

PROTECTING ADVICE FOR SMALL SAVERS ACT OF 2017

—————
AUGUST 10, 2018.—Ordered to be printed
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Mr. HENSARLING, from the Committee on Financial Services,
submitted the following

R E P O R T

together with

MINORITY VIEWS

[To accompany H.R. 3857]

[Including cost estimate of the Congressional Budget Office]

The Committee on Financial Services, to whom was referred the bill (H.R. 3857) to amend the Securities Exchange Act of 1934 to establish standards of conduct for brokers and dealers that are in the best interest of their retail customers, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

PURPOSE AND SUMMARY

On September 27, 2017, Representative Ann Wagner introduced the “Protecting Advice for Small Savers Act of 2017”, or “PASS Act”, which repeals the final rule of the U.S. Department of Labor (DOL) titled “Definition of the Term ‘Fiduciary’ Conflict of Interest Rule—Retirement Investment Advice” and related prohibited transaction exemptions published on April 8, 2016. The bill also amends the second subsection (k) of Section 15 of the Securities Exchange Act of 1934 to require a broker-dealer to act in the retail customer’s best interest when providing a recommendation, which must reflect (i) reasonable diligence and (ii) the reasonable care, skill, and prudence that a broker-dealer would exercise based on the customer’s investment profile. The bill also requires a broker-dealer to provide increased disclosures to the customer before the broker-dealer may purchase a securities product on behalf of that customer, including disclosures regarding the type and scope of services the broker-

dealer provides, the standard of conduct that applies to the relationship, the types of compensation the broker-dealer receives, and any material conflict of interest.

BACKGROUND AND NEED FOR LEGISLATION

On February 23, 2015, President Obama announced his support for the DOL to issue rules—which is not the agency designated by Congress to oversee and regulate investment advice regarding securities—to amend the definition of “investment advice” to expand the class of financial professionals subject to fiduciary duties covered by the Employee Retirement Income Security Act (ERISA) for the purpose of curbing the effects of perceived conflicts of interest in the marketing and development of retirement investments. In support of this proposal, President Obama, the DOL, and investor advocates claimed that: (i) current consumer protections for investment advice in the retail and small retirement plan markets are inadequate; and (ii) the current regulatory environment creates perverse incentives that ultimately cost retirement savers billions of dollars a year. According to President Obama’s White House, the DOL’s proposal sought “to crack down on irresponsible behavior in today’s market for financial advice by better aligning the rules between employer-based retirement savings plans and IRAs.”

The DOL estimated that conflicted advice by broker-dealers costs retirees about \$17 billion in lost returns annually. No study directly supports this estimation, however; and the number instead comes from a flawed calculation by the proposal’s proponents who couple unsupported generalizations and extrapolations with other empirical data to reach a desired result. At a September 10, 2015, joint hearing of the Subcommittees on Capital Markets and Government Sponsored Entities and Oversight and Investigations about the consequences of the DOL’s proposal, Paul Stevens, the CEO of the Investment Company Institute, testified:

Regardless of the number used—\$17 billion or \$18 billion per year—the claims have no basis. The calculations underlying these numbers misinterpret and incorrectly apply the findings of the very same academic research cited as the foundation of the claims, and do not consider the significant harm to retirement savers that is sure to result if the Department adopts the rules as currently drafted. In fact, these assertions do not stand up when tested against actual experience and data. Correcting for the Department’s many errors and omissions, we find that the Department’s proposal, if adopted, will result in net losses to investors of \$109 billion over 10 years.

On April 20, 2015, the DOL issued a Notice of Proposed Rule-making that sought public comment on its proposed amendments to the definition of a fiduciary and related exemptions. The DOL received significant opposition to the proposed rule, and many market participants believed that the proposal was unworkable as drafted and could negatively impact \$17.6 trillion in retirement assets, harm investors, and disrupt the U.S. capital markets. The DOL proposal, as drafted, was not business-neutral and was grounded in the misguided notion that for every investor charging

fees based on the amount of assets under management is superior in every respect to charging commission-based fees.

Critics of the DOL proposal also pointed out that the Securities and Exchange Commission (SEC) is the agency that Congress designated to oversee and regulate the conduct of persons providing investment advice and effecting securities transactions in the United States. Title IX of the Dodd-Frank Act provided authority to harmonize the standards applicable to broker-dealers and investment advisers. Section 913 of the Dodd-Frank Act required the SEC to report to the House Financial Services and Senate Banking Committee on the standards of care applicable to broker-dealers and investment advisers. Additionally, Section 913 permits—but does not require—the SEC to issue rules that address these standards of care.

Accordingly, the DOL should not define how an investor receives financial advice. On June 17, 2015, former Secretary of Labor Thomas Perez testified before the House Committee on Education and the Workforce that the DOL had coordinated with the SEC in the development of the fiduciary duty proposal and that the staffs of the two agencies had worked closely throughout the drafting process. But former SEC Commissioner Daniel Gallagher contradicted this assertion, who said in his comment letter to the proposed rule that he was not included in any conversations about the DOL rulemaking. Former Commissioner Gallagher further commented that “[f]rom a distance—a place where a presidentially-appointed SEC Commissioner should not be in this context—it appears that any interaction between staffs at DOL and the SEC and all of these discussions with [then-SEC] Chair White have borne no fruit.” Further undermining Secretary Perez’s assertions is a February 2016 Senate Homeland Security and Government Affairs staff report, which revealed that DOL prioritized expediency in quickly issuing the rulemaking over expressed policy concerns about the rule from career, non-partisan professional staff at the SEC, regulatory experts at the Office of Information and Regulatory Affairs (OIRA) within the Office of Management and Budget (OMB), and officials at the Department of Treasury. As noted above, the proposed rule does not contemplate or even mention potential SEC rules or the SEC’s existing regime for regulating broker-dealers and investment advisers.

Furthermore, Congress has mandated that any registered broker or dealer must be a member of a registered securities association—in this case, the Financial Industry Regulatory Authority (FINRA). The federal securities laws and FINRA rules comprehensively regulate all aspects of a broker-dealer’s business. Among the many requirements enforced by FINRA are that broker-dealers deal fairly with customers, adhere to just and equitable principles of trade, and ensure that recommendations are suitable for customers. Broker-dealers also must establish rigorous systems for compliance and supervision, which are examined regularly by FINRA and the SEC—facts the DOL ignored.

On February 3, 2017, President Trump signed an executive memorandum that ordered the DOL to review its fiduciary rule and whether it “may adversely affect the ability of Americans to gain access to retirement information and financial advice.” The rule’s expanded fiduciary definition and Impartial Conduct Stand-

ards went into effect on June 9, 2017, and the remaining rule’s requirements, such as the Best Interest Contract exemption, has been delayed until July 1, 2019, while the DOL continues to review the rule.

If changes are necessary to the delivery of financial advice, the capital markets regulatory authorities should undertake the action necessary to address any perceived inadequacies to protect investors of all sizes—not the DOL. On June 1, 2017, Chairman Jay Clayton issued a request for public comment regarding the standards of conduct applicable to investment advisers and broker-dealers to assess the current regulatory framework to guide any potential SEC regulatory actions.

Several notable events occurred subsequent to the Committee’s action to report H.R. 3857 to the House with a favorable recommendation. On March 15, 2018, the U.S. Court of Appeals for the 5th Circuit ruled, in a 2-to-1 decision¹, that the DOL abused its authority and acted unreasonably in promulgating its 2016 fiduciary rule and related exemptions. The 5th Circuit’s decision reversed a 2016 Texas district court decision and vacated the fiduciary rule and related exemptions in their entirety and on June 21, 2018, the 5th Circuit issued its formal mandate to officially vacate the DOL rule.² Furthermore, on April 18, 2018, the SEC voted to propose a package of rulemakings and interpretations designed to enhance the quality and transparency of investors’ relationships with investment advisers and broker-dealers while preserving access to a variety of types of advice relationships and investment products.³ Also known as “Regulation Best Interest”, the SEC’s proposal would require a broker-dealer when making a recommendation to a retail customer to act in the best interest of that customer at the time the recommendation is made. Under the proposed rule, the best-interest obligation would be satisfied through disclosure; a duty of care requiring the broker-dealer to exercise reasonable diligence, care, skill and prudence when dealing with the customer; and two conflict of interest obligations requiring the broker-dealer establish, maintain, and enforce written policies and procedures and disclose, mitigate, or eliminate material conflicts. Additionally, broker-dealers would be required to issue Form CRS to new customers outlining the summary of their financial relationship. Form CRS would prohibit stand-alone broker-dealers from using the titles “adviser” or “advisor,” which the SEC deemed to be too similar to an “investment adviser” which has a separate fiduciary duty. Form CRS would require financial advisors to provide investors with information regarding the types of services offered, fees the customers will pay, and certain conflicts of interest that may exist. The proposed rule was issued with a 90 day comment period.⁴

With the 5th Circuit’s ruling to vacate the DOL fiduciary rule and the SEC actions to propose Regulation Best Interest, the expert regulator is acting on the standards of conduct that financial

¹Chamber of Commerce of the United States of America, et al. v. United States Department of Labor, 2018 U.S. App. LEXIS 6472 (5th Cir. 2018).

²<https://www.naifa.org/NAIFA/media/Communications/NAIFA-Blog/CA5-Mandate.pdf>.

³<https://www.sec.gov/news/press-release/2018-68>.

⁴<https://www.sec.gov/rules/proposed/2018/34-83062.pdf>.

advisers adhere to regarding personalized investment advice, following the will of Congress set forth in Dodd-Frank.

HEARINGS

The Committee on Financial Services' Subcommittee on Financial Institutions held a hearing examining matters relating to H.R. 3857 on April 26, 2017, April 28, 2017 and July 13, 2017.

COMMITTEE CONSIDERATION

The Committee on Financial Services met in open session on October 11, 2017, and October 12, 2017, and ordered H.R. 3857 to be reported favorably to the House by a recorded vote of 34 yeas to 26 nays (recorded vote no. FC-86), a quorum being present.

COMMITTEE VOTES

Clause 3(b) of rule XIII of the Rules of the House of Representatives requires the Committee to list the record votes on the motion to report legislation and amendments thereto. The sole recorded vote was a motion by Chairman Hensarling to report the bill favorably to the House. That motion was agreed to by a recorded vote of 34 yeas to 26 nays (Record vote no. FC-86), a quorum being present.

Record vote no. FC-86

Representative	Yea	Nay	Present	Representative	Yea	Nay	Present
Mr. Hensarling	X			Ms. Maxine Waters (CA)	X		
Mr. McHenry	X			Mrs. Carolyn B. Maloney (NY)	X		
Mr. King	X			Ms. Velázquez	X		
Mr. Royce (CA)	X			Mr. Sherman	X		
Mr. Lucas	X			Mr. Meeks	X		
Mr. Pearce	X			Mr. Capuano	X		
Mr. Posey	X			Mr. Clay	X		
Mr. Luetkemeyer	X			Mr. Lynch	X		
Mr. Huizenga	X			Mr. David Scott (GA)	X		
Mr. Duffy	X			Mr. Al Green (TX)	X		
Mr. Stivers	X			Mr. Cleaver	X		
Mr. Hultgren	X			Ms. Moore	X		
Mr. Ross	X			Mr. Ellison	X		
Mr. Pittenger	X			Mr. Perlmutter	X		
Mrs. Wagner	X			Mr. Himes	X		
Mr. Barr	X			Mr. Foster	X		
Mr. Rothfus	X			Mr. Kildee	X		
Mr. Messer	X			Mr. Delaney	X		
Mr. Tipton	X			Ms. Sinema	X		
Mr. Williams	X			Mrs. Beatty	X		
Mr. Poliquin	X			Mr. Heck	X		
Mrs. Love	X			Mr. Vargas	X		
Mr. Hill	X			Mr. Gottheimer	X		
Mr. Emmer	X			Mr. Gonzalez (TX)	X		
Mr. Zeldin	X			Mr. Crist	X		
Mr. Trott	X			Mr. Kihuen	X		
Mr. Loudermilk	X						
Mr. Mooney (WV)	X						
Mr. MacArthur	X						
Mr. Davidson	X						
Mr. Budd	X						
Mr. Kustoff (TN)	X						
Ms. Tenney	X						
Mr. Hollingsworth	X						

COMMITTEE OVERSIGHT FINDINGS

Pursuant to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives, the findings and recommendations of the committee based on oversight activities under clause 2(b)(1) of rule X of the Rules of the House of Representatives, are incorporated in the descriptive portions of this report.

PERFORMANCE GOALS AND OBJECTIVES

Pursuant to clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the Committee states that H.R. 3857 will promote investor protection and ensure that individuals have access to professional investment advice by creating a best-interest standard that is appropriately designed for broker dealers, that incorporates pre-existing regulatory requirements and imposes additional requirements, and by re-establishing the SEC as the expert regulator.

NEW BUDGET AUTHORITY, ENTITLEMENT AUTHORITY, AND TAX EXPENDITURES

In compliance with clause 3(c)(2) of rule XIII of the Rules of the House of Representatives, the Committee adopts as its own the estimate of new budget authority, entitlement authority, or tax expenditures or revenues contained in the cost estimate prepared by the Director of the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974.

CONGRESSIONAL BUDGET OFFICE ESTIMATES

Pursuant to clause 3(c)(3) of rule XIII of the Rules of the House of Representatives, the following is the cost estimate provided by the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, December 11, 2017.

Hon. JEB HENSARLING,
*Chairman, Committee on Financial Services,
House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 3857, the PASS Act of 2017.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Stephen Rabent.

Sincerely,

KEITH HALL,
Director.

Enclosure.

H.R. 3857—PASS Act of 2017

H.R. 3857 would repeal regulations issued by the Department of Labor that are commonly referred to as the fiduciary rule and would direct the Securities and Exchange Commission (SEC) to develop a new standard to govern the conduct of brokers and dealers.

CBO estimates that implementing H.R. 3857 would have an insignificant effect on the federal budget.

Under current law, brokers and dealers must act as fiduciaries when they provide financial advice concerning pension and retirement plans; that is, their advice must be in the sole interest of the client. The Department of Labor issued the fiduciary rule on April 8, 2016; some parts took effect on June 9, 2017, and under current law, the rule takes full effect on January 1, 2018. H.R. 3857 would reinstate previously existing regulations.

H.R. 3857 also would amend the Securities Exchange Act of 1934 to establish a new standard of conduct for brokers and dealers. Under the bill, brokers and dealers would be required to make recommendations that are in the customer's best interest at the time the recommendation is given. They also would be required to make certain disclosures to customers regarding the standard of conduct and possible conflicts of interest. Under the bill, some individuals and financial institutions that comply with those requirements would be exempt from certain prohibitions on transactions under the Employee Retirement Income Security Act of 1974 and the Internal Revenue Code of 1986.

Using information from the SEC, CBO estimates that implementing H.R. 3857 would cost \$2 million over the 2018–2022 period for the agency to issue new guidance on the broker dealer standard of conduct and to expand examination and enforcement efforts to review compliance. However, because the SEC is authorized to collect fees sufficient to offset its annual appropriation, CBO estimates that the net effect on discretionary spending would be negligible, assuming appropriation actions consistent with that authority.

CBO and the staff of the Joint Committee on Taxation estimate that the bill would have a negligible effect on revenues over the 2018–2027 period. Because enacting H.R. 3857 would affect revenues, pay-as-you-go procedures apply. Enacting H.R. 3857 would not affect direct spending.

CBO estimates that enacting H.R. 3857 would not increase net direct spending or significantly affect on-budget deficits in any of the four consecutive 10-year periods beginning in 2028.

H.R. 3857 contains no intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA).

If the SEC increased fees to offset the costs of implementing the additional regulatory activities required by the bill, H.R. 3957 would increase the cost of an existing mandate on private entities that are required to pay those fees. Using information from the SEC, CBO estimates that the increase in fees to offset those costs would amount to about \$2 million over the 2018–2022 period and would fall well below the annual threshold for private-sector mandates established in UMRA (\$156 million in 2017, adjusted annually for inflation).

On September 18, 2017, CBO transmitted a cost estimate of H.R. 2823, the Affordable Retirement Advise for Savers Act, as ordered reported by the House Committee on Education and the Workforce on July 19, 2017. That bill has provisions similar to those in H.R. 3857 and CBO's estimate of the budgetary effects of those provisions are the same for both bills.

The CBO staff contacts for this estimate are Stephen Rabent (for federal costs) and Logan Smith (for mandates). The estimate was approved by H. Samuel Papenfuss, Deputy Assistant Director for Budget Analysis.

FEDERAL MANDATES STATEMENT

This information is provided in accordance with section 423 of the Unfunded Mandates Reform Act of 1995.

The Committee has determined that the bill does not contain Federal mandates on the private sector. The Committee has determined that the bill does not impose a Federal intergovernmental mandate on State, local, or tribal governments.

ADVISORY COMMITTEE STATEMENT

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

APPLICABILITY TO LEGISLATIVE BRANCH

The Committee finds that the legislation does not relate to the terms and conditions of employment or access to public services or accommodations within the meaning of the section 102(b)(3) of the Congressional Accountability Act.

EARMARK IDENTIFICATION

With respect to clause 9 of rule XXI of the Rules of the House of Representatives, the Committee has carefully reviewed the provisions of the bill and states that the provisions of the bill do not contain any congressional earmarks, limited tax benefits, or limited tariff benefits within the meaning of the rule.

DUPLICATION OF FEDERAL PROGRAMS

In compliance with clause 3(c)(5) of rule XIII of the Rules of the House of Representatives, the Committee states that no provision of the bill establishes or reauthorizes: (1) a program of the Federal Government known to be duplicative of another Federal program; (2) a program included in any report from the Government Accountability Office to Congress pursuant to section 21 of Public Law 111–139; or (3) a program related to a program identified in the most recent Catalog of Federal Domestic Assistance, published pursuant to the Federal Program Information Act (Pub. L. No. 95–220, as amended by Pub. L. No. 98–169).

DISCLOSURE OF DIRECTED RULEMAKING

Pursuant to section 3(k) of H. Res. 5, (115th Congress), the following statement is made concerning directed rulemakings: The Committee estimates that the bill requires no directed rulemakings within the meaning of such section.

SECTION-BY-SECTION ANALYSIS OF THE LEGISLATION

Section 1. Short title

This section cites H.R. 3857 as the “Protecting Advice for Small Savers Act of 2017” or the “PASS Act of 2017”.

Section 2. Repeal of Department of Labor fiduciary rule

This section repeals the Department of Labor final rule titled “Definition of the Term ‘Fiduciary’ Conflict of Interest Rule—Retirement Investment Advice” published on April 8, 2016.

Section 3. Standards of conduct for brokers and dealers

This section amends the second subsection (k) of section 15 of the Securities Exchange Act of 1934 by establishing a standard of conduct for broker-dealers making recommendations to retail customers. Broker-dealers must make a recommendation that is in the best interest of the retail customer and that reflects reasonable diligence and reasonable care, skill, and prudence by a broker-dealer, based on the customer’s investment profile.

Additionally, the bill requires increased disclosures to the retail customers before buying securities products on behalf of the customer, including: the type and scope of services the broker-dealer provides; the standard of conduct that applies to the relationship; the types of compensation the broker-dealer receives; and any material conflict of interest.

The bill also clarifies what is not a violation of the standard of conduct, including: the receipt of compensation, including transaction-based compensation, by a broker dealer; the recommendation by a broker-dealer to a retail customer of principal transactions; or the recommendation of affiliated, unaffiliated, or proprietary products and services. The bill does not contain a requirement that a broker-dealer recommend the least expensive product.

The bill also states that complying with the new standard of conduct does not mean that such a person is a “fiduciary” under the Employee Retirement Income Security Act of 1974 (ERISA), section 4975 of the Internal Revenue Code of 1986, the Investment Advisers Act of 1940, or any other applicable Federal, State or local regulatory regime.

Further, the bill amends section 913 of the Dodd-Frank Wall Street Reform and Consumer Protection Act to establish the SEC as the expert regulator for broker-dealers and the products that they sell to customers and grants rulemaking authority to the SEC to help facilitate compliance with the best-interest standard, only if such rulemaking does not impose any obligation that is in addition to, duplicative of, or inconsistent with the standard as set out in the legislation.

The bill provides exemptions from ERISA and the Internal Revenue Code to allow for State insurance regulators to adopt and implement practices on a nationwide basis for the sale of annuity contracts that is similar to the standard of conduct.

