104TH CONGRESS, 2d Session } HOUSE OF REPRESENTATIVES { REPORT 104–622

SECURITIES AMENDMENTS OF 1996

JUNE 17, 1996.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. BLILEY, from the Committee on Commerce, submitted the following

R E P O R T

[To accompany H.R. 3005]

[Including cost estimate of the Congressional Budget Office]

The Committee on Commerce, to whom was referred the bill (H.R. 3005) to amend the Federal securities laws in order to promote efficiency and capital formation in the financial markets, and to amend the Investment Company Act of 1940 to promote more efficient management of mutual funds, protect investors, and provide more effective and less burdensome regulation, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

CONTENTS

29–006

THE AMENDMENT

The amendment is as follows:

Strike out all after the enacting clause and insert in lieu thereof the following:

SECTION 1. SHORT TITLE; TABLE OF CONTENTS.

(a) SHORT TITLE.—This Act may be cited as the "Securities Amendments of 1996".

(b) TABLE OF CONTENTS.—The table of contents of this Act is as follows:

TITLE I—CAPITAL MARKETS DEREGULATION AND LIBERALIZATION

SEC. 101. SHORT TITLE.

This title may be cited as the "Capital Markets Deregulation and Liberalization Act of 1996".

SEC. 102. CREATION OF NATIONAL SECURITIES MARKETS.

(a) SECURITIES ACT OF 1933.—

(1) AMENDMENT.—Section 18 of the Securities Act of 1933 (15 U.S.C. 77r) is amended to read as follows:

"SEC. 18. EXEMPTION FROM STATE REGULATION OF SECURITIES OFFERINGS.

"(a) SCOPE OF EXEMPTION.—Except as otherwise provided in this section, no law, rule, regulation, or order, or other administrative action of any State or Territory of the United States, or the District of Columbia, or any political subdivision thereof—

"(1) requiring, or with respect to, registration or qualification of securities, or registration or qualification of securities transactions, shall directly or indirectly apply to a security that—

"(A) is a covered security; or

"(B) will be a covered security upon completion of the transaction;

"(2) shall directly or indirectly prohibit, limit, or impose conditions upon the use of—

"(A) with respect to a covered security described in subsection (b)(1) or (c)(1)—

"(i) any offering document that is prepared by the issuer; or

"(ii) any offering document that is not prepared by the issuer if such offering document is required to be and is filed with the Commission or any national securities organization registered under section 15A of the Securities Exchange Act of 1934 (15 U.S.C. 78o–3);

"(B) with respect to a covered security described in paragraph (2), (3), or (4) of subsection (b), any offering document; or

"(C) any proxy statement, report to shareholders, or other disclosure document relating to a covered security or the issuer thereof that is required to be and is filed with the Commission or any national securities organization registered under section 15A of the Securities Exchange Act of 1934 (15 U.S.C. 78o–3); or

"(3) shall directly or indirectly prohibit, limit, or impose conditions, based on the merits of such offering or issuer, upon the offer or sale of any security described in paragraph (1).

"(b) COVERED SECURITIES.—For purposes of this section, the following are covered securities:

"(1) EXCLUSIVE FEDERAL REGISTRATION OF NATIONALLY TRADED SECURITIES.—A security is a covered security if such security is—

"(A) listed, or authorized for listing, on the New York Stock Exchange or the American Stock Exchange, or included or qualified for inclusion in the National Market System of the National Association of Securities Dealers Automated Quotation System (or any successor to such entities);

"(B) listed, or authorized for listing, on a national securities exchange (or tier or segment thereof) that has listing standards that the Commission determines by rule (on its own initiative or on the basis of a petition) are substantially similar to the listing standards applicable to securities described in subparagraph (A); or

"(C) is a security of the same issuer that is equal in seniority or senior to a security described in subparagraph (A) or (B).

"(2) EXCLUSIVE FEDERAL REGISTRATION OF INVESTMENT COMPANIES.—A security is a covered security if such security is a security issued by an investment company that is registered under the Investment Company Act of 1940 (15 U.S.C. 80a et seq.).

"(3) SALES TO QUALIFIED PURCHASERS.—A security is a covered security with respect to the offer or sale of the security to qualified purchasers, as defined by the Commission by rule. In prescribing such rule, the Commission may define qualified purchaser differently with respect to different categories of securities, consistent with the public interest and the protection of investors.

"(4) EXEMPTION IN CONNECTION WITH CERTAIN EXEMPT OFFERINGS.—A security is a covered security if—

"(A) the offer or sale of such security is exempt from registration under this title pursuant to section 4(1) or 4(3), and—

"(i) the issuer of such security files reports with the Commission pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m, 78o(d)); or

"(ii) the issuer is exempt from filing such reports;

"(B) such security is exempt from registration under this title pursuant to section 4(4);

"(C) the offer or sale of such security is exempt from registration under this title pursuant to section 3(a), other than the offer or sale of a security that is exempt from such registration pursuant to paragraph (4) or (11) of such section, except that a municipal security that is exempt from such registration pursuant to paragraph (2) of such section is not a covered security with respect to the offer or sale of such security in the State in which such security is issued; or

"(D) the offer or sale of such security is exempt from registration under this title pursuant to Commission rule or regulation under section 4(2) of this title.

"(c) CONDITIONALLY COVERED SECURITIES.—

"(1) FEDERALLY REGISTERED OFFERINGS.—Subject to the limitations contained in paragraphs (2) and (3), a security is a covered security if—

"(A) the issuer of such security has (or will have upon conclusion of the transaction) total assets exceeding $10,000,000;

"(B) such security is the subject of a registration statement that is filed with the Commission pursuant to this title; and

"(C) the issuer files with such registration statement audited financial statements for each of the two most recent fiscal years of its operations ending before the filing of the registration statement.

"(2) LIMITATIONS FOR CERTAIN OFFERINGS.—Notwithstanding paragraph (1), a security is not a covered security if such security is—

"(A) a security of an issuer which is a blank check company (as defined in section 7(b) of this title), a partnership, a limited liability company, or a direct participation investment program;

"(B) a penny stock (as such term is defined in section 3(a)(51) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(51)); or

"(C) a security issued in an offering relating to a rollup transaction (as such term is defined in paragraphs (4) and (5) of section 14(h) of such Act (15 U.S.C. 78n(h)(4), (5)).

"(3) LIMITATIONS BASED ON MISCONDUCT.—Notwithstanding paragraph (1), a security is not a covered security—

"(A) with respect to any State, if the issuer, or a principal officer or principal shareholder thereof—

"(i) is subject to a statutory disqualification, as defined in subparagraph (A), (B), (C), or (D) of section 3(a)(39) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(39));

"(ii) has been convicted within 5 years prior to the offering of any felony under Federal or State law in connection with the offer, purchase, or sale of any security, or any felony under Federal or State law involving fraud or deceit; or

"(iii) is currently named in and subject to any order, judgment, or decree of any court of competent jurisdiction acting pursuant to Federal or State law temporarily or permanently restraining or enjoining such issuer, officer, or shareholder from engaging in or continuing any conduct or practice in connection with a security; or

"(B) with respect to a particular State, if the issuer, or a principal officer or principal shareholder thereof—

"(i) has filed a registration statement which is the subject of a currently effective stop order entered pursuant to that State's securities laws within 5 years prior to the offering;

"(ii) is currently named in and subject to any administrative enforcement order or judgment of that State's securities commission (or any agency or office performing like functions) entered within 5 years prior to the offering, or is currently named in and subject to any other administrative enforcement order or judgment of that State entered within 5 years prior to the offering that finds fraud or deceit; or

"(iii) is currently named in and subject to any administrative enforcement order or judgment of that State which prohibits or denies registration, or revokes the use of any exemption from registration, in connection with the offer, purchase, or sale of securities.

"(4) EXCEPTIONS TO LIMITATIONS.—

"(A) EXEMPTIONS.—The limitations in paragraph (3)(A) shall not apply if the Commission has exempted the subject person from the application of such paragraph by rule or order, and the limitations in paragraph (3)(B) shall not apply if the securities commission (or any agency or office performing like functions) of the affected State has exempted the subject person from the application of such paragraph by rule or order.

"(B) REASONABLE STEPS.—The provisions of paragraph (3) shall not apply if the issuer has taken reasonable steps to ascertain whether any principal officer or principal shareholder is subject to such paragraph, and such steps do not reveal a person who is subject to such paragraph. An issuer shall be considered to have taken reasonable steps if such issuer or its agent has conducted a search of any centralized data bases that the Commission may designate by rule, and has received an affidavit under oath by each such principal officer or principal shareholder stating that such officer or shareholder is not subject to the provisions of paragraph (3).

"(C) EFFECT OF LIMITATIONS ON REMEDIES.—Notwithstanding paragraph (3), an issuer shall not be subject to a right of rescission under State securities laws solely as a result of the operation of such paragraph.

"(5) NO EFFECT UNDER SUBSECTION (B).—No limitation under this subsection shall affect the treatment of a security that qualifies as a covered security under subsection (b).

"(d) PRESERVATION OF AUTHORITY.—

"(1) FRAUD AUTHORITY.—Consistent with this section, the securities commission (or any agency or office performing like functions) of any State or Territory of the United States, or the District of Columbia, shall retain jurisdiction under the laws of such State, Territory, or District to investigate and bring enforcement actions with respect to fraud or deceit in connection with securities or securities transactions.

"(2) PRESERVATION OF FILING REQUIREMENTS.—

"(A) NOTICE FILINGS PERMITTED.—Nothing contained in this section shall prohibit the securities commission (or any agency or office performing like functions) of any State or Territory of the United States, or the District of Columbia, from requiring the filing of any documents filed with the Commission pursuant to this title solely for notice purposes, together with any required fee.

"(B) PRESERVATION OF FEES.—Until otherwise provided by State law enacted after the date of enactment of the Securities Amendments of 1996, filing or registration fees with respect to securities or securities transactions may continue to be collected in amounts determined pursuant to State law as in effect on the day before such date.

"(C) FEES NOT PERMITTED ON LISTED SECURITIES.—Notwithstanding subparagraphs (A) and (B), no filing or fee may be required with respect to any security that is a covered security pursuant to subsection (b)(1) of this section, or will be such a covered security upon completion of the transaction, or is a security of the same issuer that is equal in seniority or senior to a security that is a covered security pursuant to such subsection.

"(3) ENFORCEMENT OF REQUIREMENTS.—Nothing in this section shall prohibit the securities commission (or any agency or office performing like functions) of any State or Territory of the United States, or the District of Columbia, from suspending the offer or sale of securities within such State, Territory, or District as a result of the failure to submit any filing or fee required under law and permitted under this section.

"(e) DEFINITIONS.—For purposes of this section:

"(1) PRINCIPAL OFFICER.—The term 'principal officer' means a director, chief executive officer, or chief financial officer of an issuer, or any other officer performing like functions.

"(2) PRINCIPAL SHAREHOLDER.—The term 'principal shareholder' means any person who is directly or indirectly the beneficial owner of more than 20 percent of any class of equity security of an issuer. When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed a 'person' for purposes of this paragraph. In determining, for purposes of this paragraph, any percentage of a class of any security, such class shall be deemed to consist of the amount of the outstanding securities of such class, exclusive of any securities of such class held by or for the account of the issuer or a subsidiary of the issuer.

"(3) OFFERING DOCUMENT.—The term 'offering document' has the meaning given the term 'prospectus' by section 2(10), but without regard to the provisions of clauses (a) and (b) of such section, except that, with respect to a security described in subsection (b)(2) of this section, such term also includes a communication that is not deemed to offer such a security pursuant to a rule of the Commission.

"(4) PREPARED BY THE ISSUER.—Within 6 months after the date of enactment of the Securities Amendments of 1996, the Commission shall, by rule, define the term 'prepared by the issuer' for purposes of this section.".

(2) STUDY OF UNIFORMITY.—The Securities Exchange Commission shall conduct a study after consultation with States, issuers, brokers, and dealers on the extent to which uniformity of State regulatory requirements for securities or securities transactions has been achieved for securities that are not covered securities (within the meaning of section 18 of the Securities Act of 1933 as amended by paragraph (1) of this subsection). Such study shall specifically focus on the impact of such uniformity or lack thereof on the cost of capital, innovation and technological development in securities markets, and duplicative regulation with respect to securities issuers (including small business), brokers, and dealers and the effect on investor protection. The Commission shall submit to the Congress a report on the results of such study within one year after the date of enactment of this Act.

(b) BROKER/DEALER REGULATION.—

(1) AMENDMENT.—Section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 78o) is amended by adding at the end the following new subsection:

"(h) LIMITATIONS ON STATE LAW.—

"(1) CAPITAL, MARGIN, BOOKS AND RECORDS, BONDING, AND REPORTS.—No law, rule, regulation, or order, or other administrative action of any State or political subdivision thereof shall establish capital, custody, margin, financial responsibility, making and keeping records, bonding, or financial or operational reporting requirements for brokers, dealers, municipal securities dealers, government securities brokers, or government securities dealers that differ from, or are in addition to, the requirements in those areas established under this title. The Commission shall consult periodically the securities commissions (or any agency or office performing like functions) of the States concerning the adequacy of such requirements as established under this title.

"(2) EXEMPTION TO PERMIT SERVICE TO CUSTOMERS.—No law, rule, regulation, or order, or other administrative action of any State or political subdivision thereof shall prohibit an associated person from effecting a transaction described in paragraph (3) for a customer in such State if—

"(A) such associated person is not ineligible to register with such State for any reason other than such a transaction;

"(B) such associated person is registered with a registered securities association and at least one State; and

"(C) the broker or dealer with which such person is associated is registered with such State.

"(3) DESCRIBED TRANSACTIONS.—A transaction is described in this paragraph if—

"(A) such transaction is effected—

"(i) on behalf of a customer that, for 30 days prior to the day of the transaction, maintains an account with the broker or dealer; and

"(ii) by an associated person (I) to which the customer was assigned for 14 days prior to the day of the transaction, and (II) who is registered with a State in which the customer was a resident or was present for at least 30 consecutive days during the one-year period prior to the transaction;

except that, if the customer is present in another State for 30 or more consecutive days or has permanently changed his or her residence to another State, such transaction is not described in this subparagraph unless the associated person files with such State an application for registration within 10 business days of the later of the date of the transaction or the date of the discovery of the presence of the customer in the State for 30 or more consecutive days or the change in the customer's residence;

"(B) the transaction is effected—

"(i) on behalf of a customer that, for 30 days prior to the day of the transaction, maintains an account with the broker or dealer; and

"(ii) within the period beginning on the date on which such associated person files with the State in which the transaction is effected an application for registration and ending on the earlier of (I) 60 days after the date the application is filed, or (II) the time at which such State notifies the associated person that it has denied the application for registration or has stayed the pendency of the application for cause; or

"(C) the transaction is one of 10 or fewer transactions in a calendar year (excluding any transactions described in subparagraph (A) or (B)) which the associated person effects in the States in which the associated person is not registered.

"(4) ALTERNATE ASSOCIATED PERSONS.—For purposes of paragraph (3)(A)(ii), each of up to 3 associated persons who are designated to effect transactions during the absence or unavailability of the principal associated person for a customer may be treated as an associated person to which such customer is assigned for purposes of such paragraph.".

(2) STUDY.—Within 6 months after the date of enactment of this Act, the Commission, after consultation with registered securities associations, national securities exchanges, and States, shall conduct a study of—

(A) the impact of disparate State licensing requirements on associated persons of registered brokers or dealers; and

(B) methods for States to attain uniform licensing requirements for such persons.

(3) REPORT.—Within one year after the date of enactment of this Act, the Commission shall submit to the Congress a report on the study conducted under paragraph (2). Such report shall include recommendations concerning appropriate methods described in paragraph (2)(B), including any necessary legislative changes to implement such recommendations.

(4) TECHNICAL AMENDMENT.—Section 28(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78bb(a)) is amended by striking "Nothing" and inserting "Except as otherwise specifically provided elsewhere in this title, nothing".

SEC. 103. MARGIN REQUIREMENTS.

(a) MARGIN REQUIREMENTS.—

(1) EXTENSIONS OF CREDIT BY BROKER-DEALERS.—Section 7(c) of the Securities Exchange Act of 1934 (15 U.S.C. 78g(c)) is amended to read as follows:

"(c) UNLAWFUL CREDIT EXTENSION TO CUSTOMERS.—

"(1) PROHIBITION.—It shall be unlawful for any member of a national securities exchange or any broker or dealer, directly or indirectly, to extend or maintain credit or arrange for the extension or maintenance of credit to or for any customer—

"(A) on any security (other than an exempted security), in contravention of the rules and regulations which the Board of Governors of the Federal Reserve System shall prescribe under subsections (a) and (b) of this section;

"(B) without collateral or on any collateral other than securities, except in accordance with such rules and regulations as the Board of Governors of the Federal Reserve System may prescribe—

"(i) to permit under specified conditions and for a limited period any such member, broker, or dealer to maintain a credit initially extended in conformity with the rules and regulations of the Board of governors of the Federal Reserve System; and

"(ii) to permit the extension or maintenance of credit in cases where the extension or maintenance of credit is not for the purpose of purchasing or carrying securities or of evading or circumventing the provisions of subparagraph (A) of this paragraph.

"(2) EXCEPTION.—This subsection and the rules and regulations thereunder shall not apply to any credit extended, maintained, or arranged by a member of a national securities exchange or a broker or dealer to or for a member of a national securities exchange or a registered broker or dealer—

"(A) a substantial portion of whose business consists of transactions with persons other than brokers or dealers; or

"(B) to finance its activities as a market maker or an underwriter;

except that the Board of Governors of the Federal Reserve System may impose such rules and regulations, in whole or in part, on any credit otherwise exempted by this paragraph if it determines that such action is necessary or appropriate in the public interest or for the protection of investors.".

(2) EXTENSIONS OF CREDIT BY OTHER LENDERS.—Section 7(d) of the Securities Exchange Act of 1934 (78 U.S.C. 78g(d)) is amended to read as follows:

"(d) UNLAWFUL CREDIT EXTENSION IN VIOLATION OF RULES AND REGULATIONS; EXCEPTION TO APPLICATION OF RULES, ETC.—

"(1) PROHIBITION.—It shall be unlawful for any person not subject to subsection (c) of this section to extend or maintain credit or to arrange for the extension or maintenance of credit for the purpose of purchasing or carrying any security, in contravention of such rules and regulations as the Board of Governors of the Federal Reserve System shall prescribe to prevent the excessive use of credit for the purchasing or carrying of or trading in securities in circumvention of the other provisions of this section. Such rules and regulations may impose upon all loans made for the purpose of purchasing or carrying securities limitations similar to those imposed upon members, brokers, or dealers by subsection (c) of this section and the rules and regulations thereunder.

"(2) EXCEPTIONS.—This subsection and the rules and regulations thereunder shall not apply to any credit extended, maintained, or arranged—

"(A) by a person not in the ordinary course of business;

"(B) on an exempted security;

"(C) to or for a member of a national securities exchange or a registered broker or dealer—

"(i) a substantial portion of whose business consists of transactions with persons other than brokers or dealers; or

"(ii) to finance its activities as a market maker or an underwriter;

"(D) by a bank on a security other than an equity security; or

"(E) as the Board of Governors of the Federal Reserve System shall, by such rules, regulations, or orders as it may deem necessary or appropriate in the public interest or for the protection of investors, exempt, either unconditionally or upon specified terms and conditions or for stated periods, from the operation of this subsection and the rules and regulations thereunder;

except that the Board of Governors of the Federal Reserve System may impose such rules and regulations, in whole or in part, on any credit otherwise exempted by subparagraph (C) of this paragraph if it determines that such action is necessary or appropriate in the public interest or for the protection of investors.".

(b) BORROWING BY MEMBERS, BROKERS, AND DEALERS.—Section 8 of the Securities Exchange Act of 1934 (15 U.S.C. 78h) is amended—

(1) by striking subsection (a), and

(2) by redesignating subsections (b) and (c) as subsections (a) and (b), respectively.

SEC. 104. PROSPECTUS DELIVERY.

(a) REPORT ON ELECTRONIC DELIVERY.—Within six months after the date of enactment of this Act, the Commission shall report to Congress on the steps the Commission has taken, or anticipates taking, to facilitate the electronic delivery of prospectuses to institutional and other investors.

(b) REPORT ON ADVISORY COMMITTEE RECOMMENDATIONS.—Within one year after the date of enactment of this Act, the Commission shall report to Congress on the Commission's views on the recommendations of the Advisory Committee on Capital Formation, including any actions taken to implement the recommendations of the Advisory Committee.

SEC. 105. EXEMPTIVE AUTHORITY.

(a) GENERAL EXEMPTIVE AUTHORITY UNDER THE SECURITIES ACT OF 1933.—Title I of the Securities Act of 1933 (15 U.S.C. 77a et seq.) is amended by adding at the end the following new section:

"SEC. 28. GENERAL EXEMPTIVE AUTHORITY.

"The Commission, by rules and regulations, may conditionally or unconditionally exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of this title or of any rule or regulation thereunder, to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors.".

(b) GENERAL EXEMPTIVE AUTHORITY UNDER THE SECURITIES EXCHANGE ACT OF 1934.—Title I of the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended by adding at the end the following new section:

"SEC. 36. GENERAL EXEMPTIVE AUTHORITY.

"Notwithstanding any other provision of this title, the Commission, by rule, regulation, or order, may conditionally or unconditionally exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of this title or of any rule or regulation thereunder, to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors. The Commission shall by rules and regulations determine the procedures under which an exemptive order under this section shall be granted and may, in its sole discretion, decline to entertain any application for an order of exemption under this section.".

SEC. 106. PROMOTION OF EFFICIENCY, COMPETITION, AND CAPITAL FORMATION.

(a) SECURITIES ACT OF 1933.—Section 2 of the Securities Act of 1933 (15 U.S.C. 77b) is amended—

(1) by inserting "(a) DEFINITIONS.—" after "SEC. 2."; and

(2) by adding at the end the following new subsection:

"(b) CONSIDERATION OF PROMOTION OF EFFICIENCY, COMPETITION, AND CAPITAL FORMATION.—Whenever pursuant to this title the Commission is engaged in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.".

(b) SECURITIES EXCHANGE ACT of 1934.—Section 3 of the Securities Exchange Act of 1934 (15 U.S.C. 78c) is amended by adding at the end the following new subsection:

"(f) CONSIDERATION OF PROMOTION OF EFFICIENCY, COMPETITION, AND CAPITAL FORMATION.—Whenever pursuant to this title the Commission is engaged in rulemaking, or in the review of a rule of a self-regulatory organization, and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.".

(c) INVESTMENT COMPANY ACT of 1940.—Section 2 of the Investment Company Act of 1940 (15 U.S.C. 80a–2) is amended by adding at the end the following new subsection:

"(c) CONSIDERATION OF PROMOTION OF EFFICIENCY, COMPETITION, AND CAPITAL FORMATION.—Whenever pursuant to this title the Commission is engaged in rulemaking and is required to consider or determine whether an action is consistent with the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.".

SEC. 107. PRIVATIZATION OF EDGAR.

(a) EXAMINATION.—The Securities and Exchange Commission shall examine proposals for the privatization of the EDGAR system. Such examination shall promote competition in the automation and rapid collection and dissemination of information required to be disclosed. Such examination shall include proposals that maintain free public access to data filings in the EDGAR system.

(b) REVIEW AND REPORT.—Within 180 days after the date of enactment of this Act, the Commission shall submit to the Congress a report on the examination under subsection (a). Such report shall include such recommendations for such legislative action as may be necessary to implement the proposal that the Commission determines most effectively achieves the objectives described in subsection (a).

SEC. 108. COORDINATION OF EXAMINING AUTHORITIES.

(a) AMENDMENTS.—Section 17 of the Securities Exchange Act of 1934 (15 U.S.C. 78q) is amended by adding at the end the following new subsection:

"(i) COORDINATION OF EXAMINING AUTHORITIES.—

"(1) ELIMINATION OF DUPLICATION.—The Commission and the examining authorities, through cooperation and coordination of examination and oversight as required by this subsection, shall eliminate any unnecessary and burdensome duplication in the examination process.

"(2) PLANNING CONFERENCES.—

"(A) The Commission and the examining authorities shall meet at least annually for a national general planning conference to discuss coordination of examination schedules and priorities and other areas of interest relevant to examination coordination and cooperation.

