

**Union Calendar No. 33**

103D CONGRESS  
1ST SESSION

**H. R. 578**

[Report No. 103-75]

**A BILL**

To provide for recovery of costs of supervision and regulation of investment advisers and their activities, and for other purposes.

APRIL 29, 1993

Reported with an amendment, committed to the Committee of the Whole House on the State of the Union, and ordered to be printed

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### IN THE HOUSE OF REPRESENTATIVES

JANUARY 26, 1993

Mr. BOUCHER (for himself, Mr. MARKEY, Mr. DINGELL, Mr. FIELDS of Texas, Mr. COOPER, Mr. WYDEN, Mr. LEHMAN, and Mr. SYNAR) introduced the following bill; which was referred to the Committee on Energy and Commerce

APRIL 29, 1993

Additional sponsors: Mr. MOORHEAD, Mr. MARTINEZ, Mrs. JOHNSON of Connecticut, Mr. BARRETT of Wisconsin, Mr. HUGHES, Mr. GLICKMAN, Mrs. MEEK, and Mr. STUDDS

APRIL 29, 1993

Reported with an amendment, committed to the Committee of the Whole House on the State of the Union, and ordered to be printed

[Strike out all after the enacting clause and insert the part printed in italic]

[For text of introduced bill, see copy of bill as introduced on January 26, 1993]

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## A BILL

To provide for recovery of costs of supervision and regulation of investment advisers and their activities, and for other purposes.

1       *Be it enacted by the Senate and House of Representa-*  
2       *tives of the United States of America in Congress assembled,*

3       **SECTION 1. SHORT TITLE.**

4       *This Act may be cited as the “Investment Adviser Reg-*  
5       *ulatory Enhancement and Disclosure Act of 1993”.*

6       **SEC. 2. ADDITIONAL RESOURCES FOR INVESTMENT AD-**  
7               **VISER SUPERVISION.**

8       (a) *AMENDMENT.—The Investment Advisers Act of*  
9       *1940 (15 U.S.C. 80b–1 et seq.) is amended by inserting*  
10      *after section 203 the following new section:*

11               *“FEES FOR REGISTRANTS AND APPLICANTS*

12      *“SEC. 203A. (a) IN GENERAL.—The Commission is*  
13      *authorized, in accordance with this section, to collect fees*  
14      *to recover the costs of registration, supervision, and regula-*  
15      *tion of investment advisers and their activities. Such fees*  
16      *shall be collected, and shall be available, only to the extent*  
17      *provided in advance in appropriations Acts. No appropria-*  
18      *tion Act may authorize fees to be collected under this section*  
19      *during any fiscal year unless the amount appropriated by*  
20      *such Act for such costs for such fiscal year equals or exceeds*  
21      *the aggregate amount that may reasonably be expected to*  
22      *be collected by such fees. Such fees shall be deposited as an*  
23      *offsetting collection to the Commission’s appropriation and*  
24      *may remain available for such purposes for the succeeding*  
25      *fiscal year. The costs covered by such fees shall be limited*  
26      *to the costs of Commission expenses for registration, exami-*

1 *nations, and surveys of persons registered or required to*  
2 *register under this Act.*

3 “(b) *TIME FOR PAYMENT.*—

4 “(1) *NEW REGISTRANTS.*—At the time of filing  
5 *an application for registration under this title, the*  
6 *applicant shall pay to the Commission the fee speci-*  
7 *fied in subsection (c). No part of such fee shall be re-*  
8 *funded to the applicant. The filing of an application*  
9 *for registration under this title shall not be deemed to*  
10 *have occurred unless the application is accompanied*  
11 *by the fee required under this section.*

12 “(2) *ONGOING REGISTRANTS.*—Each investment  
13 *adviser whose registration is effective on the last day*  
14 *of its fiscal year shall pay to the Commission the fee*  
15 *specified in subsection (c). Such payment shall be*  
16 *made not later than 90 days after the end of its fiscal*  
17 *year, or at such other time as the Commission, by*  
18 *rule, shall determine, unless its registration has been*  
19 *withdrawn, canceled, or revoked prior to that date. No*  
20 *part of such fee shall be refunded to the investment*  
21 *adviser.*

22 “(c) *COST-BASED SCHEDULE OF FEES.*—For any fis-  
23 *cal year for which fees are authorized to be collected by an*  
24 *appropriation Act, the amount of fees due from investment*  
25 *advisers in accordance with paragraphs (1) and (2) of sub-*

