

Via Hand Delivery

June 12, 2018

The Honorable Bill Huizenga
Chairman
Subcommittee on Capital Markets, Securities, and Investment
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

The Honorable Carolyn B. Maloney
Ranking Member
Subcommittee on Capital Markets, Securities, and Investment
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

*Re: June 13, 2018, hearing entitled "Ensuring Effectiveness, Fairness, and Transparency in Securities Law Enforcement"*¹

Dear Mr. Chairman and Ranking Member Maloney:

I am writing on behalf of the Council of Institutional Investors (CII), a nonpartisan, nonprofit association of public, corporate, and union employee benefit funds, other employee benefit plans, foundations, and endowments with combined assets under management exceeding \$3.5 trillion. Our member funds include major long-term shareholders with a duty to protect the retirement savings of millions of workers and their families.

Our associate members include a range of asset managers with more than \$25 trillion in assets under management, most also with long-term investment horizons. CII members share a commitment to healthy public capital markets and strong corporate governance.²

The purpose of this letter is to thank you for holding the above referenced hearing and to share with you some of our views on this important topic. We would respectfully request that this letter be included in the hearing record.

We offer the following summary discussion of CII views on specific issues addressed by one of the bills to be examined by the Subcommittee at the hearing. We agree with the North American

¹ Financial Services Committee, Hearings, <https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=403565>.

² For more information about the Council of Institutional Investors (CII) and our members, please visit CII's website at http://www.cii.org/about_us.

Securities Administrators Association (NASAA) that the proposed legislation, if enacted, would be “bad for investors and bad for our capital markets.”³

H.R. 5037⁴

As a threshold matter, we disagree with the putative finding in this bill that overlapping federal and state regulation contributes to “declining public interest in the United States public market.”⁵ While private and global markets are stronger than in years past, we do not believe that interest in U.S. public markets is declining.⁶ And while regulatory structures always can be improved, on the whole investor confidence in U.S. markets is so great precisely because of effective and appropriate regulation and accountability.⁷ The volume of initial public offerings is on the rise,⁸ and the companies engaging in IPOs today are stronger and healthier than at any point in the past.⁹ We respectfully submit that this legislation’s attempt to address this alleged decline is consequently misguided.

We believe that this legislation would substantially weaken the ability of state regulators to protect retail investors. State securities regulators are the closest regulators to their local markets and thus have been particularly effective in protecting retail investors from fraudulent activity.¹⁰

First, the bill would preempt the authority of state securities regulators and state law enforcement agencies to pursue certain civil claims of securities fraud.¹¹ In addition to tying the hands of the regulators best suited to protecting retail investors, the preemptive language is vague and thus risks creating uncertain and inconsistent application. Securities fraud defendants will likely argue that it applies broadly to preempt *all* state civil enforcement authority over transactions involved exchange-listed companies’ securities.¹²

³ Letter from Joseph P. Borg, NASAA President and Alabama Securities Commission Director, to The Honorable Jeb Hensarling, Chairman, House Committee on Financial Services, et. al., 1 (April 6, 2018), <http://nasaa.cdn.s3.amazonaws.com/wp-content/uploads/2018/04/NASAA-Letter-to-Congress-Re-HR5037.pdf>.

⁴ H.R. 5037, 115th Cong., 2d Sess. (Feb. 15, 2018), <https://financialservices.house.gov/uploadedfiles/bills-115hr5037ih.pdf>.

⁵ H.R. 5037 § 2(6).

⁶ See Letter from Jeffrey P. Mahoney, General Counsel, Council of Institutional Investors, to The Honorable Bill Huizenga, Chairman, and The Honorable Carolyn B. Maloney, Ranking Member, Subcommittee on Capital Markets, Securities, and Investment, House Committee on Financial Services 2 (May 22, 2018) (“U.S. public capital markets are fundamentally healthy and remain the preferred choice for businesses to seek capital”), [https://www.cii.org/files/May%2022,%202018%20Letter%20to%20Capital%20Markets%20Subcommittee%20\(financial\).pdf](https://www.cii.org/files/May%2022,%202018%20Letter%20to%20Capital%20Markets%20Subcommittee%20(financial).pdf).

⁷ Cf. K. Jeremy Ko, Division of Economic and Risk Analysis, Securities and Exchange Commission, *Economics Note: Investor Confidence* 2 (October 2017) (discussing research indicating that higher levels of investment and participation in the stock market occur when investors perceive lower risk of exposure to theft and fraud), available at https://www.sec.gov/files/investor_confidence_noteOct2017.pdf.

