

MANAGER'S JOURNAL / By Hilary Kramer

Free the Nasdaq!

THERE ARE steamships, there are rocketships, and then there's Nasdaq. In a few short years, with the advent of the Microsifts, Cisco and Intels of the world, the exchange became one of the great emblems of American entrepreneurship. At the New York Stock Exchange, new listings must have a heritage of profits; American start-ups have Nasdaq to thank for showing the faith in their ventures, giving IPOs at least the freedom to go boom or bust.

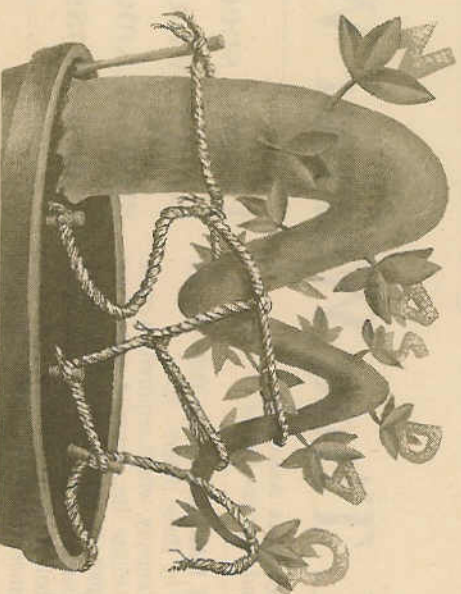
But the marketplace that gave nimble, new companies the freedom to grow could use a little freedom of its own these days. Nasdaq's dream of becoming an independent exchange is predicated on how the Securities and Exchange Commission will likely rule on a regulatory technicality this fall.

CEO Bob Greifeld, who has drastically streamlined operations since coming on the job earlier this summer, has put persuading the Intransigent SEC atop his to-do list. Nasdaq's electronic trading network manages over 5,000 transactions per second, executes and confirms orders in just over 1/15th of a second. Yet the world's fastest stock market is shackled by a regulatory bureaucracy that doesn't exist for comparable marketplaces.

The National Association of Securities Dealers, the largest self-regulatory organization in the U.S., remains the primary owner of Nasdaq. As a result, the exchange's decisions require the regulatory approval not only of the Securities and Exchange Commission, but the NASD as well.

Nasdaq's ability to react to market disruptions and to introduce continuing innovations in the market-

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place—hallmarks of the exchange's contributions to the financial world—is constrained by this additional layer of administration.

Nasdaq isn't even a registered exchange. The NASD retains voting control over Nasdaq unless the SEC approves it as a national securities exchange. So to achieve self-regulatory status—separate from that of the NASD—Nasdaq has been pressing the SEC to obtain an exchange registration. The result? The SEC has dragged its feet for two years.

In the short-run, Nasdaq won't look much different if it's granted exchange registration, since the marketplace has been operating as a de facto exchange for years now. What it will do, however, is change Nasdaq's legal status and grant it independence from the NASD—which has become an expensive \$70 million a year regulator, notably pricier than the regulation costs paid by electronic communications networks (ECNs). In the long run, however, the benefits

to the securities industry are evident. Freeing Nasdaq from NASD oversight and ownership would enable Nasdaq to compete on a par with other stock exchanges. It would afford Nasdaq access to public capital markets to raise funds to expand its trading system or to acquire competitors. And it would simply be good corporate governance, removing even the hint of potential conflicts of interest between NASD members behaving as owners of Nasdaq and the same firms acting as Nasdaq broker dealers.

Exchange status for Nasdaq would create a freer market for the entire securities industry, which inevitably fosters innovation. And Nasdaq is indeed an innovator. It was the world's first electronic stock market, the first and only U.S. stock market to meet the stringent ISO 9001 quality management and assurance standards, and the market with considerably superior execution quality, according to independent data provider, Market Systems Inc.

Nasdaq's innovative approach has certainly affected competitor exchanges. For instance, prompted by traders, institutional investors and listed companies, the old-line exchanges have begun transforming themselves into more technology-friendly marketplaces in order to keep up with Nasdaq. And recently, listed companies even succeeded in pressuring the NYSE to propose eliminating Rule 500, which will allow freer movement between exchanges instead of the current

NYSE-monopoly environment, where it's easy for companies to move to the NYSE, but almost impossible to leave.

It's no coincidence that the marketplace serving innovative companies is itself an innovator, which is why entrepreneurial companies are attracted to Nasdaq in the first place.

It's unfortunate that the SEC may be populated with old-fashioned folks who fear innovation. These are the same people who ignore the NYSE's antiquated practice of "specialists"—human, versus electronic market-makers. Yet they can't seem to find enough value in Nasdaq's inventive electronic market model to grant it exchange status comparable to that of NYSE or the American Stock Exchange—even though Nasdaq clearly offers quick order execution and fair prices in a manner comparable to or even more efficient than other exchanges.

It would be a real tragedy if the SEC left this incubator of entrepreneurialism and innovation buried in bureaucracy. Nasdaq may not be synonymous with "tech stock market," but if the S.E.C. acts with free markets in mind, it should at least be synonymous with "registered national securities exchange."

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