

CSI - Ohio

The Common Sense Initiative

Business Impact Analysis

Agency Name: Securities/ Commerce

Regulation/Package Title: 2014 Five Year Review / 123437

Rule Number(s): 1301:6-1-19; 1301:6-3-23; 1301:6-3-39.1; 1301:6-3-44; 1301:6-3-48

Date: October 28, 2014

Rule Type:

New

5-Year Review

Amended

Rescinded

The Common Sense Initiative was established by Executive Order 2011-01K and placed within the Office of the Lieutenant Governor. Under the CSI Initiative, agencies should balance the critical objectives of all regulations with the costs of compliance by the regulated parties. Agencies should promote transparency, consistency, predictability, and flexibility in regulatory activities. Agencies should prioritize compliance over punishment, and to that end, should utilize plain language in the development of regulations.

Regulatory Intent

1. Please briefly describe the draft regulation in plain language.

Please include the key provisions of the regulation as well as any proposed amendments

These rules contain prohibited activity; limitations on the Division; procedure to qualify for a retroactive exemption, qualification or registration; and records retention.

77 SOUTH HIGH STREET | 30TH FLOOR | COLUMBUS, OHIO 43215-6117

CSIOhio@governor.ohio.gov

- 1301:6-3-19 – This rule accomplishes two needs. It defines prohibited activity for dealers and salespersons. Also, to obtain and maintain a license pursuant to RC Chapter 1707 the person must be found to be of good business repute. This rule provides a definition of what constitutes good business repute. The proposed change is to correct a citation in section (D).
- 1301:6-3-23 – RC 1707.23 gives the Division the authority to conduct investigative hearings. This rule creates certain parameters for the Division and rights for the respondent, in conducting such a hearing. No change is proposed.
- 1301:6-3-39.1 – RC 1707.391 states there are occasions where neglect to timely file is considered excusable and this rule sets out the mechanism for an applicant to apply, pursuant to RC 1707.391, for retroactive filing and, upon compliance, to have the file considered as though timely filed. The proposed amendments are to omit a reference to a consent to service of process form that is no longer required and to add language to allow for a filer to be credited for any previously paid fee.
- 1301:6-3-44 – This rule was created in 1999, in conjunction with the other rules relating to Investment Advisers and representatives, to provide for general prohibitions, comparable to those that exist for dealers and salespersons, and dealing with advertisements; how customer funds are held in custody; under what circumstances a solicitor may be used; information to be disclosed to clients; and compliance practices. The proposed changes will add social media sites to advertising; revise the solicitor rule to include state securities regulatory violations as a disqualifying provision; and add a specific prohibition against any IA or IAR breaching their fiduciary duty to their client.
- 1301:6-3-48 – This rule supplements the Division’s records retention statute, RC 1707.48. The rule provides for specific types of records that the Division receives or creates and sets a minimum time for the retention of those records. The proposed amendments allow the creation, transmittal and storage of electronic records and to dispose of the hard copies once the records are converted to digital form.

2. Please list the Ohio statute authorizing the Agency to adopt this regulation.

Ohio Revised Code Section 1707.20. The rules amplify: RC 1707.19, 1707.23, 1707.391, 1707.44 and 1707.48, respectively.

3. Does the regulation implement a federal requirement?

77 SOUTH HIGH STREET | 30TH FLOOR | COLUMBUS, OHIO 43215-6117

CSIOhio@governor.ohio.gov

No.

Is the proposed regulation being adopted or amended to enable the state to obtain or maintain approval to administer and enforce a federal law or to participate in a federal program?

If yes, please briefly explain the source and substance of the federal requirement.

No.

