ADVANCE SHEET HEADNOTE
June 27, 2022

**2022 CO 36**

**No. 20SC595, *Chan v. HEI Resources, Inc.*— Securities—Colorado Securities Act—Investment Contracts—General Partnerships.**

This case requires the supreme court to determine how courts should evaluate whether an interest in a "general partnership" is an "investment contract" for purposes of the Colorado Securities Act, §§ 11-51-101 to -1008, C.R.S. (2021) (the "CSA"). General partnerships ordinarily are not investment contracts because general partners control and direct the venture, but in certain circumstances, a venture denominated a general partnership may be an investment contract in operation.

The court now adopts the generally accepted framework from *Williamson v. Tucker*, 645 F.2d 404 (5th Cir. 1981), for how to assess whether a general partnership is in fact an investment contract. Reversing the division below, the court concludes that the CSA does not allow for a "strong presumption" that general partnership interests are not securities—or for any presumption or burden

beyond that necessarily created by the plaintiff's burden of proof. The supreme court further concludes that (1) a court evaluating whether general partners lack the ability to direct the venture may find that their general business knowledge and expertise is sufficient to permit them to exercise their partnership powers, (2) if general partners themselves would not be able to serve in the place of the manager, that does not necessarily make the partnership an investment contract, and (3) a particular venture's "economic realities" can appropriately be considered as part of the *Williamson* framework. Accordingly, the supreme court reverses the court of appeals' judgment on the question of whether courts should apply a "strong presumption" and remands the case to the trial court for further findings.

**The Supreme Court of the State of Colorado**
2 East 14th Avenue • Denver, Colorado 80203

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**2022 CO 36**

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**Supreme Court Case No. 20SC595**
*Certiorari to the Colorado Court of Appeals*
Court of Appeals Case No. 18CA1769

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**Petitioner:**

Tung Chan, Securities Commissioner for the State of Colorado,

v.

**Respondents:**

HEI Resources, Inc. f/k/a Heartland Energy, Inc.; Charles Reed Cagle; Brandon Davis; Heartland Energy Development Corporation; John Schiffner; and James Pollak.

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**Judgment Affirmed in Part and Reversed in Part**
*en banc*
June 27, 2022

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**JUSTICE HART** delivered the Opinion of the Court, in which **CHIEF JUSTICE BOATRIGHT**, **JUSTICE MÁRQUEZ**, **JUSTICE HOOD**, **JUSTICE GABRIEL**, **JUSTICE SAMOUR**, and **JUSTICE BERKENKOTTER** joined.

JUSTICE HART delivered the Opinion of the Court.

¶1 This case requires us to determine how courts should evaluate whether an interest in a "general partnership" is an "investment contract" under Colorado's securities laws and thus a "security" subject to the laws and regulations of the Colorado Securities Act, §§ 11-51-101 to -1008, C.R.S. (2021) (the "CSA"). An investment contract is undefined in the statute, but Colorado has long followed federal law in applying the test set forth in *Securities & Exchange Commission v. W.J. Howey Co.*, 328 U.S. 293, 298–99 (1946), which provides that an investment contract must be (1) a contract, transaction, or scheme whereby a person invests money (2) in a common enterprise (3) in which the person is led to expect profits derived from the entrepreneurial or managerial efforts of others. General partnerships ordinarily do not satisfy the third element of *Howey* because general partners control and direct the venture. But in some instances, an investor or—as here—a security regulator claims that a contract or scheme that purports to be a general partnership in form is *actually* an investment contract in operation. In those instances, the majority of state and federal courts have turned to the opinion of the United States Court of Appeals for the Fifth Circuit in *Williamson v. Tucker*, 645 F.2d 404 (5th Cir. 1981), for guidance on how to assess whether the form of the venture is somehow belied by the economic realities of its operation.

¶2 We conclude here that the *Williamson* framework applies in Colorado. That, however, does not fully answer the questions we are presented with in this dispute, as *Williamson* has been interpreted in various ways. As relevant here, some courts, including the division below, have suggested that ventures denominated as general partnerships are entitled to a "strong presumption" that they are *not* investment contracts. *See Chan v. HEI Res., Inc.*, 2020 COA 87, ¶¶ 32–33, 490 P.3d 789, 799–800 ("*HEI II*"). We reject the notion that general partnerships are entitled to any presumption that might imply that a plaintiff bears a burden of proof greater than the preponderance of the evidence burden generally applicable in civil litigation. That said, we acknowledge, as *Williamson* did, that a plaintiff will have a "difficult factual burden" to carry when seeking to establish by a preponderance of the evidence that a venture holding the legal status of a general partnership is not in operation a general partnership. 645 F.2d at 416.