"(B) Within each geographic region designated by the Commission, the Commission and the relevant examining authorities shall meet at least annually for a regional planning conference to discuss examination schedules and priorities and other areas of related interest, and to encourage information-sharing and to avoid unnecessary duplication of examinations.

"(3) COORDINATION TRACKING SYSTEM FOR BROKER-DEALER EXAMINATIONS.—

"(A) The Commission and the examining authorities shall prepare, on a periodic basis in a uniform computerized format, information on registered broker and dealer examinations and shall submit such information to the Commission.

"(B) The Commission shall maintain a computerized database of consolidated examination information to be used for examination planning and scheduling and for monitoring coordination of registered broker and dealer examinations under this section.

"(4) COORDINATION OF EXAMINATIONS.—

"(A) The examining authorities shall share among themselves such information, including reports of examinations, customer complaint information, and other non-public regulatory information, as appropriate to foster a coordinated approach to regulatory oversight of registered brokers and dealers subject to examination by more than one examining authority.

"(B) To the extent practicable, the examining authorities shall assure that each registered broker and dealer subject to examination by more than one examining authority that requests a coordinated examination shall have all requested aspects of the examination conducted simultaneously and without duplication of the areas covered. The examining authorities shall also prepare an advance schedule of all such coordinated examinations.

"(5) PROHIBITED NON-COORDINATED EXAMINATIONS.—Any examining authority that does not participate in a coordinated examination pursuant to paragraph (4) of this subsection shall not conduct a routine examination other than a coordinated examination of that broker or dealer within 9 months of the conclusion of a scheduled coordinated examination.

"(6) EXAMINATIONS FOR CAUSE.—At any time, any examining authority may conduct an examination for cause of any broker or dealer subject to its jurisdiction.

"(7) BROKER-DEALER EXAMINATION EVALUATION PANEL.—The Commission shall establish an examination evaluation panel composed of representatives of registered brokers and dealers that are members of more than one self-regulatory organization that conducts routine examinations. Prior to each national general planning conference required by paragraph (2)(A) of this subsection, the Commission shall convene the examination evaluation panel to review consolidated and statistical information on the coordination of examinations and information on examinations that are not coordinated, including the findings of Commission examiners on the effectiveness of the examining authorities in achieving coordinated examinations. The Commission shall present any findings and recommendations of the examination evaluation panel to the next meeting of the national general planning conference, and shall report back to the examination evaluation panel on the actions taken by the examining authorities regarding those findings and recommendations. The examination evaluation panel shall not be subject to the Federal Advisory Committee Act (5 U.S.C. App.).

"(8) REPORT TO CONGRESS.—Within one year after the date of enactment of this Act, the Commission shall report to the Congress on the progress it and the examining authorities have made in reducing duplication and improving coordination in registered broker and dealer examinations, and on the activities of the examination evaluation panel. Such report shall also indicate whether the Commission has identified additional redundancies that have failed to be addressed in the coordination of examining authorities, or any recommendations of the examination evaluation panel established under paragraph (7) of this subsection that have not been addressed by the examining authorities or the Commission.".

(b) DEFINITION.—Section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78e) is amended by adding at the end the following paragraph:

"(54) The term 'examining authority' means any self-regulatory organization registered with the Commission under this title (other than registered clearing agencies) with the authority to examine, inspect, and otherwise oversee the activities of a registered broker or dealer.".

SEC. 109. FOREIGN PRESS CONFERENCES.

No later than one year after the date of enactment of this Act, the Commission shall adopt rules under the Securities Act of 1933 concerning the status under the registration provisions of the Securities Act of 1933 of foreign press conferences and foreign press releases by persons engaged in the offer and sale of securities.

SEC. 110. REPORT ON TRUST INDENTURE ACT OF 1939.

Within 6 months after the date of enactment of this Act, the Securities and Exchange Commission shall submit to the Congress a report on the benefits of, the continuing need for, and, if necessary, options for the modification or elimination of, the Trust Indenture Act of 1939 (15 U.S.C. 77aaa et seq.).

TITLE II—INVESTMENT COMPANY ACT AMENDMENTS

SEC. 201. SHORT TITLE.

This title may be cited as the "Investment Company Act Amendments of 1996".

SEC. 202. FUNDS OF FUNDS.

Section 12(d)(1) of the Investment Company Act of 1940 (15 U.S.C. 80a–12(d)(1)) is amended—

(1) in subparagraph (E)(iii)—

(A) by striking "in the event such investment company is not a registered investment company,"; and

(B) by inserting "in the event such investment company is not a registered investment company" after "(bb)";

(2) by redesignating existing subparagraphs (G) and (H) as subparagraphs (H) and (I), respectively;

(3) by inserting after subparagraph (F) the following new subparagraph:

"(G) The provisions of this paragraph (1) shall not apply to securities of a registered open-end company (the 'acquired company') purchased or otherwise acquired by a registered open-end company (the 'acquiring company') if—

"(i) the acquired company and the acquiring company are part of the same group of investment companies;

"(ii) the securities of the acquired company, securities of other registered open-end companies that are part of the same group of investment companies, Government securities, and short-term paper are the only investments held by the acquiring company;

"(iii)(I) the acquiring company does not pay and is not assessed any charges or fees for distribution-related activities with respect to securities of the acquired company unless the acquiring company does not charge a sales load or other fees or charges for distribution-related activities; or

"(II) any sales loads and other distribution-related fees charged with respect to securities of the acquiring company, when aggregated with any sales load and distribution-related fees paid by the acquiring company with respect to securities of the acquired company, are not excessive under rules adopted pursuant to either section 22(b) or section 22(c) of this title by a securities association registered under section 15A of the Securities Exchange Act of 1934 or the Commission;

"(iv) the acquired company shall have a fundamental policy that prohibits it from acquiring any securities of registered open-end companies in reliance on this subparagraph or subparagraph (F) of this subsection; and

"(v) such acquisition is not in contravention of such rules and regulations as the Commission may from time to time prescribe with respect to acquisitions in accordance with this subparagraph as necessary and appropriate for the protection of investors.

For purposes of this subparagraph, a 'group of investment companies' shall mean any two or more registered investment companies that hold themselves out to investors as related companies for purposes of investment and investor services."; and

(4) adding at the end the following new subparagraph:

"(J) The Commission, by rules and regulations upon its own motion or by order upon application, may conditionally or unconditionally exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions from any provisions of this subsection, if and to the extent such exemption is consistent with the public interest and the protection of investors.".

SEC. 203. REGISTRATION OF SECURITIES.

(a) AMENDMENTS TO REGISTRATION STATEMENTS.—Section 24(e) of the Investment Company Act of 1940 (15 U.S.C. 80a–24(e)) is amended—

(1) by striking paragraphs (1) and (2);

(2) by redesignating paragraph (3) as subsection (e); and

(3) in subsection (e) (as so redesignated) by striking "pursuant to this subsection or otherwise".

(b) REGISTRATION OF INDEFINITE AMOUNT OF SECURITIES.—Section 24(f) of the Investment Company Act of 1940 (15 U.S.C. 80a–24(f)) is amended to read as follows:

"(f) REGISTRATION OF INDEFINITE AMOUNT OF SECURITIES.—

"(1) INDEFINITE REGISTRATION OF SECURITIES.—Upon the effectiveness of its registration statement under the Securities Act of 1933, a face-amount certificate company, open-end management company, or unit investment trust shall be deemed to have registered an indefinite amount of securities.

"(2) PAYMENT OF REGISTRATION FEES.—Within 90 days after the end of the company's fiscal year, the company shall pay a registration fee to the Commission, calculated in the manner specified in section 6(b) of the Securities Act of 1933, based on the aggregate sales price for which its securities (including, for this purpose, all securities issued pursuant to a dividend reinvestment plan) were sold pursuant to a registration of an indefinite amount of securities under this subsection during the company's previous fiscal year reduced by—

"(A) the aggregate redemption or repurchase price of the securities of the company during that year, and

"(B) the aggregate redemption or repurchase price of the securities of the company during any prior fiscal year ending not more than 1 year before the date of enactment of the Investment Company Act Amendments of 1996 that were not used previously by the company to reduce fees payable under this section.

"(3) INTEREST DUE ON LATE PAYMENT.—A company paying the fee or any portion thereof more than 90 days after the end of the company's fiscal year shall pay to the Commission interest on unpaid amounts, compounded daily, at the underpayment rate established by the Secretary of the Treasury pursuant to section 3717(a) of title 31, United States Code. The payment of interest pursuant to the requirement of this paragraph shall not preclude the Commission from bringing an action to enforce the requirements of paragraph (2) of this subsection.

"(4) RULEMAKING AUTHORITY.—The Commission may adopt rules and regulations to implement the provisions of this subsection.".

(c) EFFECTIVE DATE.—The amendments made by this section shall be effective 6 months after the date of enactment of this Act or on such earlier date as the Commission may specify by rule.

SEC. 204. INVESTMENT COMPANY ADVERTISING PROSPECTUS.

Section 24 of the Investment Company Act of 1940 (15 U.S.C. 80a–24) is amended by adding at the end the following new subsection:

"(g) In addition to the prospectuses permitted or required in section 10 of the Securities Act of 1933, the Commission shall permit, by rules or regulations deemed necessary or appropriate in the public interest or for the protection of investors, the use of a prospectus for the purposes of section 5(b)(1) of such Act with respect to securities issued by a registered investment company. Such a prospectus, which may include information the substance of which is not included in the prospectus specified in section 10(a) of the Securities Act of 1933, shall be deemed to be permitted by section 10(b) of such Act.''.

SEC. 205. VARIABLE INSURANCE CONTRACTS.

(a) UNIT INVESTMENT TRUST TREATMENT.—Section 26 of the Investment Company Act of 1940 (15 U.S.C. 80a–26) is amended by adding at the end the following new subsection:

''(e)(1) Subsection (a) shall not apply to any registered separate account funding variable insurance contracts, or to the sponsoring insurance company and principal underwriter of such account.

''(2) It shall be unlawful for any registered separate account funding variable insurance contracts, or for the sponsoring insurance company of such account, to sell any such contract, unless—

''(A) the fees and charges deducted under the contract in the aggregate are reasonable in relation to the services rendered, the expenses expected to be incurred, and the risks assumed by the insurance company, and the insurance company so represents in the registration statement for the contract; and

''(B) the insurance company (i) complies with all other applicable provisions of this section as if it were a trustee or custodian of the registered separate account; (ii) files with the insurance regulatory authority of a State an annual statement of its financial condition, which most recent statement indicates that it has a combined capital and surplus, if a stock company, or an unassigned surplus, if a mutual company, of not less than $1,000,000, or such other amount as the Commission may from time to time prescribe by rule as necessary or appropriate in the public interest or for the protection of investors; and (iii) together with its registered separate accounts, is supervised and examined periodically by the insurance authority of such State.

''(3) The Commission may adopt such rules and regulations under paragraph (2)(A) as it determines are necessary or appropriate in the public interest or for the protection of investors. For the purposes of such paragraph, the fees and charges deducted under the contract shall include all fees and charges imposed for any purpose and in any manner.''.

(b) PERIODIC PAYMENT PLAN TREATMENT.—Section 27 of such Act (15 U.S.C. 80a–27) is amended by adding at the end the following new subsection:

''(i)(1) This section shall not apply to any registered separate account funding variable insurance contracts, or to the sponsoring insurance company and principal underwriter of such account, except as provided in paragraph (2).

''(2) It shall be unlawful for any registered separate account funding variable insurance contracts, or for the sponsoring insurance company of such account, to sell any such contract unless (A) such contract is a redeemable security, and (B) the insurance company complies with section 26(e) and any rules or regulations adopted by the Commission thereunder.''.

SEC. 206. REPORTS TO THE COMMISSION AND SHAREHOLDERS.

Section 30 of the Investment Company Act of 1940 (15 U.S.C. 80a–29) is amended—

(1) by striking paragraph (1) of subsection (b) and inserting the following:

''(1) such information, documents, and reports (other than financial statements), as the Commission may require to keep reasonably current the information and documents contained in the registration statement of such company filed under this title; and'';

(2) by redesignating subsections (c), (d), (e), and (f) as subsections (d), (e), (g), and (h), respectively;

(3) by inserting after subsection (b) the following new subsection:

''(c) In exercising its authority under subsection (b)(1) to require the filing of information, documents, and reports on a basis more frequently than semi-annually, the Commission shall take such steps as it deems necessary or appropriate, consistent with the public interest and the protection of investors, to avoid unnecessary reporting by, and minimize the compliance burdens on, registered investment companies and their affiliated persons. Such steps shall include considering and requesting public comment on—

''(1) feasible alternatives that minimize the reporting burdens on registered investment companies; and

''(2) the utility of such information, documents, and reports to the Commission in relation to the costs to registered investment companies and their affiliated persons of providing such information, documents, and reports.'';

(4) by inserting after subsection (e) (as redesignated by paragraph (2) of this section) the following new subsection:

"(f) The Commission may by rule require that semi-annual reports containing the information set forth in subsection (e) include such other information as the Commission deems necessary or appropriate in the public interest or for the protection of investors. In exercising its authority under this subsection, the Commission shall take such steps as it deems necessary or appropriate, consistent with the public interest and the protection of investors, to avoid unnecessary reporting by, and minimize the compliance burdens on, registered investment companies and their affiliated persons. Such steps shall include considering and requesting public comment on—

"(1) feasible alternatives that minimize the reporting burdens on registered investment companies; and

"(2) the utility of such information to shareholders in relation to the costs to registered investment companies and their affiliated persons of providing such information to shareholders."; and

(5) in subsection (g) (as so redesignated) by striking "subsections (a) and (d)" and inserting "subsections (a) and (e)".

SEC. 207. BOOKS, RECORDS AND INSPECTIONS.

Section 31 of the Investment Company Act of 1940 (15 U.S.C. 80a–30) is amended—

(1) by striking subsections (a) and (b) and inserting the following:

"(a) Every registered investment company, and every underwriter, broker, dealer, or investment adviser that is a majority-owned subsidiary of such a company, shall maintain and preserve such records (as defined in section 3(a)(37) of the Securities Exchange Act of 1934) for such period or periods as the Commission, by rules and regulations, may prescribe as necessary or appropriate in the public interest or for the protection of investors. Every investment adviser not a majority-owned subsidiary of, and every depositor of any registered investment company, and every principal underwriter for any registered investment company other than a closed-end company, shall maintain and preserve for such period or periods as the Commission shall prescribe by rules and regulations, such records as are necessary or appropriate to record such person's transactions with such registered company. In exercising its authority under this subsection, the Commission shall take such steps as it deems necessary or appropriate, consistent with the public interest and for the protection of investors, to avoid unnecessary recordkeeping by, and minimize the compliance burden on, persons required to maintain records under this subsection (hereinafter in this section referred to as 'subject persons'). Such steps shall include considering, and requesting public comment on—

"(1) feasible alternatives that minimize the recordkeeping burdens on subject persons;

"(2) the necessity of such records in view of the public benefits derived from the independent scrutiny of such records through Commission examination;

"(3) the costs associated with maintaining the information that would be required to be reflected in such records; and

"(4) the effects that a proposed recordkeeping requirement would have on internal compliance policies and procedures.

"(b) All records required to be maintained and preserved in accordance with subsection (a) of this section shall be subject at any time and from time to time to such reasonable periodic, special, and other examinations by the Commission, or any member or representative thereof, as the Commission may prescribe. For purposes of such examinations, any subject person shall make available to the Commission or its representatives any copies or extracts from such records as may be prepared without undue effort, expense, or delay as the Commission or its representatives may reasonably request. The Commission shall exercise its authority under this subsection with due regard for the benefits of internal compliance policies and procedures and the effective implementation and operation thereof.";

(2) by redesignating existing subsections (c) and (d) as subsections (e) and (f), respectively; and

(3) by inserting after subsection (b) the following new subsections:

"(c) Notwithstanding any other provision of law, the Commission shall not be compelled to disclose any internal compliance or audit records, or information contained therein, provided to the Commission under this section. Nothing in this subsection shall authorize the Commission to withhold information from Congress or prevent the Commission from complying with a request for information from any other Federal department or agency requesting the information for purposes within the scope of its jurisdiction, or complying with an order of a court of the United States in an action brought by the United States or the Commission. For purposes of section 552 of title 5, United States Code, this section shall be considered a statute described in subsection (b)(3)(B) of such section 552.

"(d) For purposes of this section—

"(1) 'internal compliance policies and procedures' means policies and procedures designed by subject persons to promote compliance with the Federal securities laws; and

"(2) 'internal compliance and audit record' means any record prepared by a subject person in accordance with internal compliance policies and procedures.".

SEC. 208. INVESTMENT COMPANY NAMES.

Section 35(d) of the Investment Company Act of 1940 (15 U.S.C. 80a–34(d)) is amended to read as follows:

"(d) It shall be unlawful for any registered investment company to adopt as a part of the name or title of such company, or of any securities of which it is the issuer, any word or words that the Commission finds are materially deceptive or misleading. The Commission is authorized, by rule, regulation, or order, to define such names or titles as are materially deceptive or misleading.".

SEC. 209. EXCEPTIONS FROM DEFINITION OF INVESTMENT COMPANY.

(a) AMENDMENTS.—Section 3(c) of the Investment Company Act of 1940 (15 U.S.C. 80a–3(c)) is amended—

(1) in paragraph (1), by inserting after the first sentence the following new sentence: "Such issuer nonetheless is deemed to be an investment company for purposes of the limitations set forth in section 12(d)(1)(A)(i) and (B)(i) governing the purchase or other acquisition by such issuer of any security issued by any registered investment company and the sale of any security issued by any registered open-end company to any such issuer.";

(2) in subparagraph (A) of paragraph (1)—

(A) by inserting after "issuer," the first place it appears the following: "and is or, but for the exception in this paragraph or paragraph (7), would be an investment company,"; and

(B) by striking all that follows "(other than short-term paper)" and inserting a period;

(3) in paragraph (2)—

(A) by striking "and acting as broker," and inserting "acting as broker, and acting as market intermediary,"; and

(B) by adding at the end of such paragraph the following new sentences: "For the purposes of this paragraph, the term 'market intermediary' means any person that regularly holds itself out as being willing contemporaneously to engage in, and is regularly engaged in the business of entering into, transactions on both sides of the market for a financial contract or one or more such financial contracts. For purposes of the preceding sentence, the term 'financial contract' means any arrangement that (A) takes the form of an individually negotiated contract, agreement, or option to buy, sell, lend, swap, or repurchase, or other similar individually negotiated transaction commonly entered into by participants in the financial markets; (B) is in respect of securities, commodities, currencies, interest or other rates, other measures of value, or any other financial or economic interest similar in purpose or function to any of the foregoing; and (C) is entered into in response to a request from a counterparty for a quotation or is otherwise entered into and structured to accommodate the objectives of the counterparty to such arrangement."; and

(4) by striking paragraph (7) and inserting the following:

"(7)(A) Any issuer (i) whose outstanding securities are owned exclusively by persons who, at the time of acquisition of such securities, are qualified purchasers, and (ii) who is not making and does not presently propose to make a public offering of such securities. Securities that are owned by persons who received the securities from a qualified purchaser as a gift or bequest, or where the transfer was caused by legal separation, divorce, death, or other involuntary event, shall be deemed to be owned by a qualified purchaser, subject to such rules, regulations, and orders as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

"(B) Notwithstanding subparagraph (A), an issuer is within the exception provided by this paragraph if—

"(i) in addition to qualified purchasers, its outstanding securities are beneficially owned by not more than 100 persons who are not qualified purchasers if (I) such persons acquired such securities on or before December

31, 1995, and (II) at the time such securities were acquired by such persons, the issuer was excepted by paragraph (1) of this subsection; and

"(ii) prior to availing itself of the exception provided by this paragraph—

"(I) such issuer has disclosed to such persons that future investors will be limited to qualified purchasers, and that ownership in such issuer is no longer limited to not more than 100 persons, and

"(II) concurrently with or after such disclosure, such issuer has provided such persons with a reasonable opportunity to redeem any part or all of their interests in the issuer for their proportionate share of the issuer's current net assets, or the cash equivalent thereof.

"(C) An issuer that is excepted under this paragraph shall nonetheless be deemed to be an investment company for purposes of the limitations set forth in section 12(d)(1)(A)(i) and (B)(i) governing the purchase or other acquisition by such issuer of any security issued by any registered investment company and the sale of any security issued by any registered open-end company to any such issuer.

"(D) For purposes of determining compliance with this paragraph and paragraph (1) of this subsection, an issuer that is otherwise excepted under this paragraph and an issuer that is otherwise excepted under paragraph (1) shall not be treated by the Commission as being a single issuer for purposes of determining whether the outstanding securities of the issuer excepted under paragraph (1) are beneficially owned by not more than 100 persons or whether the outstanding securities of the issuer excepted under this paragraph are owned by persons that are not qualified purchasers. Nothing in this provision shall be deemed to establish that a person is a bona fide qualified purchaser for purposes of this paragraph or a bona fide beneficial owner for purposes of paragraph (1) of this subsection.".

(b) DEFINITION OF QUALIFIED PURCHASER.—Section 2(a) of the Investment Company Act of 1940 (15 U.S.C. 80a–2(a)) is amended by inserting after paragraph (50) the following new paragraph:

"(51) 'Qualified purchaser' means—

"(A) any natural person who owns at least $10,000,000 in securities of issuers that are not controlled by such person, except that securities of such a controlled issuer may be counted toward such amount if such issuer is, or but for the exception in paragraph (1) or (7) of section 3(c) would be, an investment company;

"(B) any trust not formed for the specific purpose of acquiring the securities offered, as to which the trustee or other person authorized to make decisions with respect to the trust, and each settlor or other person who has contributed assets to the trust, is a person described in subparagraph (A) or (C); or

"(C) any person, acting for its own account or the accounts of other qualified purchasers, who in the aggregate owns and invests on a discretionary basis, not less than $100,000,000 in securities of issuers that are not affiliated persons (as defined in paragraph (3)(C) of this subsection) of such person, except that securities of such an affiliated person issuer may be counted toward such amount if such issuer is, or but for the exception in paragraph (1) or (7) of section 3(c) would be, an investment company.

The Commission may adopt such rules and regulations governing the persons and trusts specified in subparagraphs (A), (B), and (C) of this paragraph as it determines are necessary or appropriate in the public interest and for the protection of investors.".

(c) CONFORMING AMENDMENT.—The last sentence of section 3(a) of the Investment Company Act of 1940 (15 U.S.C. 80a–3(a)) is amended—

(1) by inserting "(i)" after "of the owner"; and

(2) by inserting before the period the following: ", and (ii) which are not relying on the exception from the definition of investment company in subsection (c)(1) or (c)(7) of this section".

(d) RULEMAKING REQUIRED.—

(1) IMPLEMENTATION OF SECTION 3(C)(1)(B).—Within one year after the date of enactment of this Act, the Commission shall prescribe rules to implement the requirements of section 3(c)(1)(B) of the Investment Company Act of 1940 (15 U.S.C. 80a–3(c)(1)(B)).

(2) EMPLOYEE EXCEPTION.—Within one year after the date of enactment of this Act, the Commission shall prescribe rules pursuant to its authority under section 6 of the Investment Company Act of 1940 (15 U.S.C. 80a–6) to permit the ownership by knowledgeable employees of an issuer or an affiliated person of the issuer of the securities of that issuer or affiliated person without loss of

the issuer's exception under section 3(c)(1) or 3(c)(7) of such Act from treatment as an investment company under such Act.

PURPOSE AND SUMMARY

The purpose of this legislation is to modernize and rationalize certain important aspects of the regulatory scheme governing our capital markets, including the respective responsibilities of Federal and State governmental authorities over the securities markets. The legislation seeks to further advance the development of national securities markets and eliminate the costs and burdens of duplicative and unnecessary regulation by, as a general rule, designating the Federal government as the exclusive regulator of national offerings of securities. State governments generally retain authority to regulate small, regional, or intrastate securities offerings, and to bring actions pursuant to State laws and regulations prohibiting fraud and deceit, including broker-dealer sales practices abuses.

The legislation also seeks to promote efficiency, competition, and capital formation in the capital markets without compromising investor protection by repealing anti-competitive restrictions on entities from whom brokers may borrow; requiring the consideration of efficiency, competition, and capital formation whenever the Securities and Exchange Commission (Commission) makes a public interest determination in its rulemaking; providing for streamlining and coordinating of examinations of broker-dealers by self-regulatory organizations; significantly reducing regulatory burdens on the mutual fund industry; simplifying and reducing ineffective and anti-competitive restrictions imposed by the Investment Company Act; and establishing a new exception from the Investment Company Act for private investment pools (such as hedge funds, as well as venture capital firms raising capital for new and growing businesses) that will eliminate certain regulatory impediments on these investment pools by permitting interests in these pools to be sold to an unlimited number of qualified purchasers.

