

2011 HOUSE JUDICIARY

HB 1091

# 2011 HOUSE STANDING COMMITTEE MINUTES

House Judiciary Committee  
Prairie Room, State Capitol

HB 1091  
January 12, 2011  
12837

☐ Conference Committee

Committee Clerk Signature



## Minutes:

Chairman DeKrey: We will open the hearing on HB 1091.

Michael Daley, Deputy Securities Commissioner & Enforcement Attorney for the Securities Dept.: Sponsor, support (see attached testimony).

Chairman DeKrey: My question is, you are asking for rule-making authority so you can be ready by this summer; but by the timeline we have on the Administrative Rules Committee on how long it takes to get a rule approved, I'm not so sure you are going to make it by this summer, even with the approval.

Rep. Koppelman: I think they could, if they started right away and could also make emergency rules under the Administrative Practices Act, which would speak about that.

Michael Daley: That's what we would be anticipating, it's about the best we can do.

Rep. Koppelman: I don't think I've ever seen, in the history of ND, where an agency of government asks for authority to supercede state law, which as I read this bill, is what you're asking for. That's not what rules are. Can you enlighten us about this.

Michael Daley: The reason for the rule-making authority and the amendment to the legislation is to permit, not supercede state law, but to permit a rule that varies with current legislation as the legislature may approve in administrative rules.

Rep. Koppelman: Maybe there is a misunderstanding of what administrative rules are and what they do. They can't trump state law. You are asking for rule-making authority to do something that is in variance with state law, to me that means the same thing as superceding state law. We've never done that before, and I've been on the administrative rules committee for 16 years and have authored a lot of legislation in that arena. I don't think that's ever happened. I know some of the background here which the other committee members may not. I know that your agency had policies that it was trying to enforce as if they were rules, so I do want to

commend you on coming forward with the intent of making rules. That's the correct procedure and that's the right way to go. The problem with the bill is, as written, we need to look at the language and talk to you and find out what you are trying to accomplish. The Administrative Practices Act, which is section 28-32, gives you inherent authority already to make rules in this area, but I welcome a bill that is specific; that says that the Commissioner shall have (on the bottom of page 1) (I don't like the first part of that language, but the second part might be something we can work with in terms of specifying where it is you want to do rule-making). In doing so, the rule making would have to be within the parameters of the statute. I also suggest that if you see things in the statute that are problematic, or you see us potentially conflicting with some rules you want to make, that you come to us during the session and talk about the meat of the statute, don't just say, give us the authority to overrule the law after you leave; let us know what you want to change in the law and then I think you would have the authority to make the rules. Of course, it would come under the review of the Administrative Rules Committee. That's not really a question, just a comment.

Michael Daley: I appreciate your comments. We fully acknowledge that rule-making authority cannot trump legislative provisions. The reason for this requested amendment is the law clearly says "no performance fees" now and it says no custody in subsection 6, and we're recognizing that some of these firms, that are going to be transitioning currently under federal law, has that authority. That's the reason for prefacing these prohibitions with except, as permitted by rule, and then a specific grant in this area to the commissioner to propose those types of rules that would not then be in conflict with the statute, because the statute specifically allows for modification in certain circumstances.

Rep. Koppelman: I think the concern then is, if I understand you correctly, that federal law permits something that state law does not permit.

Michael Daley: In certain circumstances for certain firms.

Rep. Koppelman: It is certainly permissible, this is an area of interstate commerce I assume, and that's why the federal government claims authority in it, it is certainly permissible and common for states to have laws that are more restrictive than federal law; they can't be less restrictive. Federal law says you can't sell this kind of a security, ND can't come along and say "yes we can" if it is an interstate commerce kind of issue. However, if the federal law says we will allow this kind of security, and I realize that's not the point you are talking about specifically it's just an example, but in ND we say "we don't want that kind of a security sold here" we can pass a law saying you can't. Your concern is we prohibit something in ND that the federal government is allowing and you're asking that your agency have the authority to waive that prohibition. I'm saying it's not the way to do it. If you don't like the prohibition, try and change the statute. You have rule making authority within the confines of that statute, but I don't very seriously that you are going to see us pass a bill that gives you authority to trump law.

Rep. Delmore: If you need emergency rules, I think that's one thing. I think that most of the time the administrative rules committee is pretty good to listen. You're really asking for cart blanche here, it's very open ended, and it kind of says that you really don't need to have any

statute because I can ignore it all anyway. I just don't see us passing the bill in this form. Maybe there is something else you can do, but I certainly would not support this.

Michael Daley: Certainly we are not attempting to do any kind of end run around what's permitted by current legislation. I believe that the rule making authority would not trump any statutes that are currently in place. The Uniform Act of 2002, from which I took this language of the Securities Act for States Securities Act, generally just said, under section 502(c) that investment advisory contracts will be such, in using this language as set forth in rule. When we adopted investment advisor statutes, rather than use that language, we put it in the statute what can be in the contract and what's required for record keeping. As I said, these regulations are dual, between some requirements of the federal law apply to all investment advisors. There is sovereignty with US government in certain areas, and they have, for instance, in the Investment Advisors Act of 1940 said no states can have a less diminutive position than a state registered firm that's not in the state where it is requesting registration, has fewer than 6 clients. Our statutes conforms with that and says that if you are a state covered advisor with no place of business in the state, and have 5 or fewer clients you don't have to register, because that complies with federal law. That's just one example. In the area of performance fees, it's silent as to what can be required. Performance fees, basically, are an extra bonus for the advisor if they perform, they get a % of the gain in a fund or, for instance, as against some other benchmark. Because that generally happens when they are putting their clients into riskier investments that kind of creates an inherent conflict of interest. I think that is the reason that most states just said "no performance fees". We do recognize that some of these larger firms are going to have more well-to-do clients and fall within those categories and should be allowed.

Rep. Delmore: I understand what you are saying about federal regulations, and I think we are going to hear a lot of it this session, where people want to go ahead and plan for what they may think it may say. I think we have a bottom line commitment to people of this state, to make sure that they are so protected. I think we have a process to go through with that, when there is an emergency and when we do have to react to things, and it is administrative rules, and I think you can already do this. I think you've been very forthright in coming forward with this, I don't see you as doing anything that you perceive as dishonest, but I just think this reaches far beyond the auspices, even though it is limited to one part.

Michael Daley: We would certainly be happy to look at amending the language that we proposed. This is a solution that we thought would meet the requirements and if you feel that it can be tweaked to be handled better and not leave us hanging out there for 2.5 years, we would be happy to consider the same.

