



A Culture of Compliance

CRO RICK KETCHUM DESCRIBES NYSE REGULATION'S ACCOMPLISHMENTS AND GOALS

One year ago Richard G. Ketchum joined the NYSE as its first chief regulatory officer (CRO), a newly created position within the Exchange's independent governance structure that reports directly to a committee of the NYSE board, rather than the CEO. NYSE Regulation, which employs more than 40 percent of the Exchange's staff, plays a crucial role in monitoring and regulating the activities of NYSE members, member firms and listed companies, as well as enforcing compliance with Exchange rules and federal securities laws.

The SEC recently censured the Exchange for failing to properly detect, investigate and discipline improper floor trading from 1999 to 2002. Is the problem behind the NYSE?

The Exchange accepts and acknowledges the SEC's criticisms. Our board and entire organization are committed to take whatever additional steps are necessary to meet our surveillance and enforcement obligations, including those contained in the settlement agreement. Specialist firms have changed, as have we. We've taken major strides to enhance our regulatory and investor-protection programs. We have increased staff and technology resources and appointed new division heads. We have created a new department to analyze surveillances and propose new or modified surveillances. New regulatory technology has been installed to establish better controls and accountability on the floor. Given this, and our strong culture of compliance, we're confident that the breadth and scope of this problem will not reoccur.

Please elaborate on the changes within NYSE Regulation.

Over the past year, we've built upon Regulation's strong foundation through improved specialist surveillance and increases in technolo-

gy and staff, including new leadership additions. We have a new chief of Enforcement, a new chief of Member Firm Regulation and a new chief of Market Surveillance. Susan Merrill, Grace Vogel and Robert Marchman each bring a tremendous wealth of market and industry knowledge that will ensure we're taking actions to protect investors without imposing unnecessary burdens.

We've improved our level of communication and our relationship with the SEC, and we've begun a more effective and open dialogue with the securities industry to help build an effective culture of compliance. Where necessary, we brought important enforcement actions that have sent a strong message.

Our independent governance structure is also working quite well. We communicate regularly with the Regulatory Oversight Committee,

which takes a very activist position, making sure that we receive the attention we need and the resources we require, and that we're being held accountable.

Why are corporate governance and financial compliance listed-company now under NYSE Regulation's umbrella?

Notwithstanding the outstanding way the group was already performing, it was important to make clear that the decisions and judgments we make concerning compliance with our listing standards aren't impacted by our business requirements and issuer relation-

ships. It eliminates any perception that we make decisions for anything other than the most fundamental, ethical, investor-protection reasons.

What is the function of the new Risk Assessment Unit?

This group of extremely experienced professionals can step back, view market and industry trends and, if you will, look around corners and over walls to help us anticipate problems. Our goal is to identify and fix conflicts of interest and other potential problems before investors are seriously harmed.

“Market participants should expect a regulator that’s passionate about protecting the integrity of the markets.”

— RICHARD KETCHUM

What are the changes that are occurring within Member Firm Regulation?

We have shifted to a more complete risk-based approach to more effectively focus our examination and other regulatory resources on real areas of regulatory concern, not technical violations. Grace Vogel also has led the effort to better coordinate with the NASD. We have dramatically enhanced exam coordination. We now track every exam decision with the NASD to understand which firms and what subject matter we are each going to be looking at, so we and the NASD can avoid duplication. We have also substantially coordinated the rule-making process so that our rules, and rule interpretations, remain consistent.

Self-regulation must actively address issues of duplication. We believe we've demonstrated our ability to effectively coordinate without losing the knowledge and judgment that self-regulation provides.



NYSE'S REGULATION'S LEADERSHIP TEAM (FROM LEFT): GRACE VOGEL, ROBERT MARCHMAN, SUSAN MERRILL AND RICHARD KETCHUM.

Is the Exchange implementing stricter enforcement and stiffer financial penalties?

We have always had strict enforcement. Recently we've pursued sales-practice issues and operational concerns regarding firms' handling of the proxy process and prospectus delivery. We're not in the business of imposing punitive fines, but we have to ensure that our large member firms do not view compliance failures as costs of doing business. Penalties must build incentives to enhance their compliance cultures.

How does the NYSE protect customer trade information?

A wide range of trading restrictions protects confidential information, ranging from information barriers between specialists and their upstairs operations to audit-trial restrictions on how floor brokers handle their firms' proprietary orders. We're increasing our attention on this issue, encouraging institutional investors to raise questions and reviewing from top to bottom our controls. We've got great controls in place to ensure confidentiality of information, but we're going to be even more vigilant in coming days.

Describe the educational initiatives for NYSE employees, member-firm employees and investors.

We've dramatically increased training of market-surveillance employees and new examiners, and continuing education for existing examiners. John Thain and I also have reemphasized with employees their responsibility to raise any regulatory issue that might emerge. Every employee must embrace the Exchange's ethical culture and understand this responsibility.

We're also responsible for training participants on the floor and the testing process for all professional designations among member firms. Our goal is to support the firms' efforts to build a culture of compliance. For example, we want to make sure specialist firms have the trading data they need to quickly identify problematic issues. We've begun a process to give floor personnel a better feel for our most significant exam findings and a chance to ask interpretive questions. In June

we'll host the first NYSE Regulation Compliance conference, so we can share with the industry as much regulatory information as possible. No one should ever find himself in a violation because he didn't understand the rules.

For investors, we've built a clear complaint function on nyse.com's Regulation home page (www.nyse.com/regulation), and we're building the infrastructure to ensure investors receive quick responses. Our Website now also identifies new issues that individual investors should be aware of and questions they should be asking to make sure they fully understand their investments.

What should market participants expect from NYSE Regulation in the future?

They should expect a regulator that's absolutely passionate about protecting investors and the fairness and integrity of the markets. We will do everything we can to ensure these goals are met. This will require us to stay up to date with all industry and market changes and actively involved with the market side as the NYSE implements the exciting changes that hybrid markets portend. □