¶3 Beyond the question of how to describe the weight of the burden borne by plaintiffs in disputes like this one, the parties here further disagree over exactly how to apply the *Williamson* framework. In remanding this case for proceedings consistent with this opinion, we focus on three aspects of that application. First, a court evaluating whether general partners lack the ability to direct the venture may find that their general business knowledge and expertise is in fact sufficient

to permit them to exercise their partnership powers. While industry-specific experience may be relevant, if the general partners lack such experience, that fact alone does not make the partnership an investment contract. Second, if general partners themselves would not be able to serve in the place of the manager, that does not necessarily make the partnership an investment contract; rather, a plaintiff must prove that the general partners cannot realistically replace the manager *at all*. Third, we conclude that a particular venture's "economic realities" can appropriately be considered as part of the *Williamson* framework.

¶4 As we describe in detail below, whether respondents have sold securities has been in dispute for over a decade. Today, we do not resolve that factual dispute. The question before us is not whether *these particular interests* are securities. Rather, the question is a broader one: How should a court assess a plaintiff's claim that a particular "general partnership"—which, as everyone appears to agree, in its bona fide form would not be a security—is in fact operating as an investment contract and thus is a security under the CSA?

## I. Relevant Facts and Procedural History

¶5 Between approximately 2004 and 2008, respondents HEI Resources, Inc. ("HEI"), and the Heartland Development Corporation ("HEDC"), both corporations whose principal place of business is Colorado, formed, capitalized, and operated eight separate joint ventures related to the exploration and drilling

of oil and gas wells.[1] They solicited investors for what they called Los Ojuelos Joint Ventures by cold calling thousands of individuals from all over the country. To those individuals who expressed interest in the ventures, respondents mailed promotional material and a confidential information memorandum, which described features of the ventures and disclosed certain risks. Those who joined the ventures became parties to an agreement organized as a general partnership under the Texas Revised Partnership Act.[2] Each of the eight ventures ultimately included between forty-six and ninety investors. These investors each signed a joint venture agreement that explained that the investors are "general partners" with a variety of rights and responsibilities but delegated the day-to-day management duties for the ventures to HEDC. HEI and HEDC did not register the ventures as securities, nor did they file a notice of exemption from registration. *See* § 11-51-301, C.R.S. (2021).

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[1] Charles Reed Cagle, HEI's president; Brandon Davis, HEDC's president; and John Schiffner and James Pollak, affiliates of and sales representatives for HEI and HEDC, are also respondents in this dispute.

[2] The Texas Revised Partnership Act was adopted in 1994 but has since been replaced with the Texas Business Organization Code. *See* Tex. Bus. Orgs. Code §§ 152, 154; *Energy Transfer Partners, L.P. v. Enter. Products Partners, L.P.*, 593 S.W.3d 732, 737 n.9 (Tex. 2020). The Texas Supreme Court has observed that the new rules and the old rules for determining partnership formation are "substantially the same." *Ingram v. Deere*, 288 S.W.3d 886, 894 n.4 (Tex. 2009).

¶6 In 2009, the Securities Commissioner for the State of Colorado ("the Commissioner") initiated this enforcement action. The Commissioner's complaint alleged that respondents had violated the CSA by, among other things, offering and selling unregistered securities to investors nationwide through the use of unlicensed sales representatives and in the guise of general partnerships. The Commissioner alleged that HEDC and HEI used the general partnership form deliberately in order to avoid regulation. Each of the Commissioner's claims required that the Commissioner prove that the general partnerships were securities, so the trial was bifurcated to permit resolution of that threshold question.

¶7 In 2010, the Commissioner moved for partial summary judgment, arguing that an application of the framework set out in *Williamson*, as well as consideration of other economic realities of the general partnerships, demonstrates that the ventures were in fact investment contracts. Respondents filed cross-motions, asking the trial court to conclude precisely the opposite—that, under the *Williamson* framework, the ventures were in fact operating as general partnerships and therefore were not investment contracts.

¶8 The trial court granted partial summary judgment in respondents' favor. First, the trial court agreed with respondents that under *Williamson* the general partnerships are presumed not to be securities. In reaching this conclusion, the

court referred to *Williamson* as creating a "strong presumption" that interests in general partnerships are not securities.

¶9 Second, the trial court ruled that the Commissioner's claims with respect to two of the *Williamson* tests[3] failed as a matter of law. The court described the first test as requiring that, in the partnership agreements, the relationship among the parties is tantamount to a limited partnership rather than a general partnership—that is, the agreements themselves "restrict the non-managing venturers' rights as to make the titular general partnership really a limited partnership." And it found that the agreements at issue here do not include such restrictions.

