

Union Calendar No. 865

115TH CONGRESS
2D SESSION

H. R. 3857

[Report No. 115–894, Part I]

To amend the Securities Exchange Act of 1934 to establish standards of conduct for brokers and dealers that are in the best interest of their retail customers.

IN THE HOUSE OF REPRESENTATIVES

SEPTEMBER 27, 2017

Mrs. WAGNER (for herself, Mr. BARR, Mr. MESSER, Mr. TROTT, Mr. POSEY, Mr. WILLIAMS, Mr. BUDD, Mr. HOLLINGSWORTH, and Mr. KUSTOFF of Tennessee) introduced the following bill; which was referred to the Committee on Financial Services, and in addition to the Committees on Ways and Means, and Education and the Workforce, for a period to be subsequently determined by the Speaker, in each case for consideration of such provisions as fall within the jurisdiction of the committee concerned

AUGUST 10, 2018

Reported from the Committee on Financial Services

AUGUST 10, 2018

Referral to the Committees on Ways and Means and Education and the Workforce extended for a period ending not later than November 16, 2018

NOVEMBER 16, 2018

Referral to the Committees on Ways and Means and Education and the Workforce extended for a period ending not later than December 28, 2018

DECEMBER 28, 2018

Additional sponsors: Mr. LUETKEMEYER, Mr. HILL, Mr. HULTGREN, Ms. TENNEY, Ms. MCSALLY, Mr. ROTHFUS, and Mr. SESSIONS

DECEMBER 28, 2018

Committees on Ways and Means and Education and the Workforce discharged; committed to the Committee of the Whole House on the State of the Union and ordered to be printed

A BILL

To amend the Securities Exchange Act of 1934 to establish standards of conduct for brokers and dealers that are in the best interest of their retail customers.

1 *Be it enacted by the Senate and House of Representa-*
 2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Protecting Advice for
 5 Small Savers Act of 2017” or the “PASS Act of 2017”.

6 **SEC. 2. REPEAL OF DEPARTMENT OF LABOR FIDUCIARY**
 7 **RULE.**

8 The final rule of the Department of Labor titled
 9 “Definition of the Term ‘Fiduciary’ Conflict of Interest
 10 Rule—Retirement Investment Advice” and related prohib-
 11 ited transaction exemptions published April 8, 2016 (81
 12 Fed. Reg. 20946), shall have no force or effect.

13 **SEC. 3. STANDARDS OF CONDUCT FOR BROKERS AND**
 14 **DEALERS.**

15 (a) STANDARD OF CONDUCT FOR BROKERS AND
 16 DEALERS WHEN MAKING RECOMMENDATIONS TO RETAIL
 17 CUSTOMERS.—

18 (1) IN GENERAL.—The second subsection (k) of
 19 section 15 of the Securities Exchange Act of 1934
 20 (15 U.S.C. 78o(k)) (relating to standards of con-
 21 duct) is amended to read as follows:

22 “(k) STANDARD OF CONDUCT FOR RECOMMENDA-
 23 TIONS TO RETAIL CUSTOMERS.—

24 “(1) IN GENERAL.—The standard of conduct
 25 for a broker or dealer (or registered representative)

1 when providing recommendations to a retail cus-
2 tomer is as follows:

3 “(A) RECOMMENDATION TO RETAIL CUS-
4 TOMER.—When a broker or dealer (or reg-
5 istered representative) makes a recommendation
6 to a retail customer, the recommendation shall
7 be in the retail customer’s best interest at the
8 time it is made by—

9 “(i) reflecting reasonable diligence;
10 and

11 “(ii) reflecting the reasonable care,
12 skill, and prudence that a broker or dealer
13 (or registered representative) would exer-
14 cise based on the customer’s investment
15 profile.

16 “(B) DISCLOSURE TO RETAIL CUS-
17 TOMER.—

18 “(i) IN GENERAL.—Before a broker or
19 dealer (or registered representative) exe-
20 cutes a transaction for the first time for
21 each retail customer based on a rec-
22 ommendation to such retail customer, such
23 broker or dealer (or registered representa-
24 tive) shall disclose prior to the point of sale

1 to such customer, in a clear and concise
2 manner—

3 “(I) the type and scope of serv-
4 ices the broker or dealer (or registered
5 representative) provides;

6 “(II) the standard of conduct
7 that applies to the relationship;

8 “(III) the types of compensation
9 the broker or dealer (or registered
10 representative) receives; and

11 “(IV) any material conflict of in-
12 terest.

