ORIGINAL NEW APPLICATION

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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

GARY PIERCE, Chairman
BOB STUMP
SANDRA D. KENNEDY
PAUL NEWMAN
BRENDA BURNS

In the matter of:

MARK DANA HUGHES, CRD# 1843511, and DOLLY A. HUGHES, husband and wife,

and

LEGACY FINANCIAL ADVISORS, L.L.C., CRD# 114029, an Arizona limited liability company,

Respondents.

DOCKET NO. S-20864A-12-0439

NOTICE OF OPPORTUNITY FOR HEARING REGARDING PROPOSED ORDER TO CEASE AND DESIST, ORDER FOR RESTITUTION, ORDER OF REVOCATION, ORDER FOR ADMINISTRATIVE PENALTIES, AND ORDER FOR OTHER AFFIRMATIVE ACTION

NOTICE: EACH RESPONDENT HAS 10 DAYS TO REQUEST A HEARING

EACH RESPONDENT HAS 30 DAYS TO FILE AN ANSWER

The Securities Division ("Division") of the Arizona Corporation Commission ("Commission") alleges that respondents Mark Dana Hughes and Legacy Financial Advisors, L.L.C. have engaged in acts, practices, and transactions that constitute violations of the Arizona Investment Management Act, A.R.S. § 44-3101 *et seq.* ("IM Act").

I.

JURISDICTION

1. The Commission has jurisdiction over this matter pursuant to Article XV of the Arizona Constitution and the IM Act.

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II.

RESPONDENTS

2. Mark Dana Hughes (CRD# 1843511) ("Hughes") is a married man believed to be residing in Tucson, Arizona and Pinos Altos, New Mexico. At all times relevant, Hughes resided in Tucson, Arizona.

3. At all relevant times Hughes has been the spouse of Dolly A. Hughes.

4. Dolly A. Hughes may be referred to hereafter as "Respondent Spouse." Respondent Spouse is joined in this action under A.R.S. § 44-3291(C) solely for purposes of determining the liability of Hughes' and Dolly A. Hughes' marital community.

5. At all relevant times Hughes has been acting for his own benefit, and for the benefit or in furtherance of the marital community with Respondent Spouse.

6. On or about April 7, 2008, Legacy Financial Advisors, (CRD# 114029), which was owned and operated by Hughes as a sole proprietorship, became licensed as an investment adviser in Arizona. Prior to this date, Legacy Financial Advisors had been registered with the Securities and Exchange Commission and noticed filed with the Commission. [1]

7. On or about December 8, 2009, Hughes changed the form of his business from a sole proprietorship to an Arizona limited liability company named Legacy Financial Advisors, L.L.C. Legacy Financial Advisors, L.L.C. was located in and operated from Tucson, Arizona. For the purposes of this Notice the sole proprietorship and the Arizona limited liability company will be collectively known as "LFA".

8. Hughes was LFA's sole owner, member, managing member, compliance officer and investment adviser representative.

9. Hughes or LFA may each be referred to as "Respondent."

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[1] Hughes registered the business names Legacy Financial Advisors and Legacy Financial Advisors Inc. with the SEC. The notice filing status with the Commission terminated on April 29, 2008.

10. As LFA's sole managing member and compliance officer Hughes was responsible for LFA's Form ADV regulatory filings and ensuring that LFA's policies and procedures were implemented and followed.

11. On or about July 6, 2012, LFA filed an ADV-W through the IARD system requesting to withdraw its Arizona license. In its filing LFA represented it was no longer in business or closing its business. On July 16, 2012, the Division processed LFA's ADV-W filing, thereby terminating LFA's Arizona investment adviser license effective July 6, 2012.

12. In its ADV-W filing, LFA states its principal (Hughes) will maintain "all past records…." LFA's ADV-W filing further identifies the location of its records as 4549 N. Camino Campero, Tucson, Arizona.

III.