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[3] The Fifth Circuit described these scenarios as the "limited circumstances" in which a general partnership would be a security because it would not accord the general partners "meaningful powers," *Williamson*, 645 F.2d at 425—circumstances it also called "factors," *id.* at 424, 425, 427. Courts applying *Williamson* have since used a variety of terms to refer to these circumstances. *E.g.*, *Secs. & Exch. Comm'n. v. Merch. Cap., LLC*, 483 F.3d 747, 755 (11th Cir. 2007) ("three situations" that are each "factors"); *Rome v. HEI Res., Inc.*, 2014 COA 160, ¶ 12, 411 P.3d 851, 851 ("factors" that form a "three-factor test"); *Rivanna Trawlers Unltd. v. Thompson Trawlers, Inc.*, 840 F.2d 236, 240 (4th Cir. 1988) ("narrow exception[s]"). We refer to the three scenarios as separate "tests" because they represent independent means for assessing whether the partnership is an investment contract. *See HEI II*, ¶ 3 n.2, 490 P.3d at 793 n.2 (explaining the use of "tests").

¶10 The court described the third *Williamson* test as requiring that the non-managing partners are so dependent on some unique ability of the manager that they cannot realistically replace the manager. This, too, the trial court concluded the Commissioner had failed to show.

¶11 Remaining in contention were the second test, which requires that the partners be incapable of intelligently exercising their partnership powers because of a lack of experience and knowledge, and whatever other economic realities of the ventures might be relevant.

¶12 The case proceeded to a bench trial in July 2013 to determine whether the ventures were securities. The trial court determined that the second *Williamson* test requires asking "whether the partners are so inexperienced or unknowledgeable in business affairs *generally*, not whether they are experienced and sophisticated in the particular industry or area in which the partnership engages and they have invested," that they were "incapable of intelligently exercising their partnership powers." The court looked to the investors as a whole and found that they were not so inexperienced or unknowledgeable in business affairs that they were unable to exercise their partnership powers intelligently. The trial court then looked to various "catch-all economic realities" as alternative bases for assessing whether the interests could qualify as investment contracts, but there, too, the court found that the Commissioner failed to prove by a

preponderance of the evidence that the interests were securities. Accordingly, the court concluded that the interests were not investment contracts and entered judgment vacating the setting of the remainder of the bifurcated trial.

¶13 The Commissioner appealed, arguing that the trial court erred (1) when it applied a "strong presumption" that general partnership interests are not securities, and (2) when it failed to narrow the focus from investors' *general* relevant business experience and knowledge to *industry-specific* experience and knowledge. A division of the court of appeals reversed. *Rome v. HEI Res., Inc.*, 2014 COA 160, ¶ 61, 411 P.3d 851, 863 ("*HEI I*"). The division rejected the strong presumption, *id.* at ¶ 41, 411 P.3d at 860, concluded that the second *Williamson* test looks to investors' collective experience in "the specific business of the venture," *id.* at ¶ 58, 411 P.3d at 863, and then remanded for reconsideration of "the second and third *Williamson* [tests] and any other 'catch-all' economic realities," *id.* at ¶ 61, 411 P.3d at 863.

¶14 On remand in 2016, looking to the same record from the 2013 trial, the trial court ruled that the ventures were securities. Specifically, the trial court found that the Commissioner (1) met the second *Williamson* test by showing that the partners collectively lacked experience with drilling and oil and gas exploration and thus were incapable of intelligently exercising their partnership powers; (2) met the third *Williamson* test by showing that no general partner could have

capably replaced the managing partner, and thus the general partners were dependent on HEI and HEDC's unique managerial skills; and (3) showed that the ventures' other economic realities—demonstrated by a range of facts—supported a conclusion that the interests were securities. The case proceeded to a bench trial, and the trial court found that respondents had violated provisions of the CSA.

¶15 This time around, respondents appealed. A division of the court of appeals ruled on only the threshold issue—whether the interests were securities—and issued a limited remand. *HEI II*, ¶ 61, 490 P.3d at 804. Disagreeing with *HEI I*, this division reversed the trial court and remanded with instructions to "make factual findings as to whether the interests are investment contracts under the second and third *Williamson* tests, applying the presumption, and based on the existing record alone." *Id.* at ¶ 42, 490 P.3d at 800–01. Regarding the second *Williamson* test, the division concluded that "although venture-specific experience is unquestionably relevant, it isn't necessarily required" because the material question is whether, "considering the nature of the business, the partners collectively possess sufficient knowledge and experience to intelligently exercise their powers." *Id.* at ¶ 47, 490 P.3d at 801. As to the third *Williamson* test, the division concluded that the trial court's focus on whether the investors themselves possessed the skills necessary to replace the managing partner was "too narrow." *Id.* at ¶ 51, 490 P.3d at 803. And examining the "other economic realities," the division concluded that,

