Public Law 106-102
106th Congress

An Act

Nov. 12, 1999
[S. 900]

To enhance competition in the financial services industry by providing a prudential framework for the affiliation of banks, securities firms, insurance companies, and other financial service providers, and for other purposes.

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

Gramm-Leach-Bliley Act.

Intergovernmental relations.
12 USC 1811 note.

SECTION I. SHORT TITLE; TABLE OF CONTENTS.

(a) SHORT TITLE.—This Act may be cited as the "Gramm-Leach-Bliley Act".

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

investment in the company is not insured by the Federal Deposit Insurance Corporation or any other government agency. The Commission may, after consultation with and taking into consideration the views of the Federal banking agencies (as defined in section 3 of the Federal Deposit Insurance Act), adopt rules and regulations, and issue orders, consistent with the protection of investors, prescribing the manner in which the disclosure under this paragraph shall be provided.

"(3) DEFINITIONS.—The terms 'insured depository institution' and 'appropriate Federal banking agency' have the same meanings as given in section 3 of the Federal Deposit Insurance Act.".

SEC. 215. DEFINITION OF BROKER UNDER THE INVESTMENT COMPANY ACT OF 1940.

Section 2(a)(6) of the Investment Company Act of 1940 (15 U.S.C. 80a–2(a)(6)) is amended to read as follows:

"(6) The term 'broker' has the same meaning as given in section 3 of the Securities Exchange Act of 1934, except that such term does not include any person solely by reason of the fact that such person is an underwriter for one or more investment companies.".

SEC. 216. DEFINITION OF DEALER UNDER THE INVESTMENT COMPANY ACT OF 1940.

Section 2(a)(11) of the Investment Company Act of 1940 (15 U.S.C. 80a–2(a)(11)) is amended to read as follows:

"(11) the term 'dealer' has the same meaning as given in the Securities Exchange Act of 1934, but does not include an insurance company or investment company.".

SEC. 217 REMOVAL OF THE EXCLUSION FROM THE DEFINITION OF INVESTMENT ADVISER FOR BANKS THAT ADVISE INVESTMENT COMPANIES.

(a) INVESTMENT ADVISER.—Section 202(a)(11)(A) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–2(a)(11)(A)) is amended by striking "investment company" and inserting "investment company, except that the term 'investment adviser' includes any bank or bank holding company to the extent that such bank or bank holding company serves or acts as an investment adviser to a registered investment company, but if, in the case of a bank, such services or actions are performed through a separately identifiable department or division, the department or division, and not the bank itself, shall be deemed to be the investment adviser".

(b) SEPARATELY IDENTIFIABLE DEPARTMENT OR DIVISION.—Section 202(a) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–2(a)) is amended by adding at the end the following:

"(26) The term 'separately identifiable department or division' of a bank means a unit—

"(A) that is under the direct supervision of an officer or officers designated by the board of directors of the bank as responsible for the day-to-day conduct of the bank's investment adviser activities for one or more investment companies, including the supervision of all bank employees engaged in the performance of such activities; and

"(B) for which all of the records relating to its investment adviser activities are separately maintained in or extractable from such unit's own facilities or the facilities

of the bank, and such records are so maintained or otherwise accessible as to permit independent examination and enforcement by the Commission of this Act or the Investment Company Act of 1940 and rules and regulations promulgated under this Act or the Investment Company Act of 1940.".

SEC. 218. DEFINITION OF BROKER UNDER THE INVESTMENT ADVISERS ACT OF 1940.

Section 202(a)(3) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–2(a)(3)) is amended to read as follows:

"(3) The term 'broker' has the same meaning as given in section 3 of the Securities Exchange Act of 1934.".

SEC. 219. DEFINITION OF DEALER UNDER THE INVESTMENT ADVISERS ACT OF 1940.

Section 202(a)(7) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–2(a)(7)) is amended to read as follows:

"(7) The term 'dealer' has the same meaning as given in section 3 of the Securities Exchange Act of 1934, but does not include an insurance company or investment company.".

SEC. 220. INTERAGENCY CONSULTATION.

The Investment Advisers Act of 1940 (15 U.S.C. 80b—1 et seq.) is amended by inserting after section 210 the following new section:

15 USC 80b-10a.

"SEC. 210A. CONSULTATION.

"(a) EXAMINATION RESULTS AND OTHER INFORMATION.—

"(1) The appropriate Federal banking agency shall provide the Commission upon request the results of any examination, reports, records, or other information to which such agency may have access—

"(A) with respect to the investment advisory activities of any—

"(i) bank holding company;

"(ii) bank; or

"(iii) separately identifiable department or division of bank,

that is registered under section 203 of this title; and

"(B) in the case of a bank holding company or bank that has a subsidiary or a separately identifiable department or division registered under that section, with respect to the investment advisory activities of such bank or bank holding company.

"(2) The Commission shall provide to the appropriate Federal banking agency upon request the results of any examination, reports, records, or other information with respect to the investment advisory activities of any bank holding company, bank, or separately identifiable department or division of a bank, which is registered under section 203 of this title.

"(3) Notwithstanding any other provision of law, the Commission and the appropriate Federal banking agencies shall not be compelled to disclose any information provided under paragraph (1) or (2). Nothing in this paragraph shall authorize the Commission or such agencies to withhold information from Congress, or prevent the Commission or such agencies from complying with a request for information from any other Federal department or agency or any self-regulatory organization

requesting the information for purposes within the scope of its jurisdiction, or complying with an order of a court of the United States in an action brought by the United States, the Commission, or such agencies. For purposes of section 552 of title 5, United States Code, this paragraph shall be considered a statute described in subsection (b)(3)(B) of such section 552.

"(b) EFFECT ON OTHER AUTHORITY.—Nothing in this section shall limit in any respect the authority of the appropriate Federal banking agency with respect to such bank holding company (or affiliates or subsidiaries thereof), bank, or subsidiary, department, or division or a bank under any other provision of law.

"(c) DEFINITION.—For purposes of this section, the term 'appropriate Federal banking agency' shall have the same meaning as given in section 3 of the Federal Deposit Insurance Act.".

SEC. 221. TREATMENT OF BANK COMMON TRUST FUNDS.

(a) SECURITIES ACT OF 1933.—Section 3(a)(2) of the Securities Act of 1933 (15 U.S.C. 77c(a)(2)) is amended by striking "or any interest or participation in any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of assets contributed thereto by such bank in its capacity as trustee, executor, administrator, or guardian" and inserting "or any interest or participation in any common trust fund or similar fund that is excluded from the definition of the term 'investment company' under section 3(c)(3) of the Investment Company Act of 1940".

(b) SECURITIES EXCHANGE ACT OF 1934.—Section 3(a)(12)(A)(iii) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(12)(A)(iii)) is amended to read as follows:

"(iii) any interest or participation in any common trust fund or similar fund that is excluded from the definition of the term 'investment company' under section 3(c)(3) of the Investment Company Act of 1940;".

(c) INVESTMENT COMPANY ACT OF 1940.—Section 3(c)(3) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(c)(3) is amended by inserting before the period the following: ", if—

"(A) such fund is employed by the bank solely as an aid to the administration of trusts, estates, or other accounts created and maintained for a fiduciary purpose;

"(B) except in connection with the ordinary advertising of the bank's fiduciary services, interests in such fund are not—

"(i) advertised; or

"(ii) offered for sale to the general public; and

"(C) fees and expenses charged by such fund are not in contravention of fiduciary principles established under applicable Federal or State law".

SEC. 222 STATUTORY DISQUALIFICATION FOR BANK WRONGDOING

Section 9(a) of the Investment Company act of 1940 (15 U.S.C. 80a–9(a)) is amended in paragraphs (1) and (2) by striking "securities dealer, transfer agent," and inserting "securities dealer, bank, transfer agent,".

SEC. 223 CONFORMING CHANGE IN DEFINITION.