1 *section (b) shall be determined according to the following*  
 2 *schedule:*

<b><i>“Assets under management</i></b>	<b><i>Fee due:</i></b>
<i>Less than \$10,000,000 .....</i>	<i>\$300</i>
<i>\$10,000,000 or more, but less than \$25,000,000 .....</i>	<i>\$500</i>
<i>\$25,000,000 or more, but less than \$50,000,000 .....</i>	<i>\$1,000</i>
<i>\$50,000,000 or more, but less than \$100,000,000 .....</i>	<i>\$2,500</i>
<i>\$100,000,000 or more, but less than \$250,000,000 .....</i>	<i>\$4,000</i>
<i>\$250,000,000 or more, but less than \$500,000,000 .....</i>	<i>\$5,000</i>
<i>\$500,000,000 or more .....</i>	<i>\$7,000.</i>

3       “(d) *SUSPENSION FOR FAILURE TO PAY.*—The Com-  
 4 *mission, by order, may suspend the registration of any in-*  
 5 *vestment adviser if it finds, after notice, that such invest-*  
 6 *ment adviser has failed to pay when due any fee required*  
 7 *by this section. The Commission shall reinstate such reg-*  
 8 *istration upon payment of the fee (and any penalty due),*  
 9 *if such suspension was based solely on the failure to pay*  
 10 *the fee.*

11       “(e) *RULEMAKING.*—The Commission may adopt such  
 12 *rules as are necessary to carry out this section.*

13       “(f) *DEFINITION OF ASSETS UNDER MANAGEMENT.*—  
 14 *As used in this section, the term ‘assets under management’*  
 15 *means the client assets with respect to which an investment*  
 16 *adviser provides continuous and regular supervisory or*  
 17 *management services.”.*

18       “(b) *EFFECTIVE DATE.*—This section shall become effec-  
 19 *tive upon the adoption by the Commission of implementing*  
 20 *rules, under section 203A(f) of the Investment Advisers Act*  
 21 *of 1940, as added by subsection (a).*

1 **SEC. 3. EXAMINATIONS AND SURVEYS.**

2       *The Investment Advisers Act of 1940 is amended by*  
 3 *inserting after section 222 (15 U.S.C. 80b–22) the following*  
 4 *new section:*

5                       *“EXAMINATIONS AND SURVEYS*

6           *“SEC. 223. (a) PERIODIC EXAMINATIONS.—The Com-*  
 7 *mission shall establish and periodically revise a schedule*  
 8 *for the regular examination of investment advisers. Such*  
 9 *schedule shall provide for more frequent examinations of*  
 10 *certain investment advisers based on factors that the Com-*  
 11 *mission determines increase the need for examination of*  
 12 *those investment advisers, which shall include (at a mini-*  
 13 *mum) each of the following:*

14                   *“(1) the frequency of customer complaints;*

15                   *“(2) the risks associated with newly registered*  
 16 *investment advisers;*

17                   *“(3) custody of funds and the authority to exer-*  
 18 *cise investment discretion;*

19                   *“(4) the existence of deficiencies detected during*  
 20 *an examination under this title that may continue to*  
 21 *present high risks to clients; and*

22                   *“(5) the receipt of commissions for the sale of in-*  
 23 *vestments recommended to clients.*

24           *“(b) SURVEYS OF UNREGISTERED PERSONS.—The*  
 25 *Commission shall, within 3 years after the date of enact-*  
 26 *ment of this section and periodically thereafter, provide for*

1 *the conduct of a survey to determine the extent of, and rea-*  
2 *sons for, the failure of persons to register as required by*  
3 *this Act. The Commission shall, on the basis of such survey*  
4 *results, establish objectives for the reduction or elimination*  
5 *of such failures and shall include in annual reports to Con-*  
6 *gress (under section 23(b) of the Securities Exchange Act*  
7 *of 1934) submitted after completion of the first survey, a*  
8 *statement of such objectives, an evaluation of the success in*  
9 *attaining those objectives during the preceding year, and*  
10 *such recommendations as the Commission considers appro-*  
11 *priate to assist in the attainment of those objectives. If the*  
12 *survey identifies any pattern of noncompliance with the*  
13 *registration requirements of the title and the rules there-*  
14 *under, the Commission's objectives shall include such rule-*  
15 *making proceedings as may be required to correct such non-*  
16 *compliance.*

17 *“(c) PROVISIONS NOT LIMITATION.—The provisions of*  
18 *this section shall not be construed to limit the authority*  
19 *of the Commission to prescribe rules under this Act or to*  
20 *conduct an examination or investigation at any time or*  
21 *to institute proceedings under this title or any other title.”.*

