

FAIR ACCESS TO INVESTMENT RESEARCH ACT OF 2015

JANUARY 28, 2016.—Committed to the Committee of the Whole House on the State
of the Union and ordered to be printed

Mr. HENSARLING, from the Committee on Financial Services,
submitted the following

R E P O R T

together with

MINORITY VIEWS

[To accompany H.R. 2356]

[Including cost estimate of the Congressional Budget Office]

The Committee on Financial Services, to whom was referred the bill (H.R. 2356) to direct the Securities and Exchange Commission to provide a safe harbor related to certain investment fund research reports, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

PURPOSE AND SUMMARY

Introduced by Representative Hill on May 15, 2015, H.R. 2356, the Fair Access to Investor Research Act, directs the Securities and Exchange Commission (SEC) to provide a safe harbor for research reports that cover Exchange Traded Funds (ETFs) so that these reports are not considered “offers” under Section 5 of the Securities Act of 1933. H.R. 2356 requires the SEC to revise applicable regulations within 120 days of the Act’s enactment and, if the deadline is not met, H.R. 2356 provides that an interim safe harbor will take effect until the SEC’s rules are finalized. To qualify for H.R. 2356’s safe harbor, a broker or dealer must distribute the research report in the regular course of business and the report must relate to an ETF issuer that (1) has a class of securities listed on a national securities exchange for at least 12 months prior to the publishing or distribution of the report, (2) has an aggregate market value of at least \$75 million, and (3) is either a unit investment

or an open-ended company or a trust whose assets consist primarily of interests in commodities, currencies, or derivative instruments referring commodities or currencies.

BACKGROUND AND NEED FOR LEGISLATION

An ETF is an investment company whose shares are traded intraday on stock exchanges at market-determined prices. Investors may buy or sell ETF shares through a broker or in a brokerage account just as they would the shares of any publicly traded company. In the United States, most ETFs are structured as open-end investment companies (open-end funds) or unit investment trusts, but other structures also exist—primarily for ETFs investing in commodities, currencies, and futures. Investor interest in ETFs has increased significantly in recent years, with 5.7 million U.S. households holding ETF shares in 2013. Yet despite their growing popularity and increasing importance to retail investors, anomalies in the SEC’s safe harbor rules have discouraged most broker-dealers from publishing research regarding ETFs.

The SEC has implemented safe harbors for research issued in support of other asset classes, including listed equities, corporate debt, and closed-end funds. Congress has also provided safe harbors for research covering certain securities offerings. Most recently, in Title I of the Jumpstart Our Business Startups Act, Congress codified a safe harbor for research related to offerings of EGC securities. Yet despite their similarities to these other asset classes, research that covers open-ended funds and ETFs does not benefit from similar safe harbors. As such, most broker-dealers do not publish research regarding ETFs, depriving investors of useful information when deciding whether to invest in this product.

In 2004, as part of its Securities Offering Reform proposal, the SEC requested public comment on whether research relating to ETFs should be protected by a safe harbor. While comments were universally supportive, the SEC did not adopt a final rule.

At a May 13, 2015 Capital Markets and Government Sponsored Enterprises Subcommittee hearing, U.S. Chamber of Commerce Senior Vice President Tom Quaadman testified that:

existing impediments prevent investors from obtaining decision-useful information regarding ETFs . . . Under the Exchange Acts, broker-dealers currently have safe harbors to public research on equity offerings. However, ETFs and openended funds do not have similar specific safe harbors, thereby causing enough legal vagueness to restrict information and research that may be helpful to investors. Despite receiving comments supporting an extension of the safe harbor rules to ETFs and open ended funds, the SEC has not adopted a final rule.

HEARINGS

The Committee on Financial Services’ Subcommittee on Capital Markets and Government Sponsored Enterprises held a hearing examining matters relating to H.R. 2356 on May 13, 2015.

COMMITTEE CONSIDERATION

The Committee on Financial Services met in open session on May 20, 2015, and ordered H.R. 2356 to be reported favorably to the House without amendment by a recorded vote of 48 yeas to 9 nays (recorded vote no. FC-41), a quorum being present. An amendment offered by Representative Waters was not agreed to by voice vote.

COMMITTEE VOTES

Clause 3(b) of rule XIII of the Rules of the House of Representatives requires the Committee to list the record votes on the motion to report legislation and amendments thereto. The sole recorded vote was on a motion by Chairman Hensarling to report the bill favorably to the House without amendment. The motion was agreed to by a recorded vote of 48 yeas to 9 nays (Record vote no. FC-41), a quorum being present.

