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NASAA Insight

The Voice of State & Provincial Securities Regulation

NASAA

> *"You've done a great job here in the United States and in the provinces of bringing things together and being well aware of the ... changing need for regulation. Keep that process going forward, and join us all internationally to do the same thing."*
>
> **U.S. Representative Paul Kanjorski D-PA,**
> *Commending NASAA for its approach to regulatory reform*

'09 Spring Policy Conference Showcases Ideas for Reform

NASAA members convened in Washington, D.C., on April 28 to host the 24th annual Spring Policy Conference. The conference engaged lawmakers, federal securities regulators, industry representatives, academics, and the media in a vibrant discussion of policy proposals to strengthen regulatory safeguards for Main Street investors.

"With Madoff, meltdowns, and market instability dominating the headlines, the investing public has had enough and is turning to both the industry and policymakers for answers," said NASAA President and Colorado Securities Commissioner Fred Joseph.

U.S. Rep. Paul Kanjorski (D-PA), who serves on the House Financial Services Committee and chairs its capital markets subcommittee, delivered the keynote address, commending NASAA for its collaborative approach to regulatory reform.

U.S. Rep. Paul Kanjorski (D-PA) delivers the keynote address at NASAA's 2009 Public Policy Conference in Washington, D.C., in April.

"You've done a great job here in the United States and in the provinces of bringing things together and being well aware of the changes that are moving out there and the changing need for regulation," he said. "Keep that process going forward, and join us all internationally to do the same thing."

The conference also featured two panel discussions on possible solutions to the major challenges facing the financial services regulatory structure.

Special Report p. 4 >>

NASAA to Obama: Limiting Preemption Protects Investors

The Obama administration affirmed the vital role that state securities regulators play in protecting American investors with a May 20 directive reining in the anti-investor preemption policies of previous administrations.

NASAA commended President Obama in a June 9 letter for recognizing that states have frequently been more aggressive than the federal government in protecting the public's interest.

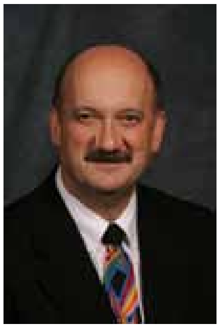
"Our members enjoy a unique proximity to investors and to the industry participants within their state borders," NASAA President and Colorado Securities Commissioner Fred Joseph wrote in the letter to White House. "As a result, state securities regulators are often the first to investigate and uncover our nation's latest and most damaging frauds."

Over a number of years, Congress and previous administrations have sought to preempt state regulation. For example, in 1996, Congress passed the National Securities Markets Improvement Act (NSMIA), which dramatically curtailed the authority of state securities regulators to oversee many aspects of the securities markets, ranging from private offerings under Regulation D to investment advisers with over $25 million in assets under management.

As the Obama administration's recent directive recognizes, federal agencies compounded the problem by extending the scope of preemption beyond congressionally intended boundaries and in ways that pose serious threats to investor and consumer protections under state law.

NASAA's letter urged the president to continue to support the enormous value of state regulation in our system of federalism as the administration moves forward with financial services regulatory reform proposals.

President's Message: Fred Joseph



The NASAA membership gathered in Washington, D.C., for our 24th annual Spring Policy Conference at a crucial moment for the financial services regulatory regime. Our April 28 meeting brought state securities regulators, our federal counterparts, lawmakers, industry, and media together at the height of the reform debate to engage in a constructive dialogue about the next generation of financial services regulation (see p. 4).

As I said when we last met for our annual conference in September, all of us – regulators and industry alike – are on a mission to serve the best interests of investors. Our mission has become more daunting amid the increasing challenges of a faltering economy. We have all been affected by layoffs and tightening budgets, but I am heartened by the proactive steps we have taken along the road to reform and recovery.

NASAA has called upon Congress to take bold actions to better protect Main Street investors (see p. 6). Through congressional testimonies and our 2009 legislative agenda, NASAA has advocated strengthening investor protection, restoring state authority in certain areas, and providing greater transparency and accountability for those in the financial services industry who share responsibility for the prosperity and safety of investors.

As the securities regulators closest to investors, our top policy priority is to preserve and enhance our investor protection role. The membership's dedicated work on the front lines of investor protection ensures that our voices are heard in the crowded policy debate over financial services regulatory reform. I was honored recently to recognize an example of this dedication by presenting the NASAA Distinguished Service Award to Benette Zivley of the Texas State Securities Board for his tenacious efforts to assist investors harmed by auction rate securities and for the expertise he has shared selflessly with our Broker-Dealer Operations Project Group.

