

Alliance For Economic Stability, Inc.
747 Third Avenue, 25th Floor
New York, New York 10017
(212) 702-8804

April 8, 2010

Phil Angelides
Chairman
Financial Crisis Inquiry Commission
1717 Pennsylvania Avenue, NW
Suite 800
Washington, D.C. 20006-4614

Dear Chairman Angelides:

I appreciate the work of the Financial Crisis Inquiry Commission (the "Commission") in its efforts to investigate the causes of the financial crisis that has negatively impacted the lives of so many Americans.

I write on behalf of the Alliance for Economic Stability ("AES") to express our hope that the Commission will thoroughly investigate the responsibilities and failures of self-regulatory organizations in allowing the practices that were the most direct cause of the financial crisis. We are specifically concerned about the self-regulatory organization known as the Financial Industry Regulatory Authority ("FINRA").

As you are aware, FINRA is a self-regulatory organization operating under the putative supervision of the Securities and Exchange Commission ("SEC"). The AES has done substantial research into the inherent conflicts of interest in FINRA's structure as a private business entity and a regulator with quasi-governmental authority. These conflicts of interest create a perverse incentive for FINRA to operate as a deficient regulator in allowing FINRA-member firms, particularly the large investment banks, to abuse basic regulatory standards and principles. This abuse created the financial crisis. Though FINRA is not part of the government, FINRA is and was the "front-line" regulator with the most direct and immediate oversight role of the investment banking and trading functions at the center of the financial crisis.

The AES research into FINRA has culminated in a report on FINRA's conflicts of interest available on the AES website, www.eally.org.

FINRA has used its court-granted immunity and protection against discovery, as well as its exclusion from the Freedom of Information Act requirements, to advance its own agenda by lobbying Congress without question or counter-argument from any concerned parties, not even the SEC. FINRA spends money gained from regulatory fees on lobbying, which also is apparently not questioned by the SEC.

Core to FINRA's conflicts of interest is its executive compensation scheme. FINRA executives earn multi-million-dollar salaries to perform government-assigned regulatory duties. These salaries increased dramatically following the merger that created FINRA from NASD and NYSE Regulation. For instance, Mary Schapiro, the CEO of FINRA until her 2009 appointment to Chairman of the SEC, saw her salary increase by more than 50% following the merger to more than \$3 million in 2008. These salary levels have been maintained despite FINRA's abysmal performance related to the financial crisis and the Madoff and Stanford Ponzi schemes, and despite FINRA showing a net loss of nearly \$700 million in 2008.¹ FINRA executives are incentivized to allow abuses at major FINRA-member firms.

In 2007 the SEC charged a former vice chairman of FINRA, Salvatore Sodano, with exploiting regulatory deficiencies at the AMEX for his personal gain. FINRA also benefited from the AMEX's deficiencies by buying it and selling it thereby gaining from Sodano's regulatory work. This may explain why FINRA paid Sodano approximately \$3 million in 2008 after he was charged. In February of this year the SEC, now led by Sodano's former colleague Ms. Schapiro, entered into a private settlement with Sodano without sanctions. The order against Sodano is the only known instance of the SEC initiating litigation against an officer of FINRA or its predecessors. The undersigned informed and lobbied Congress to investigate the AMEX in 2000. As a result, Congress called for a GAO investigation into the AMEX.

Two articles are attached that make criticisms of FINRA in these and other regards and note FINRA's attempts to expand its jurisdiction to include financial advisors, in addition to broker-dealers. FINRA has used its self-generated report on its responsibilities in the Madoff and Stanford schemes² to lobby for greater jurisdiction. FINRA's report claims that FINRA would have been able to detect the schemes if FINRA had regulatory jurisdiction over investment advisors. The failings of the FINRA report are examined in detail in the AES report. However, in brief, FINRA's central claim to need greater jurisdiction is false. FINRA can use its current jurisdiction over broker-dealers to request, under threat of disciplinary sanction, information about any business entity associated with a broker-dealer, or even about the activities of associated individuals outside of their work at broker-dealers.

