



STATE OF CALIFORNIA

Department of Financial Protection and Innovation

GOVERNOR **Gavin Newsom** · COMMISSIONER **Clothilde V. Hewlett**

NOTICE OF RULEMAKING ACTION
TITLE 10. CALIFORNIA DEPARTMENT OF FINANCIAL PROTECTION
AND INNOVATION

NOTICE IS HEREBY GIVEN [Government Code Section 11346.5, Subdivision (a)(1)]

The Commissioner of Financial Protection and Innovation (“Commissioner”) proposes to adopt new regulations under the Corporate Securities Law of 1968. Specifically, the Commissioner proposes to adopt Section 260.236.2 of Subchapter 2 of Chapter 3 of Title 10 of the California Code of Regulations. The proposed regulation relates to the implementation of continuing education requirements for Investment Adviser Representatives (“IARs”).

AUTHORITY [Government Code Section 11346.5, Subdivision (a)(2)]

Corporations Code section 25610.

REFERENCE [Government Code Section 11346.5, Subdivision (a)(2)]

Corporations Code section 25236.

PUBLIC COMMENTS [Government Code Section 11346.5, Subdivision (a)(17)]

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

WRITTEN COMMENT PERIOD [Government Code Section 11346.5, Subdivision (a)(15)]

Where to Submit Comments

Any interested person, or his or her authorized representative, may submit written comments on the proposed regulatory action to the Department of Financial Protection and Innovation (“Department”), addressed as follows, by any of these means:

Postal Mail

Department of Financial Protection and Innovation

Attn: Araceli Dyson
2101 Arena Blvd
Sacramento, CA 95834

Electronic Mail

Comments may be submitted electronically to regulations@dfpi.ca.gov. Please identify the comments as PRO 07-21 in the subject line.

Time for Comments

Comments may be submitted until January 16, 2023. If the final day for the acceptance of comments is a Saturday, Sunday or state holiday, the comment period will close on the next business day.

INFORMATIVE DIGEST [Government Code Section 11346.5, Subdivision (a)(3)]

Policy Statement and Specific Benefits Anticipated from Regulatory Action [Government Code Section 11346.5, Subdivision (a)(3)(C)]

The objective of the proposed regulation is to adopt rules that implement continuing education requirements for Investment Adviser Representatives (“IARs”).

Benefits of the proposed regulation include protecting consumers who use investment advisers to manage their funds by ensuring that IARs remain competent and knowledgeable about current industry regulations, developments, and best practices when handling their clients’ life savings. The proposed regulations will also ensure that IARs are familiar with ethical issues related to investment advising. This will greatly contribute to overall investor protection.

One impact of the regulations will be to improve the overall quality of investment advice and professionalism provided by IARs to clients. Compliance with the proposed regulations will likely reduce the risk of investor losses due to mistakes, failure to understand investment products, fraud, and abuse. Additionally, the regulations will likely increase regulatory compliance in examinations conducted by the Department. The Department also anticipates that consumers of investment adviser services will experience fewer instances of substandard services and will be subjected to fewer instances of unethical or illegal behavior as a result of these regulations.

Summary of Existing Laws and Regulations, and Effect of Proposed Action [Government Code Section 11346.5, Subdivision (a)(3)(A)]

Corporations Code section 25236, subdivision (a), provides that no investment adviser licensed under the Corporate Securities Law of 1968,¹ shall conduct any business as such investment adviser in this state unless the investment adviser and all natural

¹ Corp. Code, § 25000 et seq.

persons associated with such investment adviser meet such specified and appropriate standards with respect to training, experience and other qualifications as the Commissioner finds necessary or desirable. However, the section does not specify the training necessary for natural persons associated with investment advisers. For instance, the statute does not specify how many units of training are required, what type of training content is acceptable, and what the applicable reporting period is.

IARs are tested for knowledge before they are registered, but there is no mechanism to ensure that their level of knowledge and competence is maintained or expanded. By comparison, most other financial professionals are subject to continuing education requirements, including broker-dealer agents, insurance agents, certified financial planners, and real estate agents.

Given that IARs play an important role in their clients' financial lives, the North American Securities Administrators Association ("NASAA") received significant support from state regulators and the securities industry for the creation of a continuing education program and developed the Investment Adviser Representative Continuing Education ("IARCE") Model Rule.