FACTS

A. SUITABILITY

13. From January 2009 until Hughes closed his client trading accounts at the end of June 2012 Hughes traded almost exclusively in all LFA client accounts in leveraged Exchange Traded Funds ("ETFs"). The ETFs traded by LFA and Hughes magnified the performance of a stated index by two or three times, depending on the particular ETF, and were meant to be traded frequently with a minimal holding period. The disclosures associated with these ETFs advised investors that the ETFs do "not seek to achieve its stated investment objective over a period of time greater than one day." They were subject to frequent rapid swings in price during the day and provided more opportunities to realize short-term gains than other less volatile securities. However, just as they were designed to provide for greater profit, the potential for losses was similarly magnified.

14. These ETFs presented a series of risks. First, there is leverage risk. Whether the ETF was leveraged two or three times, the result is a reduction of 2 or 3 percent for each 1 percent daily increase, excluding the costs of financing and operating the fund. Second, there is inverse

risk. If the underlying index moves in the opposite direction than expected, there will be a loss of funds. Third, the underlying index itself may be risky. For example, an index consisting of small and/or mid-sized capitalized companies present greater investment risk than found with larger more established companies.[2]

15. Some of LFA's clients were principally conservative to moderately conservative investors. These clients described or characterized their investment objectives to Hughes in a variety of ways including telling Hughes they were either risk adverse, had limited resources, that they could ill-afford principal loss or that they did not have sufficient annual income and or assets to warrant investment in securities that were speculative or high-risk. Some of LFA's clients had moderately aggressive investment objectives when they began their relationship with LFA, however, life events caused some of these more aggressive investors to change their investment objectives to conservative which they clearly communicated to LFA/Hughes.

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[2] To better understand the risks associated with ETFs it is instructive to review the Financial Industry Regulatory Authority's ("FINRA") June 2009, Regulatory Notice 09-31 regarding non-traditional ETFs; ETFs that are leveraged and inverse exchange-traded funds. FINRA noted that these ETFs are "highly complex financial instruments that are typically designed to achieve their stated objectives on a daily basis." Because of the nature of the ETFs, their long-term performance may differ considerably from the daily objective. Therefore, FINRA concluded "inverse and leveraged ETFs that are reset daily typically are unsuitable for retail investors who plan to hold them for longer than one trading session…."

FINRA provided the two following examples of the downside risk of these types of ETFs for the time period between December 1, 2008, and April 30, 2009:

- The Dow Jones U.S. Oil & Gas Index gained 2 percent, while an ETF seeking to deliver twice the index's daily return fell 6 percent and the related ETF seeking to deliver twice the inverse of the index's daily return fell 26 percent.
- An ETF seeking to deliver three times the daily return of the Russell 1000 Financial Services Index fell 53 percent while the index actually gained 8 percent. The related ETF seeking to deliver three times the inverse of the index's daily return declined by 90 percent over the same period.

As a result, FINRA said if ETFs are to be recommended, then they "must be suitable and based on a full understanding of the terms and features of the product recommended." The suitability determination requires a review of the customer's financial status, tax status, investment objectives, and other information about the client. FINRA also refers to its Regulatory Notice regarding fair dealing with customers with new financial products. FINRA observed that every effort should be made to make customers aware of the pertinent information regarding such products and that each customer's financial situation, trading experience, ability to meet the risks involved with such products should be considered before recommending these types of products.

FINRA is the brokerage industry's self-regulatory organization operating under the supervision and oversight of the United States Securities and Exchange Commission.

THE ETFs TRADED BY LFA/HUGHES

16. Almost all of the securities traded by Hughes in LFA's client accounts involved leveraged and/or inverse ETFs.[3] Each of these ETFs was designed to correspond to a multiple of the inverse of the daily price performance of an underlying index. The majority of transactions effected in LFA client accounts involved the following inverse and/or leveraged ETFs:

- EDC - Direxion Daily Emerging Markets Bull 3x Shares – the underlying index is the MSCI Emerging Markets IndexSM.
- EDZ - Direxion Daily Emerging Markets Bear 3x Shares – the underlying index is the MSCI Emerging Markets IndexSM.
- ERX - Direxion Daily Energy Bull 3x Shares – the underlying index is the Energy Select Sector Index.
- ERY - Direxion Daily Energy Bear 3x Shares– the underlying index is the Energy Select Sector Index.
- FAS - Direxion Daily Financial Bull 3X Shares – the underlying index is the Russell 1000A® Financial Service Index.
- FAZ - Direxion Daily Financial Bear 3x Shares– the underlying index is the Russell 1000A® Financial Service Index.
- TNA - Direxion Daily Small Cap Bull 3x Shares - the underlying index is the Russell 2000® Index.
- TYH - Direxion Daily Technology Bull 3X Shares[4] - the underlying index is the Russell 1000® Technology Index.
- TYP - Direxion Daily Technology Bear 3X Shares[5] - the underlying index is the Russell 1000® Technology Index.
- TZA - Direxion Daily Small Cap Bear 3x Shares – the underlying index is the Russell 2000® Index.

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[3] Hughes made an insignificant number of trades in other ETFs and non-leveraged securities. The following is a partial list: DJP – Dow Jones UBS Commodity Total Return Index, an ETF; ACAS (American Capital) is a stock; JNK - SPDR Barclays Capital High Yield; PHK – Pimco High Yield Fund, a mutual fund; VXX – I path S&P 500 VIX Short Term Futures, an ETF; and XKN – Lehman ABS Corp 7.70 CorTS 2001.

[4] TYH trades under a new symbol: TECL.

[5] TYP trades under a new symbol: TECS.

- URE - ProShares Ultra Real Estate 2x Shares – the underlying index is the Dow Jones U.S. Real Estate Index.

- TBT – ProShares Ultra Short 20+ Year Treasury 2x Shares – the underlying index is the Barclays Capital U.S. 20+ Year Treasury Index

17. The prospectuses pertaining to these ETFs explicitly state that they employ leveraging and that the ETFs should not be expected to achieve their stated objectives when held longer than one day. One example of an ETF that Hughes traded for his clients was TZA. TZA is a 3x leveraged, inverse ETF. It does not invest in equity securities; in fact, it is 100 percent invested in derivatives. Regarding the derivatives, the TZA prospectus says TZA "uses investment techniques such as futures and forward contracts, options and swaps, which may be considered aggressive."

18. The TZA ("Fund") prospectus offered the following as important information:

> The pursuit of daily leveraged goals means that the Fund is riskier than alternatives that do not use leverage because the Fund's objective is to magnify the performance of the [Russell 2000] Index. The pursuit of daily leveraged investment goals means that the return of the Fund for a person longer than a full trading day may bear no resemblance to -300% of the return of the Index for such longer period because the aggregate return of the Fund is the product of the series of daily leveraged returns for each trading day.

19. Regarding TZA's investment objective, the TZA prospectus said:

> The Fund seeks daily investment results, before fees and expenses, of 300% of the inverse (or opposite) of the performance of the Russell 2000® Index ("Index"). **The Fund *seeks* daily leveraged investment results and does not seek to achieve its stated investment objective over a period of time greater than one day.** The Fund is different and much riskier than most exchange-traded funds.
>
> **The Fund is designed to be utilized only by knowledgeable investors who understand the potential consequences of seeking daily leveraged investment results, understand the risks associated with shorting and the use of leverage, and are willing to monitor their portfolios frequently. The Fund is not intended to be used by, and is not appropriate for, investors who do not intend to actively monitor and manage their portfolios.** (Emphasis in original).

20. Besides the risk associated with inverse and leveraging, there is also the risk with the underlying market Index. The TZA prospectus said, "Investing in the securities of small and/or mid capitalization companies involves greater risks and the possibility of greater price volatility than investing in more-established, larger capitalization companies."

CLIENTS

21. Client HM - HM was retired and had instructed Hughes to manage his retirement funds conservatively. HM told Hughes this was all the money he had, other than his pension and a small amount of money in another account, and that he was not a risk taker. Furthermore, he told Hughes this money was earmarked to pay his mortgage, and he wanted to preserve those funds.