1 **SEC. 4. DESIGNATION OF SELF-REGULATORY ORGANIZA-**  
2 **TIONS.**

3 *The Investment Advisers Act of 1940 (15 U.S.C. 80b–*  
4 *1 et seq.) is amended by inserting after section 223 (as*  
5 *added by section 3 of this Act) the following new section:*

6 “DESIGNATION OF SELF-REGULATORY ORGANIZATIONS

7 “SEC. 224. (a) DESIGNATION TO CONDUCT EXAMINA-  
8 TIONS.—The Commission, by rule, consistent with the pub-  
9 lic interest, the protection of investors, and the purposes of  
10 this title, may designate one or more self-regulatory organi-  
11 zations registered with the Commission under section 6 or  
12 15A of the Securities Exchange Act of 1934, to conduct peri-  
13 odic examinations of its members, and affiliates of mem-  
14 bers, that are registered or required to register under this  
15 title, to determine compliance with applicable provisions of  
16 this title and the rules and regulations thereunder. Such  
17 rule shall specify the minimum scope and frequency for  
18 such examinations and shall, to the extent consistent with  
19 the protection of investors, be designed to avoid unnecessary  
20 regulatory duplication or undue regulatory burdens. Such  
21 self-regulatory organization may discipline such members  
22 and affiliates of members for violations of the applicable  
23 provisions of this title and the rules and regulations there-  
24 under pursuant to the standards and procedures set forth  
25 in sections 6, 15A, and 19 of the Securities Exchange Act  
26 of 1934. The money penalties imposed by a self-regulatory



1 *organization for violations of this title shall not exceed those*  
2 *contained in section 203(i).*

3 *“(b) LIMITATIONS.—*

4 *“(1) PRIMARY BUSINESS LIMITATION.—The Com-*  
5 *mission shall not exercise the designation authority*  
6 *contained in subsection (a) for members or affiliates*  
7 *of members if the primary business of the member*  
8 *and its affiliates is investment advisory activities.*

9 *“(2) LIMITATION WITH RESPECT TO AFFILIATES*  
10 *OF MEMBERS.—The Commission shall not exercise the*  
11 *authority contained in subsection (a) for an affiliate*  
12 *of a member if—*

13 *“(A) the primary business of the affiliate is*  
14 *investment advisory activities;*

15 *“(B) the affiliate is an affiliate of the mem-*  
16 *ber solely as a result of the adviser’s (or an asso-*  
17 *ciated person of the adviser’s) registration with*  
18 *the member as a registered representative; and*

19 *“(C) the affiliate is a registered representa-*  
20 *tive of the member solely to enable the adviser to*  
21 *execute transactions that are incidental to the*  
22 *investment adviser’s primary business;*

23 *unless the Commission determines, in accordance with*  
24 *such other criteria as the Commission establishes by*  
25 *rule, that such exercise of designation authority is*

1     *consistent with the public interest, the protection of*  
2     *investors, the purposes of this title, and the objectives*  
3     *of the Commission's investment adviser examination*  
4     *program.*

5             “(3) *LIMITATION WITH RESPECT TO SAVINGS AS-*  
6     *SOCIATION AFFILIATES OF MEMBERS.—The Commis-*  
7     *sion shall not exercise the authority contained in sub-*  
8     *section (a) for an affiliate of a member if the affiliate*  
9     *is a savings association, as such term is defined in*  
10    *section 3(b)(1) of the Federal Deposit Insurance Act*  
11    *(12 U.S.C. 1813(b)(1)).*

12            “(4) *DEFINITIONAL RULES.—For purposes of*  
13    *this subsection, the Commission may, by rule, estab-*  
14    *lish criteria for defining the terms ‘primary business’*  
15    *and ‘incidental to the investment adviser’s primary*  
16    *business’.*

17            “(c) *AUTHORITY TO IMPOSE FEES.—*

18            “(1) *IN GENERAL.—Any self-regulatory organi-*  
19    *zation designated by the Commission to perform the*  
20    *examinations specified in subsection (a) shall have*  
21    *the authority to collect fees in accordance with this*  
22    *subsection.*

23            “(2) *LIMITATION.—The total fee paid by a reg-*  
24    *istered investment adviser under this subsection shall*  
25    *not exceed an amount determined in accordance with*