On November 30, 2020, NASAA announced that its membership voted to adopt a model rule to set parameters by which NASAA members could implement continuing education programs for investment adviser representatives in their jurisdictions. The model rule has a products and practices component and an ethics component and is intended to be compatible with other continuing education programs. This proposed rulemaking would implement NASAA's IARCE Model Rule.

Existing Federal Regulation or Statute [Government Code Section 11346.5, Subdivision (a)(3)(B)]

There are no existing federal regulations or statutes pertaining to continuing education requirements for Investment Adviser Representatives. The proposed regulatory action is not inconsistent with existing federal laws.

Existing State Regulations [Government Code Section 11346.5, Subdivision (a)(3)(D)]

The Commissioner has conducted an evaluation of whether the proposed regulation is consistent with existing state regulations and has concluded that this regulation is consistent with existing regulations under the Corporate Securities Law of 1968. There are no existing regulations pertaining to continuing education requirements for Investment Adviser Representatives. The proposed regulation is consistent with existing policy considerations under the Corporate Securities Law of 1968. Therefore, the proposed rulemaking is neither inconsistent nor incompatible with other existing state regulations.

FORMS INCORPORATED BY REFERENCE [Title 1, California Code of Regulations, Section 20, Subdivision (c)(3)]

There are no forms incorporated by reference in the proposed regulatory action.

DISCLOSURES REGARDING THE PROPOSED ACTION [Government Code Section 11346.5, Subdivision (a)(5) and (6), and (12)(A)]

- Mandate on local agencies or school districts: none.
- Cost or savings to any State agency: \$1,206,000 in costs to implement the proposed regulations and \$1,140,000 plus salary increases annually thereafter.
- Cost to any local agency or school district which must be reimbursed in accordance with Government Code sections 17500 through 17630: none.
- Other nondiscretionary cost or savings imposed on local agencies: none.
- Cost or savings in federal funding to the state: none.
- Significant effect on housing costs: none.

ECONOMIC IMPACT ON BUSINESS [Government Code Section 11346.5, Subdivision (a)(8)]

The Commissioner has made an initial determination that the proposed regulatory action is unlikely to have a significant, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states. In making this initial determination, the Commissioner relied on a 2021 NASAA Investment Adviser Section Annual Report and the NASAA Survey results Summary (2018) to support her initial determination that the regulatory action will likely not have a significant adverse economic impact on business. The Commissioner has not relied on any other reports, facts, evidence, documents, or testimony to support the initial determination that the regulation is unlikely to have a significant, statewide adverse economic impact on business.

EFFECT ON SMALL BUSINESS [Title 1, California Code of Regulations, Section 4]

Under Government Code section 11342.610, subdivision (b), an investment adviser is not a small business. Therefore, this rulemaking action will not have an impact on small businesses.

COST IMPACTS ON REPRESENTATIVE PRIVATE PERSON OR BUSINESS [Government Code Section 11346.5, Subdivision (a)(9)]

Investment adviser representatives will incur annual costs estimated at \$36 (for the annual reporting fee), plus the cost of continuing education courses, to comply with the continuing education requirements. Some courses will be offered by NASAA for free

while other course will be offered at varying prices depending on the authorized provider. IARs who are also registered as a broker-dealer agent and/or hold other professional designations may incur minimal to no costs for continuing education courses. This is because an IAR who is also a registered broker-dealer agent and complies with FINRA's Continuing Education requirements for broker-dealer agents will be in compliance with the requirement to report six credits of Products and Practices content under the proposed rule. IARs who hold other professional designations may also be in compliance with the IAR continuing education requirements under the proposed rule. Therefore, many IARs who are dually registered as broker-dealer agents or hold other professional designations will already meet some or all of the continuing education requirements of this regulatory proposal.

RESULTS OF THE ECONOMIC IMPACT ANALYSIS [Government Code Section 11346.5, Subdivision (a)(10)]

The Commissioner has determined:

- The proposed action will not result in the creation of new jobs within the state. The proposed rule imposes continuing education requirements on IARs registered in this state. Providers of continuing education may experience an increase in demand for services but not significantly enough to add positions or create jobs.
- The proposed action will not result in the creation of new businesses in the state. The proposed rule imposes continuing education requirements on IARs registered in California. Therefore, the rule may cause existing providers of continuing education to expand their products and services to IARs who must fulfill the new requirements. However, the Department does not anticipate a creation of new businesses. Also, the Department does not anticipate an elimination of existing businesses due to the regulation.
- The proposed action may result in the expansion of businesses currently doing business in the state. The proposed rule imposes continuing education requirements on IARs registered in California. Therefore, the proposed rule may cause existing businesses that provide continuing education to expand their products and services to IARs who must fulfill the new requirements.
- As discussed above under the Informative Digest, the proposed action may benefit the health and welfare of California residents by protecting consumers who use investment advisers to manage their funds by ensuring that IARs remain competent and knowledgeable about current industry regulations, developments, and best practices when handling their clients' life savings. The proposed regulations will also ensure that IARs are familiar with ethical issues related to investment advising, contributing to overall investor protection.
- No benefits or adverse impacts to worker safety or to the state's environment are

anticipated from this regulatory action.

BUSINESS REPORTING REQUIREMENT [Government Code Section 11346.5, Subdivision (a)(11)]

This proposed rulemaking does not impose any business reporting requirements. Under the proposed regulation, the IAR is responsible for ensuring that authorized providers of continuing education report the IAR's completion of the courses.

CONSIDERATION OF ALTERNATIVES [Government Code Section 11346.5, Subdivision (a)(13)]

The Commissioner must determine that no reasonable alternative considered by the Department, or that has otherwise been identified and brought to the attention of the Department, would: be more effective in carrying out the purpose for which the action is proposed; be as effective and less burdensome to affected private persons than the proposed action; or be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provision of the law.

AVAILABILITY OF THE NOTICE, STATEMENT OF REASONS, TEXT OF PROPOSED REGULATIONS AND RULEMAKING FILE [Government Code Section 11346.5, Subdivision (a)(16) and (20), and (b)]

As of the date this Notice is published, the rulemaking file consists of this Notice, the Initial Statement of Reasons, the Proposed Text of the regulations, and all the information upon which the proposal is based. The Notice, Initial Statement of Reasons, and Proposed Text are available by contacting the person designated below:

Department of Financial Protection and Innovation

Attn: Araceli Dyson
2101 Arena Blvd
Sacramento, CA 95834
Telephone: (916) 839-8995
E-mail: regulations@dfpi.ca.gov

The Notice, Proposed Text, and Initial Statement of Reasons are also available on the Department's website at www.dfpi.ca.gov. To access the documents from the Department's website, select the "Laws and Regulations" tab under the "Licensees" dropdown menu on the home page, select the "Regulations/Rulemaking" link, and then select the "Corporate Securities Law of 1968" link.

As required by the Administrative Procedure Act, the Department's Legal Division maintains the rulemaking file. The rulemaking file is available for public inspection and copying throughout the rulemaking process at the Department of Financial Protection and Innovation, Legal Division, 2101 Arena Blvd, Sacramento, CA 95834.

AVAILABILITY OF CHANGED OR MODIFIED TEXT [Government Code Section 11346.5, Subdivision (a)(18)]

If the Department makes changes which are sufficiently related to the original Proposed Text, it will make the modified text (with changes clearly indicated) available to the public for at least 15 days before the Department adopts, amends or repeals the regulations as revised. A request for a copy of any modified regulation(s) should be addressed to the contact person designated above. The Department will accept written comments on the modified regulations for at least 15 days after the date on which they are made available.

AVAILABILITY OF FINAL STATEMENT OF REASONS [Government Code Section 11346.5, Subdivision (a)(19)]

Upon its completion, the Final Statement of Reasons will be available to the public, and copies may be requested from the contact person named above or accessed on the Department's website listed above.

CONTACT PERSON [Government Code Section 11346.5, Subdivision (a)(14)]

Inquiries regarding the substance of the proposed regulation may be directed to:

Department of Financial Protection and Innovation
Attn: Counsel Pamela Hernandez
One Sansome Street, Suite 600
San Francisco, California 94104
Telephone: (415) 263-8514
E-mail: pamela.hernandez@dfpi.ca.gov

Non-substantive 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:

Department of Financial Protection and Innovation
Attn: Araceli Dyson
2101 Arena Blvd
Sacramento, CA 95834
Telephone: (916) 839-8995
E-mail: regulations@dfpi.ca.gov

The backup contact person for non-substantive inquiries is:

Department of Financial Protection and Innovation
Attn: Mark Dyer
2101 Arena Boulevard

Sacramento, California 95834
Telephone: (916) 576-3637
E-mail: regulations@dfpi.ca.gov

Dated: November 16, 2023
San Francisco, California