

OFFICE OF THE SECURITIES COMMISSIONER OF KANSAS

Amendment of K.A.R. 81-14-9 and Adoption of K.A.R. 81-14-11

Summary of proposed amendment and adoption of regulations:

- **K.A.R. 81-14-9** currently specifies requirements for registered investment advisers (IAs) that have custody of client funds or securities, or IAs that have discretionary authority over client funds or securities.
- Agency staff determined that several of the requirements do not effectively or significantly provide for such protection. Therefore, most of the amendments to the regulation are to delete requirements deemed unnecessary in relation to sufficient other protections in K.A.R. 81-14-9 and other regulations.
- Only 15 of the 209 IA firms currently registered in Kansas maintain custody of client funds or securities. For those 15 firms, the remaining safekeeping provisions and other requirements under K.A.R. 81-14-9, as amended, are deemed sufficient for protection of client funds and securities.
- The unnecessary requirements have already been eliminated by issuance of special orders as authorized under the Kansas Uniform Securities Act (KUSA). Special orders issued on May 21, 2012 and November 7, 2012 waived the following requirements for IAs registered or required to be registered under KUSA:
 - surety bond requirements specified under K.A.R. 81-14-9(e);
 - a notice of fee deduction required by K.A.R. 81-14-9(b)(1)(F);
 - an audited balance sheet required by K.A.R. 81-14-9(c)(1); and
 - minimum adjusted net worth required by K.A.R. 81-14-9(d).

The waivers by special orders remain in effect until amendments to K.A.R. 81-14-9 are adopted. The amendments to K.A.R. 81-14-9 will permanently eliminate the requirements listed above.

- **K.A.R. 81-14-11** is intended to encourage more investment activity in Kansas by exempting certain IAs who manage a limited number of private investment funds or portfolios of individual Kansas investors from the registration and other regulatory requirements under KUSA.

- The adoption of K.A.R. 81-14-11 will make permanent the temporary exemptions that were implemented by special orders issued March 29, 2012 and July 19, 2011 for consistency with and extension of a similar exemption under former section 203(b)(3) of the federal Investment Advisers Act of 1940 that was repealed by the Dodd-Frank Act.
- Continuation of the exemption authorized by special order will enable Kansas-based private IAs to operate without duplicative regulatory oversight or regulation deemed unnecessary by the Office of the Securities Commissioner of Kansas.
- IAs that were previously exempt from federal registration with the Securities and Exchange Commission (SEC) and which now are required to either register or file a notice as an exempt reporting adviser with the SEC when they manage assets in excess of \$25 million can continue to be exempt from registration and other regulatory requirements in Kansas if they comply with all requirements and conditions of proposed K.A.R. 81-14-11.
- Individual IA representatives employed by exempt IA firms can also be exempt from registration with the Office of the Securities Commissioner of Kansas if they meet conditions specified by the proposed K.A.R. 81-14-11.
- The exemption provided by proposed K.A.R. 81-14-11 requires a private IA to:
 - maintain its principal place of business in Kansas;
 - provide investment advice solely to fewer than 15 clients;
 - not hold out generally to the public as an investment adviser;
 - not act as an investment adviser to any investment company registered under the federal Investment Company Act of 1940 (the 1940 act) or a company that has elected and not withdrawn its election to be a Business Development Company under the 1940 act; and
 - not be, nor any of its advisory affiliates or representatives, subject to a disqualification provision as described in SEC Rule 262 under federal Regulation A.

Federal mandate considerations and comparison with similar federal law:

The amendments to K.A.R. 81-14-9 and adoption of new K.A.R. 81-14-11 are not mandated by federal law and the provisions of the regulations do not exceed

requirements of applicable federal law. In fact, the exemption from registration in Kansas provided by K.A.R. 81-14-11 reflects reduced requirements for private advisers based in Kansas as compared to federal securities laws. Private IAs with more than \$25 million of assets under management are required to either register with the SEC or file with the SEC as an exempt reporting adviser.

Anticipated economic impacts:

- For **K.A.R. 81-14-9**, the primary economic impact of the proposed amendments will be reduced costs for registered IAs doing business in Kansas, although it is not possible to accurately estimate the amount of cost savings for registered IAs.
- There will be no material fiscal impacts on the operations of the Office of the Securities Commissioner of Kansas or any other Kansas agencies.
- No adverse economic impact on the general public in Kansas is expected due to the proposed reduction in regulatory requirements for IAs registered in Kansas.
- For **K.A.R. 81-14-11**, the primary economic impact is for IAs that claim and comply with the exemption provided by the regulation to avoid the significant costs of registration and other regulatory requirements for registered IAs and representatives under KUSA.
- There will be no material fiscal impacts on the operations of the Office of the Securities Commissioner of Kansas or any other Kansas agencies. The amount of registration fees not received by the Office of the Securities Commissioner from exempt IAs and representatives at \$100 per firm and \$55 per individual each fiscal year cannot be estimated but is most likely immaterial in relation to total agency revenues.
- No material adverse economic impact on the general public in Kansas is expected due to the continued exemption of private advisers.
- The exemption may attract private advisers to locate in Kansas and possibly enhance economic benefits for private clients in Kansas communities; however, it is not possible to estimate the amount of such potential benefits.