CORRECTED*

FINAL STATEMENT OF REASONS FOR THE ADOPTION OF RULES UNDER THE CORPORATE SECURITIES LAW OF 1968

As required by Section 11346.2 of the Government Code, the California Corporations Commissioner ("Commissioner") sets forth below the reasons for the adoption of changes to regulations under the Corporate Securities Law of 1968 (Corporations Code Section 25000, et seq., "CSL") relating to the maintenance and preservation of books and records by broker-dealers, and reports required of both broker-dealers and investment advisers, under Corporations Code Section 25241. The Commissioner is repealing Sections 260.218.5 and 260.241.1, and amending Sections 260.241 and 260.241.2 of Title 10 of the California Code of Regulations (10 C.C.R. §§ 260.218.5, 260.241, 260.241.1, and 260.241.2).

Rule 260.241 under the CSL sets forth requirements for licensed broker-dealers with respect to the making and maintaining of books and records, and Rule 260.241.1 sets forth requirements for licensed broker-dealers regarding the preservation of records.

The Commissioner is repealing the existing requirements in these rules and instead requiring that broker-dealers comply with the recordkeeping requirements in Rules 17a-3 (17 C.F.R. 240.17a-3) and 17a-4 (17 C.F.R. 240.17a-4), as well as Rules 15g-2 (17 C.F.R. 240.15g-2), 15g-4 (17 C.F.R. 240.15g-4), 15g-5 (17 C.F.R. 240.15g-5), 15g-6 (17 C.F.R. 240.15g-6), and 15c2-11 (17 C.F.R. 240.15c2-11) under the Securities Exchange Act of 1934 ("Exchange Act").

The National Securities Markets Improvement Act of 1996 (Pub. L. No. 104-290, 110 Stat. 3416 (1996), "NSMIA") prohibits state securities regulators from establishing or enforcing under their state securities laws or rules, record-keeping requirements for securities broker-dealers that are inconsistent with, or not required by, the U.S. Securities and Exchange Commission ("SEC"). (Exchange Act Section 15(h)(1).)

On October 25, 2001, the SEC adopted amendments to Rules 17a-3 and 17a-4 under the Exchange Act to clarify and expand record keeping requirements in connection with purchase and sale documents, customer records, associated person records, customer complaint records, and certain other matters. The amendments also require broker-dealers to maintain or promptly produce certain records at each office to which those records relate.

Through this rulemaking action the Commissioner is amending California's recordkeeping requirements for securities broker-dealers to mirror the SEC's rules, in order to comply with the prohibition in NSMIA against differing standards. Rather than amending the books and records requirements in Rules 260.241 and 260.241.1 to be consistent with the SEC's amended rules, the Commissioner instead is repealing the existing books and records requirements and incorporating the SEC's rules by reference.

The Commissioner is incorporating Rule 17a-3, which sets forth the general business books and records that a broker-dealer must make and keep current; Rule 17a-4, which sets forth additional records that must be preserved which sets forth the periods of time for the preservation of records; Rules 15g-2, 15g-4, 15g-5, and 15g-6, which set forth

additional requirements for records related to penny stocks; and Rule 15c2-11, which sets forth certain record requirements for broker-dealers prior to publishing any quotation for a security. In addition to the foregoing, the amendments to the books and records requirements clarify that the term "member" as used by the SEC has the same meaning as "broker-dealer," and the term "associated person" as used by the SEC has the same meaning as "agent." These amendments are necessary to ensure that the state's recordkeeping requirements for broker-dealers are not inconsistent with the SEC's requirements.

The SEC's rules incorporate the customer record-keeping requirements of Commissioner's Rule 260.218.5, and therefore this rule is being repealed.

In addition, Rule 260.241.2 is amended to eliminate the mandatory filing of an annual financial report by broker-dealers registered under the Exchange Act, as specified, and instead provide the Commissioner with authority to require the report upon request. This change is necessary to reduce the regulatory burden on broker-dealers to annually file a report that the Department may either obtain through other sources, or obtain upon request from a broker-dealer. This change is the result of an internal working group recommending methods for improving the efficiency of the regulatory program.

The amendments to Rule 260.241.2 also clarify the interim and annual reporting requirements for broker-dealers and investment advisers by:

- Clarifying that, for investment advisers, the annual report consists of a balance sheet and income statement, as specified;

- Clarifying that the annual report filed by investment advisers not receiving fees of more than $500 for more than six months in advance need not be audited;

- Clarifying that the annual report is due within 90 days of fiscal year end;

- Setting forth the documents that constitute the interim report for both investment advisers and broker-dealers; and

- Clarifying which documents are provided confidential treatment.

These changes are necessary to provide clarity to broker-dealers and investment advisers filing annual and interim reports, and to enhance investor protections.

Finally, the amendments to Rule 260.241.2 make technical changes to eliminate references to Rule 260.237.1 (10 CCR § 260.237.1), which sunset on January 1, 2005.

DETERMINATION GOVERNMENT CODE SECTION 11346.9(2)

The Commissioner has determined that the adoption of the regulation does not impose a mandate on local agencies or school districts, which require reimbursement

pursuant to Part 7 (commencing with Section 17500) of Division 4 of the Government Code.

ALTERNATIVES CONSIDERED

No alternative considered by the Department would be more effective in carrying out the purpose for which the regulation is proposed, or would be as effective and less burdensome to affected private persons, or would lessen any adverse impact on small businesses.

ADDENDUM, REGARDING PUBLIC COMMENTS

No request for hearing was received during the 45-day public comment period, which ended on November 19, 2007. Accordingly, no hearing was scheduled or held.

COMMENTS RECEIVED DURING THE 45-DAY COMMENT PERIOD

The Department received one public comment letter during the 45-day public comment period. By e-mail dated October 3, 2007, William E. Graeff with Seidman Private Securities, LLC. stated that Seidman Private Securities, LLC is a FINRA Member firm and on a quarterly basis files Focus II-A reports. He asked whether the changes to the rules would change the firm's current reporting requirements.

Department's Response: The rule changes herein will not impact a firm's reporting requirements with FINRA. The changes made by this regulatory action mean that these firms will no longer be required to file an annual financial report with the Department, except upon request of the Department.

However, a firm registered with FINRA remains subject to the interim reporting requirements if the firm's net worth is reduced to less than 120% of its required minimum net worth, or the firm's current ratio is reduced to less than 1.2. The changes to the rules clarify that in these instances, broker-dealers registered with FINRA must file with the Department the same notice that FINRA requires under Rule 17a-11(c)(3) (17 CFR 240.17a-11(c)(3)).

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