Rep. Kretschmar: The Securities Dept is not exempt from our administrative rules act, is it, it's not one of our agencies that are exempt, and there is a list in the statute.

Michael Daley: That's correct; we are not one of the exempt agencies.

Rep. Kretschmar: The new language on line 23 and 24, by rule may waive the provisions and then it is by rule, modifying the rest of that sentence, the contents of the contract; or could you just do the contents of the contract as you wish.

Michael Daley: Obviously the Commissioner can't do anything that the Commissioner wishes. It would have to be set forth in the rule adopted under the emergency legislation by the Legislative committee.

Rep. Kretschmar: Your interpretation of the new language, you may by rule waive, covers both sections of the sentence.

Michael Daley: Actually, when I submitted the proposed bill to the Legislative Council, that underline language was a free standing sentence, the last sentence of section 5, was not attached to subpart d, I guess I didn't read it as a sentence in subpart d as having any material effect, so I didn't go back and say why did you do that.

Rep. Maragos: That was precisely the line I was taking as I looked at it. Why that sentence was not a standalone sub-subsection e, rather than tack it on to d. I'm curious that if you look at paragraph d, would the Commissioner be able to void, by rule, if they waived any provision in this subsection, waive the right of the client to change, could they interfere with that then and why would they want to.

Michael Daley: That is a pretty standard requirement in investment advisory contracts that they have to be able to have that ability too. A lot of the funds have limitations as to when they can withdraw, may be locked in for a number of years.

Rep. Maragos: I'm not concerned about that, I'm concerned about the part that the Commissioner may, by rule, waive any of these provisions. Why would they want to interfere, why would he want the ability to interfere.

Michael Daley: I can assure you that the would not be proposing rules along those lines, but because of the flux, and particularly not knowing what's going to happen with these private fund advisors, who heretofore have basically been unregulated, hedge funds and other things. We just wanted to have some flexibility; we're not looking to do wholesale changes in this area. Frankly, it's a very small part of what we do. There are probably 24,000 investment advisor firms in the country; 14,000 are currently state registered firms. We have 23. We have another 607 SEC firms that notice file here. It's not something that we're spending a lot of time with. There are just a handful of ND domiciled state registered firms. I don't see it as something we're going to be flooding the administrative rules committee, with proposed rules to do wholesale changes. It's just for limited purposes and we probably would have submitted legislative amendments if we knew what we needed to change.

Rep. Maragos: Let me just ask a question. Both subsection 5 and subsection 6 now have new language that states, except as permitted by rule. Obviously that means that rules can be implemented that would affect these subsections. What would happen to this bill, if you removed the new language on page 1 lines 23, 24 and page 2, lines 1 and 2? How would that significantly change what you're trying to accomplish.

Michael Daley: I don't know if that would change what we're trying to accomplish. I think the idea you are expressing is the same. We can't currently adopt a rule that is contrary to what says "it is unlawful for". We can't put in a new rule that contradicts the statute; you can't override the statute by the rule. That was the reason for the prefatory language to say, "we're anticipating that in some circumstances" a rule would allow, which would otherwise

be prohibited. If we want to move things around and accomplish the same thing, I'm all for it.

Rep. Maragos: Then the "except as permitted by rule", that's an exception in the first sentence "it is unlawful". Well, if it were permitted by rule, because it says the exception as permitted by rule. Am I reading that correctly?

Michael Daley: That's the intent of the legislation.

Rep. Klemin: I know you're familiar with the North American Securities Administrators Association, also referred to as NASA, correct.

Michael Daley: Correct.

Rep. Klemin: I'm wondering, does NASA have a standard relating to the subject matter of this bill.

Michael Daley: At this point, NASA does not have any standards; NASA has been working very closely with the SEC on what's been termed "the switch" in having a consistent ADV part 2 form, which is the electronic registration. NASA has made suggestions that are administered the CRD system, IARD system is administered federally, but our state IA is also registered through that. That's been coordinated and the SEC has proposed rules for reporting and registration of these new private fund advisor entities, and NASA is working on a proposed model rule that the states can use in deciding whether or not to register those, or exempt certain of those, from registration or just collect a registration fee. That's in the works, but there is nothing presently in place.

Rep. Klemin: So when NASA completes its work on the model rule, would there be a conflict in state law that would prevent our own Securities Commissioner from proposing a state rule that would follow that model.

Michael Daley: I don't think there would be a conflict and it probably would fall outside of this proposed legislation on the registration side of these private funds. Currently, in our definition section, 10-04-02-10, it defines investment advisor; it excludes from the definition, federal registered investment advisors and also excludes firms that would not be investment advisors under the IAA Act of 1940, which is where these private fund advisors were excluded from our statute, under current law. In the last subsection of that definition, gives the Commissioner rule making authority to exclude from registration, any other firm basically. If the model rule says "we don't need to register these firms because we haven't needed to for the last 50 years", under that section we could just adopt the rule. We wouldn't be dealing with the contracts.

Chairman DeKrey: Thank you. Further testimony in support. Testimony in opposition. We will close the hearing. The IBL committee chair wants to take a look at it. Subcommittee will be chaired by Rep. Boehning, Rep. Koppelman, and Rep. Delmore due Wednesday, 1/19/11.

# 2011 HOUSE STANDING COMMITTEE MINUTES

House Judiciary Committee  
Prairie Room, State Capitol

HB 1091  
February 7, 2011  
14132

☐ Conference Committee

Committee Clerk Signature



## Minutes:

Chairman DeKrey: We will take a look at HB 1091. What were the subcommittee's actions?

Rep. Boehning: Amendments were drafted, and Rep. Delmore and Rep. Koppelman both agree with them. Rep. Koppelman worked with both sides and will explain the amendments.

Rep. Koppelman: HB 1091 is the bill that dealt with the Insurance Commissioner and there was another bill in IBL that was dealing with that same department. The problem is that the Securities Dept., apparently for years, has been enforcing their orders as though they had statutory authority to do so; as if they were either statute or rule without really having them in rule. According to the Attorney General's office, and others who have looked into this, there may be good reason for them to have assumed that they had the authority to do that, because there are sections of Code that deals with orders. I think what we're doing this session is clearing that up. In other words, as a regulatory agency they can issue orders, and those orders have standing when they are regulating the regulated community. However, they must be based upon an administrative rule or a statute. They can't just be based upon some standard some national organization works up and they like it, and they think they are going to enforce in ND. In IBL committee, there is a bill that I believe we already passed on the Floor that says that they need to make administrative rules. This bill, as it originally came to us, would have allowed them to usurp statute by rule, we said no, we're not going to do that, so the amendment takes those troublesome provisions out and basically says, page 2, after line 5 insert, "the commissioner may by rule, specify the contents of an investment advisory contract that will comply with the requirements of this subsection". In other words, they can't usurp statute by their rule, but they can determine to some degree, what contracts contain as long it is within that authority.

