Public Law 100-181
100th Congress

An Act

To extend and amend the authorization of appropriations for the Securities and Exchange Commission, and for other purposes.

Dec. 4, 1987
[S. 1452]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION. 1. This Act may be cited as the "Securities and Exchange Commission Authorization Act of 1987."

Securities and Exchange Commission Authorization Act of 1987.
15 USC 78a note.

TITLE I—AUTHORIZATION

SEC. 101. Section 35 of the Securities Exchange Act of 1934 (15 U.S.C. 78kk) is amended to read as follows:

"AUTHORIZATION OF APPROPRIATIONS

"SEC. 35. (a) There are authorized to be appropriated to carry out the functions, powers, and duties of the Commission—

"(1) $158,600,000 for fiscal year 1988; and

"(2) $172,200,000 for fiscal year 1989.

"(b) Of the amounts authorized by subsection (a), the amount which may, subject to section 35A, be obligated or expended by the Commission for the purpose of funding a contract for the establishment and operation of the electronic data gathering, analysis, and retrieval ('EDGAR') system shall not exceed—

"(1) $15,000,000 for fiscal year 1988; and

"(2) $20,000,000 for fiscal year 1989.".

SEC. 102. The Securities Exchange Act of 1934 is amended by inserting after section 35 the following new section:

Contracts.

"REQUIREMENTS FOR THE EDGAR SYSTEM

15 USC 78*ll*.

"SEC. 35A. (a)(1) Of the funds appropriated to the Commission pursuant to section 35 of this title for fiscal year 1988 which are available pursuant to section 35(b) for establishment or operation of the electronic data gathering, analysis, and retrieval ('EDGAR') system, the Commission may not obligate or expend more than $5,000,000 for the establishment or operation of the EDGAR system unless the Commission has made the certification required by subsection (c) of this section.

"(2) Notwithstanding section 35(b), no funds appropriated for fiscal year 1989 may be obligated or expended for the establishment or operation of the EDGAR system, unless the Commission has—

Reports.

"(A) filed each report required during fiscal year 1988 by subsection (b) of this section; and

"(B) made the certification required by subsection (c) of this section.

"(3) Amounts which are available to the Commission under section 35(b) for the EDGAR contract shall be the exclusive source of funds for the procurement and operation of the systems created

SEC. 626. Section 55(a)(1)(B) of the Investment Company Act of 1940 (15 U.S.C. 80a-54(a)(1)(B)) is amended by striking out “described in sections” and inserting in lieu thereof “described in section”.

SEC. 627. Section 57(i) of the Investment Company Act of 1940 (15 U.S.C. 80a-56(i)) is amended by striking out “sections 17 (a) and (d)” each place it appears and inserting in lieu thereof “subsections (a) and (d) of section 17”.

TITLE VII— AMENDMENTS TO THE INVESTMENT ADVISERS ACT OF 1940

SEC. 701. Section 202(a)(19) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)(19)) is amended by striking out “the Canal Zone,”.

SEC. 702. Section 203 of the Investment Advisers Act of 1940 (15 U.S.C. 80b-3) is amended—

(1) by inserting “transfer agent,” after “fiduciary,” in subsection (e)(2)(B);

(2) by inserting “transfer agent,” after “government securities dealer,” in subsection (e)(3);

(3) by striking out “or seeking to become associated” in the first sentence of subsection (f) and inserting in lieu thereof “, seeking to become associated, or, at the time of the alleged misconduct, associated or seeking to become associated”; and

(4) by striking out “subsection (d)” in subsection (g) and inserting in lieu thereof “subsection (c) or subsection (e)”.

SEC. 703. Section 205 of the Investment Advisers Act of 1940 (15 U.S.C. 80b-5) is amended to read as follows:

“INVESTMENT ADVISORY CONTRACTS

“SEC. 205. (a) No investment adviser, unless exempt from registration pursuant to section 203(b), shall make use of the mails or any means or instrumentality of interstate commerce, directly or indirectly, to enter into, extend, or renew any investment advisory contract, or in any way to perform any investment advisory contract entered into, extended, or renewed on or after the effective date of this title, if such contract—

“(1) provides for compensation to the investment adviser on the basis of a share of capital gains upon or capital appreciation of the funds or any portion of the funds of the client;

“(2) fails to provide, in substance, that no assignment of such contract shall be made by the investment adviser without the consent of the other party to the contract; or

“(3) fails to provide, in substance, that the investment adviser, if a partnership, will notify the other party to the contract of any change in the membership of such partnership within a reasonable time after such change.

