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May 7, 2018

The Honorable Jeb Hensarling
Chairman
House Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Maxine Waters
Ranking Member
House Committee on Financial Services
4340 O'Neil Federal Office Building
Washington, D.C. 20024

The Honorable Bill Huizenga
Chairman
House Committee on Financial Services,
Subcommittee on Capital Markets
Washington, D.C. 20515

The Honorable Carolyn Maloney
Ranking Member
House Committee on Financial Services,
Subcommittee on Capital Markets
Washington, D.C. 20515

RE: H.R. 5037

Dear Chairman Hensarling, Ranking Member Waters, Chairman Huizenga, and Ranking Member Maloney:

Please accept this letter expressing our concerns, from the perspective of New Jersey's chief law enforcement officer and the State's securities regulator, regarding H.R. 5037, the "Securities Fraud Act of 2018." This bill would limit our agency's ability to protect the people of New Jersey from securities fraud, removing longstanding state regulatory protections, oversight, and remedies, and could jeopardize the financial security and well-being of investors, including New Jersey families and retirees.

In New Jersey, the Bureau of Securities, within the Department of Law and Public Safety's Division of Consumer Affairs, is charged with regulating the securities industry and protecting investors from securities fraud. Each year, the Bureau responds to hundreds of complaints from New Jersey residents who have fallen victim to scams in the securities market. When Bureau investigations uncover misconduct, the Bureau works to recover investors' funds, to deprive wrong-doers of their illicit gains, and to ensure that they do not harm more New Jersey investors in the future.

If passed, H.R. 5037 would restrict the Bureau's ability to enforce our State's anti-fraud laws. In fact, the bill would deprive state securities regulators like the Bureau of authority they have wielded for more than 100 years to protect against market manipulation and fraud. Specifically, the bill would prevent state securities regulators from bringing enforcement actions with respect to issuers of securities listed on an exchange (the New York Stock Exchange, NASDAQ, etc.). This means that, had H.R. 5037 been the



law of the land, state regulators would have been unable to pursue major fraud cases such as *Enron*, *Worldcom*, *AIG*, *HealthSouth*, and *Qwest Communications*.

The current version of H.R. 5037 also raises questions about whether the New Jersey Bureau of Securities could continue to prosecute the kinds of fraud that impact small-scale investors each and every day. If read broadly, the bill could leave the Bureau powerless to enforce New Jersey laws against:

- A financial advisor “churning” listed securities in the account of a New Jersey senior citizen, resulting in the total loss of her life savings;
- A broker-dealer engaging in a “pump and dump” scheme to manipulate the shares of a listed security, selling the stock to New Jersey customers at inflated prices; or
- A broker-dealer recommending unsuitable-listed securities to a New Jersey investor with disabilities, resulting in the loss of funds intended to cover a lifetime of medical care.

New Jersey’s Bureau of Securities encounters cases like these on a regular basis and strives to enable our State’s residents to recover their savings when they fall victim to such frauds. The U.S. Securities and Exchange Commission cannot respond effectively to frauds like these on its own—unfortunately, these illicit acts are too common and too widespread. Preempting States’ traditional authority to regulate securities fraud therefore would leave New Jersey residents vulnerable to fraudsters who know that the federal government alone does not have the resources necessary to police their unlawful conduct.

Not only does H.R. 5037 prevent our Bureau of Securities from protecting New Jersey investors, it may also impede state prosecution of those whose schemes violate our criminal laws. The bill’s language about criminal prosecutions is ambiguous, but one thing is clear: the bill would create new hurdles that would make it harder for state prosecutors to do their jobs. We strongly oppose these restrictions on our authority to protect New Jersey and its residents from criminal fraud.

The North American Securities Administrators Association (“NASAA”)—the association of state and provincial securities regulators from the United States, Canada, and Mexico—recently informed you of its opposition to H.R. 5037. A copy of NASAA’s letter is enclosed for reference. We fully agree with NASAA’s conclusion that H.R. 5037 would be “bad for investors and bad for our capital markets,” and respectfully encourage you to read NASAA’s letter for more information about why state securities regulators uniformly oppose H.R. 5037.

Thank you for considering our views. Should you have any questions, please do not hesitate to contact us.

Sincerely,



Gurbir S. Grewal
Attorney General of New Jersey



Christopher W. Gerold
Chief, New Jersey Bureau of Securities



NASAA

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April 6, 2018

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Re: The Securities Fraud Act of 2018 (H.R. 5037)

Dear Chairman Hensarling, Ranking Member Waters, Chairman Huizenga and Ranking Member Maloney:

On behalf of the North American Securities Administrators Association (NASAA),¹ I write to express strong opposition to H.R. 5037, the "Securities Fraud Act of 2018," which was introduced in the House and referred to the Financial Services Committee in February. This proposed legislation would harm investors by preempting state securities regulators' civil anti-fraud authority and hampering – if not outright preempting – state criminal securities fraud prosecutions. The bill is an attempt to tie the hands of the regulators who are the "cops on the beat" and the closest to Main Street investors in favor of large companies engaged in or suspected of securities fraud. It is bad for investors and bad for our capital markets.

