

# THREE COINS IN A FOUNTAIN

## NOVEMBER 2004

When I first visited Rome I set off to one of its most famous attractions, The *Trevi Fountain*. The *Trevi* legend says that if you toss a coin into the fountain over your shoulder you will one day return to the eternal city. Personally, I am not much for wishing wells but rather than risk not returning to a city I love so much, I participated in the ritual along with a million others. Tossing my coin got me thinking...Where do all those coins go? Could all those coins add up to a significant amount? How much? Who gets all that money? (Answer: At the end of the article.)

The Securities and Exchange Commission has launched another probe into the usual suspects again. You guessed it...Merrill, Morgan, Smith B., UBS, Charles Schwab etc. The SEC discovered in an audit that the brokers failed to get customers the best prices when purchasing stocks. The SEC is a little late on this prevalent infraction; we reported this on The Watchdog on Wall Street Show back in 2001, and since then has become a more prevalent and accepted practice by the big brokerage firms. *Bloomberg Online* quoted John Gavin president of **SEC Insight Inc.** a corporate research firm.

***“If the brokerage industry would actually quit pretending that they have the client’s interests at heart, maybe they wouldn’t get into trouble. Mainstream brokers want you to believe that, buyer you can trust us, but really the sign should say, buyer beware.”***

The issue this time is how firms executed trades of NASDAQ stocks when the opening bell rang at 9:30 AM. This early trading period is characterized by very intense activity due to the backlog of orders since the markets close the previous day. The SEC after reviewing data from the past four years has discovered that the trades were processed in ways that strongly favored the brokerage firms over their clients. (*Tell us something we don’t already know.*) One of the cornerstones of the brokerage industry is the critical obligation to secure the best price for investors. Brokerage firms have a **“best execution”** obligation as defined by common law, as well as fraud provisions in the securities acts and exchange rules to make sure they get the best price for investors.

What the brokerage firms have been doing is called **“internalization”** and **“payment for order flow.”** Internalization occurs when a brokerage firm completes a customer order from other pending orders or its own inventory of shares. Instead of going out and getting the best possible price they sell from their own inventory and make the spread. Payment for order flow is the practice of accepting rebates from market makers, which those market makers use to attract brokerage firm business. Once again, instead of getting the best possible price for the investor, the firm funnels trades to a preferred market maker who gives them kickbacks based on volume.

When we described this malfeasance back in 2001 we called it **“death by a thousand cuts”**. This unfortunate, yet widespread practice does not amount to much money on each trade; in fact it is usually only pennies a share. However, just like the *Trevi Fountain*, imagine the volume of trades on any given day on NASDAQ, those pennies sure can add up. The several pennies a share that are pilfered is so small, that it is near impossible for investors to realize, yet coupled with the incredible volume of trades conducted, it is the perfect crime.

This scam is another fantastic illustration of what the big brokerage houses are all about. Their ability to do anything and everything to pull one over on the consumer has reached epoch proportions. What will they think of next? Understanding what is in the heart of the entity you’re doing business with is essential to ones success. Ignoring a black heart can be devastating.

**Answer:** Roberto Cercelletta had been raking it in for years. Six days a week, under the cover of early-morning darkness, Cercelletta had dredged Rome's celebrated Trevi fountain for the cash left by tourists such as myself. He usually used a rake, but sometimes operated with a magnet. His daily take, for perhaps 15 minutes of hurried work, would occasionally top \$1000 according to police officials, who never made much fuss about him.

All of that changed in August of 2002 when the Italian media reported that the Trevi's treasure, which is supposed to go to charity, was going instead to Cercelletta, an otherwise unemployed, mentally unstable man who started fishing in the fountain back in 1968. One early August morning, when he took his usual dip in the fountain, police arrested him. Cercelletta, 50, said that someone else would be looting the Trevi if he didn't, and that the arrest ignored more than 30 years of tradition.

Roberto Cercelletta is now rumored to be working for Merrill Lynch.