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BEFORE THE DEPARTMENT OF CORPORATIONS

OF THE STATE OF CALIFORNIA

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| In the Matter of the Accusation of<br><br>THE CALIFORNIA CORPORATIONS COMMISSIONER,<br><br>Complainant,<br>v.<br><br>LEEDHA, INC., DBA FLINTRIDGE ASSET MANAGEMENT COMPANY; and EARL D. ANSCHULTZ, as an individual,<br><br>Respondents. | CASE NO.<br><br>FILE NO. 923-2223<br><br>ACCUSATION TO:<br><br>REVOKE INVESTMENT ADVISER CERTIFICATE OF LEEDHA, INC. (CORPORATIONS CODE SECTION 25232)<br><br>BAR EARL D. ANSCHULTZ (CORPORATIONS CODE SECTION 25232.1)<br><br>WITH<br><br>CLAIM FOR ANCILLARY RELIEF IN THE FORM OF DISGORGEMENT AND COSTS (CORPORATIONS CODE SECTION 25254)<br><br>AND<br><br>STATEMENT IN SUPPORT OF:<br><br>ORDER TO LEVY ADMINISTRATIVE PENALTIES (CORPORATIONS CODE SECTION 25252) |



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William P. Wood, the California Corporations Commissioner ("Commissioner") of the Department of Corporations ("Department") alleges and charges as follows:

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## I. JURISDICTION AND VENUE

1. The Commissioner brings this action pursuant to the provisions of California Corporations Code sections 25232, 25232.1, 25252 and 25254, and the rules and regulations promulgated thereunder.

2. The Commissioner is authorized to administer and enforce the provisions of the Corporate Securities Law of 1968, Corporations Code section 25000 et seq., and the regulations thereunder at California Code of Regulations, title 10, section 260.000 et seq.

## II. STATEMENT OF FACTS

3. This action is brought to revoke the investment adviser certificate issued to Respondent Leedha, Inc., dba Flintridge Asset Management Company ("Leedha") pursuant to Corporations Code section 25232, and to bar Respondent Earl D. Anschultz ("Anschultz") from any position of employment, management or control of any investment adviser, broker-dealer or commodity adviser pursuant to Corporations Code section 25232.1. In addition, this action is brought to issue an order levying an administrative penalty against Leedha pursuant to Corporations Code section 25252 and also claims ancillary relief in the form of disgorgement of excessive advisory fees charged to clients and costs pursuant to Corporations Code section 25254.

4. At all relevant times, Anschultz was the owner and President of Leedha. Leedha is a California corporation, formed in February 1990. Leedha is located at 2540 Huntington Drive, Suite 104, San Marino California 91108.

5. On July 3, 1990, the Commissioner first issued an investment adviser certificate to Leedha.

6. On October 28, 1996, the Commissioner issued an Order summarily suspending Leedha's investment adviser certificate for its failure to maintain books and records and tangible net capital in accordance with Corporations Code section 25241 and California Code of Regulations,



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title 10, sections 260.241.2 and 260.241.3. In this Order, Leedha was given 30 days to come into compliance. If Leedha failed to comply within 30 days, a revocation Order would be issued. Leedha failed to comply within 30 days as demanded. Therefore, on December 26, 1996, the Commissioner set aside the Order of suspension and issued a Summary Revocation Order for Leedha's books and records violations.

7. On March 20, 2001, the Commissioner received a customer complaint showing that Leedha was acting as an investment adviser. During this time period, Leedha did not have an investment adviser certificate. On April 27, 2001, the Commissioner issued a Desist and Refrain Order to Leedha and Anschultz for engaging in unlicensed investment adviser activity.