Much attention has lately been devoted to the "Repo 105" program used by Lehman Brothers to mask substantial liabilities from investors, following the report on the program by the independent examiner for the U.S. Bankruptcy Court in the Lehman case³. Mary Schapiro's congressional testimony on Repo 105 focused exclusively on failings at the SEC in detecting the Repo 105 program.

¹ See FINRA Annual Report for 2008, available on the FINRA website.

² "Report of the 2009 Special Review Committee on FINRA's Examination Program in Light of the Stanford and Madoff Schemes," dated September 2009, available on the FINRA website.

³ Lehman Brothers Holdings Inc. Chapter 11 Proceedings Examiner's Report, available at <http://lehmanreport.jenner.com/>.

Chairman Angelides

April 8, 2010

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No apparent attention has focused on FINRA's failings related to Repo 105, or to capital inadequacies at the major investment banks with broker-dealers under FINRA's jurisdiction. The Lehman Examiner's report shows evidence that the Repo 105 trades were conducted through Lehman's U.S.-based broker-dealer⁴. FINRA was responsible for ensuring the broker-dealer's compliance with regulatory capital levels on a monthly basis in reports required to be submitted to FINRA. These reports must have shown the large, irregular movement of capital through Lehman's U.S. broker-dealer.

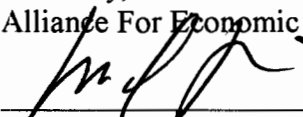
No government authority has undertaken to thoroughly investigate FINRA's failures related to Repo 105, or its other deficiencies that directly allowed the excesses that caused the financial crisis.

Attached for your review are our letters to members of Congress on the issue of FINRA, dated November 16, 2009 and December 21, 2009, containing further analysis we have conducted related to FINRA's deficiencies and lobbying efforts.

The financial crisis has revealed numerous failings at the SEC, primarily through reports of the SEC's Office of Inspector General. FINRA has no Inspector General, is run by individuals who are paid millions of dollars by those whose conduct caused the financial crisis, and is not held to the same standards of accountability and transparency as a government agency. FINRA's failings can only be far worse than those at the SEC, yet no government official or legislator has taken an active role in initiating an investigation into FINRA's failings.

In summary, we urge to devote significant attention in your investigation to the failings of FINRA that allowed the financial crisis to occur and to recommendations for changes to the self-regulatory system. It is apparent that such an investigation would help to ensure the future stability of the American financial and economic system.

Sincerely,
Alliance For Economic Stability, Inc.



Manuel P. Asensio

⁴ See reference to email from Mark Neller of Lehman at footnote 3038, page 791, of Volume 3 of Lehman Examiner's Report.

Wall St watchdog won't roll over: Finra CEO

Thu, Apr 1 2010

By Joseph Giannone and Rachelle Younglai

NEW YORK (Reuters) - One of Wall Street's biggest watchdogs concedes that it needs more bite.

After the biggest financial meltdown in history, the Financial Industry Regulatory Authority accepts responsibility for some of its shortcomings and is trying to do more to protect investors from multibillion dollar frauds such as the one committed by Bernard Madoff.

"We did take a hard look at how we operate with respect to both Stanford and Madoff," Finra Chief Executive Richard Ketchum said this week at the Reuters Global Exchanges & Trading Summit in New York.

Texas billionaire Allen Stanford has been accused of bilking investors of billions of dollars in a Ponzi scheme and is awaiting trial in January 2011.

"We could have done better on both," said Ketchum, who took the helm in April 2009 after about 30 years mostly at the New York Stock Exchange's regulatory arm; NASD, a Finra predecessor; and the U.S. Securities and Exchange Commission.

Finra, which is funded by the financial industry, supervises nearly 5,000 brokerage firms and is overseen by the SEC.

