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THE VALIDITY OF SEC RULE 3b-9 WHICH REQUIRES BANKS TO REGISTER AS BROKER-DEALERS

The Securities and Exchange Act of 1934 ('34 Act)[1] requires persons doing business as brokers[2] or dealers[3] to register with the Securities and Exchange Commission (SEC).[4] In registering with the SEC, brokers and dealers disclose information that helps the SEC ensure that broker-dealers comply with all applicable securities laws.[5] Congress imposed the registration requirement on broker-dealers primarily to protect investors from unfair practices in securities transactions.[6] In passing the '34 Act, however, Congress

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1. Securities and Exchange Act of 1934 ('34 Act), 15 U.S.C. §§ 78a-78kk (1982).

2. *See* 15 U.S.C. § 78c(a)(4) (1982) (broker is person trading securities for accounts of others).

3. *See* 15 U.S.C. § 78c(a)(5) (1982) (dealer is person trading in securities for personal account). The definitions of "broker" and "dealer" comprehend only persons who trade securities as part of a regular business. N. WOLFSON, R. PHILIPS & T. RUSSO, REGULATION OF BROKERS, DEALERS & SECURITIES MARKETS § 1.04 (1977).

4. *See* 15 U.S.C. § 78o(a)(1) (1982) (prohibiting brokers and dealers from trading securities without registering with Securities and Exchange Commission (SEC)); 15 U.S.C. § 78d (1982) (statute establishing SEC to administer '34 Act). Under the '34 Act, brokers and dealers may not trade securities in interstate commerce unless they have registered with the SEC. *See* 15 U.S.C. § 78o(a)(1) (1982). Registered broker-dealers must conform to the applicable requirements of the '34 Act and all regulations that the SEC adopts pursuant to the '34 Act, including periodic reporting requirements, unreasonable commission prohibitions, and antimanipulation provisions. *See, e.g.*, 15 U.S.C. § 78o(d) (1982) (authorizing SEC to impose periodic reporting requirements on broker-dealers); 15 U.S.C. § 78o(b) (1982) (prohibiting unreasonable broker-dealer commissions); 15 U.S.C. § 78o(c)(1) (1982) (broker-dealer antimanipulation provision). *See generally* T. HAZEN, THE LAW OF SECURITIES REGULATION 232-37 (1985) (overview of broker-dealer registration requirement).

5. *See* S. JAFFE, BROKER-DEALERS AND SECURITIES MARKETS 15-17 (1977). To satisfy the broker-dealer registration requirement, a registrant must file with the SEC a statement that discloses the registrant's financial condition, organizational structure, securities operations, and other information that the SEC in its rulemaking capacity requires. *See* 15 U.S.C. § 78o(b)(1) (1982) (authorizing SEC to adopt rules for broker-dealer registration); *see also* 17 C.F.R. § 229.101 (1982) (listing specific information that SEC requires registering broker-dealers to disclose). *See generally* T. HAZEN, *supra* note 4, at 233 (overview of broker-dealer registration). The SEC uses the broker-dealer registration information to police broker-dealer activities. *See* S. JAFFE, *supra* at 17 (discussing consequences of broker-dealer registration with SEC).

6. *See* Blaise D'Antoni & Assoc., Inc. v. SEC, 290 F.2d 688, 689 (5th Cir. 1961) (Congress subjected brokers to scrutiny of SEC to further purpose of '34 Act to create fair market for investors); *see also* 15 U.S.C. § 78o (1982) (broker-dealer registration requirements); S. 2693, 73d Cong., 2d Sess. 2-4, 78 *Cong. Rec.* 2264-72 (1934), *reprinted in* 11 LEGISLATIVE HISTORY SECURITIES EXCHANGE ACT 1934, at Item 34 (1973) (broker-dealer registration is necessary to prevent abuses in securities transactions) [hereinafter cited as *Legislative History*]. Congress enacted the Securities and Exchange Act of 1934 to effect fair dissemination of trading information and to ensure that broker-dealers deal honestly with investors. *See* Radzanower v. Touche Ross & Co., 426 U.S. 148, 155 (1976) (purpose of '34 Act is to provide fair mechanism for pricing securities and to prevent undue advantage among investors trading securities); *see*

exempted banks[7] from the broker-dealer registration requirement.[8] Congress apparently determined that requiring banks to register as broker-dealers was unnecessary because the Glass-Steagall Act[9] prohibited banks from participating in most broker-dealer activities.[10] Nevertheless, the federal banking

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also Hughes v. SEC, 174 F.2d 969, 975 (D.C. Cir. 1949) (purpose of '34 Act is to prevent dishonesty in business of trading securities); H.R. REP. No. 1383, 73d Cong., 2d Sess. 2-3 (1934), *reprinted in* 5 LEGISLATIVE HISTORY, *supra*, at Item 18 (regulation of stock exchange is necessary to protect investing public). *See generally* T. HAZEN, *supra* note 4, at 6-8 (1985) (discussing fair play objectives of '34 Act). In promulgating the '34 Act, Congress intended to restore the investing public's confidence in America's financial markets after the stock market crash of 1929. *See* T. HAZEN, *supra* note 4, at 6 (historical context of '34 Act); *see also* Ianni, *"Security" Under The Glass-Steagall Act And The Federal Securities Acts of 1933 and 1934: The Direction of The Supreme Courts Analysis*, 100 BANK. L. J. 100, 103-04 (1983) (influence of stock market crash on enactment of '34 Act). Unlike the Securities Act of 1933 ('33 Act), which focuses on corporate distributions of securities, the '34 Act governs all aspects of securities transactions. *See* T. HAZEN, *supra* note 4, at 232 (observing comprehensive character of '34 Act).

7. *See* 15 U.S.C. § 78c(a)(6) (1982) (defining "bank" as national bank, Federal Reserve member bank, or state bank that receives deposits and has fiduciary duties similar to those of national bank).

8. *See* 15 U.S.C. § 78c(a)(4)-(5) (1982) (excluding banks from definitions of "broker" and "dealer"); *see also SEC Rule on Broker-Dealer Registration for Banks*, [Jul.-Dec.] SEC. REG. & REP. (BNA) No. 28, at 1269 (July 1, 1985) (noting total bank exemption from broker-dealer registration requirement prior to promulgation of rule 3b-9). Congress exempted banks from the broker-dealer registration requirement by imposing the requirement only on persons doing business as brokers or dealers and excluding banks from the definitions of "broker" and "dealer." *See* 15 U.S.C. § 78o (1982) (requiring persons doing business as brokers or dealers to register with SEC); 15 U.S.C. § 78c(a)(4)-(5) (1982) (excluding banks from definitions of broker and dealer). Since broker-dealer registration subjects persons to the broker-dealer regulations of the '34 Act, Congress exempted banks from the broker-dealer regulations of the '34 Act by exempting banks from the broker-dealer registration requirement. *See* Note, *Regulation of Bank Securities Activities*, 41 WASH. & LEE L. REV. 1187, 1190, n.13 (1983) (explaining how Congress exempted banks from broker-dealer regulations of '34 Act).

9. Glass-Steagall Act §§ 16, 20, 21, 32, 12 U.S.C. §§ 24, 377, 378(a), 78 (1982).

10. *See id.* (prohibiting banks from offering most brokerage services). Congress passed the Glass-Steagall Act in 1933 to erect a barrier between the banking business and the investment business. *See* Investment Co. Inst. v. Camp, 401 U.S. 617, 639 (1971) (bank engaging in mutual investment business violated Glass-Steagall Act); *see also* 77 CONG. REC. 3,835 (1933) (comment of Sen. Steagall who stated that purpose of Glass-Steagall Act is to steer banks back to business of banking); 75 CONG. REC. 9,912 (1932) (comment of Sen. Bulkey who stated necessity of keeping banks out of investment securities business). In enacting the Glass-Steagall Act, Congress determined that banks could not solicit securities accounts and simultaneously provide their customers the disinterested and cautious banking service needed to restore the public's confidence in banks after the bank of the United States collapsed in 1930. *Investment Co. Inst.*, 401 U.S. at 634; *see also Hearings Pursuant to S. Res. 71 before a Subcommittee of the Senate Committee on Banking and Currency*, 71st Cong., 3d Sess., 40 (1931) (attributing failure of Bank of United States in 1930 to securities activities with affiliates); *S. Rep. No. 77*, 73d Cong., 1st Sess. 6-10 (1933) (stock market decline damaged commercial banks due to their trading in and ownership of speculative securities). To combat the mischiefs inherent in banks handling securities accounts, Congress in drafting the Glass-Steagall Act prohibited banks from conducting brokerage services, dealing in securities, and underwriting or distributing stock issues. *See* Glass-Steagall Act §§ 16, 20, 21, 32, 12 U.S.C. §§ 24, 377, 378(a), 78 (1982) (prohibiting banks from offering brokerage services).

regulators[11] recently have interpreted the Glass-Steagall Act to permit banks to offer brokerage services almost identical to services offered by registered broker-dealers.[12]

To capitalize on the relaxed standards of the Glass-Steagall Act, banks have entered the securities brokerage business aggressively.[13] Congress, how-

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11. *See* Note, *supra* note 8, at 1190-91 n.16. The primary federal agencies responsible for regulating the banking industry in the United States are the Comptroller of the Currency (Comptroller), the Federal Reserve Board (Federal Reserve), and the Federal Deposit Insurance Corporation (FDIC). *Id.* The Comptroller regulates the federally chartered national banks. *See* 12 U.S.C. §§ 21-24, 26-27 (1982) (delineating authority and duties of Comptroller). The Federal Reserve regulates bank holding companies and state chartered banks belonging to the Federal Reserve System. *See* 12 U.S.C. §§ 1841-1850 (1982) (authority to govern bank holding companies); 12 U.S.C. §§ 321, 324-325 (1982) (Federal Reserve regulates state member banks). The FDIC regulates those state banks that are not members of the Federal Reserve System but have federal deposit insurance. *See* 12 U.S.C. §§ 1815, 1817 (1982).