8. In October 2001, the Commissioner and Anschultz entered into an agreement signed by both parties entitled "Undertaking". The Undertaking permitted Leedha to once again be licensed by the Commissioner as an investment adviser. However, the Commissioner imposed conditions on the new investment adviser certificate issued to Leedha on October 30, 2001, by requiring Leedha to file two types of reports:

1) Monthly reports to the Commissioner stating that Leedha was in compliance with the capital requirements of California Code of Regulations, title 10, section 260.237.1. If during the first 12 months there were no violations of section 260.237.1, then the reports could be submitted quarterly; and

2) Quarterly reports to the Commissioner stating that they were in compliance with the books and records requirements under California Code of Regulations, title 10, sections 260.241.1, 260.241.2 and 260.241.3. If during the first twelve months there were no violations, then the reports were due biannually.

These reports were due within fifteen days of the period covered and were to continue for a two year period until October 31, 2003. **Paragraph 27 of the Undertaking states that if the licensee fails to perform any of the conditions of the Undertaking, the Commissioner may summarily revoke its certificate**.

9. On May 1, 2003, the Commissioner commenced a field examination of Leedha. During its examination, the Commissioner determined that **Leedha violated the terms of the Undertaking,**



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**which would entitle the Department of Corporations to summarily revoke Leedha's investment adviser certificate**. The first quarterly report from Leedha stating that it was complying with the capital requirements of California Code of Regulations, title 10, section 260.237.1 for November 2002 through January 2003 was due on February 15, 2003. Leedha failed to file this report as required in the Undertaking. The second quarterly report showing compliance with the capital requirements was due on May 15, 2003. Leedha also failed to file this report as required in the Undertaking.

10. Furthermore, Leedha never produced any biannual reports as required in the Undertaking stating that they were in compliance with the books and records requirements under California Code of Regulations, title 10, sections 260.241.1, 260.241.2 and 260.241.3.

11. During its May 2003 examination, the Commissioner not only determined that Leedha failed to comply with the terms of the Undertaking but also discovered that Leedha continued to violate the same books and records requirements and misrepresented the nature of its investment advisory fees charged to clients.

12. Therefore, based on Leedha's continued blatant disregard of the various books and records requirements and Leedha's violations of the California Securities Laws, it is in the public interest that Leeda's investment adviser certificate should be revoked and Anschultz should be barred from any position of employment, management or control of any investment adviser, broker-dealer or commodity adviser.

## III. RESPONDENT LEEDHA'S INVESTMENT ADVISER CERTIFICATE SHOULD BE REVOKED PURSUANT TO CORPORATIONS CODE SECTION 25232, SUBDIVISION (e).

13. Corporations Code section 25232 provided, in pertinent part:

> The commissioner may, after appropriate notice and opportunity for hearing, by order censure, deny a certificate to, or suspend for a period not exceeding 12 months or revoke the certificate of, an investment adviser, if the commissioner finds that the censure, denial, suspension, or revocation is in the public interest and that the investment adviser, whether prior or subsequent to becoming such, or any partner, officer or director thereof or any person performing similar functions or any person directly or indirectly controlling the investment adviser, whether prior or subsequent to becoming such, or any employee of the investment adviser while so employed has done any of the following:



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(e) Has willfully violated any provision of . . . Title 4 (commencing with Section 25000)... or of any rule or regulation under any of those statutes, or any order of the commissioner which is or has been necessary for the protection of any investor.

14. Leedha is subject to revocation of its investment adviser certificate pursuant to Corporations Code section 25232, subdivision (e) for willfully violating Corporations Code section 25241 and California Code of Regulations, title 10, sections 260.241.2, 260.241.3, and 260.238.

Books and Records Violations

15. These willful violations consisted of Leedha's failure to keep true, accurate and current books and records in violation of Corporations Code section 25241, including:

1) failing to maintain a cash receipt journal in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(1);

2) failing to maintain a current general ledger which contains assets, liabilities and equities accounts in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(2);

3) failing to maintain copies of client invoices for its quarterly billing for the period April through June 2001 in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(5);

4) failing to maintain all powers of attorney and other evidences of the granting of discretionary authority by any client in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(9);

5) failing to maintain all written agreements entered into by the investment adviser with any client in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(10);

6) failing to prepare and maintain monthly computations of net capital in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (j); and

7) failing to file its annual financial reports in violation of California Code of Regulations, title 10, section 260.241.2, subdivision (a).