⁸ Nasdaq, “Progress in Process, Update on Nasdaq’s Blueprint to Revitalize Capital Markets” 3 (May 2018), http://business.nasdaq.com/media/Revitalize%20Progress%20Report%20May%202018_Edits_tcm5044-61798.pdf.

⁹ See EY, “Looking Behind the Declining Number of Public Companies, An Analysis of Trends in US Capital Markets” 1, [http://www.ey.com/Publication/vwLUAssets/an-analysis-of-trends-in-the-us-capital-markets/\\$FILE/ey-an-analysis-of-trends-in-the-us-capital-markets.pdf](http://www.ey.com/Publication/vwLUAssets/an-analysis-of-trends-in-the-us-capital-markets/$FILE/ey-an-analysis-of-trends-in-the-us-capital-markets.pdf); see generally Letter from Jeffrey P. Mahoney at 2-3.

¹⁰ See Letter of William F. Galvin, Secretary of the Commonwealth, Commonwealth of Massachusetts, to The Honorable Elizabeth Warren, United States Senate 2 (March 23, 2018).

¹¹ H.R. 5037 §§ 21G(b) and (c)(1), 29(b) and (c)(2).

¹² See Letter from Joseph P. Borg at 1-2.

Second, the bill would likely have a chilling effect on state criminal prosecutions of securities fraud and lessen the deterrence effect of state criminal prosecutions. The bill would require state criminal securities fraud actions to comply with federal law “in all respects.”¹³ This vague language could be interpreted to require that state prosecutors follow federal procedural obligations, such as the federal rules of criminal procedure or federal rules of evidence, that differ from the laws and procedures of state courts.¹⁴ This could create substantial judicial inefficiency by shifting state criminal securities fraud cases into federal courts to be tried by federal prosecutors.¹⁵ By making it more difficult for state regulators to pursue securities fraud cases, the legislation would also risk increasing the amount of fraudulent activity. By increasing the amount of penalties and the probability of detection, state antifraud provisions deter improper conduct and encourage companies to provide full disclosure to investors.¹⁶

Third, this bill runs contrary to the policies and public statements of federal securities enforcement authorities. The Administration has expressed its intention to give states a *greater* role in policing the financial markets.¹⁷ Similarly, SEC Commissioner Jay Clayton recently acknowledged that state regulators play a critical role in protecting Main Street investors, especially in light of the emergence new trading vehicles like cryptocurrencies and initial coin offerings (ICOs).¹⁸ By curtailing state securities regulators’ civil enforcement authority and creating uncertainty as to when and how they may exercise their criminal enforcement authority, this legislation would conflict with federal enforcement priorities. Especially as the number of federal securities enforcement actions declines,¹⁹ this legislation would leave investors more vulnerable to fraud.

For the above reasons, CII believes that H.R. 5037, if enacted, would harm investors and U.S. capital markets.

Sincerely,



Brendan M. Tyler

¹³ H.R. 5037 §§ 21G(c)(2), 29(c)(2).

¹⁴ See Letter from Joseph P. Borg at 2.

¹⁵ See *id.* at 2, n.2 (noting that state courts are unlikely to be willing to suspend all state criminal laws and procedures and thus will refer cases to federal courts).

¹⁶ See *id.* at 2, n.3.

¹⁷ See Statement of Mick Mulvaney, Acting Director, Consumer Financial Protection Bureau (February 28, 2018) (“We’re going to be looking to state regulators and the states’ attorneys general for a lot more leadership when it comes to enforcement”), available at <https://www.c-span.org/video/?441853-4/consumer-financial-protection-bureau-acting-director-mick-mulvaney>.

¹⁸ See Chairman Jay Clayton, Statement on NASAA’s Announcement of Enforcement Sweep Targeting Fraudulent ICOs and Crypto-asset Investment Products (May 22, 2018), available at <https://www.sec.gov/news/public-statement/statement-nasaa-s-announcement-enforcement-sweep-targeting-fraudulent-icos-and>.

¹⁹ See Letter from Joseph P. Borg at 2, n.4 (reporting a 33% decline in new SEC enforcement actions against public companies from FY 2016 to FY 2017 and an 80% decline in SEC settlements over FY 2017).