consistent with *Williamson* itself, "there may be considerations in addition to the three *Williamson* tests that bear on whether an ostensible general partnership interest is an investment contract," but the same facts that would lead to the conclusion that the interests fail the *Williamson* tests "shouldn't be repackaged under a 'catch-all economic realities' test . . . absent some articulable reason akin to the *Williamson* tests. . . ." *Id.* at ¶ 56, 490 P.3d at 803. The Commissioner petitioned for certiorari, which we granted.[4]

## II. Analysis

¶16 We begin by stating the applicable standard of review and the principles governing statutory construction. We then explain the meaning of "investment contract" under Colorado and federal law before we turn to *Williamson*—which essentially sets out an approach to determining whether a joint venture or general partnership satisfies the third prong of the investment contract test established by the Supreme Court in *Howey*. We conclude that *Williamson* does not require

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[4] We granted certiorari to review the following issues:

1. [REFRAMED] Whether the court of appeals erred by holding that Colorado should apply a "strong presumption" that a general partnership is not a security.
2. Whether the court of appeals erred in its interpretation of the *Williamson* tests.

starting with a "strong presumption" that a general partnership is not a security. Neither is such a presumption an appropriate gloss on *Williamson*'s insights because it suggests that general partnerships are protected from the reach of the securities laws by imposition of a heightened burden of proof that is not included in state or federal securities laws. Instead, what *Williamson* recognized, and we accept here, is simply that a venture operating as a bona fide general partnership will likely not satisfy the third prong of the *Howey* investment contract test because general partners are not passive investors. The *Williamson* opinion elaborated three distinct factual scenarios that could demonstrate that a general partnership in name might nonetheless satisfy the *Howey* test. We conclude here that *Williamson*'s elaboration of these scenarios is a helpful approach, and we consider four aspects of the approach that the parties contest and that received different treatment in the two different division opinions below.

### A. Standard of Review and General Principles

¶17 We review questions of statutory interpretation de novo. *Thompson v. People*, 2020 CO 72, ¶ 22, 471 P.3d 1045, 1051. In interpreting a statute, we aim to identify and then give effect to the General Assembly's intent. *Id.*

¶18 As directed by the legislature, we construe provisions of the CSA broadly to effectuate its purposes "to protect investors and maintain public confidence in securities markets while avoiding unreasonable burdens on participants in capital

markets." § 11-51-101(2), C.R.S. (2021). The CSA is "remedial in nature." *Id.* Further, its provisions are to be coordinated with referenced federal law "to the extent coordination is consistent with both the purposes and of the provisions of" the CSA. § 11-51-101(3). Indeed, we have consistently recognized that "insofar as the provisions and purposes of our statute parallel those of the federal enactments, such federal authorities are highly persuasive." *Cagle v. Mathers Fam. Tr.*, 2013 CO 7, ¶ 19, 295 P.3d 460, 465 (quoting *Lowery v. Ford Hill Inv. Co.*, 556 P.2d 1201, 1204 (Colo. 1976)).[5]

### B. The Meaning of "Investment Contract" in the CSA

¶19 This dispute hinges on whether the ventures established by HEI and HEDC are "investment contracts" and therefore securities under the CSA. *See* § 11-51-201(17), C.R.S. (2021) (including "investment contract" in definition of "security"). "Investment contract" is not defined in the CSA, but we have adopted as our own the three-part test set forth by the Supreme Court in *Howey*, when it interpreted the same term's meaning under the federal securities acts. *See*

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[5]We reject the Commissioner's argument that this alignment with federal law where appropriate does not encompass federal case law. As we said recently in *Thompson*, "although we are not bound by federal law in construing the CSA, we deem federal authorities persuasive, given that the provisions and purposes of the CSA parallel those of federal enactments." ¶ 26, 471 P.3d at 1052. We have not previously limited our understanding of what "federal authorities" includes to legislative enactments and we decline to do so here.