“(b) Paragraph (1) of subsection (a) shall not—

“(1) be construed to prohibit an investment advisory contract which provides for compensation based upon the total value of a fund averaged over a definite period, or as of definite dates, or taken as of a definite date;

“(2) apply to an investment advisory contract with—

“(A) an investment company registered under title I of this Act, or

"(B) any other person (except a trust, governmental plan, collective trust fund, or separate account referred to in section 3(c)(11) of title I of this Act), provided that the contract relates to the investment of assets in excess of $1 million,

if the contract provides for compensation based on the asset value of the company or fund under management averaged over a specified period and increasing and decreasing proportionately with the investment performance of the company or fund over a specified period in relation to the investment record of an appropriate index of securities prices or such other measure of investment performance as the Commission by rule, regulation, or order may specify; or

"(3) apply with respect to any investment advisory contract between an investment adviser and a business development company, as defined in this title, if (A) the compensation provided for in such contract does not exceed 20 per centum of the realized capital gains upon the funds of the business development company over a specified period or as of definite dates, computed net of all realized capital losses and unrealized capital depreciation, and the condition of section 61(a)(3)(B)(iii) of title I of this Act is satisfied, and (B) the business development company does not have outstanding any option, warrant, or right issued pursuant to section 61(a)(3)(B) of title I of this Act and does not have a profit-sharing plan described in section 57(n) of title I of this Act.

"(c) For purposes of paragraph (2) of subsection (b), the point from which increases and decreases in compensation are measured shall be the fee which is paid or earned when the investment performance of such company or fund is equivalent to that of the index or other measure of performance, and an index of securities prices shall be deemed appropriate unless the Commission by order shall determine otherwise.

"(d) As used in paragraphs (2) and (3) of subsection (a), 'investment advisory contract' means any contract or agreement whereby a person agrees to act as investment adviser to or to manage any investment or trading account of another person other than an investment company registered under title I of this Act.".

SEC. 704. Section 209 of the Investment Advisers Act of 1940 (15 U.S.C. 80b-9) is amended by redesignating subsection (e) as subsection (d).

SEC. 705. Section 211(b) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-11(b)) is amended by striking out "the Federal Register Act" and inserting in lieu thereof "chapter 15 of title 44, United States Code,".

SEC. 706. Section 213(a) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-13(a)) is amended by striking out "sections 239 and 240 of the Judicial Code, as amended" and inserting in lieu thereof "section 1254 of title 28, United States Code".

SEC. 707. Section 214 of the Investment Advisers Act of 1940 (15 U.S.C. 80b-14) is amended by striking out "sections 128 and 240 of the Judicial Code, as amended, and section 7, as amended, of the Act entitled, 'An Act to establish a court of appeals for the District of Columbia', approved February 9, 1893", and inserting in lieu thereof "sections 1254, 1291, 1292, and 1294 of title 28, United States Code".

Calendar No. 215

100TH CONGRESS *1st Session*	SENATE	REPORT No. 100-105

SECURITIES AND EXCHANGE COMMISSION AUTHORIZATION OF APPROPRIATIONS AND TECHNICAL AMENDMENTS TO THE SECURITIES LAWS

R E P O R T

OF THE

COMMITTEE ON BANKING, HOUSING,
AND URBAN AFFAIRS
UNITED STATES SENATE

TO ACCOMPANY

S. 1452

together with

ADDITIONAL VIEWS

JULY 9 (legislative day, JUNE 23), 1987.—Ordered to be printed

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Division and stressed the need for a commitment to the issues related to the internationalization of the securities markets.

Finally, based on the Commission's effective self-funding status and the recommendations of a number of witnesses, the Subcommittee is requesting that the SEC prepare a report with recommendations regarding alternatives to the appropriations process for the Commission's funding and operations.

TECHNICAL AMENDMENTS

The Commission requested the provisions of the bill making technical, clarifying, and conforming amendments to the securities laws. The bill also clarifies the enforcement capabilities of the Commission and the other Federal regulatory agencies for transfer agents.

These technical amendments were originally requested in 1983 by Senator Timothy E. Wirth when he was Chairman of the House Subcommittee on Telecommunications, Consumer Protection, and Finance. The first version of these technical amendments was introduced in the 98th Congress as H.R. 4574, sponsored by Chairman Wirth and Chairman John D. Dingell of the House Committee on Energy and Commerce. The technical amendments were again introduced in the 99th Congress by Chairman Wirth as H.R. 1604 and by Senator D'Amato as S. 920.

The technical amendments in the bill were specifically requested by SEC Chairman John Shad in his appearance before the Subcommittee for the Commission's authorization hearing on May 13, 1987.

SECTION-BY-SECTION ANALYSIS OF THE TECHNICAL AMENDMENTS

TITLE I

Title I of the Bill would effect various amendments of the Securities Act of 1933 (the "1933 Act").

