the cost thereof to the holders, the terms and conditions on which they may be exercised, and the price at which the securities may be acquired pursuant thereto;
  - (11) Litigation. A description of any pending litigation, action, or proceeding to which the issuer or any of its subsidiaries is a party or of which any of their property is the subject and that materially affects its business or assets, and any litigation,

- action, or proceeding known to be contemplated by governmental authorities;
- (12) Legal opinion. State the name and address of the attorney who has advised the issuer with respect to the legality of the offered securities, with an English translation if it is in a language other than English, which states whether the security when sold will be validly issued, fully paid, and nonassessable and, if a debt security, a binding obligation of the issuer;
  - (13) Escrow provisions. If the officers, directors, promoters, or insiders have stock which is subject to escrow pursuant to section 485A-304(f), HRS, or subject to escrow pursuant to any state or federal statute or regulation, make a complete disclosure of the number of shares escrowed, names of persons escrowing the stock, where escrowed, and the terms and conditions of the escrow; and
  - (14) Financial statements. Provide a balance sheet of the issuer at the close of the issuer's last fiscal year preceding the date of filing of the prospectus, and a profit and loss statement and analysis of surplus for the fiscal year ended at the date of the balance sheet, all certified by an independent public accountant; together with a balance sheet of the issuer as of a date within ninety days prior to the date of filing of the prospectus and a statement of profit and loss for the period from the close of the last preceding fiscal year to the date of the balance sheet, both verified by a duly authorized officer, or the equivalent, of the issuer or, if the issuer has been in existence for less than one year, a balance sheet of the issuer as of a date within ninety days prior to the date of filing and a statement of profit and loss for the period from the date of the issuer's

organization to the date of the balance sheet, both certified by an independent public accountant.

If consolidated financial statements are used, there should also be a financial statement of the issuer alone. If the issuer has not yet commenced business, there should be submitted in lieu of the statement of profit and loss a statement of receipts and disbursements certified to by an independent public accountant. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-303, 485A-304)

B. Statements [~~of~~] of Policy Relating [~~To~~] to Registration [~~of~~] of Securities

**§16-39-310 Registration of securities by qualification.** The commissioner may deny an application for registration of a security as being fraudulent or working or tending to work a fraud upon the purchaser, or may find that the enterprise or business of the issuer is based on unsound business principles, unless the requirements of chapter 485A, HRS, and this chapter are met or good cause is shown for an exception. [Eff 6/30/08; comp ] (Auth: HRS §§485A-303, 485A-606) (Imp: HRS §§485A-303, 485A-606)

**§16-39-311 Financial reports.** Financial statements required under chapter 485A, HRS, and this chapter shall be prepared, audited, and certified by independent certified public accountants or licensed independent public accountants in accordance with generally accepted accounting procedures and practices; provided that if a report contains exceptions of a material nature, it shall not be considered to be certified. [Eff 6/30/08;

comp ] (Auth: HRS §§485A-303, 485A-606) (Imp: HRS §§485A-303, 485A-606)

**§16-39-312 Maximum commissions and expenses.**

Compensation to broker-dealers in connection with the sale and promotion of a public offering, including selling expenses and allowances or reimbursement for items such as salaries, overrides, agent's commissions, clerical, administrative, printing, postage, advertising, and all other expenditures incurred, and anything of value accruing to the broker-dealer directly or indirectly, shall not exceed fifteen per cent of the total amount of the offering. [Eff 6/30/08; comp ] (Auth: HRS §§485A-303, 485A-606) (Imp: HRS §§485A-303, 485A-606)

**§16-39-313 Offering price.** In the case of an issuer which has been actually engaged in business or operation, the amount for which a security is being offered to the public should bear some reasonable relationship to:

- (1) Market value, if any;
- (2) Price-earnings ratio, as reflected by its financial statements covering an average three-year preceding period, or the shorter duration of experience or operation as may be applied; or
- (3) In the absence of an established or determinable market value or price-earnings ratio, the book value of the issuer may be taken into consideration in justifying or substantiating the reasonableness of the offering price. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-303, 485A-606)

**§16-39-314 Compliance with Hawaii business registration laws.** No application of a Hawaii corporation, partnership, limited liability company, or other business entity for the registration of a security shall be accepted if the entity is not current in filing its annual reports as required by this State's business registration laws, and complete records as prescribed by this State's business registration laws shall be maintained at all times. [Eff 6/30/08; comp \_\_\_\_\_ ] (Auth: HRS §485A-606) (Imp: HRS §§485A-303, 485A-304, 485A-606)

**§16-39-315 NASAA statements of policy for registration of securities.** The disclosure-related provisions of certain guidelines or statements of policy adopted by NASAA may be used by the commissioner for purposes of reviewing the adequacy of the disclosures required under this chapter and chapter 485A, HRS. The following "Statements of Policy and Guidelines" of NASAA are hereby adopted and incorporated by reference into this chapter:

- (1) "Uniform Disclosure Guidelines for Cover Legends" adopted on October 2, 2004, as amended;
- (2) "NASAA Guidelines Regarding Viatical Investments" adopted on October 1, 2002, as amended;
- (3) "Statement of Policy Regarding Corporate Securities Definitions" adopted on September 28, 1999, as amended;
- (4) "Statement of Policy Regarding the Impoundment of Proceeds" adopted on September 28, 1999, as amended;
- (5) "Statement of Policy Regarding Options and Warrants" adopted on September 28, 1999, as amended;
- (6) "Statement of Policy Regarding Promotional Securities" adopted on September 28, 1999, as amended;

- (7) "Statement of Policy Regarding Specificity in Use of Proceeds" adopted on September 28, 1999, as amended;
- (8) "Statement of Policy Regarding Underwriting Expenses, Underwriter's Warrants, Selling Expenses and Selling Securities Holders" adopted on September 28, 1999, as amended;
- (9) "Statement of Policy Regarding Unsound Financial Condition" adopted on September 28, 1999, as amended;
- (10) "Statement of Policy Regarding Promoters' Equity Investment" adopted on April 27, 1997, as amended; and
- (11) "Statement of Policy Regarding Real Estate Investment Trusts" adopted on May 7, 2007, as amended. [Eff 6/30/08; comp ]  
(Auth: HRS §485A-606) (Imp: HRS §§485A-303, 485A-606)

C. Effectiveness [~~And~~] and Post-Effectiveness Requirements

**§16-39-330 Effectiveness.** When an application for the registration of securities has been declared effective by the commissioner, it shall be designated as a registration statement, and the offering may be commenced upon the issuance of a certificate of registration or notification of effectiveness. A registration statement that has become effective with the SEC under the Securities Act becomes effective in this State automatically at the moment of effectiveness with the SEC if no stop order or notice of deficiency has been entered. The applicant shall promptly advise the commissioner by telephone, fax, or electronically of the date and time of the securities' federal effectiveness. [Eff 6/30/08; comp ]  
(Auth: HRS §485A-606) (Imp: HRS §§485A-302, 485A-303, 485A-304)



**§16-39-331 Confirmations by issuer.** Every issuer selling its own securities in an intrastate offering, at or before completion of a transaction, shall give or send to each customer written confirmation, retaining copies thereof, concerning all sales of securities, and disclosing the:

- (1) Date the transaction occurred;
- (2) Price and commission charged; and
- (3) Name of the agent handling the transaction.  
[Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-303, 485A-606)

**§16-39-332 Amendments.** (a) If prior to or during the period of effectiveness any statement, document, or information contained in the registration statement or prospectus becomes materially inaccurate, incorrect, or misleading, or in the light of changes in circumstances, addendums are made necessary in order to present a full disclosure of material facts affecting the issuer's business or the offering, or if the commissioner requests additional data, information, or verification thereof, the registrant shall promptly file, and in no event later than fifteen days following the event, occurrence, discovery, or notice thereof necessitating the same, a correcting amendment.

(b) In the event an issuer amends its prospectus, the revised date together with the date of the prospectus shall be shown on the front cover, and the portion or portions of the prospectus being amended should also show the amended date. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-301, 485A-303, 485A-304)

**§16-39-333 Renewals.** A registration statement may be renewed not less than fifteen days prior to the

expiration date by filing a new prospectus containing information of a date not more than ninety days prior to the date of filing, together with the renewal fee of \$250. The front cover shall show the balance of the offering, the amount of the original registration, and the date the original registration became effective. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-302, 485A-303)

**§16-39-334 Withdrawal, termination, or completion.** (a) A request for withdrawal of a registration statement may be made before or after its effectiveness by written notification to the commissioner; provided that no request shall be granted during the pending of a stop order proceeding under section 485A-305, HRS, unless the commissioner finds that the stop order is not necessary in the public interest. Upon the granting of a request for withdrawal, no part of the registration fee shall be refunded.

(b) Notification of termination or completion of a registered offering shall be submitted to the commissioner within thirty calendar days after the termination or completion, and shall include the results of the offering. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-302, 485A-303, 485A-304, 485A-305)

D. Advertising [~~And~~] and Financial Reports

**§16-39-340 Advertising.** (a) Definition. For purposes of this section, "sales literature" means material published in connection with an offer, sale, or purchase of a security to or from the general public, including material published in electronic format, or designed for use, in a newspaper, magazine or other periodicals, radio, television, telephone solicitation or tape recording, videotaped display,

signs, billboards, motion pictures, telephone directories (other than routine listings), other public media and any other written communication distributed or made generally available to the public, electronically or otherwise including, but not limited to, prospectuses, pamphlets, circulars, form letters, seminar texts, research reports, surveys, performance reports or summaries and reprints or excerpts of other sales literature or advertising to include publications.

(b) Filing requirement. Any sales literature used in connection with the offering of a security in this State shall be filed with the commissioner at least two business days prior to its proposed use; provided that the following materials shall be exempt from the filing requirements of this section: all advertising material previously filed with and cleared by the SEC or FINRA; all "tombstone" advertisements; and all advertisements relating to a federal covered security or to a security that is exempt from registration pursuant to section 485A-201 or 485A-202, HRS.

(c) Application of antifraud provisions. Sales literature used in any manner in connection with the offer, sale, or purchase of a security shall be subject to the provisions of sections 485A-501 and 485A-505, HRS, whether or not the sales literature is required to be filed pursuant to section 485A-504, HRS, or this section. Sales literature shall not contain any ambiguity, exaggeration, or other misstatement or omission of material fact that might confuse or mislead an investor.

(d) Prohibited disclosures. Unless specifically stating that the commissioner has not approved the merits of the security offering or the sales literature, no sales literature shall contain a reference to the commissioner unless such reference is specifically requested by the commissioner. [Eff 6/30/08; comp ] (Auth: HRS §§485A-504, 485A-606) (Imp: HRS §§485A-501, 485A-504, 485A-505, 485A-606)

**§16-39-341 Reports.** A copy of all financial reports sent or intended to be sent to security holders by an issuer of securities that is registered under chapter 485A, HRS, shall be filed with the commissioner upon request during the period of time that the issuer's registration statement is in effect. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-411, 485A-606)

E. Small Company Offerings Registration

**§16-39-350 Purpose.** The purpose of sections 16-39-350 to 16-39-355 is to encourage investment in small businesses, and provide a method of registration for small companies offering securities to the public. The commissioner recognizes that small issuers raising small amounts of money face special problems not faced by issuers raising larger amounts, and that standards appropriate to registrations of larger offerings may become unduly burdensome when applied to registrations of small offerings. The registration method offered by sections 16-39-350 to 16-39-355 is intended to reduce the costs and burdens of raising capital for small business and to maximize the amount of offering proceeds available to the issuer for investment in the business, without sacrificing investor protection. Issuers eligible for this method of registration shall use the SCOR registration form as the disclosure document for the offering. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-303, 485A-606)

**§16-39-351 Application of this chapter to SCOR registrations.** (a) The provisions of subchapter 3 shall apply to SCOR registrations; provided that

section 16-39-311 relating to financial reports, and section 16-39-330 relating to SEC effective dates shall not apply.

(b) The commissioner reserves the right to apply this chapter (or any provision therein) to offerings under sections 16-39-350 to 16-39-355 if the commissioner determines that such application, even in the small business offering context, is necessary for the protection of investors. [Eff 6/30/08; comp \_\_\_\_\_] (Auth: HRS §485A-606) (Imp: HRS §§485A-303, 485A-606)

**§16-39-352 Availability.** (a) SCOR is intended to allow small companies to conduct limited offerings of securities. SCOR uses a simplified offering format designed to provide adequate disclosure to investors concerning the issuer, the security offered, and the offering itself. Certain issuers may not be able to make adequate disclosure using the SCOR format and will, therefore, be unable to utilize SCOR.

(b) The commissioner finds that SCOR is generally unsuitable for the following issuers and programs:

- (1) Holding companies, and companies whose principal purpose is owning stock in or supervising the management of other companies;
- (2) Portfolio companies, including but not limited to real estate investment trusts as defined in NASAA's "Statement of Policy Regarding Real Estate Investment Trusts" referenced in section 16-39-315(11);
- (3) Issuers with complex capital structures;
- (4) Commodity pools;
- (5) Equipment leasing programs;
- (6) A "blind pool" or other offering for which the specific business to be engaged in or property to be acquired by the issuer cannot be specified; and
- (7) Real estate programs.

(c) SCOR registrations are available only to the issuer of the securities and not to any affiliate of that issuer or to any other person for resale of the issuer's securities.

