

NOTICE OF RULEMAKING ACTION
TITLE 10. CALIFORNIA DEPARTMENT OF CORPORATIONS

NOTICE IS HEREBY GIVEN

The California Corporations Commissioner (Commissioner) proposes to amend Sections 260.210, 260.211, 260.211.1, 260.231, 1422, 1422.7, 1423, 1581, 1582, 1805.204, and 1950.122.8; and to adopt Section 1430 in 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., January 28, 2013. 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.

AUTHORITY AND REFERENCE

Corporations Code Sections 25211, 25211(b), 25231, 25610, 25612.3 and 25612.5; and Financial Code Sections 22150, 22159, 30006, 30204, and 50304 authorizes the Commissioner to adopt/amend the proposed regulation.

The proposed regulation implements, interprets and makes specific Sections 31 and 494.5, Business and Professions Code; Section 1798.17 and 1798.24, Civil Code;

Sections 22100, 22101, 22102, 22105, 22105.1, 22105.2, 22105.3, 22106, 25210, 25211, 25213, 25213.3, 25216, 25217, 25230, 25231, 25234, 25236, 25237, 25241, 25242, 25608, 25612.3, 25612.5 and 25613, Corporations Code; Section 17520, Family Code; Sections 22000, 22050, 22100, 22101, 22101.5, 22102, 22103, 22104, 22105, 22106, 22107, 22108, 22109, 22112, 22153, 22154, 22157, 22159, 22160, 22349, 22349.1, 22351, 22357(a), 30204, 50002, 50003, 50120, 50121, 50122, 50124, 50130, 50140, 50146 and 50151, Financial Code; Sections 7470, 7473, 7490 and 13140-13144, Government Code; Section 11077.1, Penal Code; and Section 7 of Public Law 93-579 (5 U.S.C. Section 552a note).

INFORMATIVE DIGEST

This regulatory action proposes to 1) amend the application forms and information practices and privacy notices under the Corporate Securities Law of 1968, the California Finance Lenders Law, the California Residential Mortgage Lending Act and the Securities Depository Law to notify applicants and licensees that the Department may deny or suspend licenses issued to individuals and businesses for failure to pay their California state tax obligation, and to request federal taxpayer identification numbers from business entities for the purpose of identifying delinquent business taxpayers, 2) change the license application form under the California Finance Lenders Law to allow operating subsidiaries of federally chartered banks or financial institutions to obtain licensure, 3) clarify the reporting of past criminal acts and other violations in the license application under the California Finance Lenders Law, 4) amend the California Finance Lenders Law application to eliminate self-certification of investor status, and 5) adopt the annual report form under the California Finance Lenders Law.

Deny or Suspend Licenses of Delinquent Taxpayers

Assembly Bill 1424 (Chap. 455, Statutes of 2011) requires state licensing agencies that issue professional or occupational licenses, certificates, registrations, or permits, to suspend or refuse to issue a license when an applicant's or licensee's name is on either the State Board of Equalization's or the Franchise Tax Board's list of the 500 largest tax delinquencies. Among other things, the law requires state licensing agencies such as the Department to collect social security numbers or federal taxpayer identification numbers from individuals and business entities who apply for or renew a license, and match the information to the names on the tax delinquencies lists; amend license and renewal license application forms to inform applicants and licensees that their licenses may be suspended if they fail to pay their state tax obligation; and notify applicants and licensees prior to denying or suspending a license.

The Department licenses broker dealers, agents of broker dealers and investment advisers under the Corporate Securities Law of 1968; lenders, brokers and servicers under the California Finance Lenders Law and the California Residential Mortgage Lending Act; and securities depositories under the Securities Depository Law. These licensees include individuals (sole proprietors) and business entities.