Section 2(a)(5) of the Investment Company Act of 1940 (15 U.S.C. 80a–2(a)(5)) is amended by striking "(A) a banking institution

106TH CONGRESS | HOUSE OF REPRESENTATIVES | REPT. 106-74
1st Session | Part 1

FINANCIAL SERVICES ACT OF 1999

MARCH 23, 1999.– Ordered to be printed

Mr. LEACH, from the Committee on Banking and Financial Services, submitted the following

R E P O R T

together with

SUPPLEMENTAL, ADDITIONAL AND

DISSENTING VIEWS

[To accompany H.R. 10]

The Committee on Banking and Financial Services, to whom was referred the bill (H.R. 10) to enhance competition in the financial services industry by providing a prudential framework for the affiliation of banks, securities firms, and other financial service providers, and for other purposes, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment is as follows:

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

SECTION 1. SHORT TITLE; PURPOSES; TABLE OF CONTENTS.

(a) SHORT TITLE.—This Act may be cited as the "Financial Services Act of 1999".

(b) PURPOSES.—The purposes of this Act are as follows:

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"(A) has been guaranteed, sponsored, recommended, or approved by the United States, or any agency, instrumentality or officer of the United States;

"(B) has been insured by the Federal Deposit Insurance Corporation; or

"(C) is guaranteed by or is otherwise an obligation of any bank or insured depository institution.

"(2) DISCLOSURES.—Any person issuing or selling the securities of a registered investment company that is advised by, or sold through, a bank shall prominently disclose that an investment in the company is not insured by the Federal Deposit Insurance Corporation or any other government agency. The Commission may adopt rules and regulations, and issue orders, consistent with the protection of investors, prescribing the manner in which the disclosure under this paragraph shall be provided.

"(3) DEFINITIONS.—The terms 'insured depository institution' and 'appropriate Federal banking agency' have the same meanings as in section 3 of the Federal Deposit Insurance Act."

SEC. 215. DEFINITION OF BROKER UNDER THE INVESTMENT COMPANY ACT OF 1940.

Section 2(a)(6) of the Investment Company Act of 1940 (15 U.S.C. 80a–2(a)(6)) is amended to read as follows:

"(6) The term 'broker' has the same meaning as in section 3 of the Securities Exchange Act of 1934, except that such term does not include any person solely by reason of the fact that such person is an underwriter for one or more investment companies.".

SEC. 216. DEFINITION OF DEALER UNDER THE INVESTMENT COMPANY ACT OF 1940.

Section 2(a)(11) of the Investment Company Act of 1940 (15 U.S.C. 80a–2(a)(11)) is amended to read as follows:

"(11) The term 'dealer' has the same meaning as in section 3 of the Securities Exchange Act of 1934, but does not include an insurance company or investment company.".

SEC. 217 REMOVAL OF THE EXCLUSION FROM THE DEFINITION OF INVESTMENT ADVISER FOR BANKS THAT ADVISE INVESTMENT COMPANIES.

(a) INVESTMENT ADVISER.—Section 202(a)(11) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–2(a)(11)) is amended in subparagraph (A), by striking "investment company" and inserting "investment company, except that the term 'investment adviser' includes any bank or bank holding company to the extent that such bank or bank holding company serves or acts as an investment adviser to a registered investment company, but if, in the case of a bank, such services or actions are performed through a separately identifiable department or division, the department or division, and not the bank itself, shall be deemed to be the investment adviser".

(b) SEPARATELY IDENTIFIABLE DEPARTMENT OR DIVISION.—Section 202(a) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–2(a)) is amended by adding at the end the following:

"(26) The term 'separately identifiable department or division' of a bank means a unit—

"(A) that is under the direct supervision of an officer or officers designated by the board of directors of the bank as responsible for the day-to-day conduct of the bank's investment adviser activities for one or more investment companies, including the supervision of all bank employees engaged in the performance of such activities; and

"(B) for which all of the records relating to its investment adviser activities are separately maintained in or extractable from such unit's own facilities or the facilities of the bank, and such records are so maintained or otherwise accessible as to permit independent examination and enforcement by the Commission of this Act of the Investment Company Act of 1940 and rules and regulations promulgated under this Act or the Investment Company Act of 1940.".

SEC. 218. DEFINITION OF BROKER UNDER THE INVESTMENT ADVISERS ACT OF 1940.

Section 202(a)(3) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–2(a)(3)) is amended to read as follows:

"(3) The term 'broker' has the same meaning as in section 3 of the Securities Exchange Act of 1934.".

SEC. 219. DEFINITION OF DEALER UNDER THE INVESTMENT ADVISERS ACT OF 1940.

Section 202(a)(7) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–2(a)(7)) is amended to read as follows:

"(7) The term 'dealer' has the same meaning as in section 3 of the Securities Exchange Act of 1934, but does not include an insurance company or investment company.".

SEC. 220. INTERAGENCY CONSULTATION.

The Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.) is amended by inserting after section 210 the following new section:

"SEC. 210A. CONSULTATION.

"(a) EXAMINATION RESULTS AND OTHER INFORMATION.—

"(1) The appropriate Federal banking agency shall provide the Commission upon request the results of any examination, reports, records, or other information to which such agency may have access with respect to the investment advisory activities—

"(A) of any—

"(i) bank holding company;

"(ii) bank; or

"(iii) separately identifiable department or division of a bank, that is registered under section 203 of this title; and

"(B) in the case of a bank holding company or bank that has a subsidiary or a separately identifiable department or division registered under that section, of such bank or bank holding company.

"(2) The Commission shall provide to the appropriate Federal banking agency upon request the results of any examination, reports, records, or other information with respect to the investment advisory activities of any bank holding company, bank, or separately identifiable department or division of a bank, any of which is registered under section 203 of this title.

"(b) EFFECT ON OTHER AUTHORITY.—Nothing in this section shall limit in any respect the authority of the appropriate Federal banking agency with respect to such bank holding company, bank, or department or division under any provision of law.

"(c) DEFINITION.—For purposes of this section, the term 'appropriate Federal banking agency' has the same meaning as in section 3 of the Federal Deposit Insurance Act".

SEC. 221. TREATMENT OF BANK COMMON TRUST FUNDS.

(a) SECURITIES ACT OF 1933.—Section 3(a)(2) of the Securities Act of 1933 (15 U.S.C. 77c(a)(2)) is amended by striking "or any interest or participation in any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of assets contributed thereto by such bank in its capacity as trustee, executor, administrator, or guardian" and inserting "or any interest or participation in any common trust fund or similar fund that is excluded from the definition of the term 'investment company' under section 3(c)(3) of the Investment Company Act of 1940".

(b) SECURITIES EXCHANGE ACT OF 1934,--Section 3(a)(12)(A)(iii) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(12)(A)(iii)) is amended to read as follows:

"(iii) any interest or participation in any common trust fund or similar fund that is excluded from the definition of the term 'investment company' under section 3(c)(3) of the Investment Company act of 1940;"

(c) INVESTMENT COMPANY ACT OF 1940.—Section 3(c)(3) of the Investment Company Act of 1940 (15 U.S.C. 80a–3(c)(3)) is amended by inserting before the period the following: ", if—

"(A) such fund is employed by the bank solely as an aid to the administration of trusts, estates, or other accounts created and maintained for a fiduciary purpose;

"(B) except in connection with the ordinary advertising of a bank's fiduciary services interests in such fund are not—

(i) advertised; or

(ii) offered for sale to the general public; and

"(C) fees and expenses charged by such fund are not in contravention of fiduciary principles established under applicable Federal or State law".

SEC. 222. INVESTMENT ADVISERS PROHIBITED FROM HAVING CONTROLLING INTEREST IN REGISTERED INVESTMENT COMPANY.