22. Hughes created an Investment Policy Statement ("IPS") for HM as he did with many of LFA's clients based on their discussions. The IPS essentially laid out an investment strategy for the client which included an asset allocation pie chart for the client's investment program. In the case of HM and other clients, Hughes did not follow the asset allocation chart he created for the client. In fact, Hughes totally disregarded the IPS and HM's instructions. Hughes traded almost exclusively and often in ETFs. Hughes' trading in HM's account resulted in a loss of $66,720.78 over a period of ten months.

23. HM contacted Hughes when he saw the first month's losses. Hughes told HM "don't worry about it" and "remember the 7 year curve." The next month and then for subsequent months HM's account value kept declining. HM kept calling Hughes and Hughes repeated the same statements – "don't worry about it" and "remember the 7 year curve." Finally, after a number of calls from HM, Hughes told the former client not to look at his statements anymore.

24. Client RJ - Another client RJ (husband and wife) had been LFA clients since approximately 2000. At that time they were younger and had a moderate to moderately aggressive risk tolerance. However, in 2008 RJ's husband had a heart attack. RJ then contacted Hughes instructing him to implement a more conservative investment strategy because their LFA account consisted of their retirement funds and they could not afford to incur any losses.

25. Hughes disregarded RJ's instruction trading almost exclusively and frequently in ETFs. As a result, their portfolio suffered losses of $234,317.24.

26. <u>Client HC</u> - HC (husband and wife) received a settlement from a Phoenix investment advisor because of that advisor's inappropriate conduct involving their investment account. When they met Hughes they told him they were not risk takers, were conservative to moderately conservative investors, and were "gun-shy" after what had happened with the Phoenix advisor. Hughes assured them that they would have a conservative portfolio.

27. Like LFA's other clients, Hughes disregarded HC's instructions. Once again Hughes traded in almost exclusively in ETFs. As a result, their portfolio suffered losses of $10,487.97.

28. <u>Client CJ</u> - CJ (husband and wife) began using LFA's services in or about 2000 or 2001. At the time their risk tolerance was aggressive and their account portfolio consisted of two small Roth IRA accounts.

29. In 2009, CJ told Hughes that he had lost his job. At that time, CJ gave LFA $50,000, which represented all of his investment funds asking Hughes for a growth strategy. Later when CJ noticed his account was "losing money" he contacted Hughes. In response, Hughes stated they should "stay the course" explaining that although the market was growing he expected a market crash, which would result in CJ profiting.

30. As with LFA's other clients, Hughes traded almost exclusively in ETFs in CJ's account producing steep losses. As a result, CJ's portfolio suffered losses of $29,280.29. CJ terminated his client relationship with LFA and Hughes because Hughes lost too much money and did not do as he was instructed.

31. For these four clients their portfolios suffered combined losses of $340,806.30.

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HOLDING ETFS BEYOND THE RECOMMENDED HOLDING PERIOD

32. Knowing the risks, Hughes more often than not actively bought and sold the ETFs on the same day for his personal account. If he held onto positions, not much was at stake. On occasion Hughes would hold a large position, but, typically, Hughes would hold only a small quantity of shares and a corresponding low dollar value of the position for those ETFs he traded.

33. Hughes employed a different approach when trading ETFs for LFA clients. Even though the prospectuses cautioned that these types of ETFs were meant to be traded daily, Hughes would generally hold his client positions for days, if not months.

OVERCONCENTRATION OF ETFS IN CLIENT ACCOUNTS

34. Beginning in or about May 2012, Hughes began the process of closing LFA's advisory relationship with LFA clients by revoking the power of attorney given to him by clients to trade and collect fees. In other words, LFA and Hughes would no longer have discretion to trade and manage client accounts.

35. On or about June 29, 2012, Hughes sent an email with an attached letter to approximately eleven clients informing of his decision to "suspend my practice until further notice." On July 6, 2012, Hughes filed on behalf of LFA Form ADV-W to withdraw from licensure in Arizona disclosing the reason for withdrawing as "No longer in business or closing business."