(d) In addition, each of the following requirements shall be met:

- (1) The issuer shall be a corporation or centrally managed limited liability company organized under the law of the United States or Canada, or any state, province, or territory or possession thereof, or the District of Columbia, and have its principal place of business in one of the foregoing;
- (2) The issuer shall be required to engage in a business other than petroleum exploration or production or mining or other extractive industries;
- (3) The issuer shall not be a development stage company that either has no specific business plan or purpose or has indicated that its business plan is to engage in merger or acquisition with an unidentified company or companies or other entity or person;
- (4) The offering price for common stock (and the exercise price, if the securities offered are options, warrants, or rights for common stock, and the conversion price, if the securities are convertible into common stock) shall be equal to or greater than one dollar per share. The offering price for common ownership interests in a limited liability company (and the exercise price, if the securities are options, warrants, or rights for common ownership interests, and the conversion price, if the securities are convertible into common ownership interests) shall be equal to or greater than one dollar per unit of interest;
- (5) The aggregate offering price of the securities offered (within or outside this State) shall not exceed \$1,000,000 less the aggregate offering price of all securities

sold within the twelve months before the start of and during the offering of the securities under the Securities Act, 17 CFR section 230.504, in reliance on any exemption under section 3(b) of the Securities Act, in reliance on the exemption under section 3(a)(11) of the Securities Act, or in violation of section 5(a) of the Securities Act;

(6) Commissions, fees, or other remuneration for soliciting any prospective purchaser in connection with the offering in this State shall only be paid to persons who, if required to be registered or licensed, the issuer believes or has reason to believe are appropriately registered or licensed in this State; and

(7) Financial statements shall be prepared in accordance with either U.S. or Canadian generally accepted accounting principles. If appropriate, a reconciliation note should be provided. If the issuer has not conducted significant operations, statements of receipts and disbursements shall be included in lieu of statements of income. Interim financial statements may be unaudited. All other financial statements shall be audited by independent certified public accountants; provided that if each of the following four conditions are met, such financial statements in lieu of being audited may be reviewed by independent certified public accountants in accordance with the Accounting and Review Service Standards promulgated by the American Institute of Certified Public Accountants or the Canadian equivalent:

(A) The issuer shall not have previously sold securities through an offering involving the general solicitation of prospective investors by means of advertising, mass mailing, public

meetings, "cold call" telephone solicitation, or any other method directed toward the public;

- (B) The issuer has not been previously required under federal, state, provincial, or territorial securities laws to provide audited financial statements in connection with any sale of its securities;
- (C) The aggregate amount of all previous sales of securities by the issuer (exclusive of debt financing with banks and similar commercial lenders) shall not exceed U.S. \$1,000,000; and
- (D) The amount of the present offering does not exceed U.S. \$1,000,000.

(e) SCOR registration shall not be available to investment companies subject to the Investment Company Act, nor shall it be available to issuers subject to the reporting requirements of section 13 or 15(d) of the Securities Exchange Act. [Eff 6/30/08; am and comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-303, 485A-606)

**§16-39-353 Disqualification from use of SCOR registration.** (a) SCOR registration shall not be available for the security of any issuer if that issuer or any of its officers, directors, ten per cent shareholders, promoters or any selling agents of the security to be offered, or any officer, director, or partner of such selling agent:

- (1) Has filed an application for registration which is the subject of a currently effective registration stop order entered pursuant to any federal, state, or provincial securities law within five years prior to the filing of the SCOR registration application;
- (2) Has been convicted within five years prior to the filing of the SCOR registration



application of any felony or misdemeanor in connection with the offer, purchase, or sale of any security or any felony involving fraud or deceit; including but not limited to forgery, embezzlement, obtaining money under false pretenses, larceny, or conspiracy to defraud;

- (3) Is currently subject to any federal, state, or provincial administrative enforcement order or judgment entered by any state or provincial securities commissioner or the SEC within five years prior to the filing of the SCOR registration application;
- (4) Is subject to any federal, state, or provincial administrative enforcement order or judgment in which fraud or deceit, including but not limited to making untrue statements of material facts and omitting to state material facts, was found and the order or judgment was entered within five years prior to the filing of the SCOR registration application;
- (5) Is subject to any federal, state, or provincial administrative enforcement order or judgment which prohibits, denies, or revokes the use of any exemption from registration in connection with the offer, purchase, or sale of securities;
- (6) Is currently subject to any order, judgment, or decree of any court of competent jurisdiction temporarily, preliminarily, or permanently restrains or enjoins such party from engaging in or continuing any conduct or practice in connection with the purchase or sale of any security, or involving the making of any false filing with any state or with the SEC, entered within five years prior to the filing of the SCOR registration application; or
- (7) Has violated the law of a foreign jurisdiction governing or regulating any aspect of the business of securities or

banking or, within the past five years, has been the subject of an action of a securities regulator of a foreign jurisdiction denying, revoking, or suspending the right to engage in the business of securities as a broker-dealer, agent, or investment adviser, or investment adviser representative or is the subject of an action of any securities exchange or self-regulatory organization operating under the authority of the securities regulator of a foreign jurisdiction suspending or expelling such person from membership in the exchange or self-regulatory organization.

(b) The prohibitions of subsection (a) (1) through (3) and (a) (5) shall not apply if the person subject to the disqualification is duly licensed or registered to conduct securities-related business in the state or province in which the administrative order or judgment was entered against the person, or if the broker-dealer employing the person is licensed or registered in this State and the Form BD filed in this State discloses the order, conviction, judgment, or decree relating to the person.

(c) No person disqualified under this section may act in any capacity other than that for which the person is licensed or registered. Any disqualification under this section shall be automatically rescinded if the jurisdiction that created the basis for the disqualification determines upon a showing of good cause that it is not necessary to deny or sanction the registration. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-303, 485A-606)

**§16-39-354 Agreement by registrant on splits and dividends of stock or ownership interests.** By filing for SCOR registration in this State, the registrant agrees that it shall not split its common stock or common ownership interests, or declare a stock or

ownership interest dividend, for two years after the effective date of the registration. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-303, 485A-606)

**§16-39-355 Documents to be filed for SCOR registration.** In addition to filing a properly completed SCOR form, an applicant for SCOR registration shall file the following exhibits with the commissioner:

- (1) Form of selling agency agreement;
- (2) The issuer's articles of incorporation, articles of organization, or other charter documents, and all amendments thereto;
- (3) The issuer's bylaws or operating agreement, as amended to date;
- (4) Copies of any resolutions by directors setting forth terms and provisions of capital stock to be issued or by managers or managing members setting forth terms and provisions of capital ownership interest to be issued;
- (5) Any indenture, form of note, or other contractual provision containing terms of notes or other debt, or of options, warrants, or rights to be offered;
- (6) Specimen of security or ownership interest certificate to be offered (including any legend restricting resale);
- (7) Consent to service of process accompanied by appropriate corporate or company resolution;
- (8) Copy of all advertising or other materials directed to or to be provided to investors in the offering;
- (9) Form of escrow agreement for the escrow of proceeds;
- (10) Consent to inclusion in the disclosure document of the accountant's report;



is of good repute, and otherwise satisfies the requirements of chapter 485A, HRS, and this chapter. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-401, 485A-406)

**§16-39-402 Eligibility requirements.** (a) An applicant, if a natural person, shall have attained the age of eighteen years.

(b) A broker-dealer that is a foreign business entity that intends to establish a branch office in this State shall, in addition to the requirements under this chapter and chapter 485A, HRS, comply with the requirements of this State's business registration laws, as applicable.

(c) An applicant, except an applicant that is registered as a broker or dealer under the Securities Exchange Act, shall have a minimum net capital of not less than \$5,000 and comply with the requirements of section 16-39-404(b).

(d) A partner or an officer of a registered broker-dealer or issuer may engage in the capacity of an agent only if that person has been duly registered as provided under this chapter and chapter 485A, HRS. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-401, 485A-406)

**§16-39-403 Application.** (a) An application for registration of a broker-dealer shall be filed on Form BD, which may be filed with the commissioner directly or through the CRD. If Form BD is filed with the commissioner directly, it shall be originally executed.

(b) The application shall be filed together with the following:

- (1) The application fee specified in section 16-39-103;
- (2) Evidence of compliance with all applicable requirements of section 16-39-402; and

- (3) Financial statements consisting of either:
  - (A) A balance sheet as of a date within thirty days of filing, verified by a duly authorized officer, or the equivalent, of the applicant and notarized, or if the applicant has been engaged in business one year or more preceding, an audited financial statement as of the last fiscal year, together with a balance sheet as of a date within thirty calendar days of filing, verified by a duly authorized officer, or the equivalent, of the applicant and notarized; or
  - (B) If the applicant is registered under the Securities Exchange Act, the applicant shall include with its application a copy of its most recent annual financial statement.

(c) The commissioner may also require additional information regarding the applicant's previous history, record, and association, including without limitation the following:

- (1) Disclosure of any injunction or administrative order or conviction of a misdemeanor involving a security or any aspect of the securities business, and any conviction of a felony;
- (2) The applicant's financial condition and history;
- (3) Disclosure as to whether the broker-dealer, or any person employed by or associated in business with the broker-dealer, is subject to any disqualification which would be a basis for denial, suspension, or revocation of registration of the broker-dealer under section 485A-412, HRS; and
- (4) Any other information that the commissioner deems necessary to establish the qualifications of the applicant.

(d) Additional exhibits or information not specifically required by the application may be submitted by the applicant.

(e) The commissioner may require the applicant to file additional information if the information is necessary for the commissioner to determine whether to approve or deny the application. In accordance with the provisions of section 16-39-105, any additional information requested by the commissioner shall be requested in writing within forty-five calendar days of the commissioner's receipt of the application.

[Eff 6/30/08; am and comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-406, 485A-410)

**§16-39-404 Financial requirements.** (a) Every registered broker-dealer shall file an annual report of condition within ninety calendar days following the end of the calendar or fiscal year adopted as follows:

- (1) Broker-dealers registered under the Securities Exchange Act shall file a copy of the annual financial report filed with the SEC; and
- (2) All other broker-dealers shall file audited financial statements that evidences the broker-dealer's compliance with the requirements of subsection (b).

(b) A broker-dealer that is subject to subsection (a)(2) shall have at all times a minimum net capital of not less than \$5,000. As used in this section, "net capital" shall mean net worth, or the difference between total assets and total liabilities or indebtedness, after adjustment to eliminate or revise assets of doubtful or uncertain value and to reflect true liabilities, in accordance with the following schedule:

- (1) Asset items not allowable:
  - (A) Furniture, fixtures, and equipment; and
  - (B) Intangible items, such as goodwill, prepaid preincorporation, or organizational expenses, etc.; and

- (2) Asset items to be adjusted or substantiated:
  - (A) Securities owned shall be adjusted to market value;
  - (B) Value of real estate shall be attested to by qualified and disinterested persons;
  - (C) Property in joint ownership shall be limited to applicant's interest therein; and
  - (D) Value of unsecured notes, accounts receivable, or advanced commissions due from an agent, officer, director, partner, or affiliate may be required by the commissioner to be substantiated by an opinion of a bank, finance company, or other lending institution satisfactory to the commissioner.

(c) Broker-dealers registered in this State, who are registered with the SEC and are members of FINRA, may satisfy the annual report requirements of this section by complying with the following:

- (1) The broker-dealer files its annual audited financial report with FINRA;
- (2) The broker-dealer's annual audited financial reports filed with FINRA are current;
- (3) The broker-dealer notifies the commissioner in writing within twenty-four hours if the broker-dealer's net capital fails to meet the minimum amount required under this section;
- (4) The broker-dealer shall provide the commissioner with financial information within one business day following a request for such information from the commissioner; and
- (5) The broker-dealer shall complete the "Waiver Eligibility Certification" form. [Eff 6/30/08; am and comp ] (Auth: HRS §§485A-406 485A-411, 485A-606) (Imp: HRS §§485A-406 485A-411, 485A-606)



**§16-39-405 Sales of securities at financial institutions.** No broker-dealer shall conduct broker-dealer services on the premises of a financial institution where retail deposits are taken unless the broker-dealer complies initially and continuously with the following requirements:

- (1) Setting. Wherever practical, broker-dealer services shall be conducted in a physical location distinct from the area in which the financial institution's retail deposits are taken. In those situations where there is insufficient space to allow separate areas, the broker-dealer has a heightened responsibility to distinguish its services from those of the financial institution. In all situations, the broker-dealer shall identify its services in a manner that clearly distinguishes those services from the financial institution's retail deposit-taking activities. The broker-dealer's name shall be clearly displayed in the area in which the broker-dealer conducts its services.
- (2) Networking arrangements and program management. Networking arrangements shall be governed by a written agreement that sets forth the responsibilities of the parties and the compensation arrangements. Networking arrangements shall provide that supervisory personnel of the broker-dealer and representatives of state securities authorities, shall be permitted access to the financial institution's premises where the broker-dealer conducts broker-dealer services in order to inspect the books and records and other relevant information maintained by the broker-dealer with respect to its broker-dealer services. Management of the broker-dealer shall be responsible for ensuring that the networking arrangement clearly outlines the duties and

responsibilities of all parties, including those of the financial institution's personnel.

- (3) Customer disclosure and written acknowledgment.
  - (A) At or prior to the time that a customer's securities brokerage account is opened by a broker-dealer on the premises of a financial institution where retail deposits are taken, the broker-dealer shall:
    - (i) Disclose, orally and in writing, that the securities purchased or sold in a transaction with the broker-dealer are: not insured by the FDIC; not deposits or other obligations of the financial institution and are not guaranteed by the financial institution; and subject to investment risks, including possible loss of the principal invested[-]; and
    - (ii) Make reasonable efforts to obtain from each customer during the account opening process a written acknowledgment of the disclosures required by clause (i).
  - (B) If broker-dealer services include any written or oral representations concerning insurance coverage, other than FDIC insurance coverage, then clear and accurate written or oral explanations of the coverage must also be provided to the customers when the presentations are first made.
- (4) Communications with the public.
  - (A) All of the broker-dealer's confirmations and account statements shall indicate clearly that the broker-

dealer services are provided by the broker-dealer.

- (B) Advertisements and sales literature that announce the location of a financial institution where broker-dealer services are provided by the broker-dealer, or that are distributed by the broker-dealer on the premises of a financial institution, shall disclose that the securities: are not insured by the FDIC; are not deposits or other obligations of the financial institution and are not guaranteed by the financial institution; and are subject to investment risks, including possible loss of the principal invested. The shorter, logo format described in subparagraph (D) may be used to provide these disclosures.
- (C) Recommendations by a broker-dealer concerning non deposit investment products with a name similar to that of a financial institution shall only occur pursuant to policies and procedures reasonably designed to minimize risk of customer confusion.
- (D) The following shorter, logo format disclosures may be used by a broker-dealer in advertisements and sales literature, including material published, or designed for use, in radio or television broadcasts, automated teller machine ("ATM") screens, billboards, signs, posters and brochures, to comply with the requirements of subparagraph (B); provided that such disclosures are displayed in a conspicuous manner:
  - (i) Not FDIC insured;
  - (ii) No bank guarantee; and
  - (iii) May lose value.