Chairman DeKrey: Rep. Boehning moves the Rep. Koppelman amendment to HB 1091.

Rep. Koppelman: Second the motion.

Chairman DeKrey: Voice vote, motion carried. We now have HB 1091 before us as amended. What are the committee's wishes in regard to HB 1091?

Rep. Delmore: I move a Do Pass as amended.

Rep. Maragos: Second the motion.

**14 YES 0 NO 0 ABSENT DO PASS AS AMENDED**

**CARRIER: Rep. Koppelman**



VR  
2/7/11

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1091

Page 1, line 1, replace "subsections" with "subsection"

Page 1, line 1, remove "and 6"

Page 1, line 2, remove "and custody of securities or"

Page 1, line 3, remove "funds"

Page 1, line 5, replace "Subsections" with "Subsection"

Page 1, line 5, remove "and 6"

Page 1, line 6, replace "are" with "is"

Page 1, line 7, remove the overstrike over "it"

Page 1, line 7, remove "Except as permitted by rule, it"

Page 1, line 23, remove "The commissioner may by rule waive any"

Page 1, remove line 24

Page 2, replace lines 1 through 5 with:

"e. The commissioner may specify by rule the contents of an investment advisory contract that will comply with the requirements of this subsection."

Renumber accordingly

Date: 2/7/11  
Roll Call Vote # 1

2011 HOUSE STANDING COMMITTEE ROLL CALL VOTES  
BILL/RESOLUTION NO. 1091

House JUDICIARY Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number 11. 8016. 01003 . 02000

Action Taken: ☒ Do Pass ☐ Do Not Pass ☒ Amended ☐ Adopt Amendment

☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Rep. Delmore Seconded By Rep. Maragos

Representatives	Yes	No	Representatives	Yes	No
Ch. DeKrey	✓		Rep. Delmore	✓	
Rep. Klemin	✓		Rep. Guggisberg	✓	
Rep. Beadle	✓		Rep. Hogan	✓	
Rep. Boehning	✓		Rep. Onstad	✓	
Rep. Brabandt	✓				
Rep. Kingsbury	✓				
Rep. Koppelman	✓				
Rep. Kretschmar	✓				
Rep. Maragos	✓				
Rep. Steiner	✓				

Total (Yes) 14 No 0

Absent 0

Floor Assignment Rep. Koppelman

If the vote is on an amendment, briefly indicate intent:

**REPORT OF STANDING COMMITTEE**

**HB 1091: Judiciary Committee (Rep. DeKrey, Chairman) recommends AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (14 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). HB 1091 was placed on the Sixth order on the calendar.

Page 1, line 1, replace "subsections" with "subsection"

Page 1, line 1, remove "and 6"

Page 1, line 2, remove "and custody of securities or"

Page 1, line 3, remove "funds"

Page 1, line 5, replace "Subsections" with "Subsection"

Page 1, line 5, remove "and 6"

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Page 2, replace lines 1 through 5 with:

"e. The commissioner may specify by rule the contents of an investment advisory contract that will comply with the requirements of this subsection."

Renumber accordingly

2011 SENATE INDUSTRY, BUSINESS AND LABOR

HB 1091

# 2011 SENATE STANDING COMMITTEE MINUTES

## Senate Industry, Business and Labor Committee Roosevelt Park Room, State Capitol

HB 1091  
March 2, 2011  
Job Number 14811

☐ Conference Committee

Committee Clerk Signature



### Explanation or reason for introduction of bill/resolution:

Relating to investment advisory contracts

### Minutes:

No written testimony

**Chairman Klein:** Opened the hearing on House Bill 1091.

**Karen Tyler, Securities Commissioner of North Dakota:** Stated that the bill was introduced on her behalf. She is now in opposition of the bill.

**Chairman Klein:** Asked if the bill had been changed. And stated for the committee's benefit; she had requested the bill and the bill went to the Judiciary Committee in the House, they did some amending and she no longer likes the bill.

**Commissioner Tyler:** She stated that the bill was introduced at her request. It was introduced in preparation for and in response to some changes that are coming as a result of the Dodd-Frank regulatory reform legislation that passed last year in response to the financial crisis. As a result of the federal regulations they are facing some changes at the state level as well. The bill was amended by the House Judiciary Committee in such a way that it no longer serves the purpose for which it was introduced. She is here to ask for a, "do not pass", on the bill. She stated for background on the securities department; they regulate security agents, and investment advisors. The primary distinction between stockbrokers and investment advisors is in the way they are compensated. Stockbrokers earn a commission on the trades that they make, investment advisors charge a fee for giving you advise. This bill dealt strictly with investment advisors and the fees that they can charge. They were attempting to create a very narrow exemption on a statutory prohibition on a particular type of fee they charge. This fee is called a, "performance fee", and the exemption they were trying to create would be consistent and uniform with a federal exemption. Under the federal structure the investment advisors can charge a performance fee to certain clients, they are called qualified clients. They are investors that have over seven hundred and fifty thousand dollars with the advisors or who have a net worth of at least 1.5 million dollars. These fees are most commonly seen in the hedge fund industry, advisors to hedge funds will typically charge one percent of assets under management and then if there is capital appreciation in the portfolio, they will charge a percentage of that appreciation as well. That is called a performance fee. In the Federal Regulatory Structure

they can do this, in the State Regulatory Structure we have an expressed prohibition against it. They were trying to create an exemption that matched up with the Federal exemption. There were a number of reasons for this; first of all they have a statutory obligation created by the legislature to be uniformed. The second reason is most of the people in the companies that they regulate are not local. They do business regionally, nationally and internationally. Some examples, they regulate over 65 thousand stockbrokers, eleven hundred are domiciled here. They regulate over 630 investment advisor firms, twenty eight are located here. So uniformity for these companies and people are really important. The third reason is the Dodd-Frank Legislation. As a result of that regulation they will be taking on regulation of more investment advisors. Currently they share they jurisdiction with Securities and Exchange Commission. They take and regulate advisors who have less than 25 million of assets under management, and the Securities and Exchange gets the rest. The Dodd-Frank regulation raised that threshold too, one hundred million dollars. In July of this year they will have jurisdiction over investment advisors who have one hundred million or less, under management and the Securities Exchange will have the rest. They will be having all these advisors transitioning from Federal to State regulation and they want to make sure that the regulatory provisions are consistent. They don't want them to be having to rewrite all their contracts with clients and change their compensation structures. The Judiciary Committee put an amendment on it that says, you can write rules that are consistent with your statute. In statute we have an expressed prohibition and that is what we are trying to deal with. The amendment on the bill serves no purpose because they already have rule writing authority.