Assembly Bill 1424 provides that state governmental licensing entities shall adopt regulations as necessary to implement the bill's provisions (Business and Professions Code Section 494.5(p)). Accordingly, this regulatory action proposes to amend the

application forms and information practices and privacy notices under the Corporate Securities Law of 1968 (10 CCR Sections 260.210, 260.211, 260.211.1 and 260.231), the California Finance Lenders Law (10 CCR Sections 1422, 1422.7, 1423, 1581 and 1582), the California Residential Mortgage Lending Act (10 CCR Section 1950.122.8) and the Securities Depository Law (10 CCR Section 1805.204) to request federal taxpayer identification numbers from business entities for the purpose of identifying delinquent business taxpayers, add a statement to the application forms informing applicants and licensees that their licenses may be suspended if they fail to pay their state tax obligation, and notify applicants in the notices that their social security numbers and federal taxpayer identification numbers will be used to identify certain delinquent taxpayers for the purposes of denying or suspending their licenses.

The California Information Practices Act of 1977 (Civil Code Section 1798, et seq.) and the Federal Privacy Act of 1974 (5 U.S.C.S. 552a) require the Department to notify individuals about whether disclosure of a social security number is voluntary or mandatory and what uses will be made of the information when the Department requests personal information, including social security numbers. The Department currently requests in license applications social security numbers from individuals, but not federal taxpayer identification numbers from businesses. The notices required under state and federal information privacy laws are included in or as an attachment to license application forms, or in the regulations concerning national uniform license application forms.

The proposed changes are required to ensure continued compliance under state and federal information privacy laws, and to conform to new state requirements under Assembly Bill 1424.

Change to License Application for Operating Subsidiaries

This regulatory action proposes to amend Section 1422 of the rules, the "Application for a License under the California Finance Lenders Law" (Application), to delete the declaration regarding operating subsidiary status (item number 2 in the Execution Section of the Application), so that an applicant no longer needs to declare that it is not an operating subsidiary of a federally chartered bank or financial institution in order to obtain licensure. The proposed change is necessary because federal law no longer preempts the state from requiring operating subsidiaries of national banks and savings associations to comply with state lending laws.

Currently, the applicant is required to sign a declaration in the Application, providing among other things, "[t]hat the applicant is not an operating subsidiary of a federally chartered bank or financial institution that is subject to oversight by the federal regulatory agency in accordance with federal law (12 U.S.C. §1 et seq.)."

Previously, an appellate court ruling held that operating subsidiaries meeting certain requirements and doing business under federal laws relating to national banks were not subject to the licensing provisions of the California Finance Lenders Law¹. However, effective July 21, 2011, the federal Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub.L. 111-203, signed into law on July 21, 2010) effectively

¹ (Wells Fargo Bank N.A. v. Boutris, 419 F.3d 949 (CA9 2005).)

ended preemption for operating subsidiaries, agents and affiliates of national banks and federal savings associations.

Clarify When to Report Past Criminal Acts and Other Violations in the California Finance Lenders Law Application

The regulatory action proposes to amend question number 7 of the Application to clarify that disclosure in the Application is 1) limited to the past 10 years for criminal convictions or acts involving dishonesty, fraud or deceit substantially related to qualifications and functions of lending, brokering or servicing of loans under the California Finance Lenders Law license, and 2) not limited to any time period for violations of the California Finance Lenders Law or rules, or other similar regulatory schemes, e.g., applicants must report any and all of these violations (Financial Code Section 22109(a)(2) and (3)).

Currently, question number 7 does not identify the period of time in which to report on the information and does not make clear that the reporting periods are different for past crimes and acts, and for regulatory violations. The proposed change is necessary to ensure that applicants understand the disclosure requirements and the Department receives complete information in deciding whether to issue or deny an application.

Background Checks on Passive Investors Under the California Finance Lenders Law

The regulatory action proposes to delete the self-certification from the Application for passive investors concerning background investigations (instructions to Exhibit C in the Application). The California Finance Lenders Law requires a background investigation to be conducted on all principal officers, directors, general partners, managing members and persons owning or controlling, directly or indirectly, 10% or more of the outstanding interest or equity securities of the applicant (Financial Code Section 22105). If the person directly owning or controlling 10% or more of the applicant is an entity, the entity's principal officers, directors, general partners, managing members and persons owning or controlling 10% or more of that entity are also subject to background investigation under Financial Code Section 22105.

