

Testimony of James B. Ropp  
Commissioner, Delaware Division of Securities and  
Chair of the Enforcement Section  
North American Securities Administrators Association, Inc.  
Before the  
United States House Committee on Financial Services

“Federal and State Enforcement of Financial Consumer  
and Investor Protection Laws”

March 20, 2009

Chairman Frank, Ranking Member Bachus, and members of the Committee,

I'm Jim Ropp, Delaware Securities Commissioner and Chair of the Enforcement Section of the North American Securities Administrators Association, Inc. (NASAA).<sup>1</sup> I appreciate the opportunity to focus on the role of state securities regulators in the current economic crisis, and to provide you with recommendations to enhance our ability to pursue financial fraud and prosecute the perpetrators of those crimes.

### Overview

The securities administrators in your states are responsible for enforcing state securities laws, licensing firms and investment professionals, registering certain securities offerings, examining broker-dealers and investment advisers, and providing investor education programs and materials to your constituents. Ten of my colleagues are appointed by state Secretaries of State, such as Secretary Galvin; five, like me, fall under the jurisdiction of their states' Attorneys General; some are independent commissions and others are appointed by their Governors and Cabinet officials. By nature, we are the first line of defense for Main Street investors and for us, enforcement is a top priority.

My own state of Delaware has a somewhat unique situation with regard to enforcement actions. Since it is a small state, historically all state criminal prosecutions are brought by the State Attorney General. There are no county District Attorneys. Since the Delaware Securities Division is part of the Delaware Attorney General's office, we have statutory jurisdiction over administrative, civil and criminal actions to address securities fraud. Unlike most state securities administrators, we do not have to refer our state criminal actions to an independent prosecutorial agency. This allows us more freedom to

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<sup>1</sup> 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, the U.S. Virgin Islands, Canada, Mexico and Puerto Rico. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

pursue offenders criminally and we do not shy away from bringing criminal cases. This is consistent with our philosophy that most Ponzi schemes are basically cases of criminal theft and securities fraud. We recently indicted a Ponzi scheme operator who was offering investments in fraudulent real estate deals. He was under investigation in a number of states and by at least one federal agency. Delaware was the first to indict. In another case, Delaware indicted a broker who had defrauded a senior citizen out of more than \$200,000. The broker created a fictitious account at a different brokerage house and diverted funds from the client's account into the fictitious account. Shortly thereafter, the broker withdrew the money and left the country. Warrants are outstanding and we are attempting to locate him to secure his extradition to the United States. In short, criminal prosecution is an important tool for effective enforcement of state and federal securities laws.

Delaware obtains its cases from a number of sources. The primary source of securities cases come from investor complaints about either a financial professional or an unregistered fraud artist who has offered or sold them a fraudulent investment opportunity. We also obtain cases from branch office examinations, referrals from local law enforcement agencies, referrals from other states, NASAA working groups, the Securities Exchange Commission (SEC) and FINRA. Like my colleagues in all 50 states, I see what happens when dreams are destroyed by con artists who aggressively target senior citizens who have saved for retirement and families who are saving for college expenses.

### **State Securities Enforcement**

State securities regulators have a century-long record of investor protection, and NASAA has long supported that effort. Within NASAA, for example, the Enforcement Section helps coordinate large, multi-state enforcement actions by facilitating the sharing of information and leveraging the limited resources of the states more efficiently. Members of this Section also help identify new fraud trends such as those promising high returns in today's down market, and they act as points of contact for other federal agencies and the self-regulatory organizations (SROs).

State securities regulators respond to investors who typically call them first with complaints, or request information about securities firms or individuals. They work on the front lines, investigating potentially fraudulent activity and alerting the public to problems. Because they are closest to the investing public, state securities regulators are often first to identify new investment scams and to bring enforcement actions to halt and remedy a wide variety of investment related violations. The \$60 billion returned to investors to resolve the demise of the Auction Rate Securities (ARS) market is the most recent example of the states initiating a collaborative approach to a national problem.