The books and records requirements provide the Department with a regulatory mechanism to validate a firm's liquidity and financial integrity on a monthly basis to ensure that licensees maintain



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the necessary net capital for the protection of the public. Leedha's failure to keep true, accurate and current books and records prevents the Department from determining as part of its regulatory examination, if it meets the capital requirements imposed by the Corporations Code and the regulations enacted thereunder.

16. Corporations Code section 25241 provides that investment advisers are required to maintain books and records that are subject to examinations by the Commissioner. Corporations Code section 25241 provides, in relevant part, as follows:

> (a) [E]very investment adviser licensed under Section 25230 shall make and keep accounts, correspondence, memorandums, papers, books, and other records and shall file financial and other reports as the commissioner by rule requires...
>
> ....
>
> (c) All records referred to in this section are subject at any time and from time to time to reasonable periodic, special or other examinations by the commissioner, within or without this state, as the commissioner deems necessary or appropriate in the public interest or for the protection of investors.

Leedha violated Corporations Code section 25241 by failing to keep true, accurate and current books and records as required under California Code of Regulations, title 10, sections 260.241.3 and 260.241.2.

17. California Code of Regulations, title 10, section 260.241.3 sets forth the specific books and records required to be maintained by investment advisers. Specifically, section 260.241.3 provides in relevant part as follows:

> (a) Every licensed investment adviser shall make and keep true, accurate and current the following books and records relating to such person's investment advisory business:
>
> (1) A journal or journals, including cash receipts and disbursements records, and any other records of original entry forming the basis of entries in any ledger.
>
> (2) General and auxiliary ledgers (or other comparable records) reflecting asset, liability, reserve, capital, income and expense accounts.
>
> (5) All bills or statements (or copies thereof), paid or unpaid, relating to the business of the investment adviser as such.
>
> (9) All powers of attorney and other evidences of the granting of any discretionary authority by any client to the investment adviser, or copies thereof.
>
> (10) All written agreements (or copies thereof) entered into by the investment adviser with



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any client or otherwise relating to the business of such investment adviser as such.

18. During the Commissioner's May 1, 2003 regulatory examination, the Commissioner determined that Leedha does not maintain a cash receipt journal in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(1).

19. In addition, Mr. Anschultz told the Commissioner that Leedha does not maintain a cash receipt journal.

20. As of May 1, 2003, the general ledger and accounting records were not current through March 31, 2003, as required. Leedha's financial statements and general ledger obtained on May 1, 2003, was as of December 31, 2002, three months behind. Furthermore, Leedha's general ledger was not accurate, since it did not include an account for the unearned portion of investment advisory fees billed quarterly in advance. Therefore, Leedha did not maintain a current general and auxiliary ledger accounting system in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(2).

21. Leedha billed its clients for the quarter April through June 2001, but did not maintain invoices in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(5).

22. Furthermore, Leedha did not maintain copies of the powers of attorney for forty-one of its sixty accounts. Copies of these agreements were obtained from Smith Barney's Security Account Limited Discretionary Authorization forms on July 3, 2003. Seventeen out of twenty-eight client files reviewed did not contain copies of the investment advisory agreement. This activity is in violation of California Code of Regulations, title 10, section 260.241.3, subdivisions (a)(9) and (10).

23. Prior to April 3, 2003, California Code of Regulations, title 10, section 260.241.3, subdivision (j) provided as follows:

> Any investment adviser who is subject to the minimum capital requirements of Section 260.237.1 shall, in addition to the records otherwise required under this section, maintain a record of the proof of money balances of all ledger accounts in the form of trial balances and a record of the computations of net capitals and aggregate indebtedness pursuant to Section 260.237.1 of these rules (as of the trial balance date). The trial balances and computations shall be prepared currently at least once a month.



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24. The Department's examiner found during its 2003 examination that Leedha did not prepare its net capital and aggregate indebtedness calculations for 4 months starting with December 2002 and ending with March 31, 2003. Leedha also failed to maintain its net capital and aggregate indebtedness calculations on a monthly basis for 17 months, starting with November 2001 and ending with March 31, 2003, which included the time period relevant to the Undertaking. This is in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (j).

