



NASAA

**North American
Securities Administrators Association**

**The “New Economy” and
State Securities Regulation**

**Approved Unanimously by
NASAA Membership**

September 19, 2000

North American Securities Administrators Association, Inc.¹

The “New Economy” and State Securities Regulation

The past two decades have brought enormous change to Wall Street and all our financial markets. We are now a nation of investors; half of all households own stock. Our securities markets are global, electronic and increasingly seamless. Financial services--securities, banking, insurance--are consolidating, an irreversible trend recognized by the Gramm-Leach-Bliley Act of 1999 (GLBA). This landmark legislation reaffirmed the concept of functional regulation--that securities products should be regulated by those with expertise in securities.

State securities regulators have been protecting investors from fraud and abusive sales practices for almost 90 years, beginning with the passage of the first “blue sky” law, in Kansas, in 1911. State regulation preceded federal securities laws and the creation of the Securities and Exchange Commission (SEC) and the National Association of Securities Dealers (NASD). Our system of state, federal and industry oversight supports our securities markets and has helped make them the envy of the world. When this system works well, each regulator complements the other, leveraging resources, strengths and expertise.

American investors benefit from grass-roots regulation. If someone is mugged on Main Street, they probably are not going to call the federal government; if they have a problem or need information about investments, chances are they will contact their state securities regulator for help.

We believe that with the industry, technology and consumer expectations changing so rapidly, regulation needs to change too. It is time for regulators--all regulators--to look closely at what they do. As a new century unfolds, it is time to look forward and build on our successes. State securities regulators will continue to strive for efficiency, to commit ourselves to being even more effective. America’s investors expect and deserve nothing less.

We continue to strive for consistency and uniformity. Further, we have the opportunity to use technology to leverage our resources. Consistent with the NASAA Strategic Plan, we have developed the following guiding principles for the future.

BROKER-DEALER REGULATION

For decades, broker-dealer regulation has been a central focus of state securities regulators. Through careful licensing and on-site examinations, we protect investors from malfeasance ranging from overreaching sales practices to outright fraud. Our close proximity to firms and investors allows us to be local cops on the securities beat.

¹ The oldest international organization devoted to investor protection, the North American Securities Administrators Association, Inc., was organized in 1919. Its membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico and Puerto Rico. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

Over the years, when many firms were local or regional, states developed their own in-house licensing processes. Now that many firms are national and even international, states recognize the need to enact uniform rules and streamline procedures. For broker-dealer agents, the licensing process today is much more streamlined, in large part due to the Central Registration Depository (CRD), which the states and the National Association of Securities Dealers (NASD) developed jointly. The CRD is arguably the best licensing system in existence. We are striving to use this electronic system to its fullest potential. The states are working together, through NASAA, to get all remaining states to adopt rules to automatically approve a broker-dealer agent's application if he/she has a clean record. In some cases this requires working with NASD Regulation to make changes to WebCRD. In other situations this may require continuing training on the new WebCRD system, and NASAA is committed to making that investment.

We are committed to continuing to streamline the broker-dealer registration process while preserving the investor protections that are the hallmarks of our securities markets. To this end, NASAA has a special task force committed to working with industry to reach a mutually agreeable solution and to make recommendations to the NASAA Board of Directors by the end of the first quarter of 2001 on how best to streamline and simplify the registration process in ways that continue to protect investors. NASAA will strive to create a single uniform broker-dealer registration package that works across the U.S. Of course, this doesn't mean that states can't or shouldn't exercise discretion to protect their residents from fraud and abuse.

Further, reflecting our increasingly mobile society, we are committed to exploring uniform cross-border and cross-state line exemptions, so that brokers can service their customers wherever they are. It makes sense that the state where the customer resides will exercise jurisdiction. To help reach this goal, we are committed to drafting a uniform exemption that can be adopted by each state and to spending time in our training sessions on uniformity issues.

The regulation of local offices of broker-dealers is the hallmark of state securities regulation; the point of sale contact between investors and brokers occurs locally and needs to be monitored locally. In this area, we need to strive for more efficiency and to continue to coordinate among the states, with the SEC and self-regulatory organizations on examinations. We will continue to work more with other regulators to share examination schedules, resulting data and the benefits of technology.

State securities regulators already have made much progress in streamlining the regulatory process for broker-dealers, but more can be done. We recognize that good compliance programs have costs associated with them; we are committed to keeping those costs as low as possible, while continuing to protect the interests of investors.

ENFORCEMENT

Enforcement against fraud is the essence of what state securities regulators do. We are here to protect investors and to appropriately sanction and punish those who would harm or defraud investors. Given the growth in the markets and in the number of investors, we must continue to funnel more resources into enforcement. We are committed to continue to make the punishment for committing fraud greater than the benefit of illicit gains. It is fitting and proper for the states

to play this role. The federal investigative agencies, given their focus on problems that are interstate and international, may not be able to take on the case of someone who loses \$10,000 or even \$100,000 to a securities scam artist. NASAA will continue its role of helping states work together on joint enforcement projects such as the highly effective sweeps against firms and individuals committing microcap stock fraud.

State legislatures need to beef up our enforcement resources. State and federal prosecutors rely on local securities agencies for expertise and guidance, help and support. To deliver this support we need additional staffing and resources. We need to be able to attract and retain highly qualified personnel.

As technology changes, we need to keep pace in our responses and strategies. Many of the scams that previously relied on boiler rooms have migrated to the Internet. We need more resources to deal with this growing problem. Clearly, more investor education is needed. We are committed, as always, to cooperate more and share information with other regulatory and law enforcement agencies.