- (E) As long as the omission of the disclosures required by subparagraph (B) would not cause the advertisement or sales literature to be misleading in light of the context in which the material is presented, such disclosures are not required with respect to messages contained in:
  - (i) Radio broadcasts of thirty seconds or less;
  - (ii) Electronic signs, including billboard-type signs that are electronic, time, and temperature signs and ticker tape signs, but excluding messages contained in such media as television, on-line computer services, or ATMs; and
  - (iii) Signs, such as banners and posters, when used only as location indicators.
- (5) Notification of termination. The broker-dealer shall promptly notify the financial institution if any agent of the broker-dealer who is employed by the financial institution is terminated for cause by the broker-dealer. [Eff 6/30/08; am and comp ] (Auth: HRS §§485A-406, 485A-606) (Imp: HRS §485A-406)

**§16-39-406 Books and records.** Every broker-dealer registered or required to be registered under chapter 485A, HRS, and this chapter shall prepare and maintain the books and records as described in the Securities Exchange Act, 17 CFR sections 240.17a-3 and 240.17a-4. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §485A-411)

**§16-39-407 Post-effective requirements; registration of successor broker-dealer.** (a) Every registrant shall promptly notify the commissioner of any material change in any information, exhibits, or schedules submitted, or circumstances disclosed in its last prior application, by filing a correcting amendment at the time of occurrence or discovery of the changes. Changes that shall be reported include but are not limited to the following:

- (1) Change in firm name, ownership, management, or control of a broker-dealer;
- (2) A change in any of its partners, officers, or persons in similar positions;
- (3) Change in its business address, or the creation or termination of a branch office in this State;
- (4) Change in type of business entity, general plan, or character of broker-dealer's business, method of operation or type of securities in which it is dealing or trading;
- (5) Material adverse change in financial condition, insolvency, dissolution or liquidation, or impairment of working capital, or noncompliance with the minimum net capital requirements provided in sections 16-39-402(c) and 16-39-404(b);
- (6) Termination of business or discontinuance of those activities as a broker-dealer or agent; and
- (7) The commencement of any proceeding or action that is required to be disclosed pursuant to the disciplinary questions on Form BD, including but not limited to, filing of a criminal charge or civil action against a registrant or a partner or officer in which a fraudulent, dishonest, or unethical act is alleged, or a violation of a securities law or any aspect of the securities business is involved, entry of a court or administrative order or proceeding against a registrant to deny, suspend, or revoke a registration, or

threatening to do so, or to enjoin it from engaging in or continuing any conduct or practice in the securities business, or to impose a fine, suspension, or expulsion from FINRA.

(b) Registration of successor broker-dealer. In the event that a new broker-dealer becomes the successor and continues the business of a broker-dealer registered pursuant to chapter 485A, HRS, and this chapter, the registration of the predecessor broker-dealer shall be deemed to remain effective as the registration of the successor broker-dealer only if the successor broker-dealer, within thirty days after such succession, files an application for registration on Form BD, and the predecessor broker-dealer files a notice of withdrawal from registration on Form BD-W.

- (1) The registration of the predecessor broker-dealer shall cease to be effective at such time as the application for registration on Form BD filed by the successor broker-dealer becomes effective; and
- (2) Notwithstanding any other provision of this section, if a new broker-dealer becomes the successor and continues the business of a registered broker-dealer, and the succession is based solely on a change in the predecessor broker-dealer's date or state of incorporation, form of organization, or composition of a partnership, the successor broker-dealer may, within thirty days after the succession, amend the registration of the predecessor broker-dealer on Form BD to reflect these changes. This amendment shall be deemed an application for registration filed by the predecessor broker-dealer and adopted by the successor broker-dealer.  
[Eff 6/30/08; comp \_\_\_\_\_] (Auth: HRS §485A-606) (Imp: HRS §485A-407)

**§16-39-408 Expiration, renewal, termination of registration.** (a) All registrations shall automatically expire on December 31 of each year (unless sooner terminated in accordance with chapter 485A, HRS, and this chapter) and shall be renewed as provided in this section. A broker-dealer or issuer shall be responsible for renewing the registration of its agents at the time the broker-dealer or issuer renews its registration. A member of FINRA shall renew its registration with the commissioner by filing the renewal documents and fees through the CRD. All other broker-dealers and issuers shall renew their registration by annually filing, not earlier than November 1 or later than December 1 of the current registration year, an originally executed copy of page one of Form BD together with:

- (1) All amendments to Form BD that have previously not been filed with the commissioner;
- (2) A list of all agents of the broker-dealer that are renewing their registrations for the upcoming calendar year;
- (3) A copy of all amendments to Form U-4 of all such agents if such amendments have not been previously filed with the commissioner;
- (4) A Form U-5 on each registered agent of the broker-dealer who is not renewing its agent registration; and
- (5) A renewal fee as set forth in section 16-39-103 for the broker-dealer and for each agent renewing a registration.

(b) An application for renewal registration shall not be considered filed until the required fee and all required submissions have been received by the commissioner.

(c) Where registrations are permitted to expire on December 31 without the filing of a renewal application, a subsequent application shall be considered in all respects as an initial application.

(d) Registration may be terminated prior to the expiration date by filing a Form BD-W with the commissioner or through the CRD. Termination of the

broker-dealer's registration for any reason shall automatically terminate the registration of each registered agent of the broker-dealer. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-406, 485A-408, 485A-409, 485A-410)

## B. Agents

**§16-39-420 Registration; generally.** A person may be registered as a securities agent under chapter 485A, HRS, and this chapter if the commissioner finds that the person is of good repute and otherwise satisfies the requirements of chapter 485A, HRS, and this chapter. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-402, 485A-406)

**§16-39-421 Eligibility requirements.** (a) An applicant, if a natural person, shall have attained the age of eighteen years.

(b) A broker-dealer or issuer shall submit an application with the commissioner to register an agent. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §§485A-402, 485A-406, 485A-410)

**§16-39-422 Application.** (a) An application for registration of an agent shall be filed on Form U-4, which shall be filed with the commissioner directly or through the CRD. If the broker-dealer is not registered through the CRD, an originally executed Form U-4 and fees shall be filed with the commissioner directly.

(b) The application shall be filed together with the following:



- (1) The application fee set forth in section 16-39-103; and
- (2) Evidence of compliance with section 16-39-421.

(c) The commissioner may also require additional information regarding the applicant's history, record, and association including without limitation the following:

- (1) Disclosure of any injunction or administrative order or conviction of a misdemeanor involving a security or any aspect of the securities business and any conviction of a felony;
- (2) The applicant's financial condition and history;
- (3) Disclosure as to whether the agent or any person associated in business with the agent is subject to any disqualification which would be a basis for denial, suspension, or revocation of registration of the agent under section 16-39-470 or chapter 485A, HRS; and
- (4) Any additional information that the commissioner deems necessary to establish the applicant's qualifications.

(d) All documents submitted to the commissioner shall be approved and registration shall become effective at noon on the forty-fifth calendar day after the submission of a completed application unless otherwise provided by state or federal law or unless an earlier effective date is specified by the commissioner.

(e) An agent's application that has been on file for a period of sixty calendar days with no attempt to comply with any notice of deficiency may be denied by the commissioner or withdrawn. The commissioner shall provide written notification of the denial to the broker-dealer or issuer with which the applicant is affiliated. If the application was filed through the CRD, the notification may be provided through the CRD. [Eff 6/30/08; comp ] (Auth: HRS

§§485A-402, 485A-606) (Imp: HRS §§485A-402, 485A-406, 485A-410)

**§16-39-423 Examination requirements.** (a)

Unless specifically exempt, every applicant for registration as a securities agent shall be required to pass a written examination that tests the applicant's knowledge of the securities business.

(b) The examination requirement of subsection (a) shall be deemed satisfied upon evidence to the commissioner that the applicant has passed an examination administered by FINRA that is appropriate for the type of business that will be conducted by the agent and FINRA's Uniform Securities Agent State Law Examination.

(c) An applicant who has not been registered in any jurisdiction for a period of two consecutive years immediately preceding the date of the application shall be required to comply with the examination requirements of this chapter.

(d) Notwithstanding any other provision to the contrary, the commissioner may by order waive the examination requirement if the commissioner determines that the examination is not necessary or appropriate in the public interest or for the protection of investors. [Eff 6/30/08; comp ] (Auth: HRS §§485A-406, 485A-412, 485A-606) (Imp: HRS §§485A-402, 485A-406)

**§16-39-424 Post-effective requirements.** (a)

Every applicant and registrant shall promptly file with the commissioner any and all amendments necessary to keep the information previously reported on the applicant's or registrant's Form U-4 current and accurate. If the Form U-4 being amended was filed with the commissioner through the CRD, any amendment to the form may also be filed through the CRD.

(b) Upon the receipt of an amendment, the commissioner may request additional information from the applicant or registrant to determine whether the applicant's application should be denied or the registrant's registration should be suspended or revoked. [Eff 6/30/08; comp ] (Auth: HRS §485A-606) (Imp: HRS §485A-411)

**§16-39-425 Expiration, renewal, termination of registration.**

(a) All registrations shall automatically expire on December 31 of each year (unless sooner terminated in accordance with chapter 485A, HRS, and this chapter) and shall be renewed as provided in this section.

(b) A broker-dealer or issuer shall be responsible for renewing the registration of its agents at the time the broker-dealer or issuer renews its registration.

(c) An application for renewal registration shall not be considered filed until the broker-dealer or issuer submits the following:

- (1) The renewal fee set forth in section 16-39-103; and
- (2) A copy of all amendments to Form U-4 of all such agents if the amendments have not been previously filed with the commissioner.

(d) An agent's registration may be terminated at any time prior to its expiration date by either the broker-dealer or issuer employing the agent or by the agent filing a Form U-5 with the commissioner directly or through the CRD. Termination shall be effective when the notice of termination is received by the commissioner unless another date is indicated on the Form U-5.

(e) An agent's registration shall not be transferred. When an agent terminates an affiliation with the broker-dealer or issuer with whom the agent is registered, and wishes to be employed by another broker-dealer or issuer, a notice of termination shall be filed with the commissioner. The agent may then

reapply for registration with another broker-dealer or issuer by complying with the requirements of this subchapter.

(f) The termination of any broker-dealer's or issuer's registration for any reason shall automatically terminate the registration of all agents registered thereunder.

(g) When an agent ceases the activities of an agent, or the agent otherwise becomes ineligible to be registered, a notice to terminate the registration shall be filed with the commissioner on Form U-5 by either the agent, or the broker-dealer or issuer with whom the agent is registered. The termination of the registration shall be effective upon the commissioner's receipt of such form unless another date is indicated on the Form U-5. [Eff 6/30/08; comp ] (Auth: HRS §§485A-406, 485A-606) (Imp: HRS §§485A-406, 485A-408, 485A-409)

### C. Investment Advisers

**§16-39-430 Registration; generally.** (a) A person may be registered as an investment adviser under chapter 485A, HRS, and this chapter if the commissioner finds that the applicant is of good repute and otherwise satisfies the requirements of chapter 485A, HRS, and this chapter.

(b) All services of an investment adviser shall be made pursuant to a written investment advisory contract and shall be subject to the disclosure requirements of section 16-39-439.

(c) Designation. The commissioner hereby designates the IARD to receive and store filings, and collect related fees from investment advisers and investment adviser representatives on behalf of the commissioner.

(d) Use of the IARD. Except as otherwise provided below, all investment adviser and investment adviser representative applications, amendments, reports, notices, related filings, and fees required

to be filed with the commissioner pursuant to chapter 485A, HRS, and this chapter, shall be filed electronically with and transmitted to the IARD. The following additional conditions relate to these electronic filings:

- (1) Electronic signature. When a signature or signatures are required by the particular instructions of any filing to be made through the IARD, a duly authorized officer, or the equivalent, of the applicant or the applicant him or herself, as required, shall affix his or her electronic signature to the filing by typing his or her name in the appropriate fields and submitting the filing to the IARD. Submission of a filing in this manner shall constitute irrefutable evidence of legal signature by any individuals whose names are typed on the filing;
- (2) When filed. Solely for purposes of a filing made through the IARD, a document is considered filed with the commissioner when all fees are received and the filing is accepted by the IARD on behalf of the State.

(e) Electronic filings. The electronic filing of any particular document and the collection of related processing fees shall not be required until the IARD provides for receipt of such filings and fees, and the commissioner provides at least thirty calendar days notice that electronic filing is available. Any documents or fees required to be filed with the commissioner that are not permitted to be filed with or cannot be accepted by the IARD shall be filed directly with the commissioner.

(f) Hardship exemptions. Notwithstanding subsections (d) and (e), there shall be two types of hardship exemptions from the requirements to make electronic filings:

- (1) Temporary hardship exemption.
  - (A) Investment advisers registered or required to be registered under the Investment Advisers Act who experience unanticipated technical difficulties

that prevent submission of an electronic filing to the IARD may request a temporary hardship exemption from the requirements to file electronically;

- (B) To request a temporary hardship exemption, the investment adviser shall:
    - (i) File Form ADV-H in paper format with the commissioner where the investment adviser's principal place of business is located, no later than one business day after the filing (that is the subject of the Form ADV-H) was due; and
    - (ii) Submit the filing that is the subject of the Form ADV-H in electronic format to the IARD no later than seven business days after the filing was due;
  - (C) Effective date - upon filing. The temporary hardship exemption shall be deemed effective upon receipt by the commissioner of the complete Form ADV-H. Multiple temporary hardship exemption requests within the same calendar year may be disallowed by the commissioner; and
- (2) Continuing hardship exemption.
- (A) Criteria for exemption. A continuing hardship exemption may be granted only if the investment adviser is able to demonstrate that the electronic filing requirements of this chapter are prohibitively burdensome;
  - (B) To apply for a continuing hardship exemption, the investment adviser shall:
    - (i) File Form ADV-H in paper format with the commissioner at least twenty business days before a filing is due; and

- (ii) If a filing is due to more than one commissioner, the Form ADV-H shall be filed with the commissioner where the investment adviser's principal place of business is located;
- (C) Effective date - upon approval. The continuing hardship exemption shall be deemed effective upon approval by the commissioner. The time period of the exemption shall not exceed one year after the date on which the Form ADV-H is filed. If the commissioner approves the application, the investment adviser shall, no later than five business days after the exemption approval date, submit filings to the IARD in paper format (along with the appropriate processing fees) for the period of time for which the exemption is granted.