**Senator Schneider:** Stated that if they kill the bill the advisors will not be able to charge a performance fee in North Dakota.

**Commissioner Tyler:** That is as it stands today and if we don't get this done this session we will come back and try again.

**Senator Schneider:** Said instead of killing the bill, would it make sense to clarify that you can charge a performance fee and do that in law? Asked if she could come forward with amendments to this bill, so they could solve the problem?

**Commissioner Tyler:** She said that the way they drafted the bill in the first place would give the Commissioner statutory authority to create an exemption through rule making. We then proposed putting in statute incorporating by reference the federal exemption.

**Chairman Klein:** Commented that they want to do what they believe is best for the folks in North Dakota and the people in the business of doing this. If they run into major problems in trying to fix this, they could look at killing the bill if they can't come into agreement in the conference discussions.

**Commissioner Tyler:** That would be the optimum outcome. We can provide the committee with the language we had given to the House Judiciary in amendment forms.

**Chairman Klein:** Asked if the issue was over the rule making process. He said the securities rules came to the front during the interim when there was discussion about who follows the rules. He said the securities commission was singled out as not following the

rules authority as much as following what some federal organization tells them on how to operate.

**Commissioner Tyler:** What the Chairman is referring to is a separate piece of legislation that deals with the authority of the Commissioner to apply guidelines and policies with the force and effect of law or rule. The Commissioner has that authority. There is another bill that will come before you that will deal with that, that will alter that authority. She said, she thinks that it has entered into this debate even though this is a separate issue. They can't make a rule that is in conflict with statute, so they were seeking legislative authority to create an exemption.

**Chairman Klein:** Closed the hearing.

Discussion on addressing the issue and Senator Schneider and Senator Nodland will work on a provision.

# 2011 SENATE STANDING COMMITTEE MINUTES

**Senate Industry, Business and Labor Committee**  
Roosevelt Park Room, State Capitol

HB 1091  
March 8, 2011  
Job Number 15108

☐ Conference Committee

Committee Clerk Signature

*Eva Lettich*

## Explanation or reason for introduction of bill/resolution:

Relating to investment advisory contacts

## Minutes:

Discussion and Vote

**Chairman Klein:** Brought the meeting to order.

**Senator Schneider:** Stated that this would allow an individual advisor to charge a performance fee. He said he worked with Karen from the securities commission and they came up with an amendment. They are usually wealthy investors and this would allow the investment advisor to charge a performance fee.

**Senator Laffen:** Asked if Karen Tyler had looked over the amendment and had agreed.

**Senator Schneider:** Said that she preferred the amendment and it has her support.

**Senator Schneider:** Move to adopt the amendment.

**Senator Andrist:** Seconded the motion.

**Senator Schneider:** Moved a do pass as amended.

**Senator Murphy:** Seconded the motion.

**Senator Schneider** to carry the bill



March 2, 2011

  
3-8-11

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1091

Page 1, line 6, overstrike "into"

Page 1, line 7, overstrike "it" and insert immediately thereafter "the investment advisory contract"

Page 1, line 8, overstrike "shall" and insert immediately thereafter "may"

Page 1, line 10, after "This" insert "subdivision"

Page 1, line 12, after the period insert "Upon request, the commissioner may waive the requirements of this subdivision for an investment advisory contract that conforms to the limitations of section 205 of the Investment Advisers Act of 1940 [Pub. L. 768; 54 Stat. 852; 15 U.S.C. 80b-5] and the rules adopted thereunder."

Page 2, remove lines 1 and 2

Renumber accordingly

Date: 3/8/11  
Roll Call Vote # 1

2011 SENATE STANDING COMMITTEE ROLL CALL VOTES  
BILL/RESOLUTION NO. HB 1095

Senate Industry, Business and Labor Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number \_\_\_\_\_

Action Taken: ☐ Do Pass ☐ Do Not Pass ☐ Amended ☒ Adopt Amendment  
☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Senator Schneider Seconded By Senator Andrist

Senators	Yes	No	Senators	Yes	No
Chairman Jerry Klein	✓		Senator Mac Schneider	✓	
VC George L. Nodland	✓		Senator Philip Murphy	✓	
Senator John Andrist	✓				
Senator Lonnie J. Laffen	✓				
Senator Oley Larsen	✓				

Total (Yes) 7 No 0

Absent 0

Floor Assignment \_\_\_\_\_

If the vote is on an amendment, briefly indicate intent:

Date: 3/8/11  
Roll Call Vote # 2

2011 SENATE STANDING COMMITTEE ROLL CALL VOTES  
BILL/RESOLUTION NO. HB 1091

Senate Industry, Business and Labor Committee

☐ Check here for Conference Committee

Legislative Council Amendment Number \_\_\_\_\_

Action Taken: ☒ Do Pass ☐ Do Not Pass ☒ Amended ☐ Adopt Amendment  
☐ Rerefer to Appropriations ☐ Reconsider

Motion Made By Senator Schneider Seconded By Senator Murphy

Senators	Yes	No	Senators	Yes	No
Chairman Jerry Klein			Senator Mac Schneider		
VC George L. Nodland			Senator Philip Murphy		
Senator John Andrist					
Senator Lonnie J. Laffen					
Senator Oley Larsen					

Total (Yes) 7 No 0

Absent 0

Floor Assignment Senator Schneider

If the vote is on an amendment, briefly indicate intent:

**REPORT OF STANDING COMMITTEE**

HB 1091, as engrossed: Industry, Business and Labor Committee (Sen. Klein, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (7 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). Engrossed HB 1091 was placed on the Sixth order on the calendar.

Page 1, line 6, overstrike "into"

Page 1, line 7, overstrike "it" and insert immediately thereafter "the investment advisory contract"

Page 1, line 8, overstrike "shall" and insert immediately thereafter "may"

Page 1, line 10, after "This" insert "subdivision"

Page 1, line 12, after the period insert "Upon request, the commissioner may waive the requirements of this subdivision for an investment advisory contract that conforms to the limitations of section 205 of the Investment Advisers Act of 1940 [Pub. L. 768; 54 Stat. 852; 15 U.S.C. 80b-5] and the rules adopted thereunder."