*Thompson*, ¶ 26, 471 P.3d at 1052 (noting that we adopted the *Howey* test in 1976); *Lowrey*, 556 P.2d at 1204–05. Under the *Howey* test "an 'investment contract' is: (1) a contract, transaction, or scheme whereby a person invests his or her money (2) in a common enterprise and (3) is led to expect profits [substantially] derived from the entrepreneurial or managerial efforts of others." *Toothman v. Freeborn & Peters*, 80 P.3d 804, 811 (Colo. App. 2002); *see Howey*, 328 U.S. at 298–99; *Lawrence v. People*, 2021 CO 28, ¶ 31, 486 P.3d 269, 276. The advantage of this test is that it "is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits." *Howey*, 328 U.S. at 299. The approach thus serves the purposes of the CSA as a remedial statute designed to be broad in scope. *See Thompson*, ¶ 24, 471 P.3d at 1051–52.

### C. The *Williamson* Tests

¶20 The question that confronts us here, and that confronted the Fifth Circuit in *Williamson*, is whether a venture that is denominated as a general partnership can meet the third prong of the *Howey* test—that the investors expect to make a profit substantially derived from the efforts of others. In analyzing this question, the Fifth Circuit first concluded that passive investments and general partnerships are generally distinct, given the nature of general partnerships. *See Williamson*, 645 F.2d at 422. It then set out three non-exhaustive tests that might prove that a general partnership interest is an "investment contract" within the federal acts'

definitions of "securities." *Id.* at 417, 419–23. Although several decisions of the court of appeals have cited *Williamson* approvingly, *see Toothman*, 80 P.3d at 811; *Feigin v. Digital Interactive Assocs., Inc.*, 987 P.2d 876, 882 (Colo. App. 1999); *see also Joseph v. Mieka Corp.*, 2012 COA 84, ¶¶ 18–22, 282 P.3d 509, 514–15, we have not previously considered whether it should apply when evaluating general partnerships under the CSA. This is the question we turn to now.

¶21 *Williamson* identified three features of general partnerships. First, general partners maintain control of the business venture. *Williamson*, 645 F.2d at 421–22. This is true even if they delegate day-to-day management responsibilities, *id.* at 421, though the joint and several liability for debts and obligations that attends general partnership typically incentivizes active engagement or wise delegation of management duties, *see Secs. & Exch. Comm'n v. Merch. Cap., LLC*, 483 F.3d 747, 755–56 (11th Cir. 2007). Second, general partners have rights to access information. *Williamson*, 645 F.2d at 421–22, 424. Third, relatedly, because the "partnership powers are not in the nature of a nominal role in the enterprise," "[a]n investor who is offered an interest in a general partnership or joint venture should be on notice . . . that his ownership rights are significant, and that the federal securities acts will not protect him from a mere failure to exercise his rights." *Id.* at 422.

¶22 In sum, general partners have the "sort of influence which generally provides them with . . . protection against a dependence on others." *Id.* In contrast, dependence on others "is implicit in an investment contract." *Id.* at 423.

¶23 But *Williamson* made clear that "the mere fact that an investment takes the form of a general partnership or joint venture does not inevitably insulate it from the reach of the federal securities laws." *Id.* at 422. This is because "in searching for the meaning and scope of the word 'security' in the Act[s], form should be disregarded for substance and the emphasis should be on economic reality." *United Hous. Found., Inc. v. Forman*, 421 U.S. 837, 848 (1975) (quoting *Tcherepnin v. Knight*, 389 U.S. 332, 336 (1967) (second alteration in the original)); *see also Lowery*, 556 P.2d at 1205 ("The hallmark of state and federal securities regulation has always been close attention to the facts of each case and a substantive appraisal of the commercial realities of the offering."). Thus, under the third prong of the *Howey* test, *Williamson* explained, "a partnership *can* be an investment contract [but] only when the partners are so dependent on a particular manager that they cannot replace him or otherwise exercise ultimate control." 645 F.2d at 424 (emphasis added). With this in mind, the Fifth Circuit described three circumstances, any one of which might demonstrate that a particular general partnership interest satisfies the *Howey* test:

> A general partnership or joint venture interest can be designated a security if the investor can establish, for example, that (1) an

> agreement among the parties leaves so little power in the hands of the partner or venturer that the arrangement in fact distributes power as would a limited partnership; or (2) the partner or venturer is so inexperienced and unknowledgeable in business affairs that he is incapable of intelligently exercising his partnership or venture powers; or (3) the partner or venturer is so dependent on some unique entrepreneurial or managerial ability of the promoter or manager that he cannot replace the manager of the enterprise or otherwise exercise meaningful partnership or venture powers.

*Id.*

¶24 *Williamson* identified the unusual circumstances in which a venture legally titled a general partnership might nonetheless be an investment contract in light of the actual economic realities at play. Because this approach allows for individualized scrutiny of the economic realities of a given instrument or scheme, and because it provides a clear means of applying the third prong of *Howey*, we conclude that the *Williamson* approach does apply to the CSA. That conclusion does not, however, fully answer the questions we face here. *Williamson* has been interpreted in varying ways in state and federal courts around the country. We explain below how it should be applied to the CSA.

