ARNOLD SCHWARZENEGGER, GOVERNOR

OFFICE OF ADMINISTRATIVE LAW

California Regulatory Notice Register

REGISTER 2010, NO. 24–Z PUBLISHED WEEKLY BY THE OFFICE OF ADMINISTRATIVE LAW JUNE 11, 2010

PROPOSED ACTION ON REGULATIONS

GENERAL PUBLIC INTEREST

PROPOSITION 65

(Continued on next page)

Time-Dated Material

OAL REGULATORY DETERMINATIONS

ACCEPTANCE OF PETITION TO REVIEW ALLEGED UNDERGROUND REGULATIONS

SUMMARY OF REGULATORY ACTIONS

The *California Regulatory Notice Register* is an official state publication of the Office of Administrative Law containing notices of proposed regulatory actions by state regulatory agencies to adopt, amend or repeal regulations contained in the California Code of Regulations. The effective period of a notice of proposed regulatory action by a state agency in the *California Regulatory Notice Register* shall not exceed one year [Government Code § 11346.4(b)]. It is suggested, therefore, that issues of the *California Regulatory Notice Register* be retained for a minimum of 18 months.

CALIFORNIA REGULATORY NOTICE REGISTER (USPS 002–931), (ISSN 1041-2654) is published weekly by the Office of Administrative Law, 300 Capitol Mall, Suite 1250, Sacramento, CA 95814-4339. The Register is printed by Barclays, a subsidiary of West, a Thomson Reuters Business, and is offered by subscription for $205.00 (annual price). To order or make changes to current subscriptions, please call (800) 888-3600. "Periodicals Postage Paid in Saint Paul, MN." **POSTMASTER:** Send address changes to the: CALIFORNIA REGULATORY NOTICE REGISTER, Barclays, a subsidiary of West, a Thomson Reuters Business, P.O. Box 2006, San Francisco, CA 94126. The Register can also be accessed at **http://www.oal.ca.gov.**

When Implementing the 5% Redirection Plan, the changes identified in the 3% Plan will remain in effect and will also include the following:

- During the 5% Redirection Plan, Central Facility Unit I and Unit III custody staff (gate officers) will rotate within their respective units to conduct necessary releases, i.e. Education, Textiles. For example, this rotation will require a staff member from E–Wing to report to F–Wing to assist in controlled releases.
- Central Facility Unit I and Unit III counseling staff will assist with PIA (Textiles) and Work Assignment releases if deemed necessary. This option would not be feasible if the East Dorm was deactivated.

If you have any questions regarding the attached plans, please contact me at (831) 678–5951.

/s/
RANDY GROUNDS
Warden (A)

ACCEPTANCE OF PETITION TO REVIEW ALLEGED UNDERGROUND REGULATIONS

OFFICE OF ADMINISTRATIVE LAW

ACCEPTANCE OF PETITION TO REVIEW ALLEGED UNDERGROUND REGULATIONS

(Pursuant to title 1, section 270, of the California Code of Regulations)

The Office of Administrative Law has accepted the following petition for consideration. Please send your comments to:

Kathleen Eddy, Senior Counsel
Office of Administrative Law
300 Capitol Mall, Ste. 1250
Sacramento, CA 95814

A copy of your comment must also be sent to the petitioner and the agency contact person.

Petitioner:

William Gausewitz
Michelman & Robinson, LLP
915 L Street, Ste. 1110
Sacramento, CA 95814

Agency contact:

Steve Poizner, Insurance Commissioner
300 Capitol Mall, 17th Floor
Sacramento, CA 95814

Please note the following timelines:

Publication of Petition in California Regulatory Notice Register: June 11, 2010
Deadline for Public Comment: July 12, 2010
Deadline for Agency Response: July 26, 2010
Deadline for Petitioner Rebuttal: No later than 15 days after receipt of the agency's response
Deadline for OAL Decision: October 11, 2010

The attachments are not being printed for practical reasons or space considerations. However, if you would like to view the attachments please contact Margaret Molina at (916) 324–6044 or mmolina@oal.ca.gov.

