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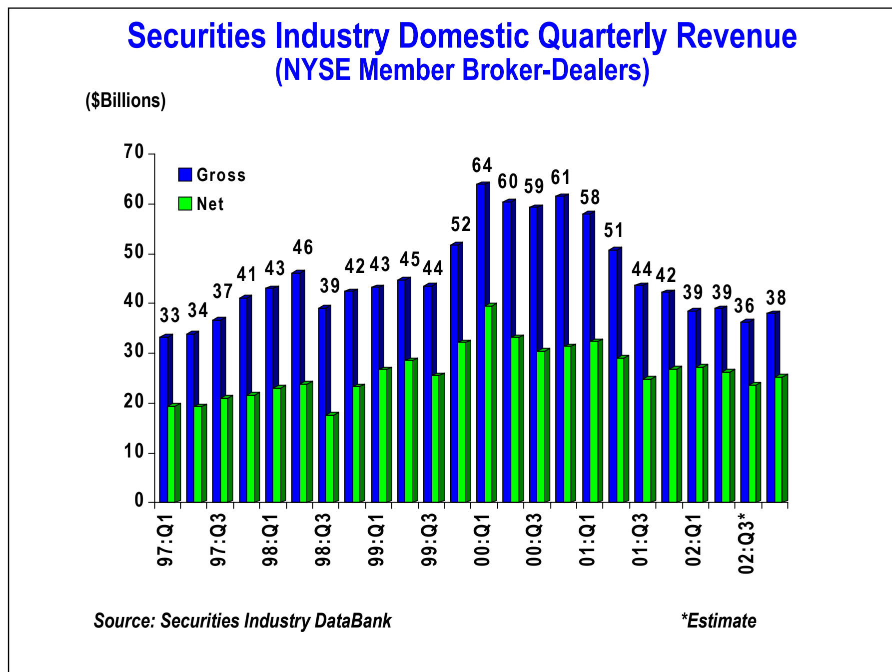
Page 19 **Analyst Update and Legal Alert**. This SIA legal alert provides important information for our firms regarding: 1) SRO analyst rules and guidance; 2) the terms of the Merrill Lynch settlement with the New York State Attorney General; 3) proposed SEC Regulation Analyst Certification (AC); and 4) implications of the Sarbanes-Oxley Act.

Page 32 **Monthly Statistical Review**, by Grace Toto. The DJIA and Nasdaq Composite Index posted modest losses of roughly 1% in August, while the S&P 500 eked out a 0.5% gain. Stock prices have since fallen further, driving these major market indices down 10% so far in September (through 9/24). Daily share and dollar volumes on the NYSE and Nasdaq sank to their lowest levels of the year in August. Domestic underwriting of all major debt and equity products slumped, with new equity issuance at its weakest level in over a decade.

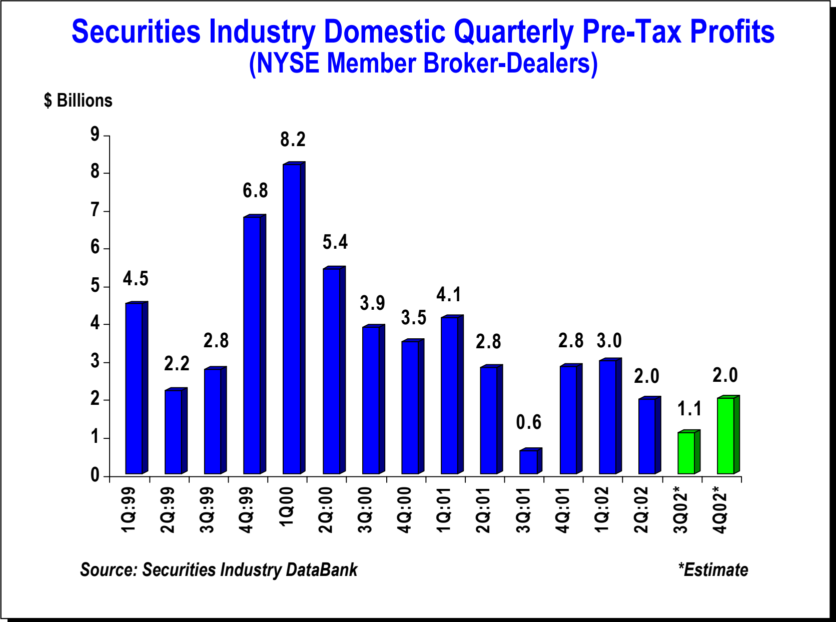
BROKER REVENUE REELING
Quarterly Profits Plummet Another $1 Billion

Securities industry domestic pre-tax profits are estimated to have been nearly halved in 3Q 2002 to $1.1 billion from the second quarter's $2.0 billion, which itself was a 50% drop from the first quarter's $3.0 billion. Every major broker reporting quarterly earnings over the past few weeks (for the three months ended August) showed sequential quarterly declines in their pre-tax profits ranging from -12% to -53%. When one includes September's horrendous results, estimates for the calendar quarter just ended are well below any previous expectations. For equity markets this was the worst September in 65 years, based on the performance of the Dow Jones Industrial Average (down 12.4%), which merely capped an 18% drop in the index for 3Q 2002, its worst quarterly showing since the market correction 15 years ago. This also nearly seals 2002 as the third straight year of overall market declines, the first time in more than 60 years, since 1939-1941, that this occurred.

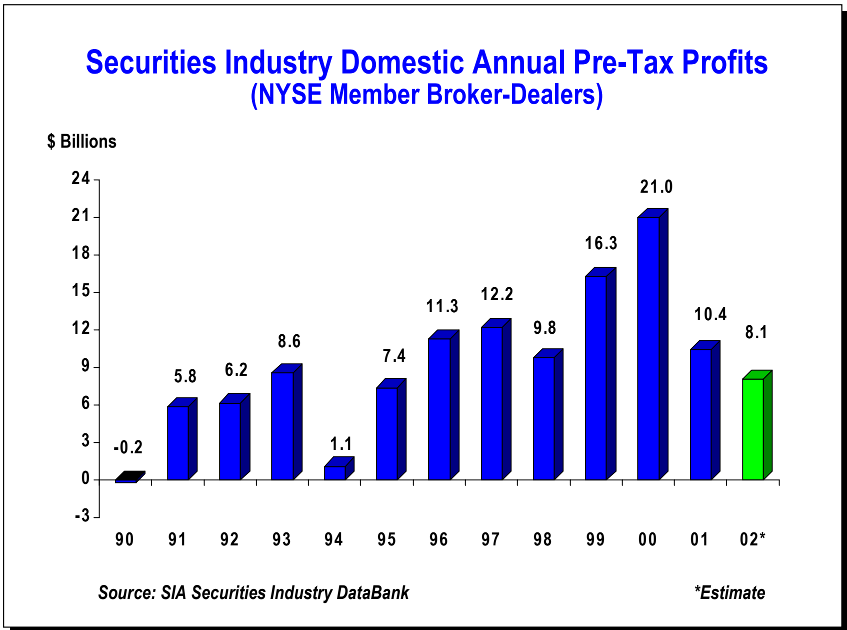


Management has been hard pressed to keep cost cutting on pace with successive spiraling declines in revenue over the past two and one-half years. Third quarter gross and net revenues fell 7% from second quarter levels which were also 16% below results for the same period last year. This brought **gross revenue** down to just $36.3 billion for the quarter, a 43% decline since 1Q 2000 and a five year low. **Total costs**, meanwhile, have been cut from $55.8 billion in 1Q 2000 to $35.2 billion in 3Q 2002, a remarkable 37% contraction over the same 2 ½-year period, but still shy of the revenue reductions.

Net revenue (net of interest) is estimated to have dropped to $23.6 billion in 3Q 2002, a 40% decline during the same 2 ½-year period and a 4 ½-year low. However, **operating expenses** declined a much smaller 28% over these 2 ½ years (which excludes the unprecedented cuts in interest costs in gross expenses) and thus **quarterly profits** have fallen 87% from the record $8.2 billion posted in 1Q 2000 to just $1.1 billion during the quarter just ended.



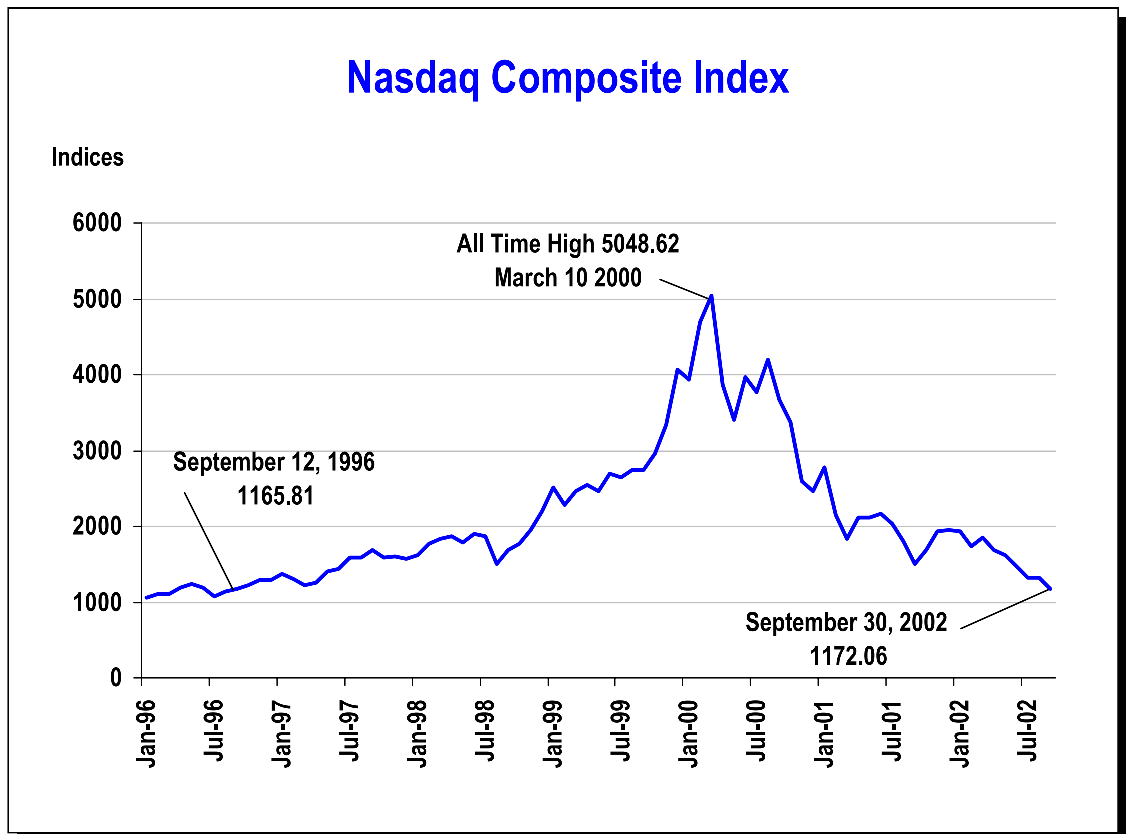
This will make 3Q 2002 the third worst quarter for industry pre-tax profits in 7 ½ years, trailing only 3Q 1998's liquidity crisis loss of $0.2 billion and the marginal profit of $0.6 billion salvaged in 3Q 2001. With an estimated $2.0 billion in profits expected to be logged in 4Q 2002, this year's annual showing will reach only $8.1 billion, the lowest in seven years. If October through December merely matches third quarter levels, a $7.1 billion annual total would be the worst in eight years.



Cooled Commissions

Every revenue source, without exception, took it on the chin during 3Q 2002. Despite a great start for the third quarter from a commissions-only standpoint, July's record share volume and volatility (albeit on cascading prices) was immediately followed by a one-third plunge in that volume for the balance of the quarter. As a result, third quarter commission revenues of $6.7 billion were down 5.7% from the previous quarter. Still, the quarter's commissions slightly outpaced 1Q 2002's $6.6 billion and remained 10.5% above last year's third quarter total. However, one factor keeping 2002 commissions above last year's level is a rapidly adopted new policy of charging commissions on Nasdaq trades versus the prior method of booking a trading gain earned from the spread. If the Nasdaq pricing change is factored out, domestic commissions would have hit a four year low during the third quarter. Over the near term, any commission comparisons to pre-2002 levels will be artificially biased upward.

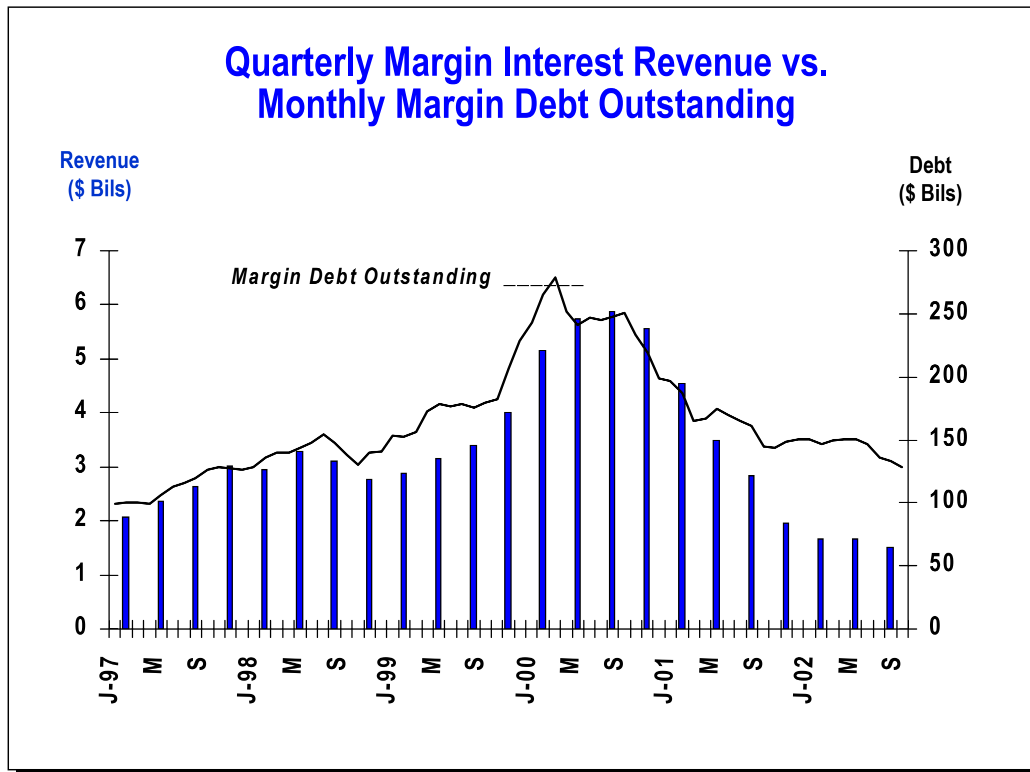
At the quarter's close, the Nasdaq Composite Index tumbled to a six year low, 1172.06, its lowest level since September 1996. This brought the Nasdaq crash to a historic 77% decline since its peak in March 2000, just 2 ½ years ago. Meanwhile, the S&P set a five-year low while Dow Jones Industrial Average set a four year low (see "Monthly Statistical Review" at the end of this report).



