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BEFORE THE DEPARTMENT OF CORPORATIONS
OF THE STATE OF CALIFORNIA

In the Matter of)	FILE NO. 923-3805
)	
THE CALIFORNIA CORPORATIONS)	
COMMISSIONER,)	
)	STATEMENT IN SUPPORT OF ORDER TO
Complainant,)	DISCONTINUE VIOLATIONS PURSUANT
v.)	TO CORPORATIONS CODE SECTION 25249
)	AND COMMISSIONER’S INTENTION TO
VERONA CAPITAL MANAGEMENT, LLC,)	MAKE ORDER FINAL
)	
Respondent.)	(CORPORATIONS CODE SECTION 25251)
)	
)	
)	

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21 Wayne Strumpfer, the Acting California Corporations Commissioner (“Commissioner”) of
22 the Department of Corporations (“Department”) alleges and charges as follows:

23 1. Verona Capital Management, LLC (“VCM”) holds a valid and unrevoked investment
24 adviser certificate issued by the Commissioner pursuant to Corporations Code section 25230 on
25 March 17, 1999. VCM is an investment adviser business located at 1821 Wilshire Boulevard, Suite
26 110, Santa Monica, California 90403. Michael J. Armijo (“Armijo”) is the president of VCM.
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1 2. On January 12, 2004, the Commissioner commenced a regulatory examination of
2 VCM. The examination revealed violations of regulations promulgated pursuant to the Corporate
3 Securities Law of 1968, found at Corporations Code section 25000 et seq.

4 3. VCM failed to prepare and maintain monthly trial balances and computations of net
5 capital and aggregate indebtedness or of minimum net worth (Cal. Code Regs., tit. 10, section
6 260.241.3, subd. (j)), failed to maintain general and auxiliary ledgers (Cal. Code Regs., tit. 10, section
7 260.241.3, subd. (a)(2)), and failed to file annual financial reports with the Commissioner (Cal. Code
8 Regs., tit. 10, section 260.241.2, subd. (a).) The books and records requirements and the annual
9 report filing requirements provide the Department with a regulatory mechanism to validate a firm's
10 liquidity and financial integrity to ensure that licensees maintain the necessary net capital for the
11 protection of the public. VCM's failure to meet its reporting requirements prevented the Department
12 from determining, as part of its regulatory examination, if VCM met the capital requirements
13 imposed by the Corporate Securities Law of 1968 and the regulations enacted thereunder.

14 4. Corporations Code section 25241 requires investment advisers to maintain books and
15 records that are subject to examination and to file such reports as required by the Commissioner.
16 Section 25241 provides, in relevant part, the following:

17 (a) Every broker dealer and every investment adviser licensed under Section 25230 shall
18 make and keep accounts, correspondence, memorandums, papers, books, and other records
and shall file financial and other reports as the commissioner by rule requires

19 5. California Code of Regulations, title 10, section 260.241.2, subdivision (a) requires
20 the filing of an annual report by certain investment advisers. Subdivision (a)(2) of section 260.241.2
21 provides as follows:

22 (a) General Rule. Subject to the provisions of Subsection (c) of this section, . . . every
23 licensed investment adviser subject to the provisions of Section 260.237.1 or Section
24 260.237.2, as applicable, of these rules, shall file an annual financial report containing the
information required by a form or forms to be supplied or approved by the Commissioner, as
25 follows:

26 . . .

27 (2) The annual report for investment advisers shall contain a Statement of Financial
28 Condition. Supporting schedules shall contain computations of net capitals, aggregate
indebtedness and ratios required under Section 260.237.1 or minimum financial requirements

1 required under Section 260.237.2, as applicable, and the certificate of the accountant required
2 under subsection (c) of Section 260.237 of these rules.

3 6. California Code of Regulations, title 10, section 260.241.3 requires that investment
4 advisers maintain specific books and records. Section 260.241.3, in relevant parts, provides as
5 follows:

6 (a) Every licensed investment adviser shall make and kept true, accurate and current the
7 following books and records, relating to such person's investment advisory business:

8 (2) General and auxiliary ledgers (or other comparable records) reflecting asset, liability,
reserve, capital, income and expense accounts.

9 (j) Any investment adviser who is subject to the minimum financial requirements of Section
10 260.237.1 or Section 260.237.2, as applicable, shall, in addition to the records otherwise
11 required under this section, maintain a record of the proof of money balances of all ledger
12 accounts in the form of trial balances and a record of the computations of net capitals and
13 aggregate indebtedness pursuant to Section 260.237.1 of these rules or minimum net worth
pursuant to Section 230.237.2 of these rules (as of the trial balance date). The trial balances
and computations shall be prepared currently at least once a month.