### 1. There is No "Strong Presumption" under the CSA that a General Partnership is not an Investment Contract

¶25 The division below interpreted *Williamson* as establishing a "strong presumption" that an entity designated as a general partnership is not an investment contract. We disagree.

¶26 We do recognize, as did the *Williamson* court, that a bona fide general partnership will ordinarily not involve passive investment and therefore will not satisfy the third prong of the *Howey* test. Indeed, the Commissioner herself acknowledged that in a "legitimate" general partnership, "the general partners have the power to affect the outcome of the business."[6] As *Williamson* explained, because "meaningful powers possessed by joint venturers under a joint venture agreement do indeed preclude a finding that joint venture interests are securities," plaintiffs "have an extremely difficult factual burden" if they are to prove that investors in a titular general partnership actually expected profits from the managerial efforts of others. 645 F.3d at 425.

¶27 In the years since *Williamson* was decided, the difference between the plaintiff's "difficult factual burden" to meet its burden of proof and a "presumption" about the status of general partnerships has led to divergent articulations of *Williamson*'s meaning in courts around the country. On one hand, many courts do, as the division below did, refer to a "presumption" or "strong

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[6] Similarly, *amicus curiae* North American Securities Administrators Association, Inc., writing in support of the Commissioner, explained, "In an appropriately formed and structured general partnership, the partners do not have such an expectation [of profits to come from the efforts of others] because they control the enterprise."

presumption" against classifying general partnerships as securities. *See, e.g.*, *Secs. & Exch. Comm'n v. Shields*, 744 F.3d 633, 643 (10th Cir. 2014); *Rivanna Trawlers Unltd. v. Thompson Trawlers, Inc.*, 840 F.2d 236, 241 (4th Cir. 1988); *Youmans v. Simon*, 791 F.2d 341, 346 (5th Cir. 1986); *Merch. Cap.*, 483 F.3d at 755. But others have done what the *HEI I* division did, and applied *Williamson* without invoking any "presumption." *See, e.g.*, *Secs. & Exch. Comm'n v. Schooler*, 905 F.3d 1107, 1112 (9th Cir. 2018); *Odom v. Slavik*, 703 F.2d 212, 215 (6th Cir. 1983); *Secs. & Exch. Comm'n v. Telecom Mktg., Inc.*, 888 F. Supp. 1160, 1165 (N.D. Ga. 1995); *McConnell v. Frank Howard Allen & Co.*, 574 F. Supp. 781, 786 (N.D. Cal. 1983); *Corp. E. Assocs. v. Meester*, 442 N.W.2d 105, 107 (Iowa 1989); *Casali v. Schultz*, 732 S.W.2d 836, 837 (Ark. 1987); *Secs. & Exch. Comm'n v. Shreveport Wireless Cable Television P'ship*, No. Civ.A. 94-1781, 1998 WL 892948, at *5–7 (D.D.C. Oct. 20, 1998); *see also Digital Interactive*, 987 P.2d at 882–83 (applying *Williamson* to determine probable cause in context of a challenge to a search warrant); *Mieka*, ¶ 22, 282 P.3d at 515 (declining to address whether a presumption is appropriate); *Pfohl v. Pelican Landing*, 567 F. Supp. 134, 137 (N.D. Ill. 1983) (describing *Williamson* without mentioning the presumption).

¶28 We conclude here that the second approach is more consistent with the CSA. First, the burden of proof in a civil action such as the civil enforcement of securities laws "shall be by a preponderance of the evidence." § 13–25–127(1), C.R.S. (2021).

That burden rests with the plaintiff—here, the Commissioner. As we have explained in other contexts, in evidence law, a presumption "shifts the burden of going forward to the party against whom it is raised." *Krueger v. Ary*, 205 P.3d 1150, 1154 (Colo. 2009); *see also* CRE 301; *People v. Hoskin*, 2016 CO 63, ¶ 10, 380 P.3d 130, 134. Because the plaintiff already bears the burden of proof in a civil enforcement action, the concept of a "presumption" being applied on top of that burden suggests some kind of heightened threshold that the plaintiff must reach. Indeed, at least one court has said as much. *See Youmans,* 791 F.2d at 346 ("[A] strong presumption remains that a general partnership or joint venture interest is not a security. A party seeking to prove the contrary must bear a heavy burden of proof."). The CSA includes no such heightened burden for a plaintiff seeking to prove that a general partnership is operating as an investment contract.