36. In his email and letter to clients, Hughes stated he "purchased three or four investments in each or [sic] your accounts that I think you could own for the foreseeable future. Some produce income and the allocation should benefit from a long-term slowly improving economy and rising interest rates." For at least one client, Hughes merely concentrated the client's assets in two highly volatile ETFs which only served to further increase the investment risk to the client. Hughes' actions were the exact opposite of what he represented to clients.

37. The LFA's clients identified in this Notice were never told that Hughes would be trading in leveraged ETFs that exposed them to outsized risks given their investment objectives, risk tolerances and express investment instructions, that he would primarily trade in these ETFs for

their accounts despite being conservative investors, that he would trade often as he did in their accounts, that he would cause client accounts to hold ETFs for longer periods than recommended, and that he would not follow the disclosures regarding allocation practices as made in his ADV. Additionally, these clients did not understand the trading activity shown on their monthly account statements.

B. LFA'S AND HUGHES' AGGREGATE (BLOCK) TRADING ALLOCATION DISCLOSURES AND PRACTICES

38. In Form ADV Part II Item #9, LFA disclosed that it or a related person "[b]uys or sell for itself securities it also recommended to clients." [6] This disclosure triggered a requirement that LFA, explain "when the applicant or a related person engages in these transactions...what restrictions, internal procedures, or disclosures are used for conflicts of interest in those transactions."

39. Investment advisors disclose their advisory business practices to their clients through regulatory Form ADV filings. The procedures through which an investment adviser ensures it complies with regulatory requirements and its disclosed practices are usually memorialized in a supervisory and/or compliance manual. In its Form ADV Part II filings, LFA made disclosures to its clients and prospective clients about how LFA handled LFA's and its associated individuals' participation or interests in client transactions including aggregated transactions. LFA also maintained Written Supervisory Procedures and a Compliance Manual (collectively referred to herein as the "WSP/Compliance Manual"), which governed how it conducted its affairs to ensure compliance with its Form ADV disclosed practices.

40. In Form ADV, Schedule F, Item 9(E), LFA explained that it had outlined procedures it or its associated persons[7] had to follow if LFA or its associated persons bought or sold securities identical to those recommended to for the client accounts because of the inherent conflict of

[6] A "related person" is defined as "an advisory affiliate and any person under common control with your firm." See glossary of terms for the Form ADV at http://www.sec.gov/about/forms/formadv-instructions.pdf

[7] Associated person is the same as a related person.

interest.[8]

41. LFA's also disclosed that it would aggregate trades[9] for itself with client trades. In aggregating orders LFA set forth certain conditions that need be met. Some of those conditions were as follows:

a. "LFA will prepare, before entering an aggregate order, a written statement ('Allocation Statement') specifying the participating client accounts and how it intends to allocate the order among those clients."

b. "If the aggregated order is filled in its entirety, it will be allocated among clients in accordance with the Allocation Statement; if the order is partially filled, it will be allocated pro-rata based on the Allocation Statement."

c. "[T]he order may be allocated on a basis different from that specified in the Allocation Statement if all client accounts receive fair and equitable treatment and the reason for different allocation is explained in writing and is approved by LFA's compliance officer no later than one hour after the opening of the markets on the trading day following the day the order was executed."

42. From at least 2008 through November 2011, LFA used the services of TD Ameritrade, Inc. ("TDA") to trade on behalf of and custody Hughes and LFA's clients' accounts. After November 2011, LFA used the services of Scottrade, Inc. ("Scottrade"). While with TDA Hughes bought and sold securities for LFA's clients' accounts and his personal account.[10] Almost all trades were made utilizing a single LFA omnibus block account with Hughes being the sole individual allocating the buys and sells to his personal and LFA's clients' account.[11]

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[8] In the WSP/Compliance Manual the same procedures are found under 7.4 Aggregation of Orders.