12. *See SEC Rule, supra* note 8, at 1263. In 1982, the Comptroller permitted a national bank to form a broker-dealer subsidiary registered with the SEC. *See Decision of Comptroller of Currency Establishing an Operating Subsidiary to be Known as Security Pacific Discount Brokerage Services, Inc.*, [Rulings-Decisions] FED. BANKING L. REP. (CCH) 99,284 (AUG. 26, 1982). The following year, the Federal Reserve approved an application from the BankAmerica Corporation, a bank holding company, to acquire a discount brokerage firm. *See Order of the Federal Reserve System Approving the Acquisition of Charles Schwab & Co. by BankAmerica Corporation*, 69 Fed. Res. Bull. 105 (1983). The United States District Court for the District of Columbia upheld the Federal Reserve's approval of BankAmerica's application in *Securities Indus. Ass'n v. Comptroller of the Currency. See* Securities Indus. Ass'n v. Comptroller of the Currency, 577 F. Supp. 252, 256 (D.D.C. 1983) (Glass-Steagall does not prohibit banks from owning brokerage firms as subsidiaries). Soon after granting BankAmerica permission to purchase a discount brokerage firm, the Federal Reserve promulgated a rule permitting bank holding companies to enter the discount brokerage and securities credit lending business. *See* 12 C.F.R. § 225.25(b)(15) (1985) (amendment to make discount securities brokerage and securities credit lending permissible activities for bank holding companies). In addition, the FDIC has indicated that insured nonmember banks may establish subsidiaries to deal in and underwrite securities and even to conduct brokerage business internally. *See* General Counsel's Opinion No. 6 - The Legality of Discount Brokerage Services When Offered By Insured Nonmember Banks, 48 Fed. Reg. 22,989 (1983). The question whether current banking practices in brokerage activities violate the Glass-Steagall Act, nevertheless, remains unanswered. *See* Note, *A Banker's Adventures in Brokerland: Looking Through Glass-Steagall at Discount Brokerage Services*, 81 Mich. L. Rev. 1498, 1500-01 (1983) (practice of banks doing brokerage business implicates Glass-Steagall Act); *see also* Pitt & Williams, *The Glass-Steagall Act: Key Issues for the Financial Services Industry*, 11 Sec. Reg. L. J. 234, 237 (1983) (Glass-Steagall barrier between investment banking and commercial banking); *supra* note 8 and accompanying text (background of Glass-Steagall Act).

13. *See SEC Rule, supra* note 8, at 1262-63. In 1984, the American Bankers Association (ABA) estimated that more than 1000 banks in the United States currently engage in securities activities. *Id.* In some cases, bank employees take securities investment orders from customers and forward the orders to nonbank brokers who process the orders. *See SEC Rule, supra* note 8, at 1262. Under this system, the bank typically shares the commission with the broker executing the trade. *Id.* In addition, banks currently aim aggressive promotional campaigns at existing and even prospective customers to solicit brokerage business that the banks, in some cases, handle internally. *Id.* Thus, rather than merely providing traditional accommodation services to existing customers, banks frequently offer services indistinguishable from broker-dealer services and receive transaction-related compensation. *Id.; see Banks May Execute*

ever, did not equip the banking regulators with statutes designed to protect investors trading securities through banks.[14] Rather, Congress designed the banking regulations to restore financial stability to the banking industry after the collapse of the Bank of the United States in 1930.[15] Consequently, a void in investor protection developed as banks entered the brokerage business because the '34 Act, although regulating persons doing brokerage business, exempted banks from the broker-dealer regulations.[16] To fill the new void in

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Customers' Instructions to Buy and Sell Shares in Tax-Exempt Mutual Funds [Current Transfer Binder] FED. BANKING L. REP. (CCH) 85,502 (Mar. 8, 1985) (letter from Peter Liebesman, Legal Advisor, Services Division of the Comptroller, noting similarity of bank brokerage activities to activities of traditional broker).

14. *See* Ianni, *supra* note 6, at 103-05 & 121-23 (discussing different orientations of federal law regulating banks and federal law regulating securities industry). Congress designed the federal securities regulations to provide investors with complete, material information in the securities market and to protect investors from fraud in securities transactions. *See supra* notes 1-5 and accompanying text (orientation of federal securities regulation). In contrast, Congress designed the banking laws to prohibit banks from becoming unduly risky enterprises and to minimize the conflicts of interest inherent in banks doing brokerage business. *See* Ianni, *supra* note 8, at 103-05.

In accordance with the different orientations of federal banking law and federal securities law, the securities regulations address specific problems that the banking regulations do not address. *See id.* at 103-105 & 121-123. For example, broker-dealers must pass qualifying examinations to satisfy minimum competency standards. *See* 15 U.S.C. §§ 78c(a)(4)-(5) & § 78o(b)(7) (1982) (broker-dealers must meet competency standards promulgated by SEC); *see also* NASD MANUAL (CCH) 1102A, at 1052-1055 (National Association of Securities Dealers (NASD) by-law requiring broker-dealers to pass qualifying test); 2 N.Y.S.E. Guide (CCH) 2304 (1983) (New York Stock Exchange (NYSE) rule 304a requires members of NYSE to meet qualifying standards). In contrast, federal banking regulations provide no mechanisms to insure the competency of bank employees executing securities trades. *See* Note, *supra* note 8, at 1195-96. Moreover, unlike federal securities regulations, federal banking laws do not require persons doing business as brokers to supervise employees handling securities transactions for customer accounts. *See* 15 U.S.C. § 78o(b)(4)(E) (1982) ('34 Act requirement that broker-dealers supervise personnel). Also unlike securities regulations, banking regulations do not impose advertising and recordkeeping requirements on persons doing brokerage business. *See, e.g.*, 17 C.F.R. § 240.15b10-6 (broker must maintain records of customer accounts and all transactions); AMER. STOCK EX. GUIDE (CCH) 9490, at 2683 (1983) (advertisements must reflect legitimate business character); 2 *N.Y.S.E. Guide* (CCH) 2472 (1983) (prohibiting misleading advertising by broker-dealers). Finally, federal banking regulations, unlike securities regulations, do not address the need for persons conducting brokerage business to tailor investment recommendations to customers' investment objectives. *See* 17 C.F.R. § 240.15b10-3 (1983) (broker-dealers advising customers must recommend only suitable investments); *see also* NASD MANUAL (CCH) 2152, at 2051 (1983) (requiring brokers to recommend investments suitable to customers' particular needs). *See generally* Note, *supra* note 8, at 1191-97 (overview of differences between bank and broker-dealer regulation respecting brokerage services).

15. *See* Ianni, *supra* note 8, at 103-05 (purpose of federal banking regulations is to make banks safe financially); *supra* note 10 (purpose of Glass-Steagall Act was to stabilize banking industry after collapse of Bank of United States).