Some entities owning 10% or more of an applicant are merely investors such as pension plans, and are not responsible for the applicant's lending activities. Conducting a background investigation of these "passive" investors is burdensome and costly to the entity, and does not further the law's intent of ensuring that those responsible for the lending activities possess the qualifications, character and fitness to engage in finance lending.

The self-certification has been subject to abuse by some applicants attempting to use it to evade background investigations or to hide the true identity of the owner(s). Accordingly, the proposed change deleting self-certification for passive investors is necessary because it will make it more difficult to conceal the identity of persons who actually own or are responsible for the lending activities of an applicant, and make it harder for them to evade background checks. The proposed change will continue to provide the Department with the necessary discretion to waive background investigations of passive investors when doing so is consistent with the intent of the law.

Adopt Annual Report Form Under the California Finance Lenders Law

The regulatory action proposes to adopt the annual report form to Section 1430 of the California Finance Lenders Law rules. Licensees are required to file an annual report on the form prescribed by the Commissioner, by March 15, providing information on business and operations conducted under the California Finance Lenders license (Financial Code Section 22159).

The annual reporting requirement is not a new requirement and the Department has been requiring licensees to file an annual report on the prescribed or similarly prescribed form since at least 1994. The proposed action merely seeks to correct an oversight by adopting the annual report by rulemaking, and does not impose additional filing or reporting requirements on licensees. The action is necessary to ensure that potential applicants are fully informed of all reporting and disclosure requirements before they decide to apply for a license, and to comply with California's administrative rulemaking requirements.

Anticipated Benefits

The benefits anticipated from this proposed regulatory action include monetary benefits to California from ensuring that all taxpayers pay their share of state taxes, protecting general welfare and promoting fairness and equity by allowing bank operating subsidiaries to do business in California under a state license, protecting the public by ensuring that licensees possess the requisite qualifications and character for the position, and increasing transparency in government by ensuring that reporting requirements for licensees are in the regulations.

EXISTING STATE REGULATIONS

The proposed regulatory action is consistent with existing regulations that require the Department to deny or suspend a license concerning child support financial obligations, state and federal information privacy regulations, the California Finance Lenders Law and rules, and state administrative rulemaking requirements. Accordingly, the proposed amendments are not inconsistent or incompatible with existing state regulations.

DISCLOSURES REGARDING THE PROPOSED ACTION

- Mandate on local agencies and school districts: none.
- Cost or savings to any state agency: none.
- 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, statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states: none.
- Significant effect on housing costs: 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. See the Anticipated Benefits section above concerning benefits to the health and welfare of California residents. No benefits or adverse impacts to worker safety or to the state's environment are anticipated as a result of this regulatory package.

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 securities or financial lending businesses.

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. The proposed action to adopt the annual report does not impose additional filing or reporting requirements on licensees because they are already required to file annual reports under Financial Code Section 22159. Accordingly, licensees would not incur additional costs as a result of the proposed regulation.

BUSINESS REPORTING REQUIREMENT

In accordance with Government Code section 11346.3, subdivision (d), the Commissioner finds that it is necessary for the health, safety, or welfare of the people of this state that this regulation requiring a report apply to businesses.

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.

AVAILABILITY OF THE NOTICE, STATEMENT OF REASONS, TEXT OF PROPOSED REGULATIONS AND RULEMAKING FILE

As of the date this notice is published, the rulemaking file consists of this notice, the initial statement of reasons and the proposed text of the regulation. The rulemaking file is available for public inspection and copying throughout the rulemaking process at the Department of Corporations, Office of Legislation and Policy, 1515 K Street, Suite 200, Sacramento, California 95814.

The notice, initial statement of reasons and proposed text is also available on the Department's website www.corp.ca.gov.

AVAILABILITY OF CHANGED OR MODIFIED TEXT

If the Department makes modifications which are sufficiently related to the originally proposed text, it will make the modified text (with the changes clearly indicated) available to the public for at least 15 days before the Department adopts the regulations as revised. The Department will accept written comments on the modified regulations for 15 days after the date on which they are made available.

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.

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
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1515 K Street, Suite 200
Sacramento, California 95814
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e-mail: karen.fong@corp.ca.gov

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

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Dated: November 26, 2012
Sacramento, California