The decision to grant or deny a request for a hardship exemption shall be made by the commissioner or authority of the state in which the investment adviser's principal place of business is located.

[Eff 6/30/08; comp ] (Auth: HRS §§ 485A-406, 485A-606) (Imp: HRS §§485A-403, 485A-406)

**§16-39-431 Notice filing for federal covered investment advisers.** (a) A federal covered investment adviser may transact business in this State upon submitting to the commissioner a notice filing and notice filing fee as set forth in section 16-39-103, unless otherwise exempt pursuant to section 485A-405, HRS. The notice filing and notice filing fee may be filed with the commissioner through the IARD.

(b) The notice filing shall consist of the federal covered investment adviser's current Form ADV on file with the SEC. The notice filing shall be effective upon receipt and shall expire December 31 of

each year. A notice filing may be renewed prior to December 31 by either:

- (1) Filing with the commissioner:
  - (A) A copy of page one of the federal covered investment adviser's most recent Form ADV;
  - (B) A copy of Item 2 of Part 1A of the federal covered investment adviser's most recent Form ADV;
  - (C) Any amendments to Form ADV that have not been previously filed with the commissioner;
  - (D) A list containing the name and social security number or the IARD number of each investment adviser representative of the adviser who is renewing its registration for the coming notice filing period together with any amendments to the investment adviser representative's Form U-4 that have not been previously filed with the commissioner;
  - (E) A Form U-5 for each registered investment adviser representative who is not renewing its registration for the upcoming notice filing period; and
  - (F) A renewal fee as specified in section 16-39-103, to cover the renewal of the federal covered investment adviser's notice filing and the registration of each of its representatives who is renewing its registration; or
- (2) Filing a renewal and renewal fees through the IARD. Any investment adviser that elects to renew its notice filing through the IARD shall be required to file directly with the commissioner any information listed in paragraph (1)(D) and (E) that have not been filed through the IARD together with any fees due under paragraph (1)(F) that have not been paid through the IARD. [Eff



6/30/08; comp ] (Auth: HRS  
§485A-606) (Imp: HRS §485A-405)

**§16-39-432 Eligibility requirements.** (a) An applicant, if a natural person, shall have attained the age of eighteen years.

(b) A partner, officer, manager, representative, or employee of a registered investment adviser may render investment advisory services only if the person meets all the requirements of and has been duly registered as an investment adviser or investment adviser representative, as provided by section 485A-404, HRS, and this chapter.

(c) A corporation, partnership, limited liability company, sole proprietorship, or other unincorporated association whose partners, officers, managers, representatives, or employees render investment advisory services as defined in section 485A-403, HRS, shall comply with registration procedures as provided by section 485A-406, HRS, and this chapter, unless otherwise exempted.

(d) An individual applying to be registered as an investment adviser shall take and pass a written examination, prescribed by the commissioner, under section 16-39-438.

(e) An applicant shall have at all times, the minimum net worth, as defined in section 16-39-433. An applicant that maintains its principal place of business in a state other than this State shall not be required to comply with the minimum net worth requirement of this section; provided that the applicant is registered in the state where it maintains its principal place of business and is in compliance with that state's net capital or net worth requirements, if any.

(f) Except as otherwise expressly provided in this subchapter, an applicant who has custody or discretionary authority over client funds or securities shall obtain a surety bond as set forth in section 16-39-434.

(g) A foreign corporation, partnership, or limited liability company intending to establish a branch office in this State shall comply with the requirements of this State's business registration laws, as applicable. [Eff 6/30/08; comp ]  
(Auth: HRS §§485A-406, 485A-606) (Imp: HRS §§485A-403, 485A-406)

**§16-39-433 Financial requirements.** (a) An investment adviser registered or required to be registered, who does not have custody of client funds or securities, and who does not have discretionary authority over client funds or securities, shall maintain a minimum net worth of \$5,000 at all times.

(b) An investment adviser registered or required to be registered, who has custody of client funds or securities shall maintain a minimum net worth of \$35,000 at all times except:

- (1) Investment advisers that have custody solely due to their authority to deduct fees from client accounts and comply with the terms described in section 16-39-436 and related books and records shall only be required to maintain a minimum net worth of \$5,000 at all times; or
- (2) Investment advisers to pooled investment vehicles that have custody solely due to the capacity in which they act in advising pooled investment vehicles and comply with the terms described in section 16-39-436 and related books and records shall only be required to maintain a minimum net worth of \$5,000 at all times.

(c) An investment adviser, registered or required to be registered, who has discretionary authority over client funds or securities, but does not have custody of client funds or securities, shall maintain a minimum net worth of \$10,000 at all times.

(d) Unless otherwise exempted, as a condition of the right to transact business in this State, every

investment adviser registered or required to be registered shall notify the commissioner if the adviser's net worth is less than the minimum required by the close of business on the next business day. After transmitting the notice, each investment adviser shall file a report with the commissioner of its financial condition by the close of business on the next business day, including the following:

- (1) A trial balance of all ledger accounts;
- (2) A statement of all client funds or securities that are not segregated;
- (3) A computation of the aggregate amount of client ledger debit balances; and
- (4) A statement as to the number of client accounts.

(e) For purposes of this chapter, the term "net worth" means an excess of assets over liabilities, as determined by generally accepted accounting principles computed in accordance with the following:

- (1) Securities owned shall be adjusted to market value;
- (2) The value of real estate shall be attested to by qualified and disinterested persons; and
- (3) Property in joint ownership shall be limited to the applicant's interest therein.

(f) For purposes of this chapter, "net worth" shall not include the following as assets:

- (1) Prepaid expenses (except as to items properly classified as assets under generally accepted accounting principles);
- (2) Deferred charges, goodwill, franchise rights, organizational expenses, patents, copyrights, marketing rights, unamortized debt discount and expense and all other intangible assets;
- (3) Homes, home furnishings, [~~automobile(s),~~] automobiles, and any other personal items not readily marketable in the case of an individual;
- (4) Advances or loans to stockholders and officers in the case of a corporation;

- (5) Advances or loans to partners in the case of a partnership; or
- (6) Advances or loans to managers or members in the case of a limited liability company.
- (g) For purposes of this section, custody shall be defined as provided in section 16-39-436.
- (h) For purposes of this section, an investment adviser shall not be deemed to be exercising discretion when the investment adviser places trade orders with a broker-dealer pursuant to a third-party trading agreement if:
  - (1) The investment adviser has executed a separate investment adviser contract exclusively with its client which acknowledges that a third-party trading agreement will be executed to allow the investment adviser to effect securities transactions for the client in the client's broker-dealer account;
  - (2) The investment adviser contract specifically states that the client does not grant discretionary authority to the investment adviser and the investment adviser in fact does not exercise discretion with respect to the account; and
  - (3) A third-party trading agreement is executed between the client and a broker-dealer which specifically limits the investment adviser's authority in the client's broker-dealer account to the placement of trade orders and deduction of investment adviser fees.
- (i) The commissioner may require that a current appraisal be submitted in order to establish the worth of any asset.
- (j) Every investment adviser that has its principal place of business in a state other than this State shall be required to maintain only such minimum net worth as required by the state in which the investment adviser maintains its principal place of business, provided that the investment adviser is licensed in such state and is in compliance with such state's minimum net worth requirements, if any. [Eff

6/30/08; am and comp ] (Auth: HRS  
§§485A-406, 485A-411, 485A-606) (Imp: HRS §§485A-  
406, 485A-411)

**§16-39-434 Bonding requirements for certain investment advisers.** (a) Any investment adviser bond required under this chapter and chapter 485A, HRS, shall be issued by a surety company qualified to do business in this State with the State as obligee, and shall be subject to the claims of all clients of such investment adviser regardless of the client's state of residence.

(1) Every investment adviser registered or required to be registered under this chapter and chapter 485A, HRS, having custody of or discretionary authority over client funds or securities shall be bonded in the amount of \$50,000.

(2) Every investment adviser registered or required to be registered under this chapter and chapter 485A, HRS, who has custody of or discretionary authority over client funds or securities and who does not meet the minimum net worth requirements prescribed in section 16-39-433 shall be bonded in the amount of the net worth deficiency rounded up to the nearest \$5,000.

(b) For purposes of this section, "custody" shall be as defined in section 16-39-436.

(c) An investment adviser that has its principal place of business in a state other than this State shall be exempt from the requirements of subsection (a), provided that the investment adviser is registered as an investment adviser in the state where the investment adviser has its principal place of business and is in compliance with such state's bonding requirements. [Eff 6/30/08; comp ]  
(Auth: HRS §§485A-411, 485A-606) (Imp: HRS §485A-411)

**§16-39-435 Application.** (a) Except as permitted by section 16 39 430(f), an application for registration shall be filed on Form ADV through the IARD and shall contain the information requested therein concerning the applicant's identification, qualification, business association, history, experience, and financial condition.

(b) The application shall be filed together with the following:

(1) The application fee set forth in section 16-39-103;

(2) Evidence of compliance with all applicable requirements of section 16-39-432(d) to (g);

(3) Financial statements consisting of either:

(A) A balance sheet as of a date within thirty calendar days of filing, verified by a duly authorized officer, or the equivalent, of the applicant and notarized, or if the applicant has been engaged in business one year or more preceding, an audited financial statement as of the last fiscal year, together with a balance sheet as of a date within thirty calendar days of filing, verified by a duly authorized officer, or the equivalent, of the applicant and notarized. However, if the applicant does not have custody or discretionary authority over client funds, the adviser need only file financial statements verified by a duly authorized officer, or the equivalent, of the applicant and notarized; or

(B) If the investment adviser maintains its principal place of business in a state other than this State, and if the investment adviser is registered in the other state and is in compliance with the other state's financial reporting requirements, if any, a copy of the

adviser's most recent financial statement filed with the state where the adviser maintains its principal place of business; and

- (4) Proof that the applicant, if an individual, has complied with the examination requirement provided in section 16-39-438, or otherwise qualifies for exemption from the examination as specified in section 16 39-438.

(c) The commissioner may also require additional information regarding the applicant's previous history, record, and association, including without limitation the following:

- (1) Disclosure of any injunction or administrative order or conviction of a misdemeanor involving a security or any aspect of the securities business, and any conviction of a felony;
- (2) The applicant's financial condition and history;
- (3) Disclosure as to whether the investment adviser, or any person employed by or associated in business with the investment adviser, is subject to any disqualification which would be a basis for denial, suspension, or revocation of registration of the investment adviser under section 485A-412, HRS; and
- (4) Any other information that the commissioner deems necessary to establish the applicant's qualifications.

(d) Additional exhibits or information not specifically required by the application may be submitted by the applicant.

(e) The commissioner may require the applicant to file additional information if such information is necessary for the commissioner to determine whether to approve or deny the application. In accordance with the provisions of section 16-39-105, any additional information requested by the commissioner shall be

requested by the commissioner in writing within forty-five calendar days of receipt of the application.

(f) An application for initial registration shall not be considered filed until the required fee and all required submissions have been received by the commissioner. [Eff 6/30/08; comp ]  
(Auth: HRS §§485A-403, 485A-406, 485A-410, 485A-411, 485A-606) (Imp: HRS §§485A-403, 485A-406, 485A-410, 485A-411)

**§16-39-436 Custody of client funds or securities by investment advisers.** (a) Safekeeping required.

It shall be unlawful and deemed to be a fraudulent, deceptive, or manipulative act, practice, or course of business for an investment adviser that is registered or required to be registered to have custody of client funds or securities unless:

- (1) Notice to commissioner. The investment adviser shall notify the commissioner promptly in writing that the investment adviser has or may have custody. Such notification is also required to be given on Form ADV through the IARD;
- (2) Qualified custodian. A qualified custodian maintains those funds and securities:
  - (A) In a separate account for each client under that client's name; or
  - (B) In accounts that contain only the client's funds and securities, under the investment adviser's name as agent or trustee for the client;
- (3) Notice to clients. If the investment adviser opens an account with a qualified custodian on the client's behalf, either under the client's name or under the investment adviser's name as agent, the investment adviser shall notify the client in writing of the qualified custodian's name, address, and the manner in which the funds or securities are maintained, promptly



when the account is opened and following any changes to this information;

(4) Account statements shall be sent to clients, either:

(A) By a qualified custodian. The investment adviser shall have a reasonable basis for believing that the qualified custodian sends an account statement, at least quarterly, to each of the investment adviser's clients for which it maintains funds or securities, identifying the amount of funds and of each security in the account at the end of the period and setting forth all transactions in the account during that period; or

(B) By the investment adviser.