As a threshold matter, the putative findings in Section 2 of the bill are inaccurate or misleading. More deeply, though, H.R. 5037 is problematic because of the negative impact it would have on the ability of states to deter and punish securities fraud, which would undermine the integrity of our capital markets and the trust of investors.

First, the bill would preempt the authority of state securities regulators and state law enforcement agencies to pursue certain civil claims of securities fraud. The preemptive language is vague and securities fraud defendants will surely assert it applies broadly to preempt all state civil enforcement authority with respect to transactions involving the securities of exchange listed

¹ The oldest international organization devoted to investor protection, the North American Securities Administrators Association, Inc. was organized in 1919. Its membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico, Puerto Rico and the U.S. Virgin Islands. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

companies. Second, the bill would impose a requirement that state criminal securities fraud activities comply “in all respects” with federal law. This would have uncertain and potentially chilling implications, and could be interpreted to require, for example, that state prosecutors follow federal procedural obligations, such as the federal rules of criminal procedure or federal rules of evidence, or abide by other federal requirements that differ from the laws and procedures of state courts. Third, under the bill, defrauded investors, such as pension funds, would no longer have a choice of forum to pursue their claims against publicly traded companies as the bill would force them to bring their claims in federal court.² *Such policies are overwhelmingly against the interests of all law-abiding market participants.*

Enacting policies that would make it more difficult, and in some cases impossible, for state regulators – the regulators closest to the investing public and the “cops on the beat” – to hold accountable the most powerful companies serves no valid interest. State antifraud provisions deter improper conduct by companies and incentivize issuers to provide investors complete and accurate information.³ Moreover, while state regulators are judicious in exercising their enforcement authority against publicly traded companies, states’ authority to pursue enforcement activity against issuers of securities, and doing so independently when appropriate, is a major deterrent to fraud and one of many reasons investors have confidence in America’s capital markets.

Beyond the overarching backwardness of the policies prescribed by H.R. 5037, the enactment of which would be inadvisable at any juncture, NASAA questions the basis for Congress’s interest in curtailing state enforcement authorities at the present time. Indeed, given the recent and marked decline in enforcement actions by the SEC against public companies, this would appear to be the most inopportune time for Congress to tie the hands of states in policing fraud by publicly traded companies.⁴ The proposed legislation would shift policies in a direction diametrically opposed to those encouraged by the Trump Administration, which favors states’ rights, and encourages the exercise of state authority in regard to enforcement activity.⁵

Further, H.R. 5037 is premised on the specious assertion that state enforcement of laws prohibiting securities fraud is detrimental to the public interest and is in some way connected to

² As a prosecutorial agency, this is preemptive in that no state judge or judiciary panel will agree to suspend all state criminal laws and procedures. In essence, this is a directive to the state courts that these state cases must be referred to federal courts to be tried exclusively by federal prosecutors.

³ State antifraud provisions can both raise the amount of the penalty and, even more importantly, raise the probability of detection and prosecution of those companies that commit securities fraud.

⁴ According to an analysis published by New York University’s Pollack Center, new SEC enforcement actions against public companies decreased by 33% from FY 2016 to FY 2017. Likewise, SEC settlements declined by more than 80% over 2017, from \$1 billion in the first half of FY 2017 to \$196 million in the second half, and penalties during the second half of FY 2017 accounted for only 16% of total settlements for the fiscal year – the lowest percentage and dollar amount for any half year since FY 2010. (“SEC Enforcement Activity: Public Companies and Subsidiaries—Fiscal Year 2017 Update.” cornerstone.com/Publications/Reports/SEC-Enforcement-Activity-2017-Update).