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3(e) 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*, and existing law in which no change is proposed is shown in *roman*):

SECURITIES EXCHANGE ACT OF 1934

TITLE I—REGULATION OF SECURITIES EXCHANGES

* * * * *

REGISTRATION AND REGULATION OF BROKERS AND DEALERS

SEC. 15. (a)(1) It shall be unlawful for any broker or dealer which is either a person other than a natural person or a natural person not associated with a broker or dealer which is a person other than a natural person (other than such a broker or dealer whose business is exclusively intrastate and who does not make use of any facility of a national securities exchange) to make use of the mails or any means or instrumentality of interstate commerce to effect any transactions in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills) unless such broker or dealer is registered in accordance with subsection (b) of this section.

(2) The Commission, by rule or order, as it deems consistent with the public interest and the protection of investors, may conditionally or unconditionally exempt from paragraph (1) of this subsection any broker or dealer or class of brokers or dealers specified in such rule or order.

(b)(1) A broker or dealer may be registered by filing with the Commission an application for registration in such form and containing such information and documents concerning such broker or dealer and any persons associated with such broker or dealer as the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors. Within forty-five days of the date of the filing of such application (or within such longer period as to which the applicant consents), the Commission shall—

(A) by order grant registration, or

(B) institute proceedings to determine whether registration should be denied. Such proceedings shall include notice of the grounds for denial under consideration and opportunity for hearing and shall be concluded within one hundred twenty days of the date of the filing of the application for registration. At the conclusion of such proceedings, the Commission, by order, shall grant or deny such registration. The Commission may extend the time for conclusion of such proceedings for up to ninety days if it finds good cause for such extension and publishes its reasons for so finding or for such longer period as to which the applicant consents.

The Commission shall grant such registration if the Commission finds that the requirements of this section are satisfied. The order granting registration shall not be effective until such broker or dealer has become a member of a registered securities association, or until such broker or dealer has become a member of a national securities exchange, if such broker or dealer effects transactions solely on that exchange, unless the Commission has exempted such broker or dealer, by rule or order, from such membership. The Commission shall deny such registration if it does not make such a finding or if it finds that if the applicant were so registered, its

registration would be subject to suspension or revocation under paragraph (4) of this subsection.

(2)(A) An application for registration of a broker or dealer to be formed or organized may be made by a broker or dealer to which the broker or dealer to be formed or organized is to be the successor. Such application, in such form as the Commission, by rule, may prescribe, shall contain such information and documents concerning the applicant, the successor, and any persons associated with the applicant or the successor, as the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors. The grant or denial of registration to such an applicant shall be in accordance with the procedures set forth in paragraph (1) of this subsection. If the Commission grants such registration, the registration shall terminate on the forty-fifth day after the effective date thereof, unless prior thereto the successor shall, in accordance with such rules and regulations as the Commission may prescribe, adopt the application for registration as its own.

(B) Any person who is a broker or dealer solely by reason of acting as a municipal securities dealer or municipal securities broker, who so acts through a separately identifiable department or division, and who so acted in such a manner on the date of enactment of the Securities Acts Amendments of 1975, may, in accordance with such terms and conditions as the Commission, by rule, prescribes as necessary and appropriate in the public interest and for the protection of investors, register such separately identifiable department or division in accordance with this subsection. If any such department or division is so registered, the department or division and not such person himself shall be the broker or dealer for purposes of this title.

(C) Within six months of the date of the granting of registration to a broker or dealer, the Commission, or upon the authorization and direction of the Commission, a registered securities association or national securities exchange of which such broker or dealer is a member, shall conduct an inspection of the broker or dealer to determine whether it is operating in conformity with the provisions of this title and the rules and regulations thereunder: *Provided, however,* That the Commission may delay such inspection of any class of brokers or dealers for a period not to exceed six months.

(3) Any provision of this title (other than section 5 and subsection (a) of this section) which prohibits any act, practice, or course of business if the mails or any means or instrumentality of interstate commerce is used in connection therewith shall also prohibit any such act, practice, or course of business by any registered broker or dealer or any person acting on behalf of such a broker or dealer, irrespective of any use of the mails or any means or instrumentality of interstate commerce in connection therewith.

(4) The Commission, by order, shall censure, place limitations on the activities, functions, or operations of, suspend for a period not exceeding twelve months, or revoke the registration of any broker or dealer if it finds, on the record after notice and opportunity for hearing, that such censure, placing of limitations, suspension, or revocation is in the public interest and that such broker or dealer, whether prior or subsequent to becoming such, or any person asso-

ciated with such broker or dealer, whether prior or subsequent to becoming so associated—

(A) has willfully made or caused to be made in any application for registration or report required to be filed with the Commission or with any other appropriate regulatory agency under this title, or in any proceeding before the Commission with respect to registration, any statement which was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, or has omitted to state in any such application or report any material fact which is required to be stated therein.

(B) has been convicted within ten years preceding the filing of any application for registration or at any time thereafter of any felony or misdemeanor or of a substantially equivalent crime by a foreign court of competent jurisdiction which the Commission finds—

(i) involves the purchase or sale of any security, the taking of a false oath, the making of a false report, bribery, perjury, burglary, any substantially equivalent activity however denominated by the laws of the relevant foreign government, or conspiracy to commit any such offense;

(ii) arises out of the conduct of the business of a broker, dealer, municipal securities dealer municipal advisor,, government securities broker, government securities dealer, investment adviser, bank, insurance company, fiduciary, transfer agent, nationally recognized statistical rating organization, foreign person performing a function substantially equivalent to any of the above, or entity or person required to be registered under the Commodity Exchange Act (7 U.S.C. 1 et seq.) or any substantially equivalent foreign statute or regulation;

(iii) involves the larceny, theft, robbery, extortion, forgery, counterfeiting, fraudulent concealment, embezzlement, fraudulent conversion, or misappropriation of funds, or securities, or substantially equivalent activity however denominated by the laws of the relevant foreign government; or

(iv) involves the violation of section 152, 1341, 1342, or 1343 or chapter 25 or 47 of title 18, United States Code, or a violation of a substantially equivalent foreign statute.

(C) is permanently or temporarily enjoined by order, judgment, or decree of any court of competent jurisdiction from acting as an investment adviser, underwriter, broker, dealer, municipal securities dealer municipal advisor,, government securities broker, government securities dealer, security-based swap dealer, major security-based swap participant, transfer agent, nationally recognized statistical rating organization, foreign person performing a function substantially equivalent to any of the above, or entity or person required to be registered under the Commodity Exchange Act or any substantially equivalent foreign statute or regulation, or as an affiliated person or employee of any investment company, bank, insurance company, foreign entity substantially equivalent to any of the above, or entity or person required to be registered under the Commodity Exchange Act or any substantially equivalent foreign

statute or regulation, or from engaging in or continuing any conduct or practice in connection with any such activity, or in connection with the purchase or sale of any security.

(D) has willfully violated any provision of the Securities Act of 1933, the Investment Advisers Act of 1940, the Investment Company Act of 1940, the Commodity Exchange Act, this title, the rules or regulations under any of such statutes, or the rules of the Municipal Securities Rulemaking Board, or is unable to comply with any such provision.

(E) has willfully aided, abetted, counseled, commanded, induced, or procured the violation by any other person of any provision of the Securities Act of 1933, the Investment Advisers Act of 1940, the Investment Company Act of 1940, the Commodity Exchange Act, this title, the rules or regulations under any of such statutes, or the rules of the Municipal Securities Rulemaking Board, or has failed reasonably to supervise, with a view to preventing violations of the provisions of such statutes, rules, and regulations, another person who commits such a violation, if such other person is subject to his supervision. For the purposes of this subparagraph (E) no person shall be deemed to have failed reasonably to supervise any other person, if—

(i) there have been established procedures, and a system for applying such procedures, which would reasonably be expected to prevent and detect, insofar as practicable, any such violation by such other person, and

(ii) such person has reasonably discharged the duties and obligations incumbent upon him by reason of such procedures and system without reasonable cause to believe that such procedures and system were not being complied with.

(F) is subject to any order of the Commission barring or suspending the right of the person to be associated with a broker, dealer, security-based swap dealer, or a major security-based swap participant;

(G) has been found by a foreign financial regulatory authority to have—

(i) made or caused to be made in any application for registration or report required to be filed with a foreign financial regulatory authority, or in any proceeding before a foreign financial regulatory authority with respect to registration, any statement that was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, or has omitted to state in any application or report to the foreign financial regulatory authority any material fact that is required to be stated therein;

(ii) violated any foreign statute or regulation regarding transactions in securities, or contracts of sale of a commodity for future delivery, traded on or subject to the rules of a contract market or any board of trade;

(iii) aided, abetted, counseled, commanded, induced, or procured the violation by any person of any provision of any statutory provisions enacted by a foreign government, or rules or regulations thereunder, empowering a foreign

financial regulatory authority regarding transactions in securities, or contracts of sale of a commodity for future delivery, traded on or subject to the rules of a contract market or any board of trade, or has been found, by a foreign financial regulatory authority, to have failed reasonably to supervise, with a view to preventing violations of such statutory provisions, rules, and regulations, another person who commits such a violation, if such other person is subject to his supervision; or

(H) is subject to any final order of a State securities commission (or any agency or officer performing like functions), State authority that supervises or examines banks, savings associations, or credit unions, State insurance commission (or any agency or office performing like functions), an appropriate Federal banking agency (as defined in section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813(q))), or the National Credit Union Administration, that—

(i) bars such person from association with an entity regulated by such commission, authority, agency, or officer, or from engaging in the business of securities, insurance, banking, savings association activities, or credit union activities; or

(ii) constitutes a final order based on violations of any laws or regulations that prohibit fraudulent, manipulative, or deceptive conduct.

(5) Pending final determination whether any registration under this subsection shall be revoked, the Commission, by order, may suspend such registration, if such suspension appears to the Commission, after notice and opportunity for hearing, to be necessary or appropriate in the public interest or for the protection of investors. Any registered broker or dealer may, upon such terms and conditions as the Commission deems necessary or appropriate in the public interest or for the protection of investors, withdraw from registration by filing a written notice of withdrawal with the Commission. If the Commission finds that any registered broker or dealer is no longer in existence or has ceased to do business as a broker or dealer, the Commission, by order, shall cancel the registration of such broker or dealer.

(6)(A) With respect to any person who is associated, who is seeking to become associated, or, at the time of the alleged misconduct, who was associated or was seeking to become associated with a broker or dealer, or any person participating, or, at the time of the alleged misconduct, who was participating, in an offering of any penny stock, the Commission, by order, shall censure, place limitations on the activities or functions of such person, or suspend for a period not exceeding 12 months, or bar any such person from being associated with a broker, dealer, investment adviser, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization, or from participating in an offering of penny stock, if the Commission finds, on the record after notice and opportunity for a hearing, that such censure, placing of limitations, suspension, or bar is in the public interest and that such person—

(i) has committed or omitted any act, or is subject to an order or finding, enumerated in subparagraph (A), (D), (E), (H), or (G) of paragraph (4) of this subsection;

(ii) has been convicted of any offense specified in subparagraph (B) of such paragraph (4) within 10 years of the commencement of the proceedings under this paragraph; or

(iii) is enjoined from any action, conduct, or practice specified in subparagraph (C) of such paragraph (4).

(B) It shall be unlawful—

(i) for any person as to whom an order under subparagraph (A) is in effect, without the consent of the Commission, willfully to become, or to be, associated with a broker or dealer in contravention of such order, or to participate in an offering of penny stock in contravention of such order;

(ii) for any broker or dealer to permit such a person, without the consent of the Commission, to become or remain, a person associated with the broker or dealer in contravention of such order, if such broker or dealer knew, or in the exercise of reasonable care should have known, of such order; or

(iii) for any broker or dealer to permit such a person, without the consent of the Commission, to participate in an offering of penny stock in contravention of such order, if such broker or dealer knew, or in the exercise of reasonable care should have known, of such order and of such participation.

(C) For purposes of this paragraph, the term “person participating in an offering of penny stock” includes any person acting as any promoter, finder, consultant, agent, or other person who engages in activities with a broker, dealer, or issuer for purposes of the issuance or trading in any penny stock, or inducing or attempting to induce the purchase or sale of any penny stock. The Commission may, by rule or regulation, define such term to include other activities, and may, by rule, regulation, or order, exempt any person or class of persons, in whole or in part, conditionally or unconditionally, from such term.

(7) No registered broker or dealer or government securities broker or government securities dealer registered (or required to register) under section 15C(a)(1)(A) shall effect any transaction in, or induce the purchase or sale of, any security unless such broker or dealer meets such standards of operational capability and such broker or dealer and all natural persons associated with such broker or dealer meet such standards of training, experience, competence, and such other qualifications as the Commission finds necessary or appropriate in the public interest or for the protection of investors. The Commission shall establish such standards by rules and regulations, which may—

(A) specify that all or any portion of such standards shall be applicable to any class of brokers and dealers and persons associated with brokers and dealers;

(B) require persons in any such class to pass tests prescribed in accordance with such rules and regulations, which tests shall, with respect to any class of partners, officers, or supervisory employees (which latter term may be defined by the Commission’s rules and regulations and as so defined shall include branch managers of brokers or dealers) engaged in the management of the broker or dealer, include questions relating

to bookkeeping, accounting, internal control over cash and securities, supervision of employees, maintenance of records, and other appropriate matters; and

(C) provide that persons in any such class other than brokers and dealers and partners, officers, and supervisory employees of brokers or dealers, may be qualified solely on the basis of compliance with such standards of training and such other qualifications as the Commission finds appropriate.

The Commission, by rule, may prescribe reasonable fees and charges to defray its costs in carrying out this paragraph, including, but not limited to, fees for any test administered by it or under its direction. The Commission may cooperate with registered securities associations and national securities exchanges in devising and administering tests and may require registered brokers and dealers and persons associated with such brokers and dealers to pass tests administered by or on behalf of any such association or exchange and to pay such association or exchange reasonable fees or charges to defray the costs incurred by such association or exchange in administering such tests.

(8) It shall be unlawful for any registered broker or dealer to effect any transaction in, or induce or attempt to induce the purchase or sale of, any security (other than or commercial paper, bankers' acceptances, or commercial bills), unless such broker or dealer is a member of a securities association registered pursuant to section 15A of this title or effects transactions in securities solely on a national securities exchange of which it is a member.

(9) The Commission by rule or order, as it deems consistent with the public interest and the protection of investors, may conditionally or unconditionally exempt from paragraph (8) of this subsection any broker or dealer or class of brokers or dealers specified in such rule or order.

(10) For the purposes of determining whether a person is subject to a statutory disqualification under section 6(c)(2), 15A(g)(2), or 17A(b)(4)(A) of this title, the term "Commission" in paragraph (4)(B) of this subsection shall mean "exchange", "association", or "clearing agency", respectively.

(11) **BROKER/DEALER REGISTRATION WITH RESPECT TO TRANSACTIONS IN SECURITY FUTURES PRODUCTS.—**

(A) **NOTICE REGISTRATION.—**

(i) **CONTENTS OF NOTICE.—**Notwithstanding paragraphs (1) and (2), a broker or dealer required to register only because it effects transactions in security futures products on an exchange registered pursuant to section 6(g) may register for purposes of this section by filing with the Commission a written notice in such form and containing such information concerning such broker or dealer and any persons associated with such broker or dealer as the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors. A broker or dealer may not register under this paragraph unless that broker or dealer is a member of a national securities association registered under section 15A(k).

(ii) **IMMEDIATE EFFECTIVENESS.—**Such registration shall be effective contemporaneously with the submis-

sion of notice, in written or electronic form, to the Commission, except that such registration shall not be effective if the registration would be subject to suspension or revocation under paragraph (4).

(iii) **SUSPENSION.**—Such registration shall be suspended immediately if a national securities association registered pursuant to section 15A(k) of this title suspends the membership of that broker or dealer.

(iv) **TERMINATION.**—Such registration shall be terminated immediately if any of the above stated conditions for registration set forth in this paragraph are no longer satisfied.

(B) **EXEMPTIONS FOR REGISTERED BROKERS AND DEALERS.**—A broker or dealer registered pursuant to the requirements of subparagraph (A) shall be exempt from the following provisions of this title and the rules thereunder with respect to transactions in security futures products:

(i) Section 8.

(ii) Section 11.

(iii) Subsections (c)(3) and (c)(5) of this section.

(iv) Section 15B.

(v) Section 15C.

(vi) Subsections (d), (e), (f), (g), (h), and (i) of section 17.

(12) **EXEMPTION FOR SECURITY FUTURES PRODUCT EXCHANGE MEMBERS.**—

(A) **REGISTRATION EXEMPTION.**—A natural person shall be exempt from the registration requirements of this section if such person—

(i) is a member of a designated contract market registered with the Commission as an exchange pursuant to section 6(g);

(ii) effects transactions only in securities on the exchange of which such person is a member; and

(iii) does not directly accept or solicit orders from public customers or provide advice to public customers in connection with the trading of security futures products.

(B) **OTHER EXEMPTIONS.**—A natural person exempt from registration pursuant to subparagraph (A) shall also be exempt from the following provisions of this title and the rules thereunder:

(i) Section 8.

(ii) Section 11.

(iii) Subsections (c)(3), (c)(5), and (e) of this section.

(iv) Section 15B.

(v) Section 15C.

(vi) Subsections (d), (e), (f), (g), (h), and (i) of section 17.

(c)(1)(A) No broker or dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security (other than commercial paper, bankers' acceptances, or commercial bills), or any security-based swap agreement

by means of any manipulative, deceptive, or other fraudulent device or contrivance.

(B) No broker, dealer, or municipal securities dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any municipal security or any security-based swap agreement involving a municipal security by means of any manipulative, deceptive, or other fraudulent device or contrivance.

(C) No government securities broker or government securities dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any government security or any security-based swap agreement involving a government security by means of any manipulative, deceptive, or other fraudulent device or contrivance.

(2)(A) No broker or dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national securities exchange of which it is a member, in connection with which such broker or dealer engages in any fraudulent, deceptive, or manipulative act or practice, or makes any fictitious quotation.

(B) No broker, dealer, or municipal securities dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any municipal security in connection with which such broker, dealer, or municipal securities dealer engages in any fraudulent, deceptive, or manipulative act or practice, or makes any fictitious quotation.

(C) No government securities broker or government securities dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or induce or attempt to induce the purchase or sale of, any government security in connection with which such government securities broker or government securities dealer engages in any fraudulent, deceptive, or manipulative act or practice, or makes any fictitious quotation.

(D) The Commission shall, for the purposes of this paragraph, by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative and such quotations as are fictitious.

(E) The Commission shall, prior to adopting any rule or regulation under subparagraph (C), consult with and consider the views of the Secretary of the Treasury and each appropriate regulatory agency. If the Secretary of the Treasury or any appropriate regulatory agency comments in writing on a proposed rule or regulation of the Commission under such subparagraph (C) that has been published for comment, the Commission shall respond in writing to such written comment before adopting the proposed rule. If the Secretary of the Treasury determines, and notifies the Commission, that such rule or regulation, if implemented, would, or as applied does (i) adversely affect the liquidity or efficiency of the market for government securities; or (ii) impose any burden on competition not

necessary or appropriate in furtherance of the purposes of this section, the Commission shall, prior to adopting the proposed rule or regulation, find that such rule or regulation is necessary and appropriate in furtherance of the purposes of this section notwithstanding the Secretary's determination.

(3)(A) No broker or dealer (other than a government securities broker or government securities dealer, except a registered broker or dealer) shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security (except a government security) or commercial paper, bankers' acceptances, or commercial bills) in contravention of such rules and regulations as the Commission shall prescribe as necessary or appropriate in the public interest or for the protection of investors to provide safeguards with respect to the financial responsibility and related practices of brokers and dealers including, but not limited to, the acceptance of custody and use of customers' securities and the carrying and use of customers' deposits or credit balances. Such rules and regulations shall (A) require the maintenance of reserves with respect to customers' deposits or credit balances, and (B) no later than September 1, 1975, establish minimum financial responsibility requirements for all brokers and dealers.