(i) The investment adviser shall send an account statement, at least quarterly, to each client for whom the investment adviser has custody of funds or securities, identifying the amount of funds and of each security of which the investment adviser has custody at the end of the period and setting forth all transactions during that period;

(ii) An independent certified public accountant shall verify all client funds and securities by actual examination at least once during each calendar year at a time chosen by the accountant without prior notice or announcement to the investment adviser and that is irregular from year to year, and shall file a copy of the auditors report and financial statements with the commissioner within

- thirty calendar days after the completion of the examination, along with a letter stating that it has examined the funds and securities and describing the nature and extent of the examination, and
- (iii) The independent certified public accountant, upon finding any material discrepancies during the course of the examination, shall notify the commissioner of the discrepancies within one business day of the finding, by means of a facsimile transmission or electronic mail, followed by first class mail, directed to the attention of the commissioner;
  - (C) Special rule for limited partnerships and limited liability companies. If the investment adviser is a general partner of a limited partnership or managing member of a limited liability company, or holds a comparable position for another type of pooled investment vehicle, the account statements required under paragraph (4) shall be sent to each limited partner or member, or other beneficial owner or their independent representative;
  - (5) Independent representatives. A client may designate an independent representative to receive, on the client's behalf, notices and account statements as required under paragraphs (3) and (4);
  - (6) Direct fee deduction. An investment adviser who has custody by having the authority to deduct fees directly deducted from client accounts shall provide the following safeguards:

- (A) Written authorization. The investment adviser shall have written authorization from the client to deduct advisory fees from the account held with the qualified custodian;
- (B) Notice of fee deduction. Each time a fee is directly deducted from a client account, the investment adviser shall concurrently:
  - (i) Send the qualified custodian an invoice of the amount of the fee to be deducted from the client's account; and
  - (ii) Send the client an invoice itemizing the fee. Such itemization shall include the formula used to calculate the fee, the amount of assets under management the fee is based on, and the time period covered by the fee;
- (C) Notice of safeguards. The investment adviser shall notify the commissioner in writing that the investment adviser intends to use the safeguards required under this section. Such notification shall be given on Form ADV[-]i;
- (D) Waiver of net worth, bonding and audited financial statement requirements. An investment adviser having custody solely because the investment adviser meets the definition of custody as defined under this section and who complies with the safekeeping requirements in paragraphs (1) through (6) shall not be required to meet the financial requirements for an investment adviser with custody as provided in section 16-39-433, the bonding requirement set forth in section 16-39-434, and the audited

financial statement requirement set forth in section 16-39-437;

- (7) Pooled investments. An investment adviser to pooled investment vehicles who has custody and who does not meet the exception provided in subsection (b)(3) shall, in addition to the safeguards set forth in paragraphs (1) through (5), comply with the following:
- (A) Engage an independent party. Hire an independent party to review all fees, expenses, and capital withdrawals from the pooled investment accounts;
  - (B) Review of fees. Send all invoices or receipts to the independent party, detailing the amount of the fee, expenses or capital withdrawal, and the method of calculation such that the independent party can:
    - (i) Determine that the payment is in accordance with the pooled investment vehicle standards (generally, the partnership agreement or membership agreement); and
    - (ii) Forward, to the qualified custodian, approval for payment of the invoice with a copy to the investment adviser;
  - (C) For purposes of this section, an "independent party" means a person that:
    - (i) Is engaged by the investment adviser to act as a gatekeeper for the payment of fees, expenses, and capital withdrawals from the pooled investment;
    - (ii) Does not control and is not controlled by, and is not under common control with the investment adviser; and

- (iii) Does not have, and has not had within the past two years, a material business relationship with the investment adviser;
  - (D) Notice of safeguards. The investment adviser shall notify the commissioner in writing that the investment adviser intends to use the safeguards required under this section. The notification shall be given on Form ADV;
  - (E) Waiver of net worth, bonding and audited financial statement requirements. An investment adviser having custody solely because the investment adviser meets the definition of custody as defined under this section and who complies with the safekeeping requirements in paragraphs (1) through (5) and (7) shall not be required to meet the financial requirements for an investment adviser with custody as provided in section 16-39-433, the bonding requirement set forth in section 16-39-434, and the audited financial statement requirement set forth in section 16-39-437;
- (8) Investment adviser or investment adviser representative as trustee. When a trust retains an investment adviser, investment adviser representative, or employee, director, or owner of an investment adviser as trustee and the investment adviser acts as the investment adviser to that trust, the investment adviser shall:
- (A) Notify the commissioner in writing that the investment adviser intends to use the safeguards required under this section. The notification shall be given on Form ADV;
  - (B) Send to the grantor of the trust, the attorney for the trust if it is a testamentary trust, the co-trustee

(other than the investment adviser, investment adviser representative, or employee, director, or owner of the investment adviser); or a defined beneficiary of the trust, at the same time that it sends any invoice to the qualified custodian, an invoice showing the amount of the trustees' fee or investment management or advisory fee, the value of the assets on which the fees were based, and the specific manner in which the fees were calculated;

- (C) Enter into a written agreement with a qualified custodian which specifies:
  - (i) That the qualified custodian shall not deliver trust securities to the investment adviser, any investment adviser representative or employee, director, or owner of the investment adviser; nor transmit any funds to the investment adviser, any investment adviser representative or employee, director or owner of the investment adviser, except that the qualified custodian may pay trustee fees to the trustee and investment management or advisory fees to investment adviser; provided that:
    - (A) The grantor of the trust or attorneys for the trust, if it is a testamentary trust, the co trustee (other than the investment adviser, investment adviser representative, or employee, director, or owner of the investment adviser); or a defined

beneficiary of the trust has authorized the qualified custodian in writing to pay those fees;

- (B) The statements for those fees show the amount of the fees for the trustee and, in the case of statements for investment management or advisory fees, show the value of the trust assets on which the fee is based and the manner in which the fee was calculated; and
- (C) The qualified custodian agrees to send to the grantor of the trust, the attorneys for a testamentary trust, the co-trustee (other than the investment adviser, investment adviser representative, or employee, director or owner of the investment adviser); or a defined beneficiary of the trust, at least quarterly, a statement of all disbursements from the account of the trust, including the amount of investment management fees paid to the investment adviser and the amount of trustees' fees paid to the trustee;

- (ii) Except as otherwise set forth below in subparagraph (8)(C)(ii)(A), the qualified custodian may transfer funds or securities, or both, of the trust only upon the direction of

the trustee (who may be the investment adviser, investment adviser representative, or employee, director, or owner of the investment adviser), who the investment adviser has duly accepted as an authorized signatory. The grantor of the trust or attorneys for the trust, if it is a testamentary trust, the co-trustee (other than the investment adviser, investment adviser representative, or employee, director, or owner of the investment adviser); or a defined beneficiary of the trust, shall designate the authorized signatory for management of the trust. The direction to transfer funds or securities, or both, can only be made to the following:

- (A) A trust company, bank trust department or brokerage firm independent of the investment adviser for the account of the trust to which the assets relate;
- (B) The named grantors or to the named beneficiaries of the trust;
- (C) A third person who is independent of the investment adviser with respect to payment of the fees or charges of the third person including, but not limited to: attorney's, accountant's, or qualified custodian's fees for the trust; and taxes, interest,



maintenance or other expenses, if there is property other than securities or cash owned by the trust;

(D) Third persons independent of the investment adviser for any other purpose legitimately associated with the management of the trust; or

(E) A broker-dealer in the normal course of portfolio purchases and sales; provided that the transfer is made on payment against delivery basis or payment against trust receipt;

(D) Waiver of net worth, bonding and audited financial statement requirements. An investment adviser having custody solely because the investment adviser meets the definition of custody as defined under this section and who complies with the safekeeping requirements in paragraphs (1) through (5) and (8) shall not be required to meet the financial requirements for an investment adviser with custody as provided in section 16-39-433, the bonding requirement set forth in section 16 39-434 and the audited financial statement requirement set forth in section 16-39-437.

(b) Exceptions.

(1) Shares of mutual funds. With respect to shares of an open-end company as defined in section 5(a)(1) of the Investment Company Act ("mutual fund"), the investment adviser may use the mutual fund's transfer agent in lieu of a qualified custodian for purposes of complying with the requirements of subsection (a);

- (2) Certain privately offered securities.
  - (A) An investment adviser shall not be required to comply with the requirements of subsection (a) with respect to securities that are:
    - (i) Acquired from the issuer in a transaction or chain of transactions not involving any public offering;
    - (ii) Uncertificated, and ownership thereof is recorded only on books of the issuer or its transfer agent in the name of the client; and
    - (iii) Transferable only with prior consent of the issuer or holders of the outstanding securities of the issuer.
  - (B) Notwithstanding subparagraph (A), the provisions of paragraph (2) are available with respect to securities held for the account of a limited partnership (or limited liability company, or other type of pooled investment vehicle) only if the limited partnership is audited, the audited financial statements are distributed, as described in paragraph (3) and the investment adviser notifies the commissioner in writing that the investment adviser intends to provide audited financial statements, as described above. The notification shall be given on Form ADV;
- (3) Limited partnerships subject to annual audit. An investment adviser shall not be required to comply with paragraph (4) with respect to the account of a limited partnership (or limited liability company, or another type of pooled investment vehicle) that is subject to audit at least annually and distributes its audited financial statements prepared in accordance with generally accepted accounting principles to all limited partners (or members or other beneficial owners) within one hundred twenty calendar days after the end of its fiscal year. The investment adviser shall also notify the commissioner in

writing that the investment adviser intends to employ the use of the audit safeguards described above. The notification is required to be given on Form ADV;

- (4) Registered investment companies. The investment adviser shall not be required to comply with this section with respect to the account of an investment company registered under the Investment Company Act;
- (5) Beneficial trusts. The investment adviser shall not be required to comply with safekeeping requirements of subsection (a) or the net worth requirement set forth in section 16-39-433 and the bonding requirements set forth in section 16 39 434 if the investment adviser has custody solely because the investment adviser, investment adviser representative, or employee, director, or owner of the investment adviser is a trustee for a beneficial trust, if all of the following conditions are met for each trust:
  - (A) The beneficial owner of the trust is a parent, grandparent, spouse, sibling, child, or grandchild of the trustee. These relationships shall include "step" relationships.
  - (B) For each account under subparagraph (A), the investment adviser shall comply with the following:
    - (i) The investment adviser shall provide a written statement to each beneficial owner of the account setting forth a description of the requirements of subsection (a) and the reasons why the investment adviser will not be complying with those requirements;
    - (ii) The investment adviser obtains from each beneficial owner a signed and dated statement acknowledging the receipt of the written statement required under clause (i); and

- (iii) The investment adviser maintains a copy of both documents described in clauses (i) and (ii) until the account is closed or the investment adviser is no longer the trustee;
- (6) Any investment adviser who intends to have custody of client funds or securities but is not able to utilize a qualified custodian as defined in subsection (c) shall first obtain approval from the commissioner and shall comply with all of the applicable safekeeping provisions under subsection (a), including taking responsibility for those provisions that are designated to be performed by a qualified custodian.
- (c) Definitions. For purposes of this section:
  - "Custody" means holding directly or indirectly, client funds or securities, or having any authority to obtain possession of them. Custody includes:
    - (1) Possession of client funds or securities unless received inadvertently and returned to the sender promptly, but in any case within three business days of receiving them;
    - (2) Any arrangement (including a general power of attorney) under which the investment adviser is authorized or permitted to withdraw client funds or securities maintained with a custodian upon the investment adviser's instruction to the custodian; and
    - (3) Any capacity (such as general partner or a limited partnership, managing member of a limited liability company or a comparable position for another type of pooled investment vehicle, or trustee of a trust) that gives the investment adviser or investment adviser's supervised person legal ownership of or access to client funds or securities;

Receipt of checks or securities drawn by clients and made payable to unrelated third parties shall not meet the definition of custody if forwarded to the third party within twenty-four hours of receipt and the adviser maintains the records required under section 16-39-442;

- "Independent representative" means a person who:
- (1) Acts as an agent for an advisory client, including in the case of a pooled investment vehicle, for limited partners of a limited partnership, members of a limited liability company, or other beneficial owners of another type of pooled investment vehicle and by law or contract is obligated to act in the best interest of the advisory client or the limited partners, members, or other beneficial owners;
  - (2) Does not control, is not controlled by, and is not under common control with the investment adviser; and
  - (3) Does not have, and has not had within the past two years, a material business relationship with the investment adviser.

"Qualified custodian" means the following independent institutions or entities that are not affiliated with the investment adviser by any direct or indirect common control and have not had a material business relationship with the adviser in the previous two years:

- (1) A bank or savings association that has deposits insured by the FDIC under the Federal Deposit Insurance Act;
  - (2) A registered broker-dealer holding the client assets in customer accounts;
  - (3) A registered futures commission merchant registered under section 4f(a) of the Commodity Exchange Act, holding the client assets in customer accounts, but only with respect to clients' funds and security futures, or other securities incidental to transactions in contracts for the purchase or sale of a commodity for future delivery and options thereon; and
  - (4) A foreign financial institution that customarily holds financial assets for its customers, provided that the foreign financial institution keeps the advisory clients' assets in customer accounts segregated from its proprietary assets.
- [Eff 6/30/08; am and comp ] (Auth: HRS §§485A-411, 485A-606) (Imp: HRS §485A-411)

**§16-39-437 Annual financial reporting**

**requirements.** (a) Every registered investment adviser shall file an annual report within ninety calendar days following the end of the investment adviser's fiscal year as follows:

- (1) An investment adviser that maintains its principal place of business in this State shall file audited financial statements; however, if an investment adviser does not have custody or discretionary authority over client funds, the investment adviser shall file financial statements verified by a duly authorized officer, or the equivalent, of the investment adviser and notarized. Any statement that does not adequately reflect the applicant's true financial picture shall not be accepted; and
  - (2) An investment adviser that maintains its principal place of business in a state other than this State shall file with the commissioner a copy of the most recent financial report or statement, if any, that the investment adviser has filed with the securities commissioner in the state in which it maintains its principal place of business. An investment adviser that maintains its principal place of business in a state other than this State but that is not registered in the state in which it maintains its principal place of business or is not in compliance with that state's financial reporting requirements, if any, shall be required to file with the commissioner financial statements that comply with the requirements of paragraph (1).
- (b) Except as otherwise provided in subsection (d), each registered investment adviser shall have at

all times a minimum net worth specified in section 16-39-433.

(c) To ensure the investment adviser's compliance with section 16-39-433 and this section, the commissioner may require that the value of unsecured notes, accounts receivable, or advanced commissions due from an agent, officer, director, partner, or affiliate be substantiated by an opinion of a bank, finance company, or other lending institution satisfactory to the commissioner.

(d) The provisions of subsections (b) and (c) shall not apply to an investment adviser that maintains its principal place of business in another state; provided that the investment adviser is registered in the state where it maintains its principal place of business and is in compliance with that state's net worth or net capital requirements, if any. [Eff 6/30/08; am and comp ]  
(Auth: HRS §§ 485A-411, 485A-606) (Imp: HRS §485A-411)

**§16-39-438 Examination requirements. (a)**

Examination requirements. Except as otherwise provided in this chapter, an individual applying to be registered as an investment adviser shall provide the commissioner with proof of obtaining a passing examination score or scores as follows:

- (1) The Uniform Investment Adviser Law Examination (Series 65 examination); or
- (2) The General Securities Representative Examination (Series 7 examination) and the Uniform Combined State Law Examination (Series 66 examination).

(b) An individual who has not been registered in any jurisdiction for a period of two consecutive years immediately preceding the date of the application shall be required to comply with the examination requirements of this section.

(c) Any investment adviser who fails to renew his or her registration for two or more consecutive

years, or who has not registered in any other jurisdiction for two or more consecutive years since passing a qualifying examination approved by the commissioner, shall be required to apply as a new applicant and comply with the examination requirements of this section.