DEPARTMENT OF INSURANCE

SANFORD L. MICHELMAN, Bar No. 179702
JOHN A. SEBASTINELLI, Bar No. 127859
WILLIAM L. GAUSEWITZ, Bar No. 91524
MICHELMAN & ROBINSON, LLP
915 L Street, Suite 1110
Sacramento, California 95814
Tel: (916) 447–4044; Fax: (916) 405–3404
BGausewitz@mrllp.com

CALIFORNIA OFFICE OF ADMINISTRATIVE LAW

CALIFORNIA DEPARTMENT OF INSURANCE

COMMUNICATIONS TO INSURERS DATED FEBRUARY 10, 2010, AND MARCH 4, 2010.

PETITION FOR DETERMINATION PURSUANT TO CALIFORNIA GOVERNMENT CODE §11340.5

1) INTRODUCTION. The Petitioner has been retained by and is acting on behalf of the American Council of Life Insurers (ACLI), the American Insurance Association (AIA), the Association of California Insurance Companies (ACIC), the Association of California Life and Health Insurance Companies (ACLHIC), and the Personal Insurance Federation of California (PIFC). This petition is submitted to the Office of Administrative Law (OAL) requesting a determination pursuant to

California Government Code § 11340.5[1] of whether the above–captioned communications contain underground regulations as defined by title 10, Cal Code Regs § 250(a)[2]. These communications designate certain companies as "doing business with the Iranian oil and natural gas, nuclear, and defense sectors", they require each California–licensed insurer to submit a statement to the California Department of Insurance (Department) stating its future intentions regarding investment in the designated companies, and they require all insurers to report investments in those companies as non–admitted assets on their quarterly and annual statements. These requirements in the communications are illegal underground regulations.

An underground regulation is invalid and unenforceable[3]. By issuing these underground regulations, the Department is attempting to implement regulations which are void, and therefore unenforceable. If the Department wishes to implement the rules that it is attempting to impose through these underground regulations it must do so within the scope of its statutory authority pursuant to section 11342.1 of the Government Code[4] and it must comply with the other procedural and substantive requirements of the California Administrative Procedure Act (APA), found in California Government Code sections 11340 *et seq*.

This petition does not ask OAL to determine whether or not the Department actually has authority to issue the challenged underground regulations. Such a determination is beyond the scope of a petition pursuant to Gov. Code § 11340.5. An evaluation of the scope of the Department's authority should occur in the course of formal APA rulemaking. The Department has never identified specific statutes which might authorize these actions, as it would be required to do in formal APA rulemaking. By issuing these rules as underground regulations, without going through formal APA rulemaking, the Department has avoided any scrutiny regarding its legal power, or lack thereof, to impose these requirements. Only by requiring the Department to obey the APA may its authority, or its lack of authority, be revealed.

The Department's authority is certainly not unlimited. An earlier attempt by the Department to regulate in the area of foreign affairs was invalidated by the United States Supreme Court, which found that federal law preempted state law in the matter under review (*American Insurance Association v. Garamendi*, 539 U.S. 396; 123 S. Ct. 2374; 156 L. Ed. 2d 376 (2003)). Since we know that the Department's authority is not unlimited, it is important to subject these rules to formal APA rulemaking so that this issue may be examined. The Department should not be permitted to avoid this review by issuing these rules as underground regulations. An OAL determination on this issue is therefore the first step in evaluating the underlying legality of the rules themselves.

2) THE PURPORTED UNDERGROUND REGULATIONS. On February 10, 2010, the Department distributed three documents related to insurer investments in business entities that the Department believes conduct business in Iran. These three documents comprise:

A) A form letter directed to insurers with the subject "Identification of Companies Doing Business in Specified Iranian Economic Sectors; Treatment of Investments in Such Companies on Insurers' Financial Statements; Request for Moratorium on Future Iran–Related Investments". A copy of that letter is attached to this petition as Exhibit A.

B) A list entitled "List Of Companies Doing Business With The Iranian Petroleum/Natural Gas, Nuclear, And Defense Sectors (As Of February 9, 2010)". A copy of that list is attached to this petition as Exhibit B.

---

[1] Section 11340.5 provides in pertinent part "(a) No state agency shall issue, utilize, enforce, or attempt to enforce any guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule, which is a regulation as defined in Section 11342.600, unless the guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule has been adopted as a regulation and filed with the Secretary of State pursuant to this chapter. ¶ (b) If the office [OAL] is notified of, or on its own, learns of the issuance, enforcement of, or use of, an agency guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule that has not been adopted as a regulation and filed with the Secretary of State pursuant to this chapter, the office may issue a determination as to whether the guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule, is a regulation as defined in Section 11342.600."