Mr. Chairman, we appreciate your affirmation during last year's ARS hearing that ***“in a number of states, it has been the state securities officials and law enforcement officials that have taken the lead.”*** Attached to my testimony is a chart, *“States, On the Frontlines of Investor Protection,”* which illustrates many examples where the states initiated investigations, uncovered illegal securities activity, then worked with federal regulators or with Congress to achieve a national solution.

These high profile national cases receive greater public attention, but they should not obscure the more routine and numerically much larger caseload representing the bulk of the states' enforcement work. Those cases affect everyday citizens in local communities across the country. In the past three months alone, the Washington State Division of Securities, working with the Federal Bureau of Investigation and the IRS Criminal Investigation Division, broke up a \$65 million oil and gas investment Ponzi scheme; Hawaii's securities commissioner, with the assistance of the SEC and CFTC, shuttered a suspected Ponzi scheme targeting the deaf community in Hawaii, parts of the mainland and Japan; an investigation by the Texas State Securities Board resulted in a 60-year prison sentence for a Ponzi scheme operator who stole at least \$2.6 million from investors; and the Arizona Corporation Commission stopped a religious affinity fraud ring and ordered more than \$11 million returned to investors. Since January 1, 2009, the Alabama Securities Commission has announced the conviction of nine different individuals convicted of securities fraud. These convictions encompass cases of fraud and abuse ranging from a classic Ponzi scheme to violations of Regulation D, Rule 506.

All convictions and charges are felonies. Currently, in the State of Alabama, the Securities Commission has twenty-seven defendants awaiting trial for securities fraud in nineteen separate cases.

Our proximity to individual investors puts us in the best position, among all law enforcement officials, to deal aggressively with securities law violations. Just one look at our enforcement statistics shows the effectiveness of state securities regulation. During our three most recent reporting periods, ranging from 2004 through 2007, state securities regulators have conducted more than 8,300 enforcement actions, which led to \$178 million in monetary fines and penalties and more than \$1.8 billion ordered returned to investors. And, we are responsible for sending fraudsters away for a total of more than 2,700 years in prison.

In spite of the states' success, a series of large scale financial frauds have rocked the capital markets since 2000. We are grateful that you have called this timely hearing to determine what actions would strengthen the states' enforcement capabilities, assist defrauded investors, and deter this type of illegal activity in the future.

### **Impediments to State Securities Regulation**

In thinking about the role of state and federal enforcement authorities, it is instructive to look back at the regulatory responses to the major financial scandals over the past decade. From the investigation into the role of investment banks in the Enron fraud, to exposing securities analyst conflicts, "market timing" in mutual funds, and the recent ARS cases, state securities regulators have consistently been in the lead. Indeed, in some cases, at the time the states began their investigations, it was unclear whether the federal regulators intended to pursue any investigation at all. There have been numerous accounts in the press and in academic journals detailing the criticism of the SEC for its failure to investigate fraud allegations as quickly as state regulators.<sup>2</sup>

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<sup>2</sup> See, e.g., Susan Antilla, *Bankers Would Love to Kneecap State Regulators*, Bloomberg News, Nov. 14, 2008 ("This year, regulators from Massachusetts and 11 other states brought cases against major banks and

State securities regulators are often first to discover and investigate our nation's largest frauds. When we bring enforcement actions pursuant to these investigations, the penalties states impose are more meaningful and the restitution component is significantly greater. In fact, it has been shown that in cases where state and federal regulators work cooperatively, the more aggressive actions of state securities regulators cause a significant increase in the penalty and restitution components of the federal regulator's enforcement efforts.<sup>3</sup>

And yet, over a number of years there has been a concerted industry assault on state securities regulation, with calls for the preemption of both state regulation and enforcement. For example, in 1996, the National Securities Markets Improvement Act (NSMIA) did preempt much of the states' regulatory apparatus for securities traded in national markets, and although it left state anti-fraud enforcement largely intact, it limited the states' ability to address fraud in its earliest stages before massive losses have been inflicted on investors.

