

FINAL STATEMENT OF REASONS
FOR THE ADOPTION OF RULES UNDER THE
CORPORATE SECURITIES LAW OF 1968
PRO 05/15

UPDATED INITIAL STATEMENT OF REASONS [Government Code Section 11346.9,
Subdivision (a)(1)]

Section 260.211.4

The proposed regulation as originally noticed to the public, would have required individuals who are ineligible for the exemption as finders to register with the Commissioner of Business Oversight (Commissioner) as broker-dealers or agents. In response to the comments received from the author and sponsor of Assembly Bill 667 (AB 667), individuals who were subject-matter experts for AB 667, and a member of the public who may be directly or indirectly affected by or otherwise interested in the proposed regulations, the Department has amended the language in subsections (f) and (g) to clarify that an individual who is ineligible for the exemption must register as a broker-dealer or agent if acting as a broker-dealer or an agent as defined under the Corporations Code and not otherwise exempt; and delete the language requiring broker-dealers and agents to register with the Commissioner. AB 667 established the exemption for finders from the broker-dealer provisions of the Corporate Securities Law of 1968 (Corporations Securities Law).¹

The proposed regulations would have also required finders to provide their social security number in the Statement of Information in subsection (g), and incorporated the Department's information privacy notices in subsection (h), which included information not relevant to the exemption. In response to the comments received, the Department has added language to subsection (g) informing finders that disclosure of social security numbers is voluntary, deleted subsection (h) and added new information privacy notices specific to the exemption to subsection (g).

The proposed regulations would have used "registered representative" instead of "agent" in the Statement of Information in subsection (g). In response to a comment, the Department has changed the wording from "registered representative" to "agent" to ensure the terminology in the proposed regulations is appropriate.

The Department has added language to subsection (f) to clarify that broker-dealers and agents who are registered pursuant to the Corporate Securities Law are ineligible for the finder exemption and made nonsubstantive changes to the section to improve readability.

The Department has revised the anticipated date to electronic file the Statement of Information to late-2018. The Department had anticipated implementing electronic filing by mid-2016, which did not happen. See page 3 of the Initial Statement of Reasons.

Section 260.211.5

¹ Chap. 743, Stats. 2015.

The proposed regulation as originally noticed to the public, would have required individuals who are ineligible to renew the exemption as finders to register with the Commissioner as broker-dealers or agents. In response to the comments received from all four commenters, the Department has amended the language in subsection (e) to clarify that a finder who is ineligible to renew the exemption must register as a broker-dealer or agent if acting as a broker-dealer or an agent as defined under the Corporations Code and not otherwise exempt, and delete the language requiring broker-dealers and agents to register with the Commissioner. The Department has also made the same changes to Part II of the Statement of Information in Section 260.211.4 for consistency.

The Department has made nonsubstantive changes to Section 260.211.5 to improve readability.

Section 260.211.7

The Department has made nonsubstantive changes to the language in Section 260.211.7 to improve readability by replacing “shall” with “must” and making other similar changes.

Economic Impact Assessment – (C) The Expansion of Businesses Currently Doing Business Within the State

The Department has updated Section (C) of the Economic Impact Assessment on page 7 of the Initial Statement of Reasons to read:

“The Commissioner has determined this regulatory proposal will likely not result in the expansion of business currently doing business within the state. The regulatory proposal will require regulation of the existing finder industry.”

LOCAL MANDATE DETERMINATION [Government Code Section 11346.9, Subdivision (a)(2)]

The proposed regulations do not impose any mandate on local agencies or school districts.

SUMMARY AND RESPONSE TO COMMENTS RECEIVED DURING THE INITIAL NOTICE PERIOD OF MAY 26, 2016 THROUGH JULY 15, 2016 [Government Code Section 11346.9, Subdivision (a)(3)]

COMMENT NO. 1.1: The Corporations Committee of the Business Law Section of the California State Bar (State Bar) stated the language of the proposed regulations is overbroad and does not reflect the permissive intent of the exemption. According to the commenter, AB 667 was intended to permit a finder who does not meet the exemption requirements to engage in his or her activities without the need to register as a broker-dealer, if the finder does not otherwise meet the definition of a broker-dealer or is otherwise exempt from registration. The proposed rule as originally noticed to the public would require any finder who does not file for the exemption to register as a broker-dealer or an agent. The State Bar suggested clarifying that the exemption is an option for

individuals acting as finders and not a mandate, and submitted revisions to the proposed rules with its comments. The State Bar sponsored AB 667. See Comments, Tab F.

Response: The Department has accommodated this comment by substantially adopting the commenter's revisions to Sections 260.211.4 and 260.211.5.

COMMENT NO. 1.2: The State Bar expressed concern that the requirement to disclose social security numbers on the Statement of Information violates federal privacy law, and creates privacy and identity theft problems, which will deter finders from electing to file the exemption and undermine the goals of AB 667. The State Bar suggested eliminating the requirement for finders to provide their social security number on the Statement of Information, or alternatively make clear the information is a voluntary disclosure and provide the federally mandated disclosures. See Comments, Tab F.

