

Chairman Garrett's Opening Statement for SIPC Legislative Hearing

Washington, D.C. -- House Financial Services Capital Markets and Government Sponsored Enterprises Subcommittee Chairman Scott Garrett (R-NJ) delivered the following opening statement at today's subcommittee hearing on H.R. 3482, the Restoring Main Street Investor Protection and Confidence Act of 2013:



“Today’s hearing is to further examine legislation introduced by myself and Ranking Member Maloney entitled, “Restoring Main Street Investor Protection and Confidence Act.” I want to begin by directly recognizing and commending the esteemed lady from New York for all of her hard work and dedication to this bill and to this issue. It has been an honor and privilege to work closely with her on this very important issue. I also want to thank the panelists for coming, especially our two victims that have felt the full brunt of two of the largest financial frauds in our nation’s history.

“I also want to specifically thank all of my fellow members of the Committee and the broader Congress that have formally cosponsored the legislation we are discussing today. I think right now we are about one quarter of the committee on the bill, and I hope that number continues to rise as Members learn more about this subject.

“I also want to express my sincere thanks to Senators David Vitter and Chuck Schumer for introducing companion legislation in the U.S. Senate. Hopefully now with this bicameral support, it will aid in us coming to a more expedited resolution to this problem.

“I want to make it absolutely clear, I am not advocating for this legislation because I am trying to score any political points. I am supporting this legislation because I have studied the law, reviewed past precedent and analyzed the original congressional intent—and it is very clear to

me that SIPC and the Trustee are not applying the law as intended by Congress and they are not adhering to their own past precedent, which has been affirmed by the courts.

“And so, the purpose of this legislation today is to reaffirm the original intent of the law and to correct the misapplication of the law by SIPC and the Trustee. It is not some retroactive change of the law; it is a reaffirmation of it.

“SIPC now argues that it is nothing like FDIC insurance. Yet, back year ago, in President Nixon’s original signing statement of SIPA said, “Just as the Federal Deposit Insurance Corporation protects the user of banking services from the danger of bank failure, so will the Securities Investor Protection Corporation protect the user of investment services from the danger of brokerage firm failure.”

“In case that was not convincing enough, I also found this quote during the Senate deliberations of the SIPA legislation from its Senate author, Edmund Muskie, “Mr. President, since 1934, the United States has insured bank deposits under the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporation. These insurance programs protect bank depositors from loss of their savings because of bank failures. And the existence of this deposit insurance has become a source of confidence in the soundness of our savings institutions. S. 2348, the Security Investor Protection Act of 1970, would accomplish a similar purpose for securities investors by protecting them from losses because of the failure of their brokers.”

“If that wasn’t enough, Senator Harrison Williams from New Jersey, and then-Chairman of the Senate Securities Subcommittee stated the legislation “would establish a Federal Broker-dealer Insurance Corporation.” Granted it’s not the FDIC but FBDIC is pretty darn close to it.

“I have an email from 2009 from Mr. Harbeck to Congressional staff where in it you directly compare SIPC to FDIC. I will later insert this into the record.

“In Mr. Hammerman’s testimony, he suggests that SIPC was never intended to cover frauds and says the legislation will “introduce a new public policy objective for SIPA and SIPC – namely, insuring investors against the risk of loss due to securities fraud.”

“Yet, when going over the reasons for the legislation, Senator Muskie specifically said, “there remain some very basic problems within certain parts of the securities industry. There are problems of obsolete management techniques, careless business practices, inadequate self-regulation, and occasional fraudulent activities.” All of these account in some part for the industry’s financial difficulties today.

“And to add further clarification to this topic, the head of the New York Stock Exchange, Robert Haack, wrote to the SEC at the time to provide their analysis on the potential loss to a new SIPC fund. The letter stated, “I should make it clear, however, that no one can, in our opinion, make a realistic or useful evaluation of the potential dollar exposure to SIPC because there is no known way to measure the liability which might be faced in the event of broker-dealer failures. The fraud of Allied Crude Vegetable Oil against Ira Haupt & Co. for example, caused a loss of some \$27 million which could in no way be anticipated in advance.”