[2] Title 10, Cal Code Regs 250(a) " 'Underground regulation' means any guideline, criterion, bulletin, manual, instruction, order, standard of general application, or other rule, including a rule governing a state agency procedure, that is a regulation as defined in Section 11342.600 of the Government Code, but has not been adopted as a regulation and filed with the Secretary of State pursuant to the AP A and is not subject to an express statutory exemption from adoption pursuant to the APA."

[3] A "regulation or order of repeal may be declared to be invalid for a substantial failure to comply with [the rulemaking chapter of the APA]" Cal Gov Code § 11350.

"[W}e conclude that DLSE's policy for determining whether to apply IWC wage orders to maritime employees constitutes a regulation and is void for failure to comply with the APA." *Tidewater Marine Western, Inc. v. Bradshaw*, 14 Cal. 4th 557, 576 (Cal. 1996)

[4] The pertinent part of Cal Gov Code § 11342.1 provides that "Each regulation adopted, to be effective, shall be within the scope of authority conferred and in accordance with standards prescribed by other provisions of law."

C) A document entitled "Response Form — Insurer Agreement Not To Invest In Companies Doing Business With The Iranian Oil And Natural Gas, Nuclear, And Defense Sectors". A copy of that document is attached to this petition as Exhibit C.

On March 4, 2010 the Department distributed an email message all California licensed insurers from "CA Department of Insurance FSB" addressed to "Statutory Financial Statement Contact Person". A copy of this email message is attached to this petition as Exhibit D.

Collectively these four documents contain at least three different underground regulations in violation of section 11340.5 of the Government Code. These underground regulations are:

A) The provision of Exhibit A declaring that "effective March 31, 2010, the Department will treat all investments by insurers holding a certificate of authority to transact insurance in California in companies on the List and affiliates owned 50% or more by companies on the List as non–admitted on the insurer's financial statements. For all financial statements filed with the Department for periods ending on or after March 31, 2010, each insurer must report all of its investment holdings on the List as not admitted assets." This will be referred to in this petition as the "Non–admitted Asset Rule."

B) The Department's determination in Exhibit A that the companies listed in Exhibit B are "subject to financial risk as a result of doing business with the Iranian oil and natural gas, nuclear, and defense sectors." This will be referred to in this petition as the "Listed Company Rule."

C) The mandate imposed upon insurers, pursuant to Exhibit A, C and D, to submit a response form to the Department not later than April 2, 2010. This will be referred to in this petition as the "Mandatory Response Rule."

3) AGENCY ACTIONS DEMONSTRATING THAT THE DEPARTMENT HAS ISSUED, USED, ENFORCED, OR ATTEMPTED TO ENFORCE THE PURPORTED UNDERGROUND REGULATIONS. Exhibits A–D are, by their own terms, directives addressed to insurers and issued by the Department. They are manifestly documents demonstrating, at the least, that the Department has issued the purported underground regulations. The letter of February 10 is signed by the General Counsel of the Department. The March 4 email was sent from the Department's Financial Surveillance Branch. Individual insurers have reported to the Petitioner that they have received these documents from the Department of Insurance, delivered by the U.S. Postal Service.

Also, the Department has publicly announced that it is taking the actions indicated in the documents. On February 10, 2010 the Department issued a press release on this subject. The lead paragraph of this press release says the following:

> California Insurance Commissioner Steve Poizner today released a list of 50 companies doing business in the Iranian oil and natural gas, nuclear and defense sectors and announced that as of March 31, 2010, no investments that an insurer holds in any of those companies will be recognized on its financial statements in California.

The Department's February 10 press release also makes reference to "the Department's form which all insurers must complete and return to the Department by March 12, 2010." These references in the Department's February 10 press release clearly demonstrate that the Department has issued the challenged underground regulations. A copy of the Department's February 10 press release on this topic is attached to this petition as Exhibit E. This copy of the press release was downloaded from the Department's web site at http://www.insurance.ca.gov/0400–news/0100–press–releases/2010/release021–10.cfm.

