

Regulatory Bulletin

RB-00-09

September 29, 2000

TO: All PCX DEA Members, Member Organizations, ASAP Members, ETP Holders, ETP Firms, and Equity ASAP Holders

FROM: Financial & Operational Compliance Department

RE: Annual Audited Financial Statements

The Pacific Exchange has confirmed with the Securities and Exchange Commission ("SEC") that all broker-dealers who conduct off-floor trading activity, which is unrelated to market making or specialist functions, must file annual audited financial statements as required pursuant to SEC Rule 17a-5(d).

SEC Rule 17a-5(d) requires every registered broker-dealer to file an annual, independently audited statement of financial condition with the SEC, the broker-dealer's designated examination authority ("DEA"), and all self-regulatory organizations ("SROs") with whom the broker-dealer maintains a membership. The annual report must be prepared in a format consistent with the statements contained in FOCUS Report Form X-17A-5. The annual report must be audited by an independent, public accountant who does not perform the firm's regular auditing functions, and the report should be filed as of the same fixed date each year, unless a change is approved in writing by the broker-dealer's DEA.

Registered broker-dealers on the floor of a national securities exchange who are subject to daily oversight by the exchange are exempt from the annual audited financial statement filing requirement. However, all PCX DEA Members, Member Organizations, ETP Holders and ETP Firms who conduct off-floor trading, which is unrelated to their market making or specialist functions, can not claim an exemption to SEC Rule 17a-5(d) and are required to file an annual audited financial statement. The annual report must be submitted to the PCX Financial & Operational Compliance Department no later than 60 days after the fiscal year end of the broker-dealer (as indicated on the broker-dealer's Form BD).

Broker-dealers whose fiscal year does not end on December 31 can elect to file an annual audited financial statement 60 days after the calendar year. Broker-dealers whose fiscal year end (or annual audit date) does not coincide with the end of a calendar quarter must also file a FOCUS Report-Part IIA within 17 business days after their fiscal year end.

For reference, the text of SEC Rule 17a-5(d) appears below. Broker-dealers and their independent accountants are also encouraged to review SEC Rule 17a-5(e) on the nature and form of reports to be filed. Questions regarding this Bulletin should be directed to Eve R. Safran at (415) 393-4130 or Donna Lee at (415) 835-5202.

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SEC Rule 17a-5(d). Annual Filing of Audited Financial Statements.

- (1)
 - (i) Every broker or dealer registered pursuant to section 15 of the Act shall file annually, on a calendar or fiscal year basis, a report which shall be audited by an independent public accountant. Reports pursuant to this paragraph (d) shall be as of the same fixed or determinable date each year, unless a change is approved in writing by the designated examining authority for the broker or dealer. A copy of such written approval should be sent to the regional or district office of the Commission for the region or district in which the broker or dealer has its principal place of business.
 - (ii) A broker or dealer succeeding to and continuing the business of another broker or dealer need not file a report under this paragraph as of a date in the fiscal or calendar year in which the succession occurs if the predecessor broker or dealer has filed a report in compliance with this paragraph as of a date in such fiscal or calendar year.
 - (iii) A broker or dealer which is a member of a national securities exchange and has transacted a business in securities solely with or for other members of a national securities exchange, and has not carried any margin account, credit balance or security for any person who is defined as a "customer" in paragraph (c)(4) of this section, shall not be required to file a report under this paragraph.
- (2) The annual audited report shall contain a Statement of Financial Condition (in a format and on a basis which is consistent with the total reported on the Statement of Financial Condition contained in Form X-17A-5 (§ 249.617 of this chapter) Part II or IIA), a Statement of Income, a Statement of Cash Flows, a Statement of Changes in Stockholders' or Partners' or Sole Proprietor's Equity, and Statement of Changes in Liabilities Subordinated to Claims of General Creditors. Such statements shall be in a format which is consistent with such statements as contained in Form X-17A-5 (§ 249.617 of this chapter) Part II or Part IIA. If the Statement of Financial Condition filed in accordance with instructions to Form X-17A-5, Part II or Part IIA, is not consolidated, a summary of financial data, including the assets, liabilities, and net worth or stockholders' equity, for subsidiaries not consolidated in the Part II or Part IIA Statement of Financial Condition as filed by the broker or dealer should be included in the notes to the consolidated statement of financial condition reported on by the independent public accountant.
- (3) Supporting schedules shall include, from Part II or Part IIA of Form X-17A-5 (§ 249.617 of this chapter) a Computation of Net Capital Under § 240.15c3-1, a Computation for Determination of the Reserve Requirements under Exhibit A of § 240.15c3-3 and Information Relating to the Possession or Control Requirements Under § 240.15c3-3 and shall be filed with said report.
- (4) A reconciliation, including appropriate explanations, of the Computation of Net Capital under § 240.15c3-1 and the Computation for Determination of the Reserve

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Requirements Under Exhibit A of § 240.15c3-3 in the audit report with the broker's or dealer's corresponding unaudited most recent Part II or Part IIA filing shall be filed with said report when material differences exist. If no material differences exist, a statement so indicating shall be filed.

- (5) The annual audit report shall be filed not more than sixty (60) days after the date of the financial statements.
- (6) The annual audit report shall be filed at the regional or district office of the Commission for the region or district in which the broker or dealer has its principal place of business, the Commission's principal office in Washington, D.C., and the principal office of the designated examining authority for said broker or dealer. Copies thereof shall be provided to all self-regulatory organizations of which said broker or dealer is a member.