Page 2, remove lines 1 and 2

Renumber accordingly

2011 HOUSE JUDICIARY

CONFERENCE COMMITTEE

HB 1091

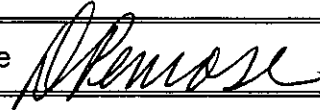
# 2011 HOUSE STANDING COMMITTEE MINUTES

House Judiciary Committee  
Prairie Room, State Capitol

HB 1091  
April 1, 2011  
16273

☒ Conference Committee

Committee Clerk Signature



## Minutes:

Chairman Koppelman: We will open the conference hearing on HB 1091. Would the Senate like to explain what the Senate did and why.

Sen. Andrist: The principle change is, of course, is the addition of lines 13-16.

Sen. Schneider: I'm passing around an email from someone I went to high school with who went to University of Minnesota Carlson School of Management, worked in New York as a financial advisory out there and ultimately returned to ND to come back and be an investment advisor. Bright, young guy, incredibly talented; his fund is doing really well. The problem is that ND does not allow for the charging of a performance fee under current law. This is something that is done on the federal level; it's done in many, many states, possibly all of them. This prohibition basically means he would have to move his business across state lines, if he wanted to charge a performance fee. The Senate amendments give the Commissioner the statutory authority to waive the requirements of subdivision a, when an investment advisory contract conforms to 15USC80B5. That is the section of the Investment Advisor's Act that spells out the requirements for these investment advisory contracts. I have that here if anyone wants to take a look at it; it's not too complicated of a statute. This is an area where the law really needs to catch up with business. This is something that is done frequently throughout the country. We know that there will be oversight of it, because they have to adhere to this federal statutory provisions regarding the requirements of investment advisory contracts and ultimately the Securities Commissioner will have oversight as well. It's a benign change that's going to allow two constituents who are investment advisors of this type to lawfully operate their business in North Dakota.

Rep. Koppelman: Any further discussion. Let me go over why the House didn't concur with your amendments. This will probably be the issue at hand that will need to be resolved as a conference committee. I've read the Senate minutes as we were sitting here, and I would encourage you to read the House minutes as well before we meet next because I think it will help get the full flavor for this. The House Judiciary Committee has no objection to working with business to allow our regulators of

business to have some flexibility in terms of doing exactly what Sen. Schneider talks about. The bone of contention that we have is more of a structural one. Sen. Andrist and I are the only two that have served on the Administrative Rules Committee and this issue really does get down to administrative rules and statute and how they function and how agencies of government work with them. As the bill originally came to us in the House, if you look at the 1000 version, it said except as permitted by rule, and then it went on to go through the statute and not change the current statute, and then it ended by saying the Commissioner may, by rule, waive any other provisions of this subsection and may specify the contents of an investment advisory contract entered into, extended or reviewed by an investment advisor. Except as permitted by rule, it is unlawful. The problem with that is it turns everything upside down. Administrative rules are subservient to law, not the other way around. I've never seen in my time in the legislature, nor has Legislative Council ever heard of an instance where we've allowed an agency of government to supersede state law by a rule that they've promulgated. That is our bone of contention in the House. I think the Senate version attempts to accommodate the Commissioner's concerns, but I think it kind of leaves that issue at play. I don't know what the way to resolve this is. Just a little background on administrative rules. We adopt laws and administrative rules do carry the force and effect of law, and that's a legislative prerogative, we are delegating to the executive branch of government, to the agencies of government, the authority essentially to make law. So they write rules, go through the process where they have public hearings and public input, publish the rules, etc. When they are about to go into effect, they come before a standing committee of the Legislature, called the Administrative Rules Committee, and that committee has the authority to do a couple of things. The committee can decide to void the rule, under certain parameters. There are parameters in law that the committee has to stay within. Some of them are if the agency went outside of legislative intent, if they are being arbitrary and capricious, etc.; there are six or seven different parameters or guidelines under which that committee can void a rule. That happens, but very seldom. The committee can void a rule or a portion of a rule that it finds is outside the boundaries of what the agency should be doing. The second thing the committee can do is that it can agree with the agency to amend the rule. So if a rule comes in and members of the Administrative Rules Committee, which is a bi-cameral, with House and Senate members, say that we've really got heartburn over this, then the agency looks at it and says that we have your point, we can change it to read this way instead and then if everybody agrees with that, a rule can be amended at that point by the consensus of both the committee and the agency involved. When the rule goes into effect, it carries the force and effect of law. It's every bit as enforceable in the public and business community, and the regulatory community as if it were a statute. That's why we're careful about making sure that 1) statutes are the highest authority, because that's what the people elect us to make and that should be the supreme law of the land; and statutes overrule Rules. That's why it's so onerous to have something in a statute that would say, well, this statute applies except/unless this agency decides to make a rule and then the rule supersedes. That's really our question. I don't have any heartburn or

problem personally over what the Commissioner is trying to accomplish. It's just that fundamental principle that I think we're dealing with.

Sen. Andrist: While you have been talking, it took me a while to get up to speed in the bill; now it's more there. You provided a very good explanation of the administrative rules and how they work. There wouldn't be a problem that I can see, having been a member of the Administrative Rules Committee, to also apply the same kind of exception that we're providing in the Senate amendment. Where the rubber meets the road on this, the Securities Commissioner came to us and explained why this was necessary. Our IBL committee deals with that agency a great deal, you probably don't. I think there is a very high level of confidence for our committee in the person who has this job. She persuaded us that, even though we don't understand all of these technicalities that this just would not work as it was amended by the House. She came to us originally and asked us to kill the bill, because she said that it just wasn't workable. Then Sen. Schneider intervened and asked if there was some way that we can fix it. This is how she fashioned a fix and that's what we did. For myself, I'm not a financial expert, even though I'm a pretty active investor and I deal with people who deal with this. I have a high level of trust for her and that's mostly why I bought into the amendments.

Rep. Koppelman: I certainly respect that and I have nothing negative to say about the Securities Commissioner as a person or the activity of her office that would be negative or call into question the excellent work that they do. I do believe, and this is based on not only this bill but other bills we have looked at this legislative session, and frankly other discussions we've had really for the past biennium on the Administrative Rules Committee, that there is a bit of misunderstanding or naiveté on the part of the Securities Commissioner's office as to how the Administrative Rules process works. Because, historically, and this has alarmed some legislators in the past couple of years; they have taken the policies. I was the chairman of the Council of State Governments. I understand these national groups. I understand that they do all kinds of things, and they have committees and make recommendations, etc. Most of the administrative officials that we have in state government have the same kinds of groups. The National Association of Insurance Commissioners, etc. and the Secretary of State have one as well. So that national body makes policy recommendations or model policies. Much to the alarm of many legislators is that the Securities commissioner has been adopting those suggested policies as policies of her agency, which she's free to do; however, she's been attempting to enforce them as law. As if they were an administrative rule or a statute. That's where the rub is, no agency in state government, can enforce a policy they decide to adopt just because they think it is a good idea with the force and effect of law unless it's either in our century code or been adopted by an administrative rule.

