



Chief Regulator

A DISCUSSION WITH NYSE CRO RICK KETCHUM

“Notwithstanding all that we’ve accomplished, we can’t be satisfied with where we are today,” says Richard G. Ketchum, who sat down with *nyse magazine* shortly after joining the Exchange on March 8 as Chief Regulatory Officer, a newly created position under the Exchange’s independent governance structure. Ketchum described not only his passionate belief in self-regulation, but the crucial role the NYSE plays in a complex and global era when it comes to trading-floor surveillance, ensuring market integrity, and regulating the major U.S. securities firms, including more than 250 member firms that handle more than 85 percent of all broker-dealer customer accounts.

Ketchum and his group report to the Regulatory Oversight & Regulatory Budget Committee, a committee of the NYSE board that is independent from the NYSE’s management, membership and listed companies. Its members are independent board directors Marshall Carter, committee chairman, Shirley Jackson and Dennis Weatherstone. A reporting structure that is independent from the business and marketing side of the institution, Ketchum explains, ensures that the regulatory function fulfills its public purpose and remains free of conflict while exercising its duties and responsibilities.

Ketchum, 53, was most recently general counsel of the Corporate and Investment Bank of **Citigroup Inc.** (C) and a member of the unit’s Planning Group, Business Practices Committee and Risk Management Committee. Prior to that, during 12 years at the NASD and Nasdaq, his roles included serving as president of Nasdaq for three years and of NASD for seven years. He also spent 14 years at the SEC, eight of them as director of Market Regulation.

Why are your newly created position and its independent reporting structure so important?

I believe it’s crucial for three reasons. First, if a key part of what defines the NYSE has always been and will be its commitment to investors, then regulation must be seen to rank equally with the business itself.

Second, separation is crucial to assuring the status, access and attention afforded to regulatory efforts. Singling out a group of people as accountable increases the board’s focus on the regulatory program and increases my access to board members about both the strategy and needs of that program.

Third, it’s absolutely key that, beyond a shadow of a doubt, the Exchange’s self-regulatory program is perceived as independent. There’s a great deal of focus today on the effectiveness of and future of self-regulation. The SEC has indicated that it will put out a concept release on the issue sometime before the summer. I have no doubt that self-regulation, with strong SEC oversight, provides the most effective, most knowledgeable

type of regulation, particularly in today’s complex environment. But self-regulation will only succeed if people accept it as absolutely independent.

Let’s talk more about your views regarding self-regulation and the NYSE’s role as a self-regulator.

I have a profound commitment to self-regulation. Self-regulation is at the core of our nation’s securities laws and infrastructure. The close proximity of a self-regulatory body to the persons it regulates, coupled with institutional knowledge and experience, makes self-regulation — if applied and executed properly — the best mechanism to oversee a market. I’ve seen it and seen it work well. Investors benefit from self-regulation because regulators are the people involved in the day-to-day workings of the market. Self-regulation can bring to bear a level of experience that is difficult to achieve from any other standpoint. For the NYSE, our greatest priority is to have self-regulatory processes that assure investors and all market participants that they can rely on our vigilant market surveillance.

Describe the scope of NYSE regulation and where you see it heading.

I've had the opportunity to see the Exchange's regulatory program from a number of different directions — as an oversight regulator at the SEC, as a regulatee last year at Citigroup and as a competitor at Nasdaq — and there is not a doubt that the NYSE is at the top rank of providing sophisticated regulatory oversight of securities firms and the trading floor. This institution has many great strengths — including the commitment to technology and the steps the board, Chairman John Reed and CEO John Thain have taken in a short time to increase the resources available to regulation. But we can't be satisfied with where we are today.

The Exchange is changing quickly. The trading environment has evolved substantially in the past two years, and the securities market undoubtedly will be more competitive going forward. We must ensure that as the market changes — as we evolve to a hybrid auction/automatic-execution marketplace — regulatory oversight systems must advance just as quickly, and we must anticipate where regulatory issues may occur. The best regulatory environment is one in which the trading systems effectively restrict violative activity. The system changes implemented over the past few months have moved us substantially in that direction. And while every new trading system is being implemented, we must identify how it can be properly surveilled.

One challenge facing all regulators today is the increasingly complex environment in which securities firms operate. Certainly the ways major securities firms control and manage risk are very different than before. So we need to be more sophisticated in evaluating the firms' ability to manage and control risk, and extremely aggressive in anticipating where inevitable conflicts exist. Our challenge is to ensure that, no matter how competitive the securities industry becomes, the firms never forget their obligation to investors. We can only do that by becoming extremely sophisticated regulators. We must not only look at the end product but focus more on the firms' controls — get in there and understand the most likely situations in which firms can

expose customers or themselves financially. The NYSE really has been quite good at this, but it's a challenge that never ends and one we're rededicating ourselves to.