14 7. California Code of Regulations, title 10, section 260.237.1, subdivision (a)(2),
15 provides, in relevant part, as follows:

16 An investment adviser licensed prior to 03/01/03 may comply with either the minimum
17 financial requirements in this section or in Section 260.237.2 until January 1, 2005, at which
18 time this section shall become inoperative and an investment adviser shall comply with the
minimum financial requirements in Section 260.237.2.

19 (a) No investment adviser who has any power of attorney from any investment advisory
20 client to execute transactions . . . shall permit its total aggregate indebtedness to exceed 500%
of its tangible net capital or permit its current aggregate indebtedness to exceed its current net
capital; and,

21 (2) If the investment adviser has any power of attorney from any investment advisory client
22 to execute transactions and does not have regular or periodic custody or possession of any of
23 its investment advisory clients' securities or funds, except the receipt of prepaid subscriptions
for periodic publications, or other investment advisory services, it shall at all times have and
24 maintain tangible net capital of not less than \$5,000

25 Subdivision (c) of section 260.237.1 provides that for purposes of section 260.237.1,
26 subdivision (a), all financial information shall be determined in accordance with generally accepted
27 accounting principles.
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1 8. California Code of Regulations, title 10, section 260.237.2, in relevant part, provides
2 as follows:

3 An investment adviser licensed prior to 03/01/03 may comply with either the minimum
4 financial requirement in this section or in Section 260.237.1 until January 1, 2005, at which
5 time Section 260.237.1 shall become inoperative and an investment adviser shall comply with
6 the minimum financial requirement in this section.

7 (a) Every investment adviser who has custody of client funds or securities shall maintain at
8 all times a minimum net worth of \$35,000, and every investment adviser who has
9 discretionary authority over client funds or securities but does not have custody of client
10 funds or securities shall maintain at all times a minimum net worth of \$10,000.

11 9. The Department's examiner found during the regulatory examination on January 12,
12 2004, that VCM had discretionary authority and power of attorney over advisory client accounts to
13 execute transactions and, therefore, VCM was required to meet either the net capital provided for
14 under section 260.237.1, subdivision (a)(2), or the minimum net capital requirements provided for
15 under section 260.237.2, subdivision (a), and to show proof of compliance with this regulation by
16 filing annual financial reports, in accordance with California Code of Regulations, title 10, section
17 260.241.2, subdivision (a). VCM was also required to prepare and maintain monthly proof of ledger
18 account money balances and either monthly computations of net capitals and aggregate indebtedness,
19 or monthly computations of minimum net worth, in accordance with California Code of Regulations,
20 title 10, section 260.241.3, subdivisions (a)(2) and (j). At the time of the January 12, 2004
21 examination, VCM had not prepared and maintained monthly proof of ledger account money
22 balances and either monthly computations of net capitals and aggregate indebtedness, or of minimum
23 net worth, in violation of California Code of Regulations, title 10, section 260.241.3, subdivisions
24 (a)(2) and (j). As a result of VCM's violation of California Code of Regulations, title 10, section
25 260.241.3, subdivisions (a)(2) and (j), the Department's examiner was unable to determine if the
26 firm, at the time of the examination, was in compliance with either the net capital requirements of
27 section 260.237.1, or the minimum net worth requirement of section 260.237.2.

28 10. The Department's examiner also found that VCM had failed to submit its annual
financial reports for the years 2001 and 2002 in violation of California Code of Regulations, title 10,
section 260.241.2, subdivision (a).

1 11. On March 29, 2004, the Department sent Armijo a regulatory letter explaining the
2 violations discovered during the January 12, 2004 examination, including violations of California
3 Code of Regulations, title 10, sections 260.241.3, subdivisions (a)(2) and (j), and 260.241.2,
4 subdivision (a)(2). Armijo responded by letter dated April 7, 2004. In his letter, Armijo stated
5 “VCM computations of aggregate indebtedness and net capital are now prepared and maintained on a
6 monthly basis.” In addition, VCM “now reflect the unearned portion of the advisory fees and have
7 recognized and recorded them as a liability on our financials.” Armijo, however, did not provide any
8 explanation why VCM had not corrected the deficiencies prior to the 2004 regulatory examination.
9 Armijo enclosed the annual financial reports for years 2001 and 2002. Armijo vowed to file timely
10 reports in the future.