Asset Management Meanders Down

The market declines played havoc on assets under management which were further diminished by actual asset outflows from retail investors continuing to flee equities. According to Bernstein Research, retail activity has plunged 66% since the first quarter of 2000. Worse still, Bernstein's analysis of retail activity in previous cycles indicates that there is no relief in sight. They note that "even if the equity market bottom was last month, retail activity will not fully recover until 2004 – not a pretty picture."

What assets have remained in managed accounts continue to shift decidedly away from the higher margin equities area. As a result, third quarter asset management fees fell to $3.0 billion, 8.4% below second quarter levels, 6% below the level for the like period last year and at lows not seen since 1999. The same factors hurt revenues from the sale of mutual funds which fell to $1.5 billion in 3Q 2002, a 6% decline from second quarter levels.



Not only have commissions, asset management and mutual fund revenues suffered from a sidelined investors, margin interest income has suffered as well, hit by a double whammy – lowered activity on record low interest rates. Margin balances are back to 1999 levels while interest rates are back to 1960s levels. The result -- quarterly margin interest revenue is now down to $1.5 billion, a mere 25% of the amount earned just two years ago, $5.9 billion in 3Q 2000, and the lowest quarterly showing in seven years.

Implosion in Investment Banking

Investment banking revenue, already shriveled for much of the past year, imploded in 3Q 2002. Underwriting revenue of $2.9 billion in 3Q 2002 came up $1.0 billion short of the preceding quarter's total and was the lowest since 3Q 1998. For details on underwriting activity, see the "Monthly Statistical Review" section at the end of this paper.

While actual M&A revenue dollars are buried in the FOCUS Report's "other revenue related" line along with interest income, the consensus is that it's the worst its been in many, many years. All areas have been hit hard, a little harder in the U.S. than overseas and hardest in the technology and communications areas. It also is not getting any better -- only $38 billion in global M&A deals were announced in September, the worst of the year and a mere three-fifths of the second worst month this past February, when globally announced M&A deals reached only $70 billion.

With no improvement in sight, investment banks are even scrambling for lower credits and smaller deals that they previously would have shunned. Further, even the final holdouts have begun to let go of talented bankers which they had been keeping in reserve for the "just over the horizon" market recovery that is now off of most firms' radar screens entirely.

Plunging Principal Transactions

Even the one saving fountain of revenues during early 2002, fixed income trading, largely dried up during 3Q 2002 as did any remaining vestiges of profitability growth. Although fixed income activity levels remained active, July's WorldCom bankruptcy catapulted credit spreads to the stratosphere for the entire quarter as already credit-spooked investors rushed to the short end of the Treasury curve. This, combined with a collapse in equity prices to four or six year lows by the quarter's close, hammered equity and fixed income trading revenues down another 20% from the prior quarter's already anemic level. At $1.9 billion, 3Q 2002 trading gains are a mere 14% of their 1Q 2000 level and touched a 15-year nadir set in the crash quarter during 1987.

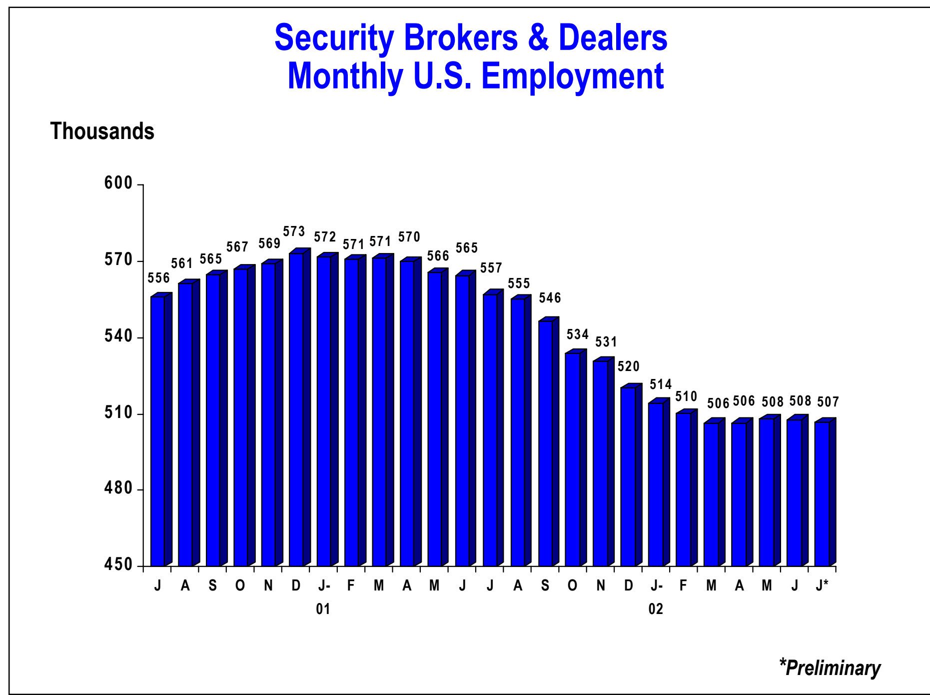
Meanwhile, realized and unrealized losses in firms' own investment accounts from severe inventory markdowns pushed this revenue line further into the red, for a loss of $400 million in 3Q 2002 from a loss of $339 million in the preceding quarter.

Compensation Cost Cutting

Quarterly compensation and benefit costs of $13.0 billion for the third quarter will be 10.1% lower than the prior quarter and 6.8% below the year-ago period due to both lower headcount and reduced payouts and bonus accruals. This is also a 36% reduction in total compensation from its quarterly apex of $20.2 billion in 1Q 2000. However, total compensation's share of net revenue is still a relatively high 55.1% and needs to be closer to 50% and preferably below that threshold. Even during compensation's peak in 1Q 2000, the ratio was an acceptable 51.1%. Nevertheless, industry management has done a remarkable job of keeping this ratio from climbing even higher given that net revenue itself has plunged an unprecedented 40% since 1Q 2000.

According to the Department of Labor, employment among "security brokers and dealers" (the subset of security and commodity brokers, dealers, exchanges and services) peaked at 573,200 at year-end 2000. The industry then trimmed 66,800 jobs, or 12% of the workforce, over the next 1 ½ years. We expect these figures are conservative, with announced layoffs not yet reflected on unemployment rolls and with actual layoffs not reflected until next Spring's annual benchmarking is completed.

In dollar terms, the industry had already cut 12% from its domestic compensation and benefits last year, from $69.0 billion during employment's peak year, 2000, to $60.6 in 2001. Our estimate for full-year 2002 compensation is $54.8 billion, a further 10% cut. This amounts to an unprecedented 21% cumulative cut in compensation in just two years' time. In comparison, the last drastic payroll cuts came during a longer three-year period, 1987-1990, and at that time compensation was cut by one-third less, just a cumulative 14%.



Other Expenses

Floor brokerage and clearance costs continued to rise in the third quarter, climbing 14% from the prior quarter and 24% over the year-ago quarter.

Amortization costs will drop thanks to FASB 142, the treatment of "Goodwill and Other Intangible Assets," which no longer allows amortizing goodwill expenses from prior mergers, producing an automatic expense reduction this year — at least on paper.

Occupancy and equipment costs experienced a slight 7.5% bump up during the third quarter. However, compared to the year-ago quarter, they were down 19% and our full year estimate calls for a 14% drop in annual costs for this line.

Promotional spending has been held in check at around $500 million per quarter and our full-year estimate shows an annual decline of 17% to $2.0 billion in 2002 from $2.4 billion last year.

Conclusion

The industry is in the grip of a major bear market, one that keeps defying all predictions of a bottom. Even if we touched a bottom today, retail activity will not return to its 2002 record level until at least 2004. Meanwhile, full-year 2002 profits are likely to set seven or eight-year lows. Management has done a very good job at trying to curtail costs in light of revenue reductions. However, with quarterly revenues down more than 40% in less than two years time, there is just so much cost cutting that can be achieved. This is particularly true now that interest rates are already at 40 year lows, can hardly be meaningfully cut more, and are just as likely to rise in the near-term than hold steady.

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UPDATE: INTERNATIONAL SECURITIES INITIATIVES

SIA plays a leading advocacy role in international securities initiatives for its member firms for several important reasons. **First**, the United States is the leading exporter of financial products and services in the world. Financial services firms based in the U.S. exported $19.5 billion in the year 2000. This figure represents a record, and exceeds the export numbers of all other service industries, according to a recent SIA white paper, with the exception of the travel industry.[1] The U.S. imported financial products and services worth $13.7 billion in 2000.

Second, 11% of U.S. holdings at the end of 2001, or $2 trillion, were foreign securities. In 2000, U.S. investors received dividend and interest payments of more than $70 billion on the $1.5 billion of those holdings that represent stocks. **Third**, levels of U.S. foreign direct investment (FDI) are more than ten times higher now than they were in 1980; at the end of 2000, levels FDI reached almost $6 trillion. That number is representative of more than 63,000 parent firms and almost 822,000 foreign affiliates.

These numbers clearly show that access to world markets is of enormous value to American financial services firms. Therefore, in this article we review some recent regulatory initiatives that are likely to affect SIA member firms operating internationally. These initiatives include: **1)** the European Union's Financial Services Action Plan (FSAP); **2)** U.K. and European regulators' discussion/position papers on analyst conflicts and internalization, respectively; and **3)** regulatory agreement on a number of important issues related to the New Basel Capital Accord. In a following issue of *Research Reports*, we will review the status of industry initiatives such as straight-through processing (STP), and selected competitive developments in cross-border clearing and settlement.

The European Union Financial Services Action Plan

The European Union (E.U.) adopted the FSAP in June 1999, aiming to develop a single, integrated E.U. capital market by 2005.[2] The plan includes more than forty banking, insurance and securities measures. These measures are divided into three categories: developing a single E.U. institutional market; ensuring open and secure retail markets; and developing state-of-the-art prudential rules and supervision. Here we briefly highlight four measures: **1)** the Financial Conglomerates Directive; **2)** the Investment Services Directive; **3)** the Prospectus Directive; and **4)** the Market Abuse Directive. The E.U. Capital Adequacy Directive is discussed below in the section on the status of the New Basel Capital Accord.

First, the Financial Conglomerates Directive involves the introduction of group-wide supervision of financial conglomerates. Under this Directive, E.U. supervisors determine whether an entity in the E.U. whose parent company is outside the E.U. is subject to consolidated supervision that is "equivalent" to E.U. regulation. If regulation is not found to be "equivalent," a firm based in the U.S. might be required to establish an E.U.-based holding company. Reorganization could impact the internal functions of the firm, perhaps most significantly the risk management function.

Second, the Investment Services Directive[3] is designed to establish an E.U.-wide "passport" allowing for cross-border investment and trading of securities. A consultation round that began in March 2002 focused on alternative trading systems, specifically concentrated on issues of trade transparency when transactions are not carried out on traditional exchanges, and how to regulate order flow internalized by investment firms.

In the September 27, 2002 issue of *Financial Times*, there are two articles related to this Directive.[4] These articles claim that a European Commission proposal providing for unfettered cross-border securities trading within the E.U. that was drawn up after a "two-year consultation with market participants" will be officially unveiled in November. Under this proposal, investment banks will be allowed to internalize trades.

Third, the Prospectus Directive[5] addresses the processes by which prospectuses are approved in cases where securities are to be sold in more than one E.U. state, and attempts to harmonize definitions and exemptions, and standardize disclosure requirements. Under the Directive, however, U.S. issuers would be obliged to deal with the member state in which the issuer first listed a security. Permitting issuers to choose the competent authority by which a prospectus is reviewed, subject to reasonable nexus requirements (e.g., where the securities are to be listed or offered or where the issuer is organized) would facilitate the realization of a single financial services market. Also under the Directive as it is currently drafted, prospectuses will remain subject to annual updates. Moreover, the definition of non-equity securities fails to include instruments such as convertible bonds.

Finally, the Market Abuse Directive restates, with some modification, the current Insider Dealing Directive, and creates a new offense of "market manipulation." Effectively, under this Directive, if a firm provides financial advice in connection with a proposed merger, it cannot also act as that company's broker or trade in its shares, as it would have access to non-public information through its advisory role. Moreover, the absence in the Directive of an element of "intent" in the definition of the offenses creates strict liability and raises the possibility of prohibition of current practice.

European Discussion/Position Papers: Analyst Conflicts, Internalization

In July 2002, the U.K. Financial Services Authority (FSA) released Discussion Paper 15, entitled, "Investment Research; Conflicts & Other Issues." The paper details FSA views on the potential for analyst conflicts of interest, compares their risk-based approach to regulation with that of other countries, in particular that of the U.S., outlines "market-based options" for consideration, and invites comment on those options by October 30, 2002.

The paper asserts that "problems" with allegedly biased investment research have thus far been less evident in London, and that investors there have not approached regulators with complaints about bias. The paper also notes, however, that the same firms operating in the U.S. market also dominate the U.K. market. The options that the FSA outlines for consideration include: **1)** maintaining the status quo**; 2)** review visits by the regulator; **3)** measures to increase investor awareness and understanding; **4)** additional regulatory rules/guidance such as aligning U.K. rules with the approach of "overseas" regulators (i.e., the SEC) and/or the introduction of registration, training & competence requirements for analysts; and **5)** steps to discourage subject company pressure on analysts. The paper asserts that, "the appropriate regulatory solution would need to recognize that it may not be possible for analysts employed by integrated investment firms, to be wholly independent." The FSA concludes by stating that they have not decided in favor of any one particular approach, and that they do not see these approaches as mutually exclusive.

Also in July of 2002, the Netherlands Authority for the Financial Markets released a Position Paper entitled, "In-House Matching."[6] The paper does conclude that the internalization of agency orders and principal trades should be allowed.

However, the paper also asserts that internalizing retail orders could: **1)** have a negative impact on liquidity in the main liquidity pool; **2)** result in wider spreads and more volatile prices; and **3)** damage the quality of price discovery. Based on these assertions, the Authority takes the position that, to ensure the adequate functioning of markets, internalization must be subject to two conditions: **1)** full pre-trade transparency; and **2)** access.

The paper does not, however, produce any empirical evidence that internalization without full pre-trade transparency and access is detrimental to investors, or that mandatory order exposure would result in more efficient markets. It is possible, for example, that if pre-trade transparency is mandated, some broker-dealers that otherwise would engage in internalization may not be willing to assume the risk of making liquidity available to the market as a whole, and therefore may decide not to provide internalization services to their customers. Mandatory order exposure also may destroy the incentives for markets to innovate and improve their services. Finally, it is possible that mandatory order exposure may award market impact to even relatively small orders, and thereby dramatically increasing the costs of OTC trading of listed stocks. In each of those instances, investors are those who ultimately would be disadvantaged. The Netherlands Authority should proceed cautiously with initiatives that could provide disincentives for competition and investor choice, particularly if a revised Investment Services Directive proposal will indeed be released in November (see discussion of the ISD in the previous section).