From left: NASAA President Fred Joseph, Benette Zivley, and President-elect Denise Voigt Crawford.

What's Inside

Executive Director's Message: Russ Iuculano

With the June 17 release of the Obama administration's sweeping plan to overhaul financial regulation, it is clear that a key element of the new system is how to address systemic risk. On May 19, NASAA, NAIC, and CSBS delivered a joint letter to the leadership of the Senate Banking Committee and House Committee on Financial Services recommending that any framework established to identify and manage systemic risk should be carried out by a collaborative council made up of federal and state regulators, rather than a single agency (see p. 7).

The need for state regulators to be involved in any systemic risk model developed by Congress was underscored at NASAA's Public Policy Conference during a panel consisting of state securities, insurance, and banking regulators (see p. 4). The panelists emphasized that managing systemic risk can only be achieved by combining the efforts of state and federal regulators.

NASAA is committed to working with Congress, the administration, and our state regulatory counterparts to ensure that any remedy aimed at mitigating systemic risk recognizes the expertise and value added by state regulators and avoids the dangers associated with consolidating power in any one federal entity.

United Against Investment **Fraud**

NASAA is preparing a new investor education program, United Against Investment Fraud, to provide members of unions and employee associations with the information they need to protect themselves from investment fraud.

"Now more than ever workers are searching for ways to shore up their finances while watching their pensions decline during the economic downturn. This is no time to lose your money to investment fraud," said NASAA President and Colorado Securities Commissioner Fred Joseph.

Members of unions or employee associations can be susceptible to affinity fraud, a type of scam that targets members of a specific demographic. The UAIF program is designed to fight affinity fraud with outreach to workers—whether they are members of unions or other types of professional associations.

Developed by the NASAA Investor Education Section's Affinity and Military Outreach Project Group, the program will teach union members how to spot con artists and how to get a background check on their stock broker or investment adviser. NASAA members will provide unbiased representatives to make presentations to help union members understand the financial challenges they face.

ARS Update

NASAA Launches Online Resource to Guide Investors Through ARS Arbitration Process

NASAA launched a new webpage to guide investors seeking damages through a special arbitration process created as part of the recent settlements reached with several major Wall Street firms.

To date, the state-led ARS settlements have led to the return of more than $60 billion to ARS investors. The settlements provide for a "special arbitration procedure" that may be used by customers seeking to recover consequential damages. Investors who have ARS-related disputes with their brokerage firms also may pursue those claims through the standard arbitration process governed by the industry's self-regulatory body, FINRA. The webpage outlines the differences in the two arbitration options and provides step-by-step guidelines.

The online ARS Arbitration Information Center is available at the following link: *www.nasaa.org/Issues___Answers/Auction_Rate_Securities/*.

Tune In

NASAA President's PBS Appearance Shares Reform Agenda with Main Street Investors

NASAA President Fred Joseph provided guest commentary for the March 17 edition of PBS Nightly Business Report.

"As Washington works to transform the financial services regulatory system, we must stay focused on the ultimate goal of restoring the trust and protecting the security of Main Street investors," Joseph said. "State securities regulators have a century- long record of investor protection and should play a pivotal role in the next generation of financial services regulation.

"Some have called for a new federal bureaucracy to oversee the nation's financial industry and markets. But one size doesn't fit all — a large, consolidated federal regulator is no substitute for an accessible, proactive presence in communities nationwide.

"As the regulators closest to investors, state securities regulators provide indispensable investor protections through enforcement, licensing, compliance examinations, and financial literacy programs.

"That's smart, strong regulation — the kind that investors deserve."

In a separate appearance on Fox Business News, Joseph spoke of the vital investor protection role NASAA members serve. NASAA Enforcement Section Chair Jim Ropp made similar remarks in an interview on Bloomberg Television.

Click On

NASAA Develops YouTube Channel to Reach Investors in the New Age of Social Media

NASAA recently launched a YouTube channel to reach an ever-growing audience that seeks its news and information from non-traditional media sources.

"Through YouTube, we can take our message of the important investor protection role of NASAA members directly to the public," said NASAA President and Colorado Securities Commissioner Fred Joseph.

NASAA joined four members — The British Columbia Securities Commission, Washington Department of Financial Institutions, New Brunswick Securities Commission, and the Kentucky Office of Financial Institutions — to take advantage of YouTube to help increase investor awareness of their programs and activities.

NASAA's YouTube channel links to these channels and provides a blend of investor awareness and policy-related videos. NASAA's YouTube channel is available at the following link: *http://www.youtube.com/user/NASAAdotORG.*

Exploring the **Causes** and the **Cures**

With Madoff, meltdowns, and market instability dominating the headlines, NASAA assembled a group of regulators and academics to discuss financial services regulatory reform and systemic risk at the April 28 Spring Policy Conference.