(B) Consistent with this title, the Commission, in consultation with the Commodity Futures Trading Commission, shall issue such rules, regulations, or orders as are necessary to avoid duplicative or conflicting regulations applicable to any broker or dealer registered with the Commission pursuant to section 15(b) (except paragraph (11) thereof), that is also registered with the Commodity Futures Trading Commission pursuant to section 4f(a) of the Commodity Exchange Act (except paragraph (2) thereof), with respect to the application of: (i) the provisions of section 8, section 15(c)(3), and section 17 of this title and the rules and regulations thereunder related to the treatment of customer funds, securities, or property, maintenance of books and records, financial reporting, or other financial responsibility rules, involving security futures products; and (ii) similar provisions of the Commodity Exchange Act and rules and regulations thereunder involving security futures products.

(C) Notwithstanding any provision of sections 2(a)(1)(C)(i) or 4d(a)(2) of the Commodity Exchange Act and the rules and regulations thereunder, and pursuant to an exemption granted by the Commission under section 36 of this title or pursuant to a rule or regulation, cash and securities may be held by a broker or dealer registered pursuant to subsection (b)(1) and also registered as a futures commission merchant pursuant to section 4f(a)(1) of the Commodity Exchange Act, in a portfolio margining account carried as a futures account subject to section 4d of the Commodity Exchange Act and the rules and regulations thereunder, pursuant to a portfolio margining program approved by the Commodity Futures Trading Commission, and subject to subchapter IV of chapter 7 of title 11 of the United States Code and the rules and regulations thereunder. The Commission shall consult with the Commodity Futures Trading Commission to adopt rules to ensure that such transactions

and accounts are subject to comparable requirements to the extent practicable for similar products.

(4) If the Commission finds, after notice and opportunity for a hearing, that any person subject to the provisions of section 12, 13, 14, or subsection (d) of section 15 of this title or any rule or regulation thereunder has failed to comply with any such provision, rule, or regulation in any material respect, the Commission may publish its findings and issue an order requiring such person, and any person who was a cause of the failure to comply due to an act or omission the person knew or should have known would contribute to the failure to comply, to comply, or to take steps to effect compliance, with such provision or such rule or regulation thereunder upon such terms and conditions and within such time as the Commission may specify in such order.

(5) No dealer (other than a specialist registered on a national securities exchange) acting in the capacity of market maker or otherwise shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security or a municipal security) in contravention of such specified and appropriate standards with respect to dealing as the Commission, by rule, shall prescribe as necessary or appropriate in the public interest and for the protection of investors, to maintain fair and orderly markets, or to remove impediments to and perfect the mechanism of a national market system. Under the rules of the Commission a dealer in a security may be prohibited from acting as broker in that security.

(6) No broker or dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security, municipal security, commercial paper, bankers' acceptances, or commercial bills) in contravention of such rules and regulations as the Commission shall prescribe as necessary or appropriate in the public interest and for the protection of investors or to perfect or remove impediments to a national system for the prompt and accurate clearance and settlement of securities transactions, with respect to the time and method of, and the form and format of documents used in connection with, making settlements of and payments for transactions in securities, making transfers and deliveries of securities, and closing accounts. Nothing in this paragraph shall be construed (A) to affect the authority of the Board of Governors of the Federal Reserve System, pursuant to section 7 of this title, to prescribe rules and regulations for the purpose of preventing the excessive use of credit for the purchase or carrying of securities, or (B) to authorize the Commission to prescribe rules or regulations for such purpose.

(7) In connection with any bid for or purchase of a government security related to an offering of government securities by or on behalf of an issuer, no government securities broker, government securities dealer, or bidder for or purchaser of securities in such offering shall knowingly or willfully make any false or misleading written statement or omit any fact necessary to make any written statement made not misleading.

(8) PROHIBITION OF REFERRAL FEES.—No broker or dealer, or person associated with a broker or dealer, may solicit or accept, di-

rectly or indirectly, remuneration for assisting an attorney in obtaining the representation of any person in any private action arising under this title or under the Securities Act of 1933.

(d) SUPPLEMENTARY AND PERIODIC INFORMATION.—

(1) IN GENERAL.—Each issuer which has filed a registration statement containing an undertaking which is or becomes operative under this subsection as in effect prior to the date of enactment of the Securities Acts Amendments of 1964, and each issuer which shall after such date file a registration statement which has become effective pursuant to the Securities Act of 1933, as amended, shall file with the Commission, in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors, such supplementary and periodic information, documents, and reports as may be required pursuant to section 13 of this title in respect of a security registered pursuant to section 12 of this title. The duty to file under this subsection shall be automatically suspended if and so long as any issue of securities of such issuer is registered pursuant to section 12 of this title. The duty to file under this subsection shall also be automatically suspended as to any fiscal year, other than the fiscal year within which such registration statement became effective, if, at the beginning of such fiscal year, the securities of each class, other than any class of asset-backed securities, to which the registration statement relates are held of record by less than 300 persons, or, in the case of a bank, a savings and loan holding company (as defined in section 10 of the Home Owners' Loan Act), or a bank holding company, as such term is defined in section 2 of the Bank Holding Company Act of 1956 (12 U.S.C. 1841), 1,200 persons. For the purposes of this subsection, the term "class" shall be construed to include all securities of an issuer which are of substantially similar character and the holders of which enjoy substantially similar rights and privileges. The Commission may, for the purpose of this subsection, define by rules and regulations the term "held of record" as it deems necessary or appropriate in the public interest or for the protection of investors in order to prevent circumvention of the provisions of this subsection. Nothing in this subsection shall apply to securities issued by a foreign government or political subdivision thereof.

(2) ASSET-BACKED SECURITIES.—

(A) SUSPENSION OF DUTY TO FILE.—The Commission may, by rule or regulation, provide for the suspension or termination of the duty to file under this subsection for any class of asset-backed security, on such terms and conditions and for such period or periods as the Commission deems necessary or appropriate in the public interest or for the protection of investors.

(B) CLASSIFICATION OF ISSUERS.—The Commission may, for purposes of this subsection, classify issuers and prescribe requirements appropriate for each class of issuers of asset-backed securities.

(e) NOTICES TO CUSTOMERS REGARDING SECURITIES LENDING.—Every registered broker or dealer shall provide notice to its cus-

tomers that they may elect not to allow their fully paid securities to be used in connection with short sales. If a broker or dealer uses a customer's securities in connection with short sales, the broker or dealer shall provide notice to its customer that the broker or dealer may receive compensation in connection with lending the customer's securities. The Commission, by rule, as it deems necessary or appropriate in the public interest and for the protection of investors, may prescribe the form, content, time, and manner of delivery of any notice required under this paragraph.

(f) The Commission, by rule, as it deems necessary or appropriate in the public interest and for the protection of investors or to assure equal regulation, may require any member of a national securities exchange not required to register under section 15 of this title and any person associated with any such member to comply with any provision of this title (other than section 15(a)) or the rules or regulations thereunder which by its terms regulates or prohibits any act, practice, or course of business by a "broker or dealer" or "registered broker or dealer" or a "person associated with a broker or dealer," respectively.

(g) Every registered broker or dealer shall establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of such broker's or dealer's business, to prevent the misuse in violation of this title, or the rules or regulations thereunder, of material, nonpublic information by such broker or dealer or any person associated with such broker or dealer. The Commission, as it deems necessary or appropriate in the public interest or for the protection of investors, shall adopt rules or regulations to require specific policies or procedures reasonably designed to prevent misuse in violation of this title (or the rules or regulations thereunder) of material, nonpublic information.

(h) REQUIREMENTS FOR TRANSACTIONS IN PENNY STOCKS.—

(1) IN GENERAL.—No broker or dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any penny stock by any customer except in accordance with the requirements of this subsection and the rules and regulations prescribed under this subsection.

(2) RISK DISCLOSURE WITH RESPECT TO PENNY STOCKS.—Prior to effecting any transaction in any penny stock, a broker or dealer shall give the customer a risk disclosure document that—

(A) contains a description of the nature and level of risk in the market for penny stocks in both public offerings and secondary trading;

(B) contains a description of the broker's or dealer's duties to the customer and of the rights and remedies available to the customer with respect to violations of such duties or other requirements of Federal securities laws;

(C) contains a brief, clear, narrative description of a dealer market, including "bid" and "ask" prices for penny stocks and the significance of the spread between the bid and ask prices;

(D) contains the toll free telephone number for inquiries on disciplinary actions established pursuant to section 15A(i) of this title;

(E) defines significant terms used in the disclosure document or in the conduct of trading in penny stocks; and

(F) contains such other information, and is in such form (including language, type size, and format), as the Commission shall require by rule or regulation.

(3) COMMISSION RULES RELATING TO DISCLOSURE.—The Commission shall adopt rules setting forth additional standards for the disclosure by brokers and dealers to customers of information concerning transactions in penny stocks. Such rules—

(A) shall require brokers and dealers to disclose to each customer, prior to effecting any transaction in, and at the time of confirming any transaction with respect to any penny stock, in accordance with such procedures and methods as the Commission may require consistent with the public interest and the protection of investors—

(i) the bid and ask prices for penny stock, or such other information as the Commission may, by rule, require to provide customers with more useful and reliable information relating to the price of such stock;

(ii) the number of shares to which such bid and ask prices apply, or other comparable information relating to the depth and liquidity of the market for such stock; and

(iii) the amount and a description of any compensation that the broker or dealer and the associated person thereof will receive or has received in connection with such transaction;

(B) shall require brokers and dealers to provide, to each customer whose account with the broker or dealer contains penny stocks, a monthly statement indicating the market value of the penny stocks in that account or indicating that the market value of such stock cannot be determined because of the unavailability of firm quotes; and

(C) may, as the Commission finds necessary or appropriate in the public interest or for the protection of investors, require brokers and dealers to disclose to customers additional information concerning transactions in penny stocks.

(4) EXEMPTIONS.—The Commission, as it determines consistent with the public interest and the protection of investors, may by rule, regulation, or order exempt in whole or in part, conditionally or unconditionally, any person or class of persons, or any transaction or class of transactions, from the requirements of this subsection. Such exemptions shall include an exemption for brokers and dealers based on the minimal percentage of the broker's or dealer's commissions, commission-equivalents, and markups received from transactions in penny stocks.

(5) REGULATIONS.—It shall be unlawful for any person to violate such rules and regulations as the Commission shall prescribe in the public interest or for the protection of investors or to maintain fair and orderly markets—

(A) as necessary or appropriate to carry out this subsection; or

(B) as reasonably designed to prevent fraudulent, deceptive, or manipulative acts and practices with respect to penny stocks.

(i) 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) FUNDING PORTALS.—

(A) LIMITATION ON STATE LAWS.—Except as provided in subparagraph (B), no State or political subdivision thereof may enforce any law, rule, regulation, or other administrative action against a registered funding portal with respect to its business as such.

(B) EXAMINATION AND ENFORCEMENT AUTHORITY.—Subparagraph (A) does not apply with respect to the examination and enforcement of any law, rule, regulation, or administrative action of a State or political subdivision thereof in which the principal place of business of a registered funding portal is located, provided that such law, rule, regulation, or administrative action is not in addition to or different from the requirements for registered funding portals established by the Commission.

(C) DEFINITION.—For purposes of this paragraph, the term “State” includes the District of Columbia and the territories of the United States.

(3) DE MINIMIS TRANSACTIONS BY ASSOCIATED PERSONS.—No law, rule, regulation, or order, or other administrative action of any State or political subdivision thereof may prohibit an associated person of a broker or dealer 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.

(4) DESCRIBED TRANSACTIONS.—

(A) IN GENERAL.—A transaction is described in this paragraph if—

(i) such transaction is effected—

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

(II) by an associated person of the broker or dealer—

(aa) to which the customer was assigned for 14 days prior to the day of the transaction; and

(bb) who is registered with a State in which the customer was a resident or was present for at least 30 consecutive days during the 1-year period prior to the day of the transaction; or

(ii) the transaction is effected—

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

(II) during the period beginning on the date on which such associated person files an application for registration with the State in which the transaction is effected and ending on the earlier of—

(aa) 60 days after the date on which the application is filed; or

(bb) the date on 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.

(B) RULES OF CONSTRUCTION.—For purposes of subparagraph (A)(i)(II)—

(i) each of up to 3 associated persons of a broker or dealer 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; and

(ii) 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, a transaction is not described in this paragraph, unless the associated person of the broker or dealer files an application for registration with such State not later than 10 business days after the later of the date of the transaction, or the date of the discovery of the presence of the customer in the other State for 30 or more consecutive days or the change in the customer's residence.

(j) RULEMAKING TO EXTEND REQUIREMENTS TO NEW HYBRID PRODUCTS.—

(1) CONSULTATION.—Prior to commencing a rulemaking under this subsection, the Commission shall consult with and seek the concurrence of the Board concerning the imposition of broker or dealer registration requirements with respect to any new hybrid product. In developing and promulgating rules under this subsection, the Commission shall consider the views of the Board, including views with respect to the nature of the new hybrid product; the history, purpose, extent, and appropriateness of the regulation of the new product under the Federal banking laws; and the impact of the proposed rule on the banking industry.

(2) LIMITATION.—The Commission shall not—

- (A) require a bank to register as a broker or dealer under this section because the bank engages in any transaction in, or buys or sells, a new hybrid product; or
- (B) bring an action against a bank for a failure to comply with a requirement described in subparagraph (A), unless the Commission has imposed such requirement by rule or regulation issued in accordance with this section.

(3) CRITERIA FOR RULEMAKING.—The Commission shall not impose a requirement under paragraph (2) of this subsection with respect to any new hybrid product unless the Commission determines that—

- (A) the new hybrid product is a security; and
- (B) imposing such requirement is necessary and appropriate in the public interest and for the protection of investors.

(4) CONSIDERATIONS.—In making a determination under paragraph (3), the Commission shall consider—

- (A) the nature of the new hybrid product; and
- (B) the history, purpose, extent, and appropriateness of the regulation of the new hybrid product under the Federal securities laws and under the Federal banking laws.

(5) OBJECTION TO COMMISSION REGULATION.—

(A) FILING OF PETITION FOR REVIEW.—The Board may obtain review of any final regulation described in paragraph (2) in the United States Court of Appeals for the District of Columbia Circuit by filing in such court, not later than 60 days after the date of publication of the final regulation, a written petition requesting that the regulation be set aside. Any proceeding to challenge any such rule shall be expedited by the Court of Appeals.

(B) TRANSMITTAL OF PETITION AND RECORD.—A copy of a petition described in subparagraph (A) shall be transmitted as soon as possible by the Clerk of the Court to an officer or employee of the Commission designated for that purpose. Upon receipt of the petition, the Commission shall file with the court the regulation under review and any documents referred to therein, and any other relevant materials prescribed by the court.

(C) EXCLUSIVE JURISDICTION.—On the date of the filing of the petition under subparagraph (A), the court has jurisdiction, which becomes exclusive on the filing of the materials set forth in subparagraph (B), to affirm and enforce or to set aside the regulation at issue.

(D) STANDARD OF REVIEW.—The court shall determine to affirm and enforce or set aside a regulation of the Commission under this subsection, based on the determination of the court as to whether—

- (i) the subject product is a new hybrid product, as defined in this subsection;
- (ii) the subject product is a security; and
- (iii) imposing a requirement to register as a broker or dealer for banks engaging in transactions in such product is appropriate in light of the history, purpose, and extent of regulation under the Federal securities

laws and under the Federal banking laws, giving deference neither to the views of the Commission nor the Board.

(E) JUDICIAL STAY.—The filing of a petition by the Board pursuant to subparagraph (A) shall operate as a judicial stay, until the date on which the determination of the court is final (including any appeal of such determination).

(F) OTHER AUTHORITY TO CHALLENGE.—Any aggrieved party may seek judicial review of the Commission’s rule-making under this subsection pursuant to section 25 of this title.

(6) DEFINITIONS.—For purposes of this subsection:

(A) NEW HYBRID PRODUCT.—The term “new hybrid product” means a product that—

(i) was not subjected to regulation by the Commission as a security prior to the date of the enactment of the Gramm-Leach-Bliley Act;

(ii) is not an identified banking product as such term is defined in section 206 of such Act; and

(iii) is not an equity swap within the meaning of section 206(a)(6) of such Act.

(B) BOARD.—The term “Board” means the Board of Governors of the Federal Reserve System.

(j) The authority of the Commission under this section with respect to security-based swap agreements shall be subject to the restrictions and limitations of section 3A(b) of this title.

(k) REGISTRATION OR SUCCESSION TO A UNITED STATES BROKER OR DEALER.—In determining whether to permit a foreign person or an affiliate of a foreign person to register as a United States broker or dealer, or succeed to the registration of a United States broker or dealer, the Commission may consider whether, for a foreign person, or an affiliate of a foreign person that presents a risk to the stability of the United States financial system, the home country of the foreign person has adopted, or made demonstrable progress toward adopting, an appropriate system of financial regulation to mitigate such risk.

(l) TERMINATION OF A UNITED STATES BROKER OR DEALER.—For a foreign person or an affiliate of a foreign person that presents such a risk to the stability of the United States financial system, the Commission may determine to terminate the registration of such foreign person or an affiliate of such foreign person as a broker or dealer in the United States, if the Commission determines that the home country of the foreign person has not adopted, or made demonstrable progress toward adopting, an appropriate system of financial regulation to mitigate such risk.

[(k) STANDARD OF CONDUCT.—

[(1) IN GENERAL.—Notwithstanding any other provision of this Act or the Investment Advisers Act of 1940, the Commission may promulgate rules to provide that, with respect to a broker or dealer, when providing personalized investment advice about securities to a retail customer (and such other customers as the Commission may by rule provide), the standard of conduct for such broker or dealer with respect to such customer shall be the same as the standard of conduct applicable to an investment adviser under section 211 of the Investment

Advisers Act of 1940. The receipt of compensation based on commission or other standard compensation for the sale of securities shall not, in and of itself, be considered a violation of such standard applied to a broker or dealer. Nothing in this section shall require a broker or dealer or registered representative to have a continuing duty of care or loyalty to the customer after providing personalized investment advice about securities.

【(2) DISCLOSURE OF RANGE OF PRODUCTS OFFERED.—Where a broker or dealer sells only proprietary or other limited range of products, as determined by the Commission, the Commission may by rule require that such broker or dealer provide notice to each retail customer and obtain the consent or acknowledgment of the customer. The sale of only proprietary or other limited range of products by a broker or dealer shall not, in and of itself, be considered a violation of the standard set forth in paragraph (1).】

(k) STANDARD OF CONDUCT FOR RECOMMENDATIONS TO RETAIL CUSTOMERS.—

(1) IN GENERAL.—*The standard of conduct for a broker or dealer (or registered representative) when providing recommendations to a retail customer is as follows:*

(A) RECOMMENDATION TO RETAIL CUSTOMER.—*When a broker or dealer (or registered representative) makes a recommendation to a retail customer, the recommendation shall be in the retail customer's best interest at the time it is made by—*

- (i) *reflecting reasonable diligence; and*
- (ii) *reflecting the reasonable care, skill, and prudence that a broker or dealer (or registered representative) would exercise based on the customer's investment profile.*

(B) DISCLOSURE TO RETAIL CUSTOMER.—

(i) IN GENERAL.—*Before a broker or dealer (or registered representative) executes a transaction for the first time for each retail customer based on a recommendation to such retail customer, such broker or dealer (or registered representative) shall disclose prior to the point of sale to such customer, in a clear and concise manner—*

- (I) *the type and scope of services the broker or dealer (or registered representative) provides;*
- (II) *the standard of conduct that applies to the relationship;*
- (III) *the types of compensation the broker or dealer (or registered representative) receives; and*
- (IV) *any material conflict of interest.*

(ii) CONTENT OF DISCLOSURE.—*The Commission may issue regulations determining the content of the disclosure required in clause (i). Such regulations may provide for a disclosure of fees received by the broker or dealer, whether from the retail customer or a third party, prior to the execution of the transaction.*

(C) MATERIAL CONFLICT OF INTEREST.—*A broker or dealer (or registered representative) shall avoid, disclose, or oth-*

erwise reasonably manage any material conflict of interest with a retail customer.