The New Basel Capital Accord: Basel II

On July 10, 2002, the Basel Committee on Banking Supervision reached agreement on a number of key issues related to the New Basel Capital Accord, which was initially released as a proposal in January 2001.[7] These key issues are outlined below.[8] The new Accord, consisting of three "pillars," will govern all business undertaken by financial holding companies, including that of their broker/dealer affiliates. **Pillar 1** establishes capital requirements related to credit and operational risk. Firms choose between a standard approach, using risk weights set by supervisory bodies, and an internal ratings-based (IRB) approach. Firms choosing the latter will have a higher qualification standard than under the former, and will likely be subject to increased disclosure requirements under Pillar 3. **Pillar 2** governs supervisory review. **Pillar 3** attempts to facilitate market discipline through mandating the disclosure of a firm's capital, risk exposures, assessment processes, management processes and capital adequacy measures to other market participants.

The issues that were agreed upon by the Committee in July include: **1)** creating a new IRB risk-weight curve designed to provide a more risk-sensitive treatment of certain revolving retail exposures, including many credit card exposures; **2)** confirming that banks using the most advanced IRB approaches will need to take account of a loan's remaining maturity when determining regulatory capital, but that national supervisors may exempt smaller domestic borrowers from this requirement; **3)** approving new elements of the corporate and retail IRB frameworks and the standardized approach designed to ensure a more appropriate treatment of small- and medium-sized enterprises under the New Accord; **4)** reaffirming that there will be Pillar 1 capital treatment for operational risk, but recognizing the need for significant flexibility in the development of bank measurement and management systems under the advanced measurement approaches (AMA), and eliminating the separate floor capital requirement that had been proposed for the AMA; **5)** narrowing the gap between the amount of capital required in the foundation and advanced IRB approaches, revising the structure of the floor capital requirements to base them on Current Accord requirements, and, with the elimination of the operational risk floor, moving to a single overall floor that would apply for the first two years following implementation; **6)** agreeing

that meaningfully conservative credit risk stress testing by banks should be a requirement under the IRB approaches as a means of ensuring that banks hold a sufficient capital buffer under Pillar 2.

An updated version of the New Accord will be released for public comment in the second quarter of 2003, and will be finalized in the fourth quarter of 2003. Firms will be required to implement this new framework by year-end 2006. However, those making use of IRB and AMA approaches will need to engage in the new calculations along with the calculations mandated by the current Accord beginning year-end 2005. Currently, the Committee is collecting 2001 data on operational risk for the most recent financial year in order to refine the new operational risk charge calculation.[9] The Committee is also conducting its third Quantitative Impact Survey from October 1, 2002 to December 20, 2002, designed to help firms assess how exactly the New Accord will affect them.

In parallel, the E.U. is revising its capital requirements with the draft Capital Adequacy Directive 3 (CAD3). The E.U. regime is based on the Basel rules, but applies to all banks, securities firms and asset managers, regardless of size or geographic scope of operations. Consequently, CAD3 will have a significant impact on the European operations of investment firms and could substantially increase regulatory capital costs.

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Endnotes

1 SIA's white paper, "Why World Markets are important to U.S. Financial Services Firms," is available at: http://www.sia.com/international/pdf/Markets7-02.pdf. The U.K. is the second largest exporter, having exported $17 billion in financial products and services in 2000.

2 Based on the testimony by SIA President Marc Lackritz before the House Financial Services Committee on May 22, 2002. See: http://www.sia.com/testimony/, or "The U.S. View of Europe's Financial Services Integration," *SIA Issue Bulletin*, #104, August 2002.

3 See: http://europa.eu.int/comm/internal_market/en/finances/mobil/isd/index.htm.

4 See "Europe Plans Big Shake-up for Stock Exchanges," by Francesco Guerrera, p.1, and "Brussels Looks to Set E.U. Markets Free," by Francesco Guerrera, p.4, *Financial Times*, September 27, 2002.

5 See: http://europa.eu.int/comm/internal_market/en/finances/mobil/prospectus.htm.

6 The discussion of this paper is based on an SIA Comment Letter filed with the Netherlands Authority for the Financial Markets on September 20, 2002. See: http://www.sia.com/2002_comment_letters/.

7 This Committee, of the Bank for International Settlements (BIS), is comprised of banking supervisory authorities of the G-10 countries. In 1996, the Committee amended the 1988 capital adequacy framework, for the first time basing these requirements on financial institutions' internal risk measurement models. This New Accord is said to have been developed in response to the significant progress made to develop statistical models to measure other types of risk, most notably credit risk.

8 For more detailed information on the issues agreed upon in July, see the relevant BIS press release at: http://www.bis.org/press/p020710.htm.

9 For more information on this operational risk exercise, see: http://www.bis.org/bcbs/qis/index.htm.

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THE DOUBLE TAXATION OF DIVIDENDS

In assessing the absolute and relative costs and benefits of tax structures, we should consider to what degree the specific taxes or tax regimes encourage efficient capital formation, the growth of productivity and employment as well as contributing to long run fiscal stability and moving the tax system towards fundamental reform, such as elimination of distortions and biases.

The current tax treatment of dividends introduces a number of distortions. The most important of these is that the double taxation of dividends introduces a tax bias against equity financing and in favor of debt financing that encourages companies to become more highly leveraged. Under current law, dividends are taxed once at the corporate tax rate and then again (net of corporate taxes) at the full individual tax rate when distributed to the individual taxpayer, producing an effective tax rate sometimes greater than 60%. Although interest payments to bondholders are treated as taxable income, those interest costs are deducted from a firm's net revenue before taxes are assessed. This encourages retention of earnings and greater use of debt. It is hardly coincidental that as the average corporate dividend rate continued its long decline to historic lows last year, the corporate sector in both real terms and nominal terms is more heavily indebted than at any point in US history.

Chart 1

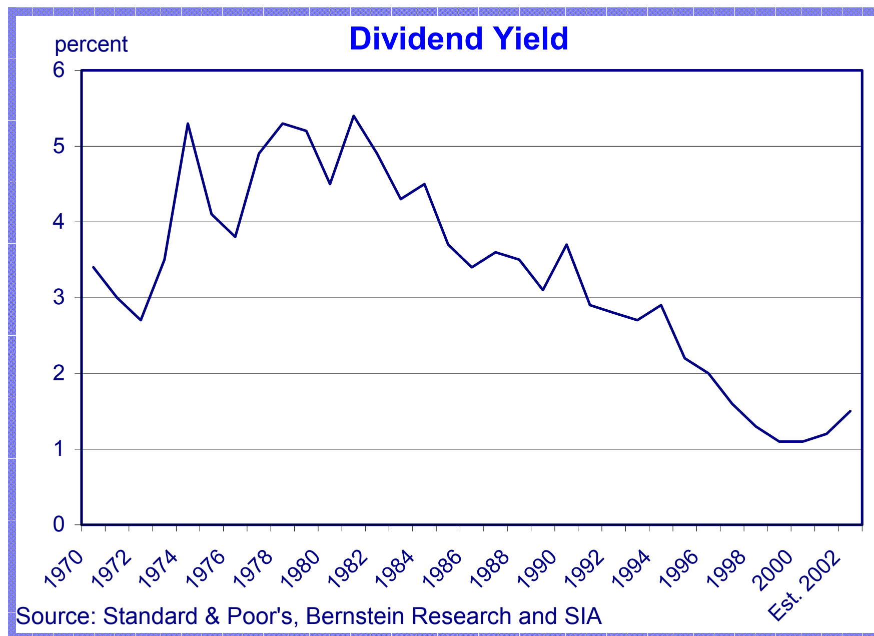
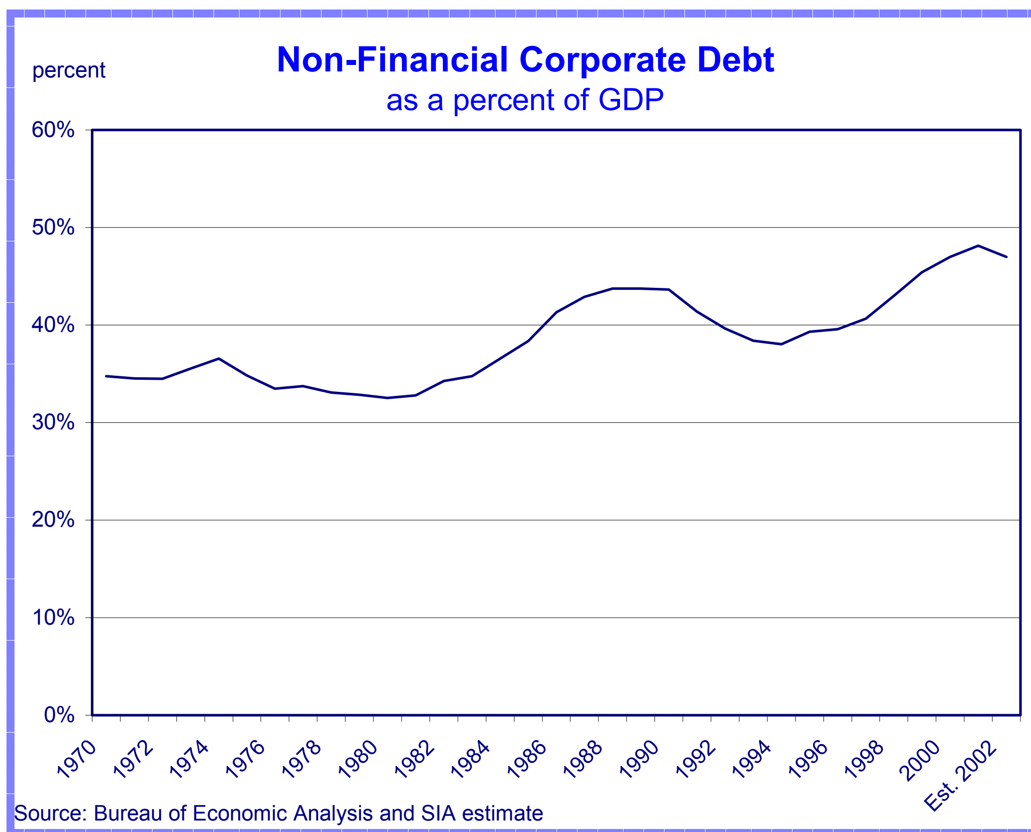


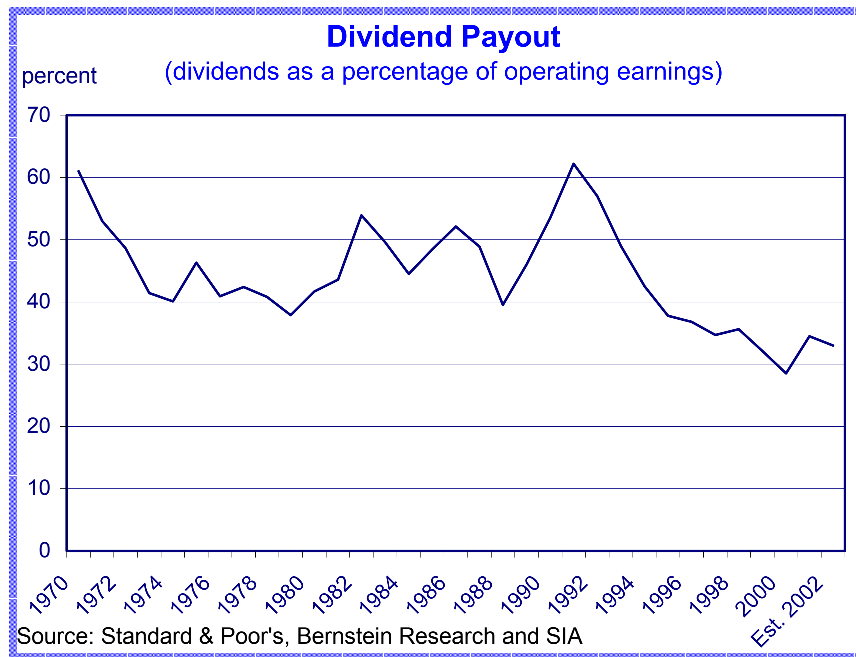
Chart 2



This bias towards greater leverage leaves corporations more prone to failure when their revenues fall and/or market interest rates rise. A corporation that relies more heavily on equity financing has more flexibility to meet fluctuations in the business cycle, reducing or raising dividends to reflect changes in net income. A heavily indebted company has much less adjustment capability in the face of market forces it cannot influence. Logically, one would expect higher bankruptcy rates and greater volatility in asset prices as a result.

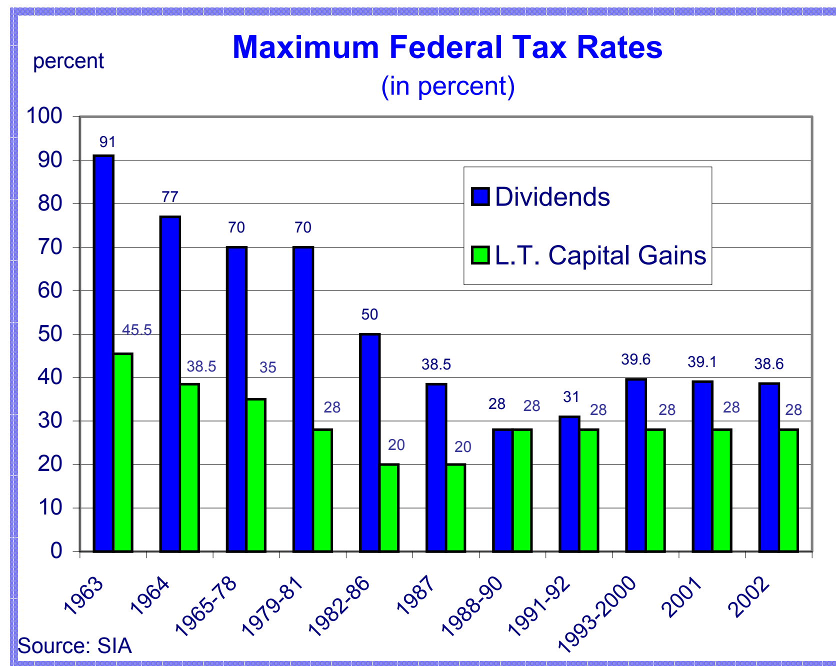
Other distortions are introduced as well. From the standpoint of the corporation trying to provide the greatest economic benefits to its shareholders, the current tax systems favors retaining earnings and using them to buy back stock rather than distribute them in the form of dividends. To the investor, the buyback raises stock prices (or prevents them from falling) and generates a capital gains tax liability only if the investor chooses to sell. To tax-sensitive investors, the lower tax rate on capital gains makes it a preferable way to receive income. A surge in buybacks in the past decade has been coincident with dramatic growth of option-based compensation programs, and, increasingly, retained earnings have been used to fund the repurchase of shares granted through the exercise of these options. During the 1990s, this form of variable compensation accounted for a greater and greater share of total compensation.

Chart 3



Bernstein Research[1] recently pointed out that "the dividend payout ratio (dividends as a percent of operating income) appears to have declined sharply from about 40% in 1990 to around 30% in 2002. However, if we include net share repurchases as part of the dividend payout, the conclusion changes, with the payout ratio actually rising since the early 1980s and remaining at historically average levels throughout most of the 1990s. Much of the shift may be attributable to the difference in the tax treatments of dividends and capital gains."