13 “(ii) CONTENT OF DISCLOSURE.—The
14 Commission may issue regulations deter-
15 mining the content of the disclosure re-
16 quired in clause (i). Such regulations may
17 provide for a disclosure of fees received by
18 the broker or dealer, whether from the re-
19 tail customer or a third party, prior to the
20 execution of the transaction.

21 “(C) MATERIAL CONFLICT OF INTER-
22 EST.—A broker or dealer (or registered rep-
23 resentative) shall avoid, disclose, or otherwise
24 reasonably manage any material conflict of in-
25 terest with a retail customer.

1 “(2) NONVIOLATION OF STANDARD OF CON-
2 DUCT.—The following is not, by itself, a violation of
3 the standard of conduct described in paragraph (1):

4 “(A) The receipt of compensation, includ-
5 ing transaction-based compensation, by a
6 broker or dealer (or registered representative)
7 or any affiliate of such broker or dealer (or reg-
8 istered representative).

9 “(B) The recommendation by a broker or
10 dealer (or registered representative) to a retail
11 customer of principal transactions (including
12 cross transactions), or the recommendation of
13 affiliated, unaffiliated, or proprietary products
14 or services, or a limited range of products or
15 services.

16 “(3) NO REQUIREMENT TO RECOMMEND LEAST
17 EXPENSIVE PRODUCT.—Nothing in this subsection
18 shall require a broker or dealer (or registered rep-
19 resentative) to recommend the least expensive secu-
20 rity or investment strategy (however quantified) or
21 to analyze all possible securities, other products, or
22 investment strategies before making a recommenda-
23 tion.

24 “(4) DEFINITIONS.—In this subsection:

1 “(A) COMPENSATION.—The term ‘com-
2 pensation’ includes commissions or sales
3 charges, or other fees or variable compensation,
4 for or related to the sale of securities or for the
5 servicing of customer accounts, whether paid by
6 the retail customer or received from a third
7 party.

8 “(B) CUSTOMER’S INVESTMENT PRO-
9 FILE.—The term ‘customer’s investment profile’
10 has the meaning of such term as described in
11 Rule 2111 of the Financial Industry Regulatory
12 Authority as of the date of the enactment of
13 this subsection.

14 “(C) INSTITUTIONAL ACCOUNT.—The term
15 ‘institutional account’ has the same meaning
16 given such term in Rule 4512 of the Financial
17 Industry Regulatory Authority as of the date of
18 the enactment of this subsection.

19 “(D) MATERIAL CONFLICT OF INTER-
20 EST.—The term ‘material conflict of interest’
21 means a financial interest of a broker or dealer
22 (or registered representative) that a reasonable
23 person would expect to affect the impartiality of
24 a recommendation.

1 “(E) REASONABLE DILIGENCE.—The term
2 ‘reasonable diligence’ has the meaning of such
3 term as described in Rule 2111 of the Financial
4 Industry Regulatory Authority as of the date of
5 the enactment of this subsection.

6 “(F) RECOMMENDATION.—The term ‘rec-
7 ommendation’ means either of the following rec-
8 ommendations (under the meaning ascribed to
9 such term in Rule 2111 of the Financial Indus-
10 try Regulatory Authority) for which the broker
11 or dealer (or registered representative) making
12 the recommendation receives or will receive
13 compensation:

14 “(i) A non-discretionary recommenda-
15 tion to buy, hold, or sell securities, or to
16 follow an investment strategy involving se-
17 curities, for taxable or non-taxable ac-
18 counts.

19 “(ii) A non-discretionary recommenda-
20 tion to rollover or transfer assets in an em-
21 ployer-sponsored retirement plan to an in-
22 dividual retirement account.

23 “(G) RETAIL CUSTOMER.—The term ‘re-
24 tail customer’ means a natural person or legal
25 entity, or the legal representative of such nat-

1 ural person or legal entity, in each case other
2 than an institutional account, who—

3 “(i) receives a recommendation from a
4 broker or dealer (or registered representa-
5 tive); and

6 “(ii) implements such recommenda-
7 tion with such broker or dealer primarily
8 for personal, family, retirement, or house-
9 hold purposes.