25. As a result of Leedha's violations of California Code of Regulations, title 10, section 260.241.3, subdivisions (a)(2) and (j), the Department was unable to determine at the time of the examination, if the firm was in compliance with the net capital requirements under California Code of Regulations, title 10, section 260.237.1.

26. Prior to April 3, 2003, California Code of Regulations, title 10, section 260.237.1 set forth the capital requirements for investment advisers. California Code of Regulations, title 10, section 260.237.1, subdivision (a)(2) provided, in relevant part, as follows:

> (a) No investment adviser who has any power of attorney from any investment advisory client to execute transactions...shall permit its total aggregate indebtedness to exceed 500% of its tangible net capital or permit its current aggregate indebtedness to exceed its current net capital; and,
>
> (2) If the investment adviser has any power of attorney from any investment advisory client to execute transactions and does not have regular or periodic custody or possession of any of its investment advisory clients' securities or funds,...it shall at all times have and maintain tangible net capital of not less than $5,000.00.

California Code of Regulations, title 10, section 260.237.1, subdivision (c) provided that for purposes of section 260.237.1, subdivision (a), all financial information shall be determined in accordance with generally accepted accounting principles ("GAAP").

27. During the Department's 2003 regulatory examination, the examiner found that Leedha had power of attorney over advisory client accounts to execute transactions. Therefore Leedha was required to maintain a tangible net capital of not less than $5,000.

28. Prior to April 3, 2003, California Code of Regulations, title 10, section 260.241.2 set forth the specific annual financial report required by investment advisers. Section 260.241.2, subdivision (a)(2) provided, in relevant part, as follows:



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> (a) **General Rule**. Subject to the provisions of Subsection (c) of this section, ... every licensed investment adviser subject to the provisions of section 260.237.1 of these rules, shall file an annual financial report containing the information required by a form or forms to be supplied or approved by the Commissioner as follows:
>
> (2) The annual report for investment advisers shall contain a Statement of Financial Condition. Supporting schedules shall contain computations of net capitals, aggregate indebtedness and ratios required under Section 260.237.1 and the certificate of the accountant required under subsection (e) of Section 260.237 of these rules.

29. Because Leehda was subject to the capital requirements under California Code of Regulations, title 10, section 260.237.1, it was also required to file annual financial reports. The Department's examiner found during the 2003 regulatory examination that Leedha had failed to file annual financial reports for years 2001 through 2002 in violation of California Code of Regulations, title 10, section 260.241.2, subdivision (a).

Violations of Fair, Equitable and Ethical Principles

30. California Code of Regulations, title 10, section 260.238 sets forth fair, equitable and ethical principles required of investment advisers. Section 260.238, subdivision (h) provides as follows:

> The following activities do not promote "fair, equitable or ethical principles" as that phrase is used in section 25238 of the Code.
>
> (h) **Misrepresenting to any advisory client**, or any prospective advisory client, the qualifications of the adviser, its representatives or any employees, or misrepresenting the nature of the advisory services being offered or **fees to be charged for such service, or omitting to state a material fact necessary to make the statements made regarding the** qualifications, services or **fees, in light of the circumstances under which they are made, not misleading**. (emphasis added)

31. Leedha misrepresented the nature of its investment advisory client fees to numerous clients from January 2001 through March 31, 2003. Leedha overcharged its clients approximately $79,082.05 as a result of math errors, double billing, billing after services were terminated and billing clients while Leedha was an unlicensed investment adviser from April through June 2001. Therefore, Leedha misrepresented the nature of the fees to be charged for such services in willful violation of California Code of Regulations, title 10, section 260.238, subdivision (h).