BACKGROUND AND NEED FOR LEGISLATION

The Subcommittee on Telecommunications and Finance held a series of hearings in 1995 to examine the need for legislation modernizing and rationalizing our scheme of securities regulation. Several themes recurred throughout the testimony of the majority of witnesses. One was the need to rethink the system of dual Federal and State securities regulation. Testimony demonstrated a clear need for modernization and indicated that, notwithstanding past reform efforts, there continues to be a substantial degree of duplication between Federal and State securities regulation, and that this duplication tends to raise the cost of capital to American issuers of securities without providing commensurate protection to investors or our markets. Testimony also indicated that technological change has transformed the capital raising process, necessitating changes in the regulatory scheme to facilitate the flow of information to potential investors and reduce the marginal cost of capital to firms.

The explosive growth of the investment company industry dramatically illustrates the transformation that our nation's capital raising process has undergone in recent years. In the 56 years since the Investment Company Act became law, the mutual fund industry has grown from 68 funds with assets of about $400 million to over 5,500 funds with over $3 trillion in assets. Americans are relying on mutual fund investments with increasing frequency for purposes of investing and saving for retirement, college education, and other fundamental financial needs. Today, nearly one in every three American households owns mutual fund shares.

The Investment Company Act has not, however, undergone significant change in response to the developments in the industry; the Act has been amended significantly only once, in 1970. Accordingly, certain of the Act's provisions have become outdated and unduly burdensome, imposing unnecessary costs on funds and impeding innovation in the industry. The costs borne by the industry are passed on to shareholders in the form of lower returns on their investments and reduced flexibility in investment options.

The Securities Amendments of 1996 eliminate many of these burdens and enhance innovation and efficiency for investment companies. The legislation facilitates the creation of funds of funds, which can be simple and economical asset allocation devices for investors. The legislation simplifies and streamlines the registration process that investment companies must undertake to sell their shares continuously. This change in the registration process eliminates the risk under current law that can cause investment companies to pay inordinately large penalties for a technical or clerical error that results in missing a filing deadline. And the legislation facilitates more flexible and useful investment company advertising by creating a new type of advertising document. Investment companies may use this new document to advertise performance data and other up-to-date information without having to limit the advertisement to information "the substance of which" is contained in the statutory prospectus.

The growth of the industry has also raised questions with respect to industry regulation that were not anticipated by the authors of the Investment Company Act. To help maintain the strong record of investor protection that has characterized the regulation of the mutual fund industry, the legislation grants the Commission specific additional authority regarding investment company books and records, and the preparation of shareholder reports. In exercising this authority, the legislation directs the Commission to take appropriate steps to avoid unnecessary reporting by, and to minimize the compliance burdens on, investment companies and to consider the effects of new recordkeeping requirements on the integrity and continued effectiveness of internal compliance programs of investment companies. The legislation also grants the Commission new authority to adopt rules that will help ensure that an investment company's name is consistent with its investment objectives and policies, rather than having to seek to have the use of such a name enjoined by a Federal court.

The legislation also clarifies and refines the regulation of variable insurance products, which are currently subject to anomalous regulatory requirements arising from the application of principles in the Investment Company Act that are not suited to these products, which did not exist at the time the Act was enacted.

The legislation also provides a new exception from the definition of "investment company" to permit investment pools that sell their securities only to "qualified purchasers" who are deemed to be sophisticated investors to sell to an unlimited number of these investors. These pools, which include not only hedge funds but also financing vehicles such as venture capital funds that provide capital directly to start-up companies or businesses, currently operate pursuant to an exception in the Investment Company Act that limits the number of investors that can invest in these pools. Although there is no exact accounting of the total number and size of these private investment partnerships, estimates indicate that the total number may be as high as 3,000, with assets estimated between $75 and $160 billion. The Committee recognizes the important role that these pools can play in facilitating capital formation for U.S. companies. The Committee expects that the legislation will significantly reduce regulatory restrictions that have affected these pools, and will remove incentives that have caused some Americans to invest in unregulated offshore markets.

During the course of the hearings on this bill, the Subcommittee on Telecommunications and Finance received written and oral testimony from witnesses representing the managed futures industry regarding the need for an explicit exception from both the Investment Company Act and the Investment Advisers Act of 1940 for commodity pools and commodity trading advisers whose business it is to trade, or give advice with respect to trading, commodity interests. Such persons are otherwise subject to regulation by an independent Federal agency, the Commodity Futures Trading Commission ("CFTC"), pursuant to a separate Federal statute, the Commodity Exchange Act, as amended ("CEA") and the regulations thereunder, and are also subject to oversight by the National Futures Association, a self-regulatory organization.

Commodity pool offering documents are subject to review by the CFTC. These documents are also subject to review by the Commission in a manner similar to offerings under the Securities Act. To some extent, this extensive regulatory system evolved in response to the volatility and risk associated with commodity pool investments. The Committee is concerned, however, that aspects of the regulations of commodity pools and commodity trading advisers under the Investment Company and Investment Advisers Acts may constitute unnecessarily burdensome regulation which does not enhance the protection of investors.

The Commission staff has recognized a distinction between commodity pools and investment companies. The Committee, however, has been informed that the relief that the Commission staff has provided from the Investment Company and Investment Advisers Acts with respect to commodity pools and commodity trading advisers has proven to be unnecessarily restrictive to these entities.

The Commission staff has represented to the Committee that it is willing to take appropriate action, pursuant to the Commission's authority under the Investment Company Act, to provide administrative relief from the provisions of that Act to issuers that are primarily engaged in the business of operating a commodity pool or investing in interests of such pools, operated by a person subject to regulation as a commodity pool operator under the CEA, and are held out as being primarily engaged in such business. The Commission staff has also represented that it is willing to consider recommending that the Commission take appropriate action pursuant to its authority under the Investment Advisers Act to provide administrative relief from the provisions of the Act to any commodity pool operator or commodity trading adviser registered as such with the CFTC pursuant to the CEA whose advice, analyses or reports concerning securities is solely related to (a) the securities issued by commodity pools that are the subject of any administrative relief by the Commission under the Investment Company Act, or (b) securities investments by such commodity pools.

The Committee expects the Commission to take appropriate action to effect the administrative relief discussed above as soon as practicable following the date of enactment of this legislation.

In addition, the Committee supports appropriate administrative action by the Commission to prevent the Investment Company Act from having unintended and adverse consequences to U.S. companies in the business of developing or acquiring and operating foreign infrastructure projects.

The Committee has been informed that some of these companies face regulatory impediments under the Investment Company Act in connection with the acquisition of minority ownership interests in the foreign subsidiaries they establish in connection with these projects. Under current law, if the minority interest constitutes an investment security for purposes of the Investment Company Act, the company holding such an interest may meet the definition of an investment company set out in section 3(a)(3) of the Investment Company Act. Because registration and regulation under the Act can be inconsistent with the intended operations of the company, such a company may determine to avoid participation in such a project in order to avoid becoming subject to the Act.

The Investment Company Act may therefore place U.S. companies at a competitive disadvantage vis-a-vis their foreign competitors, who are not subject to its requirements in developing or acquiring foreign infrastructure projects. These projects include roads, bridges, airports, schools, housing, and hospitals, among many other types of infrastructure projects. The activities of U.S. companies involved in foreign infrastructure projects are not the sort of activities the Investment Company Act was designed to regulate.

The Committee is not suggesting that exemptive relief from the Commission is necessarily required in order for investments in these projects to proceed. However, where such relief is necessary, the Committee expects the Commission to take administrative action expeditiously, either on a case-by-case basis through exemptive orders or through rule making, to exempt from regulations as investment companies U.S. companies that own substantial interests in foreign infrastructure companies and that are (directly or through affiliates) actively involved in foreign infrastructure projects. Any such exemption or rulemaking should be subject to such conditions as the Commission deems necessary and appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the Investment Company Act.

Hearings

The Subcommittee on Telecommunications and Finance held three days of hearings on H.R. 2131, the Capital Markets Deregulation and Liberalization Act of 1995, on November 14, 1995, November 30, 1995, and December 5, 1995.

Testifying before the Subcommittee on November 14, 1995, were: Dr. Charles Cox, Chief Executive Officer, Lexecon; Mr. J. Carter Beese, Jr., Chairman, Capital Markets Regulatory Reform Project, Center for Strategic and International Studies; Mr. Saul S. Cohen, Rosenman & Colin LLP; Professor John C. Coffee, Jr., Adolphe Berle Professor of Law, Columbia University; and Mr. A.A. Sommer, Jr., Morgan, Lewis & Bockius, LLP.

Testifying before the Subcommittee on November 30, 1995, were: The Honorable Arthur Levitt, Chairman, Securities and Exchange Commission; and The Honorable Alan Greenspan, Chairman, Board of Governors, Federal Reserve System.

Testifying before the Subcommittee on December 5, 1995, were: Mr. A.B. Krongard, Chairman, Securities Industry Association; Ms. Elaine LaRoche, Vice-Chair, Public Securities Association; Mr. John Gaine, General Counsel, Managed Futures Association; Mr. Matthew P. Fink, President, Investment Company Institute; Mr. R. Charles Shufeldt, representing the American Bankers Association; Mr. Stephen J. Friedman, Partner, Debevoise & Plimpton; Professor Mark A. Sargent, University of Maryland School of Law; Professor Rutherford B. Campbell, Jr., University of Kentucky College of Law; Mr. Morey W. McDaniel; Mr. Bradley D. Belt, Director of Capital Markets and Domestic Policy Issues, Center for Strategic and International Studies; Mr. Dee Harris, President, North American Securities Administrators Association; and Mr. Mark Saladino, representing the Government Finance Officers Association.

The Subcommittee on Telecommunications and Finance also held a hearing on H.R. 1495, the Investment Company Act Amendments of 1995, on October 31, 1995. Testifying before the Subcommittee on October 31, 1995, were: Mr. Barry P. Barbash, Director, Division of Investment Management, Securities and Exchange Commission; Mr. Matthew P. Fink, President, Investment Company Institute; Mr. James S. Riepe, Managing Director, T. Rowe Price Associates, Inc.; Mr. Don G. Powell, Chief Executive Officer, Van Kampen American Capital, Inc.; Ms. Marianne Smythe, Partner, Wilmer, Cutler & Pickering; and Mr. Paul G. Haaga, Director and Senior Vice President, Capital Research & Management Company.

Committee Consideration

On March 7, 1996, the Subcommittee on Telecommunications and Finance met in open markup session and approved H.R. 3005, the Securities Amendments of 1996, as amended, for Full Committee consideration, by a roll call vote of 25 yeas to 0 nays, in lieu of H.R. 2131 and H.R. 1495. On May 15, 1996, the Full Committee met in open markup session and ordered H.R. 3005 reported to the House, as amended, by a voice vote, a quorum being present.

ROLLCALL VOTES

Clause 2(l)2(B) of rule XI of the Rules of the House requires the Committee to list the recorded votes on the motion to report legislation and amendments thereto. There were no recorded votes taken in connection with ordering H.R. 3005 reported or in adopting the amendment. The voice votes taken in Committee are as follows:

COMMITTEE ON COMMERCE—104TH CONGRESS

VOICE VOTES—MAY 15, 1996

Bill: H.R. 3005, Securities Amendments of 1996.
Amendment: Amendment in the Nature of a Substitute offered by Mr. Bliley.
Disposition: Agreed to, by a voice vote.
Motion: Motion by Mr. Bliley to order H.R. 3005, as amended, reported to the House.
Disposition: Agreed to, by a voice vote.

COMMITTEE OVERSIGHT FINDINGS

Pursuant to clause 2(l)(3)(A) of rule XI of the Rules of the House of Representatives, the Committee held legislative hearings and made findings that are reflected in this report.

COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT

Pursuant to clause 2(l)(3)(D) of rule XI of the Rules of the House of Representatives, no oversight findings have been submitted to the Committee by the Committee on Government Reform and Oversight.

NEW BUDGET AUTHORITY AND TAX EXPENDITURES

In compliance with clause 2(l)(3)(B) of rule XI of the Rules of the House of Representatives, the Committee states that H.R. 3005 would result in no new or increased budget authority or tax expenditures or revenues.

COMMITTEE COST ESTIMATE

The Committee adopts as its own, with the reservation described below, the cost estimate prepared by the Director of the Congressional Budget Office (CBO) pursuant to section 403 of the Congressional Budget Act of 1974.

The Committee notes that in the Estimated Cost of Intergovernmental Mandates, the CBO states that the provision of H.R. 3005 entitled "exemption to permit service to customers" could result in a loss of revenue to States of as much as $10 million. In reaching that conclusion, the CBO assumes that under current law, registered representatives will routinely register in States in which their customers temporarily reside, if such customers seek to conduct transactions while out of their own State of residence. The Committee believes that under current law, transactions for such customers may be delayed until such customers return to their State of residence, or may be effected by the registered representative without knowledge of the location of the customer. As a result of the transactions permitted under the legislation's exemption, there will be minimal (if any) loss of revenue to States. The Committee further believes that the current volume of brokerage transactions of traveling clients is indeterminate, and thus any loss of revenue resulting from this provision is not able to be quantified with any degree of precision.

CONGRESSIONAL BUDGET OFFICE ESTIMATE

Pursuant to clause 2(l)(3)(C) of rule XI of the Rules of the House of Representatives, the following is the cost estimate provided by the Congressional Budget Office pursuant to section 403 of the Congressional Budget Act of 1974:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, June 12, 1996.

Hon. THOMAS J. BLILEY, Jr.
Chairman, Committee on Commerce, House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimates for H.R. 3005, the Securities Amendments of 1996. The estimates encompass costs to the federal government, private-sector impacts (incorporated in the federal costs estimate), and costs to state and local governments (discussed in a separate intergovernmental mandate statement). The intergovernmental mandate statement supersedes the statement we prepared on June 6, 1996, and reflects a technical and conforming change to the base text of H.R. 3005 regarding the scope of the preemption of state registration requirements.

Enactment of H.R. 3005 would affect receipts. Therefore, pay-as-you-go procedures would apply to the bill.

If you wish further details on this estimate, we will be pleased to provide them.

Sincerely,

JUNE E. O'NEILL,
Director.

CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

1. Bill number: H.R. 3005.
2. Bill title: Securities Amendments of 1996.
3. Bill status: As ordered reported by the House Committee on Commerce on May 15, 1996.
4. Bill purpose: H.R. 3005 would amend federal laws that regulate securities. The bill would streamline the securities laws and decrease the regulation of certain products offered by the capital markets.

Title I of H.R. 3005 would preempt state law with respect to the following types of capital offerings: (1) securities issued by investment companies, (2) securities listed on the New York Stock Exchange and the American Stock Exchange, or included on the National Market System of the National Association of Securities Dealers Automated Quotation System (NASDAQ), (3) off-exchange securities that meet certain threshold requirements, and (4) offers or sales of securities to "qualified purchasers" as defined by the Securities and Exchange Commission (SEC) in later rulemaking. In addition, the bill would preempt state law regarding the registration of most debt securities. The bill would preserve the ability of states to require certain filings and fees and would allow states to pursue instances of fraud.

Title I would require the SEC to study the following issues:

privatization of the Electronic Data Gathering and Retrieval (EDGAR) system;

the impact of disparate state licensing requirements on broker-dealers;

the uniformity of state securities laws not preempted by H.R. 3005;

the feasibility of transmitting prospectuses electronically; and

possible modifications to the Trust Indenture Act.

The bill also would require the SEC to promulgate a number of rules to consider the impact of such rules on the efficiency of the capital markets. Finally, Title I would exempt most broker-dealers and members of a national exchange from the margin requirements set by the Federal Reserve System, thus enabling sellers of securities to extend more credit to buyers.

Title II would amend the Investment Company Act of 1940 to establish rules governing investment companies that wish to offer mutual funds comprised of other mutual funds. In addition, the title would authorize investment companies to include data related to the performance of mutual funds in a fund's prospectus and would exempt certain types of investment companies from the securities laws. The bill also would ease the regulations on the amount of fees that insurance companies could charge to customers who buy variable annuities.

Title II would provide the SEC with more flexibility in determining which records are necessary for the agency to monitor investment companies. The SEC would be required to consider the costs and benefits of requiring additional filings and recordkeeping from the investment companies. Title II also would require the SEC to promulgate a number of rules concerning companies exempted from the Investment Company Act and suitable names for investment company products.

Current law requires investment companies to file a registration statement with the SEC before offering shares of a mutual fund to the public. At the time of registration most mutual funds register an "indefinite" number of shares and pay a $500 regulatory fee. At the end of a company's fiscal year, the firm must pay a registration fee to the SEC based upon the net number of shares sold. H.R. 3005 would simplify the calculations needed to determine the amount owed to the SEC and would extend the window during which the investment companies must pay the registration fee from 60 days to 90 days after the end of a company's fiscal year.

5. Estimated cost to the Federal Government: CBO estimates that enacting H.R. 3005 would result in a loss of revenues of about $9 million in fiscal year 1997, and new discretionary spending totaling about $1 million over fiscal years 1997 and 1998, assuming

appropriation of the necessary funds. The estimated budgetary impact of the bill is summarized in the following table.

[By fiscal year, in million of dollars]

	1996	1997	1998	1999	2000	2001	2002
SPENDING SUBJECT TO APPROPRIATIONS							
Spending under current law:							
Estimated authorization level [1]	103	103	103	103	103	103	103
Estimated outlays	102	105	103	103	103	103	103
Proposed changes:							
Estimated authorization level	....	1	([2])	....	....	....	....
Estimated outlays	....	1	([2])	....	....	....	....
Estimated spending under H.R. 3005:							
Estimated authorization level [1]	103	104	103	103	103	103	103
Estimated outlays	102	106	103	103	103	103	103
CHANGES IN REVENUES							
Registration fees: Estimated revenues	....	−9	....	....	....	....	....

[1] The 1996 level is the amount appropriated for that year. The estimated authorization levels for 1997 through 2002 reflect CBO baseline estimates for the SEC, assuming no adjustment for inflation.
[2] Less than $500,000.

The costs of this bill fall within budget function 370.

6. Basis of estimate:

Spending subject to appropriations.—Based on information from the SEC, CBO estimates that enacting H.R. 3005 would result in additional discretionary spending of about $1 million in 1997 and less than $500,000 in 1998, assuming appropriations of the necessary funds. This additional funding would be used to conduct the rulemakings and studies required by H.R. 3005. The bill also would require the SEC to consider the burden of regulations or rules on capital formation, efficiency, and competition. Because the SEC currently conducts cost-benefit analyses in conjunction with its rulemakings, CBO would not expect this provision to result in any additional costs to the federal government. Many other provisions of the bill would affect those who engage in securities; transactions but would not significantly affect spending by the SEC.

Revenues.—H.R. 3005 would extend the deadline for investment companies to file registration fees on the net value of mutual funds sold to the public from 60 days to 90 days after the end of a company's fiscal year. CBO estimates that this delay in payments to the SEC would result in a one-time reduction in governmental receipts of about $9 million in fiscal year 1997, because it would shift payments by some companies from fiscal year 1997 into 1998. Similar shifts would occur in subsequent years. Thus, while total receipts from registration fees would remain largely unchanged, there would be a budgetary effect in 1997.

Because companies filing beyond the deadline are subject to higher fees, extending the filing period also could reduce total fee collections. However, the bill would authorize the SEC to collect interest on late payments, and such interest would partially offset any reduction in the amount of delinquent fees. In addition, the bill would simplify the procedures by which registration fees are calculated; that simplification could increase fee collections through greater compliance. CBO estimates that these provisions taken together would not significantly affect the amount of fees collected by the SEC.

7. Pay-as-you-go considerations: Section 252 of the Balanced Budget and Emergency Deficit Control Act of 1985 sets up pay-as-you-go procedures for legislation affecting direct spending or receipts through 1998. CBO estimates that enactment of H.R. 3005 would affect receipts by extending the due date for certain registration fees. Therefore, pay-as-you-go procedures would apply to the bill. The following table summarizes the estimated pay-as-you-go impact of H.R. 3005.

[By fiscal year, in millions of dollars]

	1996	1997	1998
Change in outlays	[1]	[1]	[1]
Change in receipts	0	−9	0

[1] Not applicable.

8. Estimated impact on State, local, and tribal governments: The bill would impose mandates on state governments (see the attached intergovernmental mandate cost statement).

9. Estimated impact on the private sector: CBO has identified three private-sector mandates in this bill. We expect that these mandates would not impose any significant costs on the private sector. The first mandate would impose requirements on examining authorities, also referred to as self-regulating organizations (SROs), such as the National Association of Securities Dealers, the New York Stock Exchange, and the American Stock Exchange. The other two mandates would impose requirements on investment companies and certain related entities.

The bill would require that the SROs meet annually to discuss the coordination of examination schedules for brokers and dealers, to develop a computerized tracking system for these examinations, and to coordinate the examination process to eliminate duplicate and overlapping examinations. The SROs currently conduct these activities and, therefore, would not incur any additional costs.

The bill would give the SEC the authority to require investment companies to file information, documents, and reports more frequently and to include additional information in their semi-annual reports. In addition, the bill would allow the SEC to require investment companies to maintain additional record that are similar to those that the commission currently requires of investment advisers, brokers, and dealers. The SEC does not anticipate changing current filing and recordkeeping requirements as a result of these provisions. Therefore, CBO estimates that investment companies' costs would not be affected.

10. Previous CBO estimate: None.

11. Estimate prepared by: Federal cost estimate: Rachel Forward and Stephanie Weiner; Private sector impact: Jean Wooster.

12. Estimate approved by: Robert A. Sunshine for Paul N. Van de Water, Assistant Director for Budget Analysis.

CONGRESSIONAL BUDGET OFFICE ESTIMATED COST OF INTERGOVERNMENTAL MANDATES

1. Bill number: H.R. 3005.
2. Bill title: Securities Amendments of 1996.

3. Bill status: As ordered reported by the House Committee on Commerce on May 15, 1996, and including a technical and conforming change to the base text.

4. Bill purpose: H.R. 3005 would amend or repeal sections of the Securities Act of 1933, the Securities Exchange Act of 1934, and the Investment Company Act of 1940. In doing so, the bill would preempt state laws and regulations regarding certain types of securities and transactions. The legislation would preserve the ability of states to require certain filings and fees and would allow states to pursue instances of fraud. H.R. 3005 would also create a uniform exemption from state registration for securities salespersons.

The bill would require the Securities and Exchange Commission (SEC) to conduct several studies, would exempt most broker-dealers and members of a national exchange from the margin requirements set by the Federal Reserve System, and would amend certain federal restrictions on investment companies.

5. Intergovernmental mandates contained in bill: H.R. 3005 would preempt, with certain limitations, state laws, rules, and regulations that require the registration or qualification of the following securities or transactions:

securities listed or authorized for listing on the New York Stock Exchange (NYSE), the American Stock Exchange (AMEX), or included on the National Market System (NMS) of the National Association of Securities Dealers Automatic Quotation System (NASDAQ);

debt securities issued by companies that have securities listed on the above-mentioned exchanges;

securities issued by investment companies registered under the Investment Company Act of 1940;

securities issued by companies that have (or will have upon conclusion of the transaction) more than $10 million in total assets, subject to certain conditions;

offers or sales of securities to "qualified purchasers" as defined by the SEC in later rulemaking; and

certain offers or sales of securities that are already exempt from federal registration requirements.

The bill would also preempt state laws that:

prohibit, limit, or impose conditions on the offering documents, shareholder reports, or other disclosure documents related to certain kinds of securities;

prohibit, limit, or impose conditions on offers of the securities listed above based on the merits of the offer or the issuer; and

establish capital, margin, books and records, bonding, or reporting requirements for securities brokers and dealers.

Finally, H.R. 3005 would partially preempt state laws that require securities salespersons to register and pay a fee in order to conduct business in a state. Currently, most state laws contain some kind of "de minimis" exemption that allows a salesperson to conduct certain transactions in the state without registering there. The bill would create a national uniform exemption that is broader than most state laws, and would thus allow a salesperson to conduct business with pre-existing customers who are temporarily residing in states even though the salesperson is not registered there.