Like the SEC, Finra has been criticized for failing to catch Madoff before he bilked investors of \$65 billion. Finra has also been criticized for being captive to the industry it is supposed to monitor. Although the SEC oversees Finra, it is seen as being hands-off.

But Ketchum said: "We aren't unaccountable. We are tightly interwoven into the securities regulatory environment. The suggestion of a lack of accountability is, I think, a political suggestion."

Now as Congress and the White House try to reform the way the financial system is supervised, Finra is trying to expand its jurisdiction to include investment advisers.

The watchdog is also trying to bolster its enforcement division, creating a whistleblower office and vowing to be more aggressive in investigating the advisory activities of the registered broker dealers.

But although Ketchum has spent more than three decades moving through the regulatory ranks, he is not seen as a tough regulator.

"I have a high opinion of Rick, but that goes to his acute knowledge about the microstructure of capital markets and not to either his regulatory zeal, enforcement experience, or overall management style, none of which have been tested before moving to the NYSE, then Nasdaq and Finra," said James Cox, a securities law professor at Duke University.

Ketchum has been a regulator through some of the biggest U.S. securities scandals, including the insider trading scandals of the 1980s and the Nasdaq trading-spread scandal of the mid-1990s to the dot-com bubble at the turn of the millennium.

The trading industry views Ketchum as someone who understands markets thoroughly. "There's no regulator who cares as much about markets as Rick," said Chris Concannon, the former head of transaction services at Nasdaq OMX and a former SEC attorney. Concannon is a senior partner at electronic trading firm Virtu Financial LLC.

At the Reuters Summit, Ketchum spoke out about the need for a consistent fiduciary standard for brokers and investment advisers who provide financial advice. He also said Finra's fraud detection and whistleblower offices will "ensure that we have a central focus with respect to people who are sophisticated from a fraud detection standpoint."

To his credit, Ketchum has often been brought in to help clean up messes such as when he became general counsel of Citigroup's investment bank in the aftermath of its tech bubble scandal. For the first time in his regulatory career, Ketchum will be solely accountable for the successes and failures of his organization.

"I have no doubt about his integrity, and I'm telling you no one in the regulatory sector has more experience," said John Coffee, a securities professor at Columbia Law School.

"Yes, he's been around some collisions that have damaged others' reputations. ... But that is far different than saying I think he's responsible."

(Reporting by Rachelle Younglai; Editing by Richard Chang)

BARRON'S

MONDAY, MARCH 8, 2010

Finra, First Heal Thyself

By JIM MCTAGUE

Funding Finra's failures.

IN 2007-08, REGULATORS AT FINRA WERE so distracted with empire-building and lining their pockets, they overlooked the world's two largest Ponzi schemers: Bernie Madoff and, allegedly, R. Allen Stanford. So what's the deeply flawed Financial Industry Regulatory Authority up to now? Building itself an even bigger empire.

The quasigovernmental body, which advertises itself as the white knight of 90 million investors, is lobbying Congress for the power to regulate 11,000 investment advisors who now fall under the jurisdiction of the Securities and Exchange Commission and state securities regulators. The states regulate those with less than \$25 million in assets, but want Congress to bump that to \$100 million. Why? The SEC does such a poor job, it visits an average of one advisor every nine to 11 years!

Finra currently regulates Nasdaq and New York Stock Exchange brokers and securities dealers, and pays its executive staff high-on-the-hog salaries, despite abysmal performances. This is the same behavior that contributed to the failure of big financial firms that operated under Finra's purview. If Congress accedes to its power grab, the kingdom of Finra will be able to fatten its coffers with millions more dollars in fees from its new charges. Given Finra's sorry enforcement record, there's little reason to believe investors would be any better off.

Why would investment advisors want to shell out money for the privilege of being regulated when the SEC does it free? The state regulators oppose Finra's grab because they say there's no adequate oversight of the organization.

