Blogs
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Section 848 of the Financial Choice Act 2017: Unwise at any Speed (Part 3)

This series of posts examines 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. Section 848 of the pending Financial Choice Act 2017 would attempt to accelerate the process of obtaining exemptive orders by forcing the SEC to grant or deny an exemptive application within a fixed time frame. My first post discussed the current process of obtaining an exemptive order. This post examines a problem overlooked by proposed Section 848, perhaps due to the Committee's limited understanding of the exemptive process.

Shortcomings of Hearings

Recourse to a hearing before an SEC administrative law judge, typically in response to an objection to the proposed exemptive order, is not well suited to achieving a thorough and wise regulatory analysis of an exemptive application. The author has personally been involved in a number of SEC administrative hearings, including the money market fund amortized cost hearings in 1979-1980, the Narragansett Capital hearings in the mid-1980s, and the TIAA-CREF hearings from 1987 to 1989. Each of those hearings involved serious public policy questions—not questions of fact or of witness credibility—that were especially challenging for the SEC administrative law judge (ALJ). Where an aggrieved person (an "objector") requests a hearing in response to a notice of a proposed exemptive order, the SEC engages in a process of determining whether the objector has standing and has raised an issue that is germane to the proposed order. A petition from a person determined not to have standing is dismissed, as is a petition raising issues that are not germane to the exemptive order. These decisions are made by the SEC itself, not by the Division pursuant to delegated authority, and prevent the SEC, like any other adjudicative tribunal, from being tied up by frivolous requests from persons who are abusing the statutory process. Even if the SEC orders a matter be set down for a hearing, the Rules of Practice were designed to handle contested evidentiary proceedings, not broad questions of public policy. For example, in a hearing the Division of Investment Management is deemed to be a party and the applicant is deemed to be a party, which gives both of them procedural rights not enjoyed by the objector. The SEC administrative law judge may allow an objector to participate in the hearing, but this would be a matter of grace, not of right. Moreover, once the matter is set down for a hearing the Division assumes the role of the right honorable opposition and the applicant is left to defend its application against the protestor and the Division. While that may be the correct role for the applicant to assume, it puts the Division in a difficult position since it may or may not have any sympathy for the position(s) taken by the objector. As a result, a hearing may not result in vigorous advocacy of all sides of an issue. In any event, the arguments will be directed at an ALJ who is supposed to implement, not establish, broad SEC regulatory policies.

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