The exemption would also allow a salesperson to conduct a total of ten other transactions annually in those states in which the salesperson is not registered.

6. Estimated direct costs of mandates to State, local, and tribal governments: (a) *Is the $50 million threshold exceeded?* No.

(b) *Total direct costs of mandates: The Unfunded Mandates Reform Act of 1995 (Public Law 104–4) defines the direct costs of an intergovernmental mandate as "the aggregate estimated amounts that all state, local, and tribal governments would be required to spend or would be prohibited from raising in revenues in order to comply with the Federal intergovernmental mandate." CBO estimates that the mandates in this bill—particularly the preemption of state requirements for securities listed on the national exchanges and the partial preemption of state registration requirements for securities salesperson—would prohibit states from collecting fees totaling about $15 million annually that they otherwise would collect.*

(c) *Estimate of necessary budget authority:* Not applicable.

7. Basis of estimate: For the purposes of preparing this estimate, CBO contacted state securities regulators in twenty-seven states to understand how state securities laws would be affected by H.R. 3005, and to request data about states' collections from fees that would be preempted by this bill. CBO also contacted securities industry associations for information about how the industry would likely react to provisions of the bill.

Preemption of State requirements for exchange-listed securities

CBO estimates that the bill would lower state fee revenues by about $5 million annually by preempting state registration and filing requirements for securities listed or authorized for listing on the NYSE or the AMEX, or included on the NASDAQ NMS. While most states currently exempt these securities form any state requirements, CBO identified a few states that do not. We estimate that revenue losses in those states would total about $5 million annually.

Partial preemption of State registration requirements for securities salespersons

The bill would partially preempt state laws to create a uniform exemption from registration for securities salespersons. Because the exemption in the bill is broader than most of the exemptions in current state laws, the bill would likely result in fewer registrations by salespersons and thus a reduction in revenues from associated fees. States' annual registration fees for salespersons currently range from $15 to $235 per agent. CBO estimates that states collect a total of $150 million to $250 million annually from these fees. None of the states we surveyed collect data about the number of transactions that registered salespersons conduct in their states, but based on conversations with state regulators, CBO estimates that state fee collections would decrease by as much as $10 million per year. Revenue losses would be concentrated in those states that do not currently have an exemption, especially those that have a large number of seasonal residents.

State enforcement costs could increase as a result of the uniform exemption, but CBO cannot estimate the extent of the increase. A state that does not currently offer an exemption need only prove that a salesperson who is conducting business in the state does not have a license in order to take action against the salesperson. If H.R. 3005 were enacted into law, however, the state would have to prove that the transactions conducted by the salesperson were not covered by the exclusion.

Preemption of State registration requirements

The bill would preempt state laws requiring the registration or qualification of certain categories of securities and certain securities transactions. The bill provides, however, that states may require the filing of documents filed with the SEC together with any required fee. It further provides that states may continue to collect filing or registration fees pursuant to state laws in effect prior to the enactment of H.R. 3005. CBO estimates that these fees currently generate revenues for the states totaling $210 million to $240 million annually, and that this bill would not preclude the collection of such fees.

There is, however, some uncertainty as to whether these fee collections would continue uninterrupted in all states if H.R. 3005 is enacted. The North American Securities Administrators Association and several states securities regulators have expressed concern that if H.R. 3005 were enacted, some states, because of the construction of their own statutes, would not be able to withstand legal challenges to their right to collect current fees. However, CBO believes that because the scope of the federal preemption in H.R. 3005 is limited, any loss of revenues would not be a direct cost of a federal mandate as defined in Public Law 104–4.

By prohibiting states from registering investment company offering or reviewing disclosure documents, the bill would produce administrative savings for those states that currently devote staff resources to those tasks. In our survey of state securities regulators, however, CBO found that only about a dozen states actively review and comment on disclosure documents, and that only a few staff members in each state were assigned those tasks. Therefore, we estimate that the administrative savings to states would not significantly offset revenue losses from other mandates in the bill.

Other preemptions of State laws

CBO estimates that the other preemptions of state law contained in the bill would not impose direct costs on state, local, or tribal governments.

8. Appropriation or other Federal financial assistance provided in bill to cover mandate costs: None.

9. Other impacts on State, local, and tribal governments: None.

10. Previous CBO estimate: On June 6, 1996, CBO provided a cost estimate for H.R. 3005, the Securities Amendments of 1996, as ordered reported by the House Committee on Commerce on May 15, 1996. At that time, CBO estimated that H.R. 3005 contained intergovernmental mandates that would prohibit states from collecting certain fees totaling over $125 million annually that they otherwise would collect. Based on a technical and conforming change to the base text of H.R. 3005 regarding the scope of the preemption of state registration requirements, CBO now estimates

that the mandate costs in H.R. 3005 would total about $15 million annually.

11. Estimate prepared by: Pepper Santalucia.

12. Estimate approved by: Robert A. Sunshine for Paul N. Van de Water, Assistant Director for Budget Analysis.

Inflationary Impact Statement

Pursuant to clause 2(l)(4) of rule XI of the Rules of the House of Representatives, the Committee finds that the bill would have no inflationary impact.

Advisory Committee Statement

No advisory committees within the meaning of section 5(b) of the Federal Advisory Committee Act are created by this legislation.

Section-by-Section Analysis of the Legislation

SECTION 1.—SHORT TITLE; TABLE OF CONTENTS

Section 1 states that this Act may be cited as the "Securities Amendments of 1996". Section 1 also provides a table of contents for Titles I and II of the Act.

TITLE I.—CAPITAL MARKETS DEREGULATION AND LIBERALIZATION

SECTION 101—SHORT TITLE

Section 101 provides that Title I may be cited as the "Capital Markets Deregulation and Liberalization Act of 1996".

SECTION 102—CREATION OF NATIONAL SECURITIES MARKETS

Section 102(a)—Exemption from State Regulation of Securities Offerings. This provision replaces existing section 18 of the Securities Act of 1933 ("Securities Act"). Section 18 currently provides that the authority of State governments to regulate securities offerings is not limited or restricted by the Securities Act. This provision adds a new Section 18 to the Securities Act in order to realign the respective responsibilities of Federal and State governmental authorities over certain aspects of the securities markets.

Section 18(a) prohibits State governments from requiring the registration of, or otherwise imposing conditions on, offerings of "covered securities" as defined in Section 18(b), subject to Section 18(d), which preserves State authority to investigate and bring enforcement actions with respect to fraud or deceit (including broker-dealer sales practices) in connection with securities or securities transactions. Section 18(d) also preserves the authority of States to require notice filings and fees with respect to certain offerings, and to suspend the offer or sale of securities within a State as a result of the failure to submit a filing or fee. Section 18(a) also limits State governments from requiring the regulation or otherwise imposing conditions on offerings of "conditionally covered securities" as defined in Section 18(c). Section 18(a) specifically provides that States may not conduct merit reviews of these offerings. In addition, Section 18(a) prohibits States from placing limits or imposing conditions upon (including outright prohibition of) the use of offering documents with respect to such "covered securities" offerings, including advertising or sales literature used in connection with such offerings. It further preempts State regulation of other disclosure documents such as proxy statements and annual reports. In each case, the prohibition applies both to direct and indirect State action, thus precluding States from exercising indirect authority to regulate the matters preempted by Section 18(a). Also, in each case, the prohibitions are subject to the provisions of subsection (d). By extending the prohibition to indirect State action, the Committee specifically intends to prevent State regulators from circumventing the provisions of section 18(a) that expressly prohibit them from requiring the registration of, or otherwise imposing conditions or limitations upon, offerings of covered securities. The Committee does not intend, however, that the extension of the prohibition to indirect actions by State regulators restrict or limit their ability to investigate, bring actions, or enforce orders, injunctions, judgments or remedies based on alleged violations of State laws that prohibit fraud and deceit or that govern broker-dealer sales practices in connection with securities or securities transactions.

Section 18(b) defines "covered securities" for the purposes of the provisions of the bill that limit the securities regulatory authority of State governmental bodies. The following four categories of securities are set forth as "covered securities."

Paragraph 18(b)(1) includes as "covered securities" those securities listed, or authorized for listing, on the New York Stock Exchange (NYSE) or the American Stock Exchange (AMEX) as well as those that are included, or qualify for inclusion, in the National Market System of the National Association of Securities Dealers Automated Quotation System (NASDAQ–NMS). This paragraph codifies in the Securities Act of 1933 an exemption from State registration requirements similar to existing State statutes excepting from State registration requirements securities traded in such markets. In order to avoid competitive disparities, the Commission is given discretionary authority to extend similar preemption treatment to other national securities exchanges (or tiers or segments thereof) that have substantially similar listing standards. Some of the regional exchanges have developed tiers that have listing standards similar to NASDAQ–NMS and it is anticipated that other regional exchanges (or new exchanges) may seek to develop such tiers or segments of their markets. The Committee intends that the Commission use this authority to facilitate listings on such qualifying exchanges or tiers or segments thereof. The Committee expects the Commission to monitor the listing requirements of these exchanges, consistent with its supervisory authority under the Exchange Act, to ensure the continued integrity of these markets and the protection of investors.

Finally, securities of the same issuer that are equal in seniority or senior to such listed or qualified securities are also "covered securities" for the purposes of Section 18(a). This provision is intended to afford to issuers of debt securities the same benefits of preemption as are enjoyed by issuers of equity securities.

Paragraph 18(b)(2) includes as "covered securities" those securities issued by investment companies regulated under the Investment Company Act of 1940. In recent years, the Commission has directed an increasing percentage of its resources to overseeing the regulation of registered investment companies. The National Association of Securities Dealers (NASD) also maintains an effective program of reviewing the sales materials and advertising of registered investment companies that are also broker-dealers, accounting for approximately 90% of the industry. Registered investment companies themselves often maintain strong internal compliance departments, and the industry has a laudable record of maintaining a strong and genuine commitment to the principle of investor protection. The Committee expects that rather than being burdened with the time-consuming task of conducting a second review of investment company offering and sales materials, State regulatory authorities will be freed to spend more time investigating customer complaints, broker-dealer sales practice problems, and related issues.

Paragraph 18(b)(3) includes as "covered securities" sales to qualified purchasers. This has the effect of preempting State regulation of offers and sales of securities to qualified purchasers. This paragraph anticipates that the Commission will adopt by rule or regulation a definition of qualified purchaser that would be used for determining the scope of this provision. The Committee intends that the Commission move promptly to adopt such a rule or regulation to give effect to the provision.

The Committee believes that securities offered or sold to qualified purchasers generally should be included as "covered securities" for three reasons. First, many States currently exempt such securities from registration requirements, but the qualification standard can vary from State to State. This provision will result in a uniform national rule for qualified purchasers, which should greatly facilitate the ability of issuers to use it.

Second, the Committee expects that the securities to be included will be fundamentally national in character and generally (though not always) subject to regulation at the Federal level. Thus, the Committee expects the Commission to craft and construe the definition so that, for example, purchasers of mortgaged-backed, asset-backed and other structured securities, as well as securities issued in connection with project financings, are generally included as qualified purchasers. The Committee notes that structured securities are routinely issued by special purpose vehicles or by trusts that are not listed on an exchange, and will often not have two years of audited financial statements needed to qualify for the listing exemption created by paragraph 18(b)(1). As such, it is essential that the Commission craft regulations for qualified purchasers that will implement Congress's intention that such structured offerings be regulated exclusively by the Federal government.

Third, the Commission is given flexible authority to establish various definitions of qualified purchasers. In all cases, however, the Committee intends that the Commission's definition be rooted in the belief that "qualified" purchasers are sophisticated investors, capable of protecting themselves in a manner that renders regulation by State authorities unnecessary. For guidance, the Committee suggests that the Commission consider a definition of qualified purchaser not more restrictive than that provided in Title II of this legislation under Section 3(c) of the Investment Company Act. The Committee further intends that the qualified purchaser exemption apply to all offerings of securities, whether registered or exempt under the Securities Act. In prescribing any such rule, the Commission may define the term "qualified purchaser" differently with respect to different categories of securities, consistent with the public interest (including consideration of efficiency, competition and capital formation) and the protection of investors.

Finally, the qualified purchaser provision allows State preemption, State exemptions and State registrations to be tacked together to comply with State requirements. Thus, sales to qualified purchasers would qualify for preemption without regard to whether, in the same offering, offers and sales are also made to nonqualified purchasers.

Paragraph 18(b)(4) defines as "covered securities" certain offerings and transactions that are exempted from registration under the Securities Act of 1933. Specifically, a "covered security" would include secondary market trading transactions exempt from Federal registration pursuant to sections 4(1) or 4(3) of the Securities Act (provided that the issuer is reporting under the Securities Exchange Act of 1934 ("Exchange Act") or is exempt from filing such reports), as well as similar transactions exempt from registration pursuant to section 4(4) of the Securities Act. "Exempted securities" under section 3(a) of the Securities Act also would be "covered securities" and thus preempted from State registration, with three exceptions: (i) securities of non-profit and similar entities set forth in Section 3(a)(4); (ii) intrastate offerings under section 3(a)(11)(i); and (iii) municipal securities as defined in section 3(a)(2) (which would be preempted in every State but the State in which the issuer of such municipal securities is located). Finally, securities sold in private transactions under section 4(2) of the Securities Act would be "covered securities," and thus preempted, if offered or sold pursuant to a Commission rule or regulation adopted under such section 4(2). The Committee intends that the section 4(2) exemption from State regulation facilitate private placement of securities consistent with the public interest and the protection of investors.

Section 18(c) defines "conditionally covered securities," which will not be subject to registration requirements and routine review by State securities regulators, subject to certain conditions, and subject to 18(d).

Paragraph 18(c)(1) states that, subject to the conditions set forth in paragraphs (2) and (3), certain Federally registered offerings also will be "covered securities" for the purpose of this legislation. Such offerings are defined as: registered securities offerings by issuers with total assets exceeding $10 million (which may be measured upon conclusion of the transaction) and two years of audited financial statements ending before the filing of the registration statement. The Committee intends that an issuer qualifying under this provision would have at least two years of actual operating history.

Paragraph 18(c)(2) provides that certain offerings—those involving securities issued by blank check companies, partnerships, limited liability companies, direct participation investment programs, penny stock companies, and roll-up transactions, are excluded from the operation of paragraph 18(c)(1). Thus, certain, categories of offerings that have been a disproportionate source of fraudulent practices and disclosure abuse would continue to be subject to State regulation (as well as Federal regulation), unless they are "covered securities" pursuant to Section 18(b).

Paragraph 18(c)(3) would preserve State review of offerings otherwise covered by paragraph 18(c)(1) that involve a person subject to a specified disqualification. Certain persons associated with the issuer—the issuer itself, its principal financial officers, and principal shareholders—must not be subject to previous action for misconduct in order for the securities offering to be a "covered security" and for the requisite State preemption to apply. The disqualifying conduct consists of statutory disqualifications, as defined in subparagraphs (A), (B), (C), and (D) of Section 39(a)(39) of the Exchange Act, as well as a range of other specified Federal and State offenses, generally relevant to the securities business. The paragraph provides that certain of These specified State offenses, generally relating to administrative or largely technical violations of State law, will give rise to disqualification of an offering only in the particular State in which the conduct occurred.

The paragraph also provides that an issuer of securities that cease to be "covered securities" pursuant to the operation of paragraph 18(c)(3) will not be subject to a right of rescission under State securities law solely as a result of the operation of paragraph 18(c)(3)

Paragraph 18(c)(4) provides the Commission with discretionary authority to exempt a person subject to a specified disqualification by rule or order, similar to the process currently in effect in connection with Commission Regulation A offerings. An issuer may avoid the operation of the conduct disqualification provision by taking reasonable steps to ascertain where any of its principal officers or shareholders is subject to any of the specified disqualifying conduct. The paragraph also provides that the limitations of paragraph 3(B) may be waived by a securities commission in the relevant State that has exempted the affected person from the application of the paragraph.

The paragraph establishes a non-exclusive safe harbor for the determination of reasonable steps. An issuer shall be conclusively deemed to have taken reasonable steps if it searches centralized data bases specified by the Commission to ascertain the disciplinary background of its principal officers and shareholders and reveals no person subject to the disqualification provisions of paragraph 18(c)(4), and receives sworn affidavits from such persons stating that they are not subject to the conduct disqualifications set forth in paragraph (3). Conclusive proof of such reasonable steps shall constitute appending the results of such search to the affidavits, or to some other duly executed certificate. This safe harbor is not subject to any qualification.

Section 18(d) preserves State authority in certain defined areas.

Paragraph 18(d)(1) preserves specified State authority, pursuant to State law, consistent with Section 18. The relationship between Section 18(d) and Section 18(a) is especially important. The Committee intends to preserve the ability of the States to investigate and bring enforcement actions under the laws of their own State with respect to fraud and deceit (including broker-dealer sales practices) in connection with any securities or any securities transactions, whether or not such securities or transactions are otherwise preempted from State regulation by Section 18. It is the Committee's intent that the limitations on State law established by Section 18 apply to State law registration and regulation of securities offerings, and do not affect existing State laws governing broker-dealers, including broker-dealer sales practices. In preserving State laws against fraud and deceit, (including broker-dealer sales practice abuse), however, the Committee intends to prevent the States from indirectly doing what they have been prohibited from doing directly. The Committee intends that the authority that States retain over broker-dealers to allow the States to impose conditions on, or otherwise to regulate, offerings of securities. The legislation preempts authority that would allow the States to employ the regulatory authority they retain to reconstruct in a different form the regulatory regime for covered securities that Section 18 has preempted.

Thus, for example, Section 18 precludes State regulators from, among other things, citing a State law against fraud or deceit or regarding broker-dealer sales practices as its justification for prohibiting the circulation of a prospectus or other offering document or advertisement for a covered security that does not include a legend or disclosure that the States believes is necessary or that includes information that a State regulator criticizes based on the format or content thereof. The Committee intends to eliminate States' authority to require or otherwise impose conditions on the disclosure of any information for covered securities. If, however, a State had undertaken an enforcement action that alleged, for example, that the prospectus contained fraudulent financial data or failed to disclose that principals in the offering had previously been convicted of securities fraud, it is conceivable that State laws regarding fraud and deceit could serve as the basis of a judgment or remedial order that could include a restriction or prohibition on the use of the prospectus or other offering document or advertisement within that State. The Committee does not intend Section 18 to be interpreted in a manner that would prohibit such judgments or remedial orders.

It is also the Committee's intention not to alter, limit, expand, or otherwise affect in any way any State statutory or common law with respect to fraud or deceit, including broker-dealer sales practices, in connection with securities or securities transactions.

Paragraph 18(d)(2) retains for the States the authority to require notice filings and require and collect fees with respect to certain securities offerings. This section is intended to accomplish two things: first, it is intended to ensure that States can continue to receive filings for notice purposes from issuers selling their securities within the jurisdiction, notwithstanding the fact that States will no longer be permitted to require the issuers' covered securities to be registered. Second, it is intended to ensure that States can continue to receive fees from issuers selling securities within the jurisdiction, notwithstanding the fact that States will no longer be permitted to require the issuers' covered securities to be registered.

In this regard, paragraph 18(d)(2)(B) specifies that, until otherwise provided by State law, each State may continue to collect fees in connection with securities or securities transactions in amounts determined pursuant to that State's law in effect prior to enactment of the legislation. The Committee notes that some commentators expressed concern that the legislation's preemption of State registration authority over covered securities would prevent a State that links a securities issuer's obligation to pay fees to registration of those securities from collecting such fees. These commentators suggested that, in order to continue to require that a securities issuer pay fees to a State notwithstanding the preemption of the issuer's obligation to register the securities, a State might have to revise its statutes to provide for a fee requirement in connection with the notice filings the legislation permits States to require. Paragraph 18(d)(2)(B) permits a State that currently requires securities issuers to pay fees in connection with registration to continue to receive such fees during any interim period between enactment of this legislation and such time as the State may revise its statutes. Thus, the preemptive effect of the legislation with respect to State registration authority does not extend to a State's ability to continue to collect registration fees, but does extend to all other aspects of State registration authority over covered securities. Paragraph 18(d)(2)(C) follows the practice under the securities laws of most States in not permitting such notice filing or fees in connection with securities listed or eligible for listing on the New York Stock Exchange, American Stock Exchange, or the NASDAQ National Market System, or any securities of the same class as or senior to such securities.

Paragraph 18(d)(3) preserves the authority of the States to suspend the offer or sale of securities within a State as a result of the failure to submit a filing or fee permitted under paragraph 18(d)(2). It is the Committee's intent that the States retain authority to take actions permitted under this section in order to enforce any filing and fee requirements permitted under this section and to calculate accurately any applicable fees. In addition, for any State that wishes to assess fees based upon the amount of sales within that State within a given period of time (e.g., true indefinite registration), this section is intended to preserve the State's right to receive the sales information necessary to compute the amount of the fee. However, the Committee does not intend that this provision will allow States to regulate indirectly offerings or sales of securities or transactions preempted under this title.

Section 18(e) defines the terms "principal officer" and "principal shareholder" for the purpose of Section 18, and directs the Commission to define by rule, for the purpose of Section 18, the term "prepared by the issuer." In addition, Section 18(e) defines the term "offering document" for the purpose of Section 18 by reference to the definition of "prospectus" contained in Section 2(10) of the Securities Act, without regard to exceptions (a) and (b) in Section 2(10). Specifically, the term "offering document" would include any prospectus, notice, circular, advertisement, letter, or communication, written or by radio or television, which offers any security for sale or confirms the sale of any security. Notably, materials that the Commission determines not to be a prospectus by Commission rule also are offering documents for the purpose of Section 18, as are materials that accompany or follow the final prospectus. With respect to securities of registered investment companies, the term "offering document" also is defined to include materials that the Commission has defined not to be offers, such as Rule 135a advertisements.

Section 102(a)(2) requires the Commission to conduct a study, within one year of enactment, on the extent to which uniformity of State regulatory requirements for securities or securities transactions has been achieved for securities that are not "covered securities." In conducting the study, the Commission shall review the impact of such uniformity or lack thereof on the cost of capital, innovation and technological development in securities markets, on securities issuers, including small businesses, and on the protection of investors.

Section 102(b)—Broker-Dealer Regulation. This section requires the Commission, after consultation with the self-regulatory organizations ("SROs") and the States, to conduct a study of the effect of disparate state licensing requirements on associated persons of registered broker-dealers and methods for the States to establish uniform licensing requirements. The Commission, within one year, is required to submit to Congress a report on the study that includes recommendations for establishing uniform requirements. This section amends Section 15 of the Securities Exchange Act of 1934 by adding a new section 15(h).

Section 15(h) addresses issues of duplicative or inconsistent regulation of associated persons of broker-dealers by State and Federal government.

Paragraph 15(h)(1) preempts State laws that impose financial responsibility and reporting requirements inconsistent with or exceeding requirements established under the Exchange Act. This preemption extends to any regulation of capital, margin, books and records, bonding, record making and record keeping.

Paragraph 15(h)(2) establishes a uniform national exemption for associated persons effecting transactions for existing customers. It permits associated persons to effect certain transactions with existing customers in States in which they are not licensed. For purposes of this provision, a customer is an existing customer if he or she maintained an account with the broker-dealer for at least 30 days.

In order to be exempt from a State's licensing requirements, the associated person (1) must not be ineligible to register in the State for any reason, (2) must be registered with the NASD and with at least one State, and (3) must be associated with a broker-dealer that is registered in the State in which the transaction is effected. In addition, the transaction effected in a State in which the associated person is not licensed must fall into one of the following categories.

The first type of permitted transaction is one effected on behalf of an existing customer assigned to the associated person while that customer is temporarily away from home, for example on vacation or business. If, however, the customer is present in a State for 30 or more days or permanently changes residence, the associated person must file an application for registration. This application must be filed within 10 calendar days of the later of the date of the transaction or of discovering that the customer has been present in the State for 30 or more days or has permanently changed his or her address.

The second type of permitted transaction is one effected on behalf of an existing customer during the pendency of the associated person's application for licensing in the State. The associated person, however, must cease effecting transactions in the State on the earlier of 60 days after the application is filed, or when the State notifies the associated person that it has denied the application or stayed the pendency of the application for cause.

Finally, 10 or fewer total transactions with any person are permitted in States in which the associated person is not licensed. Any transaction that falls within one of the other two above categories does not count toward the 10 transactions permitted in this category. The Committee intends that these provisions be construed so as not to permit cold calling of potential customers by unlicensed brokers.