A prime example is in the area of private offerings under Rule 506 of Regulation D. Even though these securities do not share the essential characteristics of the other national securities offerings addressed in NSMIA, Congress nevertheless precluded the states from subjecting them to regulatory review. These offerings also enjoy an exemption from registration under federal securities law, so they receive virtually no

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securities firms that had marketed auction-rate securities to investors as "safe," only to see that market collapse. The states negotiated agreements that got customers' money back. The SEC hopped on those auction-rate cases after the tough work already had been done"); Gretchen Morgenson, *Call In the Feds. Uh, Maybe Not*, The New York Times, Feb. 29, 2004 (the SEC's failure to protect investors in Washington State is Exhibit A for why state regulators should stay in the oversight mix); Editorial, *Wall Street and the States*, The Washington Post, Wednesday, July 23, 2003 ("ANYONE WHO'S WATCHED the scandals that engulfed Wall Street over the past few years understands the importance of the role played by state officials in going after corporate wrongdoing. While the Securities and Exchange Commission snoozed, New York state Attorney General Eliot L. Spitzer led the way in cracking down on firms whose stock analysts simultaneously evaluated companies for investors and milked them for investment banking business."); Susanne Craig, *Local Enforcers Gain Clout on Street*, The Wall Street Journal, June 21, 2002 ("States have stepped up to fill the void' left by what some perceive to be weak federal regulators, says John Coffee, a U.S. securities-law professor at Columbia University.")

<sup>3</sup> Eric Zitzewitz, *An Eliot Effect? Prosecutorial Discretion in Mutual Fund Settlement Negotiations*, 2003-7, [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1091035](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1091035).

regulatory scrutiny. Thus, for example, NSMIA has preempted the states from prohibiting Regulation D offerings even where the promoters or broker-dealers have a criminal or disciplinary history. Some courts have even held that offerings made under the guise of Rule 506 are immune from scrutiny under state law, regardless of whether they actually comply with the requirements of the rule. *See, e.g., Temple v. Gorman*, 201 F. Supp. 2d 1238 (S.D. FL. 2002).

As a result, since the passage of NSMIA, we have observed a steady and significant rise in the number of offerings made pursuant to Rule 506 that are later discovered to be fraudulent. Further, most hedge funds are offered pursuant to Rule 506, so state securities regulators are prevented from examining the offering documents of these investments, which represent a huge dollar volume. Although Congress preserved the states' authority to take enforcement actions for fraud in the offer and sale of all "covered" securities, including Rule 506 offerings, this power is no substitute for a state's ability to scrutinize offerings for signs of potential abuse and to ensure that disclosure is adequate *before* harm is done to investors. In light of the growing popularity of Rule 506 offerings and the expansive reading of the exemption given by certain courts, NASAA believes the time has come for Congress to reinstate state regulatory oversight of all Rule 506 offerings by repealing Subsection 18(b)4(D) of the Securities Act of 1933.

And, there have been more recent attempts to preempt state regulation, resulting in a strain between federal and state regulators. In some instances, state investigations into corporate abuses that federal officials missed resulted not in reform at the federal level, but in criticism of the states. Some federal agencies have responded by issuing regulations broadly preempting state law.<sup>4</sup> Federal agencies have also aggressively

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<sup>4</sup> *See* Office of Comptroller of the Currency, Investment Securities: Bank Activities Operations; Leasing, 66 Fed. Reg. 34784, 34788 (2001); *see also* Office of Comptroller of the Currency, Notice: Preemption Determination and Order, 68 Fed. Reg. 46264 (Aug. 5, 2003) (declaring state Consumer Protection laws dealing with mortgage lenders preempted); *see also* Office of Thrift Supervision Opinion Letter No. P-2004-7, "Authority of a Federal Savings Association to Perform Banking Activities through Agents Without Regard to State Licensing Agreements" 10 (Oct. 25, 2004), *available at* <http://www.ots.treas.gov/docs/5/560404.pdf>.

moved to preempt state law by bringing suit against state officials.<sup>5</sup> It is troubling that states are now facing efforts to preempt state authority through federal rules and regulations that ignore clear statements of Congressional intent. States now find themselves engaged in a battle with certain federal authorities simply to retain the authority to protect the interests of investors and consumers.