¶29 Second, application of a presumption beyond the established burden of proof ignores a core tenet of securities law: Courts should look to the substantive, economic realities of a particular instrument, scheme, or transaction when determining whether it fits the definition of a security. *Cagle*, ¶ 26, 295 P.3d at 467; *Lowery*, 556 P.2d at 1205; *see also Landreth Timber Co. v. Landreth*, 471 U.S. 681, 686 (1985); *Int'l Bhd. of Teamsters, Chauffeurs, Warehousemen & Helpers of Am. v. Daniel*, 439 U.S. 551, 558 (1979); *Tcherepnin*, 389 U.S. at 336. And while the economic realities of a general partnership that is in fact operating as a general partnership

will tend to show that it is not an investment contract, the obligation to look at economic realities requires an examination not only of form but also of the substance of a particular venture.

¶30 Accordingly, courts evaluating whether a general partnership is an investment contract under the CSA should not start with any presumption beyond that necessarily created by the fact that the plaintiff carries the burden of proof to demonstrate that a particular interest is a security. Instead, courts should examine the economic realities of the venture, requiring the plaintiff to demonstrate the existence of an investment contract by a preponderance of the evidence. Respondents argue that the presumption plays an important role in business: It lends transactions a degree of predictability and certainty because it not only alerts investors who join partnerships that the securities laws will not protect them, but it also clarifies for promoters how to comply with regulatory requirements. Yet just as the form of a venture cannot insulate it from the reach of the securities laws, the absence of a presumption will not convert a venture into an investment contract if it is not one under *Howey*. We are not today altering the definition of investment contract, nor are we departing from other courts in recognizing that the economic realities of a bona fide general partnership are such that ordinarily it would not be an investment contract.

¶31 *Williamson* offers helpful guidance on how to analyze the substantive, economic realities of a particular general partnership. We turn now to the three aspects of this guidance about which the parties disagree.

## D. The *Williamson* Framework

¶32 As we have discussed, general partnership interests are not ordinarily investment contracts because they grant partners control over significant decisions of the enterprise. However, they may be investment contracts when "the general partner in fact retains little ability to control the profitability of the investment." *Merch. Cap.*, 483 F.3d at 755. *Williamson* identified three specific situations in which that might occur. Two of those are in dispute here.

### 1. *Williamson* Test Two

¶33 *Williamson* recognized that a general partnership may be an investment contract if "the partner or venturer is so inexperienced and unknowledgeable in business affairs that he is incapable of intelligently exercising his partnership or venture power." 645 F.2d at 424. The logic of this exception is straightforward: A partner who cannot exercise powers intelligently is dependent upon the investment's promoter or manager. *See id.* at 423. Dependent investors cannot protect themselves, are led to expect profits from the efforts of others, and thus require the protection of securities laws. *See id.*

¶34 The Commissioner argues that courts should look to investors' venture- or industry-specific knowledge. She urges us to conclude that only that specific knowledge will ensure that investors can exercise partnership powers intelligently. But we think that approach would be too narrow. Certainly, as the division below recognized, specialized knowledge or lack thereof may be relevant to the question of whether investors can exercise their partnership powers. But it does not follow that a lack of industry-specific knowledge, regardless of the nature of the underlying venture or the partner's level of sophistication, renders that partner dependent on the manager. In *Williamson*, for example, the court concluded that an investor's position as a corporate director in the food production industry constituted adequate knowledge and experience for a real estate venture. *Id.* at 424–25; *see also Robinson v. Glynn*, 349 F.3d 166, 170–72 (4th Cir. 2003); *Holden v. Hagopian*, 978 F.2d 1115, 1121 (9th Cir. 1992). Undoubtedly, there are circumstances in which a lack of specialized knowledge or experience would be probative of an inability to exercise partnership powers meaningfully, and courts should certainly look to that evidence when relevant. But specialized knowledge is not always required.

¶35 The division below surveyed cases applying this *Williamson* test and set out a list of questions that courts might consider when determining whether investors possess sufficient knowledge or experience:

(1) Do the partners generally have some prior business experience?

(2) What was the nature of that experience, both in their investing and in their other business dealings?

(3) "Are the partners otherwise financially sophisticated?"

(4) Did the partners hold themselves out as being experienced in business?

(5) Do the partners in fact have experience in the same type of business venture or industry?

(6) Is the nature of this particular venture such that industry- or venture-specific experience would be essential?

(7) Did the partners consult counsel or indicate that they would do so?

(8) Did the partners in fact exercise partnership powers?

(9) "Did the partners previously invest in one of the defendant's businesses?"

(10) "How did the partnership acquire its members?"

(11) How much meaningful access to information about the venture is available to the partners?

