STATEMENT BY CHAIRMAN ARTHUR LEVITT
U.S. SECURITIES AND EXCHANGE COMMISSION
PRESS CONFERENCE REGARDING THE NASD
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This is a good day for investors, and a good day for our markets. Today we are announcing the settlement of an enforcement action against the National Association of Securities Dealers, which operates and oversees the Nasdaq stock market -- the second largest market in America.

Nasdaq is a powerful engine of growth for our economy. It is home to some of the largest companies in the world, and some of the smallest. It provides millions of Americans with the opportunity to share in these companies' growth.

But markets exist by the grace of investors. When those who direct them lose sight of that cardinal rule, and sacrifice investor interests on the altar of short-term gain, then far from helping their market, they hurt it. History regularly attests to this truth: witness the New York Stock Exchange in the 1930s, the American Stock Exchange in the 1960s, and now Nasdaq, in the 1990s.

During an 18-month investigation, the Commission found serious shortcomings in the way this market has operated. In a few moments, the Commission's Director of Enforcement, Bill McLucas, will describe the laws that were violated, as well as the details of our settlement. I want to set the context for this action, and talk about the future.

Our securities markets operate under a "self-regulatory" system. Markets serve an important public interest, and deserve public oversight; but markets are also innovative and fast-moving, and easily stifled by the heavy hand of government.

So Congress arrived at a formula in which the industry polices itself, with SEC oversight. This keeps us out of most day-to-day affairs, and allows us to keep our hands off, but our eyes open. And on those rare occasions when self-regulation goes off track, the SEC must act in the public interest.

This is one of those occasions.

I will state it simply and up front. We have found a widespread course of conduct among market makers to coordinate their quotes. Investors paid too much, and received too little, when they bought and sold stock on Nasdaq. New traders were, as a matter of course, trained in this fashion. Over time, this practice became the expected standard. In some instances, those who did not comply were harassed and penalized, even if they had acted in the best interest of investors.

This culture of collaboration subverted the price mechanism and curtailed competition. It raised the cost of capital and undermined market efficiency. It hurt investors and damaged the reputation of Nasdaq.

Where was the NASD, the cop on the Nasdaq beat?

The NASD was not blind to these practices in the marketplace. It simply looked the other way.

As the issue of the pricing convention was brought to the attention of the NASD, as the press and others raised it with increasing frequency, the NASD sounded no alarm; it conducted no investigation.

Nor was the pricing convention the only unacceptable practice. The NASD failed to ensure the accuracy and fairness of quotation and transaction information -- the backbone of securities trading. It failed to apply certain rules to its members, and selectively enforced rules against others. The NASD allowed the interests of large marketmaking firms to have undue influence over the conduct of its affairs and the regulation of its market.

The evidence -- gathered from hundreds of witnesses, thousands of hours of tapes, and more than a million pages of documents -- shows that the NASD did not fulfill its most basic responsibilities -- and I quote from its charter: "to promote just and equitable principles of trade for the protection of investors." On the contrary, American investors were hurt -- large and small, sophisticated and inexperienced, institutional and individual -- all were hurt by these practices.

Nor has the SEC emerged unscathed. To the extent these practices took place on our watch, we should have acted sooner. We, as well as the NASD, need to be faster and more vigilant, to assure that the public interest is protected.

So far, I've talked about the past. But a brighter future lies ahead, and in fact has already begun. Both the SEC and the NASD are taking steps to assure that investors can have full confidence in our markets.

One year ago, the NASD commissioned a blue ribbon committee under former Senator Warren Rudman to examine this SRO and make recommendations. Chief among those was the reorganization this spring of its corporate structure, and the creation of a new regulatory subsidiary, NASDR. The Board of the NASD now has a majority of public directors, and its operating companies have boards balanced among all the NASD's constituencies. The members of these boards are as highly qualified and dedicated as any directors anywhere. They will guard the interests of investors with energy and enthusiasm. They have my complete confidence, and they deserve yours, too.

In addition, by the terms of our settlement, the NASD will spend an additional $100 million over the next five years on regulatory enhancements, in lieu of a financial penalty. Changes have already been made in surveillance and enforcement. These and other changes made in the context of our settlement will ensure that the NASD moves into the next century as a vibrant marketplace and staunch defender of investor interests.

It's inevitable that some will complain that we're hurting the market by reducing profitability. That's the perennial refrain, uttered at every turning point in the industry, from registering stock in the 1930s to unfixing commissions in the 1970s. It's a phony argument. Far from condemning the dealer market, our action today affirms it. Let the firms make as much profit as they can -- we don't care. All we ask is that prices be set by competition, not coordination.

The Commission has also taken steps to sharpen its own watchdog skills. More than a year ago, we consolidated our inspections and examinations functions, including those that relate to SRO oversight, into a new, more efficient group that is independent of any operating division. This will assure a higher level of oversight of all SROs.

Comprehensive and lasting reform of this market, however, requires fundamental change. The Commission proposed last year a series of order handling rules that will address structural problems in all markets. But I believe they will play an especially important role in protecting investors on the Nasdaq market. We hope to have these rules in place this year.

Let me now address a few words to the people of Nasdaq. This is a difficult moment. But long experience in the industry has taught me that the vast majority of people who work in it are good, honest, decent people. Any system can lend itself to excesses, especially under the pressures of explosive growth. But where we find such excesses, we can do no less than to face them forthrightly and put them behind us. No one is saying that the Nasdaq market has been "bad" for investors, but simply that it could and should be <u>better</u> for investors. I look forward to working together to ensure that it is.

I would be remiss if I failed also to say a word to the many dedicated SEC staff who worked on or contributed to this case. You've done an extraordinary job that will serve our nation's investors well for many years to come.

If I seem passionate about this issue, it's because I've been around the capital markets for most of my life. I owe almost everything I have to those markets and I've seen firsthand the enormous good they can do for our communities, for our economy, and for our nation. I believe that the historic changes taking place today and in the weeks and months ahead will result in the strongest, most innovative, and best-led dealer market in history, and I will dedicate myself to making it so. But if the Nasdaq fulfills those expectations, it will be in large measure because of your hard work over the past year and a half. And so as highly as I may praise you today, I believe that posterity will praise you higher still. On behalf of the Commission, I thank you.

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