Is this going to require more resources?

The decisions the Exchange has made in the past few months to increase resources on the regulatory side are encouraging. [The NYSE's 2004 budget includes adding 43 new regulatory positions, bringing the staff to 650.] I'm a big believer in absorbing those increases before deciding whether we need even more resources. But an organization must make sure resources are available where necessary. Those aren't necessarily people — they may be investments in technology and in new skills sets to help existing employees analyze and evaluate risk. What excites me about my conversations with John Reed, John Thain and Marshall Carter is the absolute commitment that NYSE Regulation will have the resources it needs to do the job.

What is striking to me in my first weeks here is the pride people have in their jobs. They are highly capable, knowledgeable, tremendously enthusiastic and passionate about their work, notwithstanding how difficult the last year has been. The independence of my reporting relationship gives us the opportunity to take that culture to the next level, to build on the feeling that we're doing something that matters to the markets and to investors. There's no better place to make a difference as a regulator than here at the NYSE.



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What elements of your background prepare you to lead the NYSE's regulatory efforts?

I spent the first eight of my 12 years at the NASD and Nasdaq with one foot on the self-regulatory side and one on the market side. So I understand how the world of self-regulation has changed, how a self-regulatory organization survives under pressure and how to put together an effective, separate regulatory environment and create a culture absolutely committed to being a top regulator. I've been a competitor four of the last five years, and sometimes there's no more effective way to understand an organization's strengths. That role gave me perspective

on the enormous strengths of the NYSE's trading and regulatory systems.

During my last year at Citigroup I had the chance to see many different regulatory styles — that of the SEC, the NYSE, the NASD, the Fed, the Office of the Comptroller of the Currency, the Financial Services Authority — and this gave me a strong appreciation for the complexity of major securities firms and their issues, challenges and risks. It also provided a strong lesson in the strengths and weaknesses of the different styles of regulation. I hope these experiences will help me to evolve the Exchange's self-regulatory program and continue to make it the most sophisticated, most effective one that exists.

Let's talk about the role technology plays in regulation today.

Technology has played a critical role in regulation and inevitably will play an even greater role. With the speed and complexity of the securities markets and financial firms today, there is no effective way to do our job without greater dependence on technology. But regulatory technology cannot be a stepchild of the market. It has to be integrated into the marketplace to ensure that, as the market changes and new regulatory compliance issues arise, we have the technological solutions to identify problem trading situations. If one thing has been a part of my life in the last 13 years it is trying to advance technology on both the market and the regulatory side. That will be a first priority of mine — to ensure that across the program we're making the maximum use of technology. And I find what I see here very encouraging.

What are some of your other priorities?

To truly get to know my people and to continue my education on the trading floor — how that floor has changed and modernized and what issues are involved with respect to the changes John Thain will be putting in place. Another key priority is to ensure that we're working effectively with the SEC and the NASD and getting the most possible out of our regulatory resources.

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systems have been more effective in identifying the behavior? Those lapses have already been changed, and our commitment is redoubled to ensure that we'll meet the challenges going forward.

Looking ahead, we've got the resources, the capability, the technology and the surveillance systems to ensure that the Exchange continues to earn its reputation as the best-regulated market in the world.

What more can the Exchange do to rebuild investor confidence?

The best thing we can do is to be the best possible self-regulatory organization. Trading on the floor has to be above doubt. We must be able to identify and prosecute violations quickly, and we've got to continue working with the SEC to identify potential conflicts and address them before they escalate to conflict situations. A challenge for the firms and the regulators is to work together to identify areas that could result in abuse before it occurs and harms investors.

What might you say to a listed-company CEO?

The problems over the past two years in the securities industry and with respect to the specialist investigation can be quite bewildering. CEOs need the ability to respond to shareholders, to assure them that the securities markets are addressing the problems and their stocks are trading in the best-regulated trading environment in the world. That's our commitment, through a combination of independence and a commitment of resources, sophisticated technology and talented and experienced people. They should understand what's going on in our market and be absolutely confident that we're focused on protecting investors and ensuring market integrity. ▢

ISSUERS MUST UNDERSTAND WHAT'S GOING ON IN OUR MARKET AND BE CONFIDENT THAT WE'RE FOCUSED ON PROTECTING INVESTORS AND ENSURING MARKET INTEGRITY.