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Ingram: Memo to Nasdaq — don't do it

By MATHEW INGRAM
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Wondering just how desperate things have gotten in tech-land? The Nasdaq Stock Market — the former titan of the dot-com boom, which dubs itself the "stock market for the next 100 years" — is said to be thinking about dropping a rule that listed stocks must trade above $1. So many stocks are in violation of the rule that the exchange is reportedly worried about having to delist them all. Here's a tip for the Nasdaq: Don't do it.

Nasdaq chairman Hardwick Simmons made the controversial suggestion during a recent speech at a meeting of the Securities Traders Association in Boca Raton, Fla. He said that the market selloff over the past couple of years has had a negative effect on "companies with real balance sheets and real businesses," and that the Nasdaq was looking at ways of helping those companies retain their listings until their businesses improve.

The rationale for Mr. Simmons' proposal is obvious. More than 500 of the Nasdaq's almost 4,000 stocks are below the $1 mark, including i2 Technologies, a member of the high-profile Nasdaq 100 which used to trade at over $100. Even European phone giant Ericsson AG was in penny-stock territory until recently (it announced a reverse share split last week). More than 60 per cent of Nasdaq-listed stocks are trading below $5.

That said, however, Mr. Simmons should be thinking about the message that such a rule change risks sending to investors — and to companies too. For investors, it would cement in their minds the image of the Nasdaq as a penny-stock market, the kind of place where vaguely disreputable companies are traded. Companies, meanwhile, would be handed a "get out of responsibility free" card, absolving them of any guilt for having diluted their own stock through share issues and

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stock splits during the dot-com boom.

Relax, some market watchers say; Mr. Simmons was just making an observation and it got blown out of proportion — the Nasdaq would never lower the bar like that. The market put the rule on hold in the aftermath of the Sept. 11 attacks, but that was a response to an extraordinary event, and it reinstated the rule in January (although it later doubled the amount of time a stock can trade below $1 before it gets a warning, to 180 days from 90). Doing away with the requirement altogether would never fly.

Brooks McFeeley, CEO of a trading firm called MidnightTrader, told the South China Morning Post that he doubted the Securities and Exchange Commission would even allow the Nasdaq to drop the rule, and said if it did, "it just wouldn't be fair to investors; the Nasdaq has a responsibility to protect investors from these sorts of companies. It would not be good for the market's image... It is not in the best interests of anyone except the failing companies that desperately need to remain public."

Despite that kind of criticism, however, some members of the Nasdaq board seem to be warming up to the idea. Richard Romano, CEO of trading firm Romano Brothers, said there is "great merit" to it. Because of the market's fall over the past few years, he said, "the time has come to relax the standard." Mr. Romano said good companies that are below $1 still "deserve all the advantages of a first-class trading platform."

Others believe the proposal is aimed at helping the Nasdaq itself rather than any of its listed companies. "I suspect the real reason Nasdaq wants to do this is so it can keep more listings and collect more fees," Larry Swedroe of Buckingham Asset Management told the New York Post. With 15 per cent of its listings below $1, "This appears to be a move that's in the best interest of the Nasdaq, not in the best interest of investors," said Todd Salamone of Schaeffer's Investment Research.

In the year 2000, the Nasdaq market had to delist about 600 companies for failing to meet the listing criteria, and last year it delisted another 500. The average up to that point was about 200 per year. Over 1,000 stocks in just two years is a big hit for a market such as the Nasdaq, which derives much of its revenue from listing fees — not to mention trading fees, which have declined along with share prices.

Some companies solve the problem with a reverse split, consolidating their shares one-for-10 or one-for-20 — a move Nortel and Lucent are considering — but only 114 Nasdaq stocks have done one this year. And a reverse split doesn't really serve the Nasdaq market's needs, since it reduces the number of shares outstanding, and listing fees are based on the number of shares. Companies with between one million and four million shares pay $8,000 a year, while those with over 200

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Mr. Simmons should reconsider his proposal. Companies suffering from the effects of their own poor judgement should be held accountable — and investors who have already been through a vicious battering need to know the stocks they are buying are held to a certain standard.

E-mail Mathew Ingram at mingram@globeandmail.ca

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