(2) **NONVIOLATION OF STANDARD OF CONDUCT.**—*The following is not, by itself, a violation of the standard of conduct described in paragraph (1):*

(A) *The receipt of compensation, including transaction-based compensation, by a broker or dealer (or registered representative) or any affiliate of such broker or dealer (or registered representative).*

(B) *The recommendation by a broker or dealer (or registered representative) to a retail customer of principal transactions (including cross transactions), or the recommendation of affiliated, unaffiliated, or proprietary products or services, or a limited range of products or services.*

(3) **NO REQUIREMENT TO RECOMMEND LEAST EXPENSIVE PRODUCT.**—*Nothing in this subsection shall require a broker or dealer (or registered representative) to recommend the least expensive security or investment strategy (however quantified) or to analyze all possible securities, other products, or investment strategies before making a recommendation.*

(4) **DEFINITIONS.**—*In this subsection:*

(A) **COMPENSATION.**—*The term “compensation” includes commissions or sales charges, or other fees or variable compensation, for or related to the sale of securities or for the servicing of customer accounts, whether paid by the retail customer or received from a third party.*

(B) **CUSTOMER’S INVESTMENT PROFILE.**—*The term “customer’s investment profile” has the meaning of such term as described in Rule 2111 of the Financial Industry Regulatory Authority as of the date of the enactment of this subsection.*

(C) **INSTITUTIONAL ACCOUNT.**—*The term “institutional account” has the same meaning given such term in Rule 4512 of the Financial Industry Regulatory Authority as of the date of the enactment of this subsection.*

(D) **MATERIAL CONFLICT OF INTEREST.**—*The term “material conflict of interest” means a financial interest of a broker or dealer (or registered representative) that a reasonable person would expect to affect the impartiality of a recommendation.*

(E) **REASONABLE DILIGENCE.**—*The term “reasonable diligence” has the meaning of such term as described in Rule 2111 of the Financial Industry Regulatory Authority as of the date of the enactment of this subsection.*

(F) **RECOMMENDATION.**—*The term “recommendation” means either of the following recommendations (under the meaning ascribed to such term in Rule 2111 of the Financial Industry Regulatory Authority) for which the broker or dealer (or registered representative) making the recommendation receives or will receive compensation:*

(i) *A non-discretionary recommendation to buy, hold, or sell securities, or to follow an investment strategy involving securities, for taxable or non-taxable accounts.*

(ii) A non-discretionary recommendation to rollover or transfer assets in an employer-sponsored retirement plan to an individual retirement account.

(G) **RETAIL CUSTOMER.**—The term “retail customer” means a natural person or legal entity, or the legal representative of such natural person or legal entity, in each case other than an institutional account, who—

(i) receives a recommendation from a broker or dealer (or registered representative); and

(ii) implements such recommendation with such broker or dealer primarily for personal, family, retirement, or household purposes.

(5) **SUPERSESSON.**—The provisions of this subsection shall supersede and preempt State law, other than a State law that regulates insurance products that are not securities, insofar as they may now or hereafter relate to a broker or dealer, or registered representative of a broker or dealer.

(6) **FIDUCIARY STATUS UNDER ERISA, THE INTERNAL REVENUE CODE, THE INVESTMENT ADVISERS ACT OF 1940, OR OTHER FIDUCIARY REGIMES.**—The fact that a person may owe, or may in fact comply with, the standard of conduct under this subsection shall not mean or create any presumption that such person is a “fiduciary” under the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1001 et seq.), section 4975 of the Internal Revenue Code of 1986, the Investment Advisers Act of 1940 (15 U.S.C. 80b et seq.), or any other Federal, State, or local statutory or regulatory fiduciary regime.

[(1) **OTHER MATTERS.**—The Commission shall—

[(1) facilitate the provision of simple and clear disclosures to investors regarding the terms of their relationships with brokers, dealers, and investment advisers, including any material conflicts of interest; and

[(2) examine and, where appropriate, promulgate rules prohibiting or restricting certain sales practices, conflicts of interest, and compensation schemes for brokers, dealers, and investment advisers that the Commission deems contrary to the public interest and the protection of investors.

[(m) **HARMONIZATION OF ENFORCEMENT.**—The enforcement authority of the Commission with respect to violations of the standard of conduct applicable to a broker or dealer providing personalized investment advice about securities to a retail customer shall include—

[(1) the enforcement authority of the Commission with respect to such violations provided under this Act; and

[(2) the enforcement authority of the Commission with respect to violations of the standard of conduct applicable to an investment adviser under the Investment Advisers Act of 1940, including the authority to impose sanctions for such violations, and

the Commission shall seek to prosecute and sanction violators of the standard of conduct applicable to a broker or dealer providing personalized investment advice about securities to a retail customer under this Act to same extent as the Commission prosecutes and sanctions violators of the standard of conduct applicable to an investment advisor under the Investment Advisers Act of 1940.]

(n) DISCLOSURES TO RETAIL INVESTORS.—

(1) IN GENERAL.—Notwithstanding any other provision of the securities laws, the Commission may issue rules designating documents or information that shall be provided by a broker or dealer to a retail investor before the purchase of an investment product or service by the retail investor.

(2) CONSIDERATIONS.—In developing any rules under paragraph (1), the Commission shall consider whether the rules will promote investor protection, efficiency, competition, and capital formation.

(3) FORM AND CONTENTS OF DOCUMENTS AND INFORMATION.—Any documents or information designated under a rule promulgated under paragraph (1) shall—

(A) be in a summary format; and

(B) contain clear and concise information about—

(i) investment objectives, strategies, costs, and risks; and

(ii) any compensation or other financial incentive received by a broker, dealer, or other intermediary in connection with the purchase of retail investment products.

(o) AUTHORITY TO RESTRICT MANDATORY PRE-DISPUTE ARBITRATION.—The Commission, by rule, may prohibit, or impose conditions or limitations on the use of, agreements that require customers or clients of any broker, dealer, or municipal securities dealer to arbitrate any future dispute between them arising under the Federal securities laws, the rules and regulations thereunder, or the rules of a self-regulatory organization if it finds that such prohibition, imposition of conditions, or limitations are in the public interest and for the protection of investors.

* * * * *

**SECTION 913 OF THE DODD-FRANK WALL STREET
REFORM AND CONSUMER PROTECTION ACT**

**ISEC. 913. STUDY AND RULEMAKING REGARDING OBLIGATIONS OF
BROKERS, DEALERS, AND INVESTMENT ADVISERS**

[(a) DEFINITION.—For purposes of this section, the term “retail customer” means a natural person, or the legal representative of such natural person, who—

[(1) receives personalized investment advice about securities from a broker or dealer or investment adviser; and

[(2) uses such advice primarily for personal, family, or household purposes.

[(b) STUDY.—The Commission shall conduct a study to evaluate—

[(1) the effectiveness of existing legal or regulatory standards of care for brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers for providing personalized investment advice and recommendations about securities to retail customers imposed by the Commission and a national securities association, and other Federal and State legal or regulatory standards; and

[(2) whether there are legal or regulatory gaps, shortcomings, or overlaps in legal or regulatory standards in the protection of retail customers relating to the standards of care for brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers for providing personalized investment advice about securities to retail customers that should be addressed by rule or statute.

[(c) CONSIDERATIONS.—In conducting the study required under subsection (b), the Commission shall consider—

[(1) the effectiveness of existing legal or regulatory standards of care for brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers for providing personalized investment advice and recommendations about securities to retail customers imposed by the Commission and a national securities association, and other Federal and State legal or regulatory standards;

[(2) whether there are legal or regulatory gaps, shortcomings, or overlaps in legal or regulatory standards in the protection of retail customers relating to the standards of care for brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers for providing personalized investment advice about securities to retail customers that should be addressed by rule or statute;

[(3) whether retail customers understand that there are different standards of care applicable to brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers in the provision of personalized investment advice about securities to retail customers;

[(4) whether the existence of different standards of care applicable to brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers is a source of confusion for retail customers regarding the quality of personalized investment advice that retail customers receive;

[(5) the regulatory, examination, and enforcement resources devoted to, and activities of, the Commission, the States, and a national securities association to enforce the standards of care for brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers when providing personalized investment advice and recommendations about securities to retail customers, including—

[(A) the effectiveness of the examinations of brokers, dealers, and investment advisers in determining compliance with regulations;

[(B) the frequency of the examinations; and

[(C) the length of time of the examinations;

[(6) the substantive differences in the regulation of brokers, dealers, and investment advisers, when providing personalized investment advice and recommendations about securities to retail customers;

[(7) the specific instances related to the provision of personalized investment advice about securities in which—

[(A) the regulation and oversight of investment advisers provide greater protection to retail customers than the regulation and oversight of brokers and dealers; and

[(B) the regulation and oversight of brokers and dealers provide greater protection to retail customers than the regulation and oversight of investment advisers;

[(8) the existing legal or regulatory standards of State securities regulators and other regulators intended to protect retail customers;

[(9) the potential impact on retail customers, including the potential impact on access of retail customers to the range of products and services offered by brokers and dealers, of imposing upon brokers, dealers, and persons associated with brokers or dealers—

[(A) the standard of care applied under the Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.) for providing personalized investment advice about securities to retail customers of investment advisers, as interpreted by the Commission and the courts; and

[(B) other requirements of the Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.);

[(10) the potential impact of eliminating the broker and dealer exclusion from the definition of “investment adviser” under section 202(a)(11)(C) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)(11)(C)), in terms of—

[(A) the impact and potential benefits and harm to retail customers that could result from such a change, including any potential impact on access to personalized investment advice and recommendations about securities to retail customers or the availability of such advice and recommendations;

[(B) the number of additional entities and individuals that would be required to register under, or become subject to, the Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.), and the additional requirements to which brokers, dealers, and persons associated with brokers and dealers would become subject, including—

[(i) any potential additional associated person licensing, registration, and examination requirements; and

[(ii) the additional costs, if any, to the additional entities and individuals; and

[(C) the impact on Commission and State resources to—

[(i) conduct examinations of registered investment advisers and the representatives of registered investment advisers, including the impact on the examination cycle; and

[(ii) enforce the standard of care and other applicable requirements imposed under the Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.);

[(11) the varying level of services provided by brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers to re-

tail customers and the varying scope and terms of retail customer relationships of brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers with such retail customers;

[(12) the potential impact upon retail customers that could result from potential changes in the regulatory requirements or legal standards of care affecting brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers relating to their obligations to retail customers regarding the provision of investment advice, including any potential impact on—

[(A) protection from fraud;

[(B) access to personalized investment advice, and recommendations about securities to retail customers; or

[(C) the availability of such advice and recommendations;

[(13) the potential additional costs and expenses to—

[(A) retail customers regarding and the potential impact on the profitability of their investment decisions; and

[(B) brokers, dealers, and investment advisers resulting from potential changes in the regulatory requirements or legal standards affecting brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers relating to their obligations, including duty of care, to retail customers; and

[(14) any other consideration that the Commission considers necessary and appropriate in determining whether to conduct a rulemaking under subsection (f).

[(d) REPORT.—

[(1) IN GENERAL.—Not later than 6 months after the date of enactment of this Act, the Commission shall submit a report on the study required under subsection (b) to—

[(A) the Committee on Banking, Housing, and Urban Affairs of the Senate; and

[(B) the Committee on Financial Services of the House of Representatives.

[(2) CONTENT REQUIREMENTS.—The report required under paragraph (1) shall describe the findings, conclusions, and recommendations of the Commission from the study required under subsection (b), including—

[(A) a description of the considerations, analysis, and public and industry input that the Commission considered, as required under subsection (b), to make such findings, conclusions, and policy recommendations; and

[(B) an analysis of whether any identified legal or regulatory gaps, shortcomings, or overlap in legal or regulatory standards in the protection of retail customers relating to the standards of care for brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers for providing personalized investment advice about securities to retail customers.

[(e) PUBLIC COMMENT.—The Commission shall seek and consider public input, comments, and data in order to prepare the report required under subsection (d).

[(f) RULEMAKING.—The Commission may commence a rulemaking, as necessary or appropriate in the public interest and for the protection of retail customers (and such other customers as the Commission may by rule provide), to address the legal or regulatory standards of care for brokers, dealers, investment advisers, persons associated with brokers or dealers, and persons associated with investment advisers for providing personalized investment advice about securities to such retail customers. The Commission shall consider the findings conclusions, and recommendations of the study required under subsection (b).

[(g) AUTHORITY TO ESTABLISH A FIDUCIARY DUTY FOR BROKERS AND DEALERS.—

[(1) SECURITIES EXCHANGE ACT OF 1934.—Section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 78o) is amended by adding at the end the following:

[(k) STANDARD OF CONDUCT.—

[(1) IN GENERAL.—Notwithstanding any other provision of this Act or the Investment Advisers Act of 1940, the Commission may promulgate rules to provide that, with respect to a broker or dealer, when providing personalized investment advice about securities to a retail customer (and such other customers as the Commission may by rule provide), the standard of conduct for such broker or dealer with respect to such customer shall be the same as the standard of conduct applicable to an investment adviser under section 211 of the Investment Advisers Act of 1940. The receipt of compensation based on commission or other standard compensation for the sale of securities shall not, in and of itself, be considered a violation of such standard applied to a broker or dealer. Nothing in this section shall require a broker or dealer or registered representative to have a continuing duty of care or loyalty to the customer after providing personalized investment advice about securities.

[(2) DISCLOSURE OF RANGE OF PRODUCTS OFFERED.—Where a broker or dealer sells only proprietary or other limited range of products, as determined by the Commission, the Commission may by rule require that such broker or dealer provide notice to each retail customer and obtain the consent or acknowledgment of the customer. The sale of only proprietary or other limited range of products by a broker or dealer shall not, in and of itself, be considered a violation of the standard set forth in paragraph (1).

[(1) OTHER MATTERS.—The Commission shall—

[(1) facilitate the provision of simple and clear disclosures to investors regarding the terms of their relationships with brokers, dealers, and investment advisers, including any material conflicts of interest; and

[(2) examine and, where appropriate, promulgate rules prohibiting or restricting certain sales practices, conflicts of interest, and compensation schemes for brokers, dealers, and investment advisers that the Commission deems contrary to the public interest and the protection of investors.”

[(2) INVESTMENT ADVISERS ACT OF 1940.—Section 211 of the Investment Advisers Act of 1940, is further amended by adding at the end the following new subsections:

[(g) STANDARD OF CONDUCT.—

[(1) IN GENERAL.—The Commission may promulgate rules to provide that the standard of conduct for all brokers, dealers, and investment advisers, when providing personalized investment advice about securities to retail customers (and such other customers as the Commission may by rule provide), shall be to act in the best interest of the customer without regard to the financial or other interest of the broker, dealer, or investment adviser providing the advice. In accordance with such rules, any material conflicts of interest shall be disclosed and may be consented to by the customer. Such rules shall provide that such standard of conduct shall be no less stringent than the standard applicable to investment advisers under section 206(1) and (2) of this Act when providing personalized investment advice about securities, except the Commission shall not ascribe a meaning to the term ‘customer’ that would include an investor in a private fund managed by an investment adviser, where such private fund has entered into an advisory contract with such adviser. The receipt of compensation based on commission or fees shall not, in and of itself, be considered a violation of such standard applied to a broker, dealer, or investment adviser.

[(2) RETAIL CUSTOMER DEFINED.—For purposes of this subsection, the term ‘retail customer’ means a natural person, or the legal representative of such natural person, who—

[(A) receives personalized investment advice about securities from a broker, dealer, or investment adviser; and

[(B) uses such advice primarily for personal, family, or household purposes.

[(h) OTHER MATTERS.—The Commission shall—

[(1) facilitate the provision of simple and clear disclosures to investors regarding the terms of their relationships with brokers, dealers, and investment advisers, including any material conflicts of interest; and

[(2) examine and, where appropriate, promulgate rules prohibiting or restricting certain sales practices, conflicts of interest, and compensation schemes for brokers, dealers, and investment advisers that the Commission deems contrary to the public interest and the protection of investors.”.

[(h) HARMONIZATION OF ENFORCEMENT.—

[(1) SECURITIES EXCHANGE ACT OF 1934.—Section 15 of the Securities Exchange Act of 1934, as amended by subsection (g)(1), is further amended by adding at the end the following new subsection:

[(m) HARMONIZATION OF ENFORCEMENT.—The enforcement authority of the Commission with respect to violations of the standard of conduct applicable to a broker or dealer providing personalized investment advice about securities to a retail customer shall include—

[(1) the enforcement authority of the Commission with respect to such violations provided under this Act; and

[(2) the enforcement authority of the Commission with respect to violations of the standard of conduct applicable to an investment adviser under the Investment Advisers Act of 1940,

including the authority to impose sanctions for such violations, and the Commission shall seek to prosecute and sanction violators of the standard of conduct applicable to a broker or dealer providing personalized investment advice about securities to a retail customer under this Act to same extent as the Commission prosecutes and sanctions violators of the standard of conduct applicable to an investment advisor under the Investment Advisers Act of 1940.”.

【(2) INVESTMENT ADVISERS ACT OF 1940.—Section 211 of the Investment Advisers Act of 1940, as amended by subsection (g)(2), is further amended by adding at the end the following new subsection:

【“(i) HARMONIZATION OF ENFORCEMENT.—The enforcement authority of the Commission with respect to violations of the standard of conduct applicable to an investment adviser shall include—

【“(1) the enforcement authority of the Commission with respect to such violations provided under this Act; and

【“(2) the enforcement authority of the Commission with respect to violations of the standard of conduct applicable to a broker or dealer providing personalized investment advice about securities to a retail customer under the Securities Exchange Act of 1934, including the authority to impose sanctions for such violations, and

the Commission shall seek to prosecute and sanction violators of the standard of conduct applicable to an investment adviser under this Act to same extent as the Commission prosecutes and sanctions violators of the standard of conduct applicable to a broker or dealer providing personalized investment advice about securities to a retail customer under the Securities Exchange Act of 1934.”.】

SEC. 913. OBLIGATIONS OF BROKERS AND DEALERS AND OTHER PERSONS AND ENTITIES.

(a) RULEMAKING.—

(1) RULEMAKING BY THE COMMISSION.—*The Commission may issue regulations as the Commission determines is necessary to facilitate compliance by brokers and dealers (including their registered representative) with the obligations of such brokers and dealers (and their registered representative) under the second subsection (k) of section 15 of the Securities Exchange Act of 1934 only if such rulemaking does not impose any obligation related to standard of care on a broker or dealer (or its registered representative) that is in addition to, duplicative of, or inconsistent with, the obligations set forth in such subsection.*

(2) RULEMAKING BY THE SECRETARY OF LABOR AND THE SECRETARY OF THE TREASURY.—*After the date of the enactment of the PASS Act of 2017, the Secretary of Labor and the Secretary of the Treasury shall not promulgate any regulation under the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1001 et seq.) or section 4975 of the Internal Revenue Code of 1986, respectively, defining the circumstances under which a person is considered a fiduciary that would impose any obligation on a broker or dealer (or its registered representative) or on a life insurer fulfilling the term “insurance company” as defined in section 3(a)(2) of the Securities Act of 1933 (or its agents or distributors) that is in addition to, duplicative of, or inconsistent with, the obligations set forth in such subsection (k) of*

section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 78o).

(b) EXEMPTION AVAILABLE TO CERTAIN PERSONS WITH RESPECT TO MANUFACTURE OR SALE OF ANNUITIES.—

(1) EXEMPTION.—With respect to the manufacture or sale of annuities within paragraphs (2) or (8) of section 3(a) of the Securities Act of 1933 (15 U.S.C. 77c(a)) or section 989J of the Dodd-Frank Wall Street Reform and Consumer Protection Act (15 U.S.C. 77c note), a person regulated by a State insurance regulator may rely on the exemptions in section 408(b)(21) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1108(b)(21)) and section 4975(d)(24) of the Internal Revenue Code of 1986 (as added by the PASS Act of 2017) only if—

(A) such person adopts and implements practices on a nationwide basis for the sale of annuity contracts that meet or exceed the minimum requirements set forth in the second subsection (k) of section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 78o) and such person is subject to regulation or examination by a State insurance regulator for purposes of assessing market conduct; or

(B) such person complies with a standard substantially similar to such subsection (k) and is regulated by a State insurance regulator with respect to annuities within paragraphs (2) or (8) of section 3(a) of the Securities Act of 1933 (15 U.S.C. 77c(a)) or section 989J of the Dodd-Frank Wall Street Reform and Consumer Protection Act (15 U.S.C. 77c note).