“In 1992, the Government Accountability Office (GAO) conducted a report on the operations of the program and said, “Within the last 6 years, 26 of the 39 SIPC liquidations have involved failures due to fraud.” They also stated in the report, “In essence, SIPC is a back-up line of protection to be called upon generally in the event of fraud or breakdown of the other regulatory protections.”

“With all that, I struggle to see how we are putting a new public policy objective of fraud protection on SIPC when the record is this long and this clear that protecting investors from fraud was a core function of the original statute and has been applied that way throughout its existence.

“Again, turning to Mr. Harbeck’s testimony, he suggests that following a final account statement to determine a customer’s net equity somehow legitimizes a Ponzi scheme. Yet, SIPC argued for—and the Second Circuit Court agreed to support—using the exact same methodology in the New Times Securities Ponzi scheme resolution in 2004. The New Times case is almost identical to the Madoff case.

“You see, time and time again, SIPC changes the rules and its story after the fact when it suits its own purposes. The clear truth from a long and exhaustive record make it clear that SIPC is an insurance program set up by Congress to protect investors and ensure the appropriate functioning of our nation’s securities markets, especially in the case of fraud.

“Regardless of your views about the original appropriateness of programs like these, it is our current duty as elected representatives to ensure the law is followed and administered as originally intended by Congress and that investors receive the protections they were promised.

“The legislation before us is designed to improve protections of securities investors, particularly the regular retail investor lacking professional expertise in the market.

“It is a direct outgrowth of stunning regulatory failures to detect and promptly respond to massive frauds and failures of SEC-registered broker-dealers—as in the Madoff, Stanford, or in the now McGinn-Smith case, which destroyed the principal savings of over 12,000 investors. The devastation of these losses has been compounded by the failure of SIPC to fulfill its obligations, as intended by Congress back in 1970.

“The provisions are commonsense reforms, specifically to:

- remove the inconsistencies in the application of SIPC coverage which has led to great investor confusion;
- assure that SIPA’s protective benefits go to the innocent customers;
- limit the exposure of taxpayers by establishing new accountability measures for SIPC’s borrowing authority;
- avoid over-technical legal interpretations at odds with SIPA’s remedial objectives and the original spirit and intent of the law;
- improve the fiduciary character of SIPA liquidations;

- strengthen the SEC’s plenary oversight of the SIPC; and
- and finally, direct the SEC and FINRA to give high priority to inspection procedures which verify and validate the accuracy and authenticity of information provided by broker-dealers to their customers.

“All of these proposed amendments seek to assure that SIPA is administered with constant attention to the perspective and the reasonable expectations of the broker-dealers customers—those whose confidence in market participation SIPA is intended to engender and maintain.

“Now, a point too often overlooked is that SIPA, while using many of established practices of the bankruptcy code, is unconditionally an amendment to the Federal securities laws meant to strengthen the efficient operation of our capital markets by maintaining the confidence of their retail users, the backbone of the system. Accordingly, the bill seeks for the future administration of SIPA to clarify that the securities law’s primacy shall have operative recognition.

“Mr. Harbeck, your written statement this morning further emboldens me in my determination to put SIPC back on the right course in carrying out SIPA’s grand objective of deploying its resources to help the financially-devastated innocent and unsophisticated victims of broker-dealer bankruptcy including fraud, such as those with us this morning, rather than” lawyering up” to see how narrowly it can interpret the law’s remedial objectives.

“It is your complete confidence that SIPC is performing as the Congress of 1970 intended that troubles me. I don’t doubt for a second that you believe with genuine conviction that SIPC’s actions are absolutely correct, not only in letter but also with the spirit of the law.

“I don’t question your integrity for a moment. But, I am deeply disturbed by your satisfaction with SIPC’s performance in these massive fraud cases which have, thankfully, captured the attention of Congress now with profound concern.

“Our bill seeks to reaffirm the original intent of Congress in the enactment of SIPA, to make reforms in its administration for the future, and above all else, to change the culture at SIPC to one that seeks to fulfill and not hinder SIPA’s remedial purposes.

“I know I thanked a lot of people, but this is not a thankful day, with all of the victims and their families still reeling from these frauds. I will, however, be thankful once SIPC is reformed and the original intent of Congress is reaffirmed.”

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