[9] An aggregated order is the same as block trading.

[10] Hughes personal account was held jointly with his spouse.

[11] A block account is a vehicle that simplifies trading by aggregating trade orders for the same securities involving a number of clients. Once the trade orders are filled, which may take place in one purchase or sale or multiple purchases or sales over a period of the day, the adviser then allocates the trades to the customer accounts according to a pre-trade allocation statement.

43. Hughes had discretionary trading authority over all client accounts, which meant he had total and unrestricted control over the trades and allocations. The decisions Hughes could make included which securities to buy and sell, how many shares to buy and sell, which clients would own which securities, how many shares of a particular security a client would own, and at what price to buy and sell the securities. Since the clients had no visibility into Hughes' daily trading practices and how he allocated trades from the LFA block account, LFA's procedures, as disclosed to clients, required that he prepare pre-trade Allocation Statements.

44. Hughes, using the LFA block account, traded heavily in the aforementioned volatile leveraged ETFs. When asked how he ensured LFA's disclosed trading and allocation practices were implemented and followed so as to prevent inequitable treatment of its clients, Hughes testified before the Division that there "isn't anything to prevent it, do it, or verify it."[12] In fact, contrary to LFA's trading and allocation practice disclosures, neither LFA nor Hughes prepared any allocation statements prior to the start of trading or at any time thereafter.

45. Hughes explained that he allocated shares using two factors, "overall performance and recent performance." Hughes testified that if a client received a winning trade on one day, then the next day a winning trade will not be allocated to this same client because of the prior day's winning allocation. Another client, one who did not receive a winning trade the day before, will then receive the next day's winning trade instead.

46. Hughes also testified that he allocated shares based upon a client's overall situation which, in the example he provided, is inconsistent with his disclosures. For example, he testified that, "rightly or wrongly, I have done this in the past" explaining how he allocated two winning trades, one for $1.00 per share gain and the second for $1.20 per share gain. He allocated the $1.20 per share gain to the smaller account solely based on account size, "because it makes a bigger bang in a smaller account because it's a higher percentage gain than I will [sic] with a larger account."

[12] In early January 2012, Hughes appeared before the Division pursuant to a Division subpoena for an Examination Under Oath ("EUO"). At a second appearance in February 2012, Hughes invoked his Fifth Amendment right and provided no further testimony.

47. At no time did LFA or Hughes prepare allocation statements in connection with aggregated orders or explain in a writing, approved by LFA's compliance officer (Hughes) no later than one hour after the opening of the markets on the trading day following the day the order was executed, the reason for different allocations.

C. OTHER MATERIAL DISCLOSURES

LICENSING STATUS DISCLOSURE

48. LFA's WSP/Compliance Manual requires that individuals associated with LFA providing investment advisory services be licensed as investment adviser representatives before providing advisory services to clients. LFA's Form ADV Part II, Schedule F, Item 1D states that "Individuals associated with LFA will provide its investment advisory services. These individuals are appropriately licensed…."

49. When LFA was first licensed as an investment adviser in Arizona on April 7, 2008, LFA was a sole proprietorship. As a sole proprietorship LFA and Hughes were one and the same thus, Hughes was not required to license as an investment adviser representative under the IM Act.

50. In December 2009, when Hughes changed LFA's organizational form converting LFA to an LLC, LFA became a separate and distinct entity from Hughes. At that time Hughes was not associated with a federal covered adviser nor exempt from licensure, thus, he was required to be licensed as an investment adviser representative in association with LFA. Hughes never licensed as an investment adviser representative in association with LFA.

IV.

VIOLATION OF A.R.S. § 44-3151

(Transactions by Unlicensed Investment Advisers or Investment Adviser Representatives)

51. Hughes transacted business in Arizona as an investment adviser representative while not licensed or in compliance with Article 4 of the IM Act.

52. LFA employed Hughes, an unlicensed person, who acted as an investment adviser representative and who was required to be licensed as an investment adviser representative.

53. This conduct violates A.R.S. § 44-3151.

V.