16. *See SEC Rule, supra* note 8, at 1264 (SEC's determination that increase in bank securities activities created deficiency in federal protection of investors trading securities); *see also supra* note 14 and accompanying text (comparing banking regulation to securities regulation).

federal protection of securities investors, the SEC recently adopted rule 3b-9 which requires banks doing brokerage business to register as broker-dealers with the SEC.[17]

Under rule 3b-9, a bank must register as a broker-dealer if the bank publicly solicits brokerage business,[18] gives investment advice for compensation,[19] or deals in or underwrites securities.[20] Significantly, rule 3b-9 applies

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17. *See* 17 C.F.R. § 240.3b-9 (1985) (banks doing brokerage business must register as broker-dealers with SEC); *see also SEC Rule, supra* note 8, at 1264 (purpose of rule 3b-9 is to fill void in securities regulation caused by banks handling securities transactions not subject to securities regulation). In adopting rule 3b-9, the SEC endorsed the "regulation by function" approach to securities regulation. *See SEC Rule, supra* note 8, at 1264 n.19 (adopting regulation by function theory of securities regulation); *see also Securities Activities of Depository Institutions: Hearings on S. 1220 Before the Subcommittee on Securities of the Senate Committee on Banking, Housing, and Urban Affairs,* 97th Cong., 2d Sess. 25 (1982) (statement of John S. R. Shad, Chairman, SEC, endorsing regulation by function approach to securities regulation). The regulation by function approach focuses on the character of the securities activities being conducted and ignores the outmoded industry classifications of bank and broker-dealer which became blurred as banks entered the brokerage business. *SEC Rule, supra* note 8, at 1264 n.19. Applying the regulation by function approach to banks doing brokerage business, the SEC, in adopting rule 3b-9, determined that the investor protection purpose of the '34 Act required applying the coordinated system of federal securities regulation to bank brokerage activities. *SEC Rule, supra* note 8, at 1264.

18. *See* 17 C.F.R. § 240.3b-9(a)(1) (1985) (public solicitation prong of rule 3b-9). The public solicitation prong of rule 3b-9 applies only to banks that promote internal brokerage services. *SEC Rule, supra* note 8, 1265. For example, rule 3b-9 applies to banks that advertise the availability of their brokerage services in a newspaper or send their customers literature promoting self-directed individual retirement accounts. *Id.* The public solicitation prong of rule 3b-9 does not apply, though, to banks promoting the brokerage services of nonbank registered broker-dealers as an accommodation to bank customers. *Id.* Therefore, the public solicitation prong of rule 3b-9 will not disturb "networking" arrangements, which are contractual agreements between banks and independent broker-dealers in which the broker-dealers execute trades for the accounts of bank customers. Furthermore, the public solicitation prong of rule 3b-9 will not affect banks that incorporate or acquire subsidiaries to provide brokerage services on the banks' behalf for bank customers. *Id.* Accordingly, banks that participate in networking arrangements or provide brokerage services through subsidiaries may advertise aggressively without activating the public solicitation prong of rule 3b-9. *Id.*

19. *See* 17 C.F.R. § 240.3b-9(a)(2) (1985) (transaction-related compensation prong of rule 3b-9). Banks traditionally have provided investment advice for individual and trust accounts at the request of customers as an accommodation to existing customers. Kurucza, *Brokerage Activities and Investment Banking,* INST. ON SEC. REG. 341 (1984). In providing investment advice, banks have not profited directly but, rather, have billed customers at cost. *Id.* Although rule 3b-9 will not disturb the customary arrangement, the transaction-related compensation prong will impose the registration requirement on banks that charge customers a fee in excess of the cost of executing a trade or the cost of giving investment advice. *SEC Rule, supra* note 8, at 1266-67.

20. *See* C.F.R. § 240.3b-9(a)(3) (1985) ("dealing in and underwriting" prong of rule 3b-9). The Glass-Steagall Act prohibits banks from dealing in and underwriting securities. 12 U.S.C. § 378 (1982). The "dealing in and underwriting" prong of rule 3b-9, however, applies to dealing and underwriting activities as defined in the '33 and '34 Acts, respectively. The meanings of the terms "dealing" and "underwriting" in the '33 and '34 Acts may differ from the meanings of "dealing" and "underwriting" in the Glass-Steagall Act. *SEC Rule, supra* note 12, at 1268-70; *see also* 15 U.S.C. § 77b(11) (1982) (definition of "underwriter" in '33 Act); 15

only to banks conducting brokerage operations internally.[21] Therefore, banks wishing to do brokerage business may avoid the broker-dealer registration requirement by handling customer accounts through affiliates or subsidiaries registered as broker-dealers.[22]

Regardless of whether banks conduct brokerage business internally or through affiliates or subsidiaries, however, rule 3b-9 will cost banks money. For example, banks choosing to conduct brokerage activities internally will incur the administrative costs of registering with the SEC pursuant to rule 3b-9, complying with the periodic reporting requirements of the '34 Act, and retaining counsel for securities law advice.[23] Furthermore, banks handling customer accounts through affiliates registered as broker-dealers must forfeit the affiliates' share of brokerage commissions.[24] Moreover, banks that establish registered subsidiaries to provide brokerage services may incur legal fees in incorporating or acquiring subsidiaries and also may bear administrative expenses in registering those subsidiaries as broker-dealers pursuant to the '34 Act.[25]

Objecting to the impending SEC regulation, diminished brokerage revenues, and increased costs, the American Bankers Association (ABA) petitioned the United States District Court for the District of Columbia to set aside rule 3b-9.[26] In *American Bankers Association v. SEC*,[27] the ABA

U.S.C. § 77c(a)(5) (1982) (dealer is person buying and selling stock for his own account); 12 U.S.C. § 378 (1982) (Glass-Steagall Act's prohibition against banks dealing in or underwriting securities).

21. *SEC Rule, supra* note 8, at 1265.

22. *See SEC Rule, supra* note 8, at 1265-66 (rule 3b-9 does not apply to banks involved in networking arrangements or banks handling customer accounts through subsidiaries registered as broker-dealers); *see also supra* note 18 (noting networking and subsidiary approaches for banks wishing to do brokerage business).

23. *See* 17 C.F.R. § 240.3b-9 (1985) (requiring banks conducting brokerage business to register as broker-dealers with SEC); *see also supra* notes 4-5 and accompanying text (describing basic regulatory scheme for persons registered as broker-dealers); note 14 and accompanying text (noting examples of broker-dealer regulations which did not apply to banks doing brokerage business prior to rule 3b-9).

24. *See SEC Rule, supra* note 8, at 1265-66 (banks handling customer accounts through affiliates will sacrifice affiliates' share of brokerage commissions); *see also ABA Sues SEC to Block Commission Rule to Require Broker-Dealer Registration*, [July-Dec.] SEC. REG. & L. REP. (BNA) No. 32, at 1445 (Aug. 9, 1985) (rule 3b-9 discourages banks from handling brokerage accounts internally and, consequently, deprives banks of brokerage income that banks must share with affiliates).

25. *See SEC Rule, supra* note 8, at 1265-66 (bank subsidiary doing brokerage business must register as broker-dealer with SEC); *see also supra* notes 4, 5, & 14 and accompanying text (overview of regulatory scheme for persons registered as broker-dealers and examples of broker-dealer regulations).

26. *See* American Bankers Ass'n (ABA) v. SEC, [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1916 (D.D.C. Oct. 30, 1985). In *American Bankers*, the National Council of Savings Institutions (Savings Council) joined the ABA's suit against the SEC. *See Savings Council Joins Suit to Stop Bank Registration under SEC Rule 3b-9*, [July-Dec.] SEC. REG. & L. REP. (BNA) No. 41, at 1839. The Savings Council, a trade organization comprised of almost 600 savings institutions, represented the interests of state and federally chartered savings banks. *Savings Council, supra*, at 1839-40.

27. [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1916.

challenged the SEC's power to regulate banks.[28] Noting that the '34 Act specifically exempted banks from the broker-dealer registration requirement,[29] the ABA contended that Congress reserved the right to determine whether to impose the registration requirement on banks.[30] The SEC contested the ABA's claim by citing the provision "unless the context otherwise requires,"[31] which qualifies the definition of the term "bank" in the '34 Act.[32] The SEC argued that the "context" clause provided a statutory basis for excluding banks engaged in brokerage activities from the definition of "bank" and, consequently, from the bank registration exemption.[33]

In considering whether the SEC had power to impose the broker-dealer registration requirement on banks, the district court in American *Bankers* stated that the meaning of the context clause qualifying the bank exemption was unclear.[34] The district court explained that the language of the context clause was general and that the relevant legislative history did not indicate Congress' intent in drafting the clause.[35] Noting section 3(b) of the '34 Act which authorizes the SEC to define terms in administering the Act,[36] however, the district court found that the SEC properly could narrow the bank exemption by redefining the term "bank" as long as narrowing the exemption

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28. *See American Bankers,* [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1916 (ABA challenging SEC's power to regulate banks).

29. *See American Bankers,* [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1917 (ABA noting bank exemption from '34 Act); *see also* 15 U.S.C. § 78c(4)-(5) (1982) (definitions of "broker" and "dealer" excluding banks); *supra* note 8 (explanation of Congress' drafting technique for exempting banks from '34 Act).

