

NOTICE OF RULEMAKING ACTION
TITLE 10. CALIFORNIA DEPARTMENT OF CORPORATIONS

NOTICE IS HEREBY GIVEN

The California Corporations Commissioner (Commissioner) proposes to amend a rule under the Corporate Securities Law of 1968 relating to investment advisers with custody or possession of clients' funds or securities. The Commissioner proposes to amend Section 260.237 of Title 10 of the California Code of Regulations.

PUBLIC COMMENTS

No public hearing is scheduled. Any interested person or his or her duly authorized representative may request, in writing, a public hearing pursuant to Section 11346.8(a) of the Government Code. The request for hearing must be received by the Department of Corporations' (Department) contact person designated below no later than 15 days prior to the close of the written comment period.

WRITTEN COMMENT PERIOD

Any interested person, or his or her authorized representative, may submit written comments relevant to the proposed regulatory action to the Department, addressed as follows:

Regular Mail

Department of Corporations
Attn: Karen Fong, Office of Legislation and Policy
1515 K Street, Suite 200
Sacramento, CA 95814

Electronic Mail

regulations@corp.ca.gov

Facsimile

(916) 322-5875

Comments may be submitted until 5:00 p.m., December 31, 2012. If the final day for the acceptance of comments is a Saturday, Sunday or state holiday, the comment period will close at 5 p.m. on the next business day.

INFORMATIVE DIGEST/PLAIN ENGLISH OVERVIEW

Section 260.237

The existing rule sets forth requirements for investment advisers with custody or possession of clients' funds or securities. In general, the amendments define the term "custody," and, subject to certain limited exceptions, require that advisers with custody maintain the assets with a qualified custodian, as defined in the rule. The proposed amendments incorporate provisions from the Securities and Exchange Commission's

("SEC") custody rule adopted under the Investment Advisers Act of 1940, and the recently adopted North American Securities Administrators Association ("NASAA") Model Custody Rule (the "Model Rule").¹

The proposed regulatory action would benefit California investors by increasing safeguards relating to their funds and securities.

The Department does not believe that the proposed regulation is either inconsistent or incompatible with existing state regulations.

AUTHORITY

Sections 25235, 25237 and 25610, Corporations Code.

REFERENCE

Sections 25235 and 25237, Corporations Code.

AVAILABILITY OF MODIFIED TEXT

The text of any modified regulation (with the changes clearly indicated), unless the modification is only non-substantial or solely grammatical in nature, will be made available to the public at least 15 days prior to the date the Department adopts the regulation(s). A request for a copy of any modified regulation(s) should be addressed to the contact person designated below. The Commissioner will accept written comments on the modified regulation(s) for 15 days after the date on which they are made available. The Commissioner may thereafter adopt, amend or repeal the foregoing proposal substantially as set forth above without further notice.

AVAILABILITY OF STATEMENT OF REASONS, TEXT OF PROPOSED REGULATIONS/INTERNET ACCESS

The express terms of the proposed action may be obtained upon request from any office of the Department. Request Document PRO 04/11 - B. An initial statement of reasons for the proposed action containing all the information upon which the proposal is based is available from the contact person designated below. Request Document PRO 04/11-C. These documents are also available through the Department's website www.corp.ca.gov. As required by the Administrative Procedure Act, the Office of Legislation and Policy maintains the rulemaking file. The rulemaking file is available for public inspection at the Department of Corporations, Office of Legislation and Policy, 1515 K Street, Suite 200, Sacramento, California 95814.

AVAILABILITY OF THE FINAL STATEMENT OF REASONS

Upon its completion, the Final Statement of Reasons will be available and copies may be requested from the contact person named in this notice or may be accessed on the website listed above.

FISCAL IMPACT

- Cost or savings to any state agency: none.
- Direct or indirect costs or savings in federal funding to the state: none.

¹ Rule 206(4)-2 adopted by the Securities and Exchange Commission under the Investment Advisers Act of 1940, 17 CFR § 275.206(4)-2; see also SEC Release No. IA-2968, March 12, 2010; NASAA Custody Requirements for Investment Advisers Model Rule 102(e)(1)-1, Amended September 11, 2011).

- Cost to local agencies and school districts required to be reimbursed under Part 7 (commencing with Section 17500) of Division 4 of the Government Code: none.
- Other nondiscretionary costs/savings imposed on local agencies: none.

RESULTS OF THE ECONOMIC IMPACT ANALYSIS

Pursuant to Government Code Section 11346.5(a)(10), the Department has determined that:

- (1) The proposed action will not create or eliminate jobs within California;
- (2) The proposed action will not create new businesses or eliminate existing businesses within this state;
- (3) The proposed action will not affect the expansion of businesses currently doing businesses within California; and
- (4) Benefits to the health and welfare of California residents, worker safety, and the state's environment: The proposed regulatory action will not adversely affect the health and welfare of California residents, worker safety, or the state's environment. The proposed regulatory action will not benefit the health of California residents, worker safety, or the State's environment. The proposed regulatory action would benefit the general welfare of California investors by increasing safeguarding of investor funds and securities, including minimizing the risk of misappropriation or other misuse of investor assets by an investment adviser.

CONSIDERATION OF ALTERNATIVES

In accordance with Government Code section 11346.5(a)(13), the Department must determine that no reasonable alternative it considered to the regulation or that has otherwise been identified and brought to the attention would either be more effective in carrying out the purpose for which the action is proposed or would be as effective and less burdensome to affected private persons or would be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provision of law.

DISCLOSURES REGARDING THE PROPOSED REGULATION

The Commissioner has made an initial determination that the proposed regulatory action:

- Does not impose a mandate on local agencies or school districts, or a mandate that is required to be reimbursed pursuant to Part 7 (commencing with Section 17500) of Division 4 of the Government Code.
- Does not have an effect on housing costs.
- Does not have a significant statewide adverse economic impact directly affecting businesses, including the ability of California businesses to compete with businesses in other states.

COST IMPACTS ON REPRESENTATIVE PRIVATE PERSON OR BUSINESS

The Department is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed action.

EFFECT ON SMALL BUSINESS

The Commissioner has determined that the adoption of these regulations will not affect small business. Under Government Code Section 11342.610, "small business" does not include the professional or business activity of investment advisers.

CONTACT PERSON

Nonsubstantive inquiries concerning this action, such as requests for copies of the proposed regulation or questions regarding the timelines or rulemaking status, may be directed to Karen Fong at (916) 322-3553. The backup contact person is Tanya Bosch at (916) 322-3553. Inquiries regarding the substance of the proposed regulation may be directed to Salony Mehrok, Corporations Counsel at (916) 322-6927 or via email at salony.mehrok@corp.ca.gov.

Dated: October 18, 2012
 Sacramento, California