REMEDIES PURSUANT TO A.R.S. § 44-3201

(Denial, Revocation, or Suspension of Investment Adviser or Investment Adviser Representative License; Restitution, Penalties, or other Affirmative Action)

54. LFA's conduct is grounds to revoke and suspend LFA's license as an investment adviser with the Commission pursuant to A.R.S. § 44-3201. Specifically, revocation and suspension of LFA's license would be in the public interest, as LFA has:

a. engaged in conduct prohibited under A.R.S. § 44-3201(A)(3) by violating A.R.S. § 44-3151(C);

b. engaged in dishonest and unethical conduct within the meaning of A.R.S. § 44-3201(A)(13) as defined by A.A.C. R14-6-203(A)(8) by misrepresenting the nature of the investment advisory services being offered when allocation statements were not prepared at any time before and after block trading occurred as disclosed in its Form ADV filings and its WSP/Compliance Manual;

c. engaged in dishonest and unethical conduct within the meaning of A.R.S. § 44-3201(A)(13) as defined by A.A.C. R14-6-203(A)(8) by misrepresenting that Hughes was properly licensed to provide investment advisory services when he was not licensed; and

d. engaged in dishonest and unethical conduct within the meaning of A.R.S. § 44-3201(A)(13) by failing to prevent Hughes from engaging in fraudulent conduct when Hughes provided investment advisory services to LFA's clients without reasonably determining that the investment advisory services provided were suitable for LFA's clients based on the information from the clients.

55. LFA's conduct is grounds to assess restitution, penalties, and/or take appropriate affirmative action pursuant to A.R.S. § 44-3201. Specifically, LFA has engaged in dishonest and unethical conduct within the meaning of A.R.S. §44-3201(A)(13) when LFA misrepresented the

nature of the investment advisory services being offered when allocation statements were not prepared at any time before and after block trading occurred as disclosed in its Form ADV filings and its WSP/Compliance Manual; that Hughes was properly licensed to provide investment advisory services when he was not licensed; and that Hughes engaged in fraudulent conduct when Hughes provided investment advisory services to LFA's clients without reasonably determining that the investment advisory services provided were suitable for LFA's clients based on the information from the clients.

VI.

VIOLATION OF A.R.S. § 44-3241

(Fraud in the Provision of Investment Advisory Services)

56. Hughes engaged in a transaction or transactions within or from Arizona involving the provision of investment advisory services in which Hughes, directly or indirectly: (i) employed a device, scheme, or artifice to defraud; (ii) made untrue statements of material fact or omitted to state material facts that were necessary in order to make the statements made not misleading in light of the circumstances under which they were made; (iii) misrepresented professional qualifications with the intent that the client rely on the misrepresentation; or (iv) engaged in transactions, practices, or courses of business that operated or would operate as a fraud or deceit. Hughes' conduct includes, but is not limited to, the following:

a. Hughes misled HM when Hughes repeatedly minimized and misled HM as to the effect trading was having on HM's account.

b. Hughes informed clients he had placed them in investments they could own for the foreseeable future but in reality, he substantially increased their investment risk by concentrating their accounts in highly leveraged ETFs meant to be traded daily, not held long term.

c. Hughes principally traded in unsuitable highly volatile leveraged ETFs for LFA's clients.

d. Hughes' conduct, when viewed in its totality, of holding himself out as a licensed investment adviser when he was not licensed, failing to prepare allocation statements before entering aggregated orders or at any time thereafter in accordance with LFA's Form ADV disclosures, and rendering investment advisory services to LFA's clients without reasonably determining that the investment advisory services provided were suitable for the clients based on the information obtained from the clients.

57. This conduct violates A.R.S. § 44-3241.

VII.