Section 101 would change the definition of the term "Commission" in section 2(5) of the 1933 Act so that it refers to the Securities and Exchange Commission rather than the Federal Trade Commission. The FTC administered in the 1933 Act before the establishment of the SEC in 1934.

Section 102 would amend the definition of "Territory" in section 2(6) of the 1933 Act to exclude the Canal Zone. Pursuant to the Panama Canal Treaty between the United States and Panama, T.I.A.S. No. 10,030 (Sept. 7, 1977), the Canal Zone is no longer a possession of the United States. *Sections 202, 502, and 601* would exclude the Canal Zone from the definition of "State" under the Securities Exchange Act, the Investment Company Act, and the Investment Advisers Act, respectively, and *Section 508(1)* would exclude the Canal Zone from a list of United States possessions, for the same reason.

Section 103 would repeal as obsolete Section 3(a)(1) of the 1933 Act. Section 3(a)(1) provided and exemption from the registration provisions of the Act for offerings pending at the time the Act's enactment and, in the words of a leading commentator, "has long since spent its force." L. Loss, Fundamentals of Securities Regula-

tion 297 (1983). The bill would reserve the paragraph (1) designation for future use, rather than renumber the remaining paragraphs. These paragraphs have been in effect for over 50 years, and are among the most frequently cited provisions of the securities laws. Renumbering them would cause unnecessary confusion and result in undue expense in, for example, the extensive editing of reference works that would be required.

Section 104 would amend the registration exemption in section 3(a)(5)(A) of the 1933 Act for securities issued by regulated savings and loan associations and similar institutions by eliminating the so-called "3 percent limitation." The 3 percent limitation makes the S&L exemption inapplicable if the issuer of the security takes a fee from the purchaser in excess of 3 percent of the face value of the security.

The reason for including the 3 percent limitation in the S&L exemption is unclear. The legislative history of the 1933 Act is silent on the subject, and the Commission had rarely attempted to deny the availability of the exemption on the basis of the limitation. The only apparent recorded instance of a denial occurred in 1935, when the Commission staff indicated in a letter that the exemption would be unavailable if an S&L deducted a withdrawal fee in excess of 3 percent from the account of an investor, even if the deduction were made solely from profits previously credited to the investor's shares.

The 3 percent limitation appears to have little or no application to the securities of S&L's in today's marketplace. Moreover, it could be considered a form of discrimination against S&L's, as compared to banks, since banks are not subject to any similar restriction in the exemption provided for their securities under section 3(a)(2) of the 1933 Act.

Section 105 would delete section 6(e) of the 1933 Act as obsolete. Section 6(e) provides that no registration statement may be filed within the first 40 days following the Act's original enactment, which occurred on May 27, 1933.

Section 106 would make conforming changes to section 9 of the 1933 Act necessitated by other enactments. *Section 106(1)* would conform the nomenclature for federal appellate courts of general jurisdiction in section 9(a) of the 1933 Act from "Circuit Courts of Appeals" to "courts of appeals," to conform to the nomenclature adopted in 1948. *Section 106(2)* would conform the name of the United States Court of Appeals for the Districts of Columbia to the name change adopted in 1934. *Section 106(3)* would replace a reference to sections 239 and 240 of the Judicial Code with a reference to 28 U.S.C. 1254, where the provisions of sections 239 and 240 of the Judicial Code were codified when title 28 was enacted into law in 1948. *Sections 303 and 606* would make the same change in Section 24 of the Public Utility Holding Company Act of 1935 and section 213(a) of the Investment Advisers Act of 1940, respectively.

Section 107 would amend section 19(c) of the 1933 Act to facilitate cooperation by the Commission with state regulators and industry groups in resolving small business capital formation problems. Such cooperation was mandated by title V of Small Business Investment Incentive Act of 1980, Publ. L. No. 96-477, 94 Stat. 2275 (primarily codified at 15 U.S.C. 80a-53—64) ("Incentive Act").

requirements in the context of the meetings and communications required by title V. For example, under the FACA legislation, agencies establishing advisory committees should “require the membership * * * to be fairly balanced in terms of the points of view represented and the functions to be performed by the advisory committee.” Congress clearly had no such balance requirement in mind when it pased [sic] title V. It is of the nature of the meetings and consultations contemplated by title V that the composition of the groups formed to discuss various issues will change radically depending on the issue and the nature of the discussions. It would be impossibile [sic] to carry out the congressional mandate with one—or even several—“committees” with fixed membership and a defined charter. Applying these and other provisions of the FACA would substantially impede the cooperation that currently exists between the Commission and state securities authorities in the area of promoting small business capital formation and would hamper efforts to improve such cooperation. It would be particularly inappropriate to apply the FACA to the Commissions work with pre-existing organizations like the North American Securities Administrators Association, with which the Commission has been working closely under title V.