30. *See American Bankers,* [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1917. In *American Bankers,* the ABA noted that in 1975, Congress, observing increased bank securities activity, directed the SEC to conduct a study to determine whether the bank exemption from the '34 Act and to report back the findings. *Id.; see also* STAFF OF SENATE COMM. ON BANKING, HOUSING AND URBAN AFFAIRS, 96TH CONG. 1ST SESS. REPORT ON BANK SECURITIES ACTIVITIES, 291-92 (Comm. Print 1977) (SEC recommended that limited bank securities activities in 1977 did not justify subjecting banks to federal securities regulations). The ABA argued that Congress' directive to the SEC to "report back" demonstrates that Congress intended to reserve the authority to impose SEC regulations on banks. *American Bankers,* [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1917.

31. 15 U.S.C. § 78c (1982).

32. *See American Bankers,* [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1917 (indicating SEC's construction of context clause); *see also* 15 U.S.C. § 78c (1985) (context clause qualifies definitional section in '34 Act).

33. *See American Bankers,* [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1917 (SEC argument that recent proliferation of banks doing brokerage business is context requiring SEC to regulate bank securities activities); *see also supra* note 13 and accompanying text (more than 1000 banks participate in brokerage activities); *infra* notes 129-30 and accompanying text (explaining how SEC used context clause as statutory basis for adopting rule 3b-9).

34. *American Bankers,* [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1917.

35. *American Bankers,* [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1917. *But see infra* notes 76-85 and accompanying text (analysis of legislative history suggesting that context clause did not authorize SEC to adopt rule 3b-9).

36. *See* 15 U.S.C. § 78c(b) (1982) (empowering SEC to define terms used in '34 Act).

was rational and consistent with the purposes of the '34 Act.[37] Accordingly, the district court deferred to the SEC's judgment and upheld rule 3b-9.[38]

Aside from American *Bankers,* authority relevant to the SEC's power to require banks to register as broker-dealers is inconclusive. Congress' express exemption of banks from the broker-dealer regulations of the '34 Act suggests that the SEC acted beyond its power in adopting rule 3b-9.[39] Arguably, if Congress had intended the SEC to regulate banks, Congress would not have exempted banks from the broker-dealer registration requirement.[40] In enacting the '34 Act, however, Congress incorporated section 3(b) which authorizes the SEC to define terms used in the '34 Act.[41] In adopting rule 3b-9, the SEC interpreted section 3(b) as authority to impose the broker-dealer registration requirement on banks by redefining the word "bank," a term that Congress had defined in section 3(a)(6) of the '34 Act.[42]

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37. *American Bankers,* [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1917. In *American Bankers,* the district court refused to consider policy arguments in its determination of the SEC's authority to adopt rule 3b-9. *Id.* Instead, the district court deferred to the policy determinations that the SEC made in adopting rule 3b-9. *See id.* (district court deferring to SEC's policy judgment to adopt rule 3b-9); *see also infra* notes 43-64 and accompanying text (discussing standard of judicial review for agency statutory interpretations).

38. *See American Bankers,* [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1917. Although granting the SEC's summary judgment motion, the district court in *American Bankers* noted that the merits of the case warranted expedited appeal. *Id.* The United States Court of Appeals for the District of Columbia Circuit, however, subsequently rejected the ABA's bid for expedited review. *See* American Bankers Ass'n v. SEC, in *ABA Denied Expedited Review of Appeal over SEC Bank Registration Rule 3b-9* [July-Dec.] SEC. REG. & L. REP. (BNA) No. 46, at 2039 (D.C. Cir. Nov. 18, 1985).

39. *See* 15 U.S.C. § 78c (4)-(5) (1982) (definitions of "broker" and "dealer" specifically excluding banks); *see also* C. SANDS, J. SUTHERLAND STATUTORY CONSTRUCTION § 47.14, at 94 (4th ed. 1984) (suggesting that legislature's specific language typically should control general language); 15 U.S.C. § 78c (context clause qualifies definition of "bank" in '34 Act); *supra* note 8 and accompanying text (explaining how Congress exempted banks from broker-dealer regulations of '34 Act by excluding banks from definitions of "broker" and "dealer"). Whether a specific provision of a statute applies instead of a general qualifying provision is a matter of judgment in each instance. *See* C. SANDS, *supra,* at 94. Allowing general qualifying language in a statute to control a specific provision, however, creates the risk of giving a statute wider operation than Congress intended. *Id.*

40. *See* 15 U.S.C. § 78c (4)-(5) (1982) (excluding banks from definitions of "broker" and "dealer"); *see also supra* note 8 and accompanying text (explaining how Congress exempted banks from broker-dealer regulations of '34 Act by excluding banks from definitions of "broker" and "dealer"). Under *casus omissus,* a canon of statutory construction, if the legislature did not address the disputed idea, the reader should not supply the idea. F. R. DICKERSON, THE INTERPRETATION AND APPLICATION OF STATUTES 236 (1975). Although *casus omissus* seems to preclude an interpretation of the '34 Act that ignores Congress' specific exemption of banks, the canon has become more of a political principle than a rule and, at most, raises a mere presumption. *Id.*

41. *See* 15 U.S.C. § 78c(b) (1982) (authorizing SEC to define terms to effectuate purposes of '34 Act); *see also* S. REP. No. 70, 94th Cong., 1st Sess. 94 (1975) (Congress intended SEC to have broad authority to define terms employed in '34 Act, whether or not already defined in '34 Act).

42. *See SEC Rule, supra* note 8, at 1271 (noting SEC's reliance on section 78c(b) of '34

Courts normally refuse to second-guess an administrative ruling when it appears that the agency has interpreted the organic statute rationally.[43] For example, the United States Supreme Court in *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc. (NRDC)*[44] emphasized the broad discretion of the Environmental Protection Agency (EPA) to interpret statutory language that Congress has left unclear.[45] In *Chevron,* the EPA promulgated a regulation that permitted industrial plants containing several pollution-emitting devices to install one additional pollution-emitting device without obtaining additional building and operating permits.[46] In adopting the regulation, the EPA relied upon the provision in the Clean Air Act that authorizes the EPA to establish a permit program regulating "new or modified major stationary sources."[47]

Act as authority to redefine Congress' definition of "bank"); *see also* 17 C.F.R. § 240.3b-9 (1985) (requiring banks doing brokerage business to register as broker-dealers). Since the '34 Act requires all persons doing business as broker-dealers to register with the SEC, and since Congress exempted banks from the broker-dealer registration requirement by excluding banks from the definitions of "broker" and "dealer," rule 3b-9 imposes the broker-dealer registration requirement on banks doing brokerage business by excluding banks doing brokerage business from Congress' definition of "bank." *See* 15 U.S.C. § 78o (1982) (requiring persons doing business as brokers or dealers to register with SEC); *see also* 17 C.F.R. § 240.3b-9 (1985) (excluding banks doing brokerage business from definition of "bank"); 15 U.S.C. § 78c(4)-(5) (1982) (excluding banks from definitions of "broker" and "dealer").

43. *See, e.g.,* Blum v. Bacon, 457 U.S. 132, 141 (1982) (interpretation by agency charged with administering statute deserves substantial deference); Federal Election Comm. v. Democratic Senatorial Campaign Comm., 454 U.S. 27, 42-43 (1981) (notwithstanding contrary interpretation by court of appeals, Supreme Court deferred to Federal Election Commission's interpretation that provision of Federal Election Campaign Act permitted particular campaign contributions); NLRB v. Hearst Publications, Inc., 322 U.S. 111, 131 (1944) (deferring to National Labor Relations Board's interpretation that newsboys were "employees" under National Labor Relations Act); *see also infra* notes 44-51 and accompanying text (court may not substitute its interpretation of ambiguous statute for reasonable interpretations of agency).

44. 104 S.Ct. 2778 (1984).

45. *See id.* at 2781-83 (court may not substitute its interpretation of ambiguous statute for reasonable interpretation of agency).

46. NRDC v. Gorsuch, 685 F.2d 718, 723-24 (D.C. Cir. 1982), *rev'd,* Chevron, U.S.A., Inc. v. NRDC, 104 S.Ct. 2778 (1984); *see also* 40 C.F.R. § 51.18(j)(1)(i)-(ii) (1985) (Environmental Protection Agency's (EPA) regulation relaxing permit requirement of Clean Air Act). The Clean Air Act requires states that have not achieved national air quality standard, or nonattainment states, to impose a permit program on industrial companies installing new or modified pollution-emitting equipment. 42 U.S.C. § 7502(b)(6) (1985). Under the Clean Air Act, nonattainment states typically may not issue permits unless the companies meet stringent air quality standards. *See id.* at § 7503 (prerequisites for obtaining equipment installation permit in Clean Air Act).

47. *Gorsuch,* 685 F.2d at 720. In *Chevron,* the EPA relaxed the permit requirement by defining "stationary source," at term that Congress had incorporated into the Clean Air Act. *Id.; see also* 42 U.S.C. § 7502(b)(6) (1985) (provision of Clean Air Act requiring permits for construction or operation of "stationary sources"); 40 C.F.R. § 51.18(j)(1)(i)-(ii) (1985) (EPA's definition of "stationary source"). In enacting the Clean Air Act, however, Congress had not defined the word "stationary source." *Gorsuch,* 768 F.2d at 720-22; *see also* 42 U.S.C. § 7502(b)(6) (1985) (requiring permits for construction or operation of "stationary sources").