10 “(5) SUPERSESSION.—The provisions of this
11 subsection shall supersede and preempt State law,
12 other than a State law that regulates insurance
13 products that are not securities, insofar as they may
14 now or hereafter relate to a broker or dealer, or reg-
15 istered representative of a broker or dealer.

16 “(6) FIDUCIARY STATUS UNDER ERISA, THE IN-
17 TERNAL REVENUE CODE, THE INVESTMENT ADVIS-
18 ERS ACT OF 1940, OR OTHER FIDUCIARY REGIMES.—
19 The fact that a person may owe, or may in fact com-
20 ply with, the standard of conduct under this sub-
21 section shall not mean or create any presumption
22 that such person is a ‘fiduciary’ under the Employee
23 Retirement Income Security Act of 1974 (29 U.S.C.
24 1001 et seq.), section 4975 of the Internal Revenue
25 Code of 1986, the Investment Advisers Act of 1940

1 (15 U.S.C. 80b et seq.), or any other Federal, State,
2 or local statutory or regulatory fiduciary regime.”.

3 (2) APPLICATION.—The amendment made by
4 paragraph (1) shall apply to brokers and dealers (or
5 registered representative) on the date that is 18
6 months after the date of the enactment of this Act.

7 (b) RULEMAKING AUTHORITY.—Section 913 of the
8 Dodd-Frank Wall Street Reform and Consumer Protec-
9 tion Act is amended to read as follows:

10 **“SEC. 913. OBLIGATIONS OF BROKERS AND DEALERS AND**
11 **OTHER PERSONS AND ENTITIES.**

12 “(a) RULEMAKING.—

13 “(1) RULEMAKING BY THE COMMISSION.—The
14 Commission may issue regulations as the Commis-
15 sion determines is necessary to facilitate compliance
16 by brokers and dealers (including their registered
17 representative) with the obligations of such brokers
18 and dealers (and their registered representative)
19 under the second subsection (k) of section 15 of the
20 Securities Exchange Act of 1934 only if such rule-
21 making does not impose any obligation related to
22 standard of care on a broker or dealer (or its reg-
23 istered representative) that is in addition to, duplica-
24 tive of, or inconsistent with, the obligations set forth
25 in such subsection.

1 “(2) RULEMAKING BY THE SECRETARY OF
2 LABOR AND THE SECRETARY OF THE TREASURY.—

3 After the date of the enactment of the PASS Act of
4 2017, the Secretary of Labor and the Secretary of
5 the Treasury shall not promulgate any regulation
6 under the Employee Retirement Income Security Act
7 of 1974 (29 U.S.C. 1001 et seq.) or section 4975 of
8 the Internal Revenue Code of 1986, respectively, de-
9 fining the circumstances under which a person is
10 considered a fiduciary that would impose any obliga-
11 tion on a broker or dealer (or its registered rep-
12 resentative) or on a life insurer fulfilling the term
13 ‘insurance company’ as defined in section 3(a)(2) of
14 the Securities Act of 1933 (or its agents or distribu-
15 tors) that is in addition to, duplicative of, or incon-
16 sistent with, the obligations set forth in such sub-
17 section (k) of section 15 of the Securities Exchange
18 Act of 1934 (15 U.S.C. 78o).

19 “(b) EXEMPTION AVAILABLE TO CERTAIN PERSONS
20 WITH RESPECT TO MANUFACTURE OR SALE OF ANNU-
21 ITIES.—

22 “(1) EXEMPTION.—With respect to the manu-
23 facture or sale of annuities within paragraphs (2) or
24 (8) of section 3(a) of the Securities Act of 1933 (15
25 U.S.C. 77c(a)) or section 989J of the Dodd-Frank

1 Wall Street Reform and Consumer Protection Act
2 (15 U.S.C. 77c note), a person regulated by a State
3 insurance regulator may rely on the exemptions in
4 section 408(b)(21) of the Employee Retirement In-
5 come Security Act of 1974 (29 U.S.C. 1108(b)(21))
6 and section 4975(d)(24) of the Internal Revenue
7 Code of 1986 (as added by the PASS Act of 2017)
8 only if—