Thus, *Section 107* merely would clarify what the Commission believes to have been Congress’ original intent. The Administrative Procedure Act and the securities laws contain safeguards sufficient to prevent the kinds of abuses that concerned the court in *Center for Auto Safety*. The Commission would have to adopt any proposed regulations resulting from title V consultations pursuant to the notice and comment procedures of the Administrative Procedure Act, and in compliance with additional standards set forth in the securities laws.

Sections 108 and 109 would delete references in sections 20 and 22(a) of the 1933 Act to the District Court of the United States for the District of Columbia. These references are superfluous in view of 28 U.S.C. 132(a), which states that “[t]here shall be in each judicial district a district court which shall be a court of record known as the United States District Court for the district,” and 28 U.S.C. 88, which states that “[t]he District of Columbia constitutes one judicial district.” *Section* 108 would also make minor, nonsubstantive stylistic changes to section 20(b) and (c). *Section 109(3)* would amend section 22(a) by replacing a reference to sections 128 and 240 of the Judicial Code with a reference to sections 1254, 1291, 1292, and 1294 of title 28, where the provisions of sections 128 and 240 of the Judicial Code were codified when title 28 was enacted into law in 1948. Sec*tions 223(2), 226, 302(2), 303, 304, 606, and 607* would delete references to the United States District Court for the District of Columbia and replace references to the Judicial Code with references to title 28 in the Securities Exchange Act, the Public Utility Holding Company Act, and the Investment Advisers Act for the same reasons.

TITLE II

Title 2 of the Bill would effect various amendments of the Securities Exchange Act of 1934 (the “1934 Act”).

injunctions related to commodity futures activities and violations of the Commodity Exchange Act were added to the list of permissible bases for administrative sanctions against broker-dealers, municipal securities dealers, and their associated persons. The amendment also would effect several stylistic changes to conform section 15(b)(4) to the administrative sanctioning provisions of the Investment advisers Act of 1940, which also would be amended by the bill to add convictions and injunctions related to transfer agent activities to its list of permissible bases for administrative sanctions. See discussion of *Sections 602 (1) and (2)*, below. Sections 9 (a) and (b) of the Investment Company Act of 1940 would be amended correspondingly to and [sic] convictions and injunctions related to transfer agent activities to their lists of bases for disqualifying persons from serving in various capacities to investment companies. See discussion of *Section 509*, below.

Sections 217(3), 219, and 602(3) would clarify ambiguities in sections 15(b)(6) and 15B(c)(4) of the 1934 Act and in section 203(f) of the Investment Advisers Act of 1940. These amendments would codify the Commission's interpretation that it has jurisdiction under those sections to bring administrative proceedings against persons who were associated with, or were seeking to become associated with, a broker-dealer, municipal securities dealer, or investment adviser at the time they committed an alleged violation of the federal securities laws, regardless of their current employment or association status.

Before 1975, section 15(b)(7) of the 1934 Act and section 203(f) of the Investment Advisers Act authorized the Commission to bring administrative proceedings and to censure or suspend for not more than 12 months from the broker-dealer and investment advisory businesses "any person" found to have made false statements to the Commission, or to have otherwise violated the federal securities laws or aided or abetted a violation.

At that time, based on the plain language of these sections, the Commission brought a number of administrative proceedings under section 15(b)(7) against banks, lawyers, and other persons who had allegedly violated the federal securities laws, but who had not been and were not engaged in the securities business as brokers, dealers, or investment advisers, and had no apparent intention of becoming so engaged.[4] As mentioned above, the only sanction the Commission could impose under sections 15(b)(7) and 203(f) were censure, suspension, or a bar from the business of broker-dealer or investment adviser, respectively.

Apparently, objections were raised as to the logic and fairness of imposing these sanctions in administrative proceedings on persons who were not subject to regulation by the Commission as registered broker-dealers and investment advisers and had no intention of entering the business associated, or seeking to become associated, with or from which they might be suspended or barred.[5] In apparent response to these objections, section 15(b)(7) (renumbered section 15(b)(6)) was changed in 1975 to refer to "any per-broker or dealer," rather than to "any person," and section 203(f) was

[4] 5 Loss, Securities Regulation 3386-87 (1969).

[5] See II American Law Institute, Federal Securities Code 870 (1980).

changed to refer to "any person associated or seeking to become associated with an investment adviser."[6] Section 15B(c)(4), which was added to the 1934 Act by the 1975 amendments and applies to associated persons of municipal securities dealers, follows the same pattern.

