Blogs
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Section 848 of the Financial Choice Act 2017: Unwise at any Speed (Conclusion)

This series of posts has examined the misguided efforts of the House Financial Services Committee to reform the existing process for issuing exemptive orders pursuant to Section 6(c) of the Investment Company Act of 1940 (the "1940 Act"). The previous posts discussed the problems with the current process and why Section 848 of the pending Financial Choice Act of 2017 would make matters much worse. This concluding post considers the possibility that Section 848 may not accomplish anything and then discusses other possible reforms to the exemptive process that may prove more fruitful.

Working around Section 848

This isn't the first time that Congress tried to impose a firm deadline on the SEC's review of filings. Section 8(a) of the Securities Act of 1933 provides that:

> [T]he effective date of a registration statement shall be the twentieth day after the filing thereof or such earlier date as the Commission may determine …."

However:

> If any amendment to any such statement is filed prior to the effective date of such statement, the registration statement shall be deemed to have been filed when such amendment was filed …."

To avoid putting the SEC staff in a bind when they couldn't meet the 20 day deadline, registrants began adding the following legend to their registration statements:

> The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective …."

This practice was codified into Rule 473 in 1947. It basically turned a right into an option; a registrant can threaten to file an amendment without the legend if the review process becomes too protracted (and the SEC can respond by threatening to file a stop order). As explained in the last post, Section 848 permits a 45 day extension of the review period with the applicant's consent. One could imagine such a consent becoming standard in every initial application. Applicants might even start adding a legend that the application will be deemed to be continually resubmitted, so as to continually restart the 45 day review period. This may be the best one could hope from Section 848—that it would become a last resort for an applicant after an unconscionable delay responding to an application.

In Fairness

Section 848 raises a point that deserves more thoughtful analysis. As it presently exists, the administrative process for issuing exemptive orders is not perfect, and it can be very frustrating and disappointing for an applicant that believes it fully deserves the exemptive order that it has sought. Here are some other reforms that may be worth serious consideration—

- The SEC Chair could formally task the Division of Investment Management (the "Division") with internal deadlines for reviewing and commenting on exemptive applications (no more than X days from receipt), and could make certain that the relevant appropriations legislation contained appropriate amounts of

money fully and properly staffing this aspect of the Divisions overall responsibilities in administering the 1940 Act. Application fees could be charged to offset increased appropriations.

- The SEC could adopt procedures specifically for hearing objections to proposed orders or denials of applications. Once standing is established, objectors should be permitted to submit briefs directly and applicants should be permitted to respond. The SEC staff could then make their actual policy recommendations to the SEC, rather than trying to cast objections in their best light.
- The SEC Chair could engage with the Division to properly prioritize and re-prioritize its tasks on a regular basis so that the projects with the greatest consequences, in terms of most immediate effect on investor protection, would get expedited to the front of the line, while the least deserving would be deferred. The Division could be required to report monthly to the SEC Chair on its progress in meeting its deadlines, and the SEC Chair could be required to report to its Congressional oversight panels. Such an express oversight process by the SEC Chair and the Congressional oversight panels would give the industry several touch-points for commenting on, or even disputing, resource allocation and responsiveness issues.

Finally, any reforms should extend to every provision in the 1940 Act that permits the SEC to exercise exemptive authority. (The temporary exemption provided by Rule 6b-1 for applications filed by employee securities companies could be excluded because they don't raise the policy and shareholder protection issues raised in Section 6(c) applications.)

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