(2) COORDINATION AND COOPERATION.—Upon the request of any State insurance regulator, the Commission or the Financial Industry Regulatory Authority shall provide such reasonable assistance to the requesting Authority as needed in connection with the coordination or implementation of this section.

(3) DEFINITION OF STATE INSURANCE REGULATOR.—As used in this subsection, the term “State insurance regulator” means the principal insurance regulatory authority of a State, the District of Columbia, any territory of the United States, Puerto Rico, Guam, American Samoa, the Trust Territory of the Pacific Islands, the Virgin Islands, and the Northern Mariana Islands.

(c) ADDITIONAL EXEMPTIONS.—*A person who complies with a standard substantially similar to the second subsection (k) of section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 78o) may rely on the exemptions in section 408(b)(21) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1108(b)(21)) and section 4975(d)(24) of the Internal Revenue Code of 1986 (as added by the PASS Act of 2017) only if such person is—*

(1) registered as an investment adviser under the Investment Advisers Act of 1940 (15 U.S.C. 80b–1 et seq.) or under the laws of the State in which the person maintains its principal office and place of business; or

(2) a bank or similar financial institution supervised by the United States or a State, or a savings association (as defined in section 3(b)(1) of the Federal Deposit Insurance Act (12 U.S.C. 1813(b)(1)).

**EMPLOYEE RETIREMENT INCOME SECURITY ACT OF
1974**

* * * * *

TITLE I—PROTECTION OF EMPLOYEE BENEFIT RIGHTS

* * * * *

SUBTITLE B—REGULATORY PROVISIONS

* * * * *

PART 4—FIDUCIARY RESPONSIBILITY

* * * * *

EXEMPTIONS FROM PROHIBITED TRANSACTIONS

SEC. 408. (a) The Secretary shall establish an exemption procedure for purposes of this subsection. Pursuant to such procedure, he may grant a conditional or unconditional exemption of any fiduciary or transaction, or class of fiduciaries or transactions, from all or part of the restrictions imposed by sections 406 and 407(a). Action under this subsection may be taken only after consultation and coordination with the Secretary of the Treasury. An exemption granted under this section shall not relieve a fiduciary from any other applicable provision of this Act. The Secretary may not grant an exemption under this subsection unless he finds that such exemption is—

- (1) administratively feasible,
- (2) in the interests of the plan and of its participants and beneficiaries, and
- (3) protective of the rights of participants and beneficiaries of such plan.

Before granting an exemption under this subsection from section 406(a) or 407(a), the Secretary shall publish notice in the Federal Register of the pendency of the exemption, shall require that adequate notice be given to interested persons, and shall afford interested persons opportunity to present views. The Secretary may not grant an exemption under this subsection from section 406(b) unless he affords an opportunity for a hearing and makes a determination on the record with respect to the findings required by paragraphs (1), (2), and (3) of this subsection.

(b) The prohibitions provided in section 406 shall not apply to any of the following transactions:

- (1) Any loans made by the plan to parties in interest who are participants or beneficiaries of the plan if such loans (A) are available to all such participants and beneficiaries on a reasonably equivalent basis, (B) are not made available to highly compensated employees (within the meaning of section 414(q) of the Internal Revenue Code of 1986) in an amount greater than the amount made available to other employees, (C) are made in accordance with specific provisions regarding such loans set forth in the plan, (D) bear a reasonable rate of interest, and (E) are adequately secured. A loan made by a plan shall not fail to meet the requirements of the preceding sen-

tence by reason of a loan repayment suspension described under section 414(u)(4) of the Internal Revenue Code of 1986.

(2) Contracting or making reasonable arrangements with a party in interest for office space, or legal, accounting, or other services necessary for the establishment or operation of the plan, if no more than reasonable compensation is paid therefor.

(3) A loan to an employee stock ownership plan (as defined in section 407(d)(6)), if—

(A) such loan is primarily for the benefit of participants and beneficiaries of the plan, and

(B) such loan is at an interest rate which is not in excess of a reasonable rate.

If the plan gives collateral to a party in interest for such loan, such collateral may consist only of qualifying employer securities (as defined in section 407(d)(5)).

(4) The investment of all or part of a plan's assets in deposits which bear a reasonable interest rate in a bank or similar financial institution supervised by the United States or a State, if such bank or other institution is a fiduciary of such plan and if—

(A) the plan covers only employees of such bank or other institution and employees of affiliates of such bank or other institution, or

(B) such investment is expressly authorized by a provision of the plan or by a fiduciary (other than such bank or institution or affiliate thereof) who is expressly empowered by the plan to so instruct the trustee with respect to such investment.

(5) Any contract for life insurance, health insurance, or annuities with one or more insurers which are qualified to do business in a State, if the plan pays no more than adequate consideration, and if each such insurer or insurers is—

(A) the employer maintaining the plan, or

(B) a party in interest which is wholly owned (directly or indirectly) by the employer maintaining the plan, or by any person which is a party in interest with respect to the plan, but only if the total premiums and annuity considerations written by such insurers for life insurance, health insurance, or annuities for all plans (and their employers) with respect to which such insurers are parties in interest (not including premiums or annuity considerations written by the employer maintaining the plan) do not exceed 5 percent of the total premiums and annuity considerations written for all lines of insurance in that year by such insurers (not including premiums or annuity considerations written by the employer maintaining the plan).

(6) The providing of any ancillary service by a bank or similar financial institution supervised by the United States or a State, if such bank or other institution is a fiduciary of such plan, and if—

(A) such bank or similar financial institution has adopted adequate internal safeguards which assure that the providing of such ancillary service is consistent with sound banking and financial practice, as determined by Federal or State supervisory authority, and

(B) the extent to which such ancillary service is provided is subject to specific guidelines issued by such bank or similar financial institution (as determined by the Secretary after consultation with Federal and State supervisory authority), and adherence to such guidelines would reasonably preclude such bank or similar financial institution from providing such ancillary service (i) in an excessive or unreasonable manner, and (ii) in a manner that would be inconsistent with the best interests of participants and beneficiaries of employee benefit plans. Such ancillary services shall not be provided at more than reasonable compensation.

(7) The exercise of a privilege to convert securities, to the extent provided in regulations of the Secretary, but only if the plan receives no less than adequate consideration pursuant to such conversion.

(8) Any transaction between a plan and (i) a common or collective trust fund or pooled investment fund maintained by a party in interest which is a bank or trust company supervised by a State or Federal agency or (ii) a pooled investment fund of an insurance company qualified to do business in a State, if—

(A) the transaction is a sale or purchase of an interest in the fund,

(B) the bank, trust company, or insurance company receives not more than reasonable compensation, and

(C) such transaction is expressly permitted by the instrument under which the plan is maintained, or by a fiduciary (other than the bank, trust company, or insurance company, or an affiliate thereof) who has authority to manage and control the assets of the plan.

(9) The making by a fiduciary of a distribution of the assets of the plan in accordance with the terms of the plan if such assets are distributed in the same manner as provided under section 4044 of this Act (relating to allocation of assets).

(10) Any transaction required or permitted under part 1 of subtitle E of title IV.

(11) A merger of multiemployer plans, or the transfer of assets or liabilities between multiemployer plans, determined by the Pension Benefit Guaranty Corporation to meet the requirements of section 4231.

(12) The sale by a plan to a party in interest on or after December 18, 1987, of any stock, if—

(A) the requirements of paragraphs (1) and (2) of subsection (e) are met with respect to such stock,

(B) on the later of the date on which the stock was acquired by the plan, or January 1, 1975, such stock constituted a qualifying employer security (as defined in section 407(d)(5) as then in effect), and

(C) such stock does not constitute a qualifying employer security (as defined in section 407(d)(5) as in effect at the time of the sale).

(13) Any transfer made before January 1, 2026, of excess pension assets from a defined benefit plan to a retiree health account in a qualified transfer permitted under section 420 of

the Internal Revenue Code of 1986 (as in effect on the date of the enactment of the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015).

(14) Any transaction in connection with the provision of investment advice described in section 3(21)(A)(ii) to a participant or beneficiary of an individual account plan that permits such participant or beneficiary to direct the investment of assets in their individual account, if—

(A) the transaction is—

(i) the provision of the investment advice to the participant or beneficiary of the plan with respect to a security or other property available as an investment under the plan,

(ii) the acquisition, holding, or sale of a security or other property available as an investment under the plan pursuant to the investment advice, or

(iii) the direct or indirect receipt of fees or other compensation by the fiduciary adviser or an affiliate thereof (or any employee, agent, or registered representative of the fiduciary adviser or affiliate) in connection with the provision of the advice or in connection with an acquisition, holding, or sale of a security or other property available as an investment under the plan pursuant to the investment advice; and

(B) the requirements of subsection (g) are met.

(15)(A) Any transaction involving the purchase or sale of securities, or other property (as determined by the Secretary), between a plan and a party in interest (other than a fiduciary described in section 3(21)(A)) with respect to a plan if—

(i) the transaction involves a block trade,

(ii) at the time of the transaction, the interest of the plan (together with the interests of any other plans maintained by the same plan sponsor), does not exceed 10 percent of the aggregate size of the block trade,

(iii) the terms of the transaction, including the price, are at least as favorable to the plan as an arm's length transaction, and

(iv) the compensation associated with the purchase and sale is not greater than the compensation associated with an arm's length transaction with an unrelated party.

(B) For purposes of this paragraph, the term "block trade" means any trade of at least 10,000 shares or with a market value of at least \$200,000 which will be allocated across two or more unrelated client accounts of a fiduciary.

(16) Any transaction involving the purchase or sale of securities, or other property (as determined by the Secretary), between a plan and a party in interest if—

(A) the transaction is executed through an electronic communication network, alternative trading system, or similar execution system or trading venue subject to regulation and oversight by—

(i) the applicable Federal regulating entity, or

(ii) such foreign regulatory entity as the Secretary may determine by regulation,

(B) either—

(i) the transaction is effected pursuant to rules designed to match purchases and sales at the best price available through the execution system in accordance with applicable rules of the Securities and Exchange Commission or other relevant governmental authority, or

(ii) neither the execution system nor the parties to the transaction take into account the identity of the parties in the execution of trades,

(C) the price and compensation associated with the purchase and sale are not greater than the price and compensation associated with an arm's length transaction with an unrelated party,

(D) if the party in interest has an ownership interest in the system or venue described in subparagraph (A), the system or venue has been authorized by the plan sponsor or other independent fiduciary for transactions described in this paragraph, and

(E) not less than 30 days prior to the initial transaction described in this paragraph executed through any system or venue described in subparagraph (A), a plan fiduciary is provided written or electronic notice of the execution of such transaction through such system or venue.

(17)(A) Transactions described in subparagraphs (A), (B), and (D) of section 406(a)(1) between a plan and a person that is a party in interest other than a fiduciary (or an affiliate) who has or exercises any discretionary authority or control with respect to the investment of the plan assets involved in the transaction or renders investment advice (within the meaning of section 3(21)(A)(ii)) with respect to those assets, solely by reason of providing services to the plan or solely by reason of a relationship to such a service provider described in subparagraph (F), (G), (H), or (I) of section 3(14), or both, but only if in connection with such transaction the plan receives no less, nor pays no more, than adequate consideration.

(B) For purposes of this paragraph, the term "adequate consideration" means—

(i) in the case of a security for which there is a generally recognized market—

(I) the price of the security prevailing on a national securities exchange which is registered under section 6 of the Securities Exchange Act of 1934, taking into account factors such as the size of the transaction and marketability of the security, or

(II) if the security is not traded on such a national securities exchange, a price not less favorable to the plan than the offering price for the security as established by the current bid and asked prices quoted by persons independent of the issuer and of the party in interest, taking into account factors such as the size of the transaction and marketability of the security, and

(ii) in the case of an asset other than a security for which there is a generally recognized market, the fair market value of the asset as determined in good faith by a fi-

duciary or fiduciaries in accordance with regulations prescribed by the Secretary.

(18) FOREIGN EXCHANGE TRANSACTIONS.—Any foreign exchange transactions, between a bank or broker-dealer (or any affiliate of either), and a plan (as defined in section 3(3)) with respect to which such bank or broker-dealer (or affiliate) is a trustee, custodian, fiduciary, or other party in interest, if—

(A) the transaction is in connection with the purchase, holding, or sale of securities or other investment assets (other than a foreign exchange transaction unrelated to any other investment in securities or other investment assets),

(B) at the time the foreign exchange transaction is entered into, the terms of the transaction are not less favorable to the plan than the terms generally available in comparable arm's length foreign exchange transactions between unrelated parties, or the terms afforded by the bank or broker-dealer (or any affiliate of either) in comparable arm's-length foreign exchange transactions involving unrelated parties,

(C) the exchange rate used by such bank or broker-dealer (or affiliate) for a particular foreign exchange transaction does not deviate by more than 3 percent from the interbank bid and asked rates for transactions of comparable size and maturity at the time of the transaction as displayed on an independent service that reports rates of exchange in the foreign currency market for such currency, and

(D) the bank or broker-dealer (or any affiliate of either) does not have investment discretion, or provide investment advice, with respect to the transaction.

(19) CROSS TRADING.—Any transaction described in sections 406(a)(1)(A) and 406(b)(2) involving the purchase and sale of a security between a plan and any other account managed by the same investment manager, if—

(A) the transaction is a purchase or sale, for no consideration other than cash payment against prompt delivery of a security for which market quotations are readily available,

(B) the transaction is effected at the independent current market price of the security (within the meaning of section 270.17a-7(b) of title 17, Code of Federal Regulations),

(C) no brokerage commission, fee (except for customary transfer fees, the fact of which is disclosed pursuant to subparagraph (D)), or other remuneration is paid in connection with the transaction,

(D) a fiduciary (other than the investment manager engaging in the cross-trades or any affiliate) for each plan participating in the transaction authorizes in advance of any cross-trades (in a document that is separate from any other written agreement of the parties) the investment manager to engage in cross trades at the investment manager's discretion, after such fiduciary has received disclosure regarding the conditions under which cross trades may take place (but only if such disclosure is separate

from any other agreement or disclosure involving the asset management relationship), including the written policies and procedures of the investment manager described in subparagraph (H),

(E) each plan participating in the transaction has assets of at least \$100,000,000, except that if the assets of a plan are invested in a master trust containing the assets of plans maintained by employers in the same controlled group (as defined in section 407(d)(7)), the master trust has assets of at least \$100,000,000,

(F) the investment manager provides to the plan fiduciary who authorized cross trading under subparagraph (D) a quarterly report detailing all cross trades executed by the investment manager in which the plan participated during such quarter, including the following information, as applicable: (i) the identity of each security bought or sold; (ii) the number of shares or units traded; (iii) the parties involved in the cross-trade; and (iv) trade price and the method used to establish the trade price,

(G) the investment manager does not base its fee schedule on the plan's consent to cross trading, and no other service (other than the investment opportunities and cost savings available through a cross trade) is conditioned on the plan's consent to cross trading,

(H) the investment manager has adopted, and cross-trades are effected in accordance with, written cross-trading policies and procedures that are fair and equitable to all accounts participating in the cross-trading program, and that include a description of the manager's pricing policies and procedures, and the manager's policies and procedures for allocating cross trades in an objective manner among accounts participating in the cross-trading program, and

(I) the investment manager has designated an individual responsible for periodically reviewing such purchases and sales to ensure compliance with the written policies and procedures described in subparagraph (H), and following such review, the individual shall issue an annual written report no later than 90 days following the period to which it relates signed under penalty of perjury to the plan fiduciary who authorized cross trading under subparagraph (D) describing the steps performed during the course of the review, the level of compliance, and any specific instances of non-compliance.

The written report under subparagraph (I) shall also notify the plan fiduciary of the plan's right to terminate participation in the investment manager's cross-trading program at any time.

(20)(A) Except as provided in subparagraphs (B) and (C), a transaction described in section 406(a) in connection with the acquisition, holding, or disposition of any security or commodity, if the transaction is corrected before the end of the correction period.

(B) Subparagraph (A) does not apply to any transaction between a plan and a plan sponsor or its affiliates that involves the acquisition or sale of an employer security (as defined in

section 407(d)(1) or the acquisition, sale, or lease of employer real property (as defined in section 407(d)(2)).

(C) In the case of any fiduciary or other party in interest (or any other person knowingly participating in such transaction), subparagraph (A) does not apply to any transaction if, at the time the transaction occurs, such fiduciary or party in interest (or other person) knew (or reasonably should have known) that the transaction would (without regard to this paragraph) constitute a violation of section 406(a).

(D) For purposes of this paragraph, the term “correction period” means, in connection with a fiduciary or party in interest (or other person knowingly participating in the transaction), the 14-day period beginning on the date on which such fiduciary or party in interest (or other person) discovers, or reasonably should have discovered, that the transaction would (without regard to this paragraph) constitute a violation of section 406(a).

(E) For purposes of this paragraph—

(i) The term “security” has the meaning given such term by section 475(c)(2) of the Internal Revenue Code of 1986 (without regard to subparagraph (F)(iii) and the last sentence thereof).

(ii) The term “commodity” has the meaning given such term by section 475(e)(2) of such Code (without regard to subparagraph (D)(iii) thereof).

(iii) The term “correct” means, with respect to a transaction—

(I) to undo the transaction to the extent possible and in any case to make good to the plan or affected account any losses resulting from the transaction, and

(II) to restore to the plan or affected account any profits made through the use of assets of the plan.

(21) *Any transaction involving a recommendation made by a broker or dealer (including its registered representative), or other persons or entities, that is subject to the requirements of the second subsection (k) of section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 78o(k)).*

(c) Nothing in section 406 shall be construed to prohibit any fiduciary from—

(1) receiving any benefit to which he may be entitled as a participant or beneficiary in the plan, so long as the benefit is computed and paid on a basis which is consistent with the terms of the plan as applied to all other participants and beneficiaries;

(2) receiving any reasonable compensation for services rendered, or for the reimbursement of expenses properly and actually incurred, in the performance of his duties with the plan; except that no person so serving who already receives full time pay from an employer or an association of employers, whose employees are participants in the plan, or from an employee organization whose members are participants in such plan shall receive compensation from such plan, except for reimbursement of expenses properly and actually incurred; or

(3) serving as a fiduciary in addition to being an officer, employee, agent, or other representative of a party in interest.

(d)(1) Section 407(b) and subsections (b), (c), and (e) of this section shall not apply to a transaction in which a plan directly or indirectly—

- (A) lends any part of the corpus or income of the plan to,
- (B) pays any compensation for personal services rendered to the plan to, or
- (C) acquires for the plan any property from, or sells any property to,

any person who is with respect to the plan an owner-employee (as defined in section 401(c)(3) of the Internal Revenue Code of 1986), a member of the family (as defined in section 267(c)(4) of such Code) of any such owner-employee, or any corporation in which any such owner-employee owns, directly or indirectly, 50 percent or more of the total combined voting power of all classes of stock entitled to vote or 50 percent or more of the total value of shares of all classes of stock of the corporation.

(2)(A) For purposes of paragraph (1), the following shall be treated as owner-employees:

- (i) A shareholder-employee.
- (ii) A participant or beneficiary of an individual retirement plan (as defined in section 7701(a)(37) of the Internal Revenue Code of 1986).
- (iii) An employer or association of employees which establishes such an individual retirement plan under section 408(c) of such Code.

(B) Paragraph (1)(C) shall not apply to a transaction which consists of a sale of employer securities to an employee stock ownership plan (as defined in section 407(d)(6)) by a shareholder-employee, a member of the family (as defined in section 267(c)(4) of such Code) of any such owner-employee, or a corporation in which such a shareholder-employee owns stock representing a 50 percent or greater interest described in paragraph (1).

(C) For purposes of paragraph (1)(A), the term “owner-employee” shall only include a person described in clause (ii) or (iii) of subparagraph (A).

(3) For purposes of paragraph (2), the term “shareholder-employee” means an employee or officer of an S corporation (as defined in section 1361(a)(1) of such Code) who owns (or is considered as owning within the meaning of section 318(a)(1) of such Code) more than 5 percent of the outstanding stock of the corporation on any day during the taxable year of such corporation.