Sen. Andrist: I just want to say. You are talking about another bill that has dealt with this agency, where the House proposed that we make her write all of this in Administrative rules. The rest of the group isn't in the administrative rules process



like you are Rep. Koppelman. We get into minutia, the tiny legal details. When we get 200 pages of environmental changes from the Health Department, if they have to put into administrative rules, we don't read that stuff, we just approve it. Most of these rules, I think the Securities Commissioner is subject to administrative rules, the agency is generally. But most of these items she's putting in, is language passed at the federal level, they comply with federal law. From my standpoint, as a long-term administrative rules member, I'm happy not to have to look at 200 more pages and kill a couple more trees to read some of this minutia, because someplace along the line, we have to trust the agency heads, because invariably if they make serious mistakes, those mistakes get back. I think they are relatively careful. I would hope that you would accede to the Senate amendment. I think we can trust the Securities Commissioner on this to be judicious. I would like to keep these investment advisors in ND too.

Sen. Schneider: I think your comments on administrative rules are dead on. We trust appointed Bureaucrats, and I don't mean that in a pejorative way to essentially enact rules that have the force of law. I share that concern and that's why I feel good about the Senate amendments because there's really no rule-making authority involved here. There is just a narrow statutory authority to waive the requirements of the subdivision. Reading this language as I see this operating mechanically, upon request the commissioner may waive the requirements of this subdivision for an investment advisory contract that conforms to the limitations of this federal law. It's very narrow and direct. It would only be used upon request. I can tell you right now, that there would only be two requests for this. There's really no rule-making involved here. We're giving her statutory authority, which is our duty as legislators to waive the requirements currently under law of the investment advisory contract. I think your concerns are valid but I think they are addressed to some extent in the Senate version. If we can address them further, I would be amenable to that.

Rep. Koppelman: The concern that I still have, and again, I don't think we disagree on the practical outcome that we're all seeking, allowing the securities commissioner to do this. I think what we're disagreeing about is the mechanics of how that's accomplished. Maybe we have a disagreement with the Securities Commissioner's office or misunderstanding of how that ought to be accomplished. What sticks in our craw on the House side, and it was unanimous in our Committee, and it was a pretty strong feeling on the House side that we've really got to be careful here that we don't set a precedent that is really dangerous. Any time I see in a statute that says, here's the law of the land, but this Bureaucrat can decide to waive it in these cases, if he/she decides that. I think that is setting us on a path that is really a road we don't want to go down. I would like to see this committee visit with the securities commissioner and try to help them better understand the concerns of the legislature and maybe come up with some language that either the statute needs to be narrowed and we can say, that they can do this if rules are the proper way to do it, they can do it that way, or allow them to write something. But anytime we allow them to supersede what a statute says, that's where my concern lies. The other matter that I mentioned, that what happened to a couple of constituents during the

last biennium and I think it had to do with investment advisory contracts, but I'm not positive of that. The concern was that the securities commissioner's office was attempting to enforce those policies that they adopted on the investment advisors of our state as if they were the law. In other words, they were saying that you have to do this in your contract and the investment advisor would say, who says I have to. Well I do (commissioner). Where is the rule that says I have to? I'm the securities commissioner and I say you have to. That was the problem. Frankly you might get people to kowtow doing that, but if that ever came down to a legal question, I'm sure an attorney would tell us that they're going to have trouble enforcing that if it's not a statute or a rule. We could be putting the full faith and credit of the state in jeopardy by an agency of government attempting to do something that is beyond their bounds of authority. That's really where my concern lies.

Sen. Schneider: I was just wondering if anybody has any specific direction as to how we can narrow this further. I think it is pretty narrow now. An investment advisory contract has to conform to this federal law. If there is some other concern, the commissioner may or may not waive. We're only talking about a handful of people and maybe a couple more over the course of the next couple of decades. I don't think that we are superseding any statute because we're the ones providing statutory authority to do this.

Rep. Koppelman: That's kind of my point. If we put in a statute, that here is the law of the land, but (anyone) can waive it if they decide to. I think that's really bad law. I think the direction we should look at is to visit with the security commissioner's office about this. I think this is different from the way they've done business, but I think the way they've done business is dangerous and precarious for the state. I want to give them the authority to do what they are there to do, statutorily that's fine. But maybe we need to narrow the statute instead of saying that they can waive the statute, maybe we need to narrow the statute and give them some authority statutorily to do more than what the statute gives them now or something like that. That might be the amendment that comes out of the committee.

Sen. Andrist: We spent quite a bit of time visiting with the securities commissioner and she came to us not with this proposal, she came and asked us to kill the bill because it does me more harm than good. A couple of our members intervened and asked if we could fix it. That's what we tried to do. We were satisfied that it was pretty well fixed, so I think at this point we ought to have you and Sen. Schneider visit with the securities commissioner and talk to her to see if there is a way to satisfy the needs of both sides. If we can't come up with something, we will follow her advice and kill the bill.

Rep. Koppelman: I think that's a good suggestion. I think we should be constructive and try to come up with something. I think if you would ask any executive branch official in the tower or elsewhere in the city, would you rather go through the rule-making process and have those public hearings and publish the notices of those in the newspaper and then come before the Administrative Rules Committee or would

you rather just decide what you want to do by edict and just do it, and they would all choose the latter, but that's not the way we do things in ND. That's why I think it is important that we have an understanding there and I think your suggestions is good. I think with myself, Sen. Schneider and the intern meeting with the securities commissioner or someone from that office could be a subcommittee of the conference committee and see if there is something we can do and come back. We will recess the conference committee.