*HEI II*, ¶ 48, 490 P.3d at 802. We agree that these questions, among others that might be appropriate to the facts of a particular case, are helpful in evaluating the economic realities of a venture to determine whether investors are true general partners or are in fact passive investors because of their inability to meaningfully exercise their partnership powers.

### 2. *Williamson* Test Three

¶36 *Williamson* recognized that,

> [a] genuine dependence on others might also exist where the partners are forced to rely on some particular non-replaceable expertise on the part of a promoter or manager. Even the most knowledgeable partner may be left with no meaningful option when there is no reasonable replacement for the investment's manager.

645 F.2d at 423. Thus, a general partnership may be an investment contract if "the partner or venturer is so dependent on some unique entrepreneurial or managerial ability of the promoter or manager that [they] cannot replace the manager of the enterprise or otherwise exercise meaningful partnership or venture powers." *Id.* at 424.

¶37 The dispute between the parties regarding this test hinges on whether the Commissioner must prove only that the partners themselves could not realistically step into the shoes of HEI and HEDC if they wanted to, or whether the Commissioner must prove that the partners could not exercise their partnership powers to find a replacement manager who would fit the bill.

¶38 On that question, it is clear that partners can delegate day-to-day management responsibilities but still retain ultimate control over the business; they do not themselves need to have the skills to manage the venture in place of the manager. *See, e.g.*, *Holden*, 978 F.2d at 1123 ("A showing that the general partners do not possess the skills or abilities required to fill the manager's shoes

simply is insufficient."). "So long as the investor retains ultimate control, [they have] the power over the investment and the access to information about it which is necessary to protect against any unwilling dependence on the manager." *Williamson*, 645 F.2d at 424. But if the "partners are so dependent on a particular manager that they cannot replace him or otherwise exercise ultimate control," then the partners are not truly active investors, and the venture might be an investment contract. *Id.*

¶39 On this test, *HEI II* remanded to the trial court for further findings in part because it was not clear on the record whether the trial court looked only to whether *the partners themselves* could replace the manager. *HEI II*, ¶¶ 50–52, 490 P.3d at 802–03. We agree that this question requires clarification of the record here. On remand, the court should consider whether the general partners can realistically, in accordance with their partnership powers, find a reasonable replacement for the manager.

### 3. Other Economic Realities

¶40 To determine if a given instrument or scheme is a security requires "close attention to the facts of each case and a substantive appraisal of the commercial realities of the offering." *Lowery*, 556 P.2d at 1205. Consistent with this approach, *Williamson* qualified its three tests as nonexhaustive—they are examples of the unusual situations in which a general partnership meets the *Howey* test, and they

were the tests that were relevant (and unsatisfied) in that particular case. *Williamson*, 645 F.2d at 424 n.15. We similarly recognize that the three tests are not exclusive and cannot trump or restrict courts' obligation to look to the "substantive economic realities underlying the transaction," *Cagle*, ¶ 26, 295 P.3d at 467 (quoting *Viatica Mgmt.*, 55 P.3d at 266).

¶41 The *HEI II* division cautioned that (1) *Williamson*'s three tests provide room for analysis of a range of facts, and, (2) if facts are perceived to be relevant but do not fit one of the three exceptions, then the economic realities that the court looks to should "be articulated in terms of some relatively concrete principle that will assist the court in deciding whether the partners were 'led to expect profits derived from the entrepreneurial or managerial efforts of others.'" *HEI II*, ¶ 60, 490 P.3d at 804 (quoting *Toothman*, 80 P.3d at 811). Here, the Commissioner asserts that *HEI II* disregarded "longstanding," "well-established" federal and Colorado law by narrowing the catch-all, open nature of the types of "economic realities" courts may consider when determining whether a general partnership is an investment contract. But *HEI II* was not nearly as restrictive as the Commissioner claims. Notably, it did not clearly foreclose the trial court from considering the various facts that the Commissioner puts forth as the material facts in this case (facts that are not at issue before us today).

¶42 An overly expansive approach to "economic realities" would effectively undermine the value of applying *Williamson* to the particular context of general partnership interests. As may be clear by now, we find the logic of the *Williamson* framework compelling, and we consider the framework bound by both the principles of general partnerships and the *Howey* test.

## III. Conclusion

¶43 When faced with an assertion that an interest in a general partnership is an investment contract and thus within the CSA's definition of a "security," the plaintiff bears the burden of proving this claim by a preponderance of the evidence. No presumption beyond that burden applies. Accordingly, we reverse the court of appeals' judgment on the question of whether courts should apply a "strong presumption," and we remand the case to the trial court for further findings consistent with this opinion.