Chart 4



As dividends became less and less important in investors' expectations of the total return on investments, an equity holder looks chiefly, if not solely, to price appreciation. This may have encouraged corporate management to focus more than in the past on these and other activities that sustain stock price appreciation and relatively less on continuous, profitable operation of the firm required to sustain a long-term dividend stream.

Some see additional benefits from ending double taxation of dividends, such as "more accurate financial statements and a better alignment of management with shareholders interest" and " halt the increasing number of firms that seek to re-incorporate outside the U.S. in such tax havens as Bermuda".[2] In addition, setting dividend tax rates above capital gains tax rates may have a negative effect on share prices and future profitability and increase the cost of equity financing. Some recent studies support the "tax capitalization hypothesis"[3], which posits that firm value decreases as tax dividend rates rise, and "this price effect is independent of dividend policy".[4]

Eliminating the double taxation of dividends would lead to a greater use of equity financing by leveling the playing field between corporate equity investments and other business investments that are subject to tax only once. The movement away from debt financing would reduce risk in the corporate sector. Increasing the distribution of corporate profits through dividend payments would make it more difficult for companies to mask profitability or management problems. This proposal should lead to less focus on short-term share price movements and more attention to sustainable profitability. Depending on how it was done, this proposal could greatly simplify the tax laws.

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Endnotes

1 Bernstein Research, *Bernstein Quantitative Handbook*, September 2002, p.7.

2 Gompers, P., Metrick, A. and Siegel, J., "This Tax Cut Will Pay Dividends," *The Wall Street Journal*, Opinion page, August 13, 2002.

3 Fama, E.F., and French, K.R., "Taxes, Financing Decisions and Firm Value," *Journal of Finance* 53, 1998, pp. 819-843.

4 Hubbard, Glenn R., Kemsley, D. and Nissim, D., "Dividends, Capital Gains and Taxes," Columbia Univ., May 2001.

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ANALYST UPDATE AND LEGAL ALERT

Following is a legal alert released by SIA on August 15th that provides important information about: 1) SRO analyst rules and guidance; 2) the terms of the Merrill Lynch settlement with the New York State Attorney General; 3) proposed SEC Regulation Analyst Certification (AC); and 4) implications of the Sarbanes-Oxley Act. Since that alert was released, there have been several developments with regard to these issues. First, SIA filed a comment letter with the SEC on September 23rd suggesting revisions to clarify or strengthen the provisions in the proposed Regulation AC. These include: 1) clarifying the function and scope of "certification;" 2) ensuring that the new rule is consistent with the rules of self-regulatory organizations; and 3) addressing issues arising from disclosures during public appearances.[1]

Second, it was announced that Salomon Smith Barney reached an agreement with the NASD to pay $5 million to settle a civil suit relating to research on Winstar Communications.[2] Several days after that, the press reported that Citigroup offered "to create a new, separate research company…as part of a global settlement with regulators."[3] Around that same time, the press reported that SEC Chairman Harvey Pitt was "expected to require for the first time that Wall Street research departments clearly be split from investment banking operations," and that such a "proposal is still being formulated."[4] Finally, The Financial Times reported that the NYSE was "to propose a further separation of analysts' research work and investment banking activity," an initiative that is expected to be announced this week.[5]

August 15, 2002: Legal Alert 2002-07

Regulatory and Legislative Actions Regarding Analyst Integrity.

Controversy over sell-side analyst objectivity, while dating back to the deregulation of brokerage commissions in the mid-1970s, became vastly more acute as a result of the "high tech" boom of the 1990s and the proliferation of business reporting on the Internet and cable television. While some analysts became minor celebrities for a time, public adulation turned to anger when most analysts failed to foresee the sharp decline in technology stocks in late 2000 and early 2001.

Critics pointed to many instances where broker-dealer analysts maintained buy ratings, and/or optimistic price targets, on many high-tech companies even as their stock prices plummeted, and charged that these analysts' views were tainted by pressures from their firms' investment banking departments, which either had investment banking ties with, or sought business from these companies. This criticism resulted in a series of Congressional hearings beginning in the spring of 2001. SIA adopted a set of best practices intended to strengthen investor confidence in the integrity of analyst recommendations. However, since these were voluntary standards they did not satisfy critics. The epic financial scandals at Enron and Worldcom further inflamed antagonism toward sell-side analysts, since many analysts following these companied maintained positive ratings right up until the moment the scope of the apparent wrongdoing was exposed.

All of this fueled notable regulatory and prosecutorial developments, as well as provisions of the newly-passed Sarbanes-Oxley Act addressing analyst conflicts. These developments are summarized below.

1. Summary of NASD and NYSE Analyst Rules and Interpretive Guidance.

On May 10, 2002 the Securities and Exchange Commission issued an order approving significant amendments to NASD Rule 2711 of the National Association of Securities Dealers, Inc. and Rule 472 of the New York Stock Exchange. These amendments are intended to deal with the current high level of public concern about buy-side equity securities' conflicts of interest, and the impact that those conflicts may have on recommendations and price targets contained in analysts' research reports. On June 26, 2002 the NYSE and NASD issued a Joint Memorandum providing interpretive guidance on some aspects of the new rules.[6] This section summarizes both the rules and the guidance.[7]

The NASD and NYSE have substantially identical provisions. They apply to "research reports," the persons who prepare them, and their firms.

"*Research Reports*."

The term "research report" is defined as "a written or electronic communication which includes an analysis of equity securities of the individual companies or industries, and which provides information reasonably sufficient upon which to base an investment decision and includes a recommendation."

The definition does not apply to non-equities research, such as research on fixed income securities, currencies or commodities. In addition, compendiums of research that cover six or more companies need not contain the required disclosures, but instead can refer prominently to a place (such as a web site) where the current disclosures can be found. The guidance states that the term does not cover

- reports discussing broad-based indices, reports commenting on economic, political or market conditions that do not rate or recommend individual securities,

- technical analysis concerning demand and supply for a sectors, index or industry based on trading volume and price,

- statistical summaries of multiple companies' financial data,

- reports that recommend increasing or decreasing holdings in particular industries or sectors, but that do not recommend or rate individual securities,

- notices of ratings or price target changes that doe not contain any narrative discussion or analysis of the company, provided that the report directs the reader of the notice as to where they may obtain the most recent research report on the company that includes the disclosures required under the rules,

- an analysis prepared for a specific customer's account, and

- internal communications that are not given to customers.

The definition also provides that, where a member firm distributes research in the U.S. prepared by a nonmember affiliate, the disclosures apply only to the member firm. The disclosure requirement does not apply to independently produced research. The SRO guidance adds that, where a firm distributes research from a foreign affiliate or investment adviser affiliate, or through an independent third party (other than a soft-dollar arrangement) the research must include disclosures concerning the member's and its affiliates' ownership of the subject company's securities (as described below), the member's or its affiliates' underwriting or compensation relationships with the issuer (described below), or any other actual, material conflict of interest of the member known at the time of distribution of the research report. While these requirements are significant, it is notable that the quiet periods for research by lead and co-managing underwriters (described below) apparently do not apply to third-party research distributed by those underwriters.

The guidance also indicates that a member will not be considered to have distributed third-party research to a customer if the customer independently requests it or accesses it through a web site that permits customers to select their own research.

Restrictions on Investment Banking Department Relationship with Research Department.

The new rules prohibit investment banking from exercising supervision or control over research analysts. In particular, investment bankers cannot review or approve a research report prior to publication, except to verify factual accuracy or to review for any potential conflict of interest.

Any written communication between a research analyst and investment banking personnel regarding a draft research report must be made through a legal or compliance official, or such an official must be copied on the document (the "intermediation requirement"). Any oral communication must be "documented and made through" a legal or compliance official acting as intermediary, or in the presence of such an official.

For most firms the intermediation requirement will take effect on September 9, 2002. The NASD and NYSE announced that they will delay implementation of these requirements until November 6, 2002 for firms that over the past three years have averaged 10 or fewer investment banking transactions per year and generated $5 million or less in gross investment banking revenues from those transactions.

Restrictions on Contacts between Research Analyst and the Subject Company.

The rules permit analysts to share draft research reports with the subject company, but only as necessary to verify factual accuracy. Any draft that is shared must omit the research summary, rating or price target. In addition, a complete draft must be sent to the legal or compliance department prior to submission to the subject company.

If the analyst proposes to change a rating or price target after submitting the report to the subject company, the research department must provide a written justification for the change to the legal or compliance department, and the legal or compliance department must provide written authorization for the change. The draft and final version of a research report that is changed in this manner must be retained for three years following publication.

A subject company can only be notified of a change in its rating after the close of trading in its principal market on the business day prior to publication of the change.

Prohibitions and Restrictions on Analysts.

Compensation. Broker-dealers cannot pay any bonus, salary or other form of compensation to a research analyst that is based on a specific investment banking services transaction. The SROs' guidance indicates that firms can compensate analysts pursuant to contractual commitments entered into before the July 9, 2002 effective date of this provision, for deals that closed prior to that date.

Promises of Favorable Research. A broker-dealer cannot directly or indirectly offer to a company favorable research, a specific rating or price target, or threaten to change research, a rating or a price target, as consideration or inducement for business or compensation. However, the SROs' guidance states that this does not prevent a firm's

investment banking department from getting a research analyst's view of a prospective client before committing to undertake an investment banking transaction. The guidance also indicates that a firm can agree to provide research as part of its investment banking agreement with a company, as long as there is no promise that the research will be favorable.

Restrictions on Personal Trading. These restrictions apply to "research analyst accounts," which are defined to include any account over which a member of the analyst's household has a financial interest or over which the analyst has discretion or control, other than a registered investment company. The SRO guidance indicates that the term "research analyst" does not encompass registered representatives who recommend securities to their customers, and also excludes investment advisers, such as mutual fund portfolio managers, who are not principally responsible for preparing the substance of a research report. Consequently, the personal trading restrictions do not apply to these individuals.

The trading restrictions include the following:

- Research analyst accounts are barred from selling any securities (including options or derivatives) of a company that the analyst follows during the 30 calendar days prior to publishing a research report or changing a rating or price target on the company, and for 5 calendar days after such a report or change. Exceptions are provided for sales within 30 days of beginning coverage of a company, or for research or ratings or price target changes due to significant news or events, if the legal or compliance department pre-approves the report or change.

- Analysts must not purchase or sell securities in a manner inconsistent with the analyst's most recent published recommendation.

- Trades can be excepted from the restrictions described above if they are based on an unanticipated significant change in the analyst's personal financial circumstances, if pre-approved by the legal or compliance department.

- An analyst cannot receive any pre-IPO securities of an issuer that is principally engaged in the same type of business as companies that the analyst follows.

None of these restrictions on analyst accounts apply to purchases or sales of securities of a registered diversified investment company. They also do not apply to purchases or sales of securities of any other investment fund not controlled by the analyst or a member of the analyst's household, provided that the analyst owns less than 1 per cent of the fund assets, the fund invests no more than 20 per cent of its assets in issuers principally engaged in the businesses of companies covered by the analyst, and if the fund distributes securities in kind to the analyst or a household member prior to an IPO, the analyst either divests them immediately or refrains from preparing research on that company.

The SRO guidance clarified several open issues about these restrictions, including the following:

- An analyst need not divest pre-IPO shares of a company that the analyst owned before the new rules took effect. However, a research analyst in such a situation cannot provide research on the company until the analyst divests all pre-IPO shares in the company.

- The blackout periods on analyst trading run based on when a research report is first disseminated.

- Holdings of investment funds that were received prior to the July 9, 2002 effective date of these provisions are not subject to these restrictions, unless additional investments are made in these investments after July 9. In that case, all fund holdings would become subject to the trading restrictions.

- The restriction against an analyst account trading against the analyst's recommendations will not apply until November 6, 2002 in situations where the member firm is in the midst of adopting a policy that bans outright research analysts' ownership of stocks that they cover, and the analyst is liquidating his or her position according to a plan approved by the firm's legal or compliance department, and the firm notifies the NASD and/or NYSE about its intent to delay implementation of this provision.

Disclosure Requirements.

A broker-dealer must disclose in research reports:

- whether the analyst or a household member has a financial interest in the securities of a subject company, and the nature of that interest (i.e., option, right, warrant, future, long or short position);

- if, as of the month immediately preceding the of publication of the report (or the end of the second most recent month if the date is less than 10 calendar days after the end of the most recent calendar month) the broker-dealer or its affiliates own more than 1 per cent of any class of common equity securities of the subject company. Computation of ownership is to be made using the same standards as under Section 13(d) of the Exchange Act;[8]

- whether the analyst principally responsible for preparing the report received compensation that is based in part upon the broker-dealer's investment banking revenues;

- whether the broker-dealer or its affiliates managed or co-managed a public offering of the securities of the subject company in the past 12 months, received compensation for investment banking services from the

subject company in the past 12 months, or expects to receive or intends to seek compensation for investment banking services from the subject company in the next three months;

- whether the analyst or a member of the analyst's household serves as an officer, director or advisory board member of the subject company;

- any other actual, material conflict of interest of the analyst of which the analyst or broker-dealer knows or has reason to know, and any other actual material conflict of interest of the broker-dealer of which the broker-dealer has reason to know at the time of publication of the report.[9]

The analyst must also make the above disclosures in public appearances, except that, instead of disclosing information about investment banking compensation, the analyst must disclose whether the subject company is an investment banking services client of the broker-dealer or its affiliates. The SRO guidance indicates that analysts are only responsible for providing this material to a broadcaster when the analyst makes a television appearance, and will not be held accountable if the broadcaster cuts out the disclosure. However, the SRO guidance states that the analyst should decline further appearances on an outlet that has previously edited out the disclosures.[10] The public appearance obligations also do not apply to appearances outside the United States. It is not clear whether these disclosure obligations apply to interviews with the print media.

The SRO rules permit a firm to use its own distinctive ratings categories, as long as the firm gives a clear explanation in each research report of the meaning of the ratings terms used. Regardless of the ratings system that a firm uses, the rules require the firm to disclose in each research report the percentage of all securities rated by the firm to which it would assign a "buy," "hold/neutral," or "sell" rating. The firm must also disclose the percentage of companies in each category for whom the firm has provided investment banking services in the past 12 months. If the firm does not use this or similar nomenclature in its ratings system, it must use its judgment to determine into which of these three categories each of its ratings should fall. If the firm employs multiple ratings systems based on the investor's time horizon (e.g., short term buy, medium term hold, etc.), the firm must disclose the distribution of ratings used in each rating system. .

Research reports on equity securities that have been covered for at least one year must also contain a line graph of the security's daily closing price for the period in which it has assigned a rating, up to 3 years. The graph must indicate the dates when ratings or price targets changed, "depict" each rating and price target on those dates, and be current as of the most recent calendar quarter (or the second most recent quarter if the report is issued within 15 days of the end of the most recent quarter.[11] The written guidance from the SROs indicates that

- firms can substitute a table containing all the required information for a chart if the report is delivered through a technology that does not allow transmission of graphic illustrations;

- If the firm uses a multiple ratings system based on time horizons, its chart or table must provide ratings and price targets under each ratings system;

- Firms can include benchmarks such as the S&P 500 Index in their charts;

- In situations where coverage of a security is passed from one analyst to another, the chart should reflect all ratings and price targets during the specified period, regardless of a change in the analyst providing coverage; and

- In situations where there are breaks in coverage, the clock will not restart to determine if coverage has been in effect for one year. In addition, the price charts should indicate breaks in coverage.