REQUESTED RELIEF

The Division requests that the Commission grant the following relief:

1. Order LFA and Hughes to permanently cease and desist from violating the IM Act, pursuant to A.R.S. §§ 44-3201 and 44-3292;

2. Order LFA to pay the state of Arizona administrative penalties of up to one thousand dollars ($1,000) for each violation of the IM Act, pursuant to A.R.S. §§ 44-3201, and 44-3296;

3. Order Hughes to pay the state of Arizona administrative penalties of up to one thousand dollars ($1,000) for each violation of the IM Act, pursuant to A.R.S. § 44-3296;

4. Order the revocation of LFA's license as an investment adviser pursuant to A.R.S. § 44-3201;

5. Order LFA to take affirmative action to correct the conditions resulting from his acts, practices or transactions, including a requirement to make restitution pursuant to A.R.S. §§ 44-3201 and 44-3292;

6. Order Hughes to take affirmative action to correct the conditions resulting from his acts, practices or transactions, including a requirement to make restitution pursuant to A.R.S. § 44-3292;

7. Order that the marital community of Hughes and Respondent Spouse is subject to any order of restitution, rescission, administrative penalties, or other appropriate affirmative action pursuant to A.R.S. § 25-215; and

8. Order any other relief that the Commission deems appropriate.

VIII.

HEARING OPPORTUNITY

Each respondent including Respondent Spouse may request a hearing pursuant to A.R.S. § 44-3212 and A.A.C. R14-4-306. **If a Respondent or Respondent Spouse requests a hearing, the requesting respondent must also answer this Notice.** A request for hearing must be in writing and received by the Commission within 10 business days after service of this Notice of Opportunity for Hearing. The requesting respondent must deliver or mail the request to Docket Control, Arizona Corporation Commission, 1200 W. Washington, Phoenix, Arizona 85007. Filing instructions may be obtained from Docket Control by calling (602) 542-3477 or on the Commission's Internet web site at http://www.azcc.gov/divisions/hearings/docket.asp.

If a request for a hearing is timely made, the Commission shall schedule the hearing to begin 20 to 60 days from the receipt of the request unless otherwise provided by law, stipulated by the parties, or ordered by the Commission. If a request for a hearing is not timely made the Commission may, without a hearing, enter an order granting the relief requested by the Division in this Notice of Opportunity for Hearing.

Persons with a disability may request a reasonable accommodation such as a sign language interpreter, as well as request this document in an alternative format, by contacting Shaylin A. Bernal, ADA Coordinator, voice phone number 602/542-3931, e-mail sabernal@azcc.gov. Requests should be made as early as possible to allow time to arrange the accommodation. Additional information about the administrative action procedure may be found at http://www.azcc.gov/divisions/securities/enforcement/AdministrativeProcedure.asp

IX.

ANSWER REQUIREMENT

Pursuant to A.A.C. R14-4-305, if a Respondent or a Respondent Spouse requests a hearing, the requesting respondent must deliver or mail an Answer to this Notice of Opportunity for Hearing to Docket Control, Arizona Corporation Commission, 1200 W. Washington, Phoenix, Arizona 85007, within 30 calendar days after the date of service of this Notice. Filing instructions may be obtained from Docket Control by calling (602) 542-3477 or on the Commission's Internet web site at http://www.azcc.gov/divisions/hearings/docket.asp.

Additionally, the answering respondent must serve the Answer upon the Division. Pursuant to A.A.C. R14-4-303, service upon the Division may be made by mailing or by hand-delivering a copy of the Answer to the Division at 1300 West Washington, 3rd Floor, Phoenix, Arizona, 85007, addressed to Aikaterine Vervilos.

The Answer shall contain an admission or denial of each allegation in this Notice and the original signature of the answering respondent or respondent's attorney. A statement of a lack of sufficient knowledge or information shall be considered a denial of an allegation. An allegation not denied shall be considered admitted.

When the answering respondent intends in good faith to deny only a part or a qualification of an allegation, the respondent shall specify that part or qualification of the allegation and shall admit the remainder. Respondent waives any affirmative defense not raised in the Answer.

The officer presiding over the hearing may grant relief from the requirement to file an Answer for good cause shown.

Dated this 17 day of October, 2012.

Matthew J. Neubert
Director of Securities