This phrasing creates a possible ambiguity, however. It raises the possibility of an argument that a person who was associated with a broker-dealer, municipal securities dealer, or investment adviser at the time of the violation, but who is no longer so associated at the time of the bringing of an administrator proceeding, could not be the subject of such a proceeding. It also raises the possibility of an argument that someone who was seeking to become associated with a broker-dealer, municipal securities dealer, or investment adviser at the time of alleged misconduct, but is not seeking such association at the time of an administrative proceeding, cannot be subject of the proceeding.

These interpretations would clearly be contrary to the purposes of the sections, however, since they would allow persons who had violated the federal securities laws to avoid administrative sanctions merely by leaving the business and stating that they were [sic] longer associated with a broker-dealer, municipal securities dealer, or investment adviser and were not seeking to become so associated. This situation could arise, for example, if an employee charged with violations resigned his employment or, in the case of principals of a firm, resigned or caused the firm to cease doing businesss [sic]. It could also arise if someone who files a fraudulent application for registration abandons the application.

The proposed amendments correct this potential problem by inserting, in sections 15(b)(6), 15B(c)(4), and 203(f), the phrase "or, at the time of the alleged misconduct, associated or seeking to become associated." These amendments make clear Congress' original intent that misconduct during a *past* association or attempt at association, as well as during a *present* or *prospective* association, subjects a person to administrative proceedings and sanctions under the Securities Exchange Act and the Investment Advisers Act.

The proposed amendments follow closely the language and the rationale of section 1809(a) of the American Law Institute's Federal Securities Code.[7] There the proposed statutory language subjects a

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[6] The definition of "associated person" does not include lawyers, banks, or other persons unless they are employed in the securities business or are in a control relationship with a broker-dealer or investment adviser.

Section 3(a)(18) of the 1934 Act defines the term "person associated with a broker or dealer" as

> any partner, officer, director, or branch manager of such broker or dealer (or any person occupying a similar status or performing similar functions), any person directly or indirectly controlling, controlled by, or under common control with such broker or dealer, or any employee of such broker or dealer, except that any person associated with a broker or dealer whose functions are solely clerical or ministerial shall not be included in the meaning of such term for purposes of section 15(b) of this title (other than paragraph (6) thereof).

Similarly, section 202(a)(17) of the Investment Advisers Act defines "person associated with an investment adviser" as

> any partner, officer, or director of such investment adviser (or any person performing similar functions), or any person directly or indirectly controlling or controlled by such investment adviser, including any employee of such investment adviser, except that for the purposes of section 203 of this title (other than subsection (f) thereof), persons associated with an investment adviser whose functions are clerical or ministerial shall not be included in the meaning of such term.

[7] II American Law Institute, Federal Securities Code § 1809(a) (2d Supp. 1981).

person to liability who "*is, was* at the time of any conduct alleged [to be a violation] * * * or *is seeking* to become * * * an associate" (emphasis supplied). The commentary on this section in effect acknowledges that it would be merely codification of present law: "[I]t does seem fair enough to make clear that the Commission can proceed against a person who *was* a broker, etc., *at the time of the alleged conduct"* (emphasis in original).[8]

Section 217(4) would correct an apparent typographical error in section 15(b)(10) of the 1934 Act where there is a cross reference to "statutory disqualification" under section 17A(b)(4)(B), but that section does not use the term "statutory disqualification," whereas section 17A(b)(4)(A) does use the term, and it is apparent that the correct reference is section 17A(4)(A).

Section 218 would correct several obvious typographical errors in section 15B(b)(2)(C) of the 1934 Act.

Section 219 would effect two changes in section 15B(c)(4) of the 1934 Act, which deals with administrative proceedings against persons associated with municipal securities dealers. The first change would conform the remedies available against persons associated with municipal securities dealers to those provided in parallel provisions of the federal securities laws for persons associated with broker-dealers and investment advisers. The second change would clarify that administrative proceedings may be instituted against a person who was associated or seeking to become associated with a municipal securities dealer at the time of the conduct complained of. See discussion of *Section 217(3)*, above.