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32. Also, the contract used by Leedha grants Leedha with the authority to issue investment instructions on behalf of the client, but is not signed by Leedha. After Leedha received a signed contract from its clients, Leedha sent a letter to clients stating that the advisory fee charged was **1.5% annually of the value of the portfolio**, billed quarterly in advance based upon values at the beginning of the quarter. Leedha, however, failed to specify that the portfolio credit line, which is actually the margin balance in the client account, would be added to the net value of the portfolio and cost clients higher undisclosed investment advisory fees. Therefore, Leedha further misrepresented the nature of the fees to be charged for such services by making material omissions regarding fees it would charge in violation of California Code of Regulations, title 10, section 260.238, subdivision (h).

33. As a result, it is in the public interest that Leedha's investment adviser certificate should be revoked pursuant to Corporations Code section 25232, subdivision (e).

## IV. RESPONDENT ANSCHULTZ SHOULD BE BARRED FROM ANY POSITION OF EMPLOYMENT, MANAGEMENT OR CONTROL OF ANY INVESTMENT ADVISER, BROKER-DEALER OR COMMODITY ADVISER PURSUANT TO CORPORATIONS CODE SECTION 25232.1

34. Corporations Code Section 25232.1 provided, in pertinent part:

> The commissioner may, after appropriate notice and opportunity for hearing, by order censure, or suspend for a period not exceeding 12 months, or bar from any position of employment, management or control of any investment adviser, broker-dealer or commodity adviser, any officer, director, partner, employee of, or person performing similar functions for, an investment adviser, or any other person, if he or she finds that the censure, suspension or bar is in the public interest and that the person has committed any act or omission enumerated in subdivision (a), (e), (f), or (g) of Section 25232…

35. Corporations Code section 25232, subdivision (e), provides that the Commissioner may bar any person from any position of employment, management or control of any investment adviser, broker-dealer or commodity adviser for any violation of the Corporate Securities Law, which is found in Title 4 of the Corporations Code, or any of its rules or regulations.

36. Therefore, by engaging in the activity described in paragraphs 15 through 32 above, Anschultz is subject to being barred from any position of employment, management or control of any investment adviser, broker-dealer or commodity adviser pursuant to Corporations Code section



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25232.1, for willfully violating Corporations Code section 25241 and California Code of Regulations, title 10, sections 260.241.2, 260.241.3, and 260.238.

37. As a result, it is in the public interest that Anschultz should be barred from any position of employment, management or control of any investment adviser, broker-dealer or commodity adviser pursuant to Corporations Code section 25232.1.

## V. ANCILLARY RELIEF SHOULD BE AWARDED

38. Leedha's clients are also entitled to relief, including disgorgement of excessive investment advisory fees paid to Leedha as described above and recovery of costs, investigative expenses and attorney's fees in an amount of at least $10,000, pursuant to Corporation Code section 25254.

39. Section 25254, in pertinent part, states:

> (a) If the commissioner determines it is in the public interest, the commissioner may include in any administrative action brought under this part a claim for ancillary relief, including, but not limited to, a claim for restitution or disgorgement or damages on behalf of the persons injured by the act or practice constituting the subject matter of the action, and the administrative law judge shall have jurisdiction to award additional relief.
>
> (b) In an administrative action brought under this part, the commissioner is entitled to recover costs, which in the discretion of the administrative law judge may include an amount representing reasonable attorney's fees and investigative expenses for the services rendered, for deposit into the State Corporations Fund for the use of the Department of Corporations.

## VI. STATEMENT IN SUPPORT OF ORDER LEVYING ADMINISTRATIVE PENALTIES

40. This Accusation, based on the conduct described above, also serves as a basis for a Statement in Support of an Order Levying Administrative Penalties. Leedha willfully violated the California Securities Laws and regulations thereunder justifying the issuance of an order levying administrative penalties. Leedha, having applied for and secured an investment adviser certificate is obligated to have knowledge of and comply with the provisions of the California Securities Laws



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and regulations. Anschultz, as President and Owner of Leedha, is also obligated to have knowledge of and comply with provisions of the California Securities Laws and regulations.