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

"(g) CONTROLLING INTEREST IN INVESTMENT COMPANY PROHIBITED.—

"(1) IN GENERAL.—If an investment adviser to a registered investment company, or an affiliated person of that investment adviser, holds a controlling in-

SECTION 214. ADDITIONAL SEC DISCLOSURE AUTHORITY

Section 214 amends Section 35(a) of the Investment Company Act. Section 35(a) currently makes it unlawful for any person issuing or selling any security of an investment company to represent or imply in any manner that such security or company is guaranteed, sponsored, recommended, or approved by the United States or any agency, instrumentality or officer thereof. New Section 35(a) further makes it unlawful for any person issuing or selling any security of an investment company to represent or imply in any manner that such security or company is insured by the FDIC or is guaranteed by or is an obligation of any bank.

New Section 35(a) further requires any person issuing or selling the securities of an investment company that is advised by, or sold through, a bank to disclose prominently that an investment in the company is not insured by the FDIC or any other government agency. The SEC is given authority to issue rules prescribing the manner in which this disclosure will be provided.

SECTION 25. DEFINITION OF BROKER UNDER THE INVESTMENT COMPANY ACT OF 1940

Section 215 amends Section 2(a)(6) of the Investment Company Act. Section 2(a)(6) defines "broker" for purposes of the Investment Company Act and currently contains an exemption for banks. New Section 2(a)(6) defines "broker" as having the same meaning as in the Securities Exchange Act, except that for purposes of the Investment Company Act it does not include any person solely by reason of the fact that such person is an underwriter for one or more investment companies. The exemption for banks is deleted.

SECTION 216. DEFINITION OF DEALER UNDER THE INVESTMENT COMPANY ACT OF 1940

Section 216 amends Section 2(a)(11) of the Investment Company Act. Section 2(a)(11) defines "dealer" for purposes of the Investment Company Act and currently contains an exemption for banks. New Section 2(a)(11) defines "dealer" as having the same meaning as in the Securities Exchange Act, except that for purposes of the Investment Company Act it does not include any insurance company or investment company. The exemption for banks is deleted.

SECTION 217. REMOVAL OF THE EXCLUSION FROM THE DEFINITION OF INVESTMENT ADVISER FOR BANKS THAT ADVISE INVESTMENT COMPANIES

Section 217(a) amends Section 202(a)(11) of the Investment Advisers Act of 1940. Section 202(a)(11) defines "investment adviser" and currently exempts any bank of BHC that is not an investment company. New Section 202(a)(11) removes this exemption for any bank or BHC to the extent it serves or acts as an investment adviser to an investment company. If such services or actions performed through a separately identifiable department or division of a bank, the department or division and not the bank itself shall be deemed to be the investment adviser.

Section 217(b) adds a new Section 202(a)(26) to the Investment Advisers Act. New Section 202(a)(26) defines "separately identifi-

able department or division" of a bank as a unit under the direct supervision of an officer or officers designated by the bank's directors as responsible for the day-to-day conduct of the bank's investment adviser activities for one or more investment companies, including the supervision of all bank employees engaged in the performance of such activities. All records relating to investment adviser activities must be separately maintained in or extractable from the unit's own facilities or the facilities of the bank so as to permit examination and enforcement by the SEC.

SECTION 218. DEFINITION OF BROKER UNDER THE INVESTMENT ADVISERS ACT OF 1940

Section 218 amends Section 202(a)(3) of the Investment Advisers Act. Section 202(a)(3) defines "broker" for purposes of the Investment Advisers Act and currently contains a blanket exemption for banks. New Section 202(a)(3) defines "broker" as having the same meaning as in the Securities Exchange Act. The blanket exemption for banks is deleted.

SECTION 219. DEFINITION OF DEAL UNDER THE INVESTMENT ADVISERS ACT OF 1940

Section 219 amends Section 202(a)(7) of the Investment Advisers Act. Section 202(a)(7) defines "dealer" for purposes of the Investment Advisers Act and currently contains a blanket exemption for banks. New Section 202(a)(7) defines "dealer" as having the same meaning as in the Securities Exchange Act, except that for purposes of the Investment Advisers Act it does not include any insurance company or investment company. The blanket exemption for banks is deleted.

SECTION 220. INTERAGENCY CONSULTATION

Section 202 amends the Investment Advisers Act to add a new Section 210A. New Section 210A authorizes the SEC to receive from a federal banking agency the results of any examination, reports, records, or other information to which such agency may have access regarding the investment advisory activities of any BHC, bank, or separately identifiable department or division of a bank, that is registered as an investment adviser or that has a subsidiary or separately identifiable department or division registered as an investment adviser. New Section 210A similarly authorizes the federal banking agencies to receive from the SEC the results of any examination, reports, records, or other information regarding the identifiable department or division of a bank, that is registered as an investment adviser. Section 210A does not limit the authority of any federal banking agency with respect for such bank holding company, bank, or separately identifiable department or division under any provision of law.

SECTION 221. TREATMENT OF BANK COMMON TRUST FUNDS

Section 221(a) amends Section 3(a)(2) of the Securities Act of 1933. Section 3(a)(2) currently exempts from the application of the Securities Act any interest or participation in any common trust

(2) DISCLOSURES.—Any person issuing or selling the securities of a registered investment company that is advised by, or sold through, a bank shall prominently disclose that an investment in the company is not insured by the Federal Deposit Insurance Corporation or any other government agency. The Commission may adopt rules and regulations, and issue orders, consistent with the protection of investors, prescribing the manner in which the disclosure under this paragraph shall be provided.

"(3) DEFINITIONS.—The terms "insured depository institution" and "appropriate Federal banking agency" have the same meanings as in section 3 of the Federal Deposit Insurance Act.

* * * * * * *

BREACH OF FIDUCIARY DUTY

SEC. 36. (a) The Commission is authorized to bring an action in the proper district court of the United States, or in the United States court of any territory or other place subject to the jurisdiction of the United States, alleging that a person serving or acting in one or more of the following capacities has engaged within five years of the commencement of the action or is about to engage in any act or practice constituting a breach of fiduciary duty involving personal misconduct in respect of any registered investment company for which such person so serves or acts—

(1) as officer, director, member of any advisory board, investment adviser, or depositor; **[**or**]**

(2) as principal underwriter, if such registered company is an open-end company, unit investment trust, or face-amount certificate company**[**.**]**; *or*

(3) as custodian.

If such allegations are established, the court may enjoin such persons from acting in any or all such capacities either permanently or temporarily and award such injunctive or other relief against such person as may be reasonable and appropriate in the circumstances, having due regard to the protection of investors and to the effectuation of the policies declared in section 1(b) of this title.

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INVESTMENT ADVISERS ACT OF 1940

TITLE II—INVESTMENT ADVISERS

* * * * * * *

DEFINITIONS

SEC. 202. (a) When used in this title, unless the context otherwise requires, the following definitions shall apply:

(1) * * *

* * * * * * *

[(3) "Broker" means any person engaged in the business of effecting transactions in securities for the account of others, but does not include a bank.**]**

(3) The term "broker" has the same meaning as in section 3 of the Securities Exchange Act of 1934.

* * * * * * *

[(7) "Dealer" means any person regularly engaged in the business of buying and selling securities for his own account, through a broker or otherwise, but does not include a bank, insurance company, or investment company, or any person insofar as he is engaged in investing, reinvesting or trading in securities, or in owning or holding securities, for his own account, either individually or in some fiduciary capacity, but not as a part of a regular business.**]**

(7) The term "dealer" has the same meaning as in section 3 of the Securities Exchange Act of 1934, but does not include an insurance company or investment company.

