State of California
Office of Administrative Law

In re:
Professional Fiduciaries Bureau

Regulatory Action:

Title 16, California Code of Regulations

Adopt section: 4640
Amend section:
Repeal section:

DECISION OF DISAPPROVAL OF REGULATORY ACTION

Government Code Section 11349.3

OAL Matter Number: 2016-0825-01

OAL Matter Type: Regular (S)

SUMMARY OF REGULATORY ACTION

This rulemaking action by the Professional Fiduciaries Bureau (Bureau) of the Department of Consumer Affairs proposed to add section 4640 to title 16 of the California Code of Regulations. This section establishes client notification requirements for Bureau licensees.

DECISION

On October 7, 2016, the Office of Administrative Law (OAL) notified the Bureau of the disapproval of this regulatory action. The reasons for the disapproval were failure to comply with the "clarity" and "necessity" standards of Government Code section 11349.1, and failure to follow procedures set forth in Government Code sections 11346.8 and 11346.9.

DISCUSSION

Regulations adopted by the Bureau must generally be adopted pursuant to the rulemaking provisions of the California Administrative Procedure Act (APA), chapter 3.5 of part 1 of division 3 of title 2 of the Government Code (sections 11340-11361). Pursuant to section 11346 of the Government Code, any regulatory action a state agency adopts through the exercise of quasi-legislative power delegated to the agency by statute is subject to the requirements of the APA, unless a statute expressly exempts or excludes the regulation from compliance with the APA. No exemption or exclusion applies to the present regulatory action under review. Consequently, before these regulations may become effective, the regulations and rulemaking record must be reviewed by OAL for compliance with the substantive standards and procedural requirements of the APA, in accordance with Government Code section 11349.1.

A. CLARITY

OAL must review regulations for compliance with the "clarity" standard of the APA, as required by Government Code section 11349.1. Government Code section 11349, subdivision (c), defines "clarity" as meaning "...written or displayed so that the meaning of regulations will be easily understood by those persons directly affected by them."

The "clarity" standard is further defined in section 16 of title 1 of the California Code of Regulations (CCR), OAL's regulation on "clarity," which provides the following:

> In examining a regulation for compliance with the "clarity" requirement of Government Code section 11349.1, OAL shall apply the following standards and presumptions:
>
> (a) A regulation shall be presumed not to comply with the "clarity" standard if any of the following conditions exists:
>
> (1) the regulation can, on its face, be reasonably and logically interpreted to have more than one meaning; or
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> (2) the language of the regulation conflicts with the agency's description of the effect of the regulation; or
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> (3) the regulation uses terms which do not have meanings generally familiar to those "directly affected" by the regulation, and those terms are defined neither in the regulation nor in the governing statute; or
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> (4) the regulation uses language incorrectly. This includes, but is not limited to, incorrect spelling, grammar or punctuation; or
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> (5) the regulation presents information in a format that is not readily understandable by persons "directly affected;" or
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> (6) the regulation does not use citation styles which clearly identify published material cited in the regulation.
>
> (b) Persons shall be presumed to be "directly affected" if they:
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> (1) are legally required to comply with the regulation; or
>
> (2) are legally required to enforce the regulation; or
>
> (3) derive from the enforcement of the regulation a benefit that is not common to the public in general; or

(4) incur from the enforcement of the regulation a detriment that is not common to the public in general.

In this "Client Notification" rulemaking, there are three instances in which proposed section 4640 fails to comply with the "clarity" standard.

1. The opening paragraph of proposed Section 4640 reads, in part:

> "Every licensed Professional Fiduciary shall at all times provide notice reasonably calculated to be received by the licensee's current ***and prospective*** clients, of the fact that the licensee is licensed by the Professional Fiduciaries Bureau, as set forth in subdivisions (a), (b), and (c) below. [...] Notice shall be provided to all current ***and prospective clients by all of the following methods***[.]" [Emphasis added.]

Pursuant to Government Code section 11349, subdivision (c), and section 16(a)(1) of title 1 of the CCR, proposed regulatory language must be patently clear and unambiguous to a reasonable, directly affected reader. Based on a plain reading of the opening paragraph, it is unclear what the Bureau meant by "prospective client." At what point does a person become prospective? A clear, unambiguous definition of this term is especially important if licensees may be subject to penalties for failure to provide the required notice to all customers who the Bureau considers to be prospective.

2. Proposed section 4640, subdivision (b), states:

> "Licensees shall provide a written notice as described in subsection (a) to all parties as described in subdivisions (1), (2), (3), and (4) of this subsection. Notice can be provided in person, by email, by mail, or by facsimile. If notice is provided in person, licensee shall maintain dated copies, signed by all required parties in the client file. If notice is provided by email, licensee shall maintain a copy of email confirming notice was sent. ***If notice is provided by mail, licensee shall maintain proof of mailing, including proof of service in accordance with California Code of Civil Procedure 1013(a), registered mail or certified mail.*** If notice is provided by facsimile, licensee shall maintain a copy of notice and facsimile confirmation in client file. **Dated copies of the written notice shall be kept in the case file as proof of mailing** and provided to the following parties in at least 14-point Arial font:" [Emphases added.]