"They aren't accountable to anyone but their own members," says Texas Securities Commissioner Denise Voigt Crawford. As for being investor-friendly, she points to their "abhorrent" mandatory system of dispute resolution by arbitration, a process she says is stacked in favor of the firms.

FINRA'S STORY is that had it been regulating investment-advisory firms in 2007, it might have caught on to Madoff. Although Madoff's brokerage business was regulated by Finra, his investment-advisory business, where the fraud took place, was regulated by the equally hapless SEC.

Says Finra spokeswoman Nancy Condon, "The absence of a comprehensive examination program for investment advisors impacts the level of protection for every member of the public who entrusts funds to one of those advisors. It's clear that dedicating more resources to a regular and vigorous examination program and day-to-day oversight of the investment advisors could improve investor protection for their customers, just as it has for customers of broker-dealers."

Finra's critics find this argument risible, pointing out that there's scant evidence that the regulator examined Madoff's brokerage business in recent years. Furthermore, they contend Finra failed to properly regulate a host of firms at the center of the financial meltdown, including Bear Stearns, Lehman Brothers, and Merrill Lynch.

The nonprofit Project on Government Oversight says an internal Finra review shows Finra missed key opportunities to uncover alleged fraud by Stanford, in part because it is too cozy with Wall Street.

Finra is what is known in the securities world as a self-regulatory organization, or SRO. Congress wrote a provision in the Securities and Exchange Act of 1934 permitting exchanges to create SROs to regulate member conduct and punish scofflaws. The SEC conducts regular inspections of Finra. But there are no regular oversight hearings by the Congress.

In 2006, the NYSE and the Nasdaq each had an SRO. In 2007, the two exchanges agreed to create Finra, to realize cost efficiencies and regulatory harmony. The merger required emendation of the Nasdaq market's bylaws by some 5,000 members.

Its SRO decided to prod the change by offering members \$35,000 apiece from \$2 billion in members' equity it had amassed as a result of the public listing of the Nasdaq stock market between 2001 and 2006. The SRO had owned shares of Nasdaq stock. In a prospectus and in road shows, Finra contended that the Internal Revenue Service threatened to yank its nonprofit status if it paid Nasdaq's members \$35,000 each.

Several broker-dealers subsequently sued Finra, alleging the officers had lied and subsequently had used some of the money to give themselves exorbitant pay raises. Mary Schapiro, who led Finra then, received \$7.3 million in salary and accumulated benefits when she left; now chairman of the SEC, Schapiro makes \$158,500 a year. This month, Judge Jed Rakoff of the U.S. District Court for the Southern District of New York dismissed the lawsuits, not on their merits, but because under the law, Finra and its officers enjoy "absolute immunity" from private actions challenging their official conduct as regulators. The judge's action startled the investment-advisory community.

"I don't think Finra is accountable to anyone," says David Tittsworth, executive director of the Investment Advisor Association in Washington. He's right. Congress should change this, not give Finra an expanded kingdom.

Finra's Accountability

To the Editor:

The March 8 D.C. Current column, "[Finra, First Heal Thyself](#)," contained complaints that the Financial Industry Regulatory Association isn't "accountable to anyone." One critic said Finra is accountable only to Finra-registered firms and brokers. But the Finra board of governors is composed of a majority of public members, unaffiliated with securities firms or brokers.

Another critic [David Tittsworth, executive director of the Investment Advisor Association] said Finra was accountable to no one, as if the organization were a sovereign state. In addition to its board, Finra also is overseen by the Securities and Exchange Commission. It reviews and approves all rules written by Finra, regularly examines Finra activities and has the authority to sanction Finra.

In response to the Madoff and [alleged] Stanford scandals, Finra has enhanced its routine-examination programs for detecting fraud, instituted new procedures for review of arbitration matters and established an Office of Fraud Detection and Market Intelligence, among many other initiatives.