Research reports on equity securities must also disclose the valuation method used to determine any price target. The price target must have a reasonable basis and must be accompanied by a list of risk factors that may impede achievement of the target. Firms must also disclose in research reports if they make a market in the securities of the subject company. In addition, firms must induce any other disclosures required by other NASD or NYSE rules, or by the antifraud provisions of the federal securities laws. The disclosures required under the new rules must be presented on the front page of the research report, or the front page must refer to the page on which disclosures are found. Disclosures "must be clear, comprehensive and prominent."

All of the disclosures required in research reports must appear on the front page of the report, or the front page must refer to the page where the disclosures are found. In any event, the disclosures must be prominent and clear. In the case of electronic research reports, hyperlinks can be used to the required disclosure, provided that the first screen that users see clearly and prominently labels the hyperlinks. If hyperlinks are not possible, as in the case of a report in PDF format, the report should follow the same format as for paper reports.

The rules provide an exception from the disclosure requirements for "compendium" reports that cover six or more companies, as long as the compendium directs readers in a clear manner to a means of obtaining the disclosures, such as by reference to a toll-free number or postal address. Nevertheless, the SROs' written guidance encourages firms to disclose in compendium reports the information about ratings distributions, since this information will be the same regardless of the number of companies covered in the report.

Imposition of Quiet Periods.

The rules bar a lead or co-managing underwriter from publishing a research report regarding a public company for 40 calendar days following an initial public offering, or from 10 calendar days following a secondary offering. The rule provides two exceptions: (i) research can be published during these periods concerning the effects of "significant news or a significant event" on the subject company, if given prior authorization by the legal or compliance department; and (ii) research can be published regarding a secondary offering pursuant to Rule 139 of the Securities Act of 1933 if the

company has "actively-traded securities" as defined in Regulation M under the Securities Exchange Act of 1934.

The SROs' written guidance clarifies that this provision is only intended to apply to "equity security" offerings, as defined in Section 3(a)(11) of the Exchange Act. It therefore would apply to convertible debt offerings, but not to straight debt offerings.

Notwithstanding SIA's overall support for the new SRO rules, it should be noted that SIA has specifically criticized the quiet period provisions. SIA's view is that this provision will be unintentionally unfair to retail investors, who often have no source of research on a new company other than research offered by the lead or co-managing underwriters. Institutional investors, by contrast, are likely to be able to obtain research either in-house or, in many instances, from providers outside the United States. SIA has also argued that the quiet period provision will deprive the market of information about a new company from the analysts who are likely to have the deepest understanding of its business, and at a time, just after an IPO, when investors have the greatest need for that information.

Supervisory Procedures.

The rules require every firm subject to the rules to adopt and implement written supervisory procedures reasonably designed to ensure compliance. In addition, a senior member of the firm must attest annually to the NASD and/or NYSE (whichever it is a member of) that it has adopted and implemented those procedures.

Implementation Period.

The provision on disclosure of 1 per cent positions will take effect on November 6, 2002. The provisions concerning communications between research and investment banking or subject companies will take effect on September 9, 2002. All other provisions of the rules took effect on July 9, 2002, with certain narrow exceptions until November 6, 2002 that the SROs announced shortly before the July 9 effective date. These exceptions are:

- Small broker-dealers will have a grace period to implement the requirements to have legal or compliance personnel intermediate all communications between research and investment banking regarding draft research reports;

- All firms will have a grace period to include compensation received by their foreign affiliates in the required disclosure of receipt of compensation from subject companies; and

- Subject to certain conditions described earlier, firms that are in the process of requiring analysts to divest themselves completely of securities holdings in companies that they cover will have a grace period to allow their analysts to sell those securities even if contrary to the analyst's most recent published recommendation.

2. Merrill Lynch Settlement.

On May 21, 2002, the New York State Attorney General announced a settlement of a proceeding against Merrill Lynch based on alleged improper interference by Merrill's investment banking department with research reports. The settlement includes a $100 million fine, and procedural undertakings that are largely consistent with the requirements of the new SRO analyst rules, although more detailed. These terms include the following requirements.

- Investment banking is barred from giving any input on analyst compensation, and the analyst's supervisors barred in determining analyst compensation from considering analyst's role in bringing in investment banking transactions. Apart from investment banking, other Merrill divisions can give input on analyst compensation decisions.

- The required research disclosures are similar to the SRO rules, but also include a required legend on first page of report that investors should assume that Merrill is seeking or will seek investment banking or other business from the company. (Interestingly, the NASD and NYSE staffs have stated informally that they do not want this type of boilerplate disclosure).

- Merrill is required to establish Research Recommendations Committee ("RRC"). The RRC is to monitor the performance of equity research recommendations for independence and objectivity. The Chair of the committee will have his or her bonus determined primarily by how well research recommendations perform for investors.

- Initiation of, or change in a research recommendation will require approval of RRC.

- Merrill also undertakes to hire a compliance monitor for one year to ensure compliance with the settlement agreement.

- Analyst participation with investment bankers in solicitations of any potential investment banking transaction will have to be approved in advance by RRC. Analyst must also disclose in research whether he or she participated in solicitation of investment banking transaction in the last 12 months

- Whenever Merrill terminates coverage, it must publish a report disclosing the termination, the reason for the termination, and that the last recommendation prior to termination should not be relied upon going forward

Other major firms have announced that they will voluntarily adopt the procedural changes agreed to by Merrill. Moreover, on July 1, 2002 officials from California, New York and North Carolina announced an initiative[12] to require investment banking firms that do business with their state pension plans to adhere to certain "investment

protection principles," including compliance with the terms of the Merrill Lynch settlement.

3. Proposed SEC Rule AC.

On July 24, 2002 the SEC voted to propose new Rule AC.[13] The proposed rule would require

- a clear and prominent certification on each research report that the views expressed accurately reflect the analyst's personal views, and a statement certifying that no part of the analyst's compensation is directly or indirectly related to the specific recommendation or views expressed in the report. If such a certification cannot be made, the report must certify that such compensation is affected by the specific content of the report, disclose the amount of such compensation, and state that such compensation may influence the recommendation in the report; and

- a record made by the broker-dealer for each public appearance by a research analyst that would include a written statement by the analyst containing certifications similar to those described above. If the analyst cannot certify that the views expressed are his or her personal views, the broker-dealer must disclose in all research reports for 120 days after the analyst notifies the broker-dealer that the certifications cannot be made that the research analyst did not comply with the certification requirements of the rule, and the reasons why. The record would have to be made within 30 days after each calendar quarter in which the research analyst made the public appearance.

Comments on proposed Rule AC are due by September 23, 2002.

4. Sarbanes-Oxley Act.

On July 30, 2002 the President signed into law the Sarbanes-Oxley Act of 2002 (the "Act"). While the primary foci of the Act are on regulating the accounting profession and setting standards for corporate governance, the Act also addresses the issue of analyst objectivity. As is discussed in greater detail in legal alert 2002-06, the Act "backstops" the SRO rules by requiring that the SEC or SROs adopt such rules. This may help to restore investor confidence in buy-side research. However, the statutory provisions raise a number of issues.

The Act also goes further than the SRO rules in a number of respects. For example, it contains a definition of "research report" that is broader than the SRO rules, in that it drops the limitation in the SRO rules that a document must include a recommendation to be considered a research report. This might force the SROs to amend their rules to apply the conflict disclosure requirements and trading restrictions to trading strategy reports and their authors, even though these reports and analysts are far removed from the concerns driving the debate about analyst conflicts of interest.

Another notable divergence from the SRO rules is the provision in the Act on disclosure of compensation, which requires that rules be adopted requiring disclosure of "whether any compensation has been received by the registered broker or dealer, or any affiliate thereof . . . ." In contrast, the SRO rules limit this requirement to disclosure of compensation "for investment banking services" received by the broker-dealer or its affiliates. The Act's directive to the SEC and SROs could impose very substantial compliance costs, for little if any gain in terms of useful information for investors. The SROs proposed a similar requirement, but dropped it in their final rules in response to this objection by SIA and other commenters.

Endnotes

[1] SIA's comment letter on Reg AC is available at: http://www.sia.com/2002_comment_letters/pdf/regulation_ac.pdf.

[2] Charles Gasparino, "Salomon Agrees to Settle Stock-Hype Case," *The Wall Street Journal*, Tuesday, September 24, 2002, p. C1.

[3] Charles Gasparino and Randall Smith, "Citigroup Offers Separate Research Arm in Settlement Bid," *The Wall Street Journal*, Monday, September 30, 2002, p. C1.

[4] Susan Pulliam and Randall Smith, "SEC's Pitt Seeks Split of Banking, Analyst Areas," *The Wall Street Journal*, Thursday, September 26, 2002, p. C1.

[5] Adrian Michaels, Gary Silverman, and Joshua Chaffin, "NYSE Planning to Impose Tighter Rules on Analysts," *The Financial Times*, Friday, September 27, 2002, p. 15.

[6] See NASD NTM 02-39 (June 26, 2002) and NYSE Information Memo 2-26 (June 26, 2002).

[7] The NYSE and NASD have indicated that they intend to issue further interpretive guidance at a later date.

[8] However, the SRO rules require tracking companies that may not be tracked for 13D purposes. This could pose a number of practical problems. For example, foreign securities not subject to 13D reporting also would not have CUSIP numbers, making it very challenging to track positions in those securities among global affiliates of a large multiservice financial institution.

[9] The SRO guidance states that this does not create a duty on the part of an analyst to inquire concerning confidential, non-public information that is segregated behind an information barrier.

[10] According to the SRO guidance, firms should retain records of appearances on television, radio or the Internet. Presumably this would also enable firms to determine whether the broadcaster carried the disclosures.

[11] The NASD provided an example on its web site of what how it envisions the price chart might look. See http://www.nasdr.com/pdf-text/analyst_price_chart.pdf.

[12] See http://www.oag.state.ny.us/press/2002/jul/jul01a_02.html.

[13] Release No. 33-8119, 34-46301, File No. S7-30-02, available at www.sec.gov/rules/proposed/33-8119.htm.

[14] In contrast to the SRO rules, the term "public appearance" is defined in the proposed rule in a way that seems to exclude interviews with the print media.

[15] Public Law No. 107-204.

[16] SIA stated in its comment letter on the SRO rules:

> "custodial or other pension management services to the subject company by an asset management affiliate of the broker-dealer, payroll administration services to the subject company by a data services affiliate of the broker-dealer, corporate credit cards used by the subject company and sponsored by an affiliate, or a rebate received from the subject company for office equipment purchased from it by an affiliate of the broker-dealer, all would have to be centrally tracked by the broker-dealer and would trigger disclosure under this provision. Unfortunately, disclosure this broad provides virtually no useful information to the intended audience – readers of research reports seeking to evaluate analysts' forecasts and recommendations. . . .
>
> "Balanced against the fact that the disclosure is . . . largely of no practical use, it will be extremely expensive for firms to implement systems to track this information. Firms that perform most investment banking business in the U.S. tend to be affiliates of many other large entities, located both domestically and internationally, that perform a wide range of services, not all of which are necessarily even financial in nature. Tracking on a real-time basis every form of compensation received by every entity from the issuer will be enormously expensive. This cost will translate into less timely research coverage. This requirement will also have anticompetitive effects, since it is a cost that will not be borne by other providers of research, such as a buy-side institution, financial periodical, or foreign broker-dealer, all of whom will be able to communicate recommendations of their analysts without the costs and burdens imposed by this requirement."

See letter from Stuart J. Kaswell to Jonathan G. Katz, U.S. Securities and Exchange Commission, April 11, 2002, at 16-17.

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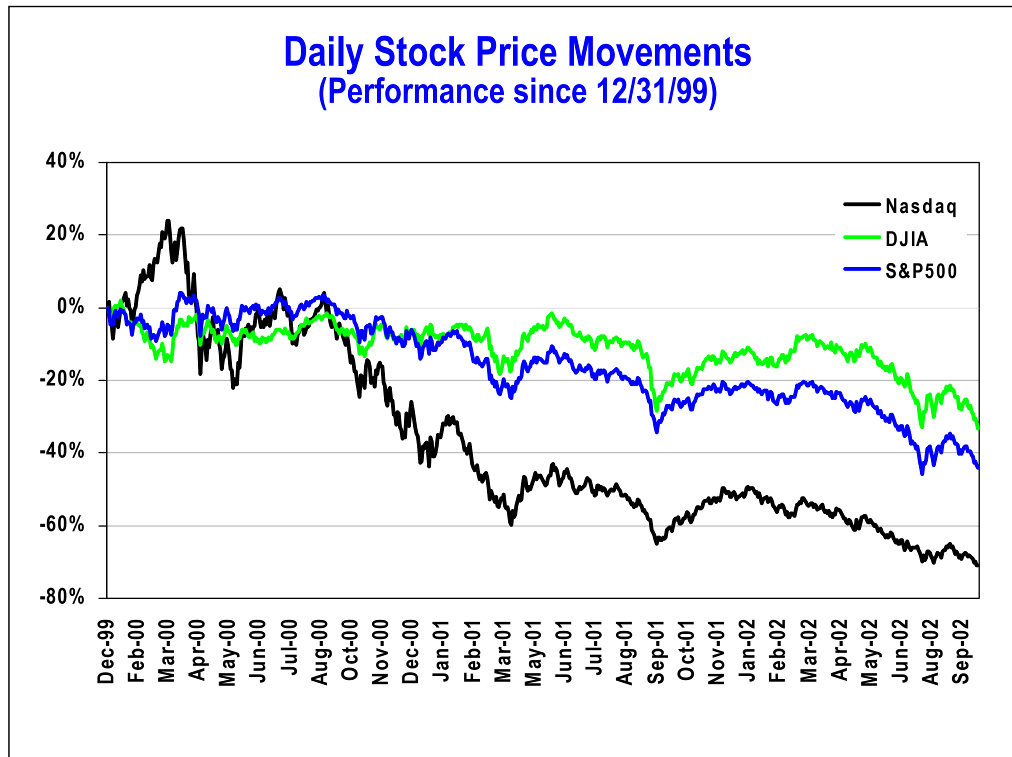
U.S. Equity Market Activity