Response: The Department has accommodated this comment by adding language to the Statement of Information in Section 260.211.4 informing finders that disclosure of their social security number is voluntary. This change is consistent with the Department's policy to generally treat the disclosure of social security numbers as voluntary.

COMMENT NO. 1.3: The State Bar recommended clarifying that finders who fail to comply with the requirements for renewal may subsequently refile an initial Statement of Information to the extent they are eligible. The State Bar suggested this is consistent with the intent and objectives of AB 667. The proposed rule as originally noticed to the public would prohibit finders who failed to comply with the exemption requirements from renewing the exemption. See Comments, Tab F.

Response: The Department has decided not to accommodate this comment because AB 667 does not address whether a finder who does not meet the conditions to renew the exemption may start over by refiling the original exemption or the circumstances under which the original exemption may be refilled. The Department requires time to review the renewal filings and examine finders before considering adopting any additional requirements. The Department has revised the language in the Statement of Information form in Section 260.211.4 to state that finders are not eligible to renew the exemption (rather than they are prohibited from renewing the exemption) to provide the Department regulatory flexibility to address these situations.

COMMENT NO. 2: Assembly Member Donald P. Wagner stated AB 667 was not intended to regulate activities that would not otherwise trigger broker-dealer registration under existing guidance nor was it by definition applicable to all persons or situations. He suggested clarifying the proposed rules to be consistent with definition and use of the term "finder" in AB 667, in accordance with the revisions recommended by the State Bar. Assembly Member Wagner authored AB 667. See Comments, Tab F.

Response: The Department has accommodated this comment as discussed above in the response to Comment No. 1.1.

COMMENT NO. 3: Julie Ryan and Robert Rugani stated the proposed regulations exceed the scope of and are inconsistent with AB 667 because they would require any person who does not meet the requirements of AB 667 to register as a broker-dealer,

regardless of his or her activities. The commenters concurred with the State Bar's interpretation of AB 667 as requiring an individual who does not satisfy the requirements of the AB 667 exemption to register as a broker-dealer if engaged in the business of transacting securities. The commenters were subject-matter experts for AB 667 during the legislative process. See Comments, Tab F.

Response: The Department has accommodated this comment as discussed above in the response to Comment No. 1.1.

COMMENT NO. 4.1: Keith Bishop stated the Department cannot mandate the disclosure of social security numbers under federal privacy law. See Comments, Tab F.

Response: The Department has accommodated this comment as discussed above in the response to Comment No. 1.2.

COMMENT NO. 4.2: Keith Bishop stated the notices under Section 260.211 of the existing regulations for broker-dealers should not be incorporated in the proposed regulations because the notices include information specific to licenses issued by state agencies and the Statement of Information is not a license. See Comments, Tab F.

Response: The Department agrees the information privacy notices should not be incorporated in the proposed regulations because the exemption is not a professional or occupational license or otherwise subject to Family Code section 17250 or Business and Professions Code section 494.5. The Department has accommodated this comment by adding new information privacy notices to the Statement of Information in subsection (g) and deleting subsection (h) of Section 260.211.4.

COMMENT NO. 4.3: Keith Bishop stated the proposed rule is overbroad and inconsistent with the statutory exemption because the rule would require all individuals who do not meet the conditions of the exemption to register as broker-dealers. The commenter recommended clarifying that an individual who meets the definition of "broker-dealer" in Section 25004 and not otherwise exempt from registration must register as broker-dealers. See Comments, Tab F.

Response: The Department has accommodated this comment as discussed above in the response to Comment No. 1.1.

Comment No. 4.4: Keith Bishop commented the proposed regulations incorrectly state agents must register with the Commissioner. See Comments, Tab F.

Response: The Department has accommodated the comment by deleting "with the Commissioner".

COMMENT NO. 4.5: Keith Bishop stated referring to "An individual" and "A natural person" in the instructions to the Statement of Form is redundant. See Comments, Tab F.

Response: The Department has decided not to accommodate this comment for purposes of ensuring clarity for filers of the Statement of Information.

COMMENT NO. 4.6: Keith Bishop stated “registered representative” should be deleted from Part I, Section 1(H) of the Statement of Information because the term is not used in the Corporate Securities Law and the statutory exemption does not expressly disqualify “registered representatives” from relying on the exemption. See Comments, Tab F.

Response: The Department has accommodated the comment by deleting “registered representative” from subsection (g) of Section 260.211.4 and replacing it with “registered as an agent”, which is the term used in the Corporate Securities Law.

SUMMARY AND RESPONSE TO COMMENTS RECEIVED DURING THE PERIOD THE MODIFIED TEXT WAS MADE AVAILABLE TO THE PUBLIC [Government Code Section 11346.9, Subdivision (a)(3)]

The modified text was made available to the public for comment from March 28, 2017 through April 14, 2017. The Department received the following comments from the State Bar. See Comments, Tab E.