Steve Irwin, Pennsylvania Securities Commissioner and NASAA's Policy Conference Chair, opens NASAA's panel on restoring investor confidence. Panelists from left: Moderator James Cox, Duke University securities law professor; Mark Cooper, research director for the Consumer Federation of America; Missouri Securities Commissioner Matt Kitzi; and Donald Langevoort, securities law professor at Georgetown School of Law.

Boosting Investor Confidence

Duke University securities law professor James Cox moderated the first panel, "Answering an Angry Public: Restructuring Our Regulatory System and Restoring Investor Confidence." The panelists included Missouri Securities Commissioner Matt Kitzi; Mark Cooper, research director for the Consumer Federation of America; and Donald Langevoort, securities law professor at Georgetown School of Law.

Cox directed the panel to explore "the causes and the cures" of the investing public's declining faith in the markets. A strong consensus emerged that investors prefer to turn to state securities regulators, their first line of defense.

The public puts a great deal of trust in their state securities regulators, Matt Kitzi said. "We're not an obscure, tucked-away agency," he explained. "We live in the communities that we regulate."

Investors want accountability, he said. "(NASAA members) are a known entity that investors expect something from. That's what drives the good results that we're able to provide."

Mark Cooper of the CFA also highlighted the need for strong state securities regulation to boost investor confidence. "We made a big mistake taking the state regulators off the beat," he said. "We can never again trust a federal regulator to do the job alone."

Georgetown's Langevoort pointed to three factors that contributed to the meltdown: lack of resources, individuals who flouted securities laws, and federal regulators' hesitancy to litigate tough cases.

"We are at a place where the United States has seriously under-invested in the task of regulation," Langevoort said, calling for "all the help you can get," including state involvement.

Cooper advocated a return to New Deal-style regulation and offered straight-forward regulatory solutions to the main culprits of the financial meltdown.

Instead of propping up those organizations that are too big to fail, "we will simply make it too expensive to be too big," with large capital and insurance requirements," Cooper said.

Cooper suggested reinstating the Glass-Steagall Act and banning certain financial products such as derivatives.

The panel addressed the ineffectiveness of a principles-based approach to regulation of the huge financial services industry, as well as the need to regulate institutions on the basis of the function they serve, not the form they take.

Controlling Systemic Risk

The second panel of the conference, "Risky Business: Rebuilding Market Integrity through Systemic Risk Regulation," was moderated by Joe Borg, Director of the Alabama Securities Commission. The panelists included Dean Shahinian, senior counsel for the Senate Banking Committee; Montana Commissioner of Insurance and Securities Monica Lindeen; and Sarah Bloom Raskin, Maryland Commissioner of Financial Regulation.

Shahinian outlined the merits of various ways to monitor systemic risk, including the approach subsequently advanced by the Obama Administration to centralize this responsibility within the Federal Reserve. Another approach, introduced by Sen. Susan Collins (R-ME), would establish a council of representatives from a number of federal regulatory agencies to oversee systemic risk. The Obama Administration's proposal modifies this approach by having a risk council serve in an advisory capacity to the Federal Reserve.

Borg noted that neither model currently includes the input of state securities regulators. Shahinian recognized that NASAA President Fred Joseph was on record calling for state participation in systemic risk in his March 26 Senate testimony. "I think the council would lend itself more to state involvement of the two (proposals)," Shahinian said.

Montana Commissioner Lindeen provided the National Association of Insurance Commissioner (NAIC)'s take on systemic risk, saying the job should be left to the states. She emphasized the need for regulatory checks and balances. "We watch over one another," she said of state regulatory agencies. "This creates a very powerful dynamic. Multiple reviews of a problem … are more effective from a regulatory perspective."

Commissioner Raskin also argued that a federal systemic risk regulator is not the answer to the financial crisis. "We should be controlling for systemic risk on the state level before it becomes systemic risk," she said.

Joe Borg, Director of the Alabama Securities Commission, moderated a panel on system risk featuring (from left) Montana Commissioner of Insurance and Securities Monica Lindeen; Sarah Bloom Raskin, Maryland Commissioner of Financial Regulation; and Dean Shahinian, senior counsel for the Senate Banking Committee.

Kanjorski Calls for Collaboration, Compromise in Keynote Address

U.S Rep. Paul Kanjorski (D-PA) delivered the keynote address at NASAA's 2009 Spring Policy Conference. A senior member of the House Financial Services Committee and chairman of its Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises, Rep. Kanjorski helps lead the debate in the House over how to help restore investor confidence in the markets and jump-start the economy.