These calls for preemption or for more SRO authority at the expense of state jurisdiction defy common sense, if only because the evidence clearly demonstrates that the state-federal regulatory structure actually works for the investor. State involvement drives the performance level of all participants upwards and provides protection against the possibility of regulatory capture.

### **Recommendations**

**Resources.** There are a number of legislative proposals now pending to significantly increase funding for federal law enforcement agencies responsible for investigating and prosecuting financial fraud. NASAA supports these efforts, but, at the same time, urges Congress to consider establishing a federal grant program to assist State law enforcement agencies, including securities divisions, involved in the prevention, investigation and prosecution of certain financial crimes. State securities regulators have the determination, willpower and experience to pursue perpetrators of financial crime. We've learned how to accomplish more with less. However, there's little doubt that additional resources would enhance our ability to uncover and prosecute securities fraud during this economic downturn, which has resulted in vulnerable investors looking to recover their losses.

One innovative approach proposed last year is S. 2794, the "Senior Investor Protection Act of 2008." Introduced by Senator Herb Kohl (D-WI), it would make grant funding

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<sup>5</sup> *State Farm Bank, FSB v. Reardon*, No. 07-4260 (Aug. 22, 2008), (Opinion Letter from the Chief Counsel for the Office of Thrift Supervision effective to preempt state law as it affects exclusive agents for a federal thrift) *See also*, *State Farm Bank v. Reardon*, --- F.3d ---, 2008 WL 3876196 (6th Cir. Aug. 22, 2008)



available to states that adopt NASAA's model rule prohibiting the misleading use of "senior designations," which are titles that unscrupulous agents often used to defraud senior investors. The bill addresses a serious form of elder abuse while at the same time making significant funding available to the states for enforcement.

The current levels of funding for law enforcement agencies is low, given the billions upon billions of dollars being used to shore up distressed banks and other institutions, some of which undoubtedly contributed to the current financial crisis through illegal or reckless behavior. Increasing enforcement and more effectively deterring fraud is vastly more cost effective than trying to compensate victims and repair the damage to our economy once the frauds have occurred.

**Securities Prosecutions.** In many states, the attorney general, county attorney or district attorney may request that a duly employed attorney of a state securities division be appointed a special prosecutor to prosecute or assist in the prosecution of criminal violations on behalf of the state. These special prosecutors have all the powers and duties prescribed by law for assistant attorneys general or assistant district attorneys, but they don't technically have full independent prosecutorial authority. As a practical matter, deputizing a state securities attorney gives the local prosecutors and the state Attorney General the ability to formally utilize the expertise of the state securities division attorney in prosecuting complex securities cases. This is a valuable leveraging of talent and resources and should be encouraged in all jurisdictions and at the federal level.

**Remedies.** The nature and extent of the unlawful conduct occurring in our financial markets today requires that Congress thoroughly review all of the civil and criminal remedies that apply in all sectors to ensure they more effectively deter misconduct.

In 1990, Congress granted the SEC its first comprehensive authority to seek monetary penalties in both administrative and civil enforcement actions for violations of the securities laws. For the most serious or "third tier" offenses, penalties for each violation

may be up to, but not more than, \$100,000 for natural persons and \$500,000 for entities.<sup>6</sup> It does not appear that these penalty amounts are high enough, at least relative to the scope of the fraud still evident in our markets.

In 2002, Congress substantially increased the criminal penalties under the 1934 Act.<sup>7</sup> Fines rose to a maximum of \$5 million for individuals and \$25 million for entities, and jail terms rose to a maximum of 20 years. These criminal penalties have not had the deterrent effect that one might expect.