On March 26, 2010 the Department issued another press release discussing the "progress" in the Department's "initiative" regarding Iran. The fact that the Department is reporting progress on this initiative clearly demonstrates that the Department has issued, used enforced or attempted to enforce the purported underground regulations. The Department's March 26 press release is available on its web site at http://www.insurance.ca.gov/0400–news/0100–press–releases/2010/release045–10.cfm. A copy of the March 26, 2010 press release downloaded from this web site is attached to this petition as Exhibit F.

4) THE LEGAL BASIS FOR BELIEVING THAT THE ALLEGED UNDERGROUND REGULATIONS ARE REGULATIONS AS DEFINED IN SECTION 11342.600 OF THE GOVERNMENT CODE AND THAT NO EXPRESS STATUTORY EXEMPTION TO THE REQUIREMENTS OF THE APA IS APPLICABLE.

4a) The challenged underground regulations satisfy the legal definition of "regulation" and are not exempt from APA requirements. The APA defines a regulation as "every rule, regulation, order, or standard of general application or the amendment, supplement, or revision of any rule, regulation, order, or standard adopted by any state agency to implement, interpret, or make specific the law enforced or administered by it, or to govern its procedure" (Cal Gov Code § 11342.600). The California Supreme Court has refined this definition as follows:

> A regulation subject to the APA thus has two principal identifying characteristics. (See *Union of American Physicians & Dentists v. Kizer* (1990) 223 Cal. App. 3d 490, 497 [272 Cal. Rptr. 886] [describing two–part test of the Office of Administrative Law].) First, the agency must intend its rule to apply generally, rather than in a specific case. The rule need not, however, apply universally; a rule applies generally so long as it declares how a certain class of cases will be decided (*Roth v. Department of Veterans Affairs* (1980) 110 Cal. App. 3d 622, 630 [167 Cal. Rptr. 552].) Second, the rule must "implement, interpret, or make specific the law enforced or administered by [the agency], or . . . govern [the agency's] procedure" (Gov. Code, § 11342, subd. (g).) *Tidewater Marine Western, Inc. v. Bradshaw*, 14 Cal. 4th 557, 571 (Cal. 1996)

In order to conclude that the purported underground regulations satisfy the legal standard, therefore, it must be demonstrated that each of them is intended to apply generally and that each implements, interprets or makes specific a more general law. Each of the challenged underground regulations meets these standards.

A third requirement of Gov. Code § 11340.5 is that the challenged regulation must not be exempt from APA rulemaking requirements. Pursuant to Gov. Code § 11346, any law exempting a regulation from APA rulemaking requirements "must do so expressly." The challenged underground regulations, therefore, are required to be adopted pursuant to APA rulemaking requirements unless they are subject to an express statutory exemption from those requirements. They are not.

4b) The Non–admitted Asset Rule. The Non–admitted Asset Rule is stated in Exhibit A as follows:

> [E]ffective March 31, 2010, the Department will treat all investments by insurers holding a certificate of authority to transact insurance in California in companies on the List and affiliates owned 50% or more by companies on the List as non–admitted on the insurer's financial statements. For all financial statements filed with the Department for periods ending on or after March 31, 2010, each insurer must report all of its investment holdings on the list as not admitted assets.

This rule explicitly applies to "all investments by insurers holding a certificate of authority". Since an insurer is prohibited by law from transacting insurance in the state of California if it doesn't hold a California certificate of authority[5], the Non–admitted Asset Rule, if valid, applies to every insurer permitted by law to operate in the state of California.

Furthermore, the Non–admitted Asset Rule would apply to all investments equally. It does not distinguish, for example, between equity investments and debt investments, even though these two different types of investments are subject to very different types and degrees of financial risk. This is clearly a "rule, regulation, order, or standard of general application" within the meaning of section 11342.600 of the APA.

The reporting requirement in the Non–admitted Asset Rule is similarly imposed upon "each insurer". The rule provides no case–by–case review for individual insurers, nor does it provide any mechanism for individual insurers to appeal the designation of its assets as non–admitted assets. Both with respect to the requirement that listed assets are considered to be non–admitted by the Department and the requirement that they be reported that way by insurers, the Non–admitted Asset Rule is a rule of general application.