- 4. If the regulation includes provisions not specifically required by the federal government, please explain the rationale for exceeding the federal requirement.**

Not applicable

- 5. What is the public purpose for this regulation (i.e., why does the Agency feel that there needs to be any regulation in this area at all)? **

- 1301:6-3-19 – The term “good business repute” is used in RC 1707.19 without being defined. In addition, rules prescribing fraudulent, evasive, deceptive and grossly unfair practices or devices are to be defined by the Division. The rule provides notice to the licensees, and the public, what conduct is prohibited and what constitutes good business repute, or lack thereof.
- 1301:6-3-23 – To investigate violations of the Ohio Securities Act, the Division is given the authority to conduct investigative hearings. The rule sets out how a hearing will be conducted and what limitations are placed on the Division and the outcome of the hearing to comply with due process and provide transparency in the hearing process.
- 1301:6-3-39.1 - RC 1707.391 was created to excuse a late filing. There are statutory exemptions and registrations that require a filing be made within a certain time-frame (e.g.: within 60 days of the last sale – RC 1707.03(Q)) and failure to timely file, even by one day, causes a violation of the Securities Act by selling unregistered securities. It was recognized that such strict liability was, under some circumstances, overly harsh. This rule defines “excusable neglect” and provides a mechanism for an issuer who has filed late to have the late filing excused and the securities sold considered not in violation of the Act.
- 1301:6-3-44 – RC 1707.19(C) gives the Division the responsibility to prescribe rules relating to investment advisers and investment adviser representatives. RC 1707.44(M) contains prohibited conduct and states the Division may create rules reasonably designed to prevent acts, practices, or courses of business that are fraudulent, deceptive, or manipulative. 1301:6-3-44 is intended to work in conjunction with the other IA and IAR rules to create a system comparable with the

77 SOUTH HIGH STREET | 30TH FLOOR | COLUMBUS, OHIO 43215-6117

CSIOhio@governor.ohio.gov

federal regulation of IAs and IARs for the protection of the public and the marketplace. Federal law (Investment Advisers Act of 1940) and case law have long imposed a fiduciary obligation on investment advisers and their representatives. The purpose of the proposed specific Ohio prohibition is to explicitly state that such fiduciary duty is an Ohio requirement for the protection of the investing public.

- 1301:6-3-48 – This rule provides more detail relating to specific records created or received by the Division. It puts the public on notice how long those records will be maintained, promoting transparency. The proposed amendments are to allow the recordkeeping to keep pace with the industry and public’s expectations of electronic access. Eventually, it is hoped that the use of electronic recordkeeping will reduce the economic and manpower burdens imposed by paper records.

6. How will the Agency measure the success of this regulation in terms of outputs and/or outcomes?

These rules cover a range of areas within the securities field, but success will be measured generally by how well the regulations balance the goal of investor protection and the goal of a fair and strong market. The Division encourages feedback, during Advisory group meetings at its Annual Conference and throughout the year.

Development of the Regulation

7. Please list the stakeholders included by the Agency in the development or initial review of the draft regulation.

If applicable, please include the date and medium by which the stakeholders were initially contacted.

See attached list. Stakeholders were emailed a package of the rules with a cover letter indicating which rules were No Change and which were amendments. The email was sent Oct. 3, 2014, and comments were requested by Oct. 31. Prior to that, conversations were held individually with representatives of stakeholders for input on various rule changes.

8. What input was provided by the stakeholders, and how did that input affect the draft regulation being proposed by the Agency?

One response was received indicating the organization had no comments.

9. What scientific data was used to develop the rule or the measurable outcomes of the rule? How does this data support the regulation being proposed?

The prohibitions contained in the rules are generally similar to the prohibitions at the federal level and have existed and developed over a long period. The concept of “excusable neglect”

77 SOUTH HIGH STREET | 30TH FLOOR | COLUMBUS, OHIO 43215-6117

CSIOhio@governor.ohio.gov

was developed in response to inequities perceived in the strict application of the filing time requirements. The extension limitations were developed by examining a wide variety of late filings and determining what the general average.

10. What alternative regulations (or specific provisions within the regulation) did the Agency consider, and why did it determine that these alternatives were not appropriate? If none, why didn't the Agency consider regulatory alternatives?

Strictly applying the filing deadlines was considered and latitude for inadvertent mistake was determined to be more appropriate. In imposing the prohibitions and duties, consistency with the prevalent federal and other state language was a guiding factor.