In addition to the requirement that proposed regulatory language be patently clear and unambiguous, section 16(a)(4) of title 1 of the CCR requires language to be used correctly. Incorrect use of language includes, but is not limited to, incorrect spelling, grammar or punctuation. The italicized portion of subdivision (b) is unclear because the sentence is not grammatically sound. Is it unclear whether the Bureau is defining "proof of mailing" as "proof of service," or if proof of mailing must also include a separate proof of service. Further, based

on a reading of both statutes, it appears to OAL that the Bureau meant to cite California Code of Civil Procedure section 1013a, not 1013(a). Section 1013(a) does not specifically include a requirement or explanation of "proof of service." Ultimately, the poor syntax that renders this provision ambiguous and unclear must be remedied.

3. The requirement that dated copies of the notice be kept by a licensee as proof of mailing, underlined in subdivision (b), presents a number of clarity issues. First, this provision requires dated copies to be kept as proof of mailing, though it is clear from the rest of subdivision (b) that notice may be provided in a variety of ways other than by mail. However, even if the Bureau meant proof of service instead of proof of mailing, this provision would still conflict with some of the other requirements in subdivision (b). Only when notice is provided in person or by fax does subdivision (b) require dated copies of the notice itself to be maintained. Otherwise, subdivision (b) apparently requires only the proof of service (e.g., email confirmation, registered mail receipt, etc.) to be maintained in the client file, not the notice itself. It is unclear to the directly affected reader which documents must be maintained in each provided scenario. These ambiguities must be resolved in order for subdivision (b) to meet the "clarity" standard.

B. NECESSITY

OAL must review regulations for compliance with the "necessity" standard of Government Code section 11349.1. Government Code section 11349, subdivision (a), defines "necessity" as meaning "...the record of the rulemaking proceeding demonstrates by substantial evidence the need for a regulation to effectuate the purpose of the statute, court decision, or other provision of law that the regulation implements, interprets, or makes specific, taking into account the totality of the record. For purposes of this standard, evidence includes, but is not limited to, facts, studies, and expert opinion."

To further explain the meaning of substantial evidence in the context of the "necessity" standard, subdivision (b) of section 10 of title 1 of the CCR provides:

> In order to meet the "necessity" standard of Government Code section 11349.1, the record of the rulemaking proceeding shall include:
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> (1) a statement of the specific purpose of each adoption, amendment, or repeal; and
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> (2) information explaining why each provision of the adopted regulation is required to carry out the described purpose of the provision. Such information shall include, but is not limited to, facts, studies, or expert opinion. When the explanation is based upon policies, conclusions, speculation, or conjecture, the rulemaking record must include, in addition, supporting facts, studies, expert opinion, or other information. An "expert"

> within the meaning of this section is a person who possesses special skill or knowledge by reason of study or experience which is relevant to the regulation in question.

The evidence of necessity provided in the rulemaking record for this regulatory action is inadequate. Documents in the record either include general statements of motivation behind the action instead of specific evidence to justify the need for each regulatory provision, or simply describe "what" the regulations do instead of "why" they are needed. The record fails to provide the public with the rationale for the determinations by the Bureau as to why the specific regulatory changes are needed to carry out the purpose for which they are proposed. This vital information should have been made available to the public during the rulemaking process so that the public is informed of the basis of the proposed action and can comment knowledgably during the public comment period.

The following examples demonstrate the types of necessity issues to be addressed by the Bureau prior to its resubmission of this regulatory action. However, all of the regulatory provisions in this action need to be supported by adequate necessity and will have to be resolved prior to approval by OAL.

For reference, the primary statute being implemented, interpreted, and/or made specific by proposed section 4640 is section 138 of the Business and Professions Code, which states, in relevant part:

> Every board in the department, as defined in Section 22, shall initiate the process of adopting regulations on or before June 30, 1999, to require its licentiates, as defined in Section 23.8, to provide notice to their clients or customers that the practitioner is licensed by this state.

1. The Bureau did not explain in the record why the opening paragraph of section 4640 broadens the language of the statute from "clients" to "current and prospective clients."

2. The Bureau did not explain in the record why subdivision (b) of section 4640 requires licensees to obtain signed, dated copies of the notice when provided to clients in person.

3. The Bureau did not explain in the record why subdivision (b) of section 4640 requires licensees to retain either written notice or proof of transmission of the notice, or both, nor why these records must apparently be retained in perpetuity.

4. Though subdivisions (b)(1)-(b)(4) were added in response to a public comment, the Bureau did not explain in the record why it was reasonably necessary to draft these provisions in their respective ways. For example, if Business and Professions Code section 138 only requires notice to be provided to clients, why does proposed section 4640, subdivision (b)(2), require a licensee

serving as conservator to provide notice to all parties referred to in Probate Code section 1822(b) as well as any attorney for the conservatee? Are all of these parties "clients" according to the Bureau?