The Department has not identified any statutory authority for the Non–admitted Asset Rule. Therefore, any discussion of whether it implements, interprets, or makes specific the law enforced or administered by it must first speculate upon what law the Department might assert if it were to identify its purported legal authority. If the underground regulations were subjected to the APA rulemaking procedure, the Department might say that it is implementing a federal law that regulates commerce with Iran, or it might assert that it is implementing Ins. Code § 900. But because this is an underground regulation for which the Department has cited no authority, a rigorous analysis of whether the rule implements "the law enforced or administered by the" Department cannot be made based upon available information.

Fortunately, such an analysis is not truly necessary. If the Department does have some statutory authority for the challenged underground regulations, the specificity of the purported underground regulations makes it clear that they "implement, interpret, or make specific" that hypothetical authority and, thus, satisfy the APA definition of "regulation". Alternatively, if there is no statutory authority that the challenged underground regulation implements, interprets, or makes specific, then the rule violates section 11342.1 of the APA. Only by subjecting these underground regulations to the rulemaking requirements of the APA may the authority question be resolved. But whatever authority the Department believes it has, it is beyond any question that the purported underground regulations attempt to implement it and make it specific.

There is no apparent express exemption permitting adoption of Non–admitted Asset Rule without complying with the rulemaking requirements of the APA. Section 900 of the Insurance Code requires insurers to file

[5] California Insurance Code section 700.

annual and quarterly financial statements "in the number, form, and by the methods prescribed by the commissioner." While this statute gives the Department an element of discretion regarding the manner of insurer filing of financial statements, it does not give any apparent authority to regulate the content of financial statements, as the Non–admitted Asset Rule purports to do. More importantly, it certainly does not amount to an express exemption from the rulemaking requirements of the APA. Even if this section authorizes the Department to regulate the content of financial statements, such regulation must be done pursuant to the rulemaking requirements of the APA. An express exemption must state explicitly that regulations may be adopted without complying with the requirements of the APA. Insurance Code section 900 does not provide such an express exemption.

There are no other express exemptions from the APA that permit the Non–admitted Asset Rule to be adopted without APA compliance. The general exemptions of Government Code § 11340.9 are not applicable. The Department has not identified any statutory authority pursuant to which it has promulgated the Non–admitted Asset Rule. Without the identification of authority and reference statutes it is difficult to demonstrate the non–existence of an express exemption definitively. The Petitioner is a California lawyer familiar with both the APA and the Insurance Code who knows of no express statutory exemption and who asserts that no such express exemption exists. A claim that this rule is subject to an express exemption amounts to an affirmative defense to the general rule that a regulation must be adopted pursuant to APA rulemaking. Therefore, the burden is on the Department to demonstrate that this rule is exempt from APA rulemaking requirements if that is the case. Rather than presuming that this purported underground regulation is expressly exempt from APA rulemaking, OAL should accept this petition and offer the Department the opportunity to defend the regulation on that basis, should it choose to do so.

4c) The Listed Company Rule. In Exhibit A the Department says that it "has developed a list of companies doing business with the Iranian oil and natural gas, nuclear, and defense sectors ("List")." Although the Department asserts that the List was developed "[f]ollowing extensive research, analysis and consultation" and identifies four sources of information upon which the List was "based", the Department identifies no criteria upon which a company was evaluated for inclusion or exclusion from the List. The List is the result of a "black box" analytical process whereby unknown inputs are evaluated pursuant to unknown criteria and the results merely announced. There is no way that any company could evaluate its operations to determine whether it will or will not result in being included on the List.

The Listed Company Rule is therefore difficult to evaluate. Due to the black box nature of the Department's development of the rule, the universe of business entities subject to this analysis cannot be determined. For purposes of APA evaluation, however, it is clear that this is a rule of general application in at least two ways. To begin with, it is clearly applicable uniformly to all of the 50 companies on the list. Each of these companies has been identified by the Department as "doing business with the Iranian oil and natural gas, nuclear, and defense sectors." The rule is applied generally to all companies on the List.

Furthermore, the Listed Company Rule does not distinguish between which of the identified "sectors" a listed company is associated. In terms of public perception, and thus in terms of reputational risk to the listed companies, it may make a large difference whether the company is identified with the Iranian oil sector or the Iranian defense sector. For example, it may be of little importance to one of the listed oil companies to be identified with the Iranian oil industry, but of a great deal of importance to that oil company if it is identified with the Iranian defense sector. The Listed Company Rule, however, does not accommodate these different interests. Since it applies to all listed companies equally, without distinguishing which of the listed "sectors" the companies are "doing business with", it is a rule of general application.