The effectiveness of stronger sanctions hinges in large part on the willingness of regulators to use them. In 2006, the SEC issued a release explaining the factors that it considers when determining the appropriate monetary penalty to seek against a corporate wrongdoer. *See* “Statement of the Securities and Exchange Commission Concerning Financial Penalties,” SEC Release 2006-4 (Jan. 4, 2006). While that release includes some helpful guidance, it also reflects an attitude of restraint in the use of monetary sanctions, especially where the impact on corporate shareholders may be adverse. If Congress provides federal regulators with better enforcement tools, then it is equally important that regulators use them aggressively.

State securities regulators have served a leading role in the fight against senior investment fraud since first focusing national attention on the issue in 2003. Given the number of baby boomers moving toward retirement who are watching their hard-earned investment portfolios decline in value, it is important that state securities regulators work together with Congress to protect those who will be the most vulnerable to investment fraud. We believe legislation to enhance penalties against perpetrators of securities fraud against seniors will assist law enforcement and regulators to ensure that those who take advantage of our nation’s elderly will be held accountable. Fraudulent investment sales to seniors will remain a problem of epidemic proportions as long as the benefits to the perpetrators outweigh the costs. It’s for that reason that NASAA supports the Senior

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<sup>6</sup> *See* 15 U.S.C. Sec. 78u (codifying provisions of the Securities Enforcement Remedies and Penny Stock Reform Act).

<sup>7</sup> *See* The Sarbanes-Oxley Act of 2002, Sec. 1106 (codified at 18 U.S.C. Sec. 1513).

Investor Protection Act that was introduced in 2008 and will be working toward its introduction and passage in both the Senate and House during the 111<sup>th</sup> Congress.

**Reexamine and Remove Hurdles Facing Private Plaintiffs.** Private actions are the principal means of redress for victims of securities fraud, but they also play an indispensable role in deterring fraud and complementing the enforcement efforts of government regulators and prosecutors. Congress and the courts alike have recognized this fact. The Senate Report accompanying the Private Securities Litigation Reform Act of 1995 (PSLRA) described the importance of private rights of action as follows:

The SEC enforcement program and the availability of private rights of action together provide a means for defrauded investors to recover damages and a powerful deterrent against violations of the securities laws. As noted by SEC Chairman Levitt, “private rights of action are not only fundamental to the success of our securities markets, they are an essential complement to the SEC’s own enforcement program.” [citation omitted]<sup>8</sup>

The problem, of course, is that over the last 15 years, Congress and the Supreme Court have restricted the ability of private plaintiffs to seek redress in court for securities fraud. These restrictions have not only reduced the compensation available to those who have been the victims of securities fraud, they have also weakened a powerful deterrent against misconduct in our financial markets.

For example, in the PSLRA, Congress imposed stringent pleading requirements and other limitations on plaintiffs seeking damages for fraud under the securities acts. The intent of the Act was to protect companies from frivolous lawsuits and costly settlements. Many observers, however, believe that PSLRA has placed unrealistic burdens on plaintiffs with meritorious claims for damages.

The Supreme Court has compounded the problem by issuing decisions that further limit the rights of private plaintiffs in two important ways. The Court has narrowed the class

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<sup>8</sup> See S. Rep. No. 104-98, at 8 (1995), *reprinted in* 1995 U.S.C.C.A.N. 679, 687; *see also Basic Inc. v. Levinson*, 485 U.S. at 230-31 (observing that the private cause of action for violations of Section 10(b) and Rule 10b-5 constitutes an “essential tool for enforcement of the 1934 Act’s requirements”).

of wrongdoers who can be held liable in court, and at the same time, it has expanded the pleading burdens that plaintiffs must satisfy to survive immediate dismissal of their claims. As Justice Stevens lamented in his dissent in *Stoneridge*, the Court has been on “a continuing campaign to render the private cause of action under Section 10(b) toothless.”<sup>9</sup>

In short, the pendulum has swung too far in the direction of limiting private rights of action. Congress should therefore hold hearings to examine whether private plaintiffs with claims for securities fraud have fair access to the courts. In that process, Congress should re-evaluate the Private Securities Litigation Reform Act and should furthermore consider reversing some of the Supreme Court’s most anti-investor decisions. One case that undoubtedly deserves to be revisited is the Court’s holding in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 114 S.Ct. 1439 (1994). The Court ruled that the private right of action under Section 10(b) of the Securities Exchange Act of 1934 cannot be used to recover damages from those who aid and abet a securities fraud, only those who actually engage in fraudulent acts. The Court’s decision insulates a huge class of wrongdoers from civil liability for their often critical role in support of a securities fraud.