(d) Exemptions.

(1) Any individual who is registered as an investment adviser or investment adviser representative in any jurisdiction in the United States on July 1, 2008 shall not be required to satisfy the examination requirements for continued registration; provided that the commissioner may require additional examinations for any individual found to have violated any state or federal securities law;

(2) Waivers. The examination requirement shall not apply to an individual who currently holds one of the following professional designations:

(A) Certified Financial Planner (CFP) awarded by the Certified Financial Planner Board of Standards, Inc.;

(B) Chartered Financial Consultant (ChFC) awarded by the American College, Bryn Mawr, Pennsylvania;

(C) Personal Financial Specialist (PFS) awarded by the American Institute of Certified Public Accountants;

(D) Chartered Financial Analyst (CFA) awarded by the Institute of Chartered Financial Analysts;

(E) Chartered Investment Counselor (CIC) awarded by the Investment Counsel Association of America, Inc.; or

(F) Such other professional designation as the commissioner may by rule or order recognize.

(e) Notwithstanding any other provision to the contrary, the commissioner, by order, may waive the examination requirement if the commissioner determines



that the examination is not necessary or appropriate in the public interest or for the protection of investors. [Eff 6/30/08; comp ] (Auth: HRS §§485A-403, 485A-406, 485A-412, 485A-606) (Imp: HRS §§485A-403, 485A-406)

**§16-39-439 Disclosure statements.** Unless waived by the commissioner, every investment adviser that is registered or required to be registered under chapter 485A, HRS, and this chapter shall furnish each advisory client and prospective advisory client with a written disclosure statement that complies with the provisions of the Investment Advisers Act, 17 CFR section 275.204-3, notwithstanding the fact that the investment adviser is not registered or required to be registered under the Investment Advisers Act. The delivery and updating of the disclosure statement required by this section shall be done in accordance with the requirements of Investment Advisers Act, 17 CFR section 275.204-3. [Eff 6/30/08; comp ] (Auth: HRS §§485A-403, 485A-406, 485A-411, 485A-502, 485A-606) (Imp: HRS §§485A-403, 485A-406, 485A-411, 485A-502)

**§16-39-440 Post-effective requirements.** (a) Every registrant shall promptly notify the commissioner of any material change in any information, exhibits, or schedules submitted, or circumstances disclosed in its last prior Form ADV by filing a correcting amendment on Form ADV. Changes to be reported shall include, but are not limited to, the following:

- (1) Change in firm name, ownership, management, or control of an investment adviser;
- (2) Change in any of its partners, officers, or persons in similar positions;

- (3) Change in its business address, or the creation or termination of a branch office in this State;
- (4) Change in type of entity, general plan, or character of the investment adviser's business, method of operation, or type of securities in which it is dealing or trading;
- (5) Material adverse change in financial condition, insolvency, dissolution, or liquidation, or impairment of working capital, or noncompliance with the minimum net worth or bond requirements hereinabove provided; and
- (6) The filing of any disciplinary proceeding that is required to be disclosed on Form ADV, including but not limited to, a criminal charge or civil action against a registrant or a partner, officer, or employee who acts as an investment adviser in which a fraudulent, dishonest, or unethical act is alleged, or a violation of a securities law or any aspect of the securities business is involved or entry of a court or administrative order or proceeding against a registrant to deny, suspend, or revoke a registration, or threatening to do so, or to enjoin it from engaging in or continuing any conduct or practice in the securities business, or to impose a fine, suspension, or expulsion from FINRA.

(b) Registration of successor to registered investment adviser. In the event that a new investment adviser becomes the successor and continues the business of an investment adviser registered pursuant to section 16-39-430, the registration of the predecessor investment adviser shall be deemed to remain effective as the registration of the successor investment adviser if the successor investment adviser, within thirty calendar days after such succession, files an application for registration on

Form ADV, and the predecessor investment adviser files a notice of withdrawal from registration on Form ADV-W.

- (1) The registration of the predecessor investment adviser shall cease to be effective at such time as the application for registration on Form ADV filed by the successor investment adviser becomes effective; and
- (2) Notwithstanding any other provision of this section, if an investment adviser succeeds to and continues the business of a registered investment adviser, and the succession is based solely on a change in the predecessor investment adviser's date or state of incorporation, form of organization, or composition of a partnership, the successor investment adviser shall, within thirty calendar days after the succession, amend the registration of the predecessor investment adviser on Form ADV to reflect these changes. This amendment shall be deemed an application for registration filed by the predecessor investment adviser and adopted by the successor investment adviser. [Eff 6/30/08; comp ] (Auth: HRS §§485A-411, 485A-606) (Imp: HRS §§ 485A-407, 485A-409, 485A-411)

**§16-39-441 Expiration, renewal, termination of registration.** (a) All registrations shall automatically expire on December 31 of each year (unless sooner terminated in accordance with chapter 485A, HRS, and this chapter) and shall be renewed as provided in this section. An investment adviser shall be responsible for renewing the registration of its investment adviser representatives at the time the investment adviser renews its registration. An investment adviser shall renew its registration with

the commissioner by filing the renewal documents and fees through the IARD. The renewal documents shall include:

- (1) All amendments to Form ADV and Form U-4 that have not previously been filed with the commissioner;
- (2) The renewal fee as set forth in section 16-39-103 for the investment adviser and for each investment adviser representative renewing a registration.

(b) An application for renewal registration shall not be considered filed until the required fee and all required submissions have been received by the commissioner.

(c) A copy of all amendments to Form ADV that have previously been filed shall be submitted directly to the commissioner.

(d) Where registrations are permitted to expire on December 31 without the filing of a renewal application, a subsequent application shall be considered in all respects as an initial application.

(e) Registration may be terminated prior to the expiration date by filing a Form ADV-W with the commissioner or through the IARD. Termination of the investment adviser's registration for any reason shall automatically terminate the registration of each registered investment adviser representative of the investment adviser. [Eff 6/30/08; comp ] (Auth: HRS §§485A-406, 485A-606) (Imp: HRS §§ 485A-406, 485A-409, 485A-606)

**§16-39-442 Books and records.** (a) Every investment adviser registered or required to be registered under chapter 485A, HRS, and this chapter shall make and keep true, accurate, and current books and records in compliance with the Investment Advisers Act, 17 CFR section 275.204-2. In addition, investment advisers who have custody, as that term is defined in section 16-39-436, of client funds or

securities, shall keep all records and evidence of compliance required by section 16-39-436.

(b) An investment adviser subject to subsection (a), before ceasing to conduct or discontinuing business as an investment adviser shall arrange for and be responsible for the preservation of the books and records required to be maintained and preserved under this section for the remainder of the period specified in this section, and shall notify the commissioner in writing of the exact address where such books and records shall be maintained during such period.

(c) To the extent that the SEC promulgates changes to the rules of the Investment Advisers Act referenced in subsection (a), investment advisers in compliance with such rules as amended shall not be subject to enforcement action by the commissioner for violation of this section to the extent that the violation results solely from the investment adviser's compliance with the amended rule.

(d) Every investment adviser that has its principal place of business in a state other than this State shall be exempt from the requirements of this section; provided the investment adviser is licensed in such state and is in compliance with the state's recordkeeping requirements. [Eff 6/30/08; comp ] (Auth: HRS §§485A-406, 485A-411, 485A-606) (Imp: §485A-411)

#### D. Investment Adviser Representatives

**§16-39-450 Registration; generally.** A person may be registered as an investment adviser representative under chapter 485A, HRS, if the commissioner finds that the applicant is of good repute and otherwise satisfies the requirements of chapter 485A, HRS, and this chapter. [Eff 6/30/08; comp ] (Auth: HRS §§485A-406, 485A-606) (Imp: HRS §§485A-404, 485A-406)

**§16-39-451 Eligibility requirements.** (a) An applicant, if a natural person, shall have attained the age of eighteen years.

(b) An investment adviser shall submit an application with the commissioner to register an investment adviser representative. [Eff 6/30/08; comp ] (Auth: HRS §§485A-406, 485A-606) (Imp: HRS §§485A-404, 485A-406)

**§16-39-452 Application.** (a) An application for registration of an investment adviser representative shall be filed on Form U-4 through the IARD.

(b) The application shall be filed together with the following:

- (1) The application fee set forth in section 16-39-103; and
- (2) Evidence of compliance with section 16-39-451.

(c) The commissioner may also require additional information regarding the applicant's history, record, and association, including without limitation the following:

- (1) Disclosure of any injunction or administrative order or conviction of a misdemeanor involving a security or any aspect of the securities business and any conviction of a felony;
- (2) The applicant's financial condition and history;
- (3) Disclosure as to whether the investment adviser representative or any person associated in business with the investment adviser representative is subject to any disqualification which would be a basis for denial, suspension, or revocation of registration of the agent under section 16-39-470 or chapter 485A, HRS; and

(4) Any additional information that the commissioner deems necessary to establish the applicant's qualifications.

(d) All documents submitted to the commissioner shall be approved and registration shall become effective at noon on the forty-fifth calendar day after the submission of a completed application unless otherwise provided by State or federal law or unless an earlier effective date is specified by the commissioner.

(e) An investment adviser representative's application that has been on file for a period of sixty calendar days with no attempt to comply with any notice of deficiency may be denied by the commissioner or withdrawn. The commissioner shall provide written notification of the denial to the investment adviser with which the applicant is affiliated. If the application was filed through the IARD, the notification may be provided through the IARD.

(f) The termination of any investment adviser's registration for any reason shall automatically terminate the registration of all investment adviser representatives registered thereunder.

(g) When an investment adviser representative ceases the activities of an investment adviser representative, or the investment adviser representative otherwise becomes ineligible to be registered, a notice to terminate the registration shall be filed with the commissioner on Form U-5 by either the investment adviser representative or the investment adviser with whom the investment adviser representative is registered. The termination of the registration shall be effective upon the commissioner's receipt of such form unless another date is indicated on the Form U-5. [Eff 6/30/08; comp ] (Auth: HRS §§485A-406, 485A-606) (Imp: HRS §§485A-406, 485A-408, 485A-409)

**§16-39-453 Examination requirements.** (a) Unless specifically exempt, every applicant for

registration as an investment adviser representative shall provide the commissioner with proof of obtaining a passing score or scores on the following examinations:

- (1) The Uniform Investment Adviser Law Examination (Series 65 examination); or
- (2) The General Securities Representative Examination (Series 7 examination) and the Uniform Combined State Law Examination (Series 66 examination).

(b) An applicant who has not been registered in any jurisdiction for a period of two consecutive years immediately preceding the date of the application shall be required to comply with the examination requirements of this section.

(c) Any investment adviser representative who fails to renew his or her registration for two or more consecutive years, or who has not registered for two or more consecutive years since passing a qualifying examination as approved by the commissioner, shall be required to apply as a new applicant and comply with the examination requirements of this section.

(d) Exemptions.

- (1) Any individual who is registered as an investment adviser or investment adviser representative in any jurisdiction in the United States on July 1, 2008 shall not be required to satisfy the examination requirements for continued registration; provided that the commissioner may require additional examinations for any individual found to have violated any state or federal securities law.
- (2) Waivers. The examination requirement shall not apply to an individual who currently holds one of the following professional designations:
  - (A) Certified Financial Planner (CFP) awarded by the Certified Financial Planner Board of Standards, Inc.;



- (B) Chartered Financial Consultant (ChFC) awarded by the American College, Bryn Mawr, Pennsylvania;
- (C) Personal Financial Specialist (PFS) awarded by the American Institute of Certified Public Accountants;
- (D) Chartered Financial Analyst (CFA) awarded by the Institute of Chartered Financial Analysts;
- (E) Chartered Investment Counselor (CIC) awarded by the Investment Counsel Association of America, Inc.; or
- (F) Such other professional designation as the commissioner may by rule or order recognize.

(e) Notwithstanding any other provision to the contrary, the commissioner, by order, may waive the examination requirement if the commissioner determines that the examination is not necessary or appropriate in the public interest or for the protection of investors. [Eff 6/30/08; comp \_\_\_\_\_] (Auth: HRS §§485A-404, 485A-406, 485A-412, 485A-606) (Imp: HRS §§485A-404, 485A-406)

**§16-39-454 Post-effective requirements.** (a)

Every applicant and every registrant shall promptly file with the commissioner any and all amendments necessary to keep the information previously reported on the applicant's or registrant's Form U-4 current and accurate. If the Form U-4 being amended was filed with the commissioner through the CRD or IARD, any amendment to the Form U-4 may also be filed through the CRD or IARD.

(b) Upon the receipt of the amendment, the commissioner may request additional information from the applicant or registrant to determine whether the applicant's application should be denied, or the registrant's registration should be suspended or revoked. [Eff 6/30/08; comp \_\_\_\_\_] (Auth:

HRS §§485A-411, 485A-606) (Imp: HRS §§485A-404, 485A-409, 485A-411)

**§16-39-454.5 Continuing education requirements.**

(a) Investment adviser representative continuing education. Every investment adviser representative registered under chapter 485A, HRS, must complete the following IAR continuing education requirements each Reporting Period:

- (1) IAR Ethics and Professional Responsibility Requirement. An investment adviser representative must complete six Credits of IAR Regulatory and Ethics Content offered by an Authorized Provider, with at least three Credits covering the topic of ethics; and
- (2) IAR Products and Practice Requirement. An investment adviser representative must complete six Credits of IAR Products and Practice Content offered by an Authorized Provider.

(b) Agent of FINRA-registered broker-dealer compliance. An investment adviser representative who is also registered as an agent of a FINRA member broker-dealer and who complies with FINRA's continuing education requirements is considered to be in compliance with the subrule (a) (2) IAR Products and Practice Requirement for each applicable Reporting Period so long as the FINRA continuing education content meets all of the following baseline criteria as determined by NASAA:

- (1) The continuing education content focuses on compliance, regulatory, ethical, and sales practices standards;
- (2) The continuing education content is derived from state and federal investment advisory statutes, rules and regulations, securities industry rules and regulations, and accepted standards and practices in the financial services industry; and

(3) The continuing education content requires that its participants demonstrate proficiency in the subject matter of the educational materials.