1       *rules prescribed by the Commission. Such rules shall*  
2       *require that the fees collected by a self-regulatory or-*  
3       *ganization under this subsection—*

4               “(A) *cover only the costs of the self-regu-*  
5               *latory organization’s expenses for examinations*  
6               *conducted pursuant to subsection (a);*

7               “(B) *as to any investment adviser, bear a*  
8               *reasonable relationship to the costs of conducting*  
9               *an examination of that adviser pursuant to sub-*  
10              *section (a); and*

11              “(C) *not exceed such portion of the fee au-*  
12              *thorized under section 203A as the Commission*  
13              *determines is allocable to the Commission’s ex-*  
14              *penses for conducting such an examination.*

15              “(3) *REDUCTION OF SECTION 203A FEES.—The*  
16              *amount of any fee that a registered investment ad-*  
17              *viser is required to pay under section 203A with re-*  
18              *spect to any fiscal year shall be reduced by the*  
19              *amount paid to a self-regulatory organization in ac-*  
20              *cordance with this subsection with respect to such fis-*  
21              *cal year.*

22              “(d) *EFFECTIVE DATE OF RULE.—A rule prescribed*  
23              *by the Commission under this section shall not be effective*  
24              *until 90 days after the date on which the Commission sub-*  
25              *mits to each House of Congress a report—*

1           “(1) containing the text of the proposed rule and  
2           the reasons therefor;

3           “(2) describing the procedures to be used to co-  
4           ordinate the collection of fees by the Commission  
5           under section 203A and by a self-regulatory organiza-  
6           tion under the rule; and

7           “(3) containing such other information as may  
8           be necessary to describe the implementation and en-  
9           forcement of the rule.

10          “(e) *DEFINITION.*—For purposes of this section, the  
11          term ‘affiliate’ shall mean any person directly or indirectly  
12          controlling, controlled by, or under common control with  
13          a member.”.

14          **SEC. 5. SUITABILITY AND OTHER ADVISER OBLIGATIONS.**

15          (a) *AMENDMENT.*—Section 206 of the Investment Ad-  
16          visers Act of 1940 (15 U.S.C. 80b–6) is amended to read  
17          as follows:

18          “*PROHIBITED TRANSACTIONS BY INVESTMENT ADVISERS*

19          “*SEC. 206. (a) PROHIBITED CONDUCT.*—It shall be  
20          unlawful for any investment adviser or any person associ-  
21          ated with an investment adviser, by use of the mails or any  
22          means or instrumentality of interstate commerce, directly  
23          or indirectly—

24                  “(1) to employ any device, scheme, or artifice to  
25                  defraud any client or prospective client;

1           “(2) to engage in any transaction, practice, or  
2           course of business which operates as a fraud or deceit  
3           upon any client or prospective client;

4           “(3) acting as principal for his own account,  
5           knowingly to sell any security to or purchase any se-  
6           curity from a client, or acting as broker for a person  
7           other than such client, knowingly to effect any sale or  
8           purchase of any security for the account of such cli-  
9           ent, without disclosing to such client in writing before  
10          the completion of such transaction the capacity in  
11          which he is acting and obtaining the consent of the  
12          client to such transaction;

13          “(4) to engage in any act, practice, or course of  
14          business which is fraudulent, deceptive, or manipula-  
15          tive;

16          “(5) to provide investment advice to any client,  
17          other than in connection with impersonal advisory  
18          services, unless the adviser—

19                  “(A) prior to providing any investment ad-  
20                  vice, and as appropriate thereafter, makes a rea-  
21                  sonable inquiry into the client’s financial situa-  
22                  tion, investment experience, and investment ob-  
23                  jectives;

24                  “(B) reasonably determines that the invest-  
25                  ment advice is suitable for the client; and

1           “(C) maintains reasonable records, in ac-  
2           cordance with such rules as the Commission shall  
3           prescribe, of the information obtained from the  
4           inquiries the adviser made in complying with  
5           this paragraph; or

6           “(6) to guarantee a client that a specific result  
7           will be achieved as a result of the advisory services  
8           provided by the investment adviser.

9           “(b) EXEMPTIONS AND SPECIAL RULES.—

10           “(1) EXEMPTION.—The prohibitions of sub-  
11           section (a)(3) shall not apply to any transaction with  
12           a customer of a broker or dealer if such broker or  
13           dealer is not acting as an investment adviser in rela-  
14           tion to such transaction.