Other cases that warrant legislative re-evaluation include *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, 128 S. Ct. 761, 779 (2008) (severely limiting the application of Section 10(b) in cases involving fraudulent conduct); and *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 127 S. Ct. 2499 (2007) (establishing burdensome requirements for pleading scienter).

It bears repeating that removing excessive restrictions on access to the courts would not only provide more fair and just compensation for investors, it would also benefit regulators by restoring a powerful deterrent against fraud and abuse: the threat of civil liability.

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<sup>9</sup> *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, 128 S. Ct. 761, 779 (2008).

## **State/Federal Coordination**

State securities regulators welcome the opportunity to work with our regulatory counterparts at the SEC and the SROs to collectively use our resources to protect investors. To facilitate communication and coordination on all financial services issues, NASAA believes the President's Working Group on Financial Markets should be expanded to include representatives from the state agencies that regulate banking, insurance, and securities.

Our current coordination and cooperation ranges from statutorily mandated meetings to working cases together to informal information sharing networks. NASAA and the SEC cosponsor an annual Conference on Federal-State Securities Regulation in accordance with Section 19(d) of the Securities Act of 1933. As part of the conference, representatives from the SEC and NASAA divide into working groups in the areas of enforcement, corporation finance, broker-dealer regulation, investment advisers, and investor education. Each group discusses methods to enhance cooperation in its subject area and to improve the efficiency and effectiveness of federal and state securities regulation.

As the NASAA Enforcement Chair, I have attended meetings of the Securities and Commodities Fraud Working Group, which is an informal association of law enforcement departments and regulatory agencies at the federal, state, and international levels. Organized under the auspices of the Justice Department in 1988, the Group seeks to enhance criminal and civil enforcement of securities and commodities laws through meetings and other information sharing activities that include discussions of current developments, and presentations on specific topics such as a major cases, sting operations, or policy initiatives.

NASAA is also a participant in the National Examination Summits. These are quarterly meetings attended by representatives from NASAA, the SEC, and FINRA in which complaint data and trends are shared and discussed. The information shared at these

meetings often results in cross-referrals for potential enforcement action or scheduling of joint examinations.

Several years ago, NASAA accepted an invitation from the U.S. Treasury Department to become a member of the Financial and Banking Information Infrastructure Committee (FBIIC), which is sponsored by President's Working Group on Financial Markets. As an active FBIIC member, NASAA helps coordinates public-sector efforts to improve the reliability and security of the U.S. financial system. FBIIC also develops procedures and systems to allow federal and state regulators to communicate among themselves and with the private sector during times of crisis.

NASAA also serves as a member of the Federal Reserve's Cross-Sector Group. The group's bi-annual meetings are hosted by the Federal Reserve and include representatives from the state and federal banking, insurance and securities regulators.

As you know, investment fraud knows no borders. That's why state and provincial securities agencies, through NASAA, have reached out to their colleagues in the international arena. NASAA plays an active role in the International Organization of Securities Commissioners (IOSCO) and the Council of Securities Regulators of the Americas (COSRA).

### **Conclusion**

The unique experiences of state securities regulators on the front lines of investor protection have provided the framework for my testimony. As the regulators closest to investors, state securities regulators provide – and must be allowed to continue to provide – an indispensable layer of protection for Main Street investors.