11. Did the Agency specifically consider a performance-based regulation? Please explain. *Performance-based regulations define the required outcome, but don't dictate the process the regulated stakeholders must use to achieve compliance.*

These rules generally limit actions, or require disclosure, that will act in the best interest of the market and for the protection of the public. Specific actions are only required in the preparation or dissemination of information.

12. What measures did the Agency take to ensure that this regulation does not duplicate an existing Ohio regulation?

All statutes and rules governing, or enforced by, the Division were reviewed to ensure there were no duplications or conflicts. The Division is the only Ohio agency regulating in this area.

13. Please describe the Agency's plan for implementation of the regulation, including any measures to ensure that the regulation is applied consistently and predictably for the regulated community.

These are long-standing rules of the Division and the industry has access to, and input into, the rules. To promote a fair and equal marketplace, the requirements are imposed on all regulated persons. Questions dealing with the interpretation or application of the rules may be directed to any staff member at any time by those impacted, including the public.

Adverse Impact to Business

14. Provide a summary of the estimated cost of compliance with the rule. Specifically, please do the following:

a. Identify the scope of the impacted business community;

The rules will impact all licensees and other regulated persons, including persons acting in violation of the Securities Act.

77 SOUTH HIGH STREET | 30TH FLOOR | COLUMBUS, OHIO 43215-6117

CSIOhio@governor.ohio.gov

b. Identify the nature of the adverse impact (e.g., license fees, fines, employer time for compliance); and

There could be time spent planning to prevent a prohibited activity. IAs will spend time and costs associated with providing clients with the necessary communications. To apply for a retroactive exemption, qualification, or registration an issuer will have to prepare a sworn statement to comply with the requirements of RC 1707.391.

c. Quantify the expected adverse impact from the regulation.

The adverse impact can be quantified in terms of dollars, hours to comply, or other factors; and may be estimated for the entire regulated population or for a “representative business.” Please include the source for your information/estimated impact.

- 1301:6-3-19 – There will be time and cost associated with establishing procedures to avoid prohibited activity. The cost will depend on the size of the business and the level of outsourcing.
- 1301:6-3-23 – the only costs will be to the Division
- 1301:6-3-39.1 – The time to prepare the form 391 and the sworn statement should be less than one hour.
- 1301:6-3-44 – In setting up an IA business, various bookkeeping and systems will have to be established. The size of the business, and the type and volume of clients will make the costs associated with the business vary as will the amount, if any, of compliance work that is outsourced. As a general guide, we have been given the estimate by an outside vendor of a one-time cost of \$3-to 5,000 to file the license applications and set up all the internal procedures and compliance manuals to begin the business. Once operational, the ongoing bookkeeping time will be an hour or more each day, as in any business, plus the mandatory client communications.
- 1301:6-3-48 – this is an internal rule to the Division and the only costs will be incurred by the Division.

15. Why did the Agency determine that the regulatory intent justifies the adverse impact to the regulated business community?

The compliance requirements mirror the federal requirements which were in place prior to the states taking over regulation of the smaller IAs. These rules promote safety and equality in the market by imposing the same recordkeeping and disclosure expectations on all firms. The rules protect the investing public and promote efficiency and confidence in the market.

Regulatory Flexibility

77 SOUTH HIGH STREET | 30TH FLOOR | COLUMBUS, OHIO 43215-6117

CSIOhio@governor.ohio.gov

16. Does the regulation provide any exemptions or alternative means of compliance for small businesses? Please explain.

1301:6-3-39.1 is primarily for smaller issuers. Smaller issuers, including those who act without counsel, are more likely to fail to timely file. The provision allowing solicitors in 1301:6-3-44(C) was created to permit smaller IAs to utilize unlicensed assistance under limited circumstances. This particularly assists solo practitioners.

17. How will the agency apply Ohio Revised Code section 119.14 (waiver of fines and penalties for paperwork violations and first-time offenders) into implementation of the regulation?