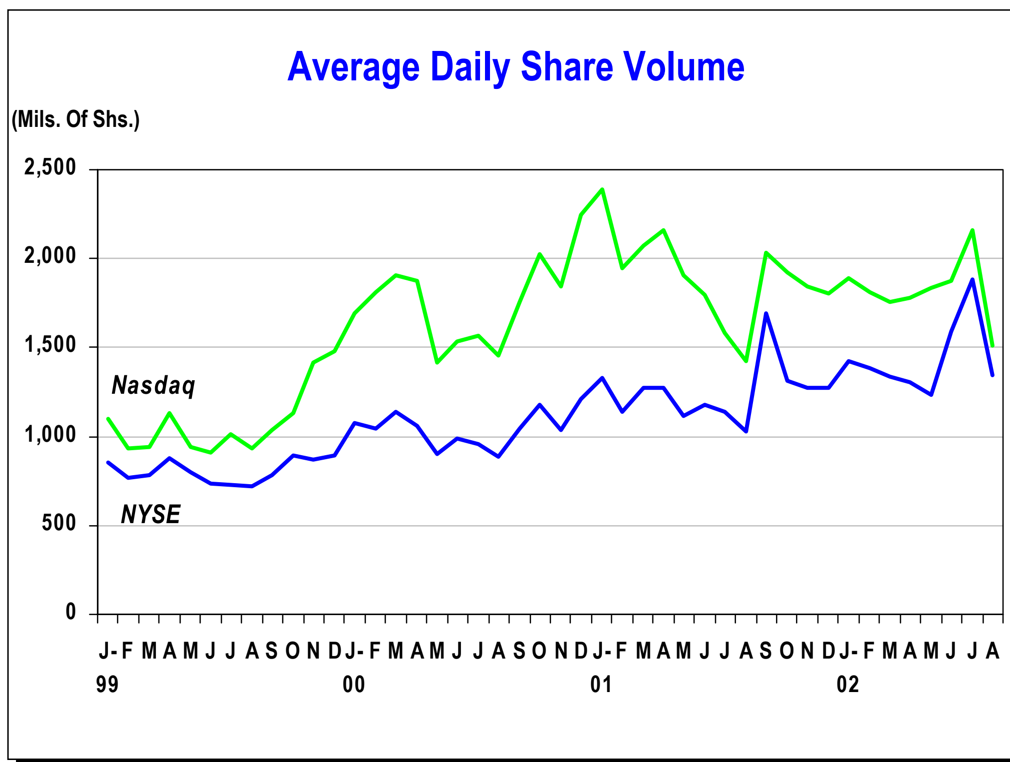
Stock Prices –Investors fastened their seat belts for the wild stock market roller coaster ride that left the gate in mid-May and continues to this day. The ride began with the S& P 500 plummeting 28% from May 17-July 23 to a five-year low of 797.70. The S&P 500 then climbed 21% to 962.70 by August 22. This was followed by four consecutive weekly losses, pushing the S&P 500 down 15% from its August peak to 819.29 on September 24. Disappointing earnings news, evidence of an economic slowdown, and threats of war with Iraq helped drag stock prices lower.

For the month of August overall, the S&P 500 index inched up 0.5% vs. July, snapping a four-month losing streak. Meanwhile, the Dow and Nasdaq Composite indexes finished the month with modest losses of 0.8% and 1.0%, respectively, recording their fifth consecutive monthly decline. A sixth month decline, the most prolonged slide since 1981, seems certain as September comes to a close. The three major stock market barometers slid an additional 10% during the first three weeks of September. Year-to-date through Sept. 24, the Nasdaq Composite has plunged 39.4%, while the S&P 500 tumbled 28.6% and the DJIA declined 23.3%.



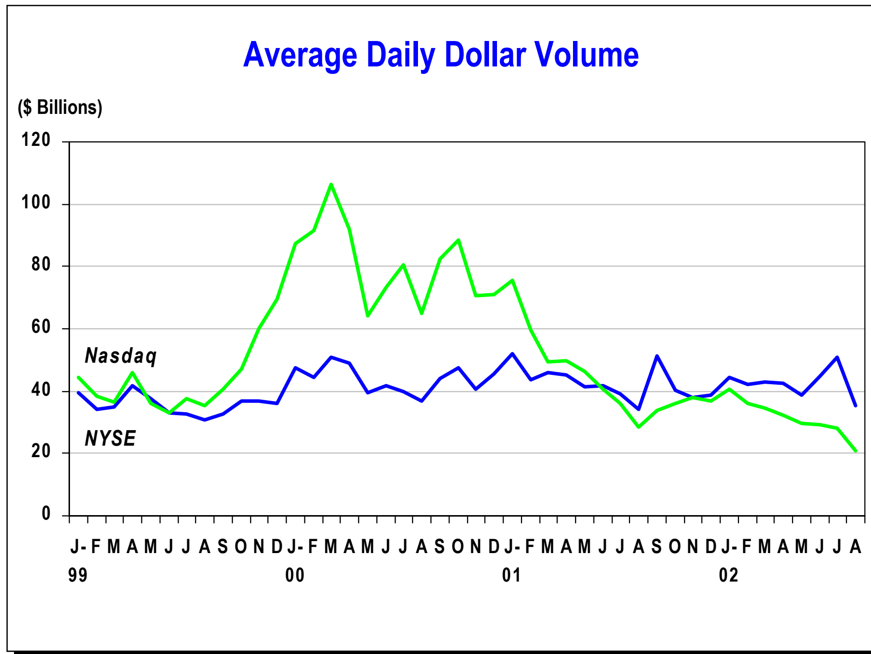
Share Volume – Average daily share volume on the major U.S. equity markets retreated in August, a common occurrence in the late summer month. NYSE volume, which surged 18.9% to a monthly record 1.89 billion shares daily in July, plunged 28.9% to 1.34 billion per day in August, marking its lowest level in three months. Despite this slowdown in trading activity, the year-to-date average of 1.44 billion shares daily is up 16.0% from the annual record pace of 1.24 billion per day set in 2001.

On Nasdaq, average daily volume sank to its lowest level of the year in August. After jumping 15.0% to 2.16 billion per day in July (its fourth best monthly volume ever), Nasdaq volume plummeted 30.1% to a 2002 monthly low of 1.51 billion shares daily in August. Through the first eight months of 2002, volume on Nasdaq is running 3.8% short of last year's pace, averaging 1.83 billion shares daily year-to-date compared with 1.90 billion shares daily in 2001.

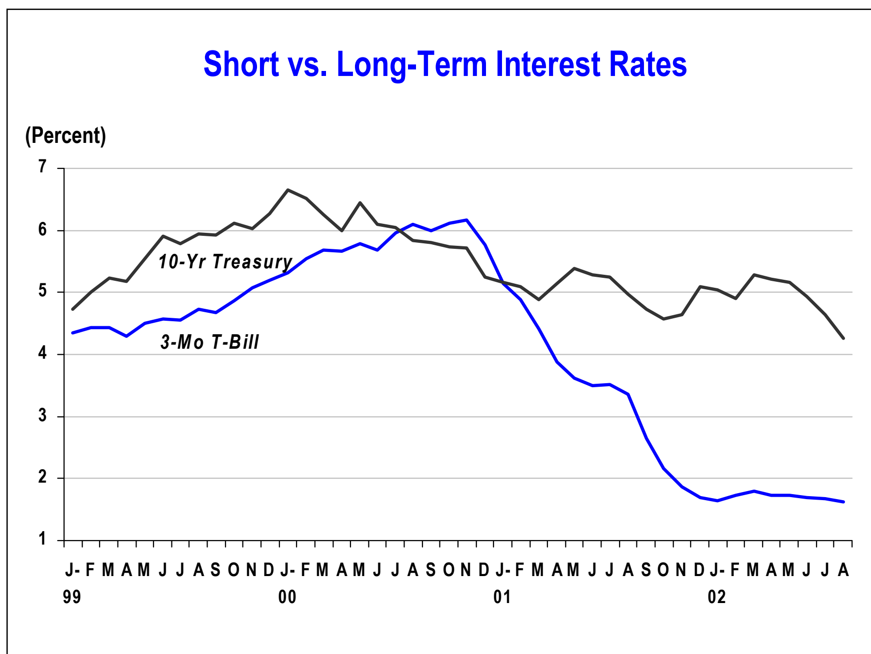


Dollar Volume – The dollar value of trading in Nasdaq stocks continued on its downward trajectory this year through August. Due to curtailed trading activity in August, the value of daily trading in Nasdaq stocks fell 25.6% from July's level to a four-year low of $20.9 billion in August. That dragged down the year-to-date average to $31.3 billion daily, a 29.0% drop from 2001's $44.1 billion daily average and 61.3% below the record $80.9 billion daily pace set in 2000.

NYSE dollar volume, after climbing to a 2002 monthly high of $50.9 billion daily in July, slid 30.3% to a 2002 low of $35.5 billion daily in August. Nevertheless, at $42.7 billion daily year-to-date, dollar volume in NYSE stocks is up a modest 0.9% over 2001's $42.3 billion daily pace, yet still trails 2000's daily record of $43.9 billion daily.



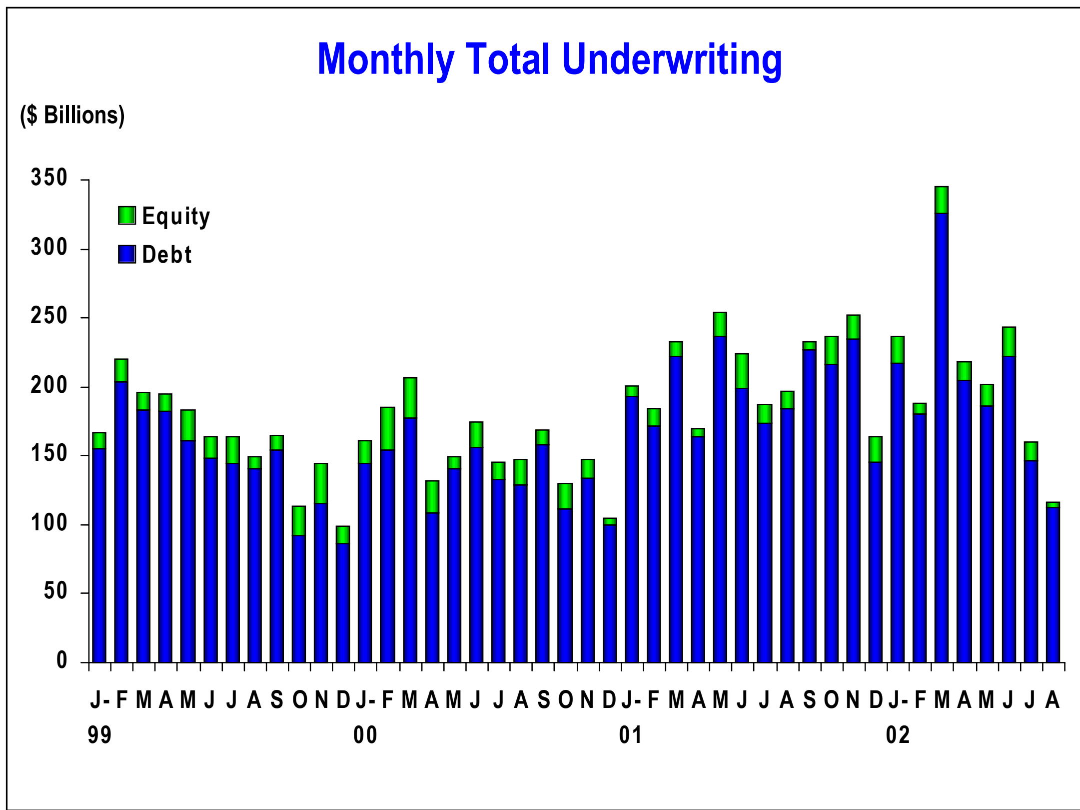
Interest Rates – Signs of economic weakness and turmoil in the stock market continued to drive a rally in Treasuries. The yield on 10-year Treasuries declined for a fifth straight month and has fallen more than 100 basis points since March. It reached a 37-year low of 4.26% in August, down 71 basis points from its year-earlier level. Meanwhile, the three-month T-bill fell on speculation that the Fed would cut the federal funds rate at its policy meeting on August 13 (ultimately, the Fed left rates unchanged). They yielded 1.62% in August, a 44-year low and 174 basis points below where it stood a year ago.



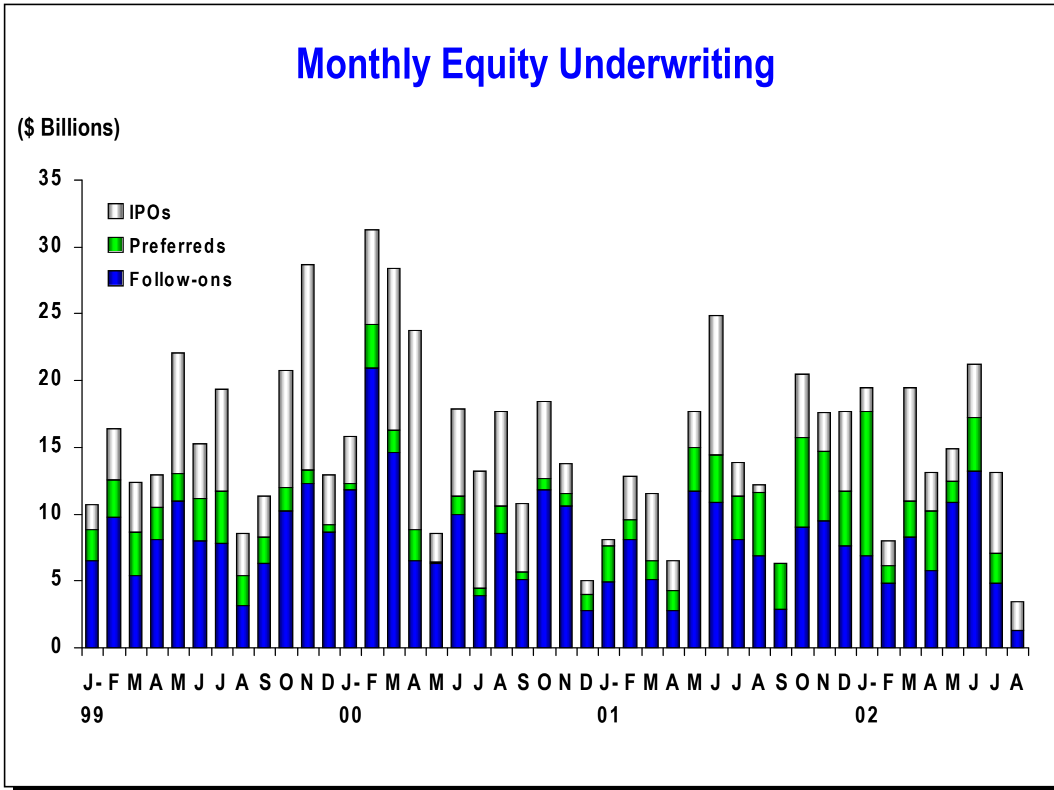
U.S. Underwriting Activity

Total Underwriting – New issuance of corporate stocks and bonds weakened further in August to its lowest level of the year due to seasonal factors and choppy market conditions. A mere $116.0 billion was raised in August, down 27.3% compared with July and less than half the average monthly amount raised in the first six months of 2002. Indeed, August's activity marked a 20-month low. September has proven to be even more dismal.

Overall volume of stock and bond underwriting in the U.S. market reached $1.7 billion during the first eight months of this year. This was up 3.5% from the same, year-earlier period due to record activity in this year's first quarter. However, the number of deals completed so far this year is running at a reduced level not seen since 1996. Only 7,554 deals were completed through August 2002, 29.6% below the 10,734 deals offered during the same period last year.

