

Common Questions Regarding the Pending Transition for Mid-Sized Investment Advisers November 2011



1. How soon may I file my application papers?

You may file your application as soon as possible. However, your application will not be approved until after January 1, 2012. Also, your firm must submit your annual updating amendment to the SEC before you are approved with California. That updating amendment must be submitted by March 30, 2012.

2. How much time should I allow for my application to be processed?

The initial review of your application usually occurs within 30 days of the date application was filed. However, high volumes of applications are being received, so expect a delay. Applications are reviewed in the order received. After a review of your application, you will receive an email notice of deficiencies that need to be corrected on your application. After all deficiencies have been satisfied, your application will be approved.

There are many variables during the review process that can delay your approval such as the complexity level of your business, how many deficiencies are noted in the application, and how quickly you respond to those deficiencies. Generally, we recommend that you allow 90-120 days from the date of filing to expect approval.

3. Is there anything I can do to help speed up processing time of my application?

Please review the [CA Instructions](#) regarding transitioning firms to ensure that all required documents are submitted, that the information is consistent between Part 1 and Part 2 of the Form ADV, and that investment adviser representatives are properly qualified.

4. What happens if I miss the June 2012 deadline? Will I still be under the SEC until I get the change done? Will I be fined? Will I be prohibited from doing business?

As of June 28, 2012, if your firm has under \$100 million in assets under management (AUM), your SEC registration will no longer permit you to perform investment advisory services in California, and your firm will be required to be licensed with the State of California in order to perform/offer these services within CA.

If you are doing business after June 28, 2012 and your firm is not registered with the State it would be considered unlicensed investment advisory activity, which could subject the firm to administrative action, including being fined. In order to ensure that your firm's business is not interrupted the Department encourages early filing and will be working with firms to assist them through the registration process.

5. In my AUM figure for purposes of determining the \$100 million benchmark, do I include assets over which I may not have discretion, but that I still bill on? For example, my client has

a 401(k) plan with her employer; I direct her when to trade/rebalance; and I bill on those assets. May I include them in calculating my AUM?

In determining the amount of your assets under management, include the securities portfolios for which you provide continuous and regular supervisory or management services.

Generally, you provide continuous and regular supervisory or management services with respect to an account if:

(a) you have *discretionary authority* over and provide ongoing supervisory or management services with respect to the account; or

(b) you do not have *discretionary authority* over the account, but you have ongoing responsibility to select or make recommendations, based upon the needs of the *client*, as to specific securities or other investments the account may purchase or sell and, if such recommendations are accepted by the *client*, you are responsible for arranging or effecting the purchase or sale.

While there are other factors to include, please keep in mind the following:

You do not provide continuous and regular supervisory or management services for an account if you:

(a) provide market timing recommendations (i.e., to buy or sell), but have no ongoing management responsibilities;

(b) provide only *impersonal investment advice* (e.g., market newsletters);

(c) make an initial asset allocation, without continuous and regular monitoring and reallocation; or

(d) provide advice on an intermittent or periodic basis (such as upon *client* request, in response to a market event, or on a specific date (e.g., the account is reviewed and adjusted quarterly).

For more assistance, please review [Instructions to Part 1A](#).

6. How often should I expect the Department of Corporations to audit me? Will it be on a regular cycle?

The Department of Corporations applies a risk-based approach to identifying firms for examination. As a result the frequency of examination can vary as risk factors change for the firm, as well as across the licensee population.

7. If my practice manages over the \$90 million benchmark and I elect to stay SEC-registered, but during a quarter I fall below \$90 million, and by quarter end, it's back above \$90 million, would I be required to de-link from the SEC and register with the State of California?

The SEC requires that if you are registered with the Commission and file an annual updating amendment to your form ADV reporting that you have less than \$90 million of assets under management, you must file an ADV-W to withdraw your SEC registration within 180 days of your fiscal year end.

You must update your brochure (i) each year at the time you file your annual updating amendment and (ii) promptly whenever any information in the brochure becomes materially inaccurate.

8. If my state application for conversion from SEC is still not approved by the deadline date, what is the correct procedure to follow?

Applications are reviewed in the order received. If your application has not been approved by the deadline and you continue to do business, you are considered to be conducting unlicensed business activities. To prevent unlicensed business activities, please file your application as soon as possible. As the June 28, 2012 deadlines approaches (i.e. is within 30 days), if your firm has filed an application and not been contacted by the Department, you should send an email to IAAPP@corp.ca.gov to inquire as to the status of the application.

9. What are the CA regulations as regards electronic mail to clients for Part 2A and 2B disclosure?

Please review DOC Proposed Rule 260.235.5. Investment Adviser Brochure Rule. Electronic delivery may be made upon prior written consent of the client.

10. Does CA follow the SEC definition of “custody” of client assets? Specifically, does deducting fees from client accounts constitute custody?

If you deduct fees from clients account, you will be considered to have custody, unless you follow the safeguarding procedures below:

1. The client has authorized the firm to deduct fees directly from their account, which is maintained by a Qualified Custodian who sends quarterly statements to clients; and
2. The client has signed a Custodial Agreement which only allows the firm to enter into transactions on their behalf and the withdraw of management fees; and
3. The client and the Qualified Custodian are sent an itemized invoice at the same time, which includes: the asset value upon which the fees are based, how the fees were computed, and the period of time for the fees.

If your firm meets the three conditions above, you will be deemed to have custody, but you will not be subject to the custodial requirements under Section 260.237.2 (CCR), Minimum Financial Requirements, and Section 260.241.2 (CCR), Reporting Requirements. For purpose of Form ADV please indicate “No” on Form ADV Part 1A, Item 9A(1)(a)(b) and “Yes” on Form ADV, Part 1B, Item 2I(1): (a), (b) and (c).

11. What are the telephone numbers if I need to call the Department? What email address may I use?

If you have any questions, please e-mail IAAPP@corp.ca.gov or call the BDIA Licensing Unit at (916) 322-6270.