SECTION 103—MARGIN

Section 103 repeals statutory restrictions under section 7 and section 8(a) of the Exchange Act on the sources from which broker-dealers may borrow. It also exempts from Federal margin requirements, adopted under section 7, credit extended, maintained, or arranged to or for a member of a national securities exchange or registered broker or dealer (1) a substantial portion of whose business consists of transactions with persons other than brokers or dealers, or (2) to finance market making or underwriting activities.

SECTION 104—PROSPECTUS DELIVERY

Section 104(a). This section requires the Commission to report to the Congress on the steps the Commission has taken, or anticipates taking, to facilitate the electronic delivery of prospectuses to institutional and other investors. Such report is to be delivered within 6 months of enactment of the Act.

Section 104(b). The provision requires the Commission to report to the Congress its views and recommendations concerning the Advisory Committee on Capital Formation. The Advisory Committee is preparing a report to the Commission, which is expected to recommend a shift in the traditional Securities Act approach of registering offerings to a "company" registration approach. The report required by section 104(b) should also describe any actions taken to implement the recommendations of the Advisory Committee and is to be delivered within 1 year of the enactment of the Act.

The Committee notes that an alternative to the existing registration approach, such as one that relies on company disclosure, could streamline both registration and disclosure requirements, while actually enhancing information flow and protection to investors. In that context, the Commission should consider whether an alternative vehicle to the prospectus can more efficiently and effectively delivery information to investors.

SECTION 105—EXEMPTIVE AUTHORITY

Section 105 provides the Commission with broad and general exemptive authority under both the Securities Act and the Exchange Act, similar to the authority provided to the Commission under other securities statutes. Both the Investment Company Act and the Investment Advisers Act provide the Commission with authority to exempt any persons, securities, or transactions from any provision of the statute or the rules thereunder. Moreover, the Trust Indenture Act of 1939 ("Trust Indenture Act") provides the Commission with similar broad exemptive authority with respect to the provisions of that Act.

Section 105(a). This section adds a new Section 28 to the Securities Act to provide the Commission with the authority, by rule or by regulation, to conditionally or unconditionally exempt any person, security, or transaction, or any class of the same, from any provision or provisions of the Act or any rule or regulation thereunder. Section 28 allows the Commission enhanced flexibility to more easily adopt new approaches to registration, disclosure, and related issues, such as are being considered by the Commission's Advisory Committee on Capital Formation. The Committee expects that the Commission will use this authority to promote efficiency, competition and capital formation in the marketplace, consistent with the public interest and investor protection. The Committee also intends that the Commission at an early date raise the ceilings on various exemptions adopted pursuant to Section 3(b) of the Securities Act, the small offering exemption under the Securities Act, from $5,000,000 to not less than $10,000,000, including increasing the exemption amount of offerings for certain employee benefit plans, pursuant to Rule 701 under the Securities Act, and small public offerings, pursuant to Regulation A under the Securities Act.

Section 105(b). The legislation adds a new Section 36 to the Exchange Act to provide the Commission with authority under the Exchange Act similar to that contained in new Section 28 of the Securities Act. Unlike its Securities Act counterpart, however, Section 36 of the Exchange Act also allows the Commission to act by order. To assist the Commission in handling individual exemptive requests, Section 36 permits the Commission to determine the procedures and circumstances under which an exemptive order may be granted. The Committee expects that the Commission will use this authority to promote efficiency, competition and capital formation in the marketplace, consistent with the public interest and investor protection.

The Department of Treasury has authority under Section 15C of the Exchange Act to regulate government securities broker-dealers. The Government Securities Act Amendments of 1993, which enacted Section 15C, prescribed a consultative process for both Treasury and Commission rulemaking under that section. The legislation provides that the broad grant of exemptive authority to the Commission in new Section 36 of the Exchange Act does not extend to Section 15C of the Exchange Act or to the definitions in Sections 3(a)(42) through (45) as used in that section.

SECTION 106—PROMOTION OF EFFICIENCY, COMPETITION, AND CAPITAL FORMATION

Section 106 requires the Commission to consider efficiency, competition, and capital formation when it engages in rulemaking or reviews SRO-proposed rules pursuant to the Securities Act, the Exchange Act, or the Investment Company Act under a "public interest" standard. The new section makes clear that matters relating to efficiency, competition, and capital formation are only part of the public interest determination, which also includes, among other things, consideration of the protection of investors. For 62 years, the foremost mission of the Commission has been investor protection, and this section does not alter the Commission's mission. In considering efficiency, competition, and capital formation, the Commission shall analyze the potential costs and benefits of any rulemaking initiative, including, whenever practicable, specific analysis of such costs and benefits. The Committee expects that the Commission will engage in rigorous analysis pursuant to this section. Such analysis will be necessary to the Congress in connection with the Congress' review of major rules pursuant to the terms of the Small Business Regulatory Enforcement Fairness Act of 1996.

SECTION 107—PRIVATIZATION OF EDGAR

Section 107 requires the Commission to examine proposals for the privatization of the EDGAR system in ways that would promote competition in the automation and rapid dissemination of information. The section also requires the Commission to report to Congress regarding its examination of those issues within 180 days of enactment of this legislation.

SECTION 108—COORDINATION OF EXAMINING AUTHORITIES

Section 108 adds a new subsection to Section 17 of the Exchange Act designed to facilitate coordination of examination of broker-dealers by self-regulatory organizations (SROs).

Section 17(i) requires examining authorities (defined as SROs with the authority to examine the activities of a registered broker-dealer) to determine whether each broker-dealer subject to examination by more than one SRO requests coordination of its regulatory examinations by all SROs. The examining authorities are required to prepare an advance schedule of all coordinated examinations and to ensure, to the maximum extent practicable, that every brokerage firm that so requests shall have all requested aspects of its examination conducted simultaneously and without duplication of the areas covered. Any examining authority that does not participate in a scheduled coordinated examination would not be able to conduct its own routine examination (other than a coordinated examination of that broker or dealer) within nine months of the conclusion of the scheduled coordinated exam. The Committee notes that, under some circumstances, an SRO primarily responsible for the financial and operational examination of a broker-dealer might miss a scheduled exam and be precluded from routinely examining that broker-dealer for nine months because of the operation of subsection (i)(5). The Securities Investor Protection Corporation ("SIPC") expressed concerns to the Committee that the imposition of this limitation or penalty could leave SIPC, which must rely on the results of Commission and SRO examination, without important information on the financial condition of its members. The Committee expects that, to avoid such a situation, the SROs will attempt to reschedule the examination in consultation with the broker, or failing that, that other reasonable steps are taken to make sure that the financial and operational examination is conducted in a timely manner. Such other steps may include designation of a participating SRO to conduct the financial and operational examination. Examinations "for cause" (which are conducted when indications of possible wrongdoing exist) may be conducted at any time. The Committee expects that SROs that fail to coordinate will not use the "for cause" exception exclusively to conduct a routine exam that was missed.

Section 17(i) also requires the Commission to create a broker-dealer advisory committee comprised of representatives of broker-dealers that are subject to examinations by more than one SRO. Because the advisory committee created by this provision is likely to be involved in discussing examination strategies and related matters that may bear on enforcement, this committee is specifically exempted from the Federal Advisory Committee Act.

The Commission would be required to report to Congress, within one year after enactment of the Act, pursuant to Section 17(i) on the progress it and the examining authorities have made in reducing duplication and improving coordination, on the activities of the advisory committee, and on any redundancies that have not been addressed by the coordination of examining authorities.

SECTION 109—FOREIGN PRESS CONFERENCES

Section 109 requires the Commission to adopt rules under the Securities Act concerning the status under the registration provisions of the Securities Act of foreign press conferences and foreign press releases by persons engaged in the offer and sale of securities. The Commission would be required to adopt these rules within one year of the enactment of the Act. The Committee intends that journalists disseminating information in the U.S. be given appropriate access to foreign press conferences involving offerings of securities in order to ensure that information is made available in the U.S. and instructs the Commission to adopt a rule that will achieve this goal consistent with the protection of U.S. investors.

SECTION 110—REPORT ON TRUST INDENTURE ACT OF 1939

Section 110 requires the Commission to report to Congress on the benefits of, the continuing need for, and, if necessary, options for the modification or elimination of the Trust Indenture Act. Such report is to be delivered within six months of enactment of the Act.

The Trust Indenture Act generally requires that all publicly issued debt securities be issued pursuant to an indenture which contains specified mandatory provisions and requires the presence of an independent trustee. The Commission shall consult with the Treasury Department on the impact of the study's recommendations on the bond market and on insured depository institutions.

In the context of the Subcommittee hearings on H.R. 2131 (Serial No. 104–50), the Committee notes that three witnesses testified on the proposal to repeal the Trust Indenture Act. Morey W. McDaniel, Esq., an indenture practitioner, questioned the Act's continued utility and supported its repeal, while SunTrust Capital Markets President and CEO R. Charles Shufeldt, testifying on behalf of the ABA Securities Association, argued that the Act still served a useful purpose and opposed repeal. Columbia University Professor of Law John C. Coffee, Jr. testified that there was a "plausible case for repealing much of the statute" but cautioned Congress to retain necessary protections for bondholders in some form. Finally, the Committee notes that it approved legislation in 1990, the Trust Indenture Reform Act (P.L. 101–550, Nov. 15, 1990), to modernize the Act and streamline its requirements to reflect evolving industry practice and market conditions. The Committee expects the Commission will consider the issues raised in the testimony and the effect of the 1990 Act.

TITLE II—INVESTMENT COMPANY ACT AMENDMENTS

SECTION 201—SHORT TITLE

Section 201 provides that Title II may be cited as the Investment Company Act Amendments of 1996.

SECTION 202—FUNDS OF FUNDS

Currently, subject to certain exceptions, Section 12(d)(1) of the Investment Company Act of 1940 (the "Investment Company Act") imposes three restrictions on the ability of one investment company to invest in another: (1) an investment company may not acquire more than 3% of another investment company's voting stock; (2) an investment company may not hold more than 5% of its assets in securities of another single investment company; and (3) an investment company may not hold more than 10% of its assets in securities of all other investment companies.

One of the exceptions to these restrictions is an arrangement in which a fund invests solely in the shares of another fund. The exemption is often used by so-called "master-feeder" funds, where one or more funds ("feeder funds") invest all of their assets in another fund ("master fund"). These arrangements are often used to facilitate the master fund's access to alternative distribution channels to sell its shares.

Section 202(1)(A). This section effects a change regarding the voting rights of shareholders in "master-feeder" arrangements. It requires all feeder funds—rather than only those that are not registered under the Investment Company Act, as is the case under current law—to vote the master fund shares that they own proportionately in accordance with the votes cast by the feeder fund's own shareholders. This will give feeder fund shareholders effectively the same voting rights they would have as direct security holders of the master fund.

Current law imposes this voting requirement only on unregistered feeder funds because it was enacted to address abusive practices of the 1970s involving off-shore (and therefore unregistered) funds that invested in U.S. funds. Today, the development of master-feeder arrangements has led to a proliferation of U.S. feeder funds, which are generally registered. In practice, registered feeder funds generally comply voluntarily with this voting requirement.

Section 202(1)(B). This section preserves the statute's limitation on the ability of unregistered investment companies to substitute securities in their portfolio. It does not effect a change in current law. The new language of this section is necessary, given the change in Section 202(1)(A) above, to preserve the status quo with respect to unregistered investment companies.

Section 202(3). This section creates a new provision, subparagraph (G) under Section 12(d)(1) of the Investment Company Act, to codify the permissibility of certain "fund of funds" arrangements if five conditions are met. These conditions, which are similar to the conditions generally imposed by the SEC on companies that are currently permitted to operate funds of funds pursuant to SEC orders, are as follows:

1. Clause (i) of new subparagraph (G) requires the acquired company and the acquiring company to be part of the same "group of investment companies." The final sentence of subparagraph (G) would define a "group of investment companies" as any two or more registered investment companies that hold themselves out to investors as related companies for purposes of investment and investor services.
2. Clause (ii) of new subparagraph (G) limits the operation of subparagraph (G) to bona fide fund of funds arrangements. The provision limits the acquiring company to investing in securities of the acquired company, securities of other registered open-end investment companies that are part of the same group of investment companies, U.S. government securities, and short-term paper. The provision for U.S. government securities and short-term paper is designed to allow the acquiring company to make short-term investments, including repurchase agreements (which often involve U.S. government securities), that provide sufficient liquidity to meet redemption requests. In the absence of such flexibility, the acquiring company might otherwise be forced to redeem securities of acquired companies to meet redemption requests when it would not otherwise be in the best interests of investors in either the acquiring or acquired company to do so.
3. Clause (iii) of new subparagraph (G) addresses the assessment of sales loads and other distribution-related fees. This clause is intended to prevent the abuses that may be associated with the layering of sales charges. It accomplishes this by providing that any sales loads and other distribution-related fees charged with respect to the acquiring company's securities (such as sales loads or rule 12b–1 fees), when aggregated with any sales load and distribution-related fees paid by the acquiring company with respect to securities of the acquired company, cannot be excessive under rules adopted pursuant to either Section 22(b) or Section 22(c) of the Act by a securities association registered under Section 15A of the Exchange Act (i.e., the National Association of Securities Dealers) or the Commis-

sion. Thus, sales charges and distribution-related fees could be assessed by both the acquiring company and the acquired company provided that, taken together, such fees are not excessive.

4. Clause (iv) of new subparagraph (G) requires the acquired company to have a fundamental policy that prohibits it from acquiring any securities of registered open-end investment companies in reliance on new subparagraph (G) or subparagraph (F) of Section 12(d)(1) (which contains an additional exception to Section 12(d)(1)). This provision will prevent a fund of funds from investing in other funds of funds. The provision is intended to avoid overly complex inter-corporate structures that may present issues that have not been presented in the types of fund of funds arrangements previously considered by the Commission.

5. Clause (i) of new subparagraph (G) requires that any acquisition of securities under new subparagraph (G) may not be in contravention of such rules and regulations as the Commission may prescribe as necessary and appropriate for the protection of investors. This provision is designed to permit the Commission, based on its experience with the operation of subparagraph (G), to adopt rules to address any perceived problems and abuses. For example, the Commission may conclude that it is necessary to adopt rules that require acquiring companies to implement procedures designed to assure that redemptions of securities of acquired companies be effected in a manner designed to limit disruptions in the portfolio management of the acquired company.

Section 202(4). This section adds a new subparagraph (J) to Section 12(d)(1) that gives the Commission the additional authority to exempt any person, security or transaction from Section 12(d)(1) of the Investment Company Act. The Commission currently has authority under Section 6(c) of the Act to exempt investment companies from Section 12(d)(1). The new subparagraph makes explicit the authority of the Commission to grant exemptions for funds of funds that might not meet the conditions of new subparagraph 12(d)(1)(G), for example, fund of fund arrangements that involve investment companies that are not part of the same group of investment companies, or fund of funds arrangements that involve a group of investment companies but do not satisfy other conditions of new subpargraph (G). The Committee notes that many investment company fund complexes may not include a sufficient number or variety of fund types to permit the creation of a workable affiliated fund of funds. The Committee intends the rulemaking and exemptive authority in new Section 12(d)(1)(J) to be used by the Commission so that the benefits of funds are not limited only to investors in the largest fund complexes, but, in appropriate circumstances, are available to investors through a variety of different types and sizes of investment company complexes.

The Committee expects that the Commission will use this authority to adopt rules and process exemptive applications in the fund of funds area in a progressive way as the fund of funds concept continues to evolve over time. In exercising the exemptive authority, the Commission shall also consider factors that relate to the protection of investors. These factors may include the extent to which a proposed arrangement is subject to conditions that are designed to address conflicts of interest and overreaching by a participant in the arrangement, so that the abuses that gave rise to the initial adoption of the Act's restrictions against investment companies investing in other investment companies are not repeated.

Section 202 of the legislation redesignates current subparagraphs (G) and (H) of Section 12(d)(1) as subparagraphs (H) and (1), respectively.

SECTION 203—REGISTRATION OF SECURITIES

Section 203 of the legislation adds new Section 24(f) to the Investment Company Act. The new provision provides that upon the effectiveness of the registration statement of an investment company, the investment company will be deemed to have registered an indefinite quantity of securities. The investment company must then pay a fee to the Commission within 90 days after the end of its fiscal year, based upon the net sales of the company for that fiscal year. The amendment specifically provides that the fee will be based on the aggregate sales price for which the company's securities were sold (including securities issued pursuant to a dividend reinvestment plan) during the fiscal year, reduced by the aggregate redemption or repurchase price of the securities during that year and the aggregate redemption or repurchase price of the securities during any prior fiscal year ending not more than one year before the enactment of this legislation that were not used previously by the company to reduce the fees payable under the section.

An investment company that misses the filing deadline must pay interest based on the amount due at the rate established by the Secretary of Treasury under the Debt Collection Act of 1982, 31 U.S.C. 3701 et seq. This provision encourages timely filing and will compensate the U.S. Treasury for any delay in the receipt of revenues by requiring interest to be paid on past due amounts. Although the new provision incorporates the rate established pursuant to section 11 of the Debt Collection Act, the other provision of that section do no apply.

This section gives the Commission rulemaking authority to implement new Section 24(f). it also effects a conforming amendment to Section 24(e) of the Investment Company Act to eliminate paragraphs (1) and (2) of that section relating to the registration of a definite amount of a company's securities. Despite the elimination of Section 24(e)(1), open-end management investment companies and unit investment trusts that have registered shares in accordance with Section 24(e) (as in effect prior to enactment of this legislation) may sell those shares without the payment of any additional registration fees. The amendments made by this section will be effective 6 months after the date of enactment of this legislation or on such earlier date as the Commission may specify by rule.

SECTION 204—INVESTMENT COMPANY ADVERTISING PROSPECTUS

This section adds subsection (g) to Section 24 of the Investment Company Act to direct the Commission to permit the use of a new "investment company advertising prospectus" for purposes of Section 5(b)(1) of the Securities Act. Unlike the "omitting" prospectus that is permitted pursuant to rules promulgated by the Commission under section 10(b) of the Securities Act, the advertising prospectus authorized by new Section 24(g) is not restricted to information "the substance of which" is included in the fund's statutory prospectus (the prospectus mandated by Section 10(a) of the Securities Act). The investment company advertising prospectus may contain performance data, and could be subject to the same standardized calculation requirements as Commission rules currently apply to performance data used by investment companies.

The investment company advertising prospectus is deemed to be permitted by Section 10(b) of the Securities Act. As a result, the advertising prospectus will be subject to prospectus liability under Section 12(2) of the Securities Act; it need not be filed as part of the registration statement, and will not be a part of the registration statement for purposes of Section 11 of the Securities Act. In addition, the Commission may prevent or suspend the use of an investment company advertising prospectus pursuant to the standards and procedures set forth in Section 10(b). This is not a new grant of authority but rather an incorporation by reference of the standards and procedures in section 10(b).

SECTION 205—VARIABLE INSURANCE CONTRACTS

Section 205(a). This section amends the Investment Company Act to exempt variable insurance contracts from the charge restrictions in Sections 26 and 27, and instead requires aggregate charges under variable contracts to be reasonable. Currently, insurance companies selling variable insurance are treated as periodic payment plan sponsors and are, therefore, limited by Section 26 of the Act in the types of fees that may be deducted under the contracts and to the assessment of "reasonable" fees for performing administrative services. In addition, variable insurance contracts are treated as periodic payment plan certificates and, thus, the issuers of the contracts must comply with Section 27 of the Act, which limits the amount, manner, and timing of sales load deductions and prescribes certain refund rights for surrendering contract owners. The legislation recognizes that variable insurance contracts and periodic payment plan certificates are different products that should not be treated identically under the Act, and subjects variable insurance separate accounts to more general prohibitions against excessive fees, similar to the way mutual funds are treated under the Act.

This section adds a new subsection (e) to Section 26. New paragraph (1) of Section 26(e) exempts a registered separate account, its sponsor, and its principal underwriter from Section 26(a), which limits the types of charges that may be deducted from separate account assets and imposes custodial requirements. New paragraph (2)(A) of Section 26(e) establishes a reasonableness standard for evaluating aggregate contract charges and requires insurers to represent that such charges are reasonable. Under this new provision, an issuer must establish aggregate charges that are reasonable in relation to the services rendered under the contract, the expenses expected to be incurred, and the risks assumed by the insurance company. New paragraph 26(e)(3) explicitly authorizes the Commission to adopt rules under subparagraph 26(e)(2)(A). New paragraph (3) also clarifies that the aggregate charges covered by paragraph (2)(A) include all fees and charges imposed for any purpose and in any manner, including, without limitation, marketing, sales, and distribution charges, compensation for investment advisory, administrative, custodial, transfer agent, or other services; insurance charges; and charges related to taxes imposed on the sponsoring insurance company; and including, without limitation, charges imposed directly on the contract holder or on the assets of the registered separate account.

This section also adds subparagraph (B) to Section 26(e)(2), in order to codify certain provisions of Commission rules that permit an insurance company rather than a bank to maintain custody of separate account assets without a trust indenture. The legislation does not change current regulation of insurance companies or their separate account operations, but simply preserves the current custodial provisions in conjunction with the exemption provided by Section 26(e)(1). To serve as custodian, an insurer must file with its domiciliary State an annual statement of financial condition that shows it has a combined capital and surplus (if a stock company) or an unassigned surplus (if a mutual company) of not less than $1,000,000 or such other amount prescribed by the Commission. In addition, the company and its separate account operations must be supervised and examined periodically by State insurance officials.

Section 205(b). This section amends Section 27 of the Investment Company Act by adding a new subsection (i), which exempts a registered separate account, its sponsor, and its principal underwriter from the sales load restrictions of Section 27. In conjunction with this exemption, new subparagraph 27(i)(2) requires separate accounts organized as management companies to comply with the provisions of new subparagraph 26(e). Currently, Section 27(c)(2) links the regulation of periodic payment plans to procedures established in Section 26 for unit investment trusts even if the issuer is organized as a management investment company. New Section 27(i)(2), in effect, preserves that cross-reference to ensure that the charges under variable contracts funded by unit investment trusts and managed separate accounts are treated alike. New Section 27(i)(2) also makes the provisions of new Section 26(e)(2)(B) concerning custody applicable to variable contracts funded by managed separate accounts. The new subparagraph also preserves the requirement that variable contracts be redeemable securities.

SECTION 206—REPORTS TO THE COMMISSION AND SHAREHOLDERS

Section 206. This section amends Section 30(b)(1) of the Investment Company Act to grant the Commission authority to require more frequent filing with the Commission of information by investment companies. Specifically, new Section 30(b)(1) allows the Commission to require investment companies to file such information, documents and reports as the Commission deems necessary to keep reasonably current the information and documents contained in an investment company's registration statement, eliminating the restriction in current law that such information need only be filed on a semi-annual or quarterly basis. However, in order to limit unnecessary regulatory burdens on investment companies, the section adds new Section 30(c), which requires the Commission, in exercising its authority to require that this information be filed more frequently than semi-annually or quarterly, to take such steps as it deems necessary and appropriate, consistent with the public interest and the protection of investors, to avoid unnecessary reporting by, and minimize compliance burdens on, investment companies and their affiliated persons. These steps include considering and requesting public comment on feasible alternatives that minimize reporting burdens on investment companies and on the utility to the Commission of the information included in the reports in relation to the costs to investment companies and their affiliated persons of providing such information.

The section also inserts a new Section 30(f), expanding the Commission's authority to require additional information to be included in an investment company's reports to shareholders. Currently, Section 30(d) limits the Commission's authority to prescribing the content of financial statements. The new subsection gives the Commission authority to require that investment companies include in annual and semi-annual reports such other information as the Commission deems necessary or appropriate in the public interest or for the protection of investors. Again, in order to limit unnecessary regulatory burdens on investment companies, the section requires the Commission, in exercising this new authority, to take such steps as it deems necessary and appropriate, consistent with the public interest and the protection of investors, to avoid unnecessary reporting, and minimize the compliance burdens on, investment companies and their affiliated persons. These steps include considering and requesting public comment on feasible alternatives that minimize reporting burdens on investment companies and on the utility to shareholders of the information provided in relation to the costs to investment companies and their affiliated persons of providing such information.