9 “(A) such person adopts and implements
10 practices on a nationwide basis for the sale of
11 annuity contracts that meet or exceed the min-
12 imum requirements set forth in the second sub-
13 section (k) of section 15 of the Securities Ex-
14 change Act of 1934 (15 U.S.C. 78o) and such
15 person is subject to regulation or examination
16 by a State insurance regulator for purposes of
17 assessing market conduct; or

18 “(B) such person complies with a standard
19 substantially similar to such subsection (k) and
20 is regulated by a State insurance regulator with
21 respect to annuities within paragraphs (2) or
22 (8) of section 3(a) of the Securities Act of 1933
23 (15 U.S.C. 77c(a)) or section 989J of the
24 Dodd-Frank Wall Street Reform and Consumer
25 Protection Act (15 U.S.C. 77c note).

1 “(2) COORDINATION AND COOPERATION.—

2 Upon the request of any State insurance regulator,
3 the Commission or the Financial Industry Regu-
4 latory Authority shall provide such reasonable assist-
5 ance to the requesting Authority as needed in con-
6 nection with the coordination or implementation of
7 this section.

8 “(3) DEFINITION OF STATE INSURANCE REGU-

9 LATOR.—As used in this subsection, the term ‘State
10 insurance regulator’ means the principal insurance
11 regulatory authority of a State, the District of Co-
12 lumbia, any territory of the United States, Puerto
13 Rico, Guam, American Samoa, the Trust Territory
14 of the Pacific Islands, the Virgin Islands, and the
15 Northern Mariana Islands.

16 “(c) ADDITIONAL EXEMPTIONS.—A person who com-
17 plies with a standard substantially similar to the second
18 subsection (k) of section 15 of the Securities Exchange
19 Act of 1934 (15 U.S.C. 78o) may rely on the exemptions
20 in section 408(b)(21) of the Employee Retirement Income
21 Security Act of 1974 (29 U.S.C. 1108(b)(21)) and section
22 4975(d)(24) of the Internal Revenue Code of 1986 (as
23 added by the PASS Act of 2017) only if such person is—

24 “(1) registered as an investment adviser under
25 the Investment Advisers Act of 1940 (15 U.S.C.

1 80b–1 et seq.) or under the laws of the State in
2 which the person maintains its principal office and
3 place of business; or

4 “(2) a bank or similar financial institution su-
5 pervised by the United States or a State, or a sav-
6 ings association (as defined in section 3(b)(1) of the
7 Federal Deposit Insurance Act (12 U.S.C.
8 1813(b)(1)).”.

9 (c) EXEMPTION FROM PROHIBITED TRANSACTIONS
10 FOR BROKERS AND DEALERS, AND OTHER PERSONS AND
11 ENTITIES, WHEN MAKING RECOMMENDATIONS TO RE-
12 TAIL CUSTOMERS.—

13 (1) Section 408(b) of the Employee Retirement
14 Income Security Act of 1974 (29 U.S.C. 1108(b)) is
15 amended by adding at the end the following:

16 “(21) Any transaction involving a recommenda-
17 tion made by a broker or dealer (including its reg-
18 istered representative), or other persons or entities,
19 that is subject to the requirements of the second
20 subsection (k) of section 15 of the Securities Ex-
21 change Act of 1934 (15 U.S.C. 78o(k)).”.

22 (2) Section 4975(d) of the Internal Revenue
23 Code of 1986 is amended by adding at the end the
24 following:

1 “(24) any transaction involving a recommenda-
2 tion made by a broker or dealer (including its reg-
3 istered representatives), or other persons or entities,
4 that is subject to the requirements of the second
5 subsection (k) of section 15 of the Securities Ex-
6 change Act of 1934 (15 U.S.C. 78o(k)).”.

7 (d) REPEAL OF CERTAIN PROVISIONS.—The fol-
8 lowing provisions are hereby repealed:

9 (1) The second subsection (l) and subsection
10 (m) of section 15 of the Securities Exchange Act of
11 1934 (15 U.S.C. 78o).

12 (2) Subsections (g), (h), and (i) of section 211
13 of the Investment Advisers Act of 1940 (15 U.S.C.
14 80b–11).

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2^D Session

H. R. 3857

[Report No. 115-894, Part I]

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