Rejecting a petition by the NRDC to set aside the EPA's regulation,[48] the Supreme Court in *Chevron* stated that when Congress expresses itself ambiguously or remains silent on an issue in drafting a statute, a reviewing court should not substitute its interpretation of the statute for the agency's interpretation unless the agency's interpretation clearly contradicts the purposes of the statute.[49] The *Chevron* Court determined that the EPA's interpretation of the term "stationary source" as including pollution-emitting equipment did not contradict the Clean Air Act.[50] Accordingly, the Supreme Court in *Chevron* upheld the EPA regulation that relaxed the permit requirement.[51]

Although concerned particularly with the EPA's power to adopt a rule relaxing Congress' permit program, the *Chevron* decision reflects the prevailing view that courts owe a high degree of deference to an agency's interpretation of a statute.[52] Thus, *Chevron* is support for judicial deference to the SEC's interpretation of section 3(b) as authority to redefine Congress' definition of "bank" in the '34 Act.[53] Under the analysis suggested by

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48. *See Chevron,* 104 S.Ct. at 2778 (rejecting Natural Resources Defense Council's (NRDC) petition to set aside EPA regulation that relaxed permit requirement). In *Chevron,* the NRDC appealed the EPA's order to implement the EPA regulation to the United States Court of Appeals for the District of Columbia Circuit. *Gorsuch,* 768 F.2d at 719-20. The NRDC noted that Congress intended the permit program of the Clean Air Act to improve existing air quality. *Gorsuch,* 768 F.2d at 719-20. The NRDC argued that the EPA's interpretation of "stationary source" to relax the permit requirement was contrary to Congress' intent and, therefore, was invalid. *Gorsuch,* 768 F.2d at 719-20.

The District of Columbia Circuit Court determined that the Clean Air Act did not indicate what Congress had perceived as "stationary source," that the legislative history did not address the issue, and that only the purposes of the permit program suggested Congress' intended meaning of "stationary sources." *Id.* at 725-28. The District of Columbia Circuit concluded that the EPA's interpretation of "stationary sources," which relaxed the requirements of the permit program, was inconsistent with Congress' purpose to improve air quality in nonattainment states. *Id.* Accordingly, the District of Columbia Circuit invalidated the EPA's regulation. *Id.*

49. *Chevron,* 104 S.Ct. at 2778. The United States Supreme Court in *Chevron* reasoned that by leaving gaps in regulatory statutes, Congress explicitly or implicitly vests authority in agencies to interpret the statutes in adopting specific rules. *Id.* at 2782. The Court stated that agencies administering statutes necessarily face policy decisions in filling gaps that Congress has left in the statutes. *Id.* The Court noted that agencies, unlike federal courts, must answer to constituencies. *Id.* at 2793. The *Chevron* Court concluded that when an agency, in interpreting a statute, has made a reasonable policy choice, federal judges must respect the agency's interpretation. *Id.* at 2793-94.

50. *Id.* at 2793-94. The *Chevron* Court determined that Congress intended the permit program to reconcile the policy of air quality improvement with the policy of economic growth. *Id.* at 2792-94. Finding that the EPA's regulation relaxing the permit program encouraged economic growth without threatening air quality, the Supreme Court upheld the regulation. *Id.*

51. *Id.* at 2781.

52. *See id.* at 2782 (court may not substitute its interpretation of ambiguous statute for reasonable interpretation of agency); *see also supra* note 43 (examples of Supreme Court deferring to statutory interpretations of various administrative agencies).

53. *See Chevron,* 104 S.Ct. at 2782 (court may not substitute its interpretation of ambiguous statute for reasonable interpretation of agency); *see also* SEC v. Paro, 468 F. Supp. 635, 643 (N.D.N.Y. 1979) (deferring to SEC's interpretation of "investment contract" because

Chevron, the only question for the judiciary is whether the SEC's interpretation of section 3(b) was reasonable.[54]

The decision of the United States Court of Appeals for the District of Columbia Circuit in *FAIC Securities, Inc. v. United States*[55] implies that the SEC's interpretation of section 3(b) as authority to redefine Congress' definition of "bank" was not reasonable.[56] In *FAIC Securities,* the Federal Deposit Insurance Corporation (FDIC) promulgated a regulation that reduced the existing insurance coverage on funds deposited by deposit brokers.[57] In adopting the regulation, the FDIC interpreted a provision in the Federal Deposit Insurance Act (FDIA)[58] as authority to redefine "amount due to any depositor,"[59] a term that Congress had defined in the FDIA.[60] In considering whether the FDIC had authority to reduce the insurance coverage,[61] the District of Columbia Circuit acknowledged the legitimacy of the

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SEC's interpretation did not contradict language, purpose, or history of '34 Act); Lockheed Aircraft Corp. v. Campbell, 110 F. Supp. 282, 284 (S.D. Cal. 1953) (upholding SEC's definition of word "officer," used but not defined in '34 Act, as valid exercise of SEC's power under section 78c(b) to define terms). *But cf.* SEC v. Sloan, 436 U.S. 103, 111-12 (1978) (rejecting as illogical SEC's interpretation of section 12(k) of '34 Act to roll over suspension orders).

54. *See Chevron,* 104 S.Ct. at 2782 (only question for court reviewing agency's interpretation is whether agency's interpretation was reasonable).

55. 768 F.2d 352 (D.C. Cir. 1985).

56. *See id.* at 362 (in administering Federal Deposit Insurance Act (FDIA), Federal Deposit Insurance Corporation (FDIC) may not redefine terms that Congress already had defined in FDIA).

57. FAIC Sec., Inc. v. United States, 595 F. Supp. 73, 75 (D.D.C. 1984); *see also* 12 C.F.R. § 330.13(b) (1985) (rule to reduce insurance coverage on funds deposited by deposit brokers). Deposit brokers bring together individual depositors and place funds of the separate depositors in banks that pay high interest rates on brokers' deposits. *FAIC Sec.,* 595 F. Supp. at 76. For a commission, deposit brokers make deposits of customer funds that draw interest and receive federal deposit insurance protection up to $100,000. *Id.*

58. Federal Deposit Insurance Act, 12 U.S.C. §§ 264, 1728, 1811-1832 (1982).

59. *Id.* at § 1813(m).

60. *FAIC Sec.,* 595 F. Supp. at 76-77; *see also* 12 U.S.C. § 1813(m)(1) (defining "amount due to any depositor" as an amount up to $100,000); 12 C.F.R. § 330.13(b) (1985) (FDIC rule to reduce insurance coverage on funds deposited by deposit brokers).

61. *See FAIC Sec.,* 768 F.2d at 362 (District of Columbia Circuit considering whether FDIC had power to reduce insurance coverage on brokered deposits). In *FAIC Securities,* FAIC Securities and the Securities Industry Association (SIA) challenged the FDIC's authority to reduce deposit broker insurance coverage. *See FAIC Sec.* 595 F. Supp. at 73 (FAIC and SIA suing to set aside FDIC rule); *see also* 12 C.F.R. § 330.13(b) (1985) (FDIC rule to reduce insurance coverage on funds deposited by deposit brokers). FAIC Securities is a private firm engaged in the deposit brokerage business. *FAIC Sec.,* 595 F. Supp. at 75. The SIA is a trade association of deposit brokers. *Id.* FAIC and the SIA also sued the Federal Home Loan Bank Board (FHLBB) which had adopted a rule similar to the FDIC rule. *Id.* at 73 (FAIC and SIA suing FHLBB); *see also* 12 C.F.R. § 564.12(b) (1985) (FHLBB rule to reduce insurance coverage on funds deposited by deposit brokers).

Contesting the claim of FAIC Securities and the SIA, the FDIC and the FHLBB cited a 1966 amendment to the FDIA as authority to define terms to clarify the insurance coverage under the FDIA and the National Housing Act (NHA). *FAIC Sec.,* 595 F. Supp. at 78; *see also* Financial Institutions Supervisory Act of 1966, Pub. L. No. 91-151, 83 Stat. 375 (1966),

general provision authorizing the FDIC to define terms in administering the FDIA.[62] The *FAIC Securities* court determined, however, that the provision authorizing the FDIC to define terms did not authorize the FDIC to redefine terms that Congress already had defined in drafting the FDIA.[63] Concluding that the FDIC, therefore, had exceeded its power by reducing insurance coverage for deposit brokers, the *FAIC Securities* court enjoined the FDIC from implementing the regulation.[64]

FAIC Securities suggests that section 3(b) of the '34 Act, which authorizes the SEC to define terms, did not authorize the SEC to redefine Congress' definition of the term "bank."[65] In passing the '34 Act, Congress defined the term "bank" in section 3(a)(6) as national banks, Federal Reserve member banks, or state banks resembling national banks.[66] Congress' definition of the term "bank" does not distinguish banks based on the extent of a bank's involvement in the securities market.[67] Congress' definition of "bank," therefore, includes even banks doing brokerage business.[68] Importantly, when Congress has defined a term clearly, *FAIC Securities* is consis-

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amending 12 U.S.C. §§ 1728(a), 1813(m) (1982) (authorizing FHLBB and FDIC to define terms under NHA and FDIA, respectively).