Record vote no. FC-41

Representative	Yea	Nay	Present	Representative	Yea	Nay	Present
Mr. Hensarling	X			Ms. Waters (CA)		X	
Mr. King (NY)				Mrs. Maloney (NY)	X		
Mr. Royce	X			Ms. Velázquez		X	
Mr. Lucas	X			Mr. Sherman	X		
Mr. Garrett	X			Mr. Meeks	X		
Mr. Neugebauer	X			Mr. Capuano		X	
Mr. McHenry	X			Mr. Hinojosa	X		
Mr. Pearce	X			Mr. Clay		X	
Mr. Posey	X			Mr. Lynch		X	
Mr. Fitzpatrick	X			Mr. David Scott (GA)	X		
Mr. Westmoreland	X			Mr. Al Green (TX)		X	
Mr. Luetkemeyer	X			Mr. Cleaver			
Mr. Huizenga (MI)	X			Ms. Moore		X	
Mr. Duffy	X			Mr. Ellison		X	
Mr. Hurt (VA)	X			Mr. Perlmutter	X		
Mr. Stivers	X			Mr. Himes	X		
Mr. Fincher	X			Mr. Carney	X		
Mr. Stutzman	X			Ms. Sewell (AL)	X		
Mr. Mulvaney	X			Mr. Foster	X		
Mr. Hultgren	X			Mr. Kildee	X		
Mr. Ross	X			Mr. Murphy (FL)	X		
Mr. Pittenger	X			Mr. Delaney	X		
Mrs. Wagner	X			Ms. Sinema	X		
Mr. Barr	X			Mrs. Beatty		X	
Mr. Rothfus	X			Mr. Heck (WA)			
Mr. Messer	X			Mr. Vargas	X		
Mr. Schweikert	X						
Mr. Guinta	X						
Mr. Tipton	X						
Mr. Williams	X						
Mr. Poliquin	X						
Mrs. Love	X						
Mr. Hill	X						
Mr. Emmer	X						

COMMITTEE OVERSIGHT FINDINGS

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

PERFORMANCE GOALS AND OBJECTIVES

Pursuant to clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the Committee states that H.R. 2356 will enhance the quantity and quality of information available to investors by providing for a safe harbor for research reports covering Exchange Traded Funds.

NEW BUDGET AUTHORITY, ENTITLEMENT AUTHORITY, AND TAX EXPENDITURES

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

COMMITTEE COST ESTIMATE

The Committee adopts as its own the cost estimate prepared by the Director of the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974.

CONGRESSIONAL BUDGET OFFICE ESTIMATES

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

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, September 28, 2015.

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

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 2356, the Fair Access to Investment Research Act of 2015.

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

Sincerely,

KEITH HALL.

Enclosure.

H.R. 2356—Fair Access to Investment Research Act of 2015

Under current law, the Securities Exchange Commission's (SEC's) rules generally prohibit an issuer from offering securities for sale without filing a registration statement with the agency.

H.R. 2356 would establish a safe harbor that would allow broker-dealers to issue research reports about certain investment funds without such reports being considered as an offering for sale of shares of those funds. To be eligible for the safe harbor, the research reports would need to meet certain requirements (for example being distributed with reasonable regularity in the normal course of business).

Based on information from the SEC, CBO expects that the commission would need six additional staff positions working across several divisions within the agency to propose and implement the broadened rule. CBO estimates that implementing H.R. 2356 would cost \$2 million over the 2016–2020 period, assuming appropriation of the necessary amounts. Under current law, the SEC is authorized to collect fees sufficient to offset its annual appropriation; therefore, CBO estimates that the net budgetary effect would be negligible. Because enacting the legislation would not affect direct spending or revenues, pay-as-you-go procedures do not apply.

If the SEC increases fees to offset the costs of implementing requirements in the bill, H.R. 2356 would increase the cost of an existing mandate as defined in the Unfunded Mandates Reform Act (UMRA) on private entities required to pay those fees. Based on information from the SEC, CBO estimates that the incremental cost of the mandate would be about \$2 million in fiscal year 2016.