15           “(2) AUTHORITY TO DEFINE AND PRESCRIBE.—  
16           The Commission shall, for the purposes of subsection  
17           (a)(4), by rules define, and prescribe means reason-  
18           ably designed to prevent, such acts, practices, and  
19           courses of business as are fraudulent, deceptive, or  
20           manipulative.

21           “(3) DEFINITION OF IMPERSONAL ADVISORY  
22           SERVICES.—As used in subsection (a)(5), the term  
23           ‘impersonal advisory services’ means any investment  
24           advisory services provided—

1           “(A) by means of written material or oral  
2           statements which do not purport to meet the ob-  
3           jectives or needs of specific individuals or ac-  
4           counts;

5           “(B) through the issuance of statistical in-  
6           formation containing no expression of opinion as  
7           to the investment merits of a particular security;  
8           or

9           “(C) by any combination of the foregoing  
10          services.”.

11          (b) *RULEMAKING REQUIRED.*—The Commission shall  
12          prescribe rules for purposes of paragraph (5)(C) of section  
13          206(a) of the Investment Advisers Act of 1940 (as added  
14          by subsection (a) of this section) within one year after the  
15          date of enactment of this Act.

16          **SEC. 6. ADDITIONAL DISCLOSURE OBLIGATIONS OF IN-**  
17          **VESTMENT ADVISERS.**

18          (a) *ADDITIONAL OBLIGATIONS.*—Section 204 of the In-  
19          vestment Advisers Act of 1940 (15 U.S.C. 80b-4) is amend-  
20          ed—

21                 (1) by striking the heading of such section and  
22                 inserting the following:

23                         “PERIODIC REPORTS AND OTHER DISCLOSURE  
24                                 REQUIREMENTS”;

25                 (2) by inserting “(a) PERIODIC AND OTHER RE-  
26                 PORTS.—” after “SEC. 204.”; and

1           (3) *by adding at the end the following new sub-*  
2 *sections:*

3           “(b) *BROCHURE REQUIRED.*—

4           “(1) *IN GENERAL.*—Each person registered under  
5 *section 203 of this title shall disseminate to each cli-*  
6 *ent or prospective client a document disclosing mate-*  
7 *rial facts concerning matters listed in paragraphs (2)*  
8 *and (3) and such other matters as the Commission*  
9 *shall prescribe. In order to provide for timely and ef-*  
10 *fective disclosure of such facts and matters to clients,*  
11 *the Commission shall by rule prescribe the format of*  
12 *the document and the timing of its dissemination.*

13           “(2) *CONTENTS OF BROCHURE.*—The document  
14 *required by paragraph (1) shall include information*  
15 *concerning—*

16           “(A) *the education and business background*  
17 *of such person and of any associated person pro-*  
18 *viding significant investment advisory services*  
19 *to the client,*

20           “(B) *compensation arrangements between*  
21 *the client and the investment adviser,*

22           “(C) *the nature of services offered,*

23           “(D) *business practices,*

24           “(E) *methods for obtaining information on*  
25 *the disciplinary history and registration of the*



1       *investment adviser and persons associated with*  
2       *the investment adviser, and*

3               “(F) *conflicts of interest which could rea-*  
4       *sonably be expected to impair the rendering of*  
5       *disinterested advice.*

6               “(3) *PROMINENT DISCLOSURES.—Such document*  
7       *shall also prominently disclose—*

8               “(A) *that—*

9                       “(i) *the registered person receives or*  
10       *may receive, directly or indirectly, sales*  
11       *commissions or other fees in connection*  
12       *with a purchase or sale effected on behalf of*  
13       *a client; or*

14                      “(ii) *the registered person will not re-*  
15       *ceive, directly or indirectly, any sales com-*  
16       *mission or other fees in connection with*  
17       *such purchase or sale, but the client may be*  
18       *charged a sales commission or other fee by*  
19       *another person in connection with such pur-*  
20       *chase or sale; and*

21               “(B) *that remedies may be available to the*  
22       *client with respect to disputes arising out of the*  
23       *advisory relationship.*

24               “(4) *DEFINITION.—The Commission shall define*  
25       *‘associated person providing significant investment*

1     *advisory services to the client’ by rule for purposes of*  
2     *this subsection.*

3     “(c) *TRANSACTION REPORTS.*—

4         “(1) *INITIAL DISCLOSURE.*—Before a purchase or  
5     *sale is effected on behalf of any client, each registered*  
6     *investment adviser shall, in accordance with rules*  
7     *prescribed by the Commission, disclose to the client*  
8     *the total amount of commissions, fees, or other charges*  
9     *that may reasonably be expected to be charged in con-*  
10    *nection with the transaction (or, in the case of pay-*  
11    *ments from third parties, that a payment will be re-*  
12    *ceived) and that the adviser or a related person will*  
13    *receive a portion of the commission, fee, charge, or*  
14    *payment. Such initial disclosure shall be in writing*  
15    *if the purchase or sale was recommended in writing.*

