

MERRILL GETS STAY FROM COURT ORDER SHARES OF BROKER SLAMMED AS DISCLOSURE TALKS CONTINUE

By Allen Wan, CBS.MarketWatch.com
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NEW YORK (CBS.MW) -- Merrill Lynch said Thursday that the New York attorney general has agreed to extend a court order requiring the country's biggest broker to make changes in the way it discloses the relationships between its equity analysts and investment bankers.

Merrill will have until Friday, April 19, to comply with the court order, which was set to expire at 5 p.m. today. "This is a mutual agreement to give us more opportunity to discuss additional disclosure in research reports," a Merrill spokesman said.

Shares of Merrill (MER) plunged 7.9 percent, or \$46.90, to \$47.79 in early afternoon trade.

New York State Attorney General Eliot Spitzer had threatened to bring a contempt of court order and even criminal action against Merrill if it didn't comply with an order requiring the firm to disclose alleged conflict of interests between its equity analysts and investment bankers. The order also required the broker to improve its stock-rating system.

In an affidavit, the New York attorney general alleged that Merrill generated huge revenues by getting companies to agree to have Merrill underwrite deals if its research analysts initiated positive coverage on those stocks. Media reports have said that Merrill is concerned about losing any competitive edge to its rivals as a result of new disclosure methods.

Steven Abernathy, the head of money management firm The Abernathy Group, said that impact of the New York attorney general's probe on the financial industry will depend largely on what the authorities extract from Merrill as well as other Wall Street firms that have come under investigation.

"If it's just a small disclaimer on the research reports, it would be the biggest disappointment. No one reads them anyway," he said. "The Attorney General has a winning case, it just has to not blow it."

But he said that if the Wall Street brokers hive off their research and investment banking divisions as a result of the pressure from authorities, that could spur positive change and help restore investor confidence at a time when the market is enduring one financial scandal after another in the wake of Enron.

"The construct needs to be changed," he said. "I think that retail investors that understand the magnitude of what's happening will be more skeptical towards any written research that's from any firm that has a banking department." On Wednesday, prosecutors widened their investigation into the alleged conflict of interests of Wall Street analysts to include at least eight investment banks.

The Financial Times named Morgan Stanley (MWD) and Credit Suisse First Boston, a unit of the Credit Suisse Group (CSR), as targets of the investigation over their research practices. Goldman Sachs (GS), Lehman Bros. (LEH), UBS Paine Webber (UBS) and Salomon Smith Barney were also on the list, according to a report by The Wall Street Journal.

Some of these banks have received subpoenas, while other will get them shortly, the Journal said, citing people close to the inquiry.

Merrill Lynch has denied the charges.

"We are still assessing our options and have nothing to say beyond what was in the statement (refuting the charges)," said a spokesman for Merrill Lynch. "But we will likely have something to say tomorrow."

While Spitzer said the problems were company wide at Merrill Lynch, he singled out for mention the brokerage's Internet research division and its high-profile head analyst, Henry Blodget.

In the 10-month-long investigation, the authorities caught the former high-flying analyst publicly recommending stocks that he was disparaging in private.

Among the list of allegations against Merrill, the attorney general's office said its five-point scale for rating stocks was a "de facto three-point system" as no "reduce" or "sell" recommendations were ever issued.

Also, the proverbial "Chinese wall" that traditionally separates the analysts who are supposed to give unbiased objective coverage of stocks and the investment bankers who drum up business was breached.

Spitzer alleged that Merrill's stock analysts, who are supposed to be objective in their evaluations, have used their coverage as a way to bolster the firm's lucrative investment banking operations. He said subpoenaed e-mail pointed to the improper ties.

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