To the extent that H.R. 2356 would eliminate an existing right of action for investors related to research reports for exchange traded funds, it would impose an additional mandate on public and private entities. The cost of the mandate would be the forgone value of the awards and settlements in such cases. To date, CBO has found no cases successfully establishing liability for information contained in or missing from such research reports and expects few, if any, in the future.

Therefore, CBO estimates the total cost of the mandates on public and private entities would be small and would fall well below the annual thresholds established in UMRA for intergovernmental and private-sector mandates (\$77 million and \$154 million in fiscal year 2015, respectively, adjusted annually for inflation).

The CBO staff contacts for this estimate are Susan Willie (for federal costs), Logan Smith (for private-sector mandates), and Melissa Merrell (for intergovernmental mandates). The estimate was approved by H. Samuel Papenfuss, Deputy Assistant Director for Budget Analysis.

FEDERAL MANDATES STATEMENT

The Committee adopts as its own the estimate of Federal mandates prepared by the Director of the Congressional Budget Office pursuant to section 423 of the Unfunded Mandates Reform Act.

ADVISORY COMMITTEE STATEMENT

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

APPLICABILITY TO LEGISLATIVE BRANCH

The Committee finds that the legislation does not relate to the terms and conditions of employment or access to public services or

accommodations within the meaning of the section 102(b)(3) of the Congressional Accountability Act.

EARMARK IDENTIFICATION

H.R. 2356 does not contain any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause 9 of rule XXI.

DUPLICATION OF FEDERAL PROGRAMS

Pursuant to section 3(g) of H. Res. 5, 114th Cong. (2015), the Committee states that no provision of H.R. 2356 establishes or re-authorizes a program of the Federal Government known to be duplicative of another Federal program, a program that was included in any report from the Government Accountability Office to Congress pursuant to section 21 of Public Law 111–139, or a program related to a program identified in the most recent Catalog of Federal Domestic Assistance.

DISCLOSURE OF DIRECTED RULEMAKING

Pursuant to section 3(i) of H. Res. 5, 114th Cong. (2015), the Committee states that H.R. 2356 contains one directed rulemaking.

SECTION-BY-SECTION ANALYSIS OF THE LEGISLATION

Section 1. Short title

This Section cites H.R. 2356 as the “Fair Access to Investment Research Act of 2015”

Section 2. Safe Harbor for Investment Fund Research

This section directs the Securities and Exchange Commission to revise its rules to establish a safe harbor for covered investment fund research reports and provides an interim safe harbor if the SEC fails to revise such rules within the time period covered by the Act.

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

H.R. 2356 does not repeal or amend any section of a statute. Therefore, the Office of Legislative Counsel did not prepare the report contemplated by Clause 3(e)(1)(B) of rule XIII of the House of Representatives.

MINORITY VIEWS

H.R. 2356 would provide a safe harbor from certain investor liability for broker-dealers to distribute research related to Exchange Traded Funds (ETFs) and other similar products. While the goal of providing retail investors with additional important information deserves merit, the bill as it stands does not appear necessary to achieve this goal nor does it address concerns raised by SEC and FINRA staff.

Today, several broker-dealers provide ETF research to retail investors, notwithstanding this threat of liability from the purchasers of ETFs, which only arises when the report contains material misstatements or omissions. It is not clear that any broker-dealers have ever been sued by investors or been subject to an enforcement action by the SEC or FINRA related to their ETF research reports.

In addition, there are several concerns with the bill, echoed by staffs of the SEC and FINRA, which have not yet been addressed. Specifically, those concerns include: the overly broad definition of research reports; the lack of clarity about whether important FINRA content regulations would apply to ETF research reports, as they apply to other research reports; the permanent ban on requiring any ETF research reports to be filed with FINRA, regardless of future abuses; the constraint on the SEC and FINRA's ability to enforce the antimanipulation and antifraud provisions of the securities laws; the fact that the bill may permit brokers to offer ETFs comprised of commodities and derivatives, as well as, registered investment companies and business development companies (BDCs); and the broad interim safe harbor that fails to protect investors and goes into effect before the SEC has enough time to finalize its rulemaking.

An amendment was offered to address these concerns, but was withdrawn during the markup as the bill's sponsors pledged to continue working to modify the language before the bill moves to the House floor. We look forward to working with the sponsor of the bill to address these concerns.

MAXINE WATERS.
AL GREEN.
JOYCE BEATTY.
GWEN MOORE.
WM. LACY CLAY.
KEITH ELLISON.

○