There will not be fines or civil penalties for violations. When the Division examines a licensee and determines there are deficiencies, communications begin in an effort to bring the licensee into compliance. For violations such as recordkeeping, there are frequently multiple communications between the Division and the licensee.

18. What resources are available to assist small businesses with compliance of the regulation?

The rules are widely available. The staff is readily available for discussions and responds to phone and email inquiries. Reoccurring issues relating to rules are addressed in the quarterly bulletin by the Division and at the annual Securities Conference. In addition, the Division conducts training and pre-licensing examinations for newly licensed or soon-to-be-licensed IAs, to which current licensees may attend.

ATTACHMENT
SECURITIES STAKEHOLDER'S LIST

FINANCIAL INDUSTRY REGULATORY AUTHORITY (FINRA)

1735 K Street Northwest

Washington, DC 20006

202-728-8000

Call Center (301) 590-6500

finra.org

Scott Borchert – State Government Liaison - (202) 728-8278

scott.borchert@finra.org

OSBA Corporation Law Committee

Securities Law Subcommittee

Professor Geoffrey Rapp (Geoff)

University of Toledo, College of Law

280 West Bancroft, MS 507

Toledo, OH 43606-3390

grapp@utnet.utoledo.edu

phone: (419) 530-2856

Thomas Geyer (Former Division Commissioner 1996-2000)

Bailey Cavalieri LLC

One Columbus

10 West Broad Street

Suite 2100

Columbus, OH 43215

phone: (614) 229-3206

(614) 221-0479

Thomas.Geyer@baileycavalieri.com

fax:

Industry

SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION

Local contact:

Antonio (Tony) C. Fiore

Kegler Brown Hill & Ritter

65 East State Street

77 SOUTH HIGH STREET | 30TH FLOOR | COLUMBUS, OHIO 43215-6117

CSIOhio@governor.ohio.gov

Columbus, Ohio 43215-4294

afiore@keglerbrown.com

Phone: (614) 462-5428

Fax: (614) 464-2634

NATIONAL ASSOCIATION OF PERSONAL FINANCIAL ADVISORS (NAPFA)

- SEC and State-registered IAs

Local Point of Contact:

Paul J. Dolce, CFP

NAPFA Registered Financial Advisor

Financial Solutions LLC

4946 Donegal Cliffs Drive

Dublin, Ohio 43017

Phone: 614-604-3551 Fax: 866-326-0396

PDolce@FinancialSols.com

Web: www.FinancialSols.com

FINANCIAL SERVICES INSTITUTE

(Independent financial services firms and advisors)

Dale Brown, President and CEO

Mr. Jigar Gandhi, State Regulatory Affairs Counsel

jigar.gandhi@financialservices.org

Financial Services Institute

607 14th St. NW

Suite 750

Washington, D.C. 20005

FINANCIAL PLANNING ASSOCIATION

- SEC and State-registered IAs

Local Point of Contact:

Mike Mulhern (mike.mulhern@LFG.com)

CENTRAL OHIO COMPLIANCE ASSOCIATION (COCA)

Christy Baker- President

Bev Langley- Vice President

77 SOUTH HIGH STREET | 30TH FLOOR | COLUMBUS, OHIO 43215-6117

CSIOhio@governor.ohio.gov

Parker Bridgeport- Secretary
Parker.Bridgeport@thompsonhine.com

at

Christy L. Baker
Director- Broker Dealer Services
Beacon Hill Fund Services, Inc.
4041 N High Street, Suite 402
Columbus, OH 43214
614.255.5547 (phone)
614.784.0211 (fax)
cbaker@b-hill.com

EDWARD JONES
Jesse Hill
Legal-Government & Regulatory Relations
12555 Manchester Road
St. Louis, MO 63131
Jesse.hill@edwardjones.com
314-515-9711

CONSUMER GROUPS

AARP Ohio
William Sundermeyer, State Director for Advocacy at AARP Ohio
AARP Ohio Office 17 S. High Street, Suite 800 Columbus, OH 43215
wSundermeyer@AARP.org
866-389-5653 Toll-free 614-224-9801 Fax ohaarp@aarp.org