(c) Credentialing organization continuing education compliance. Credits of continuing education completed by an investment adviser representative who was awarded and currently holds a credential that qualifies for an examination waiver under section 16-39-453 complies with subsection (a) (1) and (a) (2) provided all of the following are true:

- (1) The investment adviser representative completes the credits of continuing education as a condition of maintaining the credential for the relevant Reporting Period;
- (2) The credits of continuing education completed during the relevant Reporting Period by the investment adviser representative are mandatory to maintain the credential; and
- (3) The continuing education content provided by the credentialing organization during the relevant Reporting Period is Approved IAR Continuing Education Content.

(d) IAR continuing education reporting. Every investment adviser representative is responsible for ensuring that the Authorized Provider reports the investment adviser representative's completion of the applicable IAR continuing education requirements.

(e) No carry-forward. An investment adviser representative who completes Credits of continuing education in excess of the amount required for the Reporting Period may not carry forward excess credits to a subsequent Reporting Period.

(f) Failure to complete or report. An investment adviser representative who fails to comply with this rule by the end of a Reporting Period will renew as "CE Inactive" at the close of the calendar year in this state until the investment adviser representative completes and reports all required IAR continuing education Credits for all Reporting Periods as

required by this rule. An investment adviser representative who is CE inactive at the close of the next calendar year is not eligible for investment adviser representative registration or renewal of an investment adviser representative registration.

(g) Discretionary waiver by the Commissioner. The Commissioner may, in the Commissioner's discretion, waive any requirements of this rule.

(h) Home state. An investment adviser representative registered or required to be registered in this state who is registered as an investment adviser representative in the individual's Home State is considered to be in compliance with this rule provided that both of the following are true:

(1) The investment adviser representative's Home State has continuing education requirements that are at least as stringent as the NASAA Model Rule on Investment Adviser Representative Education; and

(2) The investment adviser representative is in compliance with the Home State's investment adviser representative continuing education requirements.

(i) Unregistered periods. An investment adviser representative who was previously registered under the Act and became unregistered must complete IAR continuing education for all reporting periods that occurred between the time that the investment adviser representative became unregistered and when the person became registered again under the Act unless the investment adviser representative takes and passes the examination or receives an examination waiver as required by section 16-39-453 in connection with the subsequent application for registration.

(j) Definitions. As used in this section:

"Act" means the Hawaii Uniform Securities Act (2008), codified at Chapter 485A, of the Hawaii Revised Statutes.

"Approved IAR Continuing Education Content" means the materials, written, oral, or otherwise that have been approved by NASAA or its designee and which make

up the educational program provided to an investment adviser representative under this rule.

"Authorized Provider" means a person that NASAA or its designee has authorized to provide continuing education content required by this rule.

"Credit" means a unit that has been designated by NASAA or its designee as at least fifty minutes of educational instruction.

"FINRA" means the Financial Industry Regulatory Authority.

"Home State" means the state in which the investment adviser representative has its principal office and place of business.

"IAR Ethics and Professional Responsibility Content" means Approved IAR Continuing Education Content that addresses an investment adviser representative's ethical and regulatory obligations.

"IAR Products and Practice Content" means Approved IAR Continuing Education Content that addresses an investment adviser representative's continuing skills and knowledge regarding financial products, investment features, and practices in the investment advisory industry.

"Investment adviser representative" or "IAR" means an individual who meets the definition of "investment adviser representative" under the Act and an individual who meets the definition of "investment adviser representative" under section 485A-102, HRS.

"NASAA" means the North American Securities Administrators Association or a committee designated by its Board of Directors.

"Reporting Period" means one twelve-month period as determined by NASAA. An investment adviser representative's initial Reporting Period with this state commences the first day of the first full Reporting Period after the individual is registered or required to be registered with this state. [Eff and

comp ] (Auth: HRS §§485A-406, 485A-411, 485A-606) (Imp: HRS §§485A-406, 485A-411, 485A-606)

**§16-39-455 Expiration, renewal, termination of registration.**

(a) All registrations shall automatically expire on December 31 of each year (unless sooner terminated in accordance with chapter 485A, HRS, and this chapter) and shall be renewed as provided in this section.

(b) An investment adviser shall be responsible for renewing the registration of its investment adviser representatives at the time the investment adviser renews its registration.

(c) An application for renewal registration shall not be considered filed until the investment adviser submits the following:

- (1) The renewal fee set forth in section 16-39-103; and
- (2) A copy of all amendments to Form U-4 of all such investment adviser representatives if such amendments have not been previously filed with the commissioner.

(d) An investment adviser representative's registration may be terminated at any time prior to its expiration date by the investment adviser employing the investment adviser representative or by the investment adviser representative by filing a Form U-5 with the commissioner directly or through the IARD. Termination shall be effective when the notice of termination is received by the commissioner unless another date is indicated on the Form U-5.

(e) An investment adviser representative's registration shall not be transferred. When an investment adviser representative terminates an affiliation with the investment adviser with whom the investment adviser representative is registered, and wishes to be employed by another investment adviser, a notice of termination shall be filed with the commissioner. The investment adviser representative may then reapply for registration with another investment adviser by complying with the requirements of this subchapter.

(f) The termination of any investment adviser's registration for any reason shall automatically

terminate the registration of all agents registered thereunder.

(g) When an investment adviser representative ceases the activities of an investment adviser representative, or the investment adviser representative otherwise becomes ineligible to be registered, a notice to terminate the registration shall be filed with the commissioner on Form U-5 by either the investment adviser representative, or the investment adviser with whom the investment adviser representative is registered. The termination of the registration shall be effective upon the commissioner's receipt of such form unless another date is indicated on the Form U-5. [Eff 6/30/08; comp ] (Auth: HRS §§485A-406, 485A-606) (Imp: HRS §485A-406, 485A-409, 485A-606)

E. Denial ~~[of]~~ of Application; Suspension ~~[And]~~ and Revocation ~~[of]~~ of Registration ~~[of]~~ of Broker-Dealers, Agents, Investment Advisers, ~~[And]~~ and Investment Adviser Representatives

**§16-39-470 Denial; suspension and revocation.**

(a) A proceeding to deny an application for registration, or to suspend or revoke the effectiveness of a registration may be instituted by the commissioner if the action is in the public interest, reasonable grounds exist that the applicant or registrant has violated or failed to comply with any provision of chapter 485A, HRS, or this chapter, or the applicant or registrant has demonstrated its unworthiness to transact the business of a broker-dealer, agent, investment adviser, or investment adviser representative.

(b) Without in any way limiting the generality thereof, for the purposes of section 485A-412(d)(14), HRS, any of the following shall demonstrate an applicant's or registrant's unworthiness to transact the business of a broker-dealer or agent:

- (1) Delivery delays. Engaging in a pattern of unreasonable and unjustifiable delays in the delivery of securities purchased by any of its customers or in the payment upon request of free credit balances reflecting completed transactions of any of its customers, or both;
- (2) Churning. Inducing trading in a customer's account which is excessive in size or frequency in view of the financial resources and character of the account;
- (3) Unsuitable recommendations. Recommending to a customer the purchase, sale, or exchange of any security without reasonable grounds to believe that the transaction or recommendation is suitable for the customer based upon reasonable inquiry concerning the customer's investment objectives, financial situation and needs, and any other relevant information known by the broker-dealer or agent;
- (4) Unauthorized transactions. Executing a transaction on behalf of a customer without authorization to do so;
- (5) Discretionary authority. Exercising any discretionary power in effecting a transaction for a customer's account without first obtaining written discretionary authority from the customer, unless the discretionary power relates solely to the time or price for the executing of orders, or both;
- (6) Margin accounts. Executing any transaction in a margin account without securing from the customer a properly executed written margin agreement promptly after the initial transaction in the account;
- (7) Segregation of client securities. Failing to segregate customers' free securities or securities held in safekeeping;
- (8) Hypothecating customer securities. Hypothecating a customer's securities



without having a lien thereon unless the broker-dealer secures from the customer a properly executed written consent promptly after the initial transaction, except as permitted by rules of the SEC;

- (9) Unreasonable price, commission. Entering into a transaction with or for a customer at a price not reasonably related to the current market price of the security, or receiving an unreasonable commission or profit;
- (10) Prospectus delivery. Failing to furnish to a customer purchasing securities in an offering, no later than the due date of confirmation of the transaction, either a final prospectus or a preliminary prospectus and an additional document, which together include all information set forth in the final prospectus;
- (11) Unreasonable fees. Charging unreasonable and inequitable fees for services performed, including miscellaneous services such as collection of monies due for principal, dividends or interest, exchange or transfer of securities, appraisals, safekeeping, or custody of securities and other services related to its securities business;
- (12) Offer to [~~buy/sell~~] buy or sell at stated price. Offering to buy from or sell to any person any security at a stated price unless the broker-dealer or agent is prepared to purchase or sell, as the case may be, at such price and under such conditions as are stated at the time of such offer to buy or sell;
- (13) Sales at the market. Representing that a security is being offered to a customer "at the market" or a price relevant to the market price unless the broker-dealer or agent knows or has reasonable grounds to believe that a market for the security exists other than that made, created, or

controlled by the broker-dealer or agent, or by any person for whom one is acting or with whom one is associated in the distribution, or any person controlled by, controlling or under common control with the broker-dealer or agent;

- (14) Manipulative, deceptive, or fraudulent practices. Effecting any transaction in, or inducing the purchase or sale of, any security by means of any manipulative, deceptive or fraudulent device, practice, plan, program, design or contrivance, which may include but not limited to~~[7]~~:
- (A) Effecting any transaction in a security which involves no change in the beneficial ownership thereof;
  - (B) Entering an order or orders for the purchase or sale of any security with the knowledge that an order or orders of substantially the same size, at substantially the same time and substantially the same price, for the sale of any such security, has been or will be entered by or for the same or different parties for the purpose of creating a false or misleading appearance of active trading in the security or a false or misleading appearance with respect to the market for the security; provided that nothing in this subsection shall prohibit a broker-dealer from entering bona fide agency cross transactions for its customers; or
  - (C) Effecting, alone or with one or more other persons, a series of transactions in any security creating actual or apparent active trading in such security or raising or depressing the price of such security, for the purpose of inducing the purchase or sale of such security of others;

- (15) Loss guarantees. Guaranteeing a customer against loss in any securities account of such customer carried by the broker-dealer or agent, or in any securities transaction effected by the broker-dealer or agent, or in any securities transaction effected by the broker-dealer or agent with or for such customer;
- (16) Bona fide price reports. Publishing or circulating, or causing to be published or circulated, any notice, circular, advertisement, newspaper article, investment service, or communication of any kind which purports to report any transaction as a purchase or sale of any security unless such broker-dealer or agent believes that such transaction was a bona fide purchase or sale of such security; or which purports to quote the bid price or asked price for any security, unless such broker-dealer or agent believes that such quotation represents a bona fide bid for, or offer of, such security;
- (17) Deceptive or misleading advertising. Using any advertising or sales presentation in any manner that is deceptive or misleading. An example would be the distribution of any nonfactual data, material, or presentation based on conjecture, unfounded or unrealistic claims or assertions in any brochure, flyer, or display by words, pictures, graphs or otherwise designed to supplement, detract from, supersede, or defeat the purpose or effect of any prospectus or disclosure;
- (18) Disclosure of control. Failing to disclose that the broker-dealer is controlled by, controlling, affiliated with, or under common control with the issuer of any security before entering into any contract with or for a customer for the purchase or sale of such security, the existence of such

control to such customer, and if such disclosure is not made in writing, it shall be supplemented by the giving or sending of written disclosure at or before the completion of the transaction;

- (19) Bona fide distribution. Failing to make a bona fide public offering of all of the securities allotted to a broker-dealer for distribution; whether acquired as an underwriter, a selling group member, or from a member participating in the distribution as an underwriter or selling group member;
- (20) Customer communication. Failure or refusal to furnish a customer, upon reasonable request, information to which the customer is entitled, or to respond to a formal written request or complaint from a customer;
- (21) Loans [~~to/from~~] to or from customers. Engaging in the practice of lending or borrowing money or securities from a customer, or acting as a custodian for money, securities, or an executed stock power of a customer;
- (22) Unrecorded transactions. Effecting securities transactions not recorded on the regular books or records of the broker-dealer which the agent represents, unless the transactions are authorized in writing by the broker-dealer prior to execution of the transaction;
- (23) Fictitious accounts. Establishing or maintaining an account containing fictitious information in order to execute transactions which would otherwise be prohibited;
- (24) [~~Profit/loss~~] Profit or loss sharing. Sharing directly or indirectly in profits or losses in the account of any customer without the written authorization of the customer and the broker-dealer which the agent represents;

- (25) Splitting commissions. Dividing or otherwise splitting the agent's commissions, profits, or other compensation from the purchase or sale of securities with any person not also registered as an agent for the same broker-dealer, or for a broker-dealer under direct or indirect common control;
- (26) Unsolicited transactions. Marking any order tickets or confirmations as unsolicited when in fact the transaction was solicited;
- (27) Compliance with the rules of self-regulatory organizations. Failing to comply with any applicable provision of the Conduct Rules and any other Rules of Fair Practice of the NASD or any applicable fair practice or ethical standard promulgated by the SEC or by a self-regulatory organization approved by the SEC;
- (28) Failure to cooperate. Failing to cooperate with, or providing false or incomplete information to, the commissioner in connection with any investigation under this chapter or chapter 485A, HRS;
- (29) Statement of account for OTC securities. Failing to provide each customer with a statement of account which, with respect to all OTC non-NASDAQ equity securities in the account, contains a value for each security based on the closing market bid on a date certain for any month in which activity has occurred in a customer's account, but in no event less than every three months; provided that this paragraph shall apply only if the firm has been a market maker in the security at any time during the period for which the monthly or quarterly statement is issued;
- (30) Credit to customer. Extending credit to a customer in violation of the Securities Exchange Act or the regulations of the Federal Reserve Board;

- (31) Fee disclosures. Charging a fee based on the activity, value, or contents (or lack thereof) of a customer account unless written disclosure pertaining to the fee, which shall include information about the amount of the fee, how imposition of the fee can be avoided, and any consequence of late payment or non-payment of the fee, was provided no later than the date the account was established or, with respect to an existing account, at least sixty calendar days prior to the effective date of the fee;
- (32) Business disclosures. Failing to accurately describe or disclose, in any advertising or other promotional materials (including business cards, stationery or signs) relating to an agent's business, the identity of the broker-dealer or issuer with whom the agent is associated or the nature of the securities services offered by the agent;
- (33) Boiler room tactics. Engaging or aiding in high pressure tactics in connection with the solicitation of a sale or purchase of a security by means of an intensive telephone, e-mail, or fax campaign, or unsolicited calls to persons not known by, nor having an account with, the agent or broker-dealer represented by the agent, whereby the prospective purchaser is encouraged to make a hasty decision to buy, irrespective of his or her investment needs and objectives;
- (34) Protection of non-public information. Failing to protect the security and confidentiality of the non-public personal information of any client;
- (35) Minimum capital requirements. Operating a securities business while being unable to meet current liabilities, or violating any rule or order relating to minimum capital, bond, record-keeping and reporting requirements, or provision concerning use,

- commingling, or hypothecation of a customer's funds or securities;
- (36) Outside business activity. Any agent associated with a broker-dealer registered under chapter 485A, HRS, and this chapter shall not engage in business activities, for which the agent receives compensation either directly or indirectly, outside the scope of the agent's regular employment unless the agent has provided prior written notice to his employing firm;
  - (37) Dual agency. Failing to disclose a dual agency capacity;
  - (38) Other terms or conditions. Effecting transactions upon terms and conditions other than those stated per confirmations; or
  - (39) False, misleading, deceptive, exaggerated, or flamboyant representations. Making false, misleading, deceptive, exaggerated, or flamboyant representations or predictions in the solicitation or sale of a security. Examples of this include without limitation misrepresenting:
    - (A) That the security shall be resold or repurchased;
    - (B) That the security shall be listed or traded on an exchange or established market;
    - (C) That the security shall result in an assured, immediate or extensive increase in value, future market price, or return on investment;
    - (D) With respect to the issuer's financial condition, anticipated earnings, potential growth, or success; or
    - (E) That there is a guarantee against risk or loss.