The first amendment would make it clear that the Commission and other appropriate regulatory agencies may "place limitations on the activities or functions" of a person associated with a municipal securities dealer.[9] At present, the language of section 15B(c)(4) authorizes the agencies to impose against such persons the sanctions of censure, suspension, and bar. The other provisions of the securities laws that deal with permissible sanctions against persons associated with broker-dealers and investment advisers, however, allow the Commission to censure, suspend, or bar them and also to *place limitations on* their activities.[10]

The omission of specific language giving the Commission and the other agencies "limitations" authority with respect to persons associated with municipal securities dealers is not explained in the legislative history of section 15(b)(c)(4). Indeed, the legislative history suggests that the omission was an oversight. The Senate Report that accompanied the Securities Acts Amendments of 1975, which added section 15B(c)(4) to the Act, indicated that the provision was intended to provide "limitations" authority. The Report stated that section 15B(c)(4) would authorize the Commission "by order, to censure or *impose limitations on the functions and activities,* or bar of suspend * * * any person from being associated with a municipal

[8] *Id.* at 870 (1980).

[9] Section 15B(c)(5) of the Act allows other "appropriate regulatory agencies" to impose on municipal securities dealers and associated persons within their jurisdictions the same sanctions that Sections 15B(c) (2) and (4) authorize the Commission to impose. The appropriate regulatory agency for a bank-affiliated municipal securities dealer is defined in Section 3(a)(34)(A) of the Act as one of several federal bank regulatory authorities. See note 2, above.

[10] 1934 Act § 15(b)(6), 15 U.S.C. 78o(b)(6); Investment Advisers Act § 203(f), 15 U.S.C. 80b-3(f).

Section 516(5) would delete as obsolete an exemption in the third sentence of section 22(e) of the Investment Company Act that terminated one-year after the effective date of the Investment Company Act, which was November 1, 1940.

Section 517 would delete as obsolete the provision in section 24(d) of the Investment Company Act which makes available the intrastate offering exemption in Section 3(a)(11) of the 1933 Act for new offerings of securities sold by the issuer or bona fide offered to the public before the effective date of the Investment Company Act.

Section 518 would correct a typographical error in section 26(b) of the Investment Company Act, where the word “intend,” instead of the word “intended,” is used in what is obviously intended to be the phrase “the purposes fairly intended by the policy and provisions of this title.”

Section 519 would correct a typographical error in section 26(c) of the Investment Company Act, where the word “of” is used instead of the word “or” as a conjunction.

Section 520 would correct an error in section 28(a)(2)(B) of the Investment Company Act, where the word “subsection” is used to refer to a paragraph.

Section 521 would correct a typographical error in section 28(d)(2) of the Investment Company Act, where the word “of” is omitted from what is obviously intended to be the phrase “paragraph (2) of subsection (a).”

Section 522(1) would correct a typographical error in section 36(b)(4) of the Investment Company Act, where the word “loans,” instead of the words “loads,” is used in what is obviously intended to [sic] the phrase “sales loads.”

Sections 522(2) and (3) would redesignate subsection (d) of section 36 as subsection (c) and, within redesignated subsection (c), amend the phrase “subsections (a) through (c)” to read “subsections (a) and (b).” At present, section 36 has a subsection (d) but no subsection (c).

Section 523 provides for redesignating subsection (e) of section 42 of the Investment Company Act as subsection (d), to eliminate the nonconsecutive designation that resulted from the repeal of former subsection (d) by Public Law No. 91-452 in 1970.

Section 524 deletes as obsolete the proviso in section 53 of the Investment Company Act which permitted face-amount certificate companies to register before January 1, 1941, the effective date of the Act’s provisions relating to face-amount certificate companies, and declare that such registration would not operate to change or affect the effective date as to the company or any face-amount certificates issued by it.

Sections 525 through 527 would amend sections 54(a), 55(a)(1)(B), and 57(i) of the Investment Company Act, where the word “sections” was used before a citation to a single section of the Act.

TITLE VI

Title VI would effect a number of amendments of the Investment Advisers Act of 1940.

Section 601. See discussion of *Section 102*, above.

Sections 602 (1) and (2) would amend section 203(e) of the Investment Advisers Act to add convictions and injunctions related to the transfer agent activities to the list of permissible bases upon which the Commission may impose administrative sanctions on investment advisers and persons associated with investment advisers; the amendment also would conform section 203(e) stylistically to the administrative sanction and disqualification provisions in the 1934 Act and the Investment Company Act. *See* discussions of *Sections 217 (1) and (2), and 509*, above.

Section 602(3) is a conforming amendment to correct an erroneous cross-reference in subsection (g) of section 203 of the Investment Advisers Act. The error was occasioned by amendments to subsection (d) of section 203, to which subsection (g) currently refers, in 1970 and 1975. Subsection (g) discusses the Commission's authority to deny registration to or revoke or suspend the registration of successors to registered investment advisers. This authority, which is found in subsections (c) and (e), was conferred under subsection (d) before 1970, and the cross-reference was correct. Subsection (d) was redesignated subsection (e) in section 24(c) of the 1970 amendments to the securities laws, however, and the cross-reference in subsection (g) was not altered to conform to the redesignation. *See* Pub. L. No. 91-547, § 24(c), 84 Stat. 1430. The problem was compounded by the 1975 amendments to the securities laws, which lodged the Commission's authority to deny registration in subsection (c), separating it from the Commission's authority to revoke or suspend registration, which remained in redesignated subsection (e). *See* Pub. L. No. 94-29, § 29, 89 Stat. 166-68. The proposed amendment would correct the erroneous cross-reference.