In considering the FDIC's authority to reduce deposit broker insurance coverage, the district court in *FAIC Securities* determined that Congress had intended the FDIA to guarantee each depositor insurance up to the statutory limits regardless of who deposited the funds in the bank. *FAIC Sec.*, 595 F. Supp. at 77-78. The district court further determined that the FDIC's authority to define terms was not authority to alter a depositor's right to the insurance protection guaranteed by the FDIA. *Id.* at 79. Determining that the FDIC's regulation was inconsistent with the provisions of the FDIA, the district court set aside the rule. *Id.*

62. *See FAIC Sec.*, 768 F.2d at 362 (District of Columbia Circuit acknowledged FDIC's power to define terms); *see also* 12 U.S.C. § 1813(m)(1) (1982) (FDIC has authority to define terms to clarify insurance coverage provisions).

63. *FAIC Sec.*, 768 F.2d at 362. In *FAIC Securities*, the District of Columbia Circuit determined that the FDIC had redefined "amount due to any depositor" in adopting the rule reducing the insurance coverage of deposits executed by deposit brokers. *Id.* at 362-64; *see* 12 U.S.C. § 1813(m)(1) (1982) (Congress' definition of "amount due to any depositor" as an amount up to $100,000); *see* 12 C.F.R. § 330.13(b) (1985) (FDIC rule reducing insurance coverage). The *FAIC Securities* court observed that Congress already had defined "amount due to any depositor" as equalling up to $100,000 on the aggregate deposit of each beneficial owner. *FAIC Sec.*, 758 F.2d at 361; *see* 12 U.S.C. § 1813(m)(1) (1982) (Congress' definition of "amount due to any depositor"). Accordingly, the District of Columbia Circuit in *FAIC Securities* determined that the FDIC exceeded its authority in adopting a rule that would spread a single sum of $100,000 over all deposits placed in a bank by a single deposit broker, because the rule would not guarantee each beneficial owner up to $100,000 of coverage as Congress had provided. *FAIC Sec.*, 768 F.2d at 362.

64. *FAIC Sec.*, 768 F.2d at 362-64.

65. *See* 15 U.S.C. § 78c(a)(6) (1982) (Congress defined "bank" in '34 Act as national banks, Federal Reserve member banks, or state banks similar to national banks).

66. *See ABA Sues SEC to Block Commission Rule to Require Broker-Dealer Registration*, [July-Dec.] SEC. REG. & L. REP. (BNA) No. 32, at 1445 (Aug. 9, 1985) (bank exemption from broker-dealer registration requirement of '34 Act is absolute); *see also* 15 U.S.C. § 78c(a)(6) (1982) (definition of "bank" in '34 Act).

67. *See* 15 U.S.C. § 78c(a)(6) (1982) ('34 Act definition of "bank" which makes no reference to brokerage activities).

68. *See FAIC Sec.*, 768 F.2d at 362 (FDIC could not redefine terms of FDIA that

tent with *Chevron*, which applies only when a statute is ambiguous or incomplete.[69]

Although section 3(b) of the '34 Act arguably did not authorize the SEC to redefine Congress' unambiguous definition of "bank," Congress prefaced the definition of "bank" in the '34 Act with the clause "unless the context otherwise requires."[70] Since Congress promulgated the '34 Act, courts and commentators have disagreed over the proper construction of the "context" clause.[71] Some authority equates the word "context" with the factual setting of a situation and, consequently, the definitions of terms subject to the context clause may change as the facts seem to require.[72] Other authority equates the word "context" with the various textual provisions throughout the '34 Act so that the definitions of terms prefaced by the context clause remain constant unless other provisions of the '34 Act require a different meaning.[73] Therefore, under the factual context approach, the proliferation of bank securities activities without sufficient regulation arguably constituted a factual context requiring the SEC to modify Congress' specific definition of "bank."[74] In contrast, textual construction of the context clause would preclude the SEC from changing Congress' definition of "bank," despite changes in the banking industry.[75]

The legislative history relevant to the proper construction of the context clause supports textual construction of the clause.[76] The context clause originated in a House bill that Congress ultimately enacted as the Securities

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Congress already had defined); *see also* 15 U.S.C. § 78c(a)(6) (1982) (Congress defined "bank" as national banks, Federal Reserve member banks, or state banks similar to national banks); 17 C.F.R. § 240.3b-9 (1985) (rule 3b-9 excluding banks doing brokerage business from definition of "bank").

69. *Chevron*, 104 S.Ct. at 2781-82 (court may not substitute its interpretation of ambiguous statute for reasonable interpretation by agency); *see also FAIC Sec.*, 768 F.2d at 362 (FDIC could not redefine terms of FDIA that Congress already had defined).

70. *See* 15 U.S.C. § 78c (1982) (context clause which prefaces definitional section of '34 Act).

71. *See infra* notes 86-94 and accompanying text (authorities construing context clause as applicable only when '34 Act definitions are inconsistent with particular provisions of '34 Act); notes 95-106 and accompanying text (courts that have construed context clause as contemplating underlying factual transaction of case).

72. *See infra* notes 95-106 and accompanying text (courts construing "context" clause as applicable only when '34 Act definitions are inconsistent with particular provisions of '34 Act).

73. *See infra* notes 86-94 and accompanying text (authorities construing context clause as applicable only when '34 Act definitions are inconsistent with particular provisions of '34 Act).

74. *See SEC Rule, supra* note 8, at 1269 (in adopting rule 3b-9, SEC determined that "context" of context clause referred to factual scenario of unregulated bank securities activities); *see also infra* notes 125-28 and accompanying text (analysis of propriety of SEC's factual context approach to context clause).

75. *See infra* notes 86-89 and accompanying text (analysis demonstrating that textual construction of context clause would preclude SEC from applying clause to exclude banks doing brokerage business from '34 Act definition of "bank").

76. *See infra* notes 83-85 and accompanying text (analysis of legislative history supporting textual construction of context clause).

Act of 1933 ('33 Act).[77] After the House passed the bill prefacing a list of definitions with the context clause,[78] the Senate amended the bill and without comment replaced the context clause with "unless the text otherwise indicates."[79] In reconciling the House and Senate versions of the '33 Act, the conference committee discussed several material differences, but mentioned no distinction between the "text" language of the Senate version and the context clause of the House version.[80] The committee chose the House version of the '33 Act containing the context clause.[81] The following year, Congress again used the context clause to preface the list of definitions in the '34 Act.[82]

The failure of the conference committee to distinguish the term "text" from the term "context" in the '33 Act suggests that Congress perceived the Senate's "text" language and the context clause as interchangeable.[83] Ac-

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77. *See* H.R. 5480, 73d Cong., 1st Sess. (1933), *reprinted in* 5 LEGISLATIVE HISTORY SECURITIES ACT, 1933, at Item 24 (1973) ('33 Act bill prefacing definitions with context clause).

78. *See* H.R. 5480, 73d Cong., 1st Sess. (1933), *reprinted in '33* ACT HISTORY, *supra* note 77, at Item 24 (House passing bill that prefaced definitions with context clause).

79. *See* H.R. 5480, 73d Cong., 1st Sess. (1933), *reprinted in '33* ACT HISTORY, *supra* note 77, at Item 27 (Senate revisions of House bill). The provision "unless the text otherwise indicates" appeared in several bills that Congress considered in passing the '33 Act. In addition to the Senate version containing "unless the text otherwise indicates," the first House bill sponsored for the '33 Act prefaced the defined words with the "text" language. *See* H.R. 4314, 73d Cong., 1st Sess. (1933), *reprinted in '33* ACT HISTORY, *supra* note 77, at Item 22. Moreover, the "text" language of the first House bill was identical to a clause prefacing the definitions of a Senate bill introduced on the same day. *See* S. 875, 73d Cong., 1st Sess. (1933), *reprinted in '33* ACT HISTORY, *supra* note 77, at item 28.

80. *See* H.R. REP. No. 152, 73d Cong., 1st Sess. 24-25 (1933), *reprinted in '33* ACT HISTORY, *supra* note 77, at Item 19 (conference committee comparing House version of bill to Senate version).