16         “(2) *CONFIRMATION.*—After a purchase or sale is  
17    *effected, each registered investment adviser shall*  
18    *transmit to each client a written statement that dis-*  
19    *closes the amount of commissions, fees, or other*  
20    *charges charged in connection with the transaction*  
21    *(or, in the case of payments from third parties, that*  
22    *a payment has been or will be received). Such written*  
23    *statement shall be in such form and contain such in-*  
24    *formation, and be provided in accordance with such*  
25    *rules, as the Commission shall prescribe. Such rules*

1     *shall, to the extent consistent with the protection of*  
2     *investors, permit delivery of a confirmation statement*  
3     *of a broker or a dealer that includes information that*  
4     *meets the requirements of this subsection (and the*  
5     *rules adopted thereunder) in order to satisfy such re-*  
6     *quirements.*

7             “(3) *WAIVER.—The Commission may, by rule,*  
8     *permit an investment adviser to omit disclosure re-*  
9     *quired by this subsection with the knowing written*  
10    *consent of the client.*

11            “(4) *EXCEPTIONS.—This subsection shall not*  
12    *apply—*

13                “(A) *with respect to any purchase or sale*  
14     *for which the investment adviser, and any per-*  
15     *son associated or under common control with the*  
16     *investment adviser, will not receive any portion*  
17     *of the amount charged or deducted in connection*  
18     *with the purchase or sale, and will not receive*  
19     *any payment from a third party required to be*  
20     *disclosed under paragraph (1);*

21                “(B) *with respect to accounts for which the*  
22     *person is authorized to exercise investment dis-*  
23     *cretion; or*

1           “(C) with respect to any account for which  
2           the person is not acting as an investment ad-  
3           viser.

4           “(5) *SPECIAL RULE.*—The provisions of this sub-  
5           section shall also apply to any person associated with  
6           an investment adviser effecting transactions for advi-  
7           sory clients through a broker or dealer with which the  
8           person is associated.

9           “(d) *PERIODIC REPORTS.*—

10           “(1) *IN GENERAL.*—Each registered investment  
11           adviser shall provide to each client a periodic written  
12           statement in such form and containing such informa-  
13           tion as the Commission shall prescribe by rule con-  
14           sistent with the public interest, the protection of in-  
15           vestors, and the purposes of this title. Such rule shall  
16           require the disclosure of—

17           “(A) commissions, fees, or other charges  
18           paid by the client during the period for services  
19           provided by the investment adviser and any per-  
20           son associated or under common control with the  
21           investment adviser;

22           “(B) compensation directly or indirectly re-  
23           ceived during the period by the investment ad-  
24           viser, or any person associated or under common  
25           control with the investment adviser, from any

1        *third party with respect to any recommended*  
2        *transaction;*

3                *“(C) in the case of a client account for*  
4        *which the investment adviser provides invest-*  
5        *ment supervisory services, securities positions*  
6        *held in the account at the beginning and at the*  
7        *end of the period; and*

8                *“(D) such other matters as the Commission*  
9        *shall prescribe.*

10                *“(2) COMMISSION RULES.—The rule prescribed*  
11        *by the Commission pursuant to paragraph (1) shall*  
12        *require that the format and timing of delivery be de-*  
13        *signed to present the required information in a man-*  
14        *ner that readily permits clients to compare the costs*  
15        *charged by the investment adviser with the costs*  
16        *charged by other advisers. In adopting such rule, the*  
17        *Commission shall require an investment adviser*  
18        *whose clients purchase or sell investment products*  
19        *through persons other than such adviser, or persons*  
20        *associated or under common control with such ad-*  
21        *viser, to disclose to its clients that such information*  
22        *concerning costs charged does not include commis-*  
23        *sions or other fees paid in connection with such pur-*  
24        *chases or sales. Such rule shall, to the extent consist-*  
25        *ent with the protection of investors, permit delivery of*

1     *a report of a broker or dealer that includes informa-*  
2     *tion that meets the requirements of this subsection*  
3     *(and the rules adopted thereunder) in order to satisfy*  
4     *such requirements.*