SECTION 207—BOOKS, RECORDS AND INSPECTIONS

Section 207(1). This section expands the Commission's recordkeeping authority under the Investment Company Act. Currently, Section 31(a) of the Act authorizes the Commission to require investment companies to maintain only records that relate to the company's financial statement. This section amends Section 31(a) to authorize the commission to require registered investment companies and certain of their related entities to keep any records the Commission prescribes as "necessary or appropriate in the public interest or for the protection of investors." This authority will enable the Commission to require investment companies to maintain the records necessary for examiners to conduct a thorough examination of a company's operations and thereby ensure that the investment company and its related entities are in compliance with all applicable statues and regulations (whether or not records concerning these matters are needed to support financial statements). The legislation does not change the Commission's recordkeeping authority with respect to investment company advisers that are not majority-owned subsidiaries of an investment company, depositors for, or principal underwriters of registered investment companies. These entities would continue to be required to keep only those records necessary to record their transactions with investment companies.

This section also incorporates in Section 31(a) the definition of "records" contained in Section 3(a)(37) of the Exchange Act, which is currently incorporated in section 204 of the Investment Advisers Act. Section 3(a)(37) provides that the term "records" means account, correspondence, memorandums, tapes, discs, papers, books, and other documents or transcribed information of any type, whether expressed in ordinary or machine language. Thus, the inclusion of this definition, which encompasses both paper and electronic records, would ensure uniformity between the parallel provisions of the two Acts.

In order to prevent the grant of authority under new Section 31(a) from resulting in unnecessarily burdensome regulation of investment companies and their affiliates, the legislation requires that the Commission, in exercising its authority under this new provision, to take such steps as it deems necessary and appropriate, consistent with the public interest and the protection of investors, to avoid unnecessary recordkeeping by, and minimize the compliance burdens on, investment companies and their affiliated persons. These steps include considering and requesting public comment on (1) feasible alternatives that would minimize recordkeeping burdens, (2) the necessity of such records in view of the public benefits derived from the independent scrutiny of such records through the Commission's examinations program, (3) the costs to investment companies and their affiliates of maintaining the information that would be required, and (4) the effects that a proposed recordkeeping requirement would have on internal compliance policies and procedures.

This section also amends Section 31(b) of the Investment Company Act, which relates to the Commission's authority to inspect the books and records of investment companies. The first sentence of amended Section 31(b) would authorize the Commission or its representatives to examine records that relate to the operations of, or transactions with, a registered investment company. This provision refers only to "records" because, as defined, this term encompasses the "accounts" and "books" referred to in the existing statute, as well as other forms of non-written records.

This section expands current Commission authority by permitting examiners to inspect records that may not be required by Commission rules, but that already exist and are relevant to the operations of the investment company and transactions between the investment company and other persons required to keep records with respect to the investment company—the investment company's investment adviser and principal underwriters. In addition, as under the current provision, the Commission would have the authority to inspect such other records as the Commission may require to be maintained and preserved in accordance with subsection (a).

The section also amends Section 31(b) to authorize the Commission to request copies of records. The provision differs from the current language in Section 31(b) by eliminating the requirement for examiners to seek a formal order to obtain copies of these records.

The authority granted to the Commission under the amendments may result in its having broader access to, among other things, records that a fund may keep related to the fund's internal policies and procedures for compliance with securities laws. The Committee recognizes the vital significance of effective internal compliance systems, which are essential to helping investment companies prevent problems before they become statutory violations. The Committee believes that voluntary compliance efforts by investment companies to prevent, detect, and correct violations should be strongly encouraged. Internal control systems, in turn, generally function most effectively when they operate in an atmosphere of openness and candor, which is best fostered when internal audit reports are utilized by, and maintained within, the investment company organization, and are not routinely made public to third parties or requested by regulatory authorities.

Amended Section 31(b) addresses these issues by requiring the Commission, in exercising its authority under that section, to give "due regard" to the effective implementation, operation, and benefits of internal compliance policies and procedures. The Commission expects that, in exercising "due regard," the Commission would review fund internal audit and similar compliance-related reports on a selective basis. Specifically, the Committee expects the Commission to request and review internal audit and similar reports only insofar as necessary to determine whether the internal compliance policies of the fund or other examined persons are in place, whether procedures to effect and enforce those policies have been implemented, and whether the compliance policies and procedures are reasonably designed to detect compliance problems and address them in an appropriate fashion. Thus, the Committee anticipates that, in a routine examination, the Commission staff would seek to review a sample of an examined person's internal audit reports adequate to form a basis for concluding that the compliance policies and procedures are achieving these objectives. The Committee believes that the goal of examinations effected by the Commission staff should not be simply to duplicate the role played by a fund's internal compliance staff. If a fund has a well-functioning system of internal controls, the Commission's limited resources could be directed to other areas of fund operations, or to other funds.

In addition, recognizing that the information obtained by the Commission pursuant to this expanded inspection authority may be sensitive, the legislation adds new Section 31(c), which provides that the Commission may not be compelled to disclose any internal compliance or audit records, or information contained therein under amended Section 31. The section provides that this limitation on disclosure of information by the Commission shall not authorize the Commission to withhold information from Congress or prevent the Commission from complying with a request for information from a U.S. department, agency, or court.

Finally, the section adds new Section 31(d), defining "internal compliance policies and procedures" as policies and procedures designed to promote compliance with the Federal securities laws, and defining "internal compliance and audit record" as any record prepared by an investment company or affiliate in accordance with internal compliance policies and procedures.

SECTION 208—INVESTMENT COMPANY NAMES

Section 208. This section amends Section 35(d) of the Investment Company Act to grant the Commission rulemaking authority to define investment company names or the title of the securities they issue as materially deceptive or misleading. Currently, Section 35(d) requires the Commission to find and by order declare the name to be deceptive or misleading and then to bring an action in the proper court to enjoin use of the name. This process is rarely used and is extremely cumbersome. This section would enhance the Commission's ability to prevent the use by investment companies of materially misleading names.

SECTION 209—EXCEPTED INVESTMENT COMPANIES

Section 209(a). This section amends Section 3(c)(1) of the Investment Company Act, which excepts from the Act's regulation investment pools that have no more than 100 investors and do not engage in public offerings ("Section 3(c)(1) funds"). Section 209(a)(2) of the legislation simplifies the way the 100 investor limit of Section 3(c)(1) is calculated by no longer requiring Section 3(c)(1) funds to count the underlying shareholders of their corporate, non-investment company investors under any circumstances. As amended, Section 3(c)(1) treats beneficial ownership by a company, for purposes of the 100 investor limit, as beneficial ownership by one person, unless the company (i) owns ten percent or more of the Section 3(c)(1) issuer and (ii) is a registered investment company, a Section 3(c)(1) fund, or an excepted investment company relying on the exceptions of new Section 3(c)(7) ("Section 3(c)(7) fund").

Section 209(a)(1) of the legislation applies Section 12(d)(1)(A)(i) of the Investment Company Act to Section 3(c)(1) funds. As a result, Section 3(c)(1) funds may not purchase more than three percent of any registered investment company's securities. To cover the other side of the transaction involving open-end investment companies, registered investment companies selling their securities to Section 3(c)(1) funds also are subject to the three percent limitation in Section 12(d)(1)(B)(i).

Section 209(a)(3) of the legislation amends Section 3(c)(2) of the Investment Company Act to add a new type of entity, a "market intermediary," to those that the section currently excepts from the definition of "investment company" for purposes of the Act. The amendment addresses the type of intermediary, commonly referred to as a "swap dealer," that is in the business of acting as a counterparty with respect to various financial products, such as interest rate and currency swaps. Market intermediary is defined as any person that regularly holds itself out as being willing contemporaneously to engage in, and is regularly engaged in the business of entering into, transactions on both sides of the market for financial contracts. As defined, "market intermediary" may, in some instances, encompass persons that are otherwise excluded from the definition of investment company, such as brokers.

The term “financial contract” has been drafted in a manner that is designed to be sufficiently flexible to encompass the wide variety of financial contracts that currently exist and that will continue to develop in the evolving financial markets: it is defined as an individually negotiated transaction in respect of securities, commodities, currencies, interest rates or other functionally similar financial or economic interests, that is entered into and structured to accommodate the objectives of the counterparty.

The amendment to Section 3(c)(2) addresses the status of market intermediaries under the Investment Company Act only, and not under any other Federal securities laws.

Section 209(a)(4) of the legislation adds Section 3(c)(7) to the Investment Company Act to create a new exception from the definition of investment company for investment pools whose securities are held exclusively by “qualified purchasers,” as defined under Section 209(b) of the legislation (“Section 3(c)(7) funds”).

Under new subsection 3(c)(7)(A), there is no limit on the number of “qualified purchasers” participating in a Section 3(c)(7) fund, but the Section 3(c)(7) fund is prohibited from making a public offering of its securities. In addition, this section provides that securities that are owned by persons who received the securities from a qualified purchaser as a gift or bequest, or through legal separation, divorce, death, or other involuntary event, shall be deemed to be owned by a qualified purchaser for purposes of Section 3(c)(7). The section grants the Commission rulemaking authority with respect to such transfers.

This section adds new subsection 3(c)(7)(B) to the Act, which provides a “grandfather clause” for existing companies that currently operate under the 100-person exception of Section 3(c)(1) but wish to convert to Section 3(c)(7) status. Subsection 3(c)(7)(B) provides that, notwithstanding the requirements of subsection 3(c)(7)(A), an issuer shall qualify for the Section 3(c)(7) exception if, in addition to qualified purchasers, the issuer’s outstanding securities are beneficially owned by not more than 100 persons who are not qualified persons (the “original investors”) if (1) the original investors acquired the securities on or before the date of enactment of the legislation, and (2) at the time the securities were acquired by the original investors, the issuer was excepted under Section 3(c)(1) of the Act (in other words, the issuer had 100 or fewer investors), and (3) prior to availing itself of the new exception in proposed Section 3(c)(7), the issuer (a) disclosed to the original investors who are not qualified purchasers that future investors will be limited to qualified purchasers but will not be limited in number, and (b) the issuer provided the original investors who are not qualified purchasers with a reasonable opportunity to redeem their interests in the company.

This section also adds new subsection 3(c)(7)(C) to the Act, which applies Section 12(d)(1)(A)(i) of the Investment Company Act to Section 3(c)(7) issuers (similar to the provision in relating to Section 3(c)(1) issuers, discussed above). As a result, Section 3(c)(7) issuers may not purchase more than three percent of any registered investment company’s securities. To cover the other side of the transaction involving open-end investment companies, registered investment companies selling their securities to Section 3(c)(7) issuers also are subject to the three percent limitation in Section 12(d)(1)(B)(i).

This section also adds new subsection 3(c)(7)(D) to the Act, which clarifies that a Section 3(c)(1) fund and a Section 3(c)(7) fund will not be treated as a single issuer by the Commission for purposes of determining whether investors in the Section 3(c)(7) fund will be counted toward the 100 investor limit of the Section 3(c)(1) fund, or that investors in the Section 3(c)(1) fund that are not qualified purchasers will be treated as investors in the Section 3(c)(7) fund. This provision seeks to clarify that sponsors have the flexibility to form Section 3(c)(1) and Section 3(c)(7) funds without running afoul of the integration doctrine developed under Section 3(c)(1).

This section also provides that this non-integration provision shall not be deemed to establish whether a person is a *bona fide* qualified purchaser for purposes of Section 3(c)(7) or a bona fide beneficial owner for purposes of Section 3(c)(1). For example, a promoter of a Section 3(c)(7) fund could not organize a "sham" Section 3(c)(1) fund to facilitate investment by non-qualified purchasers in the Section 3(c)(7) fund.

Section 209(b). This section amends Section 2(a) of the Investment Company Act to add a new paragraph (51), defining the term "qualified purchaser." The section creates three categories of qualified purchasers. First, under new subparagraph 2(a)(51)(A), a qualified purchaser may be a natural person who owns at least $10 million in securities (a "natural person purchaser"). Securities of an issuer that is controlled by the putative qualified purchaser could not be used to satisfy the $10 million securities test unless the issuer that is controlled by the qualified purchaser is an investment company, a Section 3(c)(1) fund or a Section 3(c)(7) fund. Under those circumstances, the securities of that issuer may be counted toward the $10 million requirement. The purpose of this exception to the "no control" rule is to ensure that purchasers who own or control securities of companies such as investment companies or excepted companies under Section 3(c)(1) of Section 3(c)(7) are not excluded from the definition of "qualified purchasers."

Second, under new subparagraph 2(a)(51)(B), a qualified purchaser may be a trust, so long as the trustee or other person authorized to make decisions with respect to the trust and each settlor or other person contributing assets to the trust is a "qualified purchaser" under subparagraphs 2(a)(51(A) or 2(a)(51(C).

Third, under subparagraph 2(a)(51)(C), a qualified purchaser may be any person who in the aggregate owns and invests on a discretionary basis at least $100 million in securities (an "institutional purchaser"). Securities issued by any person that is an affiliated person, as defined in Section 2(a)(3(C) of the Investment Company Act, of a putative qualified purchaser could not be used to satisfy the $100 million securities test unless the issuer is affiliated with the qualified purchaser but the issuer is an investment company, a Section 3(c)(1) fund or a Section 3(c)(7) fund. Under those circumstances, the securities of that issuer may be counted toward the $100 million requirement. Section 2(a)(51)(C) would permit the aggregation of an institutional purchaser's proprietary securities holdings with those under discretionary management for purposes of the $100 million securities test. An institutional purchaser, however, could invest in a Section 3(c)(7) fund only for its own account or for the accounts of other qualified purchasers.

While new Sections 2(a)(51)(A), (B), and (C) are self-operative, the legislation gives the Commission the authority to adopt additional rules relating to the objective standards. This authority would enable the Commission to develop reasonable care defenses when an issuer relying on the qualified purchaser exception in good faith sells securities to a purchaser that does not meet the qualified purchaser definition, to develop additional conditions governing qualified purchaser trusts, or to develop rules deeming a "natural person" to include a person and his or her spouse, for example.

Section 209(c). This section amends Section 3(a)(3) of the Investment Company Act to include within that section's definition of investment securities, securities of majority-owned subsidiaries that would be investment companies but for the exclusion under Section 3(c)(1) or Section 3(c)(7). This section precludes a company from avoiding regulation under the Investment Company Act by establishing a Section 3(c)(1) or Section 3(c)(7) subsidiary.

Section 209(d). This section directs the Commission to promulgate certain rules. First, under subsection 209(d)(1) of the legislation, the Commission must promulgate rules, within one year after the date of enactment of the legislation, to implement the requirements of Section 3(c)(1)(B) of the Investment Company Act. That section provides that, subject to rules adopted by the Commission, ownership of an interest in a Section 3(c)(1) fund, where the ownership is the result of an involuntary transfer (through legal separation, divorce, death, or other involuntary event), is deemed to be ownership by one person. This would have the effect of permitting an investor in a Section 3(c)(1) fund that is owned by the maximum number of investors, 100, to transfer his or her interest to more than one person (through a bequeathal, for example), without causing the Section 3(c)(1) fund to lose its Section 3(c)(1) exception. While Section 3(c)(1)(B) was enacted fifteen years ago, the Commission has never issued rules pursuant to its authority.

Second, under subsection 209(d)(2) of the legislation, the Commission must promulgate rules, within one year after the date of enactment of the legislation, to permit ownership by knowledgeable employees of an issuer (or its affiliate) of the securities of that issuer (or affiliate) without loss of the issuer's exception under Sections 3(c)(1) or 3(c)(7). Pursuant to such a rule, an excepted company under Section 3(c)(1) would be permitted to sell its shares to employees deemed "knowledgeable" pursuant to Commission rules even if such employees caused the total number of investors in the fund to exceed 100. Similarly, pursuant to such a rule, an excepted company under Section 3(c)(7) (or an affiliate of such an excepted company, such as the company's adviser, for example) would be permitted to sell its shares to employees who are not "qualified investors" under Section 3(c)(7) but who are deemed "knowledgeable" pursuant to Commission rules.

COMMITTEE CORRESPONDENCE

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND FINANCIAL SERVICES,
Washington, DC, May 22, 1996.

Hon. THOMAS J. BLILEY, Jr.,
Chairman, Committee on Commerce,
Washington, DC.

DEAR TOM: I am writing concerning H.R. 3005, the Securities Amendments of 1996, which was recently marked-up by the House Commerce Committee.

There are two provisions of H.R. 3005, as approved by the Commerce Committee, which fall within the jurisdiction of the Banking Committee. One of these provisions relates to the margin authority of the Federal Reserve Board. In addition, the House Banking Committee staff has been discussing with the Commerce Committee staff during the past two months the potential impact of a provision in H.R. 3005 on the use of common names by banks and affiliated mutual funds. The Commerce Committee staff has agreed to address the concern of the Banking Committee staff by including an amendment that eliminates this concern.

I appreciate your willingness to address this issue. In view of your desire to move H.R. 3005 to the Floor in an expeditious manner, I do not intend to seek a sequential referral of H.R. 3005. I would appreciate, however, your commitment that the agreement worked out between our staffs will be effected without the need for separate amendments by the Banking Committee on the House Floor.

Please be advised that my agreement not to seek a sequential referral is based on an understanding that this waiver will be without prejudice to the Banking Committee's jurisdictional claims with regard to H.R. 3005 and similar bills that may be offered in the future.

I appreciate your cooperation in this matter and would further appreciate the inclusion of this letter in the Commerce Committee's report on H.R. 3005.

Sincerely,

JAMES A. LEACH, *Chairman.*

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON COMMERCE,
Washington, DC, June 5, 1996.

Hon. JAMES LEACH,
Chairman Committee on Banking and Financial Services, Rayburn House Office Building, Washington, DC.

DEAR JIM: I am writing in response to your letter dated May 22, 1996, concerning H.R. 3005, the Securities Amendments of 1996.

I appreciate your willingness to expedite passage of this legislation by agreeing not to seek a sequential referral thereof. We have been able to address your concern regarding the impact on banks of a provision of the legislation dealing with investment company names. It is far more constructive for committees to work cooperatively on issues, and in this Congress we have a record between our two committees of which we can be justifiably proud.

With respect to your analysis of the bill, I respectfully disagree with your assertion that the provision of the legislation regarding regulation of investment company names falls under the jurisdiction of the Committee on Banking and Financial Services. Under Rule X of the Rules of the House, the Commerce Committee is vested with jurisdiction over securities and exchanges. Under the same rule, the Banking Committee has supervisory jurisdiction over the entry by depository institutions into securities activities in connection with its jurisdiction over the safety and soundness of such institutions. It does not have jurisdiction over functional regulation of applicable securities laws not involving safety and soundness.

Under the relevant provision of H.R. 3005, the Securities and Exchange Commission is given express authority to regulate fraudulent or misleading names of investment companies by rule or by order pursuant to the Investment Company Act of 1940. Such action by the Commission constitutes an example of functional regulation of investment companies and the securities that they issue. The determination of what constitutes a fraudulent or misleading name for an investment company is a question of securities regulation, wholly independent of what entity may be advising or distributing those securities. although you point out that such regulation could have an impact on the business practices of banks that advise investment companies, such impact is not conceptually different from the impact of such regulation on any other entity that happens to advise an investment company.

I thank you again for your consideration.

Sincerely,

THOMAS J. BLILEY, Jr., *Chairman.*

AGENCY VIEWS

U.S. SECURITIES AND EXCHANGE COMMISSION,
Washington, DC, May 14, 1996.

Hon. THOMAS J. BLILEY, Jr.,
Chairman, Committee on Commerce, House of Representatives, Rayburn House Office Building, Washington, DC.

Hon. JACK FIELDS,
Chairman, Subcommittee on Telecommunications and Finance, Committee on Commerce, House of Representatives, Rayburn House Office Building, Washington, DC.

DEAR CHAIRMEN BLILEY AND FIELDS: On behalf of the U.S. Securities and Exchange Commission, I offer our support and endorsement for the Amendment in the Nature of a Substitute to H.R. 3005 to be offered by Mr. Bliley, “Securities Act Amendments of 1996.” You and your colleagues, Congressmen Dingell and Markey, have risen above the fray of partisan politics to produce a consensus bill that could well provide the regulatory framework for our markets as we enter the twenty-first century.

Chairman Fields’ introduction of the predecessor bill last July challenged the securities industry, its regulators, and all market participants to confront serious issues that must be addressed in order for the U.S. capital markets to remain preeminent. Your leadership inspired a constructive debate on issues such as coordination of state and federal securities laws and margin requirements. We will shortly forward to you the Commission's section-by-section analysis that expresses our understanding of the Bliley Amendment and how it would impact the Commission's work.

We commend your efforts on this important initiative. In addition, I compliment the superb staff work on both sides of the aisle—without which this effort would not have been achieved.

Sincerely,

ARTHUR LEVITT, *Chairman.*

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

SECURITIES ACT OF 1933

TITLE I

SHORT TITLE

SECTION 1. This title may be cited as the "Securities Act of 1933".

DEFINITIONS

SEC. 2. *(a) DEFINITIONS.*—When used in this title, unless the context otherwise requires—

(1) * * *

* * * * * * *

(b) CONSIDERATION OF PROMOTION OF EFFICIENCY, COMPETITION, AND CAPITAL FORMATION.—Whenever pursuant to this title the Commission is engaged in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.

* * * * * * *

[STATE CONTROL OF SECURITIES

[SEC. 18. Nothing in this title shall affect the jurisdiction of the securities commission (or any agency or office performing like functions) of any State or Territory of the United States, or the District of Columbia, over any security or any person.]

SEC. 18. EXEMPTION FROM STATE REGULATION OF SECURITIES OFFERINGS.

(a) SCOPE OF EXEMPTION.—Except as otherwise provided in this section, no law, rule, regulation, or order, or other administrative action of any State or Territory of the United States, or the District of Columbia, or any political subdivision thereof—

(1) requiring, or with respect to, registration or qualification of securities, or registration or qualification of securities transactions, shall directly or indirectly apply to a security that—

(A) is a covered security; or

(B) will be a covered security upon completion of the transaction;

(2) shall directly or indirectly prohibit, limit, or impose conditions upon the use of—

(A) with respect to a covered security described in subsection (b)(1) or (c)(1)—

(i) any offering document that is prepared by the issuer; or

(ii) any offering document that is not prepared by the issuer if such offering document is required to be and is filed with the Commission or any national securities organization registered under section 15A of the Securities Exchange Act of 1934 (15 U.S.C. 78o-3);

(B) with respect to a covered security described in paragraph (2), (3), or (4) of subsection (b), any offering document; or

(C) any proxy statement, report to shareholders, or other disclosure document relating to a covered security or the issuer thereof that is required to be and is filed with the Commission or any national securities organization registered under section 15A of the Securities Exchange Act of 1934 (15 U.S.C. 78o-3); or

(3) shall directly or indirectly prohibit, limit, or impose conditions, based on the merits of such offering or issuer, upon the offer or sale of any security described in paragraph (1).

(b) COVERED SECURITIES.—For purposes of this section, the following are covered securities:

(1) EXCLUSIVE FEDERAL REGISTRATION OF NATIONALLY TRADED SECURITIES.—A security is a covered security if such security is—

(A) listed, or authorized for listing, on the New York Stock Exchange or the American Stock Exchange, or included or qualified for inclusion in the National Market System of the National Association of Securities Dealers Automated Quotation System (or any successor to such entities);

(B) listed, or authorized for listing, on a national securities exchange (or tier or segment thereof) that has listing standards that the Commission determines by rule (on its own initiative or on the basis of a petition) are substantially similar to the listing standards applicable to securities described in subparagraph (A); or

(C) is a security of the same issuer that is equal in seniority or senior to a security described in subparagraph (A) or (B).

(2) EXCLUSIVE FEDERAL REGISTRATION OF INVESTMENT COMPANIES.—A security is a covered security if such security is a security issued by an investment company that is registered under the Investment Company Act of 1940 (15 U.S.C. 80a et seq.).

(3) SALES TO QUALIFIED PURCHASERS.—A security is a covered security with respect to the offer or sale of the security to qualified purchasers, as defined by the Commission by rule. In prescribing such rule, the Commission may define qualified pur-

chaser differently with respect to different categories of securities, consistent with the public interest and the protection of investors.

(4) EXEMPTION IN CONNECTION WITH CERTAIN EXEMPT OFFERINGS.—A security is a covered security if—

(A) the offer or sale of such security is exempt from registration under this title pursuant to section 4(1) or 4(3), and—

(i) the issuer of such security files reports with the Commission pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m, 78o(d)); or

(ii) the issuer is exempt from filing such reports;

(B) such security is exempt from registration under this title pursuant to section 4(4);

(C) the offer or sale of such security is exempt from registration under this title pursuant to section 3(a), other than the offer or sale of a security that is exempt from such registration pursuant to paragraph (4) or (11) of such section, except that a municipal security that is exempt from such registration pursuant to paragraph (2) of such section is not a covered security with respect to the offer or sale of such security in the State in which such security is issued; or

(D) the offer or sale of such security is exempt from registration under this title pursuant to Commission rule or regulation under section 4(2) of this title.