We agree that it's time for reform in financial-services oversight, but the discussion surrounding it should be grounded in fact, not self-serving hyperbole.

Howard Schloss
Executive Vice President
Communications and Government Relations
Financial Industry Regulatory Authority
Washington

Alliance For Economic Stability
747 Third Avenue, 25th Floor
New York, New York 10017
(212) 702-8804

November 16, 2009

The Honorable Christopher J. Dodd
Chairman
Banking, Housing and Urban
Affairs Committee

United States Senate
534 Dirksen Senate Office Building
Washington, D.C. 20515

The Honorable Richard C. Shelby
Ranking Member
Banking, Housing and Urban
Affairs Committee

United States Senate
534 Dirksen Senate Office Building
Washington, D.C. 20515

Re: November 10, 2009 Discussion Draft of the Financial Reform Bill

Dear Chairman Dodd, Ranking Member Shelby, and Members of the Committee:

The Alliance for Economic Stability (“AES”), an organization dedicated to advocating taxpayers’ interest in financial regulation, appreciates your continued efforts aimed at improving the efficiency of the nation’s financial system. I write to express the support of AES for the Discussion Draft of the Financial Reform Bill (“Discussion Draft”) and specifically “Subtitle F – Improvement to the Management of the Securities and Exchange Commission,” which mandates the Securities and Exchange Commission (“SEC”) to report to Congress on its procedures for examining national securities associations registered under section 15A of the Securities Exchange Act of 1934. Section F also mandates an assessment by the Comptroller General of the United States of the SEC’s report under Subtitle F and of the adequacy and effectiveness of the SEC’s own controls and procedures.

This letter focuses specifically on Subtitle F’s Section 964 titled “Report on Oversight of National Securities Associations.” This section mandates that the Comptroller report on the SEC’s oversight of securities organizations specifically including their governance, conflicts of interest and effectiveness.

We urge the Committee to consider the data contained in AES’ report titled “Securities Regulatory Reform: Addressing FINRA’s Inherent Conflict and Moral Hazard” in making amendments to the Discussion Draft. The report relies and refers to studies that illustrate FINRA’s deficiencies and adverse influence on the SEC. AES’s report draws on FINRA’s price-fixing scandal, and later failures to detect the Madoff and Stanford schemes, as well as FINRA’s oversight failures of its registered investment bankers and brokers that created the sub-prime crisis that led to the collapse of Bear Stearns, Lehman Brothers, Merrill Lynch and AIG.

Given FINRA's unique role as a for-profit company that acts like a government agency that has recently become a monopoly in our financial system, and given that FINRA's regulatory failures were a direct and significant contributor to the economic crisis, we would urge the Committee to refer to FINRA specifically in the Discussion Draft along with the general references to registered entities or national securities associations.

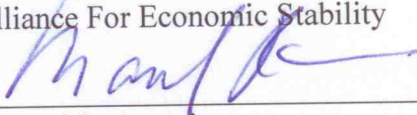
The AES FINRA report contains documentation and investigative information should provide the Committee with the basis to legislate specific changes to augment Subtitle F's reporting requirements for FINRA specifically, including a move to the SECO plan, or having the SEC as the only enforcement agency in the securities market. The SEC would become the sole rulemaker, examiner and enforcer for the industry while FINRA will remain an administrator and a powerful trade association. Such a change eliminates of FINRA's inherent conflicts-of-interest that has repeatedly allowed FINRA members to engage in economically destructive activities, while FINRA takes no accountability and the public is left to pay the cost of FINRA's failures.

The AES investigative report reveal FINRA's inherent flaws, which is useful to construct solutions that do not involve abolishing the concept of self-regulation entirely or expanding the duties of the SEC to cover all the regulatory responsibilities currently performed by FINRA.

