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Will merger weaken regulatory oversight?

Local securities experts disagree on potential impact of NASD, NYSE combination

Scott Olson solson@ibj.com

A merger of the two biggest regulators that police the nation's 5,100 investment brokerages is drawing mixed reactions from the securities industry. NASD, formerly known as the National Association of Securities Dealers, and NYSE Group Inc., parent of the New York Stock Exchange subsidiaries, want to complete the merger by June 30.

Supporters hail the alliance as a costcutting measure that will eliminate overlapping regulation and establish a uniform set of rules by placing oversight responsibility in a single, yet-to-be-named entity.

But the proposal is encountering opposition from some within the industry who think the consolidation in fact will weaken oversight by resulting in fewer regulators.

Mark Maddox, managing partner of local securities firm **Maddox** Hargett & Caruso PC and an Indiana securities commissioner from 1989 to 1991, represents victims of investment fraud.

"You're really taking cops off the beat," he said. "It would be like the city of Indianapolis saying, 'In response to more murders, we're going to cut the police force by a third.'"

Advocates argue the concerns are exaggerated. Russell Bauman, national sales manager of Chicago-based David A. Noyes & Co., said firms such as his are scrutinized plenty.

"It's obvious to me and my colleagues that the regulatory oversight is greater today than ever before," said Bauman, who manages the Indianapolis branch. "It's something that seems to increase year after year after year."

Indeed, other regulators include the Securities and Exchange Commission, state agencies and less significant self-regulatory organizations much smaller than either the NASD or NYSE.

The new department will include regulators from both enforcement teams and will operate from New York City; Washington, D.C.; and 18 district locations across the country, according to a joint release from the two partners.

Yet skepticism abounds, even from the Indiana Secretary of State's Office. It launched a Prosecution Assistance Unit within its Securities Division last year to further protect investors.

"We live in a world where we've had Enron and WorldCom," said Todd Rokita, Indiana secretary of state. "Investments are more complex than ever before. If you don't have a regulatory scheme that is helpful, people will turn away from the markets."

And **Maddox** further asserted that investors will have one less arbitration option. Arbitration is a quick and inexpensive alternative to a lawsuit and is the most popular way to resolve complicated disputes in the securities industry. The consolidation will leave only one agency in which to seek a settlement.

Another concern unrelated to consumer protection involves smaller securities firms fearful the proposal will hand oversight control to larger brokerages by restricting their voice on the new organization's consolidated board. Under the plan, small firms of 150 brokers or less, which number roughly 4,500 and far outnumber their bigger counterparts, can vote for only seven of the 23 seats. They now vote for all slots as NASD members.

The discrepancy will give larger firms complete control over securities regulation and allow them to propose rules and burdensome regulations aimed at eliminating competition from smaller rivals, said the Financial Industry Association. The year-old Florida-based group formed to represent the interests of smaller, regional brokerages and is the most vocal critic of the proposal.

"They're trying to cram this down everybody's throats and doing everything they can to get them to drink the Kool-Aid," FIA President Richard Goble said. "It's a crazy plan and an absolute amazing coup by a very small group of monopolists."

Those are the 200 largest firms that are members of both the NYSE Group and NASD. The consolidation bringing the brokerages under one umbrella is expected to reduce their expenses. The anticipated savings will be distributed in a one-time $35,000 payment to each member that detractors liken to a bribe to buy support. And annual dues will be reduced by $1,200 annually for the next five years.

Michael Bosway, CEO of locally based City Securities Corp., is unconvinced smaller firms such as his will suffer as a result of the consolidation. He chaired the NASD's District 8 committee this year that is based in Chicago and encompasses Illinois, Indiana, Kentucky, Michigan, Ohio and Wisconsin.

"It might make it more difficult for the smaller firms to be heard, but that tradeoff is not that significant," he said. "The way we operate from a client perspective won't change one iota."

Bauman at David A. Noyes doesn't view the consolidation as a power grab by large securities firms. Rather, it is in reaction to the aggressive oversight of Eliot Spitzer, former attorney general and newly elected governor of New York, he said.

Upon taking office in 1999, Spitzer investigated conflicts of interest by investment banks, illegal trading practices by mutual funds, and bid rigging by the insurance industry. His probes have led to billions of dollars in recoveries for investors, as well as industry-wide reforms.

Spitzer's success led the NASD and NYSE Group to seek additional reform, for fear of being "shown up" further, Bauman said.

A recent NASD ruling slapped Omaha, Neb.-based Securities America Inc. with a $2.5 million fine for allegedly failing to properly supervise a broker. The broker was accused of convincing a group of former ExxonMobil employees to retire early and cash out their retirement savings for variable annuities. The NASD awarded them $13.8 million in restitution.

It also fined New York-based Oppenheimer & Co. Inc. $800,000 for several alleged breaches. They included failing to respond to regulatory requests for information and failing to timely and accurately report thousands of municipal securities dealings.

The merger between NASD and NYSE is nearly complete. Directors of both have granted their consent, although amendments to bylaws still need approval from NASD members. The Securities and Exchange Commission also needs to give its blessing.