41. Corporations Code section 25252 authorizes the Commissioner to issue an order levying administrative penalties against any investment adviser for willful violations of any provisions of the California Securities Laws and any rules promulgated thereunder. Corporations Code section 25252 provides, in relevant part:

> The Commissioner may, after appropriate notice and opportunity for hearing, by order levy administrative penalties as follows: . . .
>
> (b) Any broker-dealer or investment adviser that willfully violates any provision of this division to which it is subject, or that willfully violates any rule or order adopted or issued pursuant to this division and to which it is subject, is liable for administrative penalties of not more than five thousand dollars ($5,000) for the first violation, not more than ten thousand dollars ($10,000) for the second violation, and not more than fifteen thousand dollars ($15,000) for each subsequent violation . . .
>
> (c) The administrative penalties available to the commissioner pursuant to this section are not exclusive, and may be sought and employed in any combination with civil, criminal, and other administrative remedies deemed advisable by the commissioner to enforce the provisions of this division.

## VII. SUMMARY OF VIOLATIONS

42. In summary by reason of the foregoing, Leedha willfully violated Corporations Code section 25241 by failing to keep true, accurate and current books and records. Specifically, Leedha made the following willful violations:

a. failing to maintain a cash receipt journal in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(1);

b. failing to maintain a current general ledger which contains assets, liabilities and equities accounts in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(2);

c. failing to maintain copies of client invoices for its quarterly billing for the period



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April through June 2001 in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(5);

d. failing to maintain all powers of attorney and other evidences of the granting of discretionary authority by any client in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(9);

e. failing to maintain all written agreements entered into by the investment adviser with any client in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (a)(10);

f. failing to prepare and maintain monthly computations of net capital in violation of California Code of Regulations, title 10, section 260.241.3, subdivision (j);

g. failing to file its annual financial reports in violation of California Code of Regulations, title 10, section 260.241.2, subdivision (a); and

h. failing to disclose the nature of the fees to be charged for such services in violation of California Code of Regulations, title 10, section 260.238, subdivision (h).

## VI. PRAYER

WHEREFORE, based upon the foregoing, the Commissioner finds it is in the public interest and prays that:

1. Leedha's investment adviser certificate be revoked pursuant to Corporations Code section 25232 for willful acts committed as specified in Corporations Code section 25232, subdivision (e);

2. Anschultz be barred from any position of employment, management or control of any investment adviser, broker-dealer or commodity adviser pursuant to Corporations Code section 25232.1 for willful acts committed as specified in Corporations Code section 25232, subdivision (e);

3. Ancillary relief be claimed against Leedha and Anschultz pursuant to Corporations Code section 25254 as follows:

a. disgorgement of excessive investment advisory client fees received by Leedha and Anschultz in an amount of at least $ 79,082.05 and according to proof; and

b. recovery of costs, investigative expenses and attorney's fees in an amount of at least $10,000.



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4. Good cause showing, pursuant to Corporations Code section 25252, the California Corporations Commissioner prays for an Order levying administrative penalties against Respondent Leedha in the amount of **$32,000.00**, for the following willful violations:

a. $3500 for violations of Corporations Code section 25241;

b. $3500 for violations of California Code of Regulations, title 10, section 260.241.3(a), subdivision (1);

c. $3500 for violations of California Code of Regulations, title 10, section 260.241.3(a), subdivision (2);

d. $3500 for violations of California Code of Regulations, title 10, section 260.241.3(a), subdivision (5);

e. $3500 for violations of California Code of Regulations, title 10, section 260.241.3(a), subdivision (9);

f. $3500 for violations of California Code of Regulations, title 10, section 260.241.3(a), subdivision (10);

g. $3500 for violations of California Code of Regulations, title 10, section 260.241.3(j);

h. $3500 for violations of California Code of Regulations, title 10, section 260.241.2, subdivision (a); and

i. $4000 for violations of California Code of Regulations, title 10, section 260.238, subdivision (h).

Dated: August 16, 2004

WILLIAM P. WOOD
California Corporations Commissioner

By: _____
MICHELLE LIPTON
Corporations Counsel.
Enforcement and Legal Services Division



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