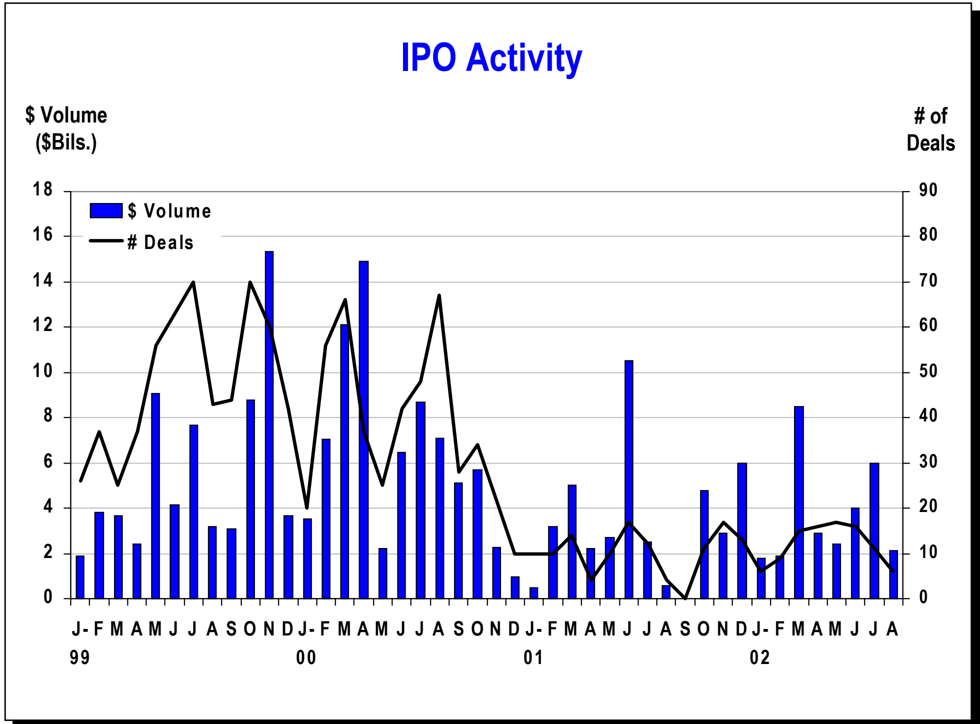


Equity Underwriting – August equity issuance sank 74.0% from the prior month to its lowest level in over 10 years (since February 1991), as no preferred stock deals were brought to market and a mere $3.4 billion was raised via common stock offerings. Despite the weak showing in August, equity underwriting year-to-date is still running ahead of last year's pace, as $112.7 billion was raised via 518 deals compared with $107.7 billion raised from 489 deals in the same period a year ago.

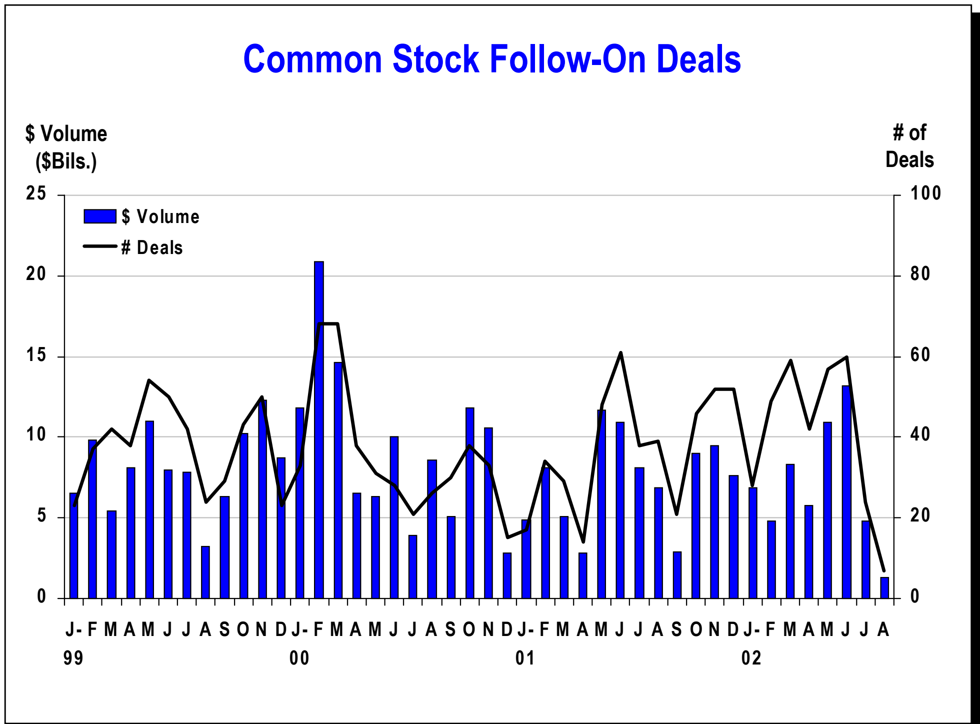


IPO volume plummeted 65.0% to $2.1 billion in August from $6.0 billion in July. It should be remembered, however, that one jumbo IPO deal kept July's volume misleadingly high, as CIT Group's $4.6 billion offering accounted for over three-fourths of July IPO volume. Despite the decreased activity in August, IPO dollar volume year-to-date, at $29.7 billion, is up 9.3%% from year-earlier levels. No IPOs were issued in September.

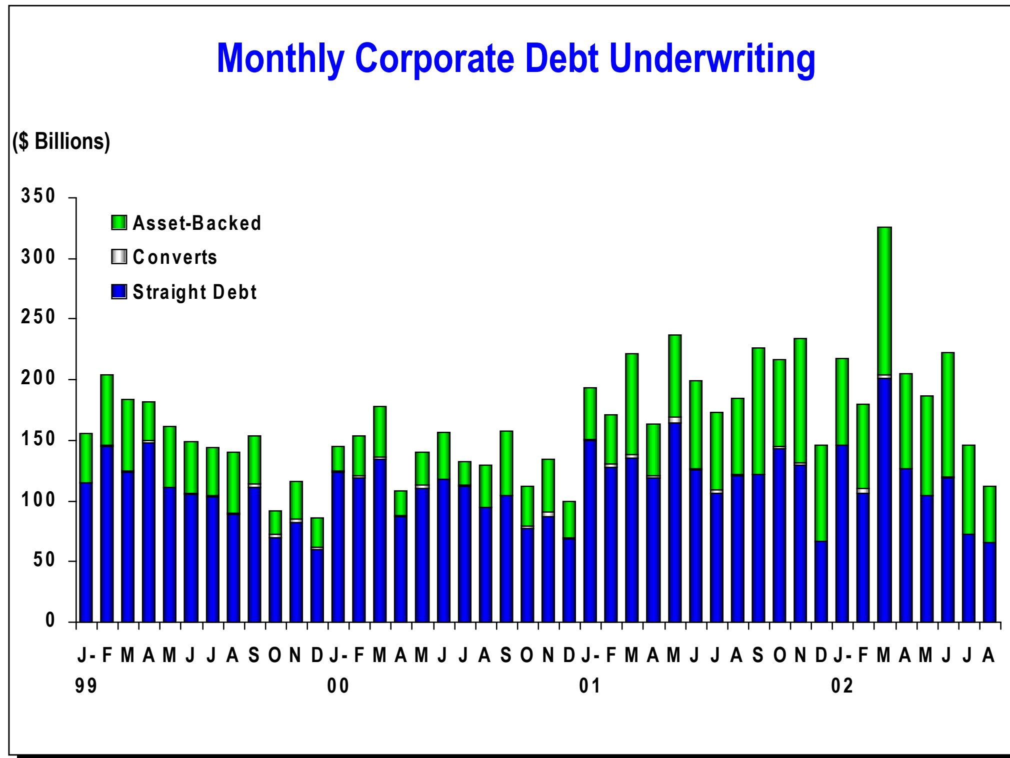
The outlook for the remainder of the year is dim, as only 65 U.S.-registered IPOs are currently in the pipeline and expected to raise only $10.3 billion.



August follow-on volume of $1.3 billion represented a 72.9% decline from July's level and was the worst monthly showing since July 1994. Year-to-date, proceeds from follow-on offerings totaled $56.0 billion and are down 4.5% from $58.6 billion in the same period last year.



Corporate Bond Underwriting – Domestic underwriting of all major debt products tumbled to their lowest levels of the year, sinking 23.1% to $112.6 billion in August from $146.4 billion in July. Despite August's woes, corporate bond underwriting activity year-to-date reached $1.6 trillion, up 3.4% from the same period a year ago.



Straight corporate bond offerings, which peaked at $201.0 billion in March, declined during the ensuing five months to a 2002 monthly low of $65.5 billion in August. That brought the year-to-date total to $941.8 billion, a 10.4% decrease from $1.1 trillion in last year's comparable period.

Asset-backed bond issuance sank 36.1% from July's level to $47.1 billion in August. Although asset-backed volume has tapered off these past two months, the year-to-date total of $645.3 billion is up 35.9% from the same period last year.

Grace Toto
Assistant Vice President and Director, Statistics

U.S. CORPORATE UNDERWRITING ACTIVITY

(In $ Billions)

	Straight Corporate Debt	Con-vertible Debt	Asset-Backed Debt	**TOTAL DEBT**	High-Yield Bonds	Common Stock	Preferred Stock	**TOTAL EQUITY**	All IPOs	Follow-Ons	**TOTAL UNDER-WRITINGS**
1985	76.4	7.5	20.8	104.7	14.2	24.7	8.6	33.3	8.5	16.2	138.0
1986	149.8	10.1	67.8	227.7	31.9	43.2	13.9	57.1	22.3	20.9	284.8
1987	117.8	9.9	91.7	219.4	28.1	41.5	11.4	52.9	24.0	17.5	272.3
1988	120.3	3.1	113.8	237.2	27.7	29.7	7.6	37.3	23.6	6.1	274.5
1989	134.1	5.5	135.3	274.9	25.3	22.9	7.7	30.6	13.7	9.2	305.5
1990	107.7	4.7	176.1	288.4	1.4	19.2	4.7	23.9	10.1	9.0	312.3
1991	203.6	7.8	300.0	511.5	10.0	56.0	19.9	75.9	25.1	30.9	587.4
1992	319.8	7.1	427.0	753.8	37.8	72.5	29.3	101.8	39.6	32.9	855.7
1993	448.4	9.3	474.8	932.5	55.2	102.4	28.4	130.8	57.4	45.0	1,063.4
1994	381.2	4.8	253.5	639.5	33.3	61.4	15.5	76.9	33.7	27.7	716.4
1995	466.0	6.9	152.4	625.3	28.9	82.0	15.1	97.1	30.2	51.8	722.4
1996	564.8	9.3	252.9	827.0	37.2	115.5	36.5	151.9	50.0	65.5	979.0
1997	769.8	8.5	385.6	1,163.9	31.4	120.2	33.3	153.4	44.2	75.9	1,317.3
1998	1,142.5	6.3	566.8	1,715.6	42.9	115.0	37.8	152.7	43.7	71.2	1,868.3
1999	1,264.8	16.1	487.1	1,768.0	36.6	164.3	27.5	191.7	66.8	97.5	1,959.8
2000	1,236.2	17.0	393.4	1,646.6	25.2	189.1	15.4	204.5	76.1	112.9	1,851.0
2001	1,511.2	21.6	832.5	2,365.4	30.6	128.4	41.3	169.7	40.8	87.6	2,535.1
<u>2001</u>											
Jan	149.6	1.7	41.7	193.0	5.9	5.4	2.7	8.1	0.5	4.9	201.1
Feb	127.5	3.3	40.5	171.3	4.1	11.3	1.5	12.8	3.2	8.1	184.1
Mar	135.5	2.3	83.8	221.6	1.3	10.1	1.4	11.5	5.0	5.1	233.1
Apr	119.3	1.1	42.9	163.4	3.1	5.0	1.5	6.5	2.2	2.8	169.9
May	164.8	4.8	67.0	236.6	3.1	14.4	3.3	17.8	2.7	11.7	254.4
June	126.1	1.0	71.9	199.0	3.6	21.4	3.5	24.9	10.5	10.9	223.8
July	106.8	2.6	63.9	173.3	0.2	10.6	3.3	13.9	2.5	8.1	187.2
Aug	121.2	0.2	63.0	184.4	2.7	7.6	4.7	12.3	0.6	6.9	196.7
Sept	121.8	0.0	104.6	226.5	0.2	2.9	3.4	6.3	0.0	2.9	232.8
Oct	142.8	2.7	70.8	216.4	1.9	13.7	6.7	20.4	4.8	9.0	236.8
Nov	129.3	1.9	102.9	234.2	3.1	12.4	5.2	17.6	2.9	9.5	251.8
Dec	66.4	0.0	79.4	145.8	1.4	13.6	4.1	17.7	6.0	7.6	163.4
<u>2002</u>											
Jan	146.0	0.2	71.0	217.1	4.8	8.6	10.8	19.4	1.8	6.9	236.5
Feb	106.1	3.8	70.2	180.0	1.2	6.7	1.3	7.9	1.9	4.8	188.0
Mar	201.0	3.2	121.7	325.8	4.5	16.9	2.7	19.6	8.5	8.3	345.4
Apr	127.1	0.0	77.5	204.6	2.6	8.7	4.4	13.1	2.9	5.8	217.8
May	104.6	0.1	81.7	186.5	0.1	13.3	1.6	14.8	2.4	10.9	201.3
June	119.2	0.4	102.5	222.1	2.8	17.3	4.0	21.3	4.0	13.2	243.4
July	72.3	0.4	73.7	146.4	0.4	10.8	2.3	13.1	6.0	4.8	159.5
Aug	65.5	0.0	47.1	112.6	0.5	3.4	0.0	3.4	2.1	1.3	116.0
Sept											
Oct											
Nov											
Dec											
YTD '01	1,050.9	17.0	474.7	1,542.6	23.9	85.8	21.9	107.7	27.2	58.6	1,650.3
YTD '02	941.8	8.1	645.3	1,595.2	16.9	85.7	27.0	112.7	29.7	56.0	1,707.9
% Change	-10.4%	-52.5%	35.9%	3.4%	-29.5%	-0.1%	23.2%	4.6%	9.3%	-4.5%	3.5%

Note: High-yield bonds is a subset of straight corporate debt. IPOs and follow-ons are subsets of common stock.
Source: Thomson Financial Securities Data

MUNICIPAL BOND UNDERWRITINGS
(In $ Billions)

INTEREST RATES
(Averages)