* * * * * * *

(11) "Investment adviser" means any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities; but does not include (A) a bank, or any bank holding company as defined in the Bank Holding Company Act of 1956, which is not an **[**investment company**]** *investment company, except that the term "investment adviser" includes any bank or bank holding company to the extent that such bank or bank holding company serves or acts as an investment adviser to a registered investment company, but if, in the case of a bank, such services or actions are performed through a separately identifiable department or division, the department or division, and not the bank itself, shall be deemed to be the investment adviser;* (B) any lawyer, accountant, engineer or teacher whose performance of such services is solely incidental to the practice of his profession; (C) any broker or dealer whose performance of such services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor; (D) the publisher of any bona fide newspaper, news magazine or business or financial publication of general and regular circulation; (E) any person whose advice, analyses, or reports relate to no securities other than securities which are direct obligations of or obligations guaranteed as to principal or interest by the United States, or securities issued or guaranteed by corporations in which the United States has a direct or indirect interest which shall have been designated by the Secretary of the Treasury, pursuant to section 3(a)(12) of the Securities Exchange Act of 1934, as exempted securities for the purposes of that Act; or (F) such other persons not within the intent of this paragraph, as the Commission may designate by rules and regulations or order.

* * * * * * *

(26) The term "separately identifiable department or division" of a bank means a unit—

(A) that is under the direct supervision of an officer or officers designated by the board of directors of the bank as responsible for the day-to-day conduct of the bank's investment adviser activities for one or more investment companies, including the supervision of all bank employees engaged in the performance of such activities; and

(B) for which all of the records relating to its investment adviser activities are separately maintained in or extractable from such unit's own facilities or the facilities of the bank, and such records are so maintained or otherwise accessible as to permit independent examination and enforcement by the Commission of this Act or the Investment Company Act of 1940 and rules and regulations promulgated under this Act or the Investment Company Act of 1940.

* * * * * * *

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

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SEC. 210 A. CONSULTATION.

(a) EXAMINATION RESULTS AND OTHER INFORMATION.—

(1) The appropriate Federal banking agency shall provide the Commission upon request the results of any examination, reports, records, or other information to which such agency may have access with respect to the investment advisory activities—

(A) of any—

(i) bank holding company;

(ii) bank; or

(iii) separately identifiable department or division of a bank, that is registered under section 203 of this title; and

(B) in the case of a bank holding company or bank that has a subsidiary or a separately identifiable department or division registered under that section, of such bank or bank holding company.

(2) The Commission shall provide to the appropriate Federal banking agency upon request the results of any examination, reports, records, or other information with respect to the investment advisory activities of any bank holding company, bank, or separately identifiable department or division of a bank, any of which is registered under section 203 of this title.

(b) EFFECT ON OTHER AUTHORITY.—Nothing in this section shall limit in any respect the authority of the appropriate Federal banking agency with respect to such bank holding company, bank, or department or division under any provision of law.

(c) DEFINITION.—For purposes of this section, the term "appropriate Federal banking agency" has the same meaning as in section 3 of the Federal Deposit Insurance Act.

* * * * * * *

SECTION 3 OF THE SECURITIES ACT OF 1933

EXEMPTED SECURITIES

SEC. 3. (a) Except as hereinafter expressly provided, the provisions of this title shall not apply to any of the following classes of securities:

(1) Reserved.

(2) Any security issued or guaranteed by the United States or any Territory thereof, or by the District of Columbia, or by any State of the United States, or by any political subdivision of a State or Territory, or by any public instrumentality of one or more States or Territories, or by any person controlled or supervised by and acting as an instrumentality of the Government of the United States pursuant to authority granted by the Congress of the United States; or any certificate of deposit for any of the foregoing; or any security issued or guaranteed by any bank; or any security issued by or representing an interest in or a direct obligation of a Federal Reserve bank; **[**or any interest or participation in any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of assets contributed thereto by such bank in its capacity as trustee, executor, administrator, or guardian**]** *or any interest or participation in any common trust fund or similar fund that is excluded from the definition of the term "investment company" under section 3(c)(3) of the Investment Company Act of 1940;* or any security which is an industrial development bond (as defined in section 103(c)(2) of the Internal Revenue Code of 1954) the interest on which is excludable from gross income under section 103(a)(1) of such Code if, by reason of the application of paragraph (4) or (6) of section 103(c) of such Code (determined as if paragraphs (4)(A), (5), and (7) were not included in such section 103(c)), paragraph (1) of such section 103(c) does not apply to such security; or any interest or participation in a single trust fund, or in a collective trust fund maintained by a bank, or any security arising out of a contract issued by an insurance company, which interest, participation, or security is issued in connection with (A) a stock bonus, pension, or profit-sharing plan which meets the requirements for qualification under section 401 of the Internal Revenue Code of 1954, (B) an annuity plan which meets the requirements for the deduction of the employer's contributions under section 404(a)(2) of such Code, or (C) a governmental plan as defined in section 414(d) of such Code which has been established by an employer for the exclusive benefit of its employees or their beneficiaries for the purpose of distributing to such employees or their beneficiaries the corpus and income of the funds accumulated under such plan, if under such plan it is impossible, prior to the satisfaction of all

106TH CONGRESS *1st Session* | HOUSE OF REPRESENTATIVES | REPT. 106-74 Part 2

FINANCIAL SERVICES ACT OF 1999

JUNE 10, 1999.– Ordered to be printed

MR. LEACH, from the Committee on Banking and Financial Services, submitted the following

SUPPLEMENTARY REPORT

[To accompany H.R. 10]

This supplemental report shows the cost estimate of the Congressional Budget Office with respect to the bill (H.R. 10) as reported, which was not included in part 1 of the report submitted by the Committee on Banking and Financial Services on March 23, 1999 (H. Rept. 106–74, pt. 1).

This supplemental report is submitted in accordance with clause 3(a)(2) of rule XIII of the Rules of the House of Representatives.

This supplemental report also contains an errata correction to page 2 of part 1 of the report.

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE
Washington, DC, June 10, 1999.

Hon. JAMES A. LEACH,
Chairman, Committee on Banking and Financial Services, House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed costs estimate and mandate statements for H.R. 10, the Financial Services Act of 1999. One enclosure includes the estimate of federal costs and the estimate of the impact of the legislation on state, local, and tribal governments. The estimated impact of mandates on the private sector is discussed in a separate enclosure.

If you wish further details on these estimates, we will be pleased to provide them. The CBO staff contacts are Robert S. Seiler (for costs to the Federal Home Loan Banks); Mary Maginniss (for other federal costs); Carolyn Lynch (for federal revenues); Susan Seig (for

activities through a financial subsidiary, the national bank and all of its depository institution affiliates must be well capitalized, be well-managed and have at least a satisfactory rating under the Community Reinvestment Act. The bill would require that any national bank having more than $10 billion in total assets and controlling a financial subsidiary be a part of a holding company. Examples of new activities for national bank subsidiaries include merchant banking, securities underwriting, and insurance agency activities not restricted to small towns. In addition, section 181 of the bill would authorize well-capitalized national banks to underwrite certain municipal revenue bonds directly in the bank.

Regulation of securities services and investment advisers

Title II of H.R. 10 would amend the securities laws in order to provide functional regulation of existing and newly authorized bank securities activities, with certain exceptions (primarily related to traditional banking activities), would be required to comply with securities regulations. Bank affiliates and subsidiaries would continue to be subject to the same regulation as other providers of securities products. Currently, national banks may engage in brokering (buying and selling) of all types of securities and investment products. State bank's securities activities vary from state to state, but most states permit state banks to engage in the sale of securities. Also under the bill, if a bank acts as an investment adviser to a registered investment company, the bank would be subject to the registration requirements and regulation under the Investment Adviser Act of 1940.

Securities Services. Generally, a firm that provides securities brokerage services (known as a broker-dealer) must register and be regulated by the Securities and Exchange Commission and at least one self-regulatory organization such as the National Association of Securities Dealers (NASD), the New York Stock Exchange, and the American Stock Exchange. Banks, however, are currently exempted from broker-dealer regulation.