Kanjorski urged NASAA members to continue their dialogue with members of Congress throughout the recovery and reform process. "Our success is only going to be as good as it affects the folks that are on the ground, yourselves," he said. "We need your input."

While Kanjorski said he recognized that the financial crisis provided a unique opportunity to completely overhaul the nation's regulatory architecture, he advocated a slower pace. "My own opinion is that we should slow down a little bit and do it right," he said. "If you look at the 1930s, it took about 5 or 6 years to really restructure the United States regulatorily and to be very successful."

Kanjorski said the 1930s-era regulation had served America well for 75 years, but "we were pretty foolish in the last ten years. . . . Greed got the better of us and all of us are responsible for that greed," he said.

Kanjorski echoed NASAA's recommendations to increase oversight of previously unregulated sectors of the financial services industry, including hedge funds and derivatives.

He said bipartisanship and compromise would be necessary to achieve effective policy.

"Good regulation comes about by good legislation, and good legislation, lasting legislation, involved legislation, really needs a general consensus of the population," he said. "We're not going to get perfection. But we can do it a lot better than it has been done and correct some of the holes in the system and the failures of the system ... We have to get transparency and accountability out there."

Kanjorski said changes to the way insurance is regulated would help protect the broader economy from the ripple effects of problems at large insurance firms such as AIG. "We're going to have to pass new legislation, and we're going to have to invade some of the control that's been reserved to the states," he said. "We're going to be moving toward regulation at a federal level of insurance … These are organizations that in some respect are too large to fail, so as a result, they do constitute systemic risk."

NASAA Brings Message to **Capitol Hill**

NASAA members testify before Congress to urge lawmakers to invest more resources in state securities regulation and support state-based investor protection.

Fred Joseph testifies before the Senate Banking Committee on March 26. "Our proximity to individual investors puts us in the best position, among all law enforcement officials, to deal aggressively with securities law violations," Joseph said.

Drawing from their experience on the front lines of investor protection, NASAA leaders offered lawmakers several proposals to enhance the states' ability to protect investors and to prosecute perpetrators of financial crimes.

NASAA President Fred Joseph recommended entrusting the states with an even broader authority over investment advisers in his March 26 Senate Banking tesitmony.

"The Madoff case illustrates the horrific consequences we face when an investment adviser's illegal activity goes undetected and unchecked for an extended period," Joseph told the Senate Banking Committee. Joseph called upon Congress to encourage the Securities and Exchange Commission to expand the class of investment advisers that are subject to state securities regulation and increase the states' enforcement authority over large investment advisers.

More Support for States

On March 20, Delaware Securities Commissioner James Ropp urged the House Financial Services Committee to support the valuable contributions of state securities regulators through federal grants.

"State securities regulators have the determination, willpower, and experience to pursue perpetrators of financial crime," Ropp said. "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."

Increased Authority

Ropp also suggested deputizing state securities attorneys to serve as special prosecutors for complex securities cases; allowing states to review securities offerings currently exempt from state oversight under Rule 506 of Regulation D; including representatives from the state banking, insurance, and securities regulatory agencies on the President's Working Group on Financial Markets; toughening civil and criminal penalties for those who commit financial crimes, especially those who target senior investors; and increasing opportunities for victims of fraud to seek private actions.

Secretary of State William Galvin, the top securities official in Massachusetts, urged the committee to "give the states the tools we need to maintain and enhance our ability to regulate effectively and protect investors."

Fiduciary Duty

Galvin also asked Congress to require that brokerages be in a fiduciary relationship to their individual retail customers. Under current law, investment advisers must act as fiduciaries, the legal term for placing the client's interest first. In contrast, stock brokers generally are not required to meet this same legal standard of care when working with customers.

Joseph called upon Congress to apply the fiduciary duty to all financial professionals who give investment advice – broker-dealers and investment advisers alike. "This step will enhance investor protection, eliminate confusion, and even promote regulatory fairness," he said. "For all financial professionals, the interests of the client must come first at all times."

Revisiting Legislation

Joseph pointed to the National Securities Markets Improvement Act (NSMIA), which preempted states from prohibiting offerings made under Rule 506 of Regulation D, as an example of misguided legislation that has limited the states' ability to address fraud in its earliest stages.

"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," he said. "NASAA believes the time has come for Congress to reinstate state regulatory oversight over Rule 506 offerings."

NASAA also supports subjecting derivatives to more comprehensive regulation, establishing an independent risk-assessment body, examining the business models of national credit rating agencies, reforming the arbitration system, and increasing consumer access to private actions, Joseph said.