5             “(3) *WAIVER.*—*The Commission may, by rule,*  
6     *permit an investment adviser to provide the statement*  
7     *required by paragraph (1) no more frequently than*  
8     *annually if the client knowingly waives, in writing,*  
9     *the right to obtain such statement more frequently*  
10    *than annually.*

11            “(4) *EXCEPTION.*—*This subsection shall not*  
12    *apply with respect to any account for which the per-*  
13    *son is not acting as an investment adviser.*

14            “(e) *FACILITIES FOR FILING RECORDS AND REPORTS;*  
15    *ACCESS TO DISCIPLINARY AND OTHER INFORMATION.*—

16            “(1) *FILING DEPOSITORIES.*—*The Commission,*  
17    *by rule, may require any investment adviser—*

18                    “(A) *to file with the Commission any fee,*  
19                    *application, report, or notice required by this*  
20                    *title or by the rules issued under this title*  
21                    *through any entity designated by the Commis-*  
22                    *sion for that purpose; and*

23                    “(B) *to pay the reasonable costs associated*  
24                    *with (i) such filing, and (ii) the maintenance of*

1           the toll-free telephone listing required by para-  
2           graph (2).

3           “(2) *LISTING FOR TOLL-FREE INQUIRIES.*—The  
4           Commission shall require the entity designated by the  
5           Commission to receive fees, applications, reports, or  
6           notices pursuant to paragraph (1) to—

7                   “(A) establish and maintain a toll-free tele-  
8                   phone listing to receive inquiries regarding the  
9                   disciplinary and other information involving in-  
10                  vestment advisers and persons associated with  
11                  investment advisers; and

12                   “(B) respond promptly to such inquiries in  
13                  writing.

14          Such designated entity may charge persons, other  
15          than individual investors, reasonable fees for the cost  
16          of providing written responses to inquiries. Such des-  
17          ignated entity shall not have any liability to any per-  
18          son for any actions taken or omitted in good faith  
19          under this paragraph.”.

20          (b) *RULEMAKING REQUIRED.*—The Commission shall  
21          prescribe rules for purposes of subsections (b), (c), and (d)  
22          of section 204 of the Investment Advisers Act of 1940 (as  
23          added by subsection (a) of this section) within one year  
24          after the date of enactment of this Act.

1 **SEC. 7. BOND REQUIREMENT.**

2 *Section 208 of the Investment Advisers Act of 1940 (15*  
3 *U.S.C. 80b–8) is amended by adding at the end the follow-*  
4 *ing:*

5 “(e) *BOND REQUIREMENT.*—

6 “(1) *IN GENERAL.*—*The Commission, by rules*  
7 *for the protection of investors, shall require any in-*  
8 *vestment adviser registered under section 203 who—*

9 “(A) *is authorized to exercise investment*  
10 *discretion, as defined in section 3(a)(35) of the*  
11 *Securities Exchange Act of 1934, with respect to*  
12 *an account,*

13 “(B) *has access to the securities or funds of*  
14 *a client, or*

15 “(C) *is an investment adviser of an invest-*  
16 *ment company, as defined in section 2(a)(20) of*  
17 *the Investment Company Act of 1940,*

18 *to obtain a bond from a reputable fidelity insurance*  
19 *company against larceny and embezzlement in such*  
20 *reasonable amounts and covering such officers, part-*  
21 *ners, directors, and employees of the investment ad-*  
22 *viser as the Commission may prescribe.*

23 “(2) *CONSIDERATIONS IN RULEMAKING.*—*In im-*  
24 *plementing paragraph (1), the Commission shall con-*  
25 *sider—*



1           “(A) the degree of risk to client assets that  
2           is involved;

3           “(B) the cost and availability of fidelity  
4           bonds;

5           “(C) existing fidelity bonding requirements;  
6           and

7           “(D) any alternative means to protect client  
8           assets.

9           “(3) EXEMPTION AUTHORITY.—The Commission  
10          by rule may exempt any person or class of persons,  
11          under such terms and conditions and for such periods  
12          as the Commission shall provide in such rule, from  
13          the requirements of this subsection and the rules  
14          thereunder.”.