In order to meet the "necessity" standard, the rulemaking record must include substantial evidence demonstrating why the Bureau needed to modify the text in the ways described above and the evidence then needs to be made available to the public pursuant to Government Code section 11347.1.

C. INCORRECT PROCEDURE – SUMMARY & RESPONSE TO PUBLIC COMMENT

Pursuant to Government Code section 11346.9, subdivision (a)(3), the Final Statement of Reasons (FSOR) of the rulemaking record must contain:

> A summary of each objection or recommendation made regarding the specific adoption, amendment, or repeal proposed, together with an explanation of how the proposed action has been changed to accommodate each objection or recommendation, or the reasons for making no change. This requirement applies only to objections or recommendations specifically directed at the agency's proposed action or to the procedures followed by the agency in proposing or adopting the action.

When an agency makes substantial but sufficiently-related changes to its original regulatory proposal and provides notice of the changes pursuant to Government Code section 11346.8, subdivision (c), that statutory provision specifically requires:

> Any written comments received regarding the change must be responded to in the final statement of reasons required by [Government Code] section 11346.9.

In this rulemaking action, the Bureau received several written public comments during two comment periods. The Bureau adequately summarized and responded to most of these comments, but not all. The public comments that did not receive adequate summaries and/or responses are identified below:

1. The Professional Fiduciary Association of California (PFAC) provided written and oral comments recommending changes to the first version of subdivision (b) of section 4640 (made publically available for 45 days), which generally required written notice to be signed by clients regardless of the type of service. PFAC said that this requirement "is not required by Section 138 of the Business and Professions Code, would place an onerous burden on licensees, and is not supported by facts demonstrating consumer harm." The Bureau's response says, "The Bureau partially accepts this comment," and goes on to describe how subdivision (b) was modified.

There is no indication of which parts of the comment the Bureau partially rejected, or which parts were specifically being addressed by the changes to subdivision (b).

2. Similar to PFAC's complaint regarding the 45-day version of subdivision (b) of section 4640, M. Lorenz commented that, "In twelve years as a professional fiduciary, who has hired dozens and dozens of professionals, I have never received a separate letter from a vendor asking me to verify that I know he or she is licensed, with the requirement that I sign such document and return it for the vendors [sic] records." The Bureau did not respond to this comment.

3. M. Lorenz also commented about a perceived inconsistency between the proposed regulations and existing rules for other licensees. Again, the response provided in the FSOR begins, "The Bureau partially accepts this comment." The response goes on to describe specific changes to subdivision (b) of section 4640, but it is unclear which parts of the comment were rejected and which parts were specifically being address by the proposed text modifications.

4. PFAC commented on proposed text modifications during the 15-day comment period. Regarding subdivision (a) of section 4640, PFAC stated that the requirement to prominently display notice at a licensee's place of business places an unreasonable burden on licensees who do not have a business location open to the public. The Bureau did not respond to this comment.

The Bureau must update the FSOR to include adequate summaries and responses to each of the above comments pursuant to Government Code section 11346.9, subdivision (a)(3).

D. INCORRECT PROCEDURE – SUBSTANTIVE CHANGES WITHOUT NOTICE

Government Code section 11346.8, subdivision (c), states, in part:

> No state agency may adopt, amend, or repeal a regulation which has been changed from that which was originally made available to the public pursuant to Section 11346.5, unless the change is (1) ***nonsubstantial*** or solely grammatical in nature, or (2) 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. If a sufficiently related change is made, the full text of the resulting adoption, amendment, or repeal, with the change clearly indicated, shall be made available to the public for at least 15 days before the agency adopts, amends, or repeals the resulting regulation. [Emphasis added.]

Section 42 of title 1 of the CCR defines nonsubstantial changes as those that "clarify without materially altering the requirements, rights, responsibilities, conditions, or prescriptions contained in the original text."

In response to a comment received during the 15-day notice period, the Bureau reduced the required minimum font size in subdivision (a) of proposed section 4640 from 48-point to 36-point. The FSOR in the record states: "Subsection (a) was changed from 48 point font to 36 point font. 48 point font was an unreasonably large sized font and would create an unreasonably large sized document for licensees to post." The Bureau further describes the change as "non-substantive."

As the Bureau's response to the comment implies, 48-point font size was unreasonable, not unclear. The Bureau materially altered the requirement from 48-point to 36-point font size in order to make the mandate more reasonable. The modified text containing this change must be made publically available for comment for at least 15 days pursuant to Government Code section 11346.8, subdivision (c).

CONCLUSION

For the reasons set forth above, OAL disapproved this regulatory action. Pursuant to Government Code section 11349.4, subdivision (a), the Bureau may resubmit this rulemaking action within 120 days of its receipt of this Decision of Disapproval.

Any changes made to the regulation text to address the clarity and procedural issues discussed above must be made available for at least 15 days for public comment pursuant to Government Code section 11346.8 and section 44 of title 1 of the CCR. The Bureau must resolve all other issues raised in this Decision of Disapproval before resubmitting to OAL.

If you have any questions, please contact me at (916) 322-3761.

Date: October 13, 2016

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