(e) Sections 406 and 407 shall not apply to the acquisition or sale by a plan of qualifying employer securities (as defined in section 407(d)(5)) or acquisition, sale or lease by a plan of qualifying employer real property (as defined in section 407(d)(4))—

- (1) if such acquisition, sale, or lease is for adequate consideration (or in the case of a marketable obligation, at a price not less favorable to the plan than the price determined under section 407(e)(1)),
- (2) if no commission is charged with respect thereto, and
- (3) if—

(A) the plan is an eligible individual account plan (as defined in section 407(d)(3)), or

(B) in the case of an acquisition or lease of qualifying employer real property by a plan which is not an eligible

individual account plan, or of an acquisition of qualifying employer securities by such a plan, the lease or acquisition is not prohibited by section 407(a).

(f) Section 406(b)(2) shall not apply to any merger or transfer described in subsection (b)(11).

(g) PROVISION OF INVESTMENT ADVICE TO PARTICIPANT AND BENEFICIARIES.—

(1) IN GENERAL.—The prohibitions provided in section 406 shall not apply to transactions described in subsection (b)(14) if the investment advice provided by a fiduciary adviser is provided under an eligible investment advice arrangement.

(2) ELIGIBLE INVESTMENT ADVICE ARRANGEMENT.—For purposes of this subsection, the term “eligible investment advice arrangement” means an arrangement—

(A) which either—

(i) provides that any fees (including any commission or other compensation) received by the fiduciary adviser for investment advice or with respect to the sale, holding, or acquisition of any security or other property for purposes of investment of plan assets do not vary depending on the basis of any investment option selected, or

(ii) uses a computer model under an investment advice program meeting the requirements of paragraph (3) in connection with the provision of investment advice by a fiduciary adviser to a participant or beneficiary, and

(B) with respect to which the requirements of paragraph (4), (5), (6), (7), (8), and (9) are met.

(3) INVESTMENT ADVICE PROGRAM USING COMPUTER MODEL.—

(A) IN GENERAL.—An investment advice program meets the requirements of this paragraph if the requirements of subparagraphs (B), (C), and (D) are met.

(B) COMPUTER MODEL.—The requirements of this subparagraph are met if the investment advice provided under the investment advice program is provided pursuant to a computer model that—

(i) applies generally accepted investment theories that take into account the historic returns of different asset classes over defined periods of time,

(ii) utilizes relevant information about the participant, which may include age, life expectancy, retirement age, risk tolerance, other assets or sources of income, and preferences as to certain types of investments,

(iii) utilizes prescribed objective criteria to provide asset allocation portfolios comprised of investment options available under the plan,

(iv) operates in a manner that is not biased in favor of investments offered by the fiduciary adviser or a person with a material affiliation or contractual relationship with the fiduciary adviser, and

(v) takes into account all investment options under the plan in specifying how a participant’s account bal-

ance should be invested and is not inappropriately weighted with respect to any investment option.

(C) CERTIFICATION.—

(i) IN GENERAL.—The requirements of this subparagraph are met with respect to any investment advice program if an eligible investment expert certifies, prior to the utilization of the computer model and in accordance with rules prescribed by the Secretary, that the computer model meets the requirements of subparagraph (B).

(ii) RENEWAL OF CERTIFICATIONS.—If, as determined under regulations prescribed by the Secretary, there are material modifications to a computer model, the requirements of this subparagraph are met only if a certification described in clause (i) is obtained with respect to the computer model as so modified.

(iii) ELIGIBLE INVESTMENT EXPERT.—The term “eligible investment expert” means any person—

(I) which meets such requirements as the Secretary may provide, and

(II) does not bear any material affiliation or contractual relationship with any investment adviser or a related person thereof (or any employee, agent, or registered representative of the investment adviser or related person).

(D) EXCLUSIVITY OF RECOMMENDATION.—The requirements of this subparagraph are met with respect to any investment advice program if—

(i) the only investment advice provided under the program is the advice generated by the computer model described in subparagraph (B), and

(ii) any transaction described in subsection (b)(14)(A)(ii) occurs solely at the direction of the participant or beneficiary.

Nothing in the preceding sentence shall preclude the participant or beneficiary from requesting investment advice other than that described in subparagraph (A), but only if such request has not been solicited by any person connected with carrying out the arrangement.

(4) EXPRESS AUTHORIZATION BY SEPARATE FIDUCIARY.—The requirements of this paragraph are met with respect to an arrangement if the arrangement is expressly authorized by a plan fiduciary other than the person offering the investment advice program, any person providing investment options under the plan, or any affiliate of either.

(5) ANNUAL AUDIT.—The requirements of this paragraph are met if an independent auditor, who has appropriate technical training or experience and proficiency and so represents in writing—

(A) conducts an annual audit of the arrangement for compliance with the requirements of this subsection, and

(B) following completion of the annual audit, issues a written report to the fiduciary who authorized use of the arrangement which presents its specific findings regarding

compliance of the arrangement with the requirements of this subsection.

For purposes of this paragraph, an auditor is considered independent if it is not related to the person offering the arrangement to the plan and is not related to any person providing investment options under the plan.

(6) DISCLOSURE.—The requirements of this paragraph are met if—

(A) the fiduciary adviser provides to a participant or a beneficiary before the initial provision of the investment advice with regard to any security or other property offered as an investment option, a written notification (which may consist of notification by means of electronic communication)—

(i) of the role of any party that has a material affiliation or contractual relationship with the fiduciary adviser in the development of the investment advice program and in the selection of investment options available under the plan,

(ii) of the past performance and historical rates of return of the investment options available under the plan,

(iii) of all fees or other compensation relating to the advice that the fiduciary adviser or any affiliate thereof is to receive (including compensation provided by any third party) in connection with the provision of the advice or in connection with the sale, acquisition, or holding of the security or other property,

(iv) of any material affiliation or contractual relationship of the fiduciary adviser or affiliates thereof in the security or other property,

(v) the manner, and under what circumstances, any participant or beneficiary information provided under the arrangement will be used or disclosed,

(vi) of the types of services provided by the fiduciary adviser in connection with the provision of investment advice by the fiduciary adviser,

(vii) that the adviser is acting as a fiduciary of the plan in connection with the provision of the advice, and

(viii) that a recipient of the advice may separately arrange for the provision of advice by another adviser, that could have no material affiliation with and receive no fees or other compensation in connection with the security or other property, and

(B) at all times during the provision of advisory services to the participant or beneficiary, the fiduciary adviser—

(i) maintains the information described in subparagraph (A) in accurate form and in the manner described in paragraph (8),

(ii) provides, without charge, accurate information to the recipient of the advice no less frequently than annually,

(iii) provides, without charge, accurate information to the recipient of the advice upon request of the recipient, and

(iv) provides, without charge, accurate information to the recipient of the advice concerning any material change to the information required to be provided to the recipient of the advice at a time reasonably contemporaneous to the change in information.

(7) OTHER CONDITIONS.—The requirements of this paragraph are met if—

(A) the fiduciary adviser provides appropriate disclosure, in connection with the sale, acquisition, or holding of the security or other property, in accordance with all applicable securities laws,

(B) the sale, acquisition, or holding occurs solely at the direction of the recipient of the advice,

(C) the compensation received by the fiduciary adviser and affiliates thereof in connection with the sale, acquisition, or holding of the security or other property is reasonable, and

(D) the terms of the sale, acquisition, or holding of the security or other property are at least as favorable to the plan as an arm's length transaction would be.

(8) STANDARDS FOR PRESENTATION OF INFORMATION.—

(A) IN GENERAL.—The requirements of this paragraph are met if the notification required to be provided to participants and beneficiaries under paragraph (6)(A) is written in a clear and conspicuous manner and in a manner calculated to be understood by the average plan participant and is sufficiently accurate and comprehensive to reasonably apprise such participants and beneficiaries of the information required to be provided in the notification.

(B) MODEL FORM FOR DISCLOSURE OF FEES AND OTHER COMPENSATION.—The Secretary shall issue a model form for the disclosure of fees and other compensation required in paragraph (6)(A)(iii) which meets the requirements of subparagraph (A).

(9) MAINTENANCE FOR 6 YEARS OF EVIDENCE OF COMPLIANCE.—The requirements of this paragraph are met if a fiduciary adviser who has provided advice referred to in paragraph (1) maintains, for a period of not less than 6 years after the provision of the advice, any records necessary for determining whether the requirements of the preceding provisions of this subsection and of subsection (b)(14) have been met. A transaction prohibited under section 406 shall not be considered to have occurred solely because the records are lost or destroyed prior to the end of the 6-year period due to circumstances beyond the control of the fiduciary adviser.

(10) EXEMPTION FOR PLAN SPONSOR AND CERTAIN OTHER FIDUCIARIES.—

(A) IN GENERAL.—Subject to subparagraph (B), a plan sponsor or other person who is a fiduciary (other than a fiduciary adviser) shall not be treated as failing to meet the requirements of this part solely by reason of the provision of investment advice referred to in section 3(21)(A)(ii)

(or solely by reason of contracting for or otherwise arranging for the provision of the advice), if—

(i) the advice is provided by a fiduciary adviser pursuant to an eligible investment advice arrangement between the plan sponsor or other fiduciary and the fiduciary adviser for the provision by the fiduciary adviser of investment advice referred to in such section,

(ii) the terms of the eligible investment advice arrangement require compliance by the fiduciary adviser with the requirements of this subsection, and

(iii) the terms of the eligible investment advice arrangement include a written acknowledgment by the fiduciary adviser that the fiduciary adviser is a fiduciary of the plan with respect to the provision of the advice.

(B) CONTINUED DUTY OF PRUDENT SELECTION OF ADVISER AND PERIODIC REVIEW.—Nothing in subparagraph (A) shall be construed to exempt a plan sponsor or other person who is a fiduciary from any requirement of this part for the prudent selection and periodic review of a fiduciary adviser with whom the plan sponsor or other person enters into an eligible investment advice arrangement for the provision of investment advice referred to in section 3(21)(A)(ii). The plan sponsor or other person who is a fiduciary has no duty under this part to monitor the specific investment advice given by the fiduciary adviser to any particular recipient of the advice.

(C) AVAILABILITY OF PLAN ASSETS FOR PAYMENT FOR ADVICE.—Nothing in this part shall be construed to preclude the use of plan assets to pay for reasonable expenses in providing investment advice referred to in section 3(21)(A)(ii).

(11) DEFINITIONS.—For purposes of this subsection and subsection (b)(14)—

(A) FIDUCIARY ADVISER.—The term “fiduciary adviser” means, with respect to a plan, a person who is a fiduciary of the plan by reason of the provision of investment advice referred to in section 3(21)(A)(ii) by the person to a participant or beneficiary of the plan and who is—

(i) registered as an investment adviser under the Investment Advisers Act of 1940 (15 U.S.C. 80b–1 et seq.) or under the laws of the State in which the fiduciary maintains its principal office and place of business,

(ii) a bank or similar financial institution referred to in subsection (b)(4) or a savings association (as defined in section 3(b)(1) of the Federal Deposit Insurance Act (12 U.S.C. 1813(b)(1)), but only if the advice is provided through a trust department of the bank or similar financial institution or savings association which is subject to periodic examination and review by Federal or State banking authorities,

(iii) an insurance company qualified to do business under the laws of a State,

(iv) a person registered as a broker or dealer under the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.),

(v) an affiliate of a person described in any of clauses (i) through (iv), or

(vi) an employee, agent, or registered representative of a person described in clauses (i) through (v) who satisfies the requirements of applicable insurance, banking, and securities laws relating to the provision of the advice.

For purposes of this part, a person who develops the computer model described in paragraph (3)(B) or markets the investment advice program or computer model shall be treated as a person who is a fiduciary of the plan by reason of the provision of investment advice referred to in section 3(21)(A)(ii) to a participant or beneficiary and shall be treated as a fiduciary adviser for purposes of this subsection and subsection (b)(14), except that the Secretary may prescribe rules under which only 1 fiduciary adviser may elect to be treated as a fiduciary with respect to the plan.

(B) AFFILIATE.—The term “affiliate” of another entity means an affiliated person of the entity (as defined in section 2(a)(3) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a)(3))).

(C) REGISTERED REPRESENTATIVE.—The term “registered representative” of another entity means a person described in section 3(a)(18) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(18)) (substituting the entity for the broker or dealer referred to in such section) or a person described in section 202(a)(17) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)(17)) (substituting the entity for the investment adviser referred to in such section).

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INTERNAL REVENUE CODE OF 1986

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Subtitle D—Miscellaneous Excise Taxes

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CHAPTER 43—QUALIFIED PENSION, ETC., PLANS

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SEC. 4975. TAX ON PROHIBITED TRANSACTIONS.

(a) INITIAL TAXES ON DISQUALIFIED PERSON.—There is hereby imposed a tax on each prohibited transaction. The rate of tax shall be equal to 15 percent of the amount involved with respect to the prohibited transaction for each year (or part thereof) in the taxable period. The tax imposed by this subsection shall be paid by any dis-

qualified person who participates in the prohibited transaction (other than a fiduciary acting only as such).

(b) **ADDITIONAL TAXES ON DISQUALIFIED PERSON.**—In any case in which an initial tax is imposed by subsection (a) on a prohibited transaction and the transaction is not corrected within the taxable period, there is hereby imposed a tax equal to 100 percent of the amount involved. The tax imposed by this subsection shall be paid by any disqualified person who participated in the prohibited transaction (other than a fiduciary acting only as such).

(c) **PROHIBITED TRANSACTION.**—

(1) **GENERAL RULE.**—For purposes of this section, the term “prohibited transaction” means any direct or indirect—

(A) sale or exchange, or leasing, of any property between a plan and a disqualified person;

(B) lending of money or other extension of credit between a plan and a disqualified person;

(C) furnishing of goods, services, or facilities between a plan and a disqualified person;

(D) transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a plan;

(E) act by a disqualified person who is a fiduciary whereby he deals with the income or assets of a plan in his own interests or for his own account; or

(F) receipt of any consideration for his own personal account by any disqualified person who is a fiduciary from any party dealing with the plan in connection with a transaction involving the income or assets of the plan.

(2) **SPECIAL EXEMPTION.**—The Secretary shall establish an exemption procedure for purposes of this subsection. Pursuant to such procedure, he may grant a conditional or unconditional exemption of any disqualified person or transaction, orders of disqualified persons or transactions, from all or part of the restrictions imposed by paragraph (1) of this subsection. Action under this subparagraph may be taken only after consultation and coordination with the Secretary of Labor. The Secretary may not grant an exemption under this paragraph unless he finds that such exemption is—

(A) administratively feasible,

(B) in the interests of the plan and of its participants and beneficiaries, and

(C) protective of the rights of participants and beneficiaries of the plan.

Before granting an exemption under this paragraph, the Secretary shall require adequate notice to be given to interested persons and shall publish notice in the Federal Register of the pendency of such exemption and shall afford interested persons an opportunity to present views. No exemption may be granted under this paragraph with respect to a transaction described in subparagraph (E) or (F) of paragraph (1) unless the Secretary affords an opportunity for a hearing and makes a determination on the record with respect to the findings required under subparagraphs (A), (B), and (C) of this paragraph, except that in lieu of such hearing the Secretary may accept any record made by the Secretary of Labor with respect to an appli-

cation for exemption under section 408(a) of title I of the Employee Retirement Income Security Act of 1974.

(3) SPECIAL RULE FOR INDIVIDUAL RETIREMENT ACCOUNTS.—An individual for whose benefit an individual retirement account is established and his beneficiaries shall be exempt from the tax imposed by this section with respect to any transaction concerning such account (which would otherwise be taxable under this section) if, with respect to such transaction, the account ceases to be an individual retirement account by reason of the application of section 408(e)(2)(A) or if section 408(e)(4) applies to such account.

(4) SPECIAL RULE FOR ARCHER MSAs.—An individual for whose benefit an Archer MSA (within the meaning of section 220(d)) is established shall be exempt from the tax imposed by this section with respect to any transaction concerning such account (which would otherwise be taxable under this section) if section 220(e)(2) applies to such transaction.

(5) SPECIAL RULE FOR COVERDELL EDUCATION SAVINGS ACCOUNTS.—An individual for whose benefit a Coverdell education savings account is established and any contributor to such account shall be exempt from the tax imposed by this section with respect to any transaction concerning such account (which would otherwise be taxable under this section) if section 530(d) applies with respect to such transaction.

(6) SPECIAL RULE FOR HEALTH SAVINGS ACCOUNTS.—An individual for whose benefit a health savings account (within the meaning of section 223(d)) is established shall be exempt from the tax imposed by this section with respect to any transaction concerning such account (which would otherwise be taxable under this section) if, with respect to such transaction, the account ceases to be a health savings account by reason of the application of section 223(e)(2) to such account.

(d) EXEMPTIONS.—Except as provided in subsection (f)(6), the prohibitions provided in subsection (c) shall not apply to—

(1) any loan made by the plan to a disqualified person who is a participant or beneficiary of the plan if such loan—

(A) is available to all such participants or beneficiaries on a reasonably equivalent basis,

(B) is not made available to highly compensated employees (within the meaning of section 414(q)) in an amount greater than the amount made available to other employees,

(C) is made in accordance with specific provisions regarding such loans set forth in the plan,

(D) bears a reasonable rate of interest, and

(E) is adequately secured;

(2) any contract, or reasonable arrangement, made with a disqualified person for office space, or legal, accounting, or other services necessary for the establishment or operation of the plan, if no more than reasonable compensation is paid therefor;

(3) any loan to an leveraged employee stock ownership plan (as defined in subsection (e)(7)), if—

(A) such loan is primarily for the benefit of participants and beneficiaries of the plan, and

- (B) such loan is at a reasonable rate of interest, and any collateral which is given to a disqualified person by the plan consists only of qualifying employer securities (as defined in subsection (e)(8));
- (4) the investment of all or part of a plan's assets in deposits which bear a reasonable interest rate in a bank or similar financial institution supervised by the United States or a State, if such bank or other institution is a fiduciary of such plan and if—
- (A) the plan covers only employees of such bank or other institution and employees of affiliates of such bank or other institution, or
- (B) such investment is expressly authorized by a provision of the plan or by a fiduciary (other than such bank or institution or affiliates thereof) who is expressly empowered by the plan to so instruct the trustee with respect to such investment;
- (5) any contract for life insurance, health insurance, or annuities with one or more insurers which are qualified to do business in a State if the plan pays no more than adequate consideration, and if each such insurer or insurers is—
- (A) the employer maintaining the plan, or
- (B) a disqualified person which is wholly owned (directly or indirectly) by the employer establishing the plan, or by any person which is a disqualified person with respect to the plan, but only if the total premiums and annuity considerations written by such insurers for life insurance, health insurance, or annuities for all plans (and their employers) with respect to which such insurers are disqualified persons (not including premiums or annuity considerations written by the employer maintaining the plan) do not exceed 5 percent of the total premiums and annuity considerations written for all lines of insurance in that year by such insurers (not including premiums or annuity considerations written by the employer maintaining the plan);
- (6) the provision of any ancillary service by a bank or similar financial institution supervised by the United States or a State, if such service is provided at not more than reasonable compensation, if such bank or other institution is a fiduciary of such plan, and if—
- (A) such bank or similar financial institution has adopted adequate internal safeguards which assure that the provision of such ancillary service is consistent with sound banking and financial practice, as determined by Federal or State supervisory authority, and
- (B) the extent to which such ancillary service is provided is subject to specific guidelines issued by such bank or similar financial institution (as determined by the Secretary after consultation with Federal and State supervisory authority), and under such guidelines the bank or similar financial institution does not provide such ancillary service—
- (i) in an excessive or unreasonable manner, and