81. *Id.*

82. *See* H.R. 9323, 73d Cong., 1st Sess. (1934), *reprinted in* 10 LEGISLATIVE HISTORY, *supra* note 6, at Items 31 & 32 (passage of '34 Act in House and Senate with "context" clause prefacing definitions).

83. Ruefenacht v. O'Halloran, 737 F.2d 320, 331 (3d Cir. 1984); *see also* H.R. REP. No. 152, 73d Cong., 1st Sess. 24-25 (1933), *reprinted in '33* ACT HISTORY, *supra* note 77 at Item 19 (conference committee comparing House version of bill to Senate version). The Third Circuit in *Ruefenacht v. O'Halloran* noted the material distinction between textual and factual construction of the context clause and determined that the drafters of the '33 and '34 Acts viewed "text" and "context" as interchangeable. *Ruefenacht*, 737 F.2d at 331. The *Ruefenacht* court determined that factual construction of the context clause would vest in the SEC a broad-ranging exemption power. *Id.* Pointing to section 78 of the '34 Act, which specifically confers a narrow exemption power on the SEC, the *Ruefenacht* court argued that Congress did not intend the context clause to ineffectuate the SEC's narrow exemption power. *Id.*

In concluding that Congress intended textual construction of the context clause, the Third Circuit in *Ruefenacht* erroneously stated that in amending the '33 Act bill, the Senate borrowed the "text" language from the first House bill and that the conference committee authored the context clause. *Id.* at 330. In fact, though, the "text" language tracked a Senate bill introduced on the same day as the first House bill, and the conference committee merely ratified the context clause. *See* S. 875, 73d Cong., 1st Sess. (1933), *reprinted in '33* ACT HISTORY, *supra* note 77, at Item 28 (Senate bill introduced on March 29, 1933 prefacing definitions with "unless

cordingly, Congress probably intended textual construction of the context clause in the '33 Act because the Senate version of the '33 Act, which incorporated the "text" language, precluded factual situations from preempting Congress' specific definitions.[84] Likewise, Congress probably intended textual construction of the context clause in the '34 Act since Congress, without comment, prefaced the definitions of the '34 Act with the identical clause.[85]

In addition to the legislative history, the prevailing conventions of statutory construction when Congress passed the '33 and '34 Acts suggest that Congress intended textual construction of the context clause.[86] When Congress passed the '33 and '34 Acts, the context clause simply reflected a canon of construction that courts otherwise implied as a license to adjust definitions as needed to make statutes internally consistent.[87] Significantly,

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the text otherwise indicates"); *see also* H.R. 4314, 73d Cong., 1st Sess. (1933), *reprinted in '33* ACT HISTORY, *supra* note 77, at Item 22 (initial House bill for '33 Act introduced on March 29, 1933, prefacing definitions with "unless the text otherwise indicates"); H.R. 5480, 73d Cong., 1st Sess. (1933), *reprinted in '33* ACT HISTORY, *supra* note 77, at Item 24 (House bill prefacing definitions with context clause).

Although incorrectly stating the legislative history, the Third Circuit, nonetheless, espoused a persuasive theory of Congress' intent in drafting the context clause by pointing out that the drafters added and deleted the two definitional prefaces in each instance without comment. *See Ruefenacht,* 737 F.2d at 330-32; *see also supra* notes 77-82 and accompanying text (Senate and House revisions of bills for '33 Act). In addition, the Third Circuit persuasively argued that Congress did not intend the context clause to ineffectuate section 78 which conferred on the SEC a narrow exemption power. *See Ruefenacht,* 737 F.2d at 331.

84. *Ruefenacht,* 737 F.2d at 331; *see also* H.R. 5480, 73d Cong., 1st Sess. 39 (1933), *reprinted in '33* ACT HISTORY, *supra* note 77, at Item 27 (Senate enactment of House bill with "unless the text otherwise indicates" prefacing definitions); *infra* notes 86-89 and accompanying text (textual construction of context clause precludes changing definitions unless other provisions of text require a different meaning). The conference committee's selection of the House version of the '33 Act bill incorporating the context clause rather than the Senate version incorporating the "text" language could support an inference that Congress rejected textual construction of the context clause. This argument would be circular, however, because it assumes that Congress intended the word "context" to mean the factual setting.

85. *Ruefenacht,* 737 F.2d at 331; *see also* H.R. 9323, 73d Cong., 1st Sess. (1934), *reprinted in* 10 LEGISLATIVE HISTORY, *supra* note 6, at Items 31 & 32 (passage of '34 Act in House and Senate with context clause prefacing definitions).

86. *See* Hammett, *Any Promissory Note: The Obscene Security A Search for the Non-Commercial Investment,* 7 TEX. TECH. L. REV. 25, 39-40 (1975) (context clause is congressionally mandated rule of construction to determine meaning of term in context of statute). When Congress passed the '34 Act, section 1 of the Revised Statutes stated that determining the meaning of any act or resolution of Congress requires singular words sometimes to extend and apply to several persons or things unless the context shows that Congress intended those words to have a more limited meaning. Act of Feb. 25, 1871, ch. 71, 16 Stat. 431. The context clause of the Revised Statutes undoubtedly refers to the text of the Statutes. *See* Hammett, *supra,* at 39-40. Congress intended the terms of its future laws to apply to facts, not to permit facts to define terms. *See id.* Conceivably, the drafters of the '33 Act borrowed the rule of construction that Congress had articulated in prefacing the Revised Statutes. *See id.*

87. *See* 4 LOSS, SECURITIES REGULATION 2485 (2d ed. Supp. 1969) (context clause is rule of statutory construction that Congress provided to help courts make statutes internally

the '33 and '34 Acts contain provisions giving words meanings that differ from the specific definitions of the same words prefaced by the context clause.[88] Therefore, the context clause arguably represents Congress' foresightful effort to help courts resolve inconsistencies among the various provisions in the '34 Act.[89]

After Congress enacted the '34 Act, the United States Supreme Court in *SEC v. National Securities, Inc.*[90] construed the context clause in determining whether an alleged fraud involved a "purchase or sale" of securities within the meaning of section 10(b) of the '34 Act.[91] Like the term "bank," the terms "purchase" and "sale" belong to the list of defined terms prefaced by the context clause in the '34 Act.[92] Rejecting the argument that "purchase" and "sale" have the same meaning in section 10(b) of the '34 Act as in section 5 of the '33 Act, the Supreme Court in *National Securities* stated that Congress prefaced the definitions with the context clause to caution that the same words may have different meanings in different provisions of the

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consistent); *see, e.g.*, Atlantic Cleaners & Dyers, Inc. v. United States, 286 U.S. 427, 433 (1932) (not unusual for same word to have different meaning in same act, and courts should apply appropriate meaning in each case); Lamar v. United States, 240 U.S. 60, 65 (1916) (in construing the term "officer," Court noted that same words may have different meanings in different parts of same act); American Sec. & Trust Co. v. Comm'rs. of the District of Columbia, 224 U.S. 491, 494 (1912) (same phrase may have different meanings in different connections).

88. *See* Dasho v. Susquehanna Corp., 380 F.2d 262, 269 (7th Cir. 1967) (determining that merger was "sale" as defined in '34 Act for purposes of section 10(b), although not for purposes of registration requirement); Schillner v. H. Vaughan Clarke & Co., 134 F.2d 875, 878 (2d Cir. 1943) (determining that context clause in '33 Act required "sell" as defined in section 2 to have narrower meaning in section 5 than in section 12); Loss, *supra* note 87, at 214-15 (in '33 Act, "context" of section 2 requires giving "underwriter" narrower meaning in section 2(3) than in section 2(11)).

89. *See* Hannan, *The Importance of Economic Reality and Risk in Defining Securities*, 25 HASTINGS L. J. 219, 277-79 (1974) (discussing context clause as statutory basis for giving same terms different meanings in different parts of '34 Act); Sonnenschein, *Federal Securities Law Coverage of Note Transactions: The Antifraud Provisions*, 35 BUS. LAW. 1567, 1577 (1980) (Congress intended context clause to refer to text of '33 and '34 Acts).

90. 393 U.S. 453 (1969).

91. *See id.* at 466. In *SEC v. National Securities, Inc.*, the SEC sued National Securities, Inc. (National Securities) in the United States District Court for the District of Arizona, claiming that National Securities had misrepresented facts to its shareholders in violation of section 10(b) of the '34 Act. SEC v. National Sec., Inc., 252 F. Supp. 623, 624 (D. Ariz. 1966). The district court granted summary judgment for National Securities, and the United States Court of Appeals for the Ninth Circuit affirmed. *Id.* at 626; *see also* SEC v. National Sec., Inc., 387 F.2d 25, 32 (9th Cir. 1967). On the SEC's appeal to the Supreme Court, National Securities argued that the Court should affirm the Ninth Circuit's decision because the alleged misrepresentations had not involved a "purchase or sale" as defined in the '34 Act. *National Sec.*, 393 U.S. at 464; *see also* 15 U.S.C. § 78c(a)(13)-(14) (1982) (definitions of "purchase" and "sale" in '34 Act). National Securities argued that section 10(b) of the '34 Act, therefore, did not apply because a purchase or sale was a prerequisite to the applicability of section 10(b). *National Sec.*, 393 U.S. at 464; *see also* Securities and Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b) (1982) (prohibiting fraud perpetuated in connection with purchase or sale of securities).