Section 603 would reenact present section 205 of the Investment Advisers Act with two major changes. First, the amendment would add new subsection and paragraph designations to section 205 to conform to the accepted usage in other portions of the Act and to make the section easier to read and understand. Several stylistic changes also would be made in connection with this rearrangement. Second, the amendment would conform the language forbidding investment advisers from charging performance fees to retirement plans described in section 3(c)(11) of the Investment Company Act to the clarifying amendments to section 3(c)(11) in *Sections 506 (1) and (2)* of the bill. The language change would make it clear that no investment adviser required to register under the Act may charge a performance fee to a governmental retirement plan. In amending section 205 in 1970, Congress intended to extend the protection of the ban on performance fees in that section to all retirement plans exempt from the operation of the Investment Company Act under section 3(c)(11). *See* discussion of *Sections 506 (1) and (2)*, above; H.R. Rep. No. 91-1631, 91st Cong., 2d Sess. 31 (1970). Because section 3(c)(11) is being amended to make it clear that all governmental retirement plans described in section 3(a)(2)(C) of the 1933 Act are within the purview of section 3(c)(11), section 205 must be correspondingly amended to refer to all such plans.

It is recommended that section 205 be reenacted in its entirety, with these changes, because confusion has resulted from the 1980 amendments to the Investment Advisers Act over the current form of section 205. Some publishers have printed current clause (C) of

the section after the last sentence, rather than immediately after clause (B) as was intended by Congress. It is hoped that this confusion will end with the reenactment of the entire section with conventional subsection and paragraph designations

Section 604 provides for redesignating subsection (e) of section 209 of the investment Advisers Act as subsection (d) to eliminate the nonconsecutive subsection designation that resulted from the repeal of former subsection (d) by Public Law No. 91-452 in 1970.

Section 605 would amend section 211(b) of the Investment Advisers Act by replacing a reference to the Federal Register Act with a reference to chapter 15 of title 44 of the United States Code, where the provisions of the Federal Register Act were codified when title 44 was enacted into law in 1968.

Section 606. See discussion of *Section 106(3), above.*

Section 607. See discussions of *Sections 109(3) and 304(2), above.*

REGULATORY IMPACT STATEMENT

In compliance with paragraph 11(b) of Rule XXVI of the Standing Rule of the Senate, the Committee makes the following statement regarding the regulatory impact of the bill. This bill will authorize funds to enable the SEC to carry out its regulatory responsibilities under current law and make technical amendments to the securities laws with no increase in regulatory burden.

CHANGES IN EXISTING LAW

In the opinion of the Committee, it is necessary to dispense with the requirements of subsection 12 of rule XXVI of the Standing Rules of the Senate in order to expedite the business of the Senate.

COST OF LEGISLATION

The Committee has requested a cost estimate of this legislation under the provision of Section 403 of the Congressional Budget Act of 1974. The cost estimate of the Congressional Budget Office appears below:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, July 1, 1987.

Hon. WILLIAM V. PROXMIRE,
Chairman, Committee on Banking, Housing, and Urban Affairs,
U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the attached cost estimate for the Securities Law Technical Amendments Act of 1987.

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

With best wishes,

Sincerely,

ROBERT F. HALE
(For Edward M. Gramlich, Acting Director).

100TH CONGRESS
1st Session

HOUSE OF REPRESENTATIVES

REPORT
100-296

SECURITIES AND EXCHANGE COMMISSION AUTHORIZATION ACT OF 1987

SEPTEMBER 9, 1987.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

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Mr. DINGELI, from the Committee on Energy and Commerce, submitted the following

REPORT

[To accompany H.R. 2600]

[Including cost estimate of the Congressional Budget Office]

The Committee on Energy and Commerce, to whom was referred the bill (H.R. 2600) to extend and amend the authorization of appropriation for the Securities and Exchange Commission, and for other purposes, having considered the same, reports favorably thereon with an amendment and recommend that the bill as amended do pass.

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Commission requested 12 new employees (8 in the regional offices) and an approximately $1.6 million increase over 1987 levels.