In addition, the rule is generally applicable to all California insurers. By virtue of a company being included on the List, all insurers are required by the Department to treat investments (of whatever form) in that company differently from any investments in companies not on the List. In this manner also the Listed Company Rule is applied generally in California. It is a standard of general application.

The Listed Company Rule, like the Non–admitted Asset Rule, cannot be evaluated as an implementation of any specific statute since no statutory authority has been identified by the Department authorizing the rule. Again, the Department may assert that it is implementing Ins. Code section 900, federal law governing commerce with Iran, or some other statute, but that cannot be determined from available information. But as with the Non–admitted Asset Rule, the Department is either making statutory law specific, thus bringing this rule within the APA definition of "regulation", or it is implementing a rule for which it lacks authority in violation of section 11342.1 of the APA. If there is statutory authority for the Listed Company Rule, it is a rule of general application which implements and makes specific that statutory authority the Department may have in this area. It is a regulation as defined by the APA.

As with the Non–admitted Asset Rule, there is no apparent express exemption permitting adoption of Listed

Company Rule without complying with the rulemaking requirements of the APA. The general exemptions of Government Code § 11340.9 are not applicable. The Department has not identified any statutory authority pursuant to which it has promulgated the Listed Company Rule. Without the identification of specific authority and reference statutes it is difficult to demonstrate the non–existence of an express exemption definitively. The Petitioner is a California lawyer familiar with both the APA and the Insurance Code who knows of no express statutory exemption and who asserts that no such express exemption exists. The burden is on the Department to demonstrate that this rule is exempt from APA rulemaking requirements, if that is the case. Rather than presuming that this purported underground regulation is expressly exempt from APA rulemaking, OAL should accept this petition and offer the Department the opportunity to defend the regulation on that basis, should it choose to do so.

4d) The Mandatory Response Rule. Exhibit C is a form which an executive officer of each California insurer is required to complete and return to the Department. In Exhibit A the Department "requests that your company agree not to invest in the future" in companies on the List. The mandatory response form requires each company to specify its intention regarding this request. Completion and return of this form is mandatory. The form was presented to California insurers subject to the instruction, found in Exhibit A, that "[y]our company must respond by March 12, 2010." Pursuant to the email message conveyed in Exhibit D, the deadline for response was delayed until April 2, 2010, but the mandatory nature of the response was not changed.

Insurers who do not return the form to the Department would, pursuant to Exhibit A, be subject to potential sanctions. Exhibit A tells each insurer that "[i]f your company does not respond to or declines the Department's request for a moratorium on future investments . . . the Department may publish your company's name on the Department's website." Thus the Department has established a potential means to enforce the Mandatory Response Rule in the form of publicly identifying a non–compliant insurer — one that does not respond or that responds in a manner that the Department does not favor — on its website. Publication of an insurer's name under these circumstances would carry the implication that the insurer has undesirable connections with Iran and, thus, the Department's threatened sanction is that it will damage the reputations of non–compliant insurers by implicitly identifying them as collaborators with the government of Iran.

The Mandatory Response Rule applies to all California insurers. It imposes a mandatory requirement upon all of them ("[y]our company *must* respond"), and it establishes potential punishment for those insurers who do not respond or who respond in a manner that the Department disfavors. It is a rule of general application which, in order to be valid, must be adopted pursuant to the rulemaking requirements of the APA.

As with the other two challenged underground regulations, the Mandatory Response Rule clearly implements and makes specific the statutory authority, if any, of the Department. The requirement imposed by the Department to file a specific response to a specific issue is far more specific than any requirement of any California statute. If there is statutory authority for this rule, the rule itself clearly implements and makes that authority specific. Since the Mandatory Response Rule is a rule of general application which implements and makes specific whatever authority the Department may have, it is a regulation pursuant to section 11342.600 of the Government Code.

As with the other two underground regulations contained in the Department's communications, there is no apparent express exemption permitting adoption of Mandatory Response Rule without complying with the rulemaking requirements of the APA. The general exemptions of Government Code § 11340.9 are not applicable. The Department has not identified any statutory authority and reference pursuant to which it has promulgated the Mandatory Response Rule. Without the identification of authority and reference statutes it is difficult to demonstrate definitively the non–existence of an express exemption. The Petitioner is a California lawyer familiar with both the APA and the Insurance Code who knows of no express statutory exemption and who asserts that no such express exemption exists. The burden is on the Department to demonstrate that this rule is exempt from APA rulemaking requirements, if that is the case. Rather than presuming that this regulation is expressly exempt from APA rulemaking, OAL should accept this petition and offer the Department the opportunity to defend the regulation on that basis, should it choose to do so.