⁵ See: Office of Management and Budget Director and Consumer Financial Protection Bureau Acting Director Mick Mulvaney remarks to the National Association of Attorneys General winter meeting. “We’re going to be looking to the state regulators and the states’ attorneys general for a lot more leadership when it comes to enforcement.” February 20, 2018. Available at c-span.org/video/?441853-4/consumer-financial-protection-bureau-acting-director-mick-mulvaney.

the “declining interest in the United States public market.”⁶ Such a premise is unsupported by logic or fact. As the U.S. Treasury Department recently reported, America’s capital markets are “the largest, deepest, and most vibrant in the world,” and U.S. businesses “successfully derive a larger portion of business financing from [America’s] capital markets, rather than the banking system, than most other advanced economies.”⁷ For more than two decades, bipartisan majorities in Congress have repeatedly recognized the importance of preserving robust state authority to protect investors from *both* civil and criminal fraud.⁸ The Financial Services Committee has, for the past five-and-a-half years, conducted rigorous oversight of the U.S. capital markets holding at least twenty hearings with dozens of witnesses. The Committee has also passed numerous capital formation bills all of which left untouched state antifraud authority in recognition of the important role this authority plays in maintaining confidence in U.S. markets.⁹

H.R. 5037 also takes the position that state enforcement authority should be curtailed by Congress as a consequence of its overlap with the federal enforcement function.¹⁰ Unfortunately, this premise is similarly misguided. In the realm of securities regulation, state and federal securities regulators often collaborate on a voluntary basis – usually at the regional level – with the common goals of sharing information and leveraging resources efficiently. However, because state securities regulators frequently prioritize the protection of retail investors, forcing states to take a backseat during investigations that involve publicly listed companies would put “mom and pop” investors more directly in harm’s way.

In summary, H.R. 5037 is a misguided and dangerous bill. It is premised on a flawed understanding of the importance of state securities enforcement functions in protecting “mom and pop” investors and deterring fraudulent conduct in our securities markets. In every instance, the

⁶ See: Section 2(6) of H.R. 5037, the “Securities Fraud Act of 2018”, as introduced on February 15, 2018.

⁷ U.S. Department of the Treasury, “A Financial System That Creates Economic Opportunities - Capital Markets,” p.4 (Oct. 2, 2017), available at [treasury.gov/press-center/press-releases/Documents/A-Financial-System-Capital-Markets-FINAL-FINAL.pdf](https://www.treasury.gov/press-center/press-releases/Documents/A-Financial-System-Capital-Markets-FINAL-FINAL.pdf).

⁸ See: Sections 102(a) and 102(b) of H.R. 1058, the Private Securities Litigation Reform Act of 1995, as enacted on December 22, 1995 (“PSLRA”); Section 102(a) of H.R. 3005, the National Securities Markets Improvement Act of 1996, as enacted on October 11, 1996 (“NSMIA”); and Sections 101(a) and 101(b) of S. 1260, the Securities Litigation Uniform Standards Act of 1998, as enacted on November 3, 1998 (“SLUSA”).

⁹ In addition to various hearings held pursuant to its mandate to oversee the U.S. Securities and Exchange Commission (“SEC”), the House Financial Services Committee and its Subcommittee on Capital Markets have held at least twenty hearings intended to examine capital formation in the U.S. equity markets under Chairman Hensarling. This includes at least eight hearings in the 113th Congress, seven in the 114th Congress, and five in the current 115th Congress, to date.

Furthermore, neither the SEC Advisory Committee on Small and Emerging Companies, which has held 17 meetings and issued 41 recommendations since January 1, 2013, nor the SEC Forum on Small Business Capital Formation, which has taken place annually and resulted in 113 recommendations since 2013, has ever considered the enforcement of state antifraud laws to be an obstacle to capital formation, much less the basis for recommendation to the SEC. On the contrary, both the Advisory Committee and the Forum have expressed their consideration of and recommendation against the preemption of state securities enforcement. (See: Recommendations Regarding the Regulation of Finders and Other Intermediaries in Small Business Capital Formation Transactions, at 4 (Sep. 23, 2015), available at [sec.gov/info/smallbus/acsec/acsec-recommendations-regulation-of-finders.pdf](https://www.sec.gov/info/smallbus/acsec/acsec-recommendations-regulation-of-finders.pdf); and Final Report on Small Business Capital Formation, at 12 (Nov. 21, 2013), available at [sec.gov/info/smallbus/gbfor32.pdf](https://www.sec.gov/info/smallbus/gbfor32.pdf)).

¹⁰ Section 2 of the bill asserts that state and federal statutes and enforcement responsibilities “overlap or contradict each other,” and expressing the view that “companies actively engaging in commerce across State lines and raising capital on national markets should be primarily regulated by the Federal Government’s uniform anti-fraud standard.”

bill places the interests of big companies above those of the hardworking Americans who look to our capital markets to help build a secure retirement. For all the foregoing reasons, NASAA opposes the bill, and strongly encourages the Committee to reject it.

Thank you for your time and consideration of NASAA's views. If I may be of any further assistance, please do not hesitate to contact me or Michael Canning, NASAA's Director of Policy and Government Affairs, at (202) 737-0900.

Sincerely,

A handwritten signature in black ink, appearing to read 'J.P. Borg', with a stylized flourish underneath.

Joseph P. Borg
NASAA President and Alabama Securities Commission Director