# 2011 HOUSE STANDING COMMITTEE MINUTES

House Judiciary Committee  
Prairie Room, State Capitol

HB 1091  
April 6, 2011  
16384

☒ Conference Committee

Committee Clerk Signature

*Openrose*

## Minutes:

Chairman Koppelman: We will reopen the conference committee on HB 1091. We met with the Securities Commissioner, Deputy Commissioner, Sen. Schneider, the intern and I asked John Walstad to join us. He works with the Administrative Rules for Legislative Council. He's also the chief code reviser, so he really understands what is needed in the legislative language and understands what we're trying to arrive at here. Because he wasn't able to be there, the folks from the Securities Dept., Sen. Schneider and I met with him yesterday. I don't think any of us disagree on the objective. I think it's just the mechanics we're talking about. I am passing around the language we discussed and that Mr. Walstad is putting into an amendment. We can look at this, but we will wait until we see the language in context before we take a vote on it (see attached 1). The Deputy Commissioner actually suggested some language in our meeting yesterday that Sen. Schneider and I agree would be a good way to resolve the issue. That's what we gave to Mr. Walstad to craft in proper legislative form and style. I think we're close to a resolution on this bill. Thanks to all for working on this, this is how all conference committee should work; to get together and figure out our differences and resolve them. The original version of the bill as submitted had language that said, except as provided by rule. We didn't like that in the House because it implied administrative rules were overruling statute. The Senate version had an exception that referenced the federal law and this really isn't far from that but I think it does it in a better way (read the proposed language).

Sen. Andrist: I would like to thank the subcommittee. This looks like very good language. It's my understanding that she couldn't have permitted an investment advisory contract that was out of compliance with the federal law anyway.

Rep. Koppelman: Unless I am misunderstanding this, what it could have done was to force some people out of the state in terms of where they do business, because the kinds of fees that are charged, under previous federal law and under the law in most states, which mirrored that law, said that you couldn't charge this kind of fee. So what we are trying to accomplish here is allowing an exception for that. If we

don't allow the exception, it means that those folks can't charge the fee in ND and they might relocate outside the state. I think this is a good solution.

Sen. Schneider: This approach is more of a true exception to the statute rather than providing statutory authority to the Commissioner to review these for conformance with the Investment Advisors Act, in that particular section of the act. This still puts us in the same place in the end.

Rep. Koppelman: In conference committees we don't rehear the bill, but I see that the Securities Commissioner and the deputy are here, is there anything that we've stated that is incorrect or need to clarify for the committee.

Karen Tyler, ND Securities Commissioner: I would just follow up on an issue that came up yesterday when we were discussing this. The issue of whether or not this language that has ultimately been crafted, if it takes away authority at all, and prevents us from safeguarding against the issue of an investment advisor perhaps charging fees that are onerous, and that isn't an issue because in the regulation of investment advisors as opposed to the regulation of stockbrokers; investment advisors are bound by a fiduciary duty to their clients. That's very different from the stockbroker who's only held to a suitability standard. An investment advisor is bound by this fiduciary duty. So charging a performance fee that would be excessive, we would be able to take an enforcement action on that matter, based on the fact that the advisor has breached their fiduciary duty to their client. So I wanted to make that point, because it came up sort of at the end of our conversation yesterday.

Sen. Andrist: It would seem to me with this language that you would still have the authority necessary to take action against an investment advisory, because it says it does not prohibit an investment. So you still have the latitude that you need, don't you.

Karen Tyler: It does exactly what we need it to do. There's an express prohibition, but then this language says it does not prohibit from charging that performance fee. We are in good shape with this language.

Rep. Koppelman: I think the language is more in keeping with what we typically do in statutory language, not that there aren't exceptions; where we craft the law and then if we want to make an exception, we state the exception. We will recess until we have the amendment from Legislative Council. We will recess the conference committee.

# 2011 HOUSE STANDING COMMITTEE MINUTES

House Judiciary Committee  
Prairie Room, State Capitol

HB 1091  
April 11, 2011  
16483

☒ Conference Committee

Committee Clerk Signature

*Openrose*

## Minutes:

Ch. Koppelman: We will re-open the conference committee on HB 1091. If you recall from our discussion at the last meeting, we had some language that had been essentially crafted by the Securities Commissioner's office after our subcommittee discussion with them and we were waiting for was properly crafted language from Legislative Council. It is in amendment form. I think it's verbatim from what I saw of what was discussed. What are the committee's wishes?

Sen. Andrist: I move that the Senate recede and adopt amendments on .02002.

Sen. Schneider: Second the motion.

**6 YES 0 NO 0 ABSENT**

**SENATE RECEDE AND ADOPT AMENDMENTS ON .02002**

VR  
4/11/11

PROPOSED AMENDMENTS TO ENGROSSED HOUSE BILL NO. 1091

That the Senate recede from its amendments as printed on pages 980 and 981 of the House Journal and page 697 of the Senate Journal and that Engrossed House Bill No. 1091 be amended as follows:

Page 1, line 6, overstrike "into"

Page 1, line 7, overstrike "it" and insert immediately thereafter "the investment advisory contract"

Page 1, line 8, overstrike "shall" and insert immediately thereafter "may"

Page 1, line 10, after "This" insert "subdivision"

Page 1, line 12, after the period insert "This subdivision does not prohibit an investment advisory contract that provides for performance fees permitted and determined in accordance with section 205 of the Investment Advisers Act of 1940 [Pub. L. 768: 54 Stat. 852; 15 U.S.C. 80b-5] and the rules adopted thereunder."

Page 2, remove lines 1 and 2

Renumber accordingly

# 2011 HOUSE CONFERENCE COMMITTEE ROLL CALL VOTES

Committee: JUDICIARY

Bill/Resolution No. 1091 as (re) engrossed

Date: 4/11/11

Roll Call Vote #: 1

## Action Taken

- ☐ HOUSE accede to Senate amendments  
☐ HOUSE accede to Senate amendments and further amend  
☐ SENATE recede from Senate amendments  
☒ SENATE recede from Senate amendments and amend as follows

House/Senate Amendments on HJ/SJ page(s) 980 -- 981

- ☐ Unable to agree, recommends that the committee be discharged and a new committee be appointed

((Re) Engrossed) 1091 was placed on the Seventh order of business on the calendar

Motion Made by: Sen. Andrisc Seconded by: Rep. Schneider

Representatives				Yes	No		Senators				Yes	No
<u>Rep. Koppelman</u>				✓			<u>Sen. Andrisc</u>				✓	
<u>Rep. Cradler</u>				✓			<u>Sen. Laffan</u>				✓	
<u>Rep. Guggisberg</u>				✓			<u>Sen. Schneider</u>				✓	

Vote Count Yes: 6 No: 0 Absent: 0

House Carrier Rep. Koppelman Senate Carrier Rep. Schneider

LC Number 11.8016.02002 . 04000 of amendment

LC Number \_\_\_\_\_ of engrossment

Emergency clause added or deleted

Statement of purpose of amendment



**REPORT OF CONFERENCE COMMITTEE**

**HB 1091, as engrossed:** Your conference committee (Sens. Andrist, Laffen, Schneider and Reps. Koppelman, Beadle, Guggisberg) recommends that the **SENATE RECEDE** from the Senate amendments as printed on HJ pages 980-981, adopt amendments as follows, and place HB 1091 on the Seventh order:

That the Senate recede from its amendments as printed on pages 980 and 981 of the House Journal and page 697 of the Senate Journal and that Engrossed House Bill No. 1091 be amended as follows:

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Page 2, remove lines 1 and 2

Renumber accordingly

Engrossed HB 1091 was placed on the Seventh order of business on the calendar.