	Compet. Rev. Bonds	Nego. Rev. Bonds	**TOTAL REVENUE BONDS**	Compet. G.O.s	Nego. G.O.s	**TOTAL G.O.s**	**TOTAL MUNICIPAL BONDS**	3-Mo. T Bills	10-Year Treasuries	SPREAD
1985	10.2	150.8	161.0	17.6	22.8	40.4	201.4	7.47	10.62	3.15
1986	10.0	92.6	102.6	23.1	22.6	45.7	148.3	5.97	7.68	1.71
1987	7.1	64.4	71.5	16.3	14.2	30.5	102.0	5.78	8.39	2.61
1988	7.6	78.1	85.7	19.2	12.7	31.9	117.6	6.67	8.85	2.18
1989	9.2	75.8	85.0	20.7	17.2	37.9	122.9	8.11	8.49	0.38
1990	7.6	78.4	86.0	22.7	17.5	40.2	126.2	7.50	8.55	1.05
1991	11.0	102.1	113.1	29.8	28.1	57.9	171.0	5.38	7.86	2.48
1992	12.5	139.0	151.6	32.5	49.0	81.5	233.1	3.43	7.01	3.58
1993	20.0	175.6	195.6	35.6	56.7	92.4	287.9	3.00	5.87	2.87
1994	15.0	89.2	104.2	34.5	23.2	57.7	161.9	4.25	7.09	2.84
1995	13.5	81.7	95.2	27.6	32.2	59.8	155.0	5.49	6.57	1.08
1996	15.6	100.1	115.7	31.3	33.2	64.5	180.2	5.01	6.44	1.43
1997	12.3	130.2	142.6	35.5	36.5	72.0	214.6	5.06	6.35	1.29
1998	21.4	165.6	187.0	43.7	49.0	92.8	279.8	4.78	5.26	0.48
1999	14.3	134.9	149.2	38.5	31.3	69.8	219.0	4.64	5.65	1.01
2000	13.6	116.2	129.7	35.0	29.3	64.3	194.0	5.82	6.03	0.21
2001	17.6	164.2	181.8	45.5	56.3	101.8	283.5	3.39	5.02	1.63
2001										
Jan	1.2	4.9	6.1	4.4	1.9	6.3	12.4	5.15	5.16	0.01
Feb	0.9	10.3	11.2	4.7	5.1	9.8	21.0	4.88	5.10	0.22
Mar	1.2	16.2	17.4	2.7	5.1	7.8	25.1	4.42	4.89	0.47
Apr	1.0	10.5	11.5	3.6	3.5	7.1	18.6	3.87	5.14	1.27
May	1.2	18.5	19.7	4.4	4.5	8.9	28.6	3.62	5.39	1.77
June	1.8	18.1	19.9	5.1	4.8	9.9	29.9	3.49	5.28	1.79
July	1.5	13.1	14.7	3.8	2.3	6.1	20.8	3.51	5.24	1.73
Aug	1.6	12.6	14.2	3.9	5.8	9.7	23.9	3.36	4.97	1.61
Sept	0.9	9.1	10.0	2.2	2.0	4.2	14.1	2.64	4.73	2.09
Oct	3.1	15.1	18.2	4.8	9.0	13.8	32.0	2.16	4.57	2.41
Nov	2.0	18.2	20.2	3.4	5.8	9.2	29.4	1.87	4.65	2.78
Dec	1.1	17.6	18.8	2.5	6.5	9.0	27.8	1.69	5.09	3.40
2002										
Jan	1.1	12.3	13.3	4.3	3.8	8.1	21.4	1.65	5.04	3.39
Feb	1.5	10.4	11.9	4.9	3.9	8.8	20.7	1.73	4.91	3.18
Mar	1.7	12.9	14.6	4.9	5.5	10.5	25.0	1.79	5.28	3.49
Apr	2.3	14.4	16.7	4.4	4.0	8.4	25.1	1.72	5.21	3.49
May	2.4	20.7	23.0	4.1	6.7	10.8	33.9	1.73	5.16	3.43
June	1.5	19.5	21.0	5.2	11.2	16.5	37.4	1.70	4.93	3.23
July	1.1	15.3	16.4	4.7	5.9	10.7	27.0	1.68	4.65	2.97
Aug	0.6	17.8	18.4	3.7	6.3	10.1	28.4	1.62	4.26	2.64
Sept										
Oct										
Nov										
Dec										
YTD '01	10.5	104.2	114.6	32.6	33.0	65.6	180.2	4.04	5.15	1.11
YTD '02	12.1	123.2	135.3	36.3	47.5	83.8	219.1	1.70	4.93	3.23
% Change	15.4%	18.3%	18.0%	11.6%	43.6%	27.7%	21.5%	-57.8%	-4.2%	191.1%

Sources: Thomson Financial Securities Data; Federal Reserve

	STOCK MARKET PERFORMANCE INDICES (End of Period)				STOCK MARKET VOLUME (Daily Avg., Mils. of Shs.)			VALUE TRADED (Daily Avg., $ Bils.)	
	Dow Jones Industrial Average	S&P 500	NYSE Composite	Nasdaq Composite	NYSE	AMEX	Nasdaq	NYSE	Nasdaq
1985	1,546.67	211.28	121.58	324.93	109.2	8.3	82.1	3.9	0.9
1986	1,895.95	242.17	138.58	348.83	141.0	11.8	113.6	5.4	1.5
1987	1,938.83	247.08	138.23	330.47	188.9	13.9	149.8	7.4	2.0
1988	2,168.57	277.72	156.26	381.38	161.5	9.9	122.8	5.4	1.4
1989	2,753.20	353.40	195.04	454.82	165.5	12.4	133.1	6.1	1.7
1990	2,633.66	330.22	180.49	373.84	156.8	13.2	131.9	5.2	1.8
1991	3,168.83	417.09	229.44	586.34	178.9	13.3	163.3	6.0	2.7
1992	3,301.11	435.71	240.21	676.95	202.3	14.2	190.8	6.9	3.5
1993	3,754.09	466.45	259.08	776.80	264.5	18.1	263.0	9.0	5.3
1994	3,834.44	459.27	250.94	751.96	291.4	17.9	295.1	9.7	5.8
1995	5,117.12	615.93	329.51	1,052.13	346.1	20.1	401.4	12.2	9.5
1996	6,448.27	740.74	392.30	1,291.03	412.0	22.1	543.7	16.0	13.0
1997	7,908.25	970.43	511.19	1,570.35	526.9	24.4	647.8	22.8	17.7
1998	9,181.43	1,229.23	595.81	2,192.69	673.6	28.9	801.7	29.0	22.9
1999	11,497.12	1,469.25	650.30	4,069.31	808.9	32.7	1,081.8	35.5	43.7
2000	10,786.85	1,320.28	656.87	2,470.52	1,041.6	52.9	1,757.0	43.9	80.9
2001	10,021.50	1,148.08	589.80	1,950.40	1,240.0	65.8	1,900.1	42.3	44.1
2001									
Jan	10,887.36	1,366.01	663.64	2,772.73	1,325.9	72.5	2,387.3	52.0	75.6
Feb	10,495.28	1,239.94	626.94	2,151.83	1,138.5	70.9	1,947.6	43.8	59.7
Mar	9,878.78	1,160.33	595.66	1,840.26	1,271.4	82.5	2,071.4	45.9	49.2
Apr	10,734.97	1,249.46	634.83	2,116.24	1,276.5	78.4	2,162.8	45.1	49.6
May	10,911.94	1,255.82	641.67	2,110.49	1,116.7	66.7	1,909.1	41.4	46.4
June	10,502.40	1,224.42	621.76	2,160.54	1,175.0	63.8	1,793.9	41.6	40.6
July	10,522.81	1,211.23	616.94	2,027.13	1,137.1	56.0	1,580.7	39.0	36.0
Aug	9,949.75	1,133.58	587.84	1,805.43	1,025.7	49.1	1,426.4	34.0	28.4
Sept	8,847.56	1,040.94	543.84	1,498.80	1,694.4	72.8	2,033.0	51.2	33.9
Oct	9,075.14	1,059.78	546.34	1,690.20	1,314.3	67.8	1,926.0	40.1	36.1
Nov	9,851.56	1,139.45	579.27	1,930.58	1,270.1	57.8	1,840.3	38.1	37.8
Dec	10,021.50	1,148.08	589.80	1,950.40	1,275.3	54.1	1,807.0	38.8	36.2
2002									
Jan	9,920.00	1,130.20	578.50	1,934.03	1,425.9	56.1	1,888.7	44.5	40.8
Feb	10,106.13	1,106.73	578.60	1,731.49	1,381.8	56.3	1,812.8	42.1	35.9
Mar	10,403.94	1,147.39	600.43	1,845.35	1,337.1	57.1	1,756.8	42.9	34.5
Apr	9,946.22	1,076.92	574.18	1,688.23	1,307.3	55.4	1,779.0	42.4	32.1
May	9,925.25	1,067.14	570.78	1,615.73	1,234.2	61.5	1,834.2	38.9	29.8
June	9,243.26	989.82	533.07	1,463.21	1,587.0	66.9	1,877.1	44.8	29.4
July	8,736.59	911.62	491.37	1,328.26	1,886.3	79.0	2,158.2	50.9	28.1
Aug	8,663.50	916.07	495.55	1,314.85	1,341.4	58.4	1,509.0	35.5	20.9
Sept									
Oct									
Nov									
Dec									
YTD '01	9,949.75	1,133.58	587.84	1,805.43	1,181.6	67.3	1,903.2	42.7	47.8
YTD '02	8,663.50	916.07	495.55	1,314.85	1,438.1	61.4	1,827.1	42.7	31.3
% Change	-12.9%	-19.2%	-15.7%	-27.2%	21.7%	-8.7%	-4.0%	-0.1%	-34.6%

MUTUAL FUND ASSETS
($ Billions)

MUTUAL FUND NET NEW CASH FLOW*
($ Billions)

	Assets: Equity	Assets: Hybrid	Assets: Bond	Assets: Money Market	**TOTAL ASSETS**	Cash Flow: Equity	Cash Flow: Hybrid	Cash Flow: Bond	Cash Flow: Money Market	**TOTAL**	Total Long-Term Funds
1985	116.9	12.0	122.6	243.8	495.4	8.5	1.9	63.2	-5.4	68.2	73.6
1986	161.4	18.8	243.3	292.2	715.7	21.7	5.6	102.6	33.9	163.8	129.9
1987	180.5	24.2	248.4	316.1	769.2	19.0	4.0	6.8	10.2	40.0	29.8
1988	194.7	21.1	255.7	338.0	809.4	-16.1	-2.5	-4.5	0.1	-23.0	-23.1
1989	248.8	31.8	271.9	428.1	980.7	5.8	4.2	-1.2	64.1	72.8	8.8
1990	239.5	36.1	291.3	498.3	1,065.2	12.8	2.2	6.2	23.2	44.4	21.2
1991	404.7	52.2	393.8	542.5	1,393.2	39.4	8.0	58.9	5.5	111.8	106.3
1992	514.1	78.0	504.2	546.2	1,642.5	78.9	21.8	71.0	-16.3	155.4	171.7
1993	740.7	144.5	619.5	565.3	2,070.0	129.4	39.4	73.3	-14.1	228.0	242.1
1994	852.8	164.5	527.1	611.0	2,155.4	118.9	20.9	-64.6	8.8	84.1	75.2
1995	1,249.1	210.5	598.9	753.0	2,811.5	127.6	5.3	-10.5	89.4	211.8	122.4
1996	1,726.1	252.9	645.4	901.8	3,526.3	216.9	12.3	2.8	89.4	321.3	232.0
1997	2,368.0	317.1	724.2	1,058.9	4,468.2	227.1	16.5	28.4	102.1	374.1	272.0
1998	2,978.2	364.7	830.6	1,351.7	5,525.2	157.0	10.2	74.6	235.3	477.1	241.8
1999	4,041.9	383.2	808.1	1,613.1	6,846.3	187.7	-12.4	-5.5	193.6	363.4	169.8
2000	3,962.0	346.3	811.1	1,845.2	6,964.7	309.4	-30.7	-49.8	159.6	388.6	228.9
2001	3,418.2	346.3	925.1	2,285.3	6,975.0	32.2	9.5	87.8	375.3	504.8	129.6
<u>2001</u>											
Jan	4,093.5	354.9	833.3	1,954.8	7,236.5	24.9	2.5	9.0	103.5	139.9	36.4
Feb	3,688.9	344.9	844.5	2,018.7	6,897.0	-3.3	1.3	8.9	58.2	65.1	6.8
Mar	3,402.9	333.7	852.1	2,035.5	6,624.2	-20.7	-0.4	7.7	13.7	0.4	-13.3
Apr	3,715.7	348.0	846.0	2,031.5	6,941.2	19.1	1.2	1.4	-10.5	11.2	21.7
May	3,744.6	352.6	858.4	2,070.9	7,026.5	18.4	0.9	6.3	34.3	59.8	25.6
June	3,677.2	349.9	860.8	2,052.5	6,940.4	10.9	1.2	2.3	-24.2	-9.8	14.3
July	3,589.3	351.7	882.3	2,069.8	6,893.1	-1.3	1.3	9.3	12.2	21.5	9.3
Aug	3,382.7	342.6	908.3	2,104.3	6,737.9	-5.0	-0.7	16.7	26.1	37.2	11.0
Sept	3,018.9	324.1	909.6	2,161.7	6,414.3	-30.0	-1.3	7.7	52.9	29.3	-23.6
Oct	3,111.2	330.3	935.2	2,239.7	6,616.4	0.9	1.6	13.6	74.2	90.2	16.0
Nov	3,348.6	343.0	934.1	2,306.5	6,932.2	15.3	1.0	6.9	60.3	83.5	23.2
Dec	3,418.2	346.3	925.1	2,285.3	6,975.0	2.9	1.0	-1.9	-25.4	-23.3	2.1
<u>2002</u>											
Jan	3,373.5	347.2	947.0	2,303.5	6,971.2	20.0	2.2	10.5	14.0	46.7	32.7
Feb	3,312.0	348.4	962.7	2,301.2	6,924.3	5.4	2.3	10.7	-5.5	12.9	18.4
Mar	3,497.4	359.2	958.4	2,247.2	7,062.2	29.6	3.3	6.7	-53.1	-13.4	39.7
Apr	3,369.5	354.5	980.8	2,230.8	6,935.7	12.9	3.3	7.8	-19.5	4.5	24.0
May	3,343.3	356.4	994.3	2,229.8	6,923.8	4.9	1.5	10.6	-4.3	12.6	16.9
June	3,089.6	341.4	1,003.6	2,196.5	6,631.1	-18.3	0.4	12.2	-43.6	-49.2	-5.6
July	2,770.3	320.7	1,033.2	2,254.6	6,378.8	-52.6	-4.7	28.1	54.6	25.4	-29.2
Aug	2,782.0	324.9	1,064.1	2,218.2	6,389.2	-2.9	0.5	17.4	-38.4	-23.4	15.0
Sept											
Oct											
Nov											
Dec											
YTD '01	3,382.7	342.6	908.3	2,104.3	6,737.9	43.1	7.3	61.6	213.3	325.2	111.9
YTD '02	2,782.0	324.9	1,064.1	2,218.2	6,389.2	-1.0	8.9	103.9	-95.7	16.1	111.8
% Change	-17.8%	-5.2%	17.2%	5.4%	-5.2%	-102.3%	22.7%	68.8%	-144.9%	-95.1%	0.0%

* New sales (excluding reinvested dividends) minus redemptions, combined with net exchanges
Source: Investment Company Institute

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