11 12. A prior regulatory examination of VCM conducted by the Department in March 2001
12 revealed, in part, identical regulatory violations. On May 8, 2001, the Department sent a letter
13 notifying VCM, among other things, of VCM’s failure to record the unearned fees as a liability,
14 compute net capital and aggregate indebtedness on a monthly basis and file annual reports in
15 violation of California Code of Regulations, title 10, sections 260.241.3, subdivisions (a)(2) and (j),
16 and 260.241.2, subdivision (a). In correspondence with the Department dated May 15, 2001, Armijo
17 stated VCM “now maintains our general ledger on a monthly basis. Our computations of net capital
18 are prepared on a monthly basis along with reconciling the bank accounts. Unearned income is
19 established as part of our accounting records.”

20 13. Corporations Code section 25249, which became effective January 1, 1999, authorizes
21 the Commissioner to issue an order directing any investment adviser to discontinue any violation of
22 any provision of the Corporate Securities Law of 1968 and any rule promulgated thereunder.

23 Specifically, Corporations Code section 25249 provides, in relevant part,

24 If, after examination or investigation, the commissioner has reasonable grounds to believe that
25 any broker-dealer or investment adviser has violated any law or rule binding upon it, the
26 commissioner shall, by written order addressed to the broker-dealer or investment adviser,
27 direct the discontinuance of the violation. The order shall be effective immediately, but shall
28 not become final except in accordance with the provision of Section 25251.

1 14. Corporations Code section 25251 provides:

2 (a) No order issued pursuant to Section 25249 or 25250 may become final except after notice

3 to the affected broker-dealer or investment adviser of the commissioner’s intention to make

4 the order final and of the reasons for the finding. The commissioner shall also notify the

5 broker-dealer or investment adviser that upon receiving a request the matter shall be set for

6 hearing to commence within 15 business days after receipt of the request. The broker-dealer

7 or investment adviser may consent to have the hearing commence at a later date. If no

8 hearing is requested within 30 days after the mailing or service of the required notice, and

9 none is ordered by the commissioner, the order may become final without a hearing and the

10 broker-dealer or investment adviser shall immediately discontinue the practices named in the

11 order. If a hearing is requested or ordered, it shall be held in accordance with the provisions

12 of the Administrative Procedure Act (Chapter 5 (commencing with Section 11500) of Part 1

13 of division 3 of title 2 of the Government Code) and the commissioner shall have all of the

14 powers granted under that act. If, upon the conclusion of the hearing, it appears to the

15 commissioner that the broker-dealer or investment adviser is conducting business in an unsafe

16 or injurious manner or is violating any law of this state, or any rule binding upon it, the

17 commissioner shall make the order of discontinuance final and the broker-dealer or

18 investment adviser shall immediately discontinue the practices named in the order.

19 (b) The broker dealer or investment adviser may within 10 days after an order is made final

20 commence an action to restrain enforcement of the order. If the enforcement of the order is

21 not enjoined within 10 days by the court in which the action is brought, the broker-dealer or

22 investment adviser shall comply with the order.

23 15. By reason of the foregoing, VCM has willfully violated California Code of

24 Regulations, title 10, sections 260.241.2, subdivision (a), and 260.241.3, subdivisions (a)(2) and (j),

25 justifying the issuance of an Order to Discontinue Violations. VCM, as a licensee, was obligated to

26 have knowledge of, and to comply with, the provisions of the Corporate Securities Law of 1968 and

27 the regulations thereunder to maintain its investment adviser certificate. Furthermore, on May 15,

28 2001, the Department notified VCM of the requirements of California Code of Regulations, title 10,

 sections 260.241.2, subdivision (a), and 260.241.3, subdivisions (a)(2) and (j). VCM violated these

 sections again, despite the Department’s actual notification.

 16. Therefore, pursuant to Corporations Code section 25249, the Commissioner has issued

 an order directing VCM to discontinue violating California Code of regulations title 10, sections

 260.241.2, subdivision (a), and 260.241.3, subdivisions (a)(2) and (j).

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1 WHEREFORE, good cause showing, and pursuant to Corporations Code section 25251, the
2 California Corporations Commissioner hereby notifies VCM of his intention to make final the Order
3 to Discontinue Violations Pursuant to Corporations Code Section 25249 issued on May 13, 2005.
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5 Dated: May 13, 2005
6 Los Angeles, California

WAYNE STRUMPFER
Acting California Corporations Commissioner

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8 By: _____
9 MARLOU de LUNA
10 Corporations Counsel
11 Enforcement Division
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