Life Settlements

Joseph also testified before the Senate Special Committee on Aging on April 29 to discuss ways to combat fraud and abuse in the sale of viaticals and life settlements. These products provide opportunities for terminally ill patients and the elderly to receive money by selling their life insurance death benefits to investors with the promise of returns to be paid upon the death of the insured.

"Life settlements are complex financial arrangements, involving both securities and insurance transactions," he said. "Consequently, regulating them effectively requires a joint effort by securities and insurance regulators, each applying their laws and expertise to different aspects of the product."

The full text versions of NASAA members' testimonies before Congress are available on the NASAA website at www.nasaa.org.

NASAA Joins Industry, Consumer Groups to Promote Systemic Risk Regulation and Fiduciary Standards

As part of its efforts to protect investors, Congress is considering a variety of measures to reform the nation's financial services regulatory structure. Among the areas under consideration is the need to better monitor and control systemic risk in our financial markets.

In a joint letter delivered to the leadership of the Senate Banking Committee and House Committee on Financial Services, organizations representing state securities, banking, and insurance regulators recommend that any framework established to identify and manage systemic risk should be carried out by a collaborative council made up of federal and state regulators, rather than a single agency.

"The unique experiences of state regulators on the front lines of consumer and investor protection provide the basis for our suggestions," the letter said. "Any regulatory reform measure must recognize the importance of ground level detection and policy sensitivity. These are critical characteristics of state regulation and necessary components of an effective financial regulatory structure."

sys – tem –ic *adjective*
Common to a system; affecting the body generally.

The letter was signed by NASAA, the Conference of State Bank Supervisors, and the National Association of Insurance Commissioners.

While investors struggle to regain their financial footing under the weight of the ongoing economic crisis, NASAA has redoubled its efforts to keep investors informed of legislative proposals that would water down any rules currently in place to protect them.

A recent push by the securities industry to convince lawmakers to provide a "universal standard of care" for all investors based on fair dealing is one example of weakened investor protection disguised as reform, NASAA has argued.

fi – du –ci –ar –y *noun*
A person to whom property or power is entrusted for the benefit of another

NASAA has called for all financial professionals who provide investment advice to be held to the highest standard of customer care, not merely a consistent one.

NASAA joined with the Consumer Federation of America and the Investment Adviser Association in a letter to Congress urging them to reject the less rigid "universal standard of care" and apply the fiduciary duty to broker-dealers and investment advisers alike.

"We believe that investors receiving advisory services deserve protections provided by the fiduciary duty standard – the highest standard of care recognized under the law," NASAA wrote in the joint letter with CFA and IAA.

To read NASAA's joint letters to Congress, visit the NASAA website at www.nasaa.org.

NASAA: Because Every Investor Deserves Protection

About Us

The North American Securities Administrators Association (NASAA) is a voluntary association of securities administrators in the 50 states, the District of Columbia, Puerto Rico, the U.S. Virgin Islands, Canada, and Mexico.

Organized in 1919, NASAA is the oldest international organization devoted to investor protection.

As the preeminent organization of securities regulators, NASAA is committed to protecting investors from fraud and abuse, educating investors, supporting capital formation, and helping ensure the integrity and efficiency of financial markets.

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NASAA Insight is a quarterly publication of the North American Securities Administrators Association.

Legal Corner

NASAA Supports SEC Regulation of Equity-Indexed Annuities

NASAA joined AARP and MetLife to file an amicus brief on March 19 to urge the D.C. Circuit Court to uphold the SEC's new rule regulating equity-indexed annuities under federal securities law.

"Indexed annuities have key securities characteristics, including the assumption of investment risk by investors, and they are marketed as a means for investors to participate in securities market gains - features shared by variable annuities," NASAA, AARP, and MetLife argued in the brief.

> *"Indexed annuities have key securities characteristics, including the assumption of investment risk by investors, and they are marketed as a means for investors to participate in securities market gains."*

State insurance regulators previously had sole oversight authority over EIAs. This arrangement did not adequately protect investors, many of them seniors, from abusive sales practices.

"In general insurance regulators do not have at their disposal the equivalent of the disclosure requirements, suitability standards, and anti-fraud measures found in the securities laws," the brief says.

The NASAA legal staff plays an important role in representing the membership's position, as amicus curiae, in significant legal proceedings that may have a widespread impact on securities regulators and the rights of investors.

NASAA also recently filed an amicus brief in the Tennessee Supreme Court, arguing that a criminal conviction under state law for willful failure to register as a broker or agent does not require a showing of specific intent.