FINRA's revenue exceeds the SEC's budget. FINRA is allowed to charge regulatory fees but has no constraints on how those fees are used for non-regulatory activities, including lobbying and questionable compensation. It is not lost on Americans that the SEC's Chairperson is the Presidential administration's wealthiest member and that she obtained her wealth exclusively through regulatory fees that were paid by the same FINRA members that she supposedly regulated.

We support the Discussion Draft and the provisions contained in Subtitle F but urge the Committee to include further provisions that eliminate the inherent conflicts and constitutional deficiencies detailed in AES' FINRA report and the expert opinions contained therein.

Sincerely,
Alliance For Economic Stability



Manuel P. Asensio

Enclosure

Alliance For Economic Stability, Inc.
747 Third Avenue, 25th Floor
New York, New York 10017
(212) 702-8804

December 21, 2009

The Honorable Spencer Bachus
Ranking Member
Financial Services Committee
U.S. House of Representatives
B371a Rayburn HOB
Washington, D.C. 20515

Dear Congressman Bachus:

After reading the transcript of The Congressional Record of the House pursuant to “WALL STREET REFORM AND CONSUMER PROTECTION ACT OF 2009” (December 11, 2009) specifically regarding Amendment 15 to Bill HR4173 advocating the striking of the Financial Industry Regulatory Authority, Inc.’s (“FINRA”) authority to regulate investment advisors, I am relieved to see that you ultimately acceded to the position of Messrs. Cohen and Frank that the Securities and Exchange Commission (“SEC”) is best positioned to oversee investment advisors, as FINRA lacks the necessary experience and expertise to do so.

It is, however, disturbing to see that despite the plethora of evidence indicating otherwise, your opinion still appears to remain that the SEC is ultimately the agency on which blame should be laid for the recent financial crisis as well as the Madoff Ponzi scheme debacle that destroyed the lives and fortunes of private individual investors on a monumental scale, as evidenced in the record when you refer to the SEC as “not doing their job.”

I am therefore compelled to write outlining some of the evidence pointing to true fault lying with FINRA, as well as to remind you of the conflicts-of-interest that make FINRA inappropriate in any regulatory role at all. I hope you see this as an effort to assist you and to set the record straight.

SEC Commissioner Luis Aguilar himself warned of this conflict-of-interest in the SEC “outsourcing its mission” when he expressed his grave concern as to “moral hazard” stemming from FINRA’s status not as a government agency operating a principles-based regime in order to protect investors, but rather as a private entity that is inherently disposed to act in the interest of its clients, the broker-dealers from whom FINRA draws revenues, which FINRA needs to pay its leaders multi-million dollar salaries. Aguilar opined that the SEC is the *only* regulatory agency that has the necessary experience and expertise to carry out the task of regulating investment advisory firms with a principles-based regime. Investment advisors’ fiduciary duty would be

diminished if FINRA were to obtain additional authority extended to the investment advisory profession, since FINRA has many deficiencies in its rules-based regime, which has been shown to be ineffective exactly in Madoff the case you cite, and would naturally be biased toward the side of broker-dealers.

Surely you must see that a "self-regulatory," non-governmental agency such as FINRA cannot and should not be in a position of regulating an industry that FINRA itself has a direct financial interest in. Yet your statement backing up your initial opposition of Amendment 15 in defense of FINRA's appropriateness in being granted that authority indicates otherwise.

With all due respect, Congressman, your explanation shows a deep misunderstanding of the facts and the situation, and given that it occurred on the House floor at such a crucial moment in our Nation's history, we at the Alliance for Economic Stability, Inc. ("AES") are compelled to set the record straight.

In the case of Madoff, you say that the fraud occurred with only one of Madoff's two entities -- and that was his "investment advisory" entity, not his broker-dealer entity. You contend that it was the SEC who oversaw investment advisors and since the SEC never examined the advisory entity, you exculpate FINRA from any wrongdoing, concluding that FINRA actually performed its duty by examining Madoff's broker-dealer entity over which it had authority while the SEC failed to investigate the investment advisory entity. And from there you took the position of advocating more regulatory power for FINRA, concluding that "gaps in regulation" were the cause of the Madoff fraud being missed by regulators for decades, as well as the cause of the recent financial crisis as a whole.