- (ii) in a manner that would be inconsistent with the best interests of participants and beneficiaries of employee benefit plans;
- (7) the exercise of a privilege to convert securities, to the extent provided in regulations of the Secretary but only if the plan receives no less than adequate consideration pursuant to such conversion;
- (8) any transaction between a plan and a common or collective trust fund or pooled investment fund maintained by a disqualified person which is a bank or trust company supervised by a State or Federal agency or between a plan and a pooled investment fund of an insurance company qualified to do business in a State if—
- (A) the transaction is a sale or purchase of an interest in the fund,
 - (B) the bank, trust company, or insurance company receives not more than a reasonable compensation, and
 - (C) such transaction is expressly permitted by the instrument under which the plan is maintained, or by a fiduciary (other than the bank, trust company, or insurance company, or an affiliate thereof) who has authority to manage and control the assets of the plan;
- (9) receipt by a disqualified person of any benefit to which he may be entitled as a participant or beneficiary in the plan, so long as the benefit is computed and paid on a basis which is consistent with the terms of the plan as applied to all other participants and beneficiaries;
- (10) receipt by a disqualified person of any reasonable compensation for services rendered, or for the reimbursement of expenses properly and actually incurred, in the performance of his duties with the plan, but no person so serving who already receives full-time pay from an employer or an association of employers, whose employees are participants in the plan or from an employee organization whose members are participants in such plan shall receive compensation from such fund, except for reimbursement of expenses properly and actually incurred;
- (11) service by a disqualified person as a fiduciary in addition to being an officer, employee, agent, or other representative of a disqualified person;
- (12) the making by a fiduciary of a distribution of the assets of the trust in accordance with the terms of the plan if such assets are distributed in the same manner as provided under section 4044 of title IV of the Employee Retirement Income Security Act of 1974 (relating to allocation of assets);
- (13) any transaction which is exempt from section 406 of such Act by reason of section 408(e) of such Act (or which would be so exempt if such section 406 applied to such transaction) or which is exempt from section 406 of such Act by reason of section 408(b)(12) of such Act;
- (14) any transaction required or permitted under part 1 of subtitle E of title IV or section 4223 of the Employee Retirement Income Security Act of 1974, but this paragraph shall not apply with respect to the application of subsection (c)(1) (E) or (F);

(15) a merger of multiemployer plans, or the transfer of assets or liabilities between multiemployer plans, determined by the Pension Benefit Guaranty Corporation to meet the requirements of section 4231 of such Act, but this paragraph shall not apply with respect to the application of subsection (c)(1) (E) or (F);

(16) a sale of stock held by a trust which constitutes an individual retirement account under section 408(a) to the individual for whose benefit such account is established if—

(A) such stock is in a bank (as defined in section 581) or a depository institution holding company (as defined in section 3(w)(1) of the Federal Deposit Insurance Act (12 U.S.C. 1813(w)(1)),

(B) such stock is held by such trust as of the date of the enactment of this paragraph,

(C) such sale is pursuant to an election under section 1362(a) by such bank or company,

(D) such sale is for fair market value at the time of sale (as established by an independent appraiser) and the terms of the sale are otherwise at least as favorable to such trust as the terms that would apply on a sale to an unrelated party,

(E) such trust does not pay any commissions, costs, or other expenses in connection with the sale, and

(F) the stock is sold in a single transaction for cash not later than 120 days after the S corporation election is made;

(17) Any transaction in connection with the provision of investment advice described in subsection (e)(3)(B) to a participant or beneficiary in a plan that permits such participant or beneficiary to direct the investment of plan assets in an individual account, if—

(A) the transaction is—

(i) the provision of the investment advice to the participant or beneficiary of the plan with respect to a security or other property available as an investment under the plan,

(ii) the acquisition, holding, or sale of a security or other property available as an investment under the plan pursuant to the investment advice, or

(iii) the direct or indirect receipt of fees or other compensation by the fiduciary adviser or an affiliate thereof (or any employee, agent, or registered representative of the fiduciary adviser or affiliate) in connection with the provision of the advice or in connection with an acquisition, holding, or sale of a security or other property available as an investment under the plan pursuant to the investment advice; and

(B) the requirements of subsection (f)(8) are met,

(18) any transaction involving the purchase or sale of securities, or other property (as determined by the Secretary of Labor), between a plan and a disqualified person (other than a fiduciary described in subsection (e)(3)) with respect to a plan if—

(A) the transaction involves a block trade,

(B) at the time of the transaction, the interest of the plan (together with the interests of any other plans maintained by the same plan sponsor), does not exceed 10 percent of the aggregate size of the block trade,

(C) the terms of the transaction, including the price, are at least as favorable to the plan as an arm's length transaction, and

(D) the compensation associated with the purchase and sale is not greater than the compensation associated with an arm's length transaction with an unrelated party,

(19) any transaction involving the purchase or sale of securities, or other property (as determined by the Secretary of Labor), between a plan and a disqualified person if—

(A) the transaction is executed through an electronic communication network, alternative trading system, or similar execution system or trading venue subject to regulation and oversight by—

(i) the applicable Federal regulating entity, or

(ii) such foreign regulatory entity as the Secretary of Labor may determine by regulation,

(B) either—

(i) the transaction is effected pursuant to rules designed to match purchases and sales at the best price available through the execution system in accordance with applicable rules of the Securities and Exchange Commission or other relevant governmental authority, or

(ii) neither the execution system nor the parties to the transaction take into account the identity of the parties in the execution of trades,

(C) the price and compensation associated with the purchase and sale are not greater than the price and compensation associated with an arm's length transaction with an unrelated party,

(D) if the disqualified person has an ownership interest in the system or venue described in subparagraph (A), the system or venue has been authorized by the plan sponsor or other independent fiduciary for transactions described in this paragraph, and

(E) not less than 30 days prior to the initial transaction described in this paragraph executed through any system or venue described in subparagraph (A), a plan fiduciary is provided written or electronic notice of the execution of such transaction through such system or venue,

(20) transactions described in subparagraphs (A), (B), and (D) of subsection (c)(1) between a plan and a person that is a disqualified person other than a fiduciary (or an affiliate) who has or exercises any discretionary authority or control with respect to the investment of the plan assets involved in the transaction or renders investment advice (within the meaning of subsection (e)(3)(B)) with respect to those assets, solely by reason of providing services to the plan or solely by reason of a relationship to such a service provider described in subparagraph (F), (G), (H), or (I) of subsection (e)(2), or both, but only

if in connection with such transaction the plan receives no less, nor pays no more, than adequate consideration,

(21) any foreign exchange transactions, between a bank or broker-dealer (or any affiliate of either) and a plan (as defined in this section) with respect to which such bank or broker-dealer (or affiliate) is a trustee, custodian, fiduciary, or other disqualified person person, if—

(A) the transaction is in connection with the purchase, holding, or sale of securities or other investment assets (other than a foreign exchange transaction unrelated to any other investment in securities or other investment assets),

(B) at the time the foreign exchange transaction is entered into, the terms of the transaction are not less favorable to the plan than the terms generally available in comparable arm's length foreign exchange transactions between unrelated parties, or the terms afforded by the bank or broker-dealer (or any affiliate of either) in comparable arm's-length foreign exchange transactions involving unrelated parties,

(C) the exchange rate used by such bank or broker-dealer (or affiliate) for a particular foreign exchange transaction does not deviate by more than 3 percent from the interbank bid and asked rates for transactions of comparable size and maturity at the time of the transaction as displayed on an independent service that reports rates of exchange in the foreign currency market for such currency, and

(D) the bank or broker-dealer (or any affiliate of either) does not have investment discretion, or provide investment advice, with respect to the transaction,

(22) any transaction described in subsection (c)(1)(A) involving the purchase and sale of a security between a plan and any other account managed by the same investment manager, if—

(A) the transaction is a purchase or sale, for no consideration other than cash payment against prompt delivery of a security for which market quotations are readily available,

(B) the transaction is effected at the independent current market price of the security (within the meaning of section 270.17a-7(b) of title 17, Code of Federal Regulations),

(C) no brokerage commission, fee (except for customary transfer fees, the fact of which is disclosed pursuant to subparagraph (D)), or other remuneration is paid in connection with the transaction,

(D) a fiduciary (other than the investment manager engaging in the cross-trades or any affiliate) for each plan participating in the transaction authorizes in advance of any cross-trades (in a document that is separate from any other written agreement of the parties) the investment manager to engage in cross trades at the investment manager's discretion, after such fiduciary has received disclosure regarding the conditions under which cross trades may take place (but only if such disclosure is separate from any other agreement or disclosure involving the asset

management relationship), including the written policies and procedures of the investment manager described in subparagraph (H),

(E) each plan participating in the transaction has assets of at least \$100,000,000, except that if the assets of a plan are invested in a master trust containing the assets of plans maintained by employers in the same controlled group (as defined in section 407(d)(7) of the Employee Retirement Income Security Act of 1974), the master trust has assets of at least \$100,000,000,

(F) the investment manager provides to the plan fiduciary who authorized cross trading under subparagraph (D) a quarterly report detailing all cross trades executed by the investment manager in which the plan participated during such quarter, including the following information, as applicable: (i) the identity of each security bought or sold; (ii) the number of shares or units traded; (iii) the parties involved in the cross-trade; and (iv) trade price and the method used to establish the trade price,

(G) the investment manager does not base its fee schedule on the plan's consent to cross trading, and no other service (other than the investment opportunities and cost savings available through a cross trade) is conditioned on the plan's consent to cross trading,

(H) the investment manager has adopted, and cross-trades are effected in accordance with, written cross-trading policies and procedures that are fair and equitable to all accounts participating in the cross-trading program, and that include a description of the manager's pricing policies and procedures, and the manager's policies and procedures for allocating cross trades in an objective manner among accounts participating in the cross-trading program, and

(I) the investment manager has designated an individual responsible for periodically reviewing such purchases and sales to ensure compliance with the written policies and procedures described in subparagraph (H), and following such review, the individual shall issue an annual written report no later than 90 days following the period to which it relates signed under penalty of perjury to the plan fiduciary who authorized cross trading under subparagraph (D) describing the steps performed during the course of the review, the level of compliance, and any specific instances of non-compliance.

The written report shall also notify the plan fiduciary of the plan's right to terminate participation in the investment manager's cross-trading program at any time, or

(23) except as provided in subsection (f)(11), a transaction described in subparagraph (A), (B), (C), or (D) of subsection (c)(1) in connection with the acquisition, holding, or disposition of any security or commodity, if the transaction is corrected before the end of the correction period.

(24) *any transaction involving a recommendation made by a broker or dealer (including its registered representatives), or other persons or entities, that is subject to the requirements of*

the second subsection (k) of section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 78o(k)).

(e) DEFINITIONS.—

(1) PLAN.—For purposes of this section, the term “plan” means—

(A) a trust described in section 401(a) which forms a part of a plan, or a plan described in section 403(a), which trust or plan is exempt from tax under section 501(a),

(B) an individual retirement account described in section 408(a),

(C) an individual retirement annuity described in section 408(b),

(D) an Archer MSA described in section 220(d),

(E) a health savings account described in section 223(d),

(F) a Coverdell education savings account described in section 530, or

(G) a trust, plan, account, or annuity which, at any time, has been determined by the Secretary to be described in any preceding subparagraph of this paragraph.

(2) DISQUALIFIED PERSON.—For purposes of this section, the term “disqualified person” means a person who is—

(A) a fiduciary;

(B) a person providing services to the plan;

(C) an employer any of whose employees are covered by the plan;

(D) an employee organization any of whose members are covered by the plan;

(E) an owner, direct or indirect, of 50 percent or more of—

(i) the combined voting power of all classes of stock entitled to vote or the total value of shares of all classes of stock of a corporation,

(ii) the capital interest or the profits interest of a partnership, or

(iii) the beneficial interest of a trust or unincorporated enterprise,

which is an employer or an employee organization described in subparagraph (C) or (D);

(F) a member of the family (as defined in paragraph (6)) of any individual described in subparagraph (A), (B), (C), or (E);

(G) a corporation, partnership, or trust or estate of which (or in which) 50 percent or more of—

(i) the combined voting power of all classes of stock entitled to vote or the total value of shares of all classes of stock of such corporation,

(ii) the capital interest or profits interest of such partnership, or

(iii) the beneficial interest of such trust or estate, is owned directly or indirectly, or held by persons described in subparagraph (A), (B), (C), (D), or (E);

(H) an officer, director (or an individual having powers or responsibilities similar to those of officers or directors), a 10 percent or more shareholder, or a highly compensated employee (earning 10 percent or more of the yearly wages

of an employer) of a person described in subparagraph (C), (D), (E), or (G); or

(I) a 10 percent or more (in capital or profits) partner or joint venturer of a person described in subparagraph (C), (D), (E), or (G).

The Secretary, after consultation and coordination with the Secretary of Labor or his delegate, may by regulation prescribe a percentage lower than 50 percent for subparagraphs (E) and (G) and lower than 10 percent for subparagraphs (H) and (I).

(3) FIDUCIARY.—For purposes of this section, the term “fiduciary” means any person who—

(A) exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets,

(B) renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or

(C) has any discretionary authority or discretionary responsibility in the administration of such plan.

Such term includes any person designated under section 405(c)(1)(B) of the Employee Retirement Income Security Act of 1974.

(4) STOCKHOLDINGS.—For purposes of paragraphs (2)(E)(i) and (G)(i) there shall be taken into account indirect stockholdings which would be taken into account under section 267(c), except that, for purposes of this paragraph, section 267(c)(4) shall be treated as providing that the members of the family of an individual are the members within the meaning of paragraph (6).

(5) PARTNERSHIPS; TRUSTS.—For purposes of paragraphs (2)(E)(ii) and (iii), (G)(ii) and (iii), and (I) the ownership of profits or beneficial interests shall be determined in accordance with the rules for constructive ownership of stock provided in section 267(c) (other than paragraph (3) thereof), except that section 267(c)(4) shall be treated as providing that the members of the family of an individual are the members within the meaning of paragraph (6).

(6) MEMBER OF FAMILY.—For purposes of paragraph (2)(F), the family of any individual shall include his spouse, ancestor, lineal descendant, and any spouse of a lineal descendant.

(7) EMPLOYEE STOCK OWNERSHIP PLAN.—The term “employee stock ownership plan” means a defined contribution plan—

(A) which is a stock bonus plan which is qualified, or a stock bonus and a money purchase plan both of which are qualified under section 401(a), and which are designed to invest primarily in qualifying employer securities; and

(B) which is otherwise defined in regulations prescribed by the Secretary.

A plan shall not be treated as an employee stock ownership plan unless it meets the requirements of section 409(h), section 409(o), and, if applicable, section 409(n), section 409(p), and section 664(g) and, if the employer has a registration-type class

of securities (as defined in section 409(e)(4)), it meets the requirements of section 409(e).

(8) **QUALIFYING EMPLOYER SECURITY.**—The term “qualifying employer security” means any employer security within the meaning of section 409(l). If any moneys or other property of a plan are invested in shares of an investment company registered under the Investment Company Act of 1940, the investment shall not cause that investment company or that investment company’s investment adviser or principal underwriter to be treated as a fiduciary or a disqualified person for purposes of this section, except when an investment company or its investment adviser or principal underwriter acts in connection with a plan covering employees of the investment company, its investment adviser, or its principal underwriter.

(9) **SECTION MADE APPLICABLE TO WITHDRAWAL LIABILITY PAYMENT FUNDS.**—For purposes of this section—

(A) **IN GENERAL.**—The term “plan” includes a trust described in section 501(c)(22).

(B) **DISQUALIFIED PERSON.**—In the case of any trust to which this section applies by reason of subparagraph (A), the term “disqualified person” includes any person who is a disqualified person with respect to any plan to which such trust is permitted to make payments under section 4223 of the Employee Retirement Income Security Act of 1974.

(f) **OTHER DEFINITIONS AND SPECIAL RULES.**—For purposes of this section—

(1) **JOINT AND SEVERAL LIABILITY.**—If more than one person is liable under subsection (a) or (b) with respect to any one prohibited transaction, all such persons shall be jointly and severally liable under such subsection with respect to such transaction.

(2) **TAXABLE PERIOD.**—The term “taxable period” means, with respect to any prohibited transaction, the period beginning with the date on which the prohibited transaction occurs and ending on the earliest of—

(A) the date of mailing a notice of deficiency with respect to the tax imposed by subsection (a) under section 6212,

(B) the date on which the tax imposed by subsection (a) is assessed, or

(C) the date on which correction of the prohibited transaction is completed.

(3) **SALE OR EXCHANGE; ENCUMBERED PROPERTY.**—A transfer of real or personal property by a disqualified person to a plan shall be treated as a sale or exchange if the property is subject to a mortgage or similar lien which the plan assumes or if it is subject to a mortgage or similar lien which a disqualified person placed on the property within the 10-year period ending on the date of the transfer.

(4) **AMOUNT INVOLVED.**—The term “amount involved” means, with respect to a prohibited transaction, the greater of the amount of money and the fair market value of the other property given or the amount of money and the fair market value of the other property received; except that, in the case of services described in paragraphs (2) and (10) of subsection (d) the

amount involved shall be only the excess compensation. For purposes of the preceding sentence, the fair market value—

(A) in the case of the tax imposed by subsection (a), shall be determined as of the date on which the prohibited transaction occurs; and

(B) in the case of the tax imposed by subsection (b), shall be the highest fair market value during the taxable period.

(5) CORRECTION.—The terms “correction” and “correct” mean, with respect to a prohibited transaction, undoing the transaction to the extent possible, but in any case placing the plan in a financial position not worse than that in which it would be if the disqualified person were acting under the highest fiduciary standards.

(6) EXEMPTIONS NOT TO APPLY TO CERTAIN TRANSACTIONS.—

(A) IN GENERAL.—In the case of a trust described in section 401(a) which is part of a plan providing contributions or benefits for employees some or all of whom are owner-employees (as defined in section 401(c)(3)), the exemptions provided by subsection (d) (other than paragraphs (9) and (12)) shall not apply to a transaction in which the plan directly or indirectly—

(i) lends any part of the corpus or income of the plan to,

(ii) pays any compensation for personal services rendered to the plan to, or

(iii) acquires for the plan any property from, or sells any property to,

any such owner-employee, a member of the family (as defined in section 267(c)(4)) of any such owner-employee, or any corporation in which any such owner-employee owns, directly or indirectly, 50 percent or more of the total combined voting power of all classes of stock entitled to vote or 50 percent or more of the total value of shares of all classes of stock of the corporation.

(B) Special rules for shareholder-employees, etc.

(i) IN GENERAL.—For purposes of subparagraph (A), the following shall be treated as owner-employees:

(I) A shareholder-employee.

(II) A participant or beneficiary of an individual retirement plan (as defined in section 7701(a)(37)).

(III) An employer or association of employees which establishes such an individual retirement plan under section 408(c).

(ii) EXCEPTION FOR CERTAIN TRANSACTIONS INVOLVING SHAREHOLDER-EMPLOYEES.—Subparagraph (A)(iii) shall not apply to a transaction which consists of a sale of employer securities to an employee stock ownership plan (as defined in subsection (e)(7)) by a shareholder-employee, a member of the family (as defined in section 267(c)(4)) of such shareholder-employee, or a corporation in which such a shareholder-employee owns stock representing a 50 percent or greater interest described in subparagraph (A).

(iii) LOAN EXCEPTION.—For purposes of subparagraph (A)(i), the term “owner-employee” shall only in-

clude a person described in subclause (II) or (III) of clause (i).

(C) SHAREHOLDER-EMPLOYEE.—For purposes of subparagraph (B), the term “shareholder-employee” means an employee or officer of an S corporation who owns (or is considered as owning within the meaning of section 318(a)(1)) more than 5 percent of the outstanding stock of the corporation on any day during the taxable year of such corporation.

(7) S CORPORATION REPAYMENT OF LOANS FOR QUALIFYING EMPLOYER SECURITIES.—A plan shall not be treated as violating the requirements of section 401 or 409 or subsection (e)(7), or as engaging in a prohibited transaction for purposes of subsection (d)(3), merely by reason of any distribution (as described in section 1368(a)) with respect to S corporation stock that constitutes qualifying employer securities, which in accordance with the plan provisions is used to make payments on a loan described in subsection (d)(3) the proceeds of which were used to acquire such qualifying employer securities (whether or not allocated to participants). The preceding sentence shall not apply in the case of a distribution which is paid with respect to any employer security which is allocated to a participant unless the plan provides that employer securities with a fair market value of not less than the amount of such distribution are allocated to such participant for the year which (but for the preceding sentence) such distribution would have been allocated to such participant.

(8) PROVISION OF INVESTMENT ADVICE TO PARTICIPANT AND BENEFICIARIES.—

(A) IN GENERAL.—The prohibitions provided in subsection (c) shall not apply to transactions described in subsection (d)(17) if the investment advice provided by a fiduciary adviser is provided under an eligible investment advice arrangement.

(B) ELIGIBLE INVESTMENT ADVICE ARRANGEMENT.—For purposes of this paragraph, the term “eligible investment advice arrangement” means an arrangement—

(i) which either—

(I) provides that any fees (including any commission or other compensation) received by the fiduciary adviser for investment advice or with respect to the sale, holding, or acquisition of any security or other property for purposes of investment of plan assets do not vary depending on the basis of any investment option selected, or

(II) uses a computer model under an investment advice program meeting the requirements of subparagraph (C) in connection with the provision of investment advice by a fiduciary adviser to a participant or beneficiary, and

(ii) with respect to which the requirements of subparagraphs (D), (E), (F), (G), (H), and (I) are met.