5) INFORMATION DEMONSTRATING THAT THE PETITION RAISES AN ISSUE OF CONSIDERABLE PUBLIC IMPORTANCE REQUIRING PROMPT RESOLUTION. There are at least three issues of considerable public importance requiring prompt resolution raised by this petition.

Issue #1: Legal Uncertainty Regarding Insurer Reporting and Reserving. The challenged underground regulations conflict with provisions of the Insurance Code and the California Code of Regulations, thus creating ambiguity regarding how insurers are to comply with the California law. Every insurer licensed to transact insurance in California is required, pursuant to California Insurance Code 900, to file annual and quarterly financial statements, which must be "completed in conformity with the Accounting Practices and

Procedures Manual adopted by the National Association of Insurance Commissioners" (Ins Code § 923). The challenged underground regulations purport to regulate the content of these financial statements in a way that is not consistent with the requirements of the Insurance Code § 923.

This is a matter of great importance. A company that files a false financial statement may lose its certificate of authority (Ins Code § 900.8). The correctness of financial statements must be certified by officers of the insurer (Ins Code § 903). The challenged underground regulations create legal uncertainty regarding the required contents of insurer financial statements and thus make it impossible for insurers to determine how to comply with the law.

If the purported underground regulations are valid an insurer reports investments in listed companies as admitted assets will violate these regulations. Conversely, if the challenged underground regulations are invalid, an insurer that prepares its financial statements in compliance with those underground regulations will violate the Insurance Code. Unless and until the validity of the challenged underground regulations is established through formal APA rulemaking, it is impossible for any insurer, no matter which choice it makes, to be certain that it is preparing its financial statements in compliance with the law.

The uncertainty created by these underground regulations is even greater for insurers licensed in California but domiciled in another state. Rather than forcing each insurer to prepare different financial statements to satisfy different reporting requirements in each state, state laws generally provide reciprocity in reporting standards. States require insurers to prepare their financial reports pursuant to the law of the state of domicile, and every state agrees to accept the financial reporting as required by the state of domicile. California imposes this requirement pursuant to regulations adopted by the Department in title 10, Cal Code Regs § 2309.5[6]. Due to the legal uncertainty created by the challenged underground regulations, insurers domiciled outside of California cannot know whether to prepare their annual financial statements in accordance with the requirements of the challenged underground regulations or the requirements of 10 CCR 2309.5 — the Department's lawfully–adopted regulation.

This uncertainty does not merely affect the contents of an insurer's financial statements. It has a significant impact in the market as well. Insurers are required to maintain adequate financial reserves to support the insurance business that it writes (Ins. Code § 923.5). Only admitted assets can be used as reserves. Thus the validity of the challenged underground regulations has a direct impact on the amount of business that an insurer may transact. In simple terms, an insurer that has investments in companies on the List may lawfully write more insurance if the challenged underground regulations are void than it may write if they are valid.

Only by requiring the Department to comply with the rulemaking requirements of the APA will the validity of the challenged rules be determined and only then will insurers be able to prepare their financial statements with the level of certainty needed to comply with the accuracy and verification requirements of the Insurance Code. Filing incorrect financial statements can potentially put an insurer's certificate of authority in jeopardy and can subject officers of insurance companies to legal exposure for falsely verifying financial statements. Resolution of these uncertainties is a matter of considerable public importance requiring prompt resolution.

Issue #2: Due Process for Listed Companies. The black box analysis employed by the Department in developing the List exposes the listed companies to potential reputational and economic harm without due process and without recourse. The Department has, through black box procedures which have never been subjected to public disclosure or evaluation, declared that the named companies are affiliated with Iran. Whether or not that is true, due process considerations dictate that companies subjected to such an evaluation should be advised of the standards by which they are being evaluated and should have a procedure for responding to that evaluation. The purported underground regulations do not allow this. This is a matter of considerable public importance requiring prompt resolution. Only by subjecting these underground regulations to the scrutiny provided by APA rulemaking can this be corrected.