## States: On the Frontlines of Investor Protection

<b>PROBLEM: \$2 billion/yr. Losses in Penny Stocks</b>	
<b>State Initiative</b>	<b>1989:</b> States determined penny stock offerings by newly formed shell companies to be per se fraudulent. These “blank check” companies had no business plan except a future merger with an unidentified company.
<b>National Response</b>	<b>1990:</b> Congress passed Penny Stock Reform Act, which mandated SEC to adopt special rules governing sale of Penny Stocks (<\$5.00 per share) and public offerings of shares in blank check companies (SEC Rule 419).
<b>PROBLEM: \$6 billion/yr. Losses in Micro-cap Stocks</b>	
<b>State Initiative</b>	<b>1996-97:</b> 33 States participated in sweep of 15 broker-dealer firms that specialized in aggressively retailing low priced securities to individual investors. States found massive fraud in firms’ manipulation of shares of start-up companies, most of which had no operating history.
<b>National Response</b>	<b>1997-98:</b> Congress held hearings on fraud in the micro-cap securities markets (shares selling between \$5-10). <b>2002:</b> Congress passed Sarbanes-Oxley Act, which made certain state actions a basis for federal statutory disqualification from the securities industry.
<b>PROBLEM: Risks of Securities offerings on the Internet</b>	
<b>State Initiative</b>	<b>1996-97:</b> States issued uniform interpretative guidance on use of Internet for legitimate securities offerings and dissemination of product information by licensed financial services professionals.
<b>National Response</b>	<b>1998:</b> SEC issued interpretative guidance based on the States’ Model on the use of Internet for securities offerings and dissemination of services and product information by licensed financial services professionals.
<b>PROBLEM: Risks of Online Trading</b>	
<b>State Initiative</b>	<b>1999:</b> In a report on trading of securities on the Internet, States found that investors did not appreciate certain risks, including buying on margin and submitting market orders.
<b>National Response</b>	<b>2001:</b> SEC approved a new NASD rule requiring brokers to provide individual investors with a written disclosure statement on the risks of buying securities on margin.
<b>PROBLEM: Risks of Day Trading</b>	
<b>State Initiative</b>	<b>1999:</b> In a report on individuals engaged in day trading, States found that day trading firms failed to tell prospective investors that 70% of day traders would lose their investment while the firm earned large trading commissions.
<b>National Response</b>	<b>2000:</b> SEC approved new NASD rules making day trading firms give written risk disclosure to individual investors. <b>2001:</b> SEC approved new NASD and NYSE rules governing margin extended to day traders.
<b>PROBLEM: Research Analyst Conflict of Interest</b>	
<b>State Initiative</b>	<b>2002-03:</b> States investigated and helped focus attention on conflicts of interest between investment analysts and major Wall Street firms.
<b>National Response</b>	<b>2002-03:</b> The SEC, NASD, NYSE, and states reached a landmark \$1.4 billion global settlement and firms agree to reform practices.
<b>PROBLEM: Illegal Mutual Fund Trading Practices</b>	
<b>State Initiative</b>	<b>2003:</b> States uncovered illegal trading schemes that had become widespread in the mutual fund industry.
<b>National Response</b>	<b>2003-2004:</b> SEC, NASD and NYSE launch investigations; reform legislation introduced in Congress but fails to gain support; SEC initiates wide-ranging effort to reform certain fund regulations.
<b>PROBLEM: Senior Investment Fraud</b>	
<b>State Initiative</b>	<b>2008:</b> After calling attention to widespread fraud against senior investors, NASAA members approved a model rule prohibiting the misleading use of senior and retiree designations and numerous states have adopted the model through legislation or regulation.
<b>National Response</b>	<b>2008:</b> Sen. Herb Kohl, chair of the U.S. Senate Special Committee on Aging, introduced legislation that would provide grants to states to enhance the protection of seniors from being misled by false designations.
<b>PROBLEM: Auction Rate Securities</b>	
<b>State Initiative</b>	<b>2008:</b> Based on investor complaints, states launched a series of investigations into the frozen market for auction rate securities. The investigations led to settlements with 11 major Wall Street firms to return \$50 billion to ARS investors.
<b>National Response</b>	<b>2006:</b> SEC looked into underwriting and sales practices of auction rate securities. While it did discover and try to remedy certain manipulative practices, the SEC failed to identify or correct fundamental conflicts of interest and self dealing that pervaded the auction rate market.

SOURCE: North American Securities Administrators Association

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