The Division of Market Regulation establishes and maintains trading standards and operations conducive to fair, orderly and efficient markets. The Division's workload is increasing due to continued sharp growth in trading volume and the number of broker-dealers, the proliferation of new and more complex financial products, the globalization of the trading markets, and last year's legislation providing for the regulation of government securities brokers and dealers.

There has been an explosion in the volume of securities traded and in the number of institutions and individuals participating in the U.S. securities markets. Since 1979, the volume of NYSE trading has climbed 300 percent; the volume of trading on NASDAQ and the over-the-counter market has climbed 500 percent; and the number of brokers has grown 60 percent. There are currently 11,400 broker-dealer firms registered with the SEC, with over 15,300 branch offices and 357,000 registered representatives. The Committee believes that the Commission needs additional staff resources in order to do an adequate job of overseeing the conduct of securities professionals.

INVESTMENT MANAGEMENT

The SEC's Investment Management program is designed to minimize the risk of investor loss through the regulation and review of disclosure by investment companies (ICs) and investment advisers (IAs). The program also is intended to ensure that interstate public utility holding companies operate in the public interest with sound financial structures. The program workload is rising due to the dramatic growth in the number of registered ICs and IAs and the increasing diversity of financial products and complexity of utility holding company transactions.

Since 1982, the number of ICs registered under the Investment Company Act has increased by 104 percent. During the same time period, the assets of those ICs increased over 280 percent, to $1.2 trillion. As a result of this rapid growth, the IC industry has become one of the nation's major financial intermediaries.

Because investments in IC's are not government insured, investors rely upon the Commission's disclosure, regulatory and inspection staff to protect their interests. Nevertheless, in 1986, the SEC staff reviewed only 675 of the 1,508 new IC registrations and only 896 of the 5,806 amendments filed during that year. The problems associated with this review of less than half of the new IC registrations are highlighted by the fact that the Commission staff found that 40 percent of the IC registrations it received contained "material deficiencies." Even under the proposed fiscal year 1988 budget, the Commission projects that it will be able to review only 799 of the 1,584 new IC registration statements projected for 1988.

Much the same is true with regard to IAs. At the beginning of 1987, there were more than 9,000 active IAs, including "financial planners," who manage— uninsured by any governemnt [sic] agency— approximately 15 percent of all financial assets owned by Americans.

Because of this rapid growth, the Commission noted that “[p]roviding an adequate level of protection has become increasingly difficult.” Indeed, during 1986 the Commission completed inspections of only 1,263 IAs. This represents only 13 percent of active advisers. Indeed, the staff managed to inspect between only 20 percent and 25 percent of those IAs it targeted as presenting “higher risks” to clients. Even under the proposed fiscal year 1988 budget, the Commission projects that it will continue to review only about 13 percent of active IAs in 1988.

This low level of Commission review is of serious concern to the Committee. In its fiscal year 1988 budget, the Commission requested an increase of only 17 employees in this area, and 13 of these positions would be in regional offices. Indeed, the entire budgeted increase for Investment Management for 1988 is slightly more that [sic] $1.5 million, from $11,739,000 (1987) to $13,296,000 (1988). The Committee believes that this level of funding may prove inadequate and that additional resources are necessary if the Commission is to carry out its mandate to protect investors and otherwise serve the public interest.

GENERAL

The Commission’s budget requested modest increases for Legal Services (from $6,940,000 in 1987, to $7,671,000 for 1988), Economic and Statistical Research (from $2,561,000 in 1987 to $2,827,000 for 1988) and Program Direction (from $12,591,000 in 1987, to $14,156,000 in 1988).

HEARINGS

The Committee’s Subcommittee on Telecommunications and Finance held one day of hearings on H.R. 2600 on June 4, 1987. Testimony was received from three Commissioners of the Securities and Exchange Commission (Charles C. Cox, Joseph A. Grundfest and Edward H. Fleischman), with additional material submitted by the SEC and the United States General Accounting Office in response to oversight questions.

COMMITTEE CONSIDERATION

On July 21, 1987, the Subcommittee on Telecommunications and Finance met in open session and ordered reported the bill H.R. 2600, as amended, by a voice vote, a quorum being present. On July 28, 1987, the Committee met in open session and ordered reported the bill H.R. 2600, without amendment, by a voice vote.

COMMITTEE OVERSIGHT FINDINGS

Pursuant to clause 2(1)(3)(A) of rule XI of the Rules of the House of Representatives, the Subcommittee on Telecommunications and Finance held oversight hearings and made findings that are reflected in the legislative report.

COMMITTEE ON GOVERNMENT OPERATIONS

Pursuant to clause 2(1)(3)(D) of rule XI of the Rules of the House of Representatives, oversight findings have been submitted to the