COMMENT NO. 1.1: The State Bar recommended for consistency replacing “engaged in the business of effecting transactions in securities” with “acting as a broker-dealer as defined in Section 25004”. The commenter stated these two terms are used interchangeably in the regulations to describe the same category of individuals, which creates unnecessary ambiguity.

Response: The Department has accommodated this comment by replacing in Section 260.211.4, subsection (g), “engaged in the business of effecting transactions in securities” with “acting as a broker-dealer as defined in Section 25004”. The Department did not make the text with this change available to the public pursuant to Government Code section 11346.8, subdivision (c), because the change is nonsubstantial or sufficiently related to the original text that the public was adequately placed on notice that the change could result from the originally proposed regulatory action. The terms, “acting as a broker-dealer as defined in Section 25004” and “engaged in the business of effecting transactions in securities” are understood by the commenters and the Department to have the same meaning. The Department subsequently sought guidance from the Office of Administrative Law on whether the text with this change must be made available to the public for comment. The Office of Administrative Law agreed with the Department that a public comment period would not be required under these circumstances.

COMMENT NO. 1.2: The State Bar stated the Statement of information appears to incorrectly require agents to register with the Department. The commenter recommended deleting “or agent” from Section 260.211.4, subsections (f) and (g), and Section 260.211.5, subsection (e).

Response: The Department agrees agents are not required to register with the Department and has accommodated this comment by deleting “with the Commissioner” in the specified sections. The Department did not make the text with this change available to the public pursuant to Government Code section 11346.8, subdivision (c), because the change is nonsubstantial or sufficiently related to the original text that the public was adequately placed on notice that the change could result from the originally proposed regulatory action. Specifically, the Department had deleted “with the Commissioner” in

subsection (f) of Section 260.211.4 of the modified text to clarify that agents are not required to register with the Commissioner. The modified text was made available to the public for comment from March 28, 2017 through April 14, 2017. However, the Department failed due to an oversight to also delete “with the Commissioner” in subsection (g) of Section 260.211.4 and in subsection (e) of Section 260.211.5.

COMMENT NO. 2: The State Bar recommended revising subsection (e) of Section 260.211.5 to clarify that finders who are prohibited from renewing the exemption because of one of the enumerated acts are not barred from refiling an initial Statement of Information if they are otherwise eligible. The State Bar previously submitted this comment during the initial 45-day comment period.

Response: The Department has decided not to accommodate this comment for the reasons discussed above in the response to Comment 1.3.

ALTERNATIVES THAT WOULD LESSEN THE ADVERSE ECONOMIC IMPACT ON SMALL BUSINESSES [Government Code Section 11346.9, Subdivision (a)(5)]

No alternatives were proposed to the Department that would lessen any adverse economic impact on small business.

ALTERNATIVES DETERMINATION [Government Code Section 11346.9, Subdivision (a)(4)]

The Department has determined that no alternative it considered or that was otherwise identified and brought to its attention would be more effective in carrying out the purposes for which the regulation is proposed, would be as effective and less burdensome to affected private persons than the adopted regulation, or would be more cost effective to affected private persons and equally effective in implementing the statutory policy or exemption for finders under the Corporate Securities Law.

The regulations adopted by the Department are the only regulatory provisions identified by the Department that accomplish the goal of implementing the exemption for finders under the Corporate Securities Law. Except as set forth and discussed in the summary and responses to comments, no other alternatives have been proposed or otherwise brought to the Department’s attention.

UPDATED INFORMATIVE DIGEST [Government Code Section 11346.9, Subdivision (b)]

The Department has updated the original informative digest, which was published in the Notice of Rulemaking Action in the May 27, 2016, California Regulatory Notice Register No. Z-2016-0517-01, as follows:

- Existing law provides that an individual who does not meet the exemption requirements for a finder is subject to Corporations Code section 25210, if the individual is acting as a broker-dealer as defined in Section 25004 or an agent as defined in Section 25003, and is not otherwise exempt. The Summary of Existing Laws and Regulations, on page 6 of the original informative digest, misstated

existing law as requiring an individual who is engaged in the business of a finder to register as a broker-dealer if the individual does not meet the exemption requirements.

- Cost of the rulemaking to the Department is estimated at \$154,602. The Disclosures Regarding the Proposed Action on page 8 of the original informative digest did not include cost to any state agency.
- Corporations Code section 25165 requires every person filing a request or notice of exemption to file with the Commissioner a consent appointing the Commissioner to be the person's attorney to receive service of process under the Corporate Securities Law and authorizes the Commissioner to prescribe the consent form. The Commissioner adopted the Consent to Service of Process form in section 260.165, title 10, California Code of Regulations. The proposed regulations would require individuals who file for exemption as a finder to file a Consent to Service of Process form. Requiring finders to file the form is necessary to authorize the Commissioner to accept lawsuits and other legal documents in any noncriminal action on the finder's behalf.

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