15   **SEC. 8. DISQUALIFYING CONDUCT.**

16          (a) AMENDMENT.—Section 203(e) of the Investment  
17          Advisers Act of 1940 (15 U.S.C. 80b–3(e)) is amended—

18               (1) by redesignating paragraphs (3) through (7)  
19               as paragraphs (4) through (8), respectively; and

20               (2) by inserting after paragraph (2) the follow-  
21               ing new paragraph:

22               “(3) has been convicted within ten years preced-  
23               ing the filing of any application for registration or  
24               at any time thereafter of any crime that is punishable  
25               by imprisonment for one or more years and that is

1       *not described in paragraph (2) of this subsection or*  
 2       *of a substantially equivalent crime by a foreign court*  
 3       *of competent jurisdiction.”.*

4       **(b) CONFORMING AMENDMENTS.**—*Section 203 of such*  
 5       *Act is further amended—*

6               *(1) in subsection (e)(6) (as redesignated by sub-*  
 7       *section (a) of this section), by striking “this para-*  
 8       *graph (5)” and inserting “this paragraph (6)”;*

9               *(2) in subsection (f)—*

10               *(A) by striking “paragraph (1), (4), (5), or*  
 11       *(7)” and inserting “paragraph (1), (5), (6), or*  
 12       *(8)”;* and

13               *(B) by striking “paragraph (3)” and insert-*  
 14       *ing “paragraph (4)”;* and

15               *(3) in subsection (i)(1)(D), by striking “section*  
 16       *203(e)(5) of this title” and inserting “subsection*  
 17       *(e)(6) of this section”.*

18       **SEC. 9. CONFIDENTIALITY.**

19       *Section 208 of the Investment Advisers Act of 1940 (15*  
 20       *U.S.C. 80b–8), as amended by section 7, is further amended*  
 21       *by adding at the end the following new subsection:*

22               **“(f) DISCLOSURE OF CLIENT INFORMATION PROHIB-**  
 23       **ITED.—**

24               **“(1) ADVISER DISCLOSURE.—***It shall be unlaw-*  
 25       *ful for any investment adviser to disclose any person-*

1 *ally identifiable financial information with respect to*  
2 *any client unless required by law to do so, or un-*  
3 *less—*

4 *“(A) the client has been adequately in-*  
5 *formed of the proposed information disclosure, in*  
6 *accordance with rules prescribed by the Commis-*  
7 *sion, and (i) has been afforded the opportunity,*  
8 *in accordance with such rules, to object to the*  
9 *disclosure, and (ii) has not objected or has af-*  
10 *firmatively consented;*

11 *“(B) the information disclosed is necessary*  
12 *and appropriate in order to establish an advi-*  
13 *sory or brokerage account or to effect or attempt*  
14 *to effect a transaction for the client;*

15 *“(C) the information (i) is requested by rep-*  
16 *resentatives of the Commission, a State agency*  
17 *whose primary assignment is the regulation of*  
18 *the securities business, or a self-regulatory orga-*  
19 *nization, or (ii) is requested by subpoena; or*

20 *“(D) the information is requested by the cli-*  
21 *ent’s auditors or accountants.*

22 *“(2) SECONDARY DISCLOSURE.—It is unlawful*  
23 *for any person to whom information is disclosed for*  
24 *the purpose described in paragraph (1)(B) to use such*

1        *information for any purpose other than the effec-*  
2        *tuation of the client's transaction."*

3        **SEC. 10. CUSTODIANSHIP.**

4        (a) *FINDINGS.—The Congress finds that—*

5                (1) *most clients of investment advisers who give*  
6                *their advisers discretionary authority over their secu-*  
7                *rities and funds provide for the safekeeping of their*  
8                *securities and funds with a custodian;*

9                (2) *it is a customary business practice for*  
10               *custodians to provide reports of the transactions in*  
11               *client accounts directly to clients;*

12               (3) *such direct reporting provides an important*  
13               *safeguard against improper use of client assets; and*

14               (4) *permitting advisers to serve as the sole recip-*  
15               *ient of custodial account communications has allowed,*  
16               *and may continue to allow, unscrupulous persons to*  
17               *misuse client assets, causing substantial losses for*  
18               *those clients.*

19        (b) *REPORT.—The Commission, within 18 months of*  
20        *enactment of this Act, after consultation with the appro-*  
21        *priate Federal banking agencies (as such term is defined*  
22        *in section 3(q) of the Federal Deposit Insurance Act), shall*  
23        *submit a report to Congress—*

24               (1) *analyzing the risks to investors when an in-*  
25               *vestment adviser is made the sole recipient of commu-*

1        *nications from the custodian or when an investment*  
2        *adviser or affiliate thereof serves as the custodian;*  
3        *and*  
4            *(2) making any recommendations the Commis-*  
5        *sion believes are necessary to eliminate or reduce these*  
6        *risks.*

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