92. *See* 15 U.S.C. § 78c(a)(13)-(14) (1982) ('34 Act definitions of "purchase" and "sale" prefaced by context clause).

securities laws.[93] Thus, the Supreme Court in *National Securities* adopted textual construction of the context clause in accordance with Congress' probable intent in drafting the clause.[94]

Despite the Supreme Court's textual context approach to the context clause in *National Securities,* many federal courts applying the clause since *National Securities* have construed the clause factually.[95] These courts typically have construed the context clause in determining the meaning of "security" under the '33 and '34 Acts.[96] Like the term "bank," the term "security" is contained in the definitional section prefaced by the context clause in the '34 Act.[97] The United States Court of Appeals for the Second Circuit in *Exchange National Bank of Chicago v. Touche Ross & Co.*[98] typifies the federal courts that have construed the context clause factually.[99]

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93. *National Sec.,* 393 U.S. at 466. In *National Securities,* National Securities noted that a merger was not a "sale" under section 5 of the '33 Act. *Id.* at 465-66; *see also* 17 C.F.R. § 230.133(a) (1985) (statutory merger is not "sale" as defined in '33 Act). National Securities argued that, similarly, a merger was not a "purchase" or "sale" under section 10(b) of the '34 Act. *National Sec.,* 393 U.S. at 466; *see also* 15 U.S.C. § 78c(a)(13)-(14) (definitions of "purchase" and "sale" in '34 Act including mergers).

94. *See National Sec.,* 393 U.S. at 466 (Congress prefaced definitions in '33 and '34 Acts with context clause because same words may have different meanings in different parts of statutes); *see also* 15 U.S.C. § 78c(a) (1982) (context clause prefacing definitions in '34 Act); *supra* notes 76-85 and accompanying text (analysis of legislative history suggesting that Congress intended textual construction of context clause); notes 86-89 and accompanying text (discussion of usage in statutory construction when Congress passed '34 Act evidencing that Congress intended textual construction of context clause).

95. *See, e.g.,* Wolf v. Banco Nacional de Mexico, S.A., 739 F.2d 1458, 1460-63 (9th Cir.) (determining that adequacy of regulation was factual context requiring exclusion of certificate of deposit issued for pesos by Mexican bank from definition of "security" in '33 Act), *cert. denied,* 105 S. Ct. 784 (1984); Frederiksen v. Poloway, 637 F.2d 1147, 1150 (7th Cir. 1981) (rejecting textual context approach to context clause and applying context clause to limit definition of security), *cert. denied,* 451 U.S. 1017 (1982); *infra* notes 96-106 and accompanying text (federal courts construing context clause factually).

The factual context approach apparently originated in the United States District Court for the Eastern District of Missouri. *See* Hammett, *supra* note 86, at 38; *see also* Joseph v. Norman's Health Club, 336 F. Supp. 307, 313 (E.D. Mo. 1971). In Joseph v. Norman's Health Club, the plaintiffs bought lifetime memberships in the defendant's health club. 336 F. Supp. at 310. The plaintiffs paid for the membership with promissory notes. *Id.* at 312. Upon learning that the defendant had discounted the notes, the plaintiffs sued the defendant under the antifraud provisions of the '34 Act. *Id.* The district court in *Joseph* found that Congress' specific definition of "security" potentially comprehended the promissory notes. *Id.* at 313. The *Joseph* court noted, however, that the context clause prefaced the definition of "security" in the '34 Act. *Id.* In construing the context clause, the district court in *Joseph* determined that exchanging promissory notes for membership in a club was a factual context making Congress' specific definition of "security" inapplicable. *Id.* Accordingly, the *Joseph* court dismissed the plaintiff's claim under the '34 Act because the transaction did not involve a security. *Id.*

96. *See supra* note 95 and accompanying text (examples of federal courts construing context clause factually in determining meaning of "security" under '34 Act).

97. *See* 15 U.S.C. § 78c(a)(10) (1982) ('34 Act definition of "security" prefaced by context clause).

98. 544 F.2d 1126 (2d Cir. 1976).

99. *See* Exchange National Bank of Chicago v. Touche Ross & Co., 544 F.2d 1126, 1137

In *Exchange National,* the brokerage firm of Weis, Voisin & Co. (Weis) sold three unsecured, subordinated notes to the Exchange National Bank of Chicago (Exchange National) for one million dollars.[100] Weis eventually went bankrupt, and the notes became worthless.[101] Exchange National sued the accounting firm of Touche Ross & Co. (Touche Ross), claiming that Touche Ross had violated the '34 Act by reporting misleading information about Weis' financial condition which had induced Exchange National to buy the notes.[102] In determining whether the '34 Act applied to the transaction,[103] the Second Circuit in *Exchange National* considered whether the definition of "security" under the '34 Act comprehended the unsecured, subordinated notes that Exchange National bought from Weis.[104] The Second Circuit cautioned that the context clause could exempt the notes from the specific definition of "security" under a variety of factual circumstances, but determined, nonetheless, that the definition of "security" included the three notes in question.[105] Accordingly, the Second Circuit held that the '34 Act applied to the unsecured, subordinated notes.[106]

The federal courts that have construed the context clause factually have not reconciled their factual context approach with the textual context approach of the Supreme Court in *National Securities.*[107] Moreover, those federal courts, in construing the context clause, have failed to address the congressional record which tends to support textual construction of the clause.[108] The inability or unwillingness of the federal courts to justify their departure from the textual context approach would cast doubt on the SEC's

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(2d Cir. 1976); *see also supra* note 95 and accompanying text (federal courts' factual context approach to context clause).

100. *See Touche Ross,* 544 F.2d at 1128 (transaction in *Touche Ross).*

101. *See id.* (brokerage firm of Weis, Voisin & Co. (Weis) went bankrupt).

102. *See id.* In *Touche Ross,* Exchange National, in determining whether to buy three notes from Weis, obtained accounting reports from Touche Ross & Co. (Touche Ross). *See id.* The reports did not reflect that the bankruptcy court had placed Weis in receivership. *See id.* Thus, upon discovering that the notes were worthless, Exchange National held Touche Ross responsible. *See id.*

103. *See Touche Ross,* 544 F.2d at 1128-36 (district court denied Touche Ross' motion to dismiss, and Touche Ross appealed to United States Court of Appeals for the Second Circuit).

104. *Id.* at 1131-38; *see also* 15 U.S.C. § 78c(a)(10) (1982) ('34 Act definition of "security").

105. *Touche Ross,* 544 F.2d at 1137-39; *see also* 15 U.S.C. § 78c(a)(10) (1982) ('34 Act definition of "security" prefaced by context clause). The Second Circuit in *Touche Ross* cited examples of factual contexts that would narrow the '34 Act's definition of "security" to include most note transactions. *See Touche Ross,* 544 F.2d at 1134-36 ('34 Act's definition of "security" not applicable when consumer delivers note in financing arrangement, when note evidences character loan to bank customer, or when small businessman delivers note against lien on business assets).

106. *Touche Ross,* 544 F.2d at 1137-39.

107. *See supra* notes 90-94 and accompanying text (Supreme Court's textual construction of context clause in *National Securities); see also* notes 95-106 and accompanying text (federal courts' factual context approach to context clause).

108. *See supra* notes 76-85 and accompanying text (legislative history of '33 and '34 Acts suggesting that Congress intended textual construction of context clause); *see also supra* notes 95-106 and accompanying text (federal courts' factual context approach to context clause).

factual construction of the context clause and, consequently, on the SEC's authority to adopt rule 3b-9.[109] The United States Supreme Court, however, recently may have construed the context clause factually in determining whether FDIC-insured certificates of deposit were "securit[ies]" as defined in the '34 Act.[110]

In *Marine Bank v. Weaver*,[111] Sam and Alice Weaver sued Marine Bank on the grounds that Marine Bank fraudulently sold them an FDIC-insured certificate of deposit in violation of the antifraud provisions of the '34 Act.[112] In considering whether the certificate of deposit was a "security" as defined in the '34 Act,[113] the Supreme Court in *Marine Bank* observed the broad definition of "security" in the Act and noted a preference to construe "security" broadly to further the investor protection purpose of the Act.[114] The Court noted, however, that the context clause qualified the broad definition of "security."[115] In considering the effect of the context clause on the definition of "security," the Court observed that the comprehensive regulatory scheme governing the banking industry already protected persons