Issue #3: The Scope of the Department's Legal Authority. The failure to employ the rulemaking process means that the scope of authority that the Department may have in this area of regulation has never been subjected to public scrutiny. There is a substantial legal question whether it is within the scope of the Department's statutory authority to pass judgment upon classes of insurer assets in the manner done in the challenged underground regulations or to require insurers to specify their future intentions regarding those investments.

In this case the Department has decreed generally that every listed company is deemed to be financially threatened with no apparent regard for the actual financial condition of any individual company. Whether or not the Department has the legal authority to make such

[6] Title 10, Cal Code Regs § 2309.5 "The annual audited financial report shall report the financial position of the insurer as of the end of the most recent calendar year and the results of its operations, cash flows and changes in capital and surplus for the year then ended in conformity with statutory accounting practices prescribed, or otherwise permitted, by the Department of Insurance of the state of domicile."

global determinations upon all investments in specified companies is a significant legal question with far–reaching implications. By enacting the challenged rules as illegal underground regulations the Department has avoided all scrutiny with respect to its authority. It is entirely possible that the Department is employing rules which exceed its authority in violation of section 11342.1 of the APA. Only by subjecting these rules to formal rulemaking pursuant to the APA may the Department's authority be properly evaluated.

6) CONCLUSION. The enactments by the Department reflected in Exhibits A–D constitute a significant exercise of regulatory power both over the companies which the Department has listed as being affiliated with Iran and over every insurer licensed to transact the business of insurance in California. This power has been exercised through rules of general application which have never been subjected to the scrutiny and public comment that is a central purpose of APA rulemaking. The Petitioner respectfully requests that OAL accept this petition so that the challenged regulations may be evaluated pursuant to the APA.

6) Certifications:

I certify that I have submitted copies of this petition and all attachments to the state agency which has issued, used, enforced, or attempted to enforce the purported underground regulation. The copies were submitted as follows:

Via hand delivery of a printed copy to:

Darrel Woo, Staff Counsel
300 Capital Mall, 17th Floor
Sacramento, CA 95814
(916) 492–3556

Via email in PDF format to:

Adam Cole, General Counsel
ColeA@insurance.ca.gov
(415) 538–4375

Peter Conlin, Counsel to the Commissioner
ConlinP@insurance.ca.gov
(916) 492–3199

I certify that all of the above information is true and correct to the best of my knowledge.

DATED: March 29, 2010

MICHELMAN & ROBINSON, LLP

By: WILLIAM L. GAUSEWITZ

SUMMARY OF REGULATORY ACTIONS

REGULATIONS FILED WITH SECRETARY OF STATE

This Summary of Regulatory Actions lists regulations filed with the Secretary of State on the dates indicated. Copies of the regulations may be obtained by contacting the agency or from the Secretary of State, Archives, 1020 O Street, Sacramento, CA 95814, (916) 653–7715. Please have the agency name and the date filed (see below) when making a request.

File# 2010–0419–01
BOARD OF CHIROPRACTIC EXAMINERS
Law Violators

This action makes a minor amendment to the regulation that imposes a duty upon licensees to notify the Secretary or any member of the Board if they learn of a violation of the Chiropractic Act or regulations of the Board, changing the person to be notified to the Executive Officer or a designee.

Title 16
California Code of Regulations
AMEND: 314
Filed 05/27/2010
Effective 06/26/2010
Agency Contact:
Dixie Van Allen (916) 263–5329

File# 2010–0427–09
CALIFORNIA ALTERNATIVE ENERGY AND ADVANCED TRANSPORTATION FINANCING AUTHORITY
Amend Regulations for CAEATFA's Fee Program

The Public Resources Code creates the California Alternative Energy and Advanced Financing Authority (Authority) and authorizes it to fix fees and charges for projects to fund expenses incurred by the Authority in carrying out its duties. Existing section 10020 of title 4 of the California Code of Regulations sets fees for projects generally, but there are no specific fees established for renewable energy projects. This filing is the certificate of compliance for an emergency regulatory action which added a separate fee structure to section 10020 to establish a renewable energy program and lower the cost of financing these technologies while allowing the Authority to be self sustaining. The initial filing of this regulatory action was mandated to be in the form of emergency regulations and deemed necessary for the