INVESTOR EDUCATION

Educating investors is a crucial function of state securities regulation. We are a nation of shareholders. While state securities regulators aren't teachers, we must be advocates for investor education because we see the consequences of financial illiteracy. Many people become victims because they lack the necessary tools and sophistication to make informed and appropriate investment decisions.

We are committed to increasing our resources to prevent fraud and abuse through outreach, distribution of written materials, web sites and the like. To demonstrate this, last year NASAA created its own investor education section, elevating this area's importance within our organization. We need to raise the bar for investor education at the state level. We always need to strive to use technology, such as the Internet, creatively and effectively as we strive to educate investors of today as well as those of tomorrow. It is critical that we target students in our investor education programs and initiatives. Without basic financial awareness and investment knowledge, our young people will not be prepared for the future personal investment decisions they must make and they will be vulnerable to poor financial advice and fraud.

State regulators can be a source of objective information for investors. As grass-roots regulators, we are uniquely positioned to provide information on scams. We can reach Main Street residents. Some states have dedicated investor education personnel but more are needed. It's important for us to work together with the stock markets, industry, local and national associations and others on investor education outreach efforts.

CORPORATE FINANCE

State securities agencies have long played a role in facilitating capital formation at the state and local level. We can and do help entrepreneurs with their business plans, help them obtain resources to grow their enterprises and create local jobs. We have made big strides toward uniformity in this area in recent years. Virtually all states now accept the Small Company Offering Registration (SCOR) form, an intuitive, fill-in-the-blank form used by entrepreneurs to make required disclosures to investors. Interstate use of this form is coordinated through regions of the country, all provide a lead reviewer who represents all the states in that region. Participating regions include the Northeast Region, the Midwest Region, the Western Region, the Mid-Atlantic Region and the Southwest Region. The remaining region has committed to join the program during the coming year. To facilitate capital formation at the state and federal level, NASAA also developed the Coordinated Equity Review (CER) program to streamline the registration process for larger offerings. Nearly all states take part in the program (CR-Equity), which saves issuers time and money. To build on this success story, we are committed to getting all states to participate in the program. Further, we are committed to expanding the number of states that have adopted the Model Accredited Investor Exemption, an exemption that dovetails with ACE-Net, a system being privatized by the Small Business Administration.

The coordinated review process has potentially much wider applications—not just for equity offerings but for non-profit debt and direct participation programs (DPP). It is our vision that all types of multi-state filings could be covered by coordinated review.

The advantages are obvious: Regulators use pooled resources to take advantage of experience and expertise. The issuer gets the benefit of reduced red tape because it only has to interact with one or two lead states assigned to interface with the applicant. It saves time, gives them a definitive schedule and allows entrepreneurs to plan. And it saves money. The issuer or issuer's counsel, for example, only has to deal with lead states coordinating the review. While utilization of these programs is increasing, we need to spread the word about their efficiencies and further encourage their use.

We are committed to using technology to make it even easier for corporate issuers to raise the money they need to grow their businesses. That means putting more forms like SCOR on the Internet, thereby making them easier to complete and submit. We will aggressively pursue possibilities in which online filings might work for other applications such as mutual fund notice filings. The goals are to get out of the paper environment and to reduce costs and duplication through one-stop, uniform filing systems.

INVESTMENT ADVISER REGULATION

Providing investment advice is the growth industry of the financial services sector. Investors are drowning in information and data; they are clamoring for advice and guidance. Regulation of investment advisers and financial planners is tailor-made for state securities regulators—it's a business that is local in nature. Following enactment of the National Securities Markets Improvement Act of 1996 (NSMIA), states have sole regulatory authority over the smaller investment advisers and all investment adviser representatives.

NASAA, with industry help, developed and implemented the new Investment Adviser Competency Exam (Series 65). We are committed to continuing to foster effective examination programs and oversight of the state-level investment adviser population. This includes both tests for IA representatives and field exams and audits of firms. As the sole regulator of small investment advisers, the states are devoting greater resources to policing this important area and NASAA is providing and will continue to provide relevant staff training and support.

Technology is the key to efficient enforcement in this area, both to uncover and prevent problems. The Investment Adviser Registration Database (IARD) will do for investment advisers and their representatives what WebCRD does for broker-dealers and their agents. This new electronic database will help promote uniformity, through use of common forms, and a paperless environment. Further, it will streamline procedures and promote consistency and help investors research the backgrounds of those who seek the privilege of rendering investment advice. We are committed to adopting and using the IARD. It will be a valuable tool for industry, investors and regulators.

FUNCTIONAL REGULATION AND THE FUTURE

We need to preserve strong and effective securities regulation. State regulators operate at the local level, shining the light on emergent problems--like microcap stock fraud. At the same time we must stay attuned to the regulatory surroundings.

The melding of securities, banking and insurance products and services drove passage of the Gramm-Leach-Bliley Act of 1999 (GLBA). State securities regulators are committed to working with our banking and insurance counterparts to efficiently police this new marketplace—in part through new information-sharing agreements with other functional regulators. GLBA also preserved functional regulation. Functional regulation assures that securities products are regulated by experts in securities. Accordingly, our job, protecting investors, can best be done through preservation of functional regulation at the state level.

For nearly 90 years, state securities regulators have been the experts in the monitoring of the sale of securities products to Main Street investors. We are committed to continuing that proven record--while at the same time adapting to and changing with the times to become even more efficient and effective in regulating the industry and protecting investors.

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