2011 TESTIMONY

HB 1091

**HB 1091**

**Testimony of Deputy Securities Commissioner Michael Daley**

**Before the House Judiciary Committee**

**January 12, 2011**

Mr. Chairman and members of the Committee, good morning. I am Michael Daley, Deputy Securities Commissioner and Enforcement Attorney for the Securities Department. I am here today to testify in favor of House Bill 1091 on behalf of Securities Commissioner Karen Tyler.

Many of you are familiar with the operation of the Securities Department but I want to briefly outline what we do. Our mandate is to protect North Dakota investors who purchase securities and investment advice in this state through the administration of the North Dakota Securities Act, N.D.C.C. Chapter 10-04. We deliver on this mandate through our efforts in four functional areas:

- 1) Regulation of the Capital Formation Process
- 2) Registration and Regulation of Securities Industry Firms and Professionals
- 3) Examinations, Investigations and Enforcement Actions
- 4) Investor Education and Financial Literacy Initiatives

House Bill 1091 and the proposed amendments to N.D.C.C. §10-04-10.1 deal solely with the regulation of state registered investment adviser firms (as opposed to “federal covered investment advisers”) and their permissible fees and contract terms. The requested rule-making authority was necessitated by the passage last July of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

There are two types of securities professionals registered with and regulated by the states in which they do business, "investment adviser representatives" and registered "agents" of broker-dealers, more commonly known as stock brokers. Investment adviser firms and their representatives are legally bound by a fiduciary duty to place their clients' interests ahead of their own. They are generally compensated on the basis of an hourly fee or a percentage of their client's assets under management (AUM). They are prohibited from charging an unreasonable fee and, for state registered advisers in North Dakota, prohibited from charging a performance fee under current law.

Agents, on the other hand, are not fiduciaries and their conduct is measured by whether or not the securities they recommend to an investor are "suitable", based on the investor's income, net worth, investment experience, tolerance for risk and diversification. Agents are generally compensated on the basis of a commission for each transaction completed.

As noted, this Bill deals only with the regulation of investment advisers.

Currently regulation of investment advisers is split between the states and the Securities and Exchange Commission. Investment advisers with AUM of \$25 million or less register with the states and those with AUM greater than \$25 million register with the SEC. Dodd-Frank changes that AUM threshold from \$25 million to \$100 million and the effective date of the switch is July 21, 2011, one year after its enactment.

Under federal law, the Investment Advisers Act of 1940 and the Investment Company Act of 1940, certain advisers of "private funds" were exempt from registration with either the states or SEC. Also, federal covered investment advisers were allowed to charge a performance fee in certain limited circumstances, when the clients were all

deemed to be “qualified clients”, defined as having \$750,000 of assets under management with the adviser, \$1.5 million dollars in net worth, or is a “qualified purchaser” as defined in section 2(a)(51)(A) of the Investment Company Act of 1940.

Dodd-Frank eliminated the exemption for “private fund advisers” but also created a new exemption for “venture capital fund” advisers and gave the SEC one year to adopt rules defining the term. Both the SEC and the North American Securities Administrators Association are currently working on proposals for the reporting and registration requirements for “private fund advisers” previously exempt, but which will now fall within the definition of “investment adviser” under N.D.C.C. § 10-04-02(10).

With the implementation of Dodd-Frank, we expect to have investment advisers currently regulated by the SEC, and currently allowed to charge performance fees and to have custody of client funds or assets in certain circumstances, transitioning to our jurisdiction. While the Securities Commissioner already has rulemaking authority under N.D.C.C. § 10-04-03, as necessary to administer the Securities Act, that rulemaking authority would not allow for rules that directly contradict current legislative prohibitions such as are set forth in the current language of N.D.C.C. § 10-04-10.1(5)(no performance fees) and (6)(no custody).

By approving House Bill 1091, to create rulemaking authority in the area of investment advisory contracts and custody, you will enable the Securities Commissioner to propose appropriate exceptions to existing law, which would eliminate business disruption and any new regulatory burden for investment advisers transitioning from federal to state law, as well as changes that are likely to be required by actions taken by

the SEC at the direction of Congress in the coming months and before the next legislative session in 2013.

The specific language in the amendment is derived from §502(c) of the Uniform Securities Act of 2002 as adopted by the National Conference of Commissioners on Uniform State Laws.

The Securities Commissioner would respectfully recommend a “do-pass” for House Bill 1091. Mr. Chairman and members of the Committee, thank you for your time and consideration. I would be happy to answer any questions you may have.

This subdivision does not prohibit an investment advisory contract that provides for performance fees permitted and determined in accordance with section 205 of the Investment Advisers Act of 1940 [Pub. L. 768; 54 Stat. 852; 15 U.S.C. 80b-5] and the rules adopted thereunder .

On Fri, Apr 1, 2011 at 9:46 AM, Steven Nelson <steven.nelson@prairiewoodvalue.com> wrote:  
HI Mac -

If ND financial advisors were able to charge a performance fee under certain circumstances, it would then be consistent with Federal law and other states. I believe the Federal rule is the client must be a qualified investor (over \$1.5 minimum net worth or \$750k of assets with the adviser).

This amendment would level the playing field as I compete with out of state firms. It would allow me to better serve clients who wish to pay for my services based upon how I perform rather than simply based upon assets under management. These clients can currently obtain a performance-based fee arrangement from non-ND financial advisors. In addition, there could be a ND-based investment advisor that is larger that would fall under SEC regulation, and then could offer his clients a performance-based fee arrangement. It would be hard to compete with them.


I don't believe there is a conflict of interest, which is the reason the current law exists. I am a fiduciary, so I am required to put my client's interests ahead of mine. ND would have no issue will me charging a very high management fee, but they currently have a problem with me charging a percentage of the gain over a market benchmark.

Thanks,

Steve

Steven M. Nelson, CFA





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