(c) CONDITIONALLY COVERED SECURITIES.—

(1) FEDERALLY REGISTERED OFFERINGS.—Subject to the limitations contained in paragraphs (2) and (3), a security is a covered security if—

(A) the issuer of such security has (or will have upon conclusion of the transaction) total assets exceeding $10,000,000;

(B) such security is the subject of a registration statement that is filed with the Commission pursuant to this title; and

(C) the issuer files with such registration statement audited financial statements for each of the two most recent fiscal years of its operations ending before the filing of the registration statement.

(2) LIMITATIONS FOR CERTAIN OFFERINGS.—Notwithstanding paragraph (1), a security is not a covered security if such security is—

(A) a security of an issuer which is a blank check company (as defined in section 7(b) of this title), a partnership, a limited liability company, or a direct participation investment program;

(B) a penny stock (as such term is defined in section 3(a)(51) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(51)); or

(C) a security issued in an offering relating to a rollup transaction (as such term is defined in paragraphs (4) and (5) of section 14(h) of such Act (15 U.S.C. 78n(h)(4), (5)).

(3) LIMITATIONS BASED ON MISCONDUCT.—Notwithstanding paragraph (1), a security is not a covered security—

(A) with respect to any State, if the issuer, or a principal officer or principal shareholder thereof—

(i) is subject to a statutory disqualification, as defined in subparagraph (A), (B), (C), or (D) of section 3(a)(39) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(39));

(ii) has been convicted within 5 years prior to the offering of any felony under Federal or State law in connection with the offer, purchase, or sale of any security, or any felony under Federal or State law involving fraud or deceit; or

(iii) is currently named in and subject to any order, judgment, or decree of any court of competent jurisdiction acting pursuant to Federal or State law temporarily or permanently restraining or enjoining such issuer, officer, or shareholder from engaging in or continuing any conduct or practice in connection with a security; or

(B) with respect to a particular State, if the issuer, or a principal officer or principal shareholder thereof—

(i) has filed a registration statement which is the subject of a currently effective stop order entered pursuant to that State's securities laws within 5 years prior to the offering;

(ii) is currently named in and subject to any administrative enforcement order or judgment of that State's securities commission (or any agency or office performing like functions) entered within 5 years prior to the offering, or is currently named in and subject to any other administrative enforcement order or judgment of that State entered within 5 years prior to the offering that finds fraud or deceit; or

(iii) is currently named in and subject to any administrative enforcement order or judgment of that State which prohibits or denies registration, or revokes the use of any exemption from registration, in connection with the offer, purchase, or sale of securities.

(4) EXCEPTIONS TO LIMITATIONS.—

(A) EXEMPTIONS.—The limitations in paragraph (3)(A) shall not apply if the Commission has exempted the subject person from the application of such paragraph by rule or order, and the limitations in paragraph (3)(B) shall not apply if the securities commission (or any agency or office performing like functions) of the affected State has exempted the subject person from the application of such paragraph by rule or order.

(B) REASONABLE STEPS.—The provisions of paragraph (3) shall not apply if the issuer has taken reasonable steps to ascertain whether any principal officer or principal shareholder is subject to such paragraph, and such steps do not reveal a person who is subject to such paragraph. An issuer shall be considered to have taken reasonable steps if such

issuer or its agent has conducted a search of any centralized data bases that the Commission may designate by rule, and has received an affidavit under oath by each such principal officer or principal shareholder stating that such officer or shareholder is not subject to the provisions of paragraph (3).

(C) EFFECT OF LIMITATIONS ON REMEDIES.—Notwithstanding paragraph (3), an issuer shall not be subject to a right of rescission under State securities laws solely as a result of the operation of such paragraph.

(5) NO EFFECT UNDER SUBSECTION (B).—No limitation under this subsection shall affect the treatment of a security that qualifies as a covered security under subsection (b).

(d) PRESERVATION OF AUTHORITY.—

(1) FRAUD AUTHORITY.—Consistent with this section, the securities commission (or any agency or office performing like functions) of any State or Territory of the United States, or the District of Columbia, shall retain jurisdiction under the laws of such State, Territory, or District to investigate and bring enforcement actions with respect to fraud or deceit in connection with securities or securities transactions.

(2) PRESERVATION OF FILING REQUIREMENTS.—

(A) NOTICE FILINGS PERMITTED.—Nothing contained in this section shall prohibit the securities commission (or any agency or office performing like functions) of any State or Territory of the United States, or the District of Columbia, from requiring the filing of any documents filed with the Commission pursuant to this title solely for notice purposes, together with any required fee.

(B) PRESERVATION OF FEES.—Until otherwise provided by State law enacted after the date of enactment of the Securities Amendments of 1996, filing or registration fees with respect to securities or securities transactions may continue to be collected in amounts determined pursuant to State law as in effect on the day before such date.

(C) FEES NOT PERMITTED ON LISTED SECURITIES.—Notwithstanding subparagraphs (A) and (B), no filing or fee may be required with respect to any security that is a covered security pursuant to subsection (b)(1) of this section, or will be such a covered security upon completion of the transaction, or is a security of the same issuer that is equal in seniority or senior to a security that is a covered security pursuant to such subsection.

(3) ENFORCEMENT OF REQUIREMENTS.—Nothing in this section shall prohibit the securities commission (or any agency or office performing like functions) of any State or Territory of the United States, or the District of Columbia, from suspending the offer or sale of securities within such State, Territory, or District as a result of the failure to submit any filing or fee required under law and permitted under this section.

(e) DEFINITIONS.—For purposes of this section:

(1) PRINCIPAL OFFICER.—The term "principal officer" means a director, chief executive officer, or chief financial officer of an issuer, or any other officer performing like functions.

(2) PRINCIPAL SHAREHOLDER.—The term "principal shareholder" means any person who is directly or indirectly the beneficial owner of more than 20 percent of any class of equity security of an issuer. When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed a "person" for purposes of this paragraph. In determining, for purposes of this paragraph, any percentage of a class of any security, such class shall be deemed to consist of the amount of the outstanding securities of such class, exclusive of any securities of such class held by or for the account of the issuer or a subsidiary of the issuer.

(3) OFFERING DOCUMENT.—The term "offering document" has the meaning given the term "prospectus" by section 2(10), but without regard to the provisions of clauses (a) and (b) of such section, except that, with respect to a security described in subsection (b)(2) of this section, such term also includes a communication that is not deemed to offer such a security pursuant to a rule of the Commission.

(4) PREPARED BY THE ISSUER.—Within 6 months after the date of enactment of the Securities Amendments of 1996, the Commission shall, by rule, define the term "prepared by the issuer" for purposes of this section.

* * * * * * *

SEC. 28. GENERAL EXEMPTIVE AUTHORITY.

The Commission, by rules and regulations, may conditionally or unconditionally exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of this title or of any rule or regulation thereunder, to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors.

* * * * * * *

SECURITIES EXCHANGE ACT OF 1934

TITLE I—REGULATION OF SECURITIES EXCHANGES

SHORT TITLE

SECTION 1. This Act may be cited as the "Securities Exchange Act of 1934".

* * * * * * *

DEFINITIONS AND APPLICATION OF TITLE

SEC. 3. (a) When used in this title, unless the context otherwise requires—

(1) * * *

* * * * * * *

(54) The term "examining authority" means any self-regulatory organization registered with the Commission under this title (other than registered clearing agencies) with the authority to examine, inspect, and otherwise oversee the activities of a registered broker or dealer.

* * * * * * *

(f) CONSIDERATION OF PROMOTION OF EFFICIENCY, COMPETITION, AND CAPITAL FORMATION.—Whenever pursuant to this title the Commission is engaged in rulemaking, or in the review of a rule of a self-regulatory organization, and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.

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MARGIN REQUIREMENTS

SEC. 7. (a) * * *

* * * * * * *

⟦(c) It shall be unlawful for any member of a national securities exchange or any broker or dealer, directly or indirectly, to extend or maintain credit or arrange for the extension or maintenance of credit to or for any customer—

⟦(1) on any security (other than an exempted security), in contravention of the rules and regulations which the Board of Governors of the Federal Reserve System shall prescribe under subsections (a) and (b) of this section;

⟦(2) without collateral or on any collateral other than securities, except in accordance with such rules and regulations as the Board of Governors of the Federal Reserve System may prescribe (A) to permit under specified conditions and for a limited period any such member, broker, or dealer to maintain a credit initially extended in conformity with the rules and regulations of the Board of Governors of the Federal Reserve System, and (B) to permit the extension or maintenance of credit in cases where the extension or maintenance of credit is not for the purpose of purchasing or carrying securities or of evading or circumventing the provisions of paragraph (1) of this subsection.

⟦(d) It shall be unlawful for any person not subject to subsection (c) of this section to extend or maintain credit or to arrange for the extension or maintenance of credit for the purpose of purchasing or carrying any security, in contravention of such rules and regulations as the Federal Reserve Board shall prescribe to prevent the excessive use of credit for the purchasing or carrying of or trading in securities in circumvention of the other provisions of this section. Such rules and regulations may impose upon all loans made for the purpose of purchasing or carrying securities limitations similar to those imposed upon members, brokers, or dealers by subsection (c) of this section and the rules and regulations thereunder. This subsection and the rules and regulations thereunder shall not apply (A) to a loan made by a person not in the ordinary course of his business, (B) to a loan on an exempted security, (C) to a loan to a dealer to aid in the financing of the distribution of securities to customers not through the medium of a national securities exchange, (D) to a loan by a bank on a security other than an equity security, or (E) to such other loans as the Federal Reserve Board shall, by such rules and regulations as it may deem necessary or appropriate in the public interest or for the protection of investors, exempt, either unconditionally or upon specified terms and conditions or for stated periods, from the operation of this subsection and the rules and regulations thereunder.]

(c) UNLAWFUL CREDIT EXTENSION TO CUSTOMERS.—

(1) PROHIBITION.—It shall be unlawful for any member of a national securities exchange or any broker or dealer, directly or indirectly, to extend or maintain credit or arrange for the extension or maintenance of credit to or for any customer—

(A) on any security (other than an exempted security), in contravention of the rules and regulations which the Board of Governors of the Federal Reserve System shall prescribe under subsections (a) and (b) of this section;

(B) without collateral or on any collateral other than securities, except in accordance with such rules and regulations as the Board of Governors of the Federal Reserve System may prescribe—

(i) to permit under specified conditions and for a limited period any such member, broker, or dealer to maintain a credit initially extended in conformity with the rules and regulations of the Board of Governors of the Federal Reserve System; and

(ii) to permit the extension or maintenance of credit in cases where the extension or maintenance of credit is not for the purpose of purchasing or carrying securities or of evading or circumventing the provisions of subparagraph (A) of this paragraph.

(2) EXCEPTION.—This subsection and the rules and regulations thereunder shall not apply to any credit extended, maintained, or arranged by a member of a national securities exchange or a broker or dealer to or for a member of a national securities exchange or a registered broker or dealer—

(A) a substantial portion of whose business consists of transactions with persons other than brokers or dealers; or

(B) to finance its activities as a market maker or an underwriter;

except that the Board of Governors of the Federal Reserve System may impose such rules and regulations, in whole or in part, on any credit otherwise exempted by this paragraph if it determines that such action is necessary or appropriate in the public interest or for the protection of investors.

(d) UNLAWFUL CREDIT EXTENSION IN VIOLATION OF RULES AND REGULATIONS; EXCEPTION TO APPLICATION OF RULES, ETC.—

(1) PROHIBITION.—It shall be unlawful for any person not subject to subsection (c) of this section to extend or maintain credit or to arrange for the extension or maintenance of credit for the purpose of purchasing or carrying any security, in contravention of such rules and regulations as the Board of Gov-

ernors of the Federal Reserve System shall prescribe to prevent the excessive use of credit for the purchasing or carrying of or trading in securities in circumvention of the other provisions of this section. Such rules and regulations may impose upon all loans made for the purpose of purchasing or carrying securities limitations similar to those imposed upon members, brokers, or dealers by subsection (c) of this section and the rules and regulations thereunder.

(2) EXCEPTIONS.—This subsection and the rules and regulations thereunder shall not apply to any credit extended, maintained, or arranged—

(A) by a person not in the ordinary course of business;

(B) on an exempted security;

(C) to or for a member of a national securities exchange or a registered broker or dealer—

(i) a substantial portion of whose business consists of transactions with persons other than brokers or dealers; or

(ii) to finance its activities as a market maker or an underwriter;

(D) by a bank on a security other than an equity security; or

(E) as the Board of Governors of the Federal Reserve System shall, by such rules, regulations, or orders as it may deem necessary or appropriate in the public interest or for the protection of investors, exempt, either unconditionally or upon specified terms and conditions or for stated periods, from the operation of this subsection and the rules and regulations thereunder;

except that the Board of Governors of the Federal Reserve System may impose such rules and regulations, in whole or in part, on any credit otherwise exempted by subparagraph (C) of this paragraph if it determines that such action is necessary or appropriate in the public interest or for the protection of investors.

* * * * * * *

RESTRICTIONS ON BORROWING BY MEMBERS, BROKERS, AND DEALERS

SEC. 8. It shall be unlawful for any registered broker or dealer, member of a national securities exchange, or broker or dealer who transacts a business in securities through the medium of any member of a national securities exchange, directly or indirectly—

⟦(a) To borrow in the ordinary course of business as a broker or dealer on any security (other than an exempted security) registered on a national securities exchange except (1) from or through a member bank of the Federal Reserve Board, (2) from any nonmember bank which shall have filed with the Federal Reserve Board an agreement, which is still in force and which is in the form prescribed by the Board, undertaking to comply with all provisions of this Act, the Federal Reserve Act, as amended, and the Banking Act of 1933, which are applicable to member banks and which relate to the use of credit to finance transactions in securities, and with such rules and regulations as may be prescribed pursuant to such provisions of law or for the purpose of preventing evasions thereof, or (3) in accordance with such rules and regulations as the Federal Reserve Board may prescribe to permit loans between such members and/or brokers and/or dealers, or to permit loans to meet emergency needs. Any such agreement filed with the Board of Governors of the Federal Reserve Board shall be subject to termination at any time by order of the Board, after appropriate notice and opportunity for hearing, because of any failure by such bank to comply with the provisions thereof or with such provisions of law or rules or regulations; and, for any willful violation of such agreement, such bank shall be subject to the penalties provided for violations of rules and regulations prescribed under this title. The provisions of sections 21 and 25 of this title shall apply in the case of any such proceeding or order of the Federal Reserve Board in the same manner as such provisions apply in the case of proceedings and orders of the Commission. Subject to such rules and regulations as the Board of Governors of the Federal Reserve System adopt in the public interest and for the protection of investors, no person shall be deemed to have borrowed within the ordinary course of business, within the meaning of this subsection, by reason of a bona fide agreement for delayed delivery of a mortgage related security or a small business related security against full payment of the purchase price thereof upon such delivery within one hundred and eighty days after the purchase, or within such shorter period as the Board of Governors of the Federal Reserve System may prescribe by rule or regulation.

[(b)**]** *(a)* In contravention of such rules and regulations as the Commission shall prescribe for the protection of investors to hypothecate or arrange for the hypothecation of any securities carried for the account of any customer under circumstances (1) that will permit the commingling of his securities without his written consent with the securities of any other customer, (2) that will permit such securities to be commingled with the securities of any person other than a bona fide customer, or (3) that will permit such securities to be hypothecated, or subjected to any lien or claim of the pledgee, for a sum in excess of the aggregate indebtedness of such customers in respect of such securities.

[(c)**]** *(b)* To lend or arrange for the lending of any securities carried for the account of any customer without the written consent of such customer or in contravention of such rules and regulations as the Commission shall prescribe for the protection of investors.

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REGISTRATION AND REGULATION OF BROKERS AND DEALERS

SEC. 15. (a) * * *

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(h) LIMITATIONS ON STATE LAW.—

(1) CAPITAL, MARGIN, BOOKS AND RECORDS, BONDING, AND REPORTS.—No law, rule, regulation, or order, or other administrative action of any State or political subdivision thereof shall establish capital, custody, margin, financial responsibility, making and keeping records, bonding, or financial or operational reporting requirements for brokers, dealers, municipal securities

dealers, government securities brokers, or government securities dealers that differ from, or are in addition to, the requirements in those areas established under this title. The Commission shall consult periodically the securities commissions (or any agency or office performing like functions) of the States concerning the adequacy of such requirements as established under this title.

(2) EXEMPTION TO PERMIT SERVICE TO CUSTOMERS.—No law, rule, regulation, or order, or other administrative action of any State or political subdivision thereof shall prohibit an associated person from effecting a transaction described in paragraph (3) for a customer in such State if—

(A) such associated person is not ineligible to register with such State for any reason other than such a transaction;

(B) such associated person is registered with a registered securities association and at least one State; and

(C) the broker or dealer with which such person is associated is registered with such State.

(3) DESCRIBED TRANSACTIONS.—A transaction is described in this paragraph if—

(A) such transaction is effected—

(i) on behalf of a customer that, for 30 days prior to the day of the transaction, maintains an account with the broker or dealer; and

(ii) by an associated person (I) to which the customer was assigned for 14 days prior to the day of the transaction, and (II) who is registered with a State in which the customer was a resident or was present for at least 30 consecutive days during the one-year period prior to the transaction;

except that, if the customer is present in another State for 30 or more consecutive days or has permanently changed his or her residence to another State, such transaction is not described in this subparagraph unless the associated person files with such State an application for registration within 10 business days of the later of the date of the transaction or the date of the discovery of the presence of the customer in the State for 30 or more consecutive days or the change in the customer's residence;

(B) the transaction is effected—

(i) on behalf of a customer that, for 30 days prior to the day of the transaction, maintains an account with the broker or dealer; and

(ii) within the period beginning on the date on which such associated person files with the State in which the transaction is effected an application for registration and ending on the earlier of (I) 60 days after the date the application is filed, or (II) the time at which such State notifies the associated person that it has denied the application for registration or has stayed the pendency of the application for cause; or

(C) the transaction is one of 10 or fewer transactions in a calendar year (excluding any transactions described in

subparagraph (A) or (B)) which the associated person effects in the States in which the associated person is not registered.

(4) ALTERNATE ASSOCIATED PERSONS.—For purposes of paragraph (3)(A)(ii), each of up to 3 associated persons who are designated to effect transactions during the absence or unavailability of the principal associated person for a customer may be treated as an associated person to which such customer is assigned for purposes of such paragraph.

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ACCOUNTS AND RECORDS, EXAMINATIONS OF EXCHANGES, MEMBERS, AND OTHERS

SEC. 17. (a) * * *

* * * * * * *

(i) COORDINATION OF EXAMINING AUTHORITIES.—

(1) ELIMINATION OF DUPLICATION.—The Commission and the examining authorities, through cooperation and coordination of examination and oversight as required by this subsection, shall eliminate any unnecessary and burdensome duplication in the examination process.

(2) PLANNING CONFERENCES.—

(A) The Commission and the examining authorities shall meet at least annually for a national general planning conference to discuss coordination of examination schedules and priorities and other areas of interest relevant to examination coordination and cooperation.

(B) Within each geographic region designated by the Commission, the Commission and the relevant examining authorities shall meet at least annually for a regional planning conference to discuss examination schedules and priorities and other areas of related interest, and to encourage information-sharing and to avoid unnecessary duplication of examinations.

(3) COORDINATION TRACKING SYSTEM FOR BROKER-DEALER EXAMINATIONS.—

(A) The Commission and the examining authorities shall prepare, on a periodic basis in a uniform computerized format, information on registered broker and dealer examinations and shall submit such information to the Commission.

(B) The Commission shall maintain a computerized database of consolidated examination information to be used for examination planning and scheduling and for monitoring coordination of registered broker and dealer examinations under this section.

(4) COORDINATION OF EXAMINATIONS.—

(A) The examining authorities shall share among themselves such information, including reports of examinations, customer complaint information, and other non-public regulatory information, as appropriate to foster a coordinated approach to regulatory oversight of registered brokers and

dealers subject to examination by more than one examining authority.

(B) To the extent practicable, the examining authorities shall assure that each registered broker and dealer subject to examination by more than one examining authority that requests a coordinated examination shall have all requested aspects of the examination conducted simultaneously and without duplication of the areas covered. The examining authorities shall also prepare an advance schedule of all such coordinated examinations.

(5) PROHIBITED NON-COORDINATED EXAMINATIONS.—Any examining authority that does not participate in a coordinated examination pursuant to paragraph (4) of this subsection shall not conduct a routine examination other than a coordinated examination of that broker or dealer within 9 months of the conclusion of a scheduled coordinated examination.

(6) EXAMINATIONS FOR CAUSE.—At any time, any examining authority may conduct an examination for cause of any broker or dealer subject to its jurisdiction.

(7) BROKER-DEALER EXAMINATION EVALUATION PANEL.—The Commission shall establish an examination evaluation panel composed of representatives of registered brokers and dealers that are members of more than one self-regulatory organization that conducts routine examinations. Prior to each national general planning conference required by paragraph (2)(A) of this subsection, the Commission shall convene the examination evaluation panel to review consolidated and statistical information on the coordination of examinations and information on examinations that are not coordinated, including the findings of Commission examiners on the effectiveness of the examining authorities in achieving coordinated examinations. The Commission shall present any findings and recommendations of the examination evaluation panel to the next meeting of the national general planning conference, and shall report back to the examination evaluation panel on the actions taken by the examining authorities regarding those findings and recommendations. The examination evaluation panel shall not be subject to the Federal Advisory Committee Act (5 U.S.C. App.).

(8) REPORT TO CONGRESS.—Within one year after the date of enactment of this Act, the Commission shall report to the Congress on the progress it and the examining authorities have made in reducing duplication and improving coordination in registered broker and dealer examinations, and on the activities of the examination evaluation panel. Such report shall also indicate whether the Commission has identified additional redundancies that have failed to be addressed in the coordination of examining authorities, or any recommendations of the examination evaluation panel established under paragraph (7) of this subsection that have not been addressed by the examining authorities or the Commission.

* * * * * * *

EFFECT ON EXISTING LAW

SEC. 28. (a) The rights and remedies provided by this title shall be in addition to any and all other rights and remedies that may exist at law or in equity; but no person permitted to maintain a suit for damages under the provisions of this title shall recover, through satisfaction of judgment in one or more actions, a total amount in excess of his actual damages on account of the act complained of. [Nothing] *Except as otherwise specifically provided elsewhere in this title, nothing* in this title shall affect the jurisdiction of the securities commission (or any agency or officer performing like functions) of any State over any security or any person insofar as it does not conflict with the provisions of this title or the rules and regulations thereunder. No State law which prohibits or regulates the making or promoting of wagering or gaming contracts, or the operation of "bucket shops" or other similar or related activities, shall invalidate any put, call, straddle, option, privilege, or other security, or apply to any activity which is incidental or related to the offer, purchase, sale, exercise, settlement, or closeout of any such instrument, if such instrument is traded pursuant to rules and regulations of a self-regulatory organization that are filed with the Commission pursuant to section 19(b) of this Act.

* * * * * * *

SEC. 36. GENERAL EXEMPTIVE AUTHORITY.

Notwithstanding any other provision of this title, the Commission, by rule, regulation, or order, may conditionally or unconditionally exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of this title or of any rule or regulation thereunder, to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors. The Commission shall by rules and regulations determine the procedures under which an exemptive order under this section shall be granted and may, in its sole discretion, decline to entertain any application for an order of exemption under this section.

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INVESTMENT COMPANY ACT OF 1940

TITLE I—INVESTMENT COMPANIES

* * * * * * *

GENERAL DEFINITIONS

SEC. 2. (a) When used in this title, unless the context otherwise requires—

(1) * * *

* * * * * * *

(51) "Qualified purchaser" means—

(A) any natural person who owns at least $10,000,000 in securities of issuers that are not controlled by such person, except that securities of such a controlled issuer may be

counted toward such amount if such issuer is, or but for the exception in paragraph (1) or (7) of section 3(c) would be, an investment company;

(B) any trust not formed for the specific purpose of acquiring the securities offered, as to which the trustee or other person authorized to make decisions with respect to the trust, and each settlor or other person who has contributed assets to the trust, is a person described in subparagraph (A) or (C); or

(C) any person, acting for its own account or the accounts of other qualified purchasers, who in the aggregate owns and invests on a discretionary basis, not less than $100,000,000 in securities of issuers that are not affiliated persons (as defined in paragraph (3)(C) of this subsection) of such person, except that securities of such an affiliated person issuer may be counted toward such amount if such issuer is, or but for the exception in paragraph (1) or (7) of section 3(c) would be, an investment company.