Your assert that FINRA performed its duty by examining Madoff's broker-dealer entity and point the finger of failure here at the SEC for not "doing its job" (assuming you were not referring to the SEC's duty to oversee FINRA). This fails to take into consideration some crucial facts as to the nature of several SEC examinations and the evidence of FINRA's exam failures and activities pertaining thereto that thwarted SEC examination.

In a comprehensive report written by AES, a copy of which I enclose herewith, the direct failings of FINRA -- not the SEC -- in Madoff are shown, supported by expert legal opinions and testimony from the SEC. These findings contradict the position that FINRA was not at fault. The report notes that FINRA is a conflicted rules-based private company that at one time included Madoff family members among its executives.

It was FINRA that had primary oversight of the investment banks that collapsed in 2008 and had *direct oversight* of the Madoff firm. What really needs to be addressed here -- and recognized for the record -- is that FINRA impaired the SEC's ability to carry out its duty of investigation and enforcement, stemming from FINRA's position of conflicts-of-interest and "moral hazard" -- *not* the failure of the SEC to "do its job."

FINRA has an incentive to work for the interests of those it is supposed to regulate, broker-dealers, over and above the interests of the general public. FINRA levies taxes on

broker-dealers and is allowed to use such regulatory funds for non-regulatory purposes, such as advertising, lobbying and paying multi-million-dollar salaries, at its sole discretion, immune from SEC and Congressional oversight.

The SEC repeatedly investigated Madoff, but it was FINRA that held control over the evidence needed to uncover the fraud. FINRA conducted numerous examinations of Madoff's broker-dealer entity, which is where Madoff claimed to be holding his client's non-existing securities and where he supposedly executed his fictitious trades. Why didn't FINRA uncover the fraud at one of its leading members? There is a history at FINRA that should help Congress understand the reason for the failure.

The investigation by the U.S. Department of Justice (DOJ) of NASDAQ's price-fixing scheme (which FINRA had a legal obligation and duty to correct) shows that Richard Ketchum, FINRA's current leader, defended the price-fixing. FINRA furthermore failed to cooperate with the DOJ in this investigation to its satisfaction to such an extent that FINRA was ultimately ordered by a federal judge to turn over documents. FINRA antagonized the SEC by refusing to turn over information as to the collusion of securities dealers, and Brandon Becker, the SEC director who was supposed to oversee FINRA, resigned under pressure from the media questioning his relationship with Ketchum, his former boss.

In fact, when the DOJ and SEC finally took action against NASDAQ after finding FINRA had failed to uncover a massive price-fixing scheme, Attorney General Janet Reno said the DOJ "found evidence of coercion and other misconduct in this industry concerning NASDAQ price fixing," and SEC Chairman Levitt confirmed evidence of FINRA's failure to fulfill "its most basic responsibilities . . . promote just and equitable principles of trade for protection of investors," adding that FINRA showed "blindness" to its members' gross misconduct when FINRA was charged with being the "cop on the beat."

In an editorial for The Wall Street Journal, Richard Lindsey, Becker's replacement at the SEC, criticized FINRA when he wrote that since FINRA "is responsible for taking action against its own members, the conditions necessary for moral hazard exist at [FINRA]."

We should add that FINRA also had direct oversight in securities firms engaged in unfair conduct in securitizing faulty mortgages, leading to the collapse of four of its largest members: AIG, Lehman, Merrill Lynch and Bear Stearns.