This subsection is not intended to be all-inclusive, and thus, acts or practices not enumerated in this subsection may also be deemed to demonstrate unworthiness to transact the business of broker-dealer or agent. Engaging in

other conduct such as forgery, embezzlement, nondisclosure, incomplete disclosure or misstatement of material facts, or manipulative or deceptive practices shall also be grounds for denial, suspension, or revocation of registration.

(c) Without in any way limiting the generality thereof, for the purposes of section 485A-412, HRS, any of the following shall demonstrate an applicant's or registrant's unworthiness to transact the business of an investment adviser or investment adviser representative:

- (1) Unsuitable recommendation. Recommending to a client to whom investment supervisory, management, or consulting services are provided the purchase, sale, or exchange of any security without reasonable grounds to believe that the recommendation is suitable for the client on the basis of information furnished by the client after reasonable inquiry concerning the client's investment objectives, financial situation and needs, and any other information known by the investment adviser;
- (2) Discretionary authority. Exercising any discretionary power in placing an order for the purchase or sale of securities for a client without obtaining written discretionary authority from the client within ten business days after the date of the first transaction place pursuant to oral discretionary authority, unless the discretionary power relates solely to the price at which, or the time when, an order involving a definite amount of a specified security shall be executed, or both;
- (3) Churning. Inducing trading in a client's account that is excessive in size or frequency in view of the financial resources, investment objectives, and character of the account in light of the fact that an investment adviser or an



investment adviser representative in such situations can directly benefit from the number of securities transactions effected in a client's account. This paragraph appropriately forbids an excessive number of transaction orders to be induced by an adviser for a "customer's account";

- (4) Unauthorized transactions. Placing an order to purchase or sell a security for the account of a client without authority to do so;
- (5) Unauthorized third-party trade. Placing an order to purchase or sell a security for the account of a client upon instruction of a third party without first having obtained a written third-party trading authorization from the client;
- (6) Loans from clients. Borrowing money or securities from a client unless the client is a broker-dealer, an affiliate of the investment adviser, or a financial institution engaged in the business of loaning funds;
- (7) Loans to clients. Loaning money to a client unless the investment adviser is a financial institution engaged in the business of loaning funds or the client is an affiliate of the investment adviser;
- (8) Misrepresentations concerning advisory services. Misrepresenting to any advisory client or prospective advisory client, the qualifications of the investment adviser or any employee of the investment adviser, or misrepresenting the nature of the advisory services being offered or fees to be charged for such service, or to omit to state a material fact necessary to make the statements made regarding qualifications, services or fees, in light of the circumstances under which they are made, not misleading;

- (9) Advisory report prepared by another. Providing a report or recommendation to any advisory client prepared by someone other than the adviser without disclosing that fact; provided that this prohibition shall not apply to a situation where the adviser uses published research reports or statistical analyses to render advice or where an adviser orders such a report in the normal course of providing service;
- (10) Unreasonable advisory fees. Charging a client an unreasonable advisory fee;
- (11) Conflict of interest. Failing to disclose to clients in writing before any advice is rendered any material conflict of interest relating to the adviser, or any of its employees which could reasonably be expected to impair the rendering of unbiased and objective advice including:
  - (A) Compensation arrangements connected with advisory services to clients which are in addition to compensation from such clients for such services; or
  - (B) Charging a client an advisory fee for rendering advice when a commission for executing securities transactions pursuant to such advice will be received by the adviser or its employees;
- (12) Guaranteeing specific results. Guaranteeing a client that a specific result will be achieved (gain or loss) with advice that will be rendered;
- (13) Advertising. Publishing, circulating, or distributing any advertisement which does not comply with the Investment Advisers Act, 17 CFR section 275-206(4)-1;
- (14) Disclosure of private information. Disclosing the identity, affairs, or investments of any client unless required by law to do so, or unless consented to by the client;

- (15) Action contrary to section 16-39-435. Taking any action, directly or indirectly, with respect to those securities or funds in which any client has any beneficial interest, where the investment adviser has custody or possession of such securities or funds when the adviser's action is subject to and does not comply with the requirements of section 16-39-435;
- (16) Advisory contract disclosure. Entering into, extending, or renewing any investment advisory contract, unless such contract is in writing and discloses, in substance, the services to be provided, the term of the contract, the advisory fee, the formula for computing the fee, the amount of prepaid fee to be returned in the event of contract termination or non-performance, whether the contract grants discretionary power to the adviser and that no assignment of such contract shall be made by the investment adviser without the consent of the other party to the contract;
- (17) Protection of non-public information. Failing to establish, maintain, and enforce written policies and procedures reasonably designed to prevent the misuse of material nonpublic information contrary to the provisions of section 204A of the Investment Advisers Act;
- (18) Advisory contract to comply with federal law. Entering into, extending, or renewing any advisory contract contrary to the provisions of section 205 of the Investment Advisers Act; provided that this provision shall apply to all advisers and investment adviser representatives registered or required to be registered under chapter 485A, HRS, and this chapter, notwithstanding whether such adviser or representative would be exempt from federal registration pursuant

to section 203(b) of the Investment Advisers Act;

- (19) Waiver of state or federal law prohibited. To indicate, in an advisory contract, any condition, stipulation, or provisions binding any person to waive compliance with any provision of chapter 485A, HRS, this chapter, or the Investment Advisers Act;
- (20) Fraudulent, deceptive, or manipulative acts. Engaging in any act, practice, or course of business which is fraudulent, deceptive, or manipulative in contrary to the provisions of section 206(4) of the Investment Advisers Act, notwithstanding the fact that such investment adviser or investment adviser representative is not registered or required to be registered under section 203 of the Investment Advisers Act;
- (21) Third party conduct. Engaging in conduct or any act, indirectly or through or by any other person, which would be unlawful for such person to do directly under the provisions of chapter 485A, HRS, and this chapter;
- (22) Disclosure of material facts. Failing to disclose to any client or prospective client all material facts that may influence the client or prospective client's ability to make an informed decision;
- (23) Compliance with exchange or SRO rules. Failing to comply~~ing~~ with any rule of a national securities exchange or self-regulatory organization approved by the SEC;
- (24) Failure to cooperate. Failing to cooperate with, or providing false or incomplete information to, the commissioner in connection with any investigation under chapter 485A, HRS, or this chapter;
- (25) Outside business activity. Any investment adviser representative associated with an investment adviser registered under chapter 485A, HRS, and this chapter, shall not

engage in business activities, for which the investment adviser representative receives compensation either directly or indirectly, outside the scope of the investment adviser representative's regular employment unless the investment adviser representative has provided prior written notice to the investment adviser representative's employing firm;

- (26) Client communication. Failing or refusing to furnish a client, upon reasonable request, information to which the client is entitled, or to respond to a formal written demand or complaint from the client;
- (27) Inside information. In connection with the offer, purchase, or sale of a security leading a client to believe that the investment adviser or investment adviser representative is in possession of material, non-public information that would affect the value of the security;
- (28) Unreasonable delay. Causing unreasonable delay or failure to execute orders, liquidate customer's accounts, or in making delivery of securities purchased or remittances (or credits) for securities sold; or
- (29) Unlicensed broker-dealer. Placing an order through an unlicensed broker-dealer or agent which the investment adviser should have known was unlicensed.

This subsection is not intended to be all inclusive, and thus, acts or practices not enumerated in this subsection may also be deemed to demonstrate unworthiness to transact the business of investment adviser or investment adviser representative. Engaging in other conduct such as non-disclosure, incomplete disclosure, or deceptive practices shall be deemed an unethical business practice. The federal statutory and regulatory provisions referenced in this section shall apply to

investment advisers, investment adviser representatives, and federal covered investment advisers to the extent permitted by the National Securities Markets Improvement Act of 1996 (Pub. L. No. 104-290). [Eff 6/30/08; comp ]  
(Auth: HRS §485A-606) (Imp: HRS §485A-412)

## SUBCHAPTER 5

### FRAUDULENT PRACTICES OF BROKER-DEALERS, BROKER-DEALER AGENTS, AND AGENTS OF AN ISSUER

**§16-39-501 Fraudulent practices of broker-dealers, broker-dealer agents, and agents of an issuer.** The purpose of this section is to identify practices in the securities business that are generally associated with schemes to manipulate. A broker-dealer, broker-dealer agent, or agent of the issuer who engages in one or more of the following practices shall be deemed to have engaged in an "act, practice, or course of business that operates or would operate as a fraud or deceit" as used in section 485A-501, HRS; provided that this section is not intended to be all-inclusive, and thus, acts or practices not enumerated herein may also be deemed fraudulent:

- (1) Unreasonable price/commission. Entering into a transaction with a customer in any security at a price not reasonably related to the current market price of the security or receiving an unreasonable commission or profit;
- (2) Contradicting prospectus information. Contradicting or negating the importance of any information contained in a prospectus or other offering materials with intent to deceive or mislead or using any advertising

- or sales presentation in a deceptive or misleading manner;
- (3) Insider information. In connection with the offer, sale, or purchase of a security, falsely leading a customer to believe that the broker-dealer or agent is in possession of material, non-public information which would impact on the value of the security;
  - (4) Contradictory recommendations. In connection with the solicitation of a sale or purchase of a security, engaging in a pattern or practice of making contradictory recommendations to different investors of similar investment objective for some to sell and others to purchase the same security, at or about the same time, when not justified by the particular circumstances of each investor;
  - (5) Bona fide distribution. Failing to make a bona fide public offering of all the securities allotted to a broker-dealer for distribution by, among other things, transferring securities to a customer, another broker-dealer or a fictitious account with the understanding that those securities will be returned to the broker-dealer or its nominees; or parking or withholding securities;
  - (6) Relating to OTC securities. Although nothing in this section precludes application of the general anti-fraud provisions against anyone for practices similar in nature to the practices discussed below, the following subparagraphs specifically apply only in connection with the solicitation of a purchase or sale of OTC unlisted non-NASDAQ equity securities:
    - (A) ~~[Bid/ask]~~ Bid and ask price disclosure. Failing to disclose the firm's present bid and ask price of a particular security at the time of solicitation;

- (B) Commission disclosure. Failing to advise the customer, both at the time of solicitation and on the confirmation, of any and all compensation related to a specific securities transaction to be paid to the agent including commissions, sales charges, or concessions;
- (C) Short inventory position. In connection with a principal transaction, failing to disclose, both at the time of solicitation and on the confirmation, a short inventory position in the firm's account of more than three per cent of the issued and outstanding shares of that class of securities of the issuer provided that this subparagraph shall apply only if the firm is a market maker at the time of the solicitation;
- (D) Sales contests. Conducting sales contests in a particular security;
- (E) Delay executing sell orders. After a solicited purchase by a customer, failing or refusing, in connection with a principal transaction, to promptly execute sell orders;
- (F) Secondary market solicitation. Soliciting a secondary market transaction when there has not been a bona fide distribution in the primary market;
- (G) Differing compensation. Engaging in a pattern of compensating an agent in different amounts for effecting sales and purchases in the same security;
- (H) Manipulative, deceptive, or fraudulent acts. Effecting any transaction in, or inducing the purchase or sale of, any security by means of any manipulative, deceptive, or other fraudulent device or contrivance including but not



limited to the use of boiler room tactics or use of fictitious or nominee accounts;

- (I) Prospectus delivery. Failure to comply with any prospectus delivery requirement promulgated under federal law; or
- (J) Penny stock sales. Effecting any transaction in, or inducing or attempting to induce the purchase or sale of, any penny stock by any customer except in accordance with the requirements as set forth in section 15(g) of the Securities Exchange Act." [Eff 6/30/08; am and comp ]  
(Auth: HRS §485A-606) (Imp: HRS §485A-501)

2. Material, except source notes and other notes, to be repealed is bracketed and stricken. New material except source notes and other notes, is underscored.

3. Additions to update source notes and other notes to reflect these amendments to sections are not bracketed, struck through, or underscored.

4. These amendments to and compilation of chapter 16-39, Hawaii Administrative Rules, shall take effect ten days after filing with the Office of the Lieutenant Governor.

I certify that the foregoing are copies of the rules, drafted in the Ramseyer format pursuant to the requirements of section 91-4.1, Hawaii Revised Statutes, which were adopted on MM DD, YYYY, and filed with the Office of the Lieutenant Governor.

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NADINE Y. ANDO  
Director of Commerce and  
Consumer Affairs

APPROVED AS TO FORM:



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ANDREW I. KIM  
Deputy Attorney General