The Commission may adopt such rules and regulations governing the persons and trusts specified in subparagraphs (A), (B), and (C) of this paragraph as it determines are necessary or appropriate in the public interest and for the protection of investors.

* * * * * * *

(c) CONSIDERATION OF PROMOTION OF EFFICIENCY, COMPETITION, AND CAPITAL FORMATION.—Whenever pursuant to this title the Commission is engaged in rulemaking and is required to consider or determine whether an action is consistent with the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.

DEFINITION OF INVESTMENT COMPANY

SEC. 3. (a) When used in this title, "investment company" means any issuer which—

(1) * * *

* * * * * * *

As used in this section, "investment securities" includes all securities except (A) Government securities, (B) securities issued by employees' securities companies, and (C) securities issued by majority-owned subsidiaries of the owner *(i)* which are not investment companies*, and (ii) which are not relying on the exception from the definition of investment company in subsection (c)(1) or (c)(7) of this section*.

* * * * * * *

(c) Notwithstanding subsection (a), none of the following persons is an investment company within the meaning of this title:

(1) Any issuer whose outstanding securities (other than short-term paper) are beneficially owned by not more than one hundred persons and which is not making and does not presently propose to make a public offering of its securities. *Such issuer nonetheless is deemed to be an investment company for*

purposes of the limitations set forth in section 12(d)(1)(A)(i) and (B)(i) governing the purchase or other acquisition by such issuer of any security issued by any registered investment company and the sale of any security issued by any registered open-end company to any such issuer. For purposes of this paragraph:

(A) Beneficial ownership by a company shall be deemed to be beneficial ownership by one person, except that, if the company owns 10 per centum or more of the outstanding voting securities of the issuer, *and is or, but for the exception in this paragraph or paragraph (7), would be an investment company,* the beneficial ownership shall be deemed to be that of the holders of such company's outstanding securities (other than short-term paper) **[**unless, as of the date of the most recent acquisition by such company of securities of that issuer, the value of all securities owned by such company of all issuers which are or would, but for the exception set forth in this subparagraph, be excluded from the definition of investment company solely by this paragraph, does not exceed 10 per centum of the value of the company's total assets. Such issuer nonetheless is deemed to be an investment company for purposes of section 12(d)(1).**]**.

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(2) Any person primarily engaged in the business of underwriting and distributing securities issued by other persons, selling securities to customers, **[**and acting as broker,**]** *acting as broker, and acting as market intermediary,* or any one or more of such activities, whose gross income normally is derived principally from such business and related activities. *For the purposes of this paragraph, the term "market intermediary" means any person that regularly holds itself out as being willing contemporaneously to engage in, and is regularly engaged in the business of entering into, transactions on both sides of the market for a financial contract or one or more such financial contracts. For purposes of the preceding sentence, the term "financial contract" means any arrangement that (A) takes the form of an individually negotiated contract, agreement, or option to buy, sell, lend, swap, or repurchase, or other similar individually negotiated transaction commonly entered into by participants in the financial markets; (B) is in respect of securities, commodities, currencies, interest or other rates, other measures of value, or any other financial or economic interest similar in purpose or function to any of the foregoing; and (C) is entered into in response to a request from a counterparty for a quotation or is otherwise entered into and structured to accommodate the objectives of the counterparty to such arrangement.*

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[(7) Reserved.**]**

(7)(A) Any issuer (i) whose outstanding securities are owned exclusively by persons who, at the time of acquisition of such securities, are qualified purchasers, and (ii) who is not making and does not presently propose to make a public offering of such securities. Securities that are owned by persons who received

the securities from a qualified purchaser as a gift or bequest, or where the transfer was caused by legal separation, divorce, death, or other involuntary event, shall be deemed to be owned by a qualified purchaser, subject to such rules, regulations, and orders as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(B) Notwithstanding subparagraph (A), an issuer is within the exception provided by this paragraph if—

(i) in addition to qualified purchasers, its outstanding securities are beneficially owned by not more than 100 persons who are not qualified purchasers if (I) such persons acquired such securities on or before December 31, 1995, and (II) at the time such securities were acquired by such persons, the issuer was excepted by paragraph (1) of this subsection; and

(ii) prior to availing itself of the exception provided by this paragraph—

(I) such issuer has disclosed to such persons that future investors will be limited to qualified purchasers, and that ownership in such issuer is no longer limited to not more than 100 persons, and

(II) concurrently with or after such disclosure, such issuer has provided such persons with a reasonable opportunity to redeem any part or all of their interests in the issuer for their proportionate share of the issuer's current net assets, or the cash equivalent thereof.

(C) An issuer that is excepted under this paragraph shall nonetheless be deemed to be an investment company for purposes of the limitations set forth in section 12(d)(1)(A)(i) and (B)(i) governing the purchase or other acquisition by such issuer of any security issued by any registered investment company and the sale of any security issued by any registered open-end company to any such issuer.

(D) For purposes of determining compliance with this paragraph and paragraph (1) of this subsection, an issuer that is otherwise excepted under this paragraph and an issuer that is otherwise excepted under paragraph (1) shall not be treated by the Commission as being a single issuer for purposes of determining whether the outstanding securities of the issuer excepted under paragraph (1) are beneficially owned by not more than 100 persons or whether the outstanding securities of the issuer excepted under this paragraph are owned by persons that are not qualified purchasers. Nothing in this provision shall be deemed to establish that a person is a bona fide qualified purchaser for purposes of this paragraph or a bona fide beneficial owner for purposes of paragraph (1) of this subsection.

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FUNCTIONS AND ACTIVITIES OF INVESTMENT COMPANIES

SEC. 12. (a) * * *

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(d)(1)(A) * * *

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(E) The provisions of this paragraph (1) shall not apply to a security (or securities) purchased or acquired by an investment company if—

(i) the depositor of, or principal underwriter for, such investment company is a broker or dealer registered under the Securities Exchange Act of 1934, or a person controlled by such a broker or dealer;

(ii) such security is the only investment security held by such investment company (or such securities are the only investment securities held by such investment company, if such investment company is a registered unit investment trust that issues two or more classes or series of securities, each of which provides for the accumulation of shares of a different investment company); and

(iii) [in the event such investment company is not a registered investment company,] the purchase or acquisition is made pursuant to an arrangement with the issuer of, or principal underwriter for the issuer of, the security whereby such investment company is obligated—

(aa) either to seek instructions from its security holders with regard to the voting of all proxies with respect to such security and to vote such proxies only in accordance with such instructions, or to vote the shares held by it in the same proportion as the vote of all other holders of such security, and

(bb) *in the event such investment company is not a registered investment company* to refrain from substituting such security unless the Commission shall have approved such substitution in the manner provided in section 26 of this Act.

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(G) The provisions of this paragraph (1) shall not apply to securities of a registered open-end company (the "acquired company") purchased or otherwise acquired by a registered open-end company (the "acquiring company") if—

(i) the acquired company and the acquiring company are part of the same group of investment companies;

(ii) the securities of the acquired company, securities of other registered open-end companies that are part of the same group of investment companies, Government securities, and short-term paper are the only investments held by the acquiring company;

(iii)(I) the acquiring company does not pay and is not assessed any charges or fees for distribution-related activities with respect to securities of the acquired company unless the acquiring company does not charge a sales load or other fees or charges for distribution-related activities; or

(II) any sales loads and other distribution-related fees charged with respect to securities of the acquiring company, when aggregated with any sales load and distribution-related fees paid by the acquiring company with respect to securities of the acquired company, are not excessive under rules adopted

pursuant to either section 22(b) or section 22(c) of this title by a securities association registered under section 15A of the Securities Exchange Act of 1934 or the Commission;

(iv) the acquired company shall have a fundamental policy that prohibits it from acquiring any securities of registered open-end companies in reliance on this subparagraph or subparagraph (F) of this subsection; and

(v) such acquisition is not in contravention of such rules and regulations as the Commission may from time to time prescribe with respect to acquisitions in accordance with this subparagraph as necessary and appropriate for the protection of investors.

For purposes of this subparagraph, a "group of investment companies" shall mean any two or more registered investment companies that hold themselves out to investors as related companies for purposes of investment and investor services.

[(G)**]** *(H)* For the purposes of this paragraph (1), the value of an investment company's total assets shall be computed as of the time of a purchase or acquisition or as closely thereto as is reasonably possible.

[(H)**]** *(I)* In any action brought to enforce the provisions of this paragraph (1), the Commission may join as a party the issuer of any security purchased or otherwise acquired in violation of this paragraph (1), and the court may issue any order with respect to such issuer as may be necessary or appropriate for the enforcement of the provisions of this paragraph (1).

(J) The Commission, by rules and regulations upon its own motion or by order upon application, may conditionally or unconditionally exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions from any provisions of this subsection, if and to the extent such exemption is consistent with the public interest and the protection of investors.

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REGISTRATION OF SECURITIES UNDER SECURITIES ACT OF 1933

SEC. 24. (a) * * *

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[(e)(1) A registration statement under the Securities Act of 1933 relating to a security issued by a face-amount certificate company or a redeemable security issued by an open-end management company or unit investment trust may be amended after its effective date so as to increase the securities specified therein as proposed to be offered. At the time of filing such amendment there shall be paid to the Commission a fee, calculated in the manner specified in section 6(b) of said Act, with respect to the additional securities therein proposed to be offered.

[(2) The filing of such an amendment to a registration statement under the Securities Act of 1933 shall not be deemed to have taken place unless it is accompanied by a United States postal money order or a certified bank check or cash for the amount of the fee required under paragraph (1) of this subsection.**]**

[(3)**]** *(e)* For the purposes of section 11 of the Securities Act of 1933, as amended, the effective date of the latest amendment filed [pursuant to this subsection or otherwise] shall be deemed the effective date of the registration statement with respect to securities sold after such amendment shall have become effective. For the purposes of section 13 of the Securities Act of 1933, as amended, no such security shall be deemed to have been bona fide offered to the public prior to the effective date of the latest amendment filed pursuant to this subsection. Except to the extent the Commission otherwise provides by rules or regulations as appropriate in the public interest or for the protection of investors, no prospectus relating to a security issued by a face-amount certificate company or a redeemable security issued by an open-end management company or unit investment trust which varies for the purposes of subsection (a)(3) of section 10 of the Securities Act of 1933 from the latest prospectus filed as a part of the registration statement shall be deemed to meet the requirements of said section 10 unless filed as part of an amendment to the registration statement under said Act and such amendment has become effective.

[(f) In the case of securities issued by a face-amount certificate company or redeemable securities issued by an open-end management company or unit investment trust, which are sold in an amount in excess of the number of securities included in an effective registration statement of any such company, such company may, in accordance with such rules and regulations as the Commission shall adopt as it deems necessary or appropriate in the public interest or for the protection of investors, elect to have the registration of such securities deemed effective as of the time of their sale, upon payment to the Commission, within six months after any such sale, of a registration fee of three times the amount of the fee which would have otherwise been applicable to such securities. Upon any such election and payment, the registration statement of such company shall be considered to have been in effect with respect to such shares. The Commission may also adopt rules and regulations as it deems necessary or appropriate in the public interest or for the protection of investors to permit the registration of an indefinite number of the securities issued by a face-amount certificate company or redeemable securities issued by an open-end management company or unit investment trust.]

(f) REGISTRATION OF INDEFINITE AMOUNT OF SECURITIES.—

(1) INDEFINITE REGISTRATION OF SECURITIES.—Upon the effectiveness of its registration statement under the Securities Act of 1933, a face-amount certificate company, open-end management company, or unit investment trust shall be deemed to have registered an indefinite amount of securities.

(2) PAYMENT OF REGISTRATION FEES.—Within 90 days after the end of the company's fiscal year, the company shall pay a registration fee to the Commission, calculated in the manner specified in section 6(b) of the Securities Act of 1933, based on the aggregate sales price for which its securities (including, for this purpose, all securities issued pursuant to a dividend reinvestment plan) were sold pursuant to a registration of an indefinite amount of securities under this subsection during the company's previous fiscal year reduced by—

(A) the aggregate redemption or repurchase price of the securities of the company during that year, and

(B) the aggregate redemption or repurchase price of the securities of the company during any prior fiscal year ending not more than 1 year before the date of enactment of the Investment Company Act Amendments of 1996 that were not used previously by the company to reduce fees payable under this section.

(3) INTEREST DUE ON LATE PAYMENT.—A company paying the fee or any portion thereof more than 90 days after the end of the company's fiscal year shall pay to the Commission interest on unpaid amounts, compounded daily, at the underpayment rate established by the Secretary of the Treasury pursuant to section 3717(a) of title 31, United States Code. The payment of interest pursuant to the requirement of this paragraph shall not preclude the Commission from bringing an action to enforce the requirements of paragraph (2) of this subsection.

(4) RULEMAKING AUTHORITY.—The Commission may adopt rules and regulations to implement the provisions of this subsection.

(g) In addition to the prospectuses permitted or required in section 10 of the Securities Act of 1933, the Commission shall permit, by rules or regulations deemed necessary or appropriate in the public interest or for the protection of investors, the use of a prospectus for the purposes of section 5(b)(1) of such Act with respect to securities issued by a registered investment company. Such a prospectus, which may include information the substance of which is not included in the prospectus specified in section 10(a) of the Securities Act of 1933, shall be deemed to be permitted by section 10(b) of such Act.

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UNIT INVESTMENT TRUSTS

SEC. 26. (a) * * *

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(e)(1) Subsection (a) shall not apply to any registered separate account funding variable insurance contracts, or to the sponsoring insurance company and principal underwriter of such account.

(2) It shall be unlawful for any registered separate account funding variable insurance contracts, or for the sponsoring insurance company of such account, to sell any such contract, unless—

(A) the fees and charges deducted under the contract in the aggregate are reasonable in relation to the services rendered, the expenses expected to be incurred, and the risks assumed by the insurance company, and the insurance company so represents in the registration statement for the contract; and

(B) the insurance company (i) complies with all other applicable provisions of this section as if it were a trustee or custodian of the registered separate account; (ii) files with the insurance regulatory authority of a State an annual statement of its financial condition, which most recent statement indicates that it has a combined capital and surplus, if a stock company, or an unassigned surplus, if a mutual company, of not less than $1,000,000, or such other amount as the Commission may from time to time prescribe by rule as necessary or appropriate in the

public interest or for the protection of investors; and (iii) together with its registered separate accounts, is supervised and examined periodically by the insurance authority of such State.

(3) The Commission may adopt such rules and regulations under paragraph (2)(A) as it determines are necessary or appropriate in the public interest or for the protection of investors. For the purposes of such paragraph, the fees and charges deducted under the contract shall include all fees and charges imposed for any purpose and in any manner.

PERIODIC PAYMENT PLANS

SEC. 27. (a) * * *

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(i)(1) This section shall not apply to any registered separate account funding variable insurance contracts, or to the sponsoring insurance company and principal underwriter of such account, except as provided in paragraph (2).

(2) It shall be unlawful for any registered separate account funding variable insurance contracts, or for the sponsoring insurance company of such account, to sell any such contract unless (A) such contract is a redeemable security, and (B) the insurance company complies with section 26(e) and any rules or regulations adopted by the Commission thereunder.

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PERIODIC AND OTHER REPORTS; REPORTS OF AFFILIATED PERSONS

SEC. 30. (a) * * *

(b) Every registered investment company shall file with the Commission—

[(1) such information and documents (other than financial statements) as the Commission may require, on a semi-annual or quarterly basis, to keep reasonably current the information and documents contained in the registration statement of such company filed under this title; and]

(1) such information, documents, and reports (other than financial statements), as the Commission may require to keep reasonably current the information and documents contained in the registration statement of such company filed under this title; and

* * * * * * *

(c) In exercising its authority under subsection (b)(1) to require the filing of information, documents, and reports on a basis more frequently than semi-annually, the Commission shall take such steps as it deems necessary or appropriate, consistent with the public interest and the protection of investors, to avoid unnecessary reporting by, and minimize the compliance burdens on, registered investment companies and their affiliated persons. Such steps shall include considering and requesting public comment on—

(1) feasible alternatives that minimize the reporting burdens on registered investment companies; and

(2) the utility of such information, documents, and reports to the Commission in relation to the costs to registered investment

companies and their affiliated persons of providing such information, documents, and reports.

[(c)] *(d)* The Commission shall issue rules and regulations permitting the filing with the Commission, and with any national securities exchange concerned, of copies of periodic reports, or of extracts therefrom, filed by any registered investment company pursuant to subsections (a) and (b), in lieu of any reports and documents required of such company under section 13 or 15(d) of the Securities Exchange Act of 1934.

[(d)] *(e)* Every registered investment company shall transmit to its stockholders, at least semi-annually, reports containing such of the following information and financial statements or their equivalent, as of a reasonably current date, as the Commission may prescribe by rules and regulations for the protection of investors, which reports shall not be misleading in any material respect in the light of the reports required to be filed pursuant to subsections (a) and (b):

(1) * * *

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(f) The Commission may by rule require that semi-annual reports containing the information set forth in subsection (e) include such other information as the Commission deems necessary or appropriate in the public interest or for the protection of investors. In exercising its authority under this subsection, the Commission shall take such steps as it deems necessary or appropriate, consistent with the public interest and the protection of investors, to avoid unnecessary reporting by, and minimize the compliance burdens on, registered investment companies and their affiliated persons. Such steps shall include considering and requesting public comment on—

(1) feasible alternatives that minimize the reporting burdens on registered investment companies; and

(2) the utility of such information to shareholders in relation to the costs to registered investment companies and their affiliated persons of providing such information

[(e)] *(g)* Financial statements contained in annual reports required pursuant to subsections (a) and [(d)] *(e)*, if required by the rules and regulations of the Commission, shall be accompanied by a certificate of independent public accountants. The certificate of such independent public accountants shall be based upon an audit not less in scope or procedures followed than that which independent public accountants would ordinarily make for the purpose of presenting comprehensive and dependable financial statements, and shall contain such information as the Commission may prescribe, by rules and regulations in the public interest or for the protection of investors, as to the nature and scope of the audit and the findings and opinion of the accountants. Each such report shall state that such independent public accountants have verified securities owned, either by actual examination, or by receipt of a certificate from the custodian, as the Commission may prescribe by rules and regulations.

[(f)] *(h)* Every person who is directly or indirectly the beneficial owner of more than 10 per centum of any class of outstanding securities (other than short-term paper) of which a registered closed-end company is the issuer or who is an officer, director, member of an advisory board, investment adviser, or affiliated person of an investment adviser of such a company shall in respect of his transactions in any securities of such company (other than short-term paper) be subject to the same duties and liabilities as those imposed by section 16 of the Securities Exchange Act of 1934 upon certain beneficial owners, directors, and officers in respect of their transactions in certain equity securities.

ACCOUNTS AND RECORDS

SEC. 31. ⟦(a) Every registered investment company, and every underwriter, broker, dealer, or investment adviser which is a majority-owned subsidiary of such a company, shall maintain and preserve for such period or periods as the Commission may prescribe by rules and regulations, such accounts, books, and other documents as constitute the record forming the basis for financial statements required to be filed pursuant to section 30 of this title, and of the auditor's certificates relating thereto. Every investment adviser not a majority-owned subsidiary of, and every depositor of any registered investment company, and every principal underwriter for any registered investment company other than a closed-end company, shall maintain and preserve for such period or periods as the Commission shall prescribe by rules and regulations, such accounts, books, and other documents as are necessary or appropriate to record such person's transactions with such registered company.

⟦(b) All accounts, books, and other records, required to be maintained and preserved by any person pursuant to subsection (a), shall be subject at any time and from time to time to such reasonable periodic, special, and other examinations by the Commission, or any member or representative thereof, as the Commission may prescribe. Any such person shall furnish to the Commission, within such reasonable time as the Commission may prescribe, copies of or extracts from such records which may be prepared without undue effort, expense, or delay, as the Commission may by order require.⟧ *(a) Every registered investment company, and every underwriter, broker, dealer, or investment adviser that is a majority-owned subsidiary of such a company, shall maintain and preserve such records (as defined in section 3(a)(37) of the Securities Exchange Act of 1934) for such period or periods as the Commission, by rules and regulations, may prescribe as necessary or appropriate in the public interest or for the protection of investors. Every investment adviser not a majority-owned subsidiary of, and every depositor of any registered investment company, and every principal underwriter for any registered investment company other than a closed-end company, shall maintain and preserve for such period or periods as the Commission shall prescribe by rules and regulations, such records as are necessary or appropriate to record such person's transactions with such registered company. In exercising its authority under this subsection, the Commission shall take such steps as it deems necessary or appropriate, consistent with the public interest and for the protection of investors, to avoid unnecessary recordkeeping by, and minimize the compliance burden on, persons required to maintain records under this subsection (hereinafter in this* *section referred to as "subject persons"). Such steps shall include considering, and requesting public comment on—*

(1) feasible alternatives that minimize the recordkeeping burdens on subject persons;

(2) the necessity of such records in view of the public benefits derived from the independent scrutiny of such records through Commission examination;

(3) the costs associated with maintaining the information that would be required to be reflected in such records; and

(4) the effects that a proposed recordkeeping requirement would have on internal compliance policies and procedures.

(b) All records required to be maintained and preserved in accordance with subsection (a) of this section shall be subject at any time and from time to time to such reasonable periodic, special, and other examinations by the Commission, or any member or representative thereof, as the Commission may prescribe. For purposes of such examinations, any subject person shall make available to the Commission or its representatives any copies or extracts from such records as may be prepared without undue effort, expense, or delay as the Commission or its representatives may reasonably request. The Commission shall exercise its authority under this subsection with due regard for the benefits of internal compliance policies and procedures and the effective implementation and operation thereof.

(c) Notwithstanding any other provision of law, the Commission shall not be compelled to disclose any internal compliance or audit records, or information contained therein, provided to the Commission under this section. Nothing in this subsection shall authorize the Commission to withhold information from Congress or prevent the Commission from complying with a request for information from any other Federal department or agency requesting the information for purposes within the scope of its jurisdiction, or complying with an order of a court of the United States in an action brought by the United States or the Commission. For purposes of section 552 of title 5, United States Code, this section shall be considered a statute described in subsection (b)(3)(B) of such section 552.

(d) For purposes of this section—

(1) "internal compliance policies and procedures" means policies and procedures designed by subject persons to promote compliance with the Federal securities laws; and

(2) "internal compliance and audit record" means any record prepared by a subject person in accordance with internal compliance policies and procedures.

[(c)**]** *(e)* The Commission may, in the public interest or for the protection of investors, issue rules and regulations providing for a reasonable degree of uniformity in the accounting policies and principles to be followed by registered investment companies in maintaining their accounting records and in preparing financial statements required pursuant to this title.

[(d)**]** *(f)* The Commission, upon application made by any registered investment company, may by order exempt a specific transaction or transactions from the provisions of any rule or regulation made pursuant to subsection (c), if the Commission finds that such rule or regulation should not reasonably be applied to such transaction.

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UNLAWFUL REPRESENTATIONS AND NAMES

SEC. 35. (a) * * *

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【(d) It shall be unlawful for any registered investment company hereafter to adopt as a part of the name or title of such company, or of any security of which it is the issuer, any word or words which the Commission finds and by order declares to be deceptive or misleading. The Commission is authorized to bring an action in the proper district court of the United States or United States court of any Territory or other place subject to the jurisdiction of the United States alleging that the name or title of any registered investment company, or of any security which it has issued, is materially deceptive or misleading. If the court finds that the Commission's allegations in this respect, taking into consideration the history of the investment company and the length of time which it may have used any such name or title, are established, the court shall enjoin such investment company from continuing to use any such name or title.】

(d) It shall be unlawful for any registered investment company to adopt as a part of the name or title of such company, or of any securities of which it is the issuer, any word or words that the Commission finds are materially deceptive or misleading. The Commission is authorized, by rule, regulation, or order, to define such names or titles as are materially deceptive or misleading.

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