(C) INVESTMENT ADVICE PROGRAM USING COMPUTER MODEL.—

(i) IN GENERAL.—An investment advice program meets the requirements of this subparagraph if the requirements of clauses (ii), (iii), and (iv) are met.

(ii) COMPUTER MODEL.—The requirements of this clause are met if the investment advice provided under the investment advice program is provided pursuant to a computer model that—

(I) applies generally accepted investment theories that take into account the historic returns of different asset classes over defined periods of time,

(II) utilizes relevant information about the participant, which may include age, life expectancy, retirement age, risk tolerance, other assets or sources of income, and preferences as to certain types of investments,

(III) utilizes prescribed objective criteria to provide asset allocation portfolios comprised of investment options available under the plan,

(IV) operates in a manner that is not biased in favor of investments offered by the fiduciary adviser or a person with a material affiliation or contractual relationship with the fiduciary adviser, and

(V) takes into account all investment options under the plan in specifying how a participant's account balance should be invested and is not inappropriately weighted with respect to any investment option.

(iii) CERTIFICATION.—

(I) IN GENERAL.—The requirements of this clause are met with respect to any investment advice program if an eligible investment expert certifies, prior to the utilization of the computer model and in accordance with rules prescribed by the Secretary of Labor, that the computer model meets the requirements of clause (ii).

(II) RENEWAL OF CERTIFICATIONS.—If, as determined under regulations prescribed by the Secretary of Labor, there are material modifications to a computer model, the requirements of this clause are met only if a certification described in subclause (I) is obtained with respect to the computer model as so modified.

(III) ELIGIBLE INVESTMENT EXPERT.—The term “eligible investment expert” means any person which meets such requirements as the Secretary of Labor may provide and which does not bear any material affiliation or contractual relationship with any investment adviser or a related person thereof (or any employee, agent, or registered representative of the investment adviser or related person).

(iv) EXCLUSIVITY OF RECOMMENDATION.—The requirements of this clause are met with respect to any investment advice program if—

(I) the only investment advice provided under the program is the advice generated by the computer model described in clause (ii), and

(II) any transaction described in subsection (d)(17)(A)(ii) occurs solely at the direction of the participant or beneficiary.

Nothing in the preceding sentence shall preclude the participant or beneficiary from requesting investment advice other than that described in clause (i), but only if such request has not been solicited by any person connected with carrying out the arrangement.

(D) EXPRESS AUTHORIZATION BY SEPARATE FIDUCIARY.—The requirements of this subparagraph are met with respect to an arrangement if the arrangement is expressly authorized by a plan fiduciary other than the person offering the investment advice program, any person providing investment options under the plan, or any affiliate of either.

(E) AUDITS.—

(i) IN GENERAL.—The requirements of this subparagraph are met if an independent auditor, who has appropriate technical training or experience and proficiency and so represents in writing—

(I) conducts an annual audit of the arrangement for compliance with the requirements of this paragraph, and

(II) following completion of the annual audit, issues a written report to the fiduciary who authorized use of the arrangement which presents its specific findings regarding compliance of the arrangement with the requirements of this paragraph.

(ii) SPECIAL RULE FOR INDIVIDUAL RETIREMENT AND SIMILAR PLANS.—In the case of a plan described in subparagraphs (B) through (F) (and so much of subparagraph (G) as relates to such subparagraphs) of subsection (e)(1), in lieu of the requirements of clause (i), audits of the arrangement shall be conducted at such times and in such manner as the Secretary of Labor may prescribe.

(iii) INDEPENDENT AUDITOR.—For purposes of this subparagraph, an auditor is considered independent if it is not related to the person offering the arrangement to the plan and is not related to any person providing investment options under the plan.

(F) DISCLOSURE.—The requirements of this subparagraph are met if—

(i) the fiduciary adviser provides to a participant or a beneficiary before the initial provision of the investment advice with regard to any security or other property offered as an investment option, a written notifi-

cation (which may consist of notification by means of electronic communication)—

(I) of the role of any party that has a material affiliation or contractual relationship with the fiduciary adviser, in the development of the investment advice program and in the selection of investment options available under the plan,

(II) of the past performance and historical rates of return of the investment options available under the plan,

(III) of all fees or other compensation relating to the advice that the fiduciary adviser or any affiliate thereof is to receive (including compensation provided by any third party) in connection with the provision of the advice or in connection with the sale, acquisition, or holding of the security or other property,

(IV) of any material affiliation or contractual relationship of the fiduciary adviser or affiliates thereof in the security or other property,

(V) the manner, and under what circumstances, any participant or beneficiary information provided under the arrangement will be used or disclosed,

(VI) of the types of services provided by the fiduciary adviser in connection with the provision of investment advice by the fiduciary adviser,

(VII) that the adviser is acting as a fiduciary of the plan in connection with the provision of the advice, and

(VIII) that a recipient of the advice may separately arrange for the provision of advice by another adviser, that could have no material affiliation with and receive no fees or other compensation in connection with the security or other property, and

(ii) at all times during the provision of advisory services to the participant or beneficiary, the fiduciary adviser—

(I) maintains the information described in clause (i) in accurate form and in the manner described in subparagraph (H),

(II) provides, without charge, accurate information to the recipient of the advice no less frequently than annually,

(III) provides, without charge, accurate information to the recipient of the advice upon request of the recipient, and

(IV) provides, without charge, accurate information to the recipient of the advice concerning any material change to the information required to be provided to the recipient of the advice at a time reasonably contemporaneous to the change in information.

(G) OTHER CONDITIONS.—The requirements of this subparagraph are met if—

(i) the fiduciary adviser provides appropriate disclosure, in connection with the sale, acquisition, or holding of the security or other property, in accordance with all applicable securities laws,

(ii) the sale, acquisition, or holding occurs solely at the direction of the recipient of the advice,

(iii) the compensation received by the fiduciary adviser and affiliates thereof in connection with the sale, acquisition, or holding of the security or other property is reasonable, and

(iv) the terms of the sale, acquisition, or holding of the security or other property are at least as favorable to the plan as an arm's length transaction would be.

(H) STANDARDS FOR PRESENTATION OF INFORMATION.—

(i) IN GENERAL.—The requirements of this subparagraph are met if the notification required to be provided to participants and beneficiaries under subparagraph (F)(i) is written in a clear and conspicuous manner and in a manner calculated to be understood by the average plan participant and is sufficiently accurate and comprehensive to reasonably apprise such participants and beneficiaries of the information required to be provided in the notification.

(ii) MODEL FORM FOR DISCLOSURE OF FEES AND OTHER COMPENSATION.—The Secretary of Labor shall issue a model form for the disclosure of fees and other compensation required in subparagraph (F)(i)(III) which meets the requirements of clause (i).

(I) MAINTENANCE FOR 6 YEARS OF EVIDENCE OF COMPLIANCE.—The requirements of this subparagraph are met if a fiduciary adviser who has provided advice referred to in subparagraph (A) maintains, for a period of not less than 6 years after the provision of the advice, any records necessary for determining whether the requirements of the preceding provisions of this paragraph and of subsection (d)(17) have been met. A transaction prohibited under subsection (c) shall not be considered to have occurred solely because the records are lost or destroyed prior to the end of the 6-year period due to circumstances beyond the control of the fiduciary adviser.

(J) DEFINITIONS.—For purposes of this paragraph and subsection (d)(17)—

(i) FIDUCIARY ADVISER.—The term “fiduciary adviser” means, with respect to a plan, a person who is a fiduciary of the plan by reason of the provision of investment advice referred to in subsection (e)(3)(B) by the person to a participant or beneficiary of the plan and who is—

(I) registered as an investment adviser under the Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.) or under the laws of the State in which the fiduciary maintains its principal office and place of business,

(II) a bank or similar financial institution referred to in subsection (d)(4) or a savings association (as defined in section 3(b)(1) of the Federal Deposit Insurance Act (12 U.S.C. 1813(b)(1)), but only if the advice is provided through a trust department of the bank or similar financial institution or savings association which is subject to periodic examination and review by Federal or State banking authorities,

(III) an insurance company qualified to do business under the laws of a State,

(IV) a person registered as a broker or dealer under the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.),

(V) an affiliate of a person described in any of subclauses (I) through (IV), or

(VI) an employee, agent, or registered representative of a person described in subclauses (I) through (V) who satisfies the requirements of applicable insurance, banking, and securities laws relating to the provision of the advice.

For purposes of this title, a person who develops the computer model described in subparagraph (C)(ii) or markets the investment advice program or computer model shall be treated as a person who is a fiduciary of the plan by reason of the provision of investment advice referred to in subsection (e)(3)(B) to a participant or beneficiary and shall be treated as a fiduciary adviser for purposes of this paragraph and subsection (d)(17), except that the Secretary of Labor may prescribe rules under which only 1 fiduciary adviser may elect to be treated as a fiduciary with respect to the plan.

(ii) **AFFILIATE.**—The term “affiliate” of another entity means an affiliated person of the entity (as defined in section 2(a)(3) of the Investment Company Act of 1940 (15 U.S.C. 80a-2(a)(3))).

(iii) **REGISTERED REPRESENTATIVE.**—The term “registered representative” of another entity means a person described in section 3(a)(18) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(18)) (substituting the entity for the broker or dealer referred to in such section) or a person described in section 202(a)(17) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)(17)) (substituting the entity for the investment adviser referred to in such section).

(9) **BLOCK TRADE.**—The term “block trade” means any trade of at least 10,000 shares or with a market value of at least \$200,000 which will be allocated across two or more unrelated client accounts of a fiduciary.

(10) **ADEQUATE CONSIDERATION.**—The term “adequate consideration” means—

(A) in the case of a security for which there is a generally recognized market—

(i) the price of the security prevailing on a national securities exchange which is registered under section 6 of the Securities Exchange Act of 1934, taking into account factors such as the size of the transaction and marketability of the security, or

(ii) if the security is not traded on such a national securities exchange, a price not less favorable to the plan than the offering price for the security as established by the current bid and asked prices quoted by persons independent of the issuer and of the party in interest, taking into account factors such as the size of the transaction and marketability of the security, and

(B) in the case of an asset other than a security for which there is a generally recognized market, the fair market value of the asset as determined in good faith by a fiduciary or fiduciaries in accordance with regulations prescribed by the Secretary of Labor.

(11) CORRECTION PERIOD.—

(A) IN GENERAL.—For purposes of subsection (d)(23), the term “correction period” means the 14-day period beginning on the date on which the disqualified person discovers, or reasonably should have discovered, that the transaction would (without regard to this paragraph and subsection (d)(23)) constitute a prohibited transaction.

(B) EXCEPTIONS.—

(i) EMPLOYER SECURITIES.—Subsection (d)(23) does not apply to any transaction between a plan and a plan sponsor or its affiliates that involves the acquisition or sale of an employer security (as defined in section 407(d)(1) of the Employee Retirement Income Security Act of 1974) or the acquisition, sale, or lease of employer real property (as defined in section 407(d)(2) of such Act).

(ii) KNOWING PROHIBITED TRANSACTION.—In the case of any disqualified person, subsection (d)(23) does not apply to a transaction if, at the time the transaction is entered into, the disqualified person knew (or reasonably should have known) that the transaction would (without regard to this paragraph) constitute a prohibited transaction.

(C) ABATEMENT OF TAX WHERE THERE IS A CORRECTION.—If a transaction is not treated as a prohibited transaction by reason of subsection (d)(23), then no tax under subsections (a) and (b) shall be assessed with respect to such transaction, and if assessed the assessment shall be abated, and if collected shall be credited or refunded as an overpayment.

(D) DEFINITIONS.—For purposes of this paragraph and subsection (d)(23)—

(i) SECURITY.—The term “security” has the meaning given such term by section 475(c)(2) (without regard to subparagraph (F)(iii) and the last sentence thereof).

(ii) COMMODITY.—The term “commodity” has the meaning given such term by section 475(e)(2) (without regard to subparagraph (D)(iii) thereof).

(iii) CORRECT.—The term “correct” means, with respect to a transaction—

(I) to undo the transaction to the extent possible and in any case to make good to the plan or affected account any losses resulting from the transaction, and

(II) to restore to the plan or affected account any profits made through the use of assets of the plan.

(g) APPLICATION OF SECTION.—This section shall not apply—

(1) in the case of a plan to which a guaranteed benefit policy (as defined in section 401(b)(2)(B) of the Employee Retirement Income Security Act of 1974) is issued, to any assets of the insurance company, insurance service, or insurance organization merely because of its issuance of such policy;

(2) to a governmental plan (within the meaning of section 414(d)); or

(3) to a church plan (within the meaning of section 414(e)) with respect to which the election provided by section 410(d) has not been made.

In the case of a plan which invests in any security issued by an investment company registered under the Investment Company Act of 1940, the assets of such plan shall be deemed to include such security but shall not, by reason of such investment, be deemed to include any assets of such company.

(h) NOTIFICATION OF SECRETARY OF LABOR.—Before sending a notice of deficiency with respect to the tax imposed by subsection (a) or (b), the Secretary shall notify the Secretary of Labor and provide him a reasonable opportunity to obtain a correction of the prohibited transaction or to comment on the imposition of such tax.

(i) CROSS REFERENCE.—For provisions concerning coordination procedures between Secretary of Labor and Secretary of the Treasury with respect to application of tax imposed by this section and for authority to waive imposition of the tax imposed by subsection (b), see section 3003 of the Employee Retirement Income Security Act of 1974.

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INVESTMENT ADVISERS ACT OF 1940

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TITLE II—INVESTMENT ADVISERS

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RULES, REGULATIONS, AND ORDERS

SEC. 211. (a) The Commission shall have authority from time to time to make, issue, amend, and rescind such rules and regulations and such orders as are necessary or appropriate to the exercise of the functions and powers conferred upon the Commission elsewhere in this title, including rules and regulations defining technical, trade, and other terms used in this title, except that the Commission may not define the term “client” for purposes of para-

graphs (1) and (2) of section 206 to include an investor in a private fund managed by an investment adviser, if such private fund has entered into an advisory contract with such adviser. For the purposes of its rules or regulations the Commission may classify persons and matters within its jurisdiction and prescribe different requirements for different classes of persons or matters.

(b) Subject to the provisions of chapter 15 of title 44, United States Code, and regulations prescribed under the authority thereof, the rules and regulations of the Commission under this title, and amendments thereof, shall be effective upon publication in the manner which the Commission shall prescribe, or upon such later date as may be provided in such rules and regulations.

(c) Orders of the Commission under this title shall be issued only after appropriate notice and opportunity for hearing. Notice to the parties to a proceeding before the Commission shall be given by personal service upon each party or by registered mail or certified mail or confirmed telegraphic notice to the party's last known business address. Notice to interested persons, if any, other than parties may be given in the same manner or by publication in the Federal Register.

(d) No provision of this title imposing any liability shall apply to any act done or omitted in good faith in conformity with any rule, regulation, or order of the Commission, notwithstanding that such rule, regulation, or order may, after such act or omission, be amended or rescinded or be determined by judicial or other authority to be invalid for any reason.

(e) DISCLOSURE RULES ON PRIVATE FUNDS.—The Commission and the Commodity Futures Trading Commission shall, after consultation with the Council but not later than 12 months after the date of enactment of the Private Fund Investment Advisers Registration Act of 2010, jointly promulgate rules to establish the form and content of the reports required to be filed with the Commission under subsection 204(b) and with the Commodity Futures Trading Commission by investment advisers that are registered both under this title and the Commodity Exchange Act (7 U.S.C. 1a et seq.).

[(g) STANDARD OF CONDUCT.—

[(1) IN GENERAL.—The Commission may promulgate rules to provide that the standard of conduct for all brokers, dealers, and investment advisers, when providing personalized investment advice about securities to retail customers (and such other customers as the Commission may by rule provide), shall be to act in the best interest of the customer without regard to the financial or other interest of the broker, dealer, or investment adviser providing the advice. In accordance with such rules, any material conflicts of interest shall be disclosed and may be consented to by the customer. Such rules shall provide that such standard of conduct shall be no less stringent than the standard applicable to investment advisers under section 206(1) and (2) of this Act when providing personalized investment advice about securities, except the Commission shall not ascribe a meaning to the term “customer” that would include an investor in a private fund managed by an investment adviser, where such private fund has entered into an advisory contract with such adviser. The receipt of compensation based on commission or fees shall not, in and of itself, be considered

a violation of such standard applied to a broker, dealer, or investment adviser.

【(2) RETAIL CUSTOMER DEFINED.—For purposes of this subsection, the term “retail customer” means a natural person, or the legal representative of such natural person, who—

【(A) receives personalized investment advice about securities from a broker, dealer, or investment adviser; and

【(B) uses such advice primarily for personal, family, or household purposes.

【(h) OTHER MATTERS.—The Commission shall—

【(1) facilitate the provision of simple and clear disclosures to investors regarding the terms of their relationships with brokers, dealers, and investment advisers, including any material conflicts of interest; and

【(2) examine and, where appropriate, promulgate rules prohibiting or restricting certain sales practices, conflicts of interest, and compensation schemes for brokers, dealers, and investment advisers that the Commission deems contrary to the public interest and the protection of investors.

【(i) HARMONIZATION OF ENFORCEMENT.—The enforcement authority of the Commission with respect to violations of the standard of conduct applicable to an investment adviser shall include—

【(1) the enforcement authority of the Commission with respect to such violations provided under this Act; and

【(2) the enforcement authority of the Commission with respect to violations of the standard of conduct applicable to a broker or dealer providing personalized investment advice about securities to a retail customer under the Securities Exchange Act of 1934, including the authority to impose sanctions for such violations, and

the Commission shall seek to prosecute and sanction violators of the standard of conduct applicable to an investment adviser under this Act to same extent as the Commission prosecutes and sanctions violators of the standard of conduct applicable to a broker or dealer providing personalized investment advice about securities to a retail customer under the Securities Exchange Act of 1934.】

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MINORITY VIEWS

H.R. 3857 is another effort by Republicans to kill the Department of Labor's (DOL) fiduciary rulemaking, which has been partially effective for four months now to finally protect American seniors and retirement savers from conflicted advice about their retirement assets. Prior to that time, unscrupulous salespeople masquerading as financial advisers were legally able to provide retirement savers with conflicted investment advice that lined their own pockets, but cost savers \$17 billion each year.

Many registered investment advisers and other financial advisers that already abide by a fiduciary standard support the DOL's fiduciary rule, as do consumer, labor and retirement groups. Those groups include the Financial Planning Coalition, AARP, AFL-CIO, NAACP, and Consumer Federation of America. In addition, nine in ten Americans reportedly agree with the DOL's rule. An overwhelming majority or around 65% of Americans who voted for President Trump also appear to support the regulation.

Nevertheless, H.R. 3857 would repeal the DOL's fiduciary rule and require SEC registered broker-dealers to comply with a vague and less protective best interest standard when providing retail investors with financial advice. This standard is essentially the current suitability standard. The bill also would prohibit the DOL from crafting a rule that is inconsistent with the SEC's regime. With respect to insurance agents, the bill would provide for substituted compliance to allow agents to comply with state law where it is substantially similar to the SEC regime; or, if state law is not substantially similar to the SEC regime, the insurer voluntarily adopts a standard that is substantially similar to the SEC regime. Finally, the bill would effectively undermine the SEC's rulemaking authority by barring any regulations that "impose any obligation related to standard of care on a broker or dealer (or its registered representative) that is in addition to" the obligations set forth in the bill.

This bill is contrary to the interests of investors, retirement savers, and seniors. It is opposed by: AARP; American Federation of State, County and Municipal Employees; Americans for Financial Reform; Center for American Progress; Center for Economic Justice; Committee for the Fiduciary Standard; Consumer Action; Consumer Federation of America; EPI Policy Center; Financial Planning Coalition; International Association of Machinists and Aerospace Workers; National Active and Retired Federal Employees Association; National Association of Social Workers; National Organization for Women; NELP; North American Securities Administrators Association; Pension Rights Center; Public Citizen; UnidosUS; U.S. PIRG; and Woodstock Institute.

For all of these reasons, we oppose H.R. 3857.

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