Professor John C. Coffee of Columbia University rightly rejected FINRA's claim that it had no jurisdiction or reason to inquire into the Madoff Ponzi scheme because FINRA *did* have jurisdiction over Madoff's broker-dealer entity *long before Madoff ever was required to register as an investment advisor.* Prior to 2006, Madoff was only a broker-dealer; there was no registered investment advisory entity of such same name. Hence, contrary to your assertion that FINRA was blameless due to lack of jurisdiction over its "advisory" arm, in fact all activity of the Madoff firm prior to 2006 and after was fully *within* the jurisdiction of FINRA -- *for decades.* FINRA was in no way "held back" from examining such broker-dealer's "advisory" side. Professor Coffee's opinion, and that of many reasonable independent experts, is that

FINRA unquestionably had more-than-sufficient jurisdiction over Madoff to uncover the fraud, and that FINRA had right to obtain the documents sought by the SEC that would have proved the fraud.

Perhaps your misunderstanding comes from former SEC Chairman Harvey Pitt who still attempts to defend FINRA with the position of “no jurisdiction,” despite all evidence to the contrary. This in turn gives rise to confusion and misconception as to what happened here and who was truly to blame by casting doubt through repetitive insistence on a nonsensical position in face undeniable evidence contained in SEC records as to FINRA’S lack of cooperation in giving SEC investigators documents that FINRA controlled, as stated on Page 22 of the AES report:

“The SEC’s OIG obtained an expert’s opinion stating that if the SEC investigators had received this information from FINRA concerning Madoff’s actual trading and holdings, it would have led the SEC to discover the Madoff fraud in 1993.”

Any position excusing FINRA from failure to comply with its regulatory duty in the Madoff scheme by pointing to lack of jurisdiction simply lacks grounding in the facts of the case.

The SEC’s own investigation as to reasons for its own possible failures to uncover Madoff’s fraudulent activity backs up this argument. Its expert stated that “FINRA *could have* provided order and execution data necessary to reveal the Ponzi scheme.” This statement is supported by SEC examiners’ statements as to their inability to gain access to documents held by FINRA.

The SEC report notes FINRA executives’ cavalier attitude towards the SEC staff members investigating Madoff and the staffers’ concerns about FINRA’s Madoff reviews, concerns that led them to request that Becker change the rules so as to obligate FINRA to do a better job. Clearly, FINRA thwarted SEC examiners and should be held accountable as ultimately responsible for the wave of financial ruin Madoff left in his wake.

Unlike the SEC’s report, the FINRA report produced to examine potential failures related to the Madoff scheme, referenced in Section 1 of the AES report, does not contain substantial examination of FINRA’s own more numerous failures to uncover the Madoff Ponzi scheme, *despite its holding all the information necessary to uncover Madoff’s fraudulent trade reporting to the SEC.* FINRA’s report fails utterly to address the most pertinent issues.

This conduct by FINRA’s current leader, and chief promoter of the misinformation you unfortunately voiced on the floor of the House, illustrates the “moral hazard” forewarned of by Lindsey, and begs the question as to just who really held the cards of authority here: Those entrusted with a duty to enforce regulations in the interest of the investors at large, or Mr. Madoff?

I attach a recent editorial that I wrote, published in [The Pittsburgh Post-Gazette](#), that may be useful to you.

Congressman Bachus
December 21, 2009
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In closing, let me reiterate that I laud you for ultimately conceding to the appropriateness of Amendment 15. And I hope you will interpret the above not as personal criticism, but rather as a factual critique of a policy position. I hope this will serve the interests of your constituents and fair market regulation. A well-informed Congress will understand that FINRA is a very serious problem at the center of the nation's economic crisis.

Sincerely,
Alliance For Economic Stability, Inc.


Manuel P. Asensio

cc: U.S. Senator Christopher J. Dodd
Chairman
U.S. Senate Committee on Banking, Housing and Urban Affairs

U.S. Senator Richard C. Shelby
Ranking Member
U.S. Senate Committee on Banking, Housing and Urban Affairs

U.S. Representative Barney Frank
Chairman
Financial Services Committee

U.S. Representative Steve Cohen