H.R. 10 would end the current blanket exemption for banks from being treated as brokers or dealers under the Securities Exchange Act of 1934. Securities activities of banks would, therefore, be subject to SEC regulation, with some exceptions. The bill would exempt from SEC regulation the securities activities of banks handling fewer than 500 transactions annually. Many of the roughly 300 small banks that currently provide brokerage services on bank premises would fall under this exemption. Sections 201 and 202 also would exempt several traditional securities activities of banks from the registration requirements and regulations that apply to brokers or dealers under SEC regulation. The exemptions would cover most products and services that banks currently offer so that they would not trigger SEC regulation. For example, sweep accounts transactions, trust activities, and U.S. government securities transactions would be exempt. However, for the products and services related to securities that would no longer be exempt under the bill, banks would most likely channel the non-exempt activities through their own securities affiliate or establish a relationship with a broker-dealer. A substantial number of banks that currently

handle securities activities have a broker-dealer affiliate so that the incremental cost of complying with SEC regulation would involve moving non-exempt activities to such an affiliate and would not be significant.

Section 203 would require the NASD to create a new limited qualification category or registration for certain persons engaged in private securities offerings (private placements). The NASD expects that the modest additional costs incurred due to this mandate would be offset by additional fees received from the industry. The bill provides that bank employees that engage in this activity would be exempt from any examination requirements if they have been engaged in private placement sales in the six months before this bill is enacted.

Section 204 would require bank regulatory agencies to establish record keeping requirements for banks that claim the exemptions allowed under sections 201 and 202. The impact of the new reporting requirements on banks that would be allowed an exemption is uncertain because it would depend on future federal rulemaking. The bill would direct regulators to make the new requirements sufficient to demonstrate compliance with the terms of the exemption. Because CBO has no basis for predicting how this provision would be implemented, we cannot estimate the costs of new requirements on banks. However, given the infrastructure that supports current reporting requirements, we expect that the incremental costs of the new requirements would be small.

Investment Advisers. Investment advisers are responsible for managing an investment portfolio in order to attain the greatest return consistent with the investment strategy established by the fund board of directors. Banks that act as investment advisers are currently exempt from the registration and other requirements of the Investment Advisers Act of 1940. Under this bill those banks and banking organizations would be required to register with the SEC as investment advisers and be subject to SEC regulation of this activity.

Section 217 would amend the Investment Advisers Act to subject banks that advise investment companies (typically, mutual funds) to the same regulatory scheme as other advisers to investment companies. Currently, about 120 large bank holding companies engage in investment adviser activities. Before enactment of the National Securities Markets Improvement Act of 1996, the SEC charged a fee of $150 to register investment advisers.

Because of the 1996 act, the SEC is in the process of formulating a fee that will be based on the expected cost of administering the registration program and the expected number of registrants. Banking organizations that continue to be investment advisers would have to pay this new registration fee annually and maintain books and records according to SEC rules. However, if such services are performed through a separately identifiable department or division of a bank, the department or division and not the bank itself shall be deemed to be the investment adviser. Since the fee would be based on the administrative costs of an electronic filing system, CBO does not expect that those costs to the industry would be large.

Section 222 would require an investment adviser that holds a controlling interest (25 percent or more) in an investment company in a trustee or fiduciary capacity, to transfer the power to vote the shares of the investment company. Under the bill, the adviser would have to transfer voting shares to another fiduciary or to the beneficial owners, vote the fiduciary shares in the same proportion as shares held by all other shareholders of the investment company, or vote the shares according to new rules that the SEC may prescribe. Inasmuch as the adviser would have the flexibility to choose either to transfer voting powers or vote following specified guidelines, the direct costs of complying with this provision should not be significant. If the adviser holds the shares in a trustee or fiduciary capacity under an employee benefit plan subject to the Employee Retirement Income Security Act of 1974 (ERISA), the adviser would have to transfer the power to vote the shares of the investment company to another plan fiduciary who is not affiliated with the adviser or an affiliate. According to some industry experts, this requirement may be in conflict with current ERISA contracts. The bill would not necessarily force advisers to amend those contracts, however. According to information obtained from the SEC, advisers affected by this provision may be able to avoid the cost of amending existing contracts by not voting those shares (or using other permissible measures) until such contracts come up for renewal and are adjusted to reflect the new restrictions on voting.

Section 214 would amend the Investment Company Act to require any person issuing or selling the securities of a registered investment company that is advised or sold through a bank to disclose that an investment in the fund is not insured by the Federal Deposit Insurance Corporation or any other government agency. Under current interagency guidelines issued by the banking regulators, when non-deposit investment products are either recommended or sold to retail customers, the disclosures must specify that the product is not insured by FDIC. In addition, guidance issued by the NASD states that advertising and sales presentations of its bank-affiliated members should disclose that mutual funds purchased through banks are not deposits of, or guaranteed by, the bank and are not federally insured or otherwise guaranteed by the federal government. Much of the industry may already be performing disclosures similar to those required by the mandate therefore, a new federal requirement to make such disclosures would not impose a large incremental cost on the industry. In general, the costs of creating a standard disclosure form and distributing such a statement at the time of a transaction are not large.

Foreign banks

Section 153 would amend the International Banking Act of 1978 (IBA) to require that foreign banks seek prior approval from the Federal Reserve Board for establishing separate subsidiaries or using nonblank subsidiaries to act as representative offices. Under current law, a foreign bank must obtain the approval of the Federal Reserve Board (FRB) before establishing a representative office in the United States. A representative office handles administrative matters and some types of sales for the foreign bank owner, but does not handle deposits. In some cases, foreign banks are

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1st Session | Part 3

FINANCIAL SERVICES ACT OF 1999

JUNE 15, 1999.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

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

R E P O R T

together with

ADDITIONAL VIEWS

[To accompany H.R. 10]

The Committee on Commerce, to whom was referred the bill (H.R. 10) to enhance competition in the financial services industry by providing a prudential framework for the affiliation of banks, securities firms, and other financial service providers, and for other purposes, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

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SEC. 218. DEFINITION OF BROKER UNDER THE INVESTMENT ADVISERS ACT OF 1940

Section 202(a)(3) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–2(a)(3)) is amended to read as follows:

"(3) The term 'broker' has the same meaning as in section 3 of the Securities Exchange Act of 1934.".

SEC. 219. DEFINITION OF DEALER UNDER THE INVESTMENT ADVISERS ACT OF 1940.

Section 202(a)(7) of the Investment Advisers Act of 1940. (15 U.S.C. 80b–2(a)(7)) is amended to read as follows:

"(7) The term 'dealer' has the same meaning as in section 3 of the Securities Exchange Act of 1934, but does not include an insurance company or investment company.".

"SEC. 210. INTERAGENCY CONSULTATION.

The Investment Advisers Act of 1940 (15 U.S.C. 80b–1 et seq.) is amended by inserting after section 210 the following new section:

"SEC. 210A. CONSULTATION

"(a) EXAMINATION RESULTS AND OTHER INFORMATION.—

"(1) The appropriate Federal banking agency shall provide the Commission upon request the results of any examination, reports, records, or other information to which such agency may have access with respect to the investment advisory activities—

"(A) of any—

"(i) bank holding company;

"(ii) bank; or

"(iii) separately identifiable department or division of a bank,

that is registered under section 203 of this title; and

"(B) in the case of a bank holding company or bank that has a subsidiary or a separately identifiable department or division registered under that section, of such bank or bank holding company.

"(2) The Commission shall provide to the appropriate Federal banking agency upon request the results of any examination, reports, records, or other information with respect to the investment advisory activities of any bank holding company, bank, or separately identifiable department or division of a bank, which is registered under section 203 of this title.

"(b) EFFECT ON OTHER AUTHORITY.—Nothing in this section shall limit in any respect the authority of the appropriate Federal banking agency with respect to such bank holding company, bank, or department or division under any other provision of law.

"(c) DEFINITION.—For purposes of this section, the term 'appropriate Federal banking agency' shall have the same meaning as in section 3 of the Federal Deposit Insurance Act.".

SEC. 221. TREATMENT OF BANK COMMON TRUST FUNDS.

(a) SECURITIES ACT OF 1933.—Section 3(a)(2) of the Securities Act of 1933 (15 U.S.C. 77c(a)(2)) is amended by striking "or any interest or participation in any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of assets contributed thereto by such bank in its capacity as trustee, executor, administrator, or guardian" and inserting "or any interest or participation in any common trust fund or similar fund that is excluded from the definition of the term 'investment company' under section 3(c)(3) of the Investment Company act of 1940".

(b) SECURITIES EXCHANGE ACT OF 1934.—Section 3(a)(12)(A)(iii) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(12)(A)(iii)is amended to read as follows:

"(iii) any interest or participation in any common trust fund or similar fund that is excluded from the definition of the term 'investment company' under section 3(c)(3) of the Investment Company Act of 1940;".

(C) INVESTMENT COMPANY ACT OF 1940.—Section 3(c)(3) of the Investment Company Act of 1940 (15 U.S.C. 80a–3(c)(3)) is amended by inserting before the period the following: ", if—

"(A) such fund is employed by the bank solely as an aid to the administration of trusts, estates, or other accounts created and maintained for a fiduciary purpose;

"(B) except in connection with the ordinary advertising of the bank's fiduciary services, interests in such fund are not—

"(i) advertised; or

"(ii) offered for sale to the general public; and

"(C) fees and expenses charged by such fund are not in contravention of fiduciary principles established under applicable Federal or State law".

SEC. 222. INVESTMENT ADVISERS PROHIBITED FROM HAVING CONTROLLING INTEREST IN REGISTERED INVESTMENT COMPANY.

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

"(g) CONTROLLING INTEREST IN INVESTMENT COMPANY PROHIBITED.—

"(1) IN GENERAL.—If an investment adviser to a registered investment company; or an affiliated person of that investment adviser, holds a controlling interest in that registered investment company in a trustee or fiduciary capacity, such person shall—

"(A) if it holds the shares in a trustee or fiduciary capacity with respect to any employee benefit plan subject to the Employee Retirement Income Security Act of 1974, transfer the power to vote the shares of the investment company through to another person acting in a fiduciary capacity with respect to the plan who is not an affiliated person of that investment adviser or any affiliated person thereof; or

"(B) if it holds the shares in a trustee or fiduciary capacity with respect to any person or entity other than an employee benefit plan subject to the Employee Retirement Income Security Act of 1974—

"(i) transfer the power to vote the shares of the investment company through to—

"(I) the beneficial owners of the shares;

"(II) another person acting in a fiduciary capacity who is not an affiliated person of that investment adviser or any affiliated person of that investment adviser or any affiliated person thereof; or

"(III) any person authorized to receive statements and information with respect to the trust who is not an affiliated person thereof;

"(ii) vote the shares of the investment company held by it in the same proportion as shares held by all other shareholders of the investment company; or

"(iii) vote the shares of the investment company as otherwise permitted under such rules, regulations, or orders as the Commission may prescribe or issue consistent with the protection of investors.

"(2) EXEMPTION.—Paragraph (1) shall not apply to any investment adviser to a registered investment company, or any affiliated person of that investment adviser, that holds shares of the investment company in a trustee or fiduciary capacity if that registered investment company consists solely of assets held in such capacities.

"(3) SAFE HARBOR.—No investment adviser to a registered investment company or any affiliated person of such investment adviser shall be deemed to have acted unlawfully or to have breached a fiduciary duty under State or Federal law solely by reason of acting in accordance with clause (i), (ii), or (iii) of paragraph (1)(B).".

SEC. 223. STATUTORY DISQUALIFICATION FOR BANK WRONGDOING.

Section 9(a) of the Investment Company Act of 1940 (15 U.S.C. 80a–9(a)) is amended in paragraphs (1) and (2) by striking "securities dealer, transfer agent," and inserting "securities dealer, bank, transfer agent,".

SEC. 224. CONFORMING CHANGE IN DEFINITION.

Section 2(a)(5) of the Investment Company Act of 1940 (15 U.S.C. 80a–2(a)(5)) is amended by striking "(A) a banking institution organized under the laws of the United States" and inserting "(A) a depository institution (as defined in section 3 of the Federal Deposit Insurance Act) or a bank or agency of a foreign bank (as such terms are defined in section 1(b) of the International Banking Act of 1978)".

SEC. 225 CONFORMING AMENDMENT.

Section 202 of the Investment Advisers Act of 1940 (15 U.S.C. 80b–2) is amended by adding at the end the following new subsection:

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

Reserve Board is the holding company regulator for wholesale financial holding companies.

Title I includes a grandfather provision that permits financial holding companies to retain all non-financial activities and affiliates, for a period of 10 years from September 1997 (with the possibility of a 5 year extension), so long as the financial holding company derives at least 85 percent of its gross worldwide revenues from financial activities. These provisions are designed to provide financial holding companies that own insured banks with the flexibility to conform their commercial operations to the limits of the Act over a sufficiently long period to allow full recovery of the value of these commercial operations by the financial holding company. The title provides a similar grandfather provision applicable to WFIs, but because WFIs are uninsured institutions, the holding period for commercial affiliates is not limited. Title I also grants the Board a limited amount of flexibility to permit financial holding companies to engage, to a limited extent, in nonfinancial activities that are complementary to a financial activity, provided that the nonfinancial activities are conducted on a small scale relative to the permissible activities to which they are associated. Title I allows these entities to directly or indirectly acquire or control shares, assets, or ownership interests in commercial concerns without limit for the purpose of appreciation and ultimate resale by expressly including "merchant banking" in the definition of activities that are "financial in nature."

With further respect to activities that are included as "financial in nature," the term "providing financial, investment, or economic advisory services, including advising an investment company (as defined in section 3 of the Investment Company Act of 1940)" is intended to include all activities that are necessary or incidental to the business or operation of an investment company or an investment adviser registered under the Investment Advisers Act of 1940, including the provision of personnel to an investment company or to a company that provides products or services to an investment company, as well as money management and investment management services and related activities for other clients. It is the Committee's intention that these activities be deemed financial in nature, regardless of whether they are conducted separately or in combination with other activities, and regardless of whether they are conducted in accordance with limitations imposed by the Federal Reserve Board prior to the enactment of this Act. The term, thus, includes, for example, such activities as acting as the sponsor, organizer, distributor, principal underwriter, sales agent, broker, dealer, placement agent, administrator, transfer agent, registrar, shareholder servicing agent, dividend disbursement agent, custodian, investment adviser or sub-investment adviser of an investment company, or controlling an investment company.

TITLE II

Subtitle A of title II of the Act amends the Federal securities laws in order to provide functional regulation of bank securities activities. The Act repeals the exemptions under the Federal securities laws that currently apply to banks, subjecting banks and their affiliates and subsidiaries to the same regulation as all other pro-

viders of securities products in order to provide investors with the same level of protections.

H.R. 10, as reported by the Committee on Banking and Financial Services, also eliminated the blanket exemptions for banks from the definition of "broker" and "dealer," but included sixteen new exceptions for activities in which banks could engage without being subject to broker-dealer regulation under the Federal securities laws. The breadth of the exceptions in the Banking Committee's bill would have had the effect of allowing banks to engage in extensive securities activities without being subject to the securities laws that apply to their broker-dealer competitors engaged in the same activity.

H.R. 10, as passed by the Full House in the 105th Congress, contained certain narrow exceptions that were intended by (1) address competitive concerns, (2) address market integrity issues, and (3) minimize the risks to investors, particularly individuals.

Accordingly, the Committee on Commerce restored H.R. 10 to the narrow approach passed last year by the Full House. This approach repeals the blanket exemptions from the definition of "broker" and "dealer" and provides a number of exceptions that permit banks to engage in certain activities that have traditionally been provided by banks, subject to certain limitations, without becoming subject to the Federal securities laws. These exceptions relate to third-party networking arrangements, trust activities, traditional banking transactions such as commercial paper and exempted securities, employee and shareholder benefit plans, sweep accounts, affiliate transactions, private placements, safekeeping and custody services, asset-backed securities, and derivatives.

Banks today also engage in a wide range of investment advisory activities that are comparable to, and competitive with, the services of other investment advisers. Banks that advise mutual funds, however, are not currently required to register as investment advisers under the Investment Advisers Act of 1940 and, therefore, are not subject to the same securities regulatory scheme that applies to other entities that advise mutual funds. The Committee believes that existing banking regulation does not adequately address the investor protection concerns that are raised by bank involvement in mutual fund activities. Subtitle B amends the Investment Advisers Act to subject banks that advise mutual funds to the same regulatory scheme as other advisers to mutual funds. Subtitle B also addresses specific conflicts of interest that may arise when banks advise mutual funds.

Subtitle B broadens the definition of "investment adviser" in the Investment Advisers Act to include banks that advise mutual funds. This amendment ensures that all mutual fund advisers are subject to the same rules. The current exclusion for banks under the Investment Advisers Act, like the exclusions for banks under the Securities Act of 1933 and the Securities Exchange act of 1934 (the Exchange Act), is a holdover from a time when it was assumed that banks could not engage in securities-related activities. That assumption is no longer valid, and the Committee believes that corrective legislation is essential Excluding banks from the definition of "investment adviser" hampers effective Commission oversight of bank-advised mutual funds because Commission examiners do not

have access to all of the books and records normally available when they examine a mutual fund whose adviser is registered with the Commission. Requiring banks that advise mutual funds to register under the Investment Advisers Act provides the Commission with the authority it needs to oversee the activities of these advisers, and provides investors in bank-advised mutual funds with the same protections enjoyed by other mutual fund investors.

Although the Investment Company Act and the Investment Advisers Act currently restrict transactions between mutual funds and their affiliates, the statutes do not address specifically all of the concerns that may exist when banks provide investment management and related services to funds. Because banks advising mutual funds may be subject to particular conflicts of interest because of the nature of their other activities, H.R. 10 provides the Commission with additional authority to address special conflicts of interest that may exist when a bank and the mutual fund it advises do business with each other. These conflicts may arise, for example, when a bank loans money to a fund it advises, acts as the fund's custodian, or holds the fund's shares in a fiduciary capacity. Another area of concern involves the potential investor confusion that may be created when a bank advises a mutual fund or sells fund shares on bank premises. Because the Federal government insures bank deposits, it is possible that some investors may mistakenly believe that a mutual fund advised by a bank or sold on bank premises also is insured. The bill addresses this concern by requiring banks to disclose, in this situation, that an investment in the fund is not insured by the Federal Deposit Insurance Corporation (FDIC) or any other government agency. Because the Committee believes that the potential for investor confusion about whether a mutual fund investment is insured by the government exists only where those funds are sold through, or advised by a bank, H.R. 10 applies this disclosure obligation only to such funds, and not to funds that are not sold through or advised by a bank.

The bill grants the Commission authority to address concerns that arise when banks advise or sell mutual funds. This authority is not intended to subject bank advisers to more regulation than other fund advisers, but rather is intended to provide the Commission with the flexibility to effectively address problems particular to mutual funds that are advised by a bank or sold on bank premises.

Subtitle C creates a new investment bank holding company structure under the Exchange Act. This subtitle is designed to implement a new concept of SEC supervision of broker/dealer holding companies that voluntarily elect SEC supervision. In addition, the bill contemplates that an investment bank holding company could include one or more wholesale financial institutions.

Under this voluntary supervision, the SEC will have greater authority to oversee the entire entity, thus satisfying the expectations of foreign jurisdictions that the entity be subject to consolidated supervision. This provision is designed to improve the competitiveness of U.S. investment bank holding companies that do business in foreign jurisdictions that require consolidated holding company supervision for securities firms.

inition continues to exclude insurance companies and investment companies.

Section 217. Removal of the exclusion from the definition of investment adviser for banks that advise investment companies

Section 202(a)(11) of the Investment Advisers Act (15 U.S.C. §80b–202(a)(11)) currently excludes banks and bank holding companies from the definition of "investment adviser." Section 217(a) of the bill amends section 202(a)(11) to include within the definition of "investment adviser" any bank or bank holding company that serves as investment to a registered investment company. This amendment is intended to make banks and bank holding companies that advise investment companies subject to the same regulatory scheme as other investment company advisers. It also is intended to help the Commission more effectively protect the interests of shareholders in bank-advised investment companies.

Section 217 protects shareholders of bank-advised investment companies by giving the Commission greater access to records and information necessary to ensure that bank advisers comply with the Federal securities laws. Currently, when Commission examiners examine an investment company that is advised by a bank that is not a registered investment adviser, the Commission staff does not have the authority to require the bank to produce trading records related to advisory customers other than registered investment companies. This limitation makes it difficult to uncover certain practices that may violate the Federal securities laws. For example, a bank that advises an investment company could allocate more profitable trades to bank trust accounts and less profitable trades to the investment company. Bank advisory personnel also could engage in frontrunning the securities transactions of the investment company by trading the same securities for their personal accounts. If all banks that advise investment companies were subject to the Advisers Act, the staff would have greater access to books and records that might reveal these practices.

A bank may establish a "separately identifiable department or division" (SID) to act as investment adviser to a registered investment company, in which case only the SID, and not the bank, would be deemed an investment adviser to a registered investment company, in which case only the SID, and not the bank, would be deemed an investment adviser under the Investment Advisers Act. Section 217(b) of the bill amends section 202(a) of the Investment Advisers Act to add a definition of a "separately identifiable department or division" of a bank.

Section 218. Definition of broker under the Investment Advisers Act of 1940

Section 218 of the bill replaces the definition of "broker" in section 202(a)(3) of the Investment Advisers Act (15 U.S.C. §80b–2(a)(3)) with a reference to the definition of "broker" in the Exchange Act.

Section 219. Definition of dealer under the Investment Advisers Act of 1940

Section 219 of the bill similarly replaces the definition of "dealer" in section 202(a)(7) of the Investment Advisers Act (15 U.S.C. §80b–

2(a)(7) with a reference to the definition of "dealer" in the Exchange Act. The amended definition continues to exclude insurance companies and investment companies.

Section 220. Interagency consultation

Section 220 of the bill adds a new section 210A to the Investment Advisers Act that requires the appropriate Federal banking agency to share with the Commission, and the Commission to share with the banking agency, upon request, the results of any examination, reports, records, or other information regarding the investment advisory activities of any bank holding company, bank, or SID that is registered as an investment adviser under the Investment Advisers Act. If a bank holding company or bank has a subsidiary or a SID registered as an investment adviser under the Investment Advisers Act, the section requires that the banking agency share with the commission, upon request, the results of any examination, reports, records, or other information regarding the bank holding company or bank. Section 220 also clarifies that it does not in any way limit the authority of the banking agency to regulate the bank holding company, bank, or SID.

Section 220 is intended to assist the Commission and the Federal banking agencies in obtaining information from one another that may be necessary or helpful in carrying out their statutory responsibilities. The section also is intended to provide the commission with access to information regarding a bank holding company or bank that, although not itself registered as an investment adviser under the Investment Advisers Act, has a subsidiary or SID that is registered as an investment adviser under the investment Advisers Act.

Section 221. Treatment of bank common trust funds

The Federal securities laws currently exempt interests in common trust funds from the registration requirements of the Securities Act and exclude common trust funds from the definition of investment company under the Investment Company Act. In addition, because interests in common trust funds are exempted securities under the Exchange Act, persons effecting transaction in these interests need not register as broker-dealers. All three statutes limit the exception to a common trust fund or similar fund maintained by a bank exclusively for the collective investment or reinvestment of moneys contributed thereto by the bank in its capacity as a trustee, executor, administrator, or guardian.

Section 221 of the bill largely codifies a long-standing Commission position that the exemption from the securities laws available to a bank common trust fund applies only when the underlying trust relationship is created for bona fide fiduciary purposes, and when the fund is operated for the administrative convenience of the bank in a manner incidental to the bank's traditional trust department activities and not as a vehicle for general investment by the public.

Section 221 amends the common trust fund exception in section 3(c)(3) of the Investment Company Act (15 U.S.C. §80a–3(c)(3)) so that it applies only to a common trust fund that meets three conditions. First, the common trust fund must be employed solely as an

Section 225. Conforming Amendment

Section 225 of the bill amends section 202 of the Investment Advisers Act to add a new subsection (c) that requires that when the Commission, as part of a rulemaking, considers whether an action is necessary or appropriate in the public interest, it consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation. This provision is intended to incorporate into the Investment Advisers Act a standard for Commission rulemaking similar to those that were added to the Securities Act, the Exchange Act, and the Investment Company Act as part of the National Securities Markets Improvement Act of 1996.

Section 226. Effective date

Subtitle B shall become effective 90 days after the date of enactment of this act.

SUBTITLE C—SECURITIES AND EXCHANGE COMMISSION SUPERVISION OF INVESTMENT BANK HOLDING COMPANIES

Subtitle C creates a new investment bank holding company structure under the Federal securities laws. This subtitle is designed to implement a new voluntary concept of Commission supervision of investment bank holding companies. Under this voluntary supervision structure, the commission will have greater authority to oversee the entire entity, thus satisfying the expectations of foreign jurisdictions and some counterparties that the entity be subject to consolidated supervision. This option should be useful, or perhaps even necessary, for investment bank holding companies that do business in foreign jurisdictions that require consolidated holding company supervision. In addition, the bill contemplates that an investment bank holding company could include one or more wholesale financial institutions (WFIs).

Section 231. Supervision of investment bank holding companies by the securities and exchange commission

Generally, section 231(a) of the bill amends section 17 of the Exchange Act by adding new subsections (i), (j), and (k).

New subsection 17(i) creates the investment bank holding company, which is defined as: (i) any person, other than a natural person, that owns or controls one or more brokers or dealers; and (ii) any associated person of an investment bank holding company. Subsection 17(i) prescribes a scheme of voluntary Commission oversight for investment bank holding companies that have no affiliated insured banks or savings associations but desire consolidated holding company oversight.

a. Elective supervision of investment bank holding companies that do not have affiliated banks or savings associations

Paragraph (1) of new subsection 17(i) permits any investment bank holding company that does not have an affiliated insured bank or savings association, but may include a WFI, to elect Commission supervision. This supervision may be useful or necessary to engage in financial activities globally, and, therefore, may be a

(3) as custodian.

If such allegations are established, the court may enjoin such persons from acting in any or all such capacities either permanently or temporarily and award such injunctive or other relief against such person as may be reasonable and appropriate in the circumstances, having due regard to the protection of investors and to the effectuation of the policies declared in section 1(b) of this title.

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INVESTMENT ADVISERS ACT OF 1940

TITLE II—INVESTMENT ADVISERS

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DEFINITIONS

SEC. 202. (a) When used in this title, unless the context otherwise requires, the following definitions shall apply:

(1)* * *

* * * * * * *

[(3) "Broker" means any person engaged in the business of effecting transactions in securities for the account of others, but does not include a bank.**]**

(3) The term "broker" has the same meaning as in section 3 of the Securities Exchange Act of 1934.

* * * * * * *

[(7) "Dealer" means any person regularly engaged in the business of buying and selling securities for his own account, through a broker or otherwise, but does not include a bank, insurance company, or investment company, or any person insofar as he is engaged in investing, reinvesting, or trading in securities, or in owning or holding securities, for his own account, either individually or in some fiduciary capacity, but not as a part of a regular business.**]**

(7) The term "dealer" has the same meaning as in section 3 of the Securities Exchange Act of 1934, but does not include an insurance company or investment company.

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(11) "Investment adviser" means any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities; but does not include (A) a bank, or any bank holding company as defined in the Bank Holding Company Act of 1956, which is not an **[**investment company**]** *investment company, except that the term "investment adviser" includes any bank or bank holding company to the extent that such bank or bank holding company serves or acts as an investment adviser to a registered investment company, but if, in the*

case of a bank, such services or actions are performed through a separately identifiable department or division, the department or division, and not the bank itself, shall be deemed to be the investment adviser; (B) any lawyer, accountant, engineer, or teacher whose performance of such services is solely incidental to the practice of his profession; (C) any broker or dealer whose performance of such services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefor; (D) the publisher of any bona fide newspaper, news magazine, or business or financial publication of general and regular circulation; (E) any person whose advice, analyses, or reports relate to no securities other than securities which are direct obligations of or obligations guaranteed as to principal or interest by the United States, or securities issued or guaranteed by corporations in which the United States has a direct or indirect interest which shall have been designated by the Secretary of the Treasury, pursuant to section 3(a)(12) of the Securities Exchange Act of 1934, as exempted securities for the purposes of that Act; or (F) such other persons not within the intent of this paragraph, as the Commission may designate by rules and regulations or order.

* * * * * * *

(26) The term "separately identifiable department or division" of a bank means a unit—

(A) that is under the direct supervision of an officer or officers designated by the board of directors of the bank as responsible for the day-to-day conduct of the bank's investment adviser activities for one or more investment companies, including the supervision of all bank employees engaged in the performance of such activities; and

(B) for which all the records relating to its investment adviser activities are separately maintained in or extractable from such unit's own facilities or the facilities of the bank, and such records are so maintained or otherwise accessible as to permit independent examination and enforcement by the Commission of this Act or the Investment Company Act of 1940 and rules and regulations promulgated under this Act or the Investment Company Act of 1940.

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

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SEC. 210A. CONSULTATION.

(a) EXAMINATION RESULTS AND OTHER INFORMATION.—

(1) The appropriate Federal banking agency shall provide the Commission upon request the results of any examination, re-

ports, records, or other information to which such agency may have access with respect to the investment advisory activities—

(A) of any—

(i) bank holding company;

(ii) bank; or

(iii) separately identifiable department or division of a bank,

that is registered under section 203 of this title; and

(B) in the case of bank holding company or bank that has a subsidiary or a separately identifiable department or division registered under that section, of such bank or bank holding company.

(2) The Commission shall provide to the appropriate Federal banking agency upon request the results of any examination, reports, records, or other information with respect to the investment advisory activities of any bank holding company, bank, or separately identifiable department or division of bank, which is registered under section 203 of this tile.

(b) EFFECT ON OTHER AUTHORITY.—Nothing in this section shall limit in any respect the authority of the appropriate Federal banking agency with respect to such bank holding company, bank, or department or division under any other provision of law.

(c) DEFINITION.—For purposes of this section, the term "appropriate Federal banking agency" shall have the same meaning as in section 3 of the Federal Deposit Insurance Act.

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SECTION 3 OF THE SECURITIES ACT OF 1933

EXEMPTED SECURITIES

SEC. 3 (a) Except as hereinafter expressly provided, the provisions of this title shall not apply to any of the following classes of securities:

(1) Reserved.

(2) Any security issued or guaranteed by the United States or any Territory thereof, or by the District of Columbia, or by any State of the United States, or by any political subdivision of a State or Territory, or by any public instrumentality of one or more States or Territories, or by any person controlled or supervised by and acting as an instrumentality of the Government of the United States pursuant to authority granted by the Congress of the United States; or any certificate of deposit for any of the foregoing; or any security issued or guaranteed by any bank; or any security issued by or representing an interest in or a direct obligation of a Federal Reserve bank; **[**or any interest or participation in any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of assets contributed thereto by such bank in its capacity as trustee, executor, administrator, or guardian**]** *or any interest or participation in any common trust fund or similar fund that is excluded from the definition of the term "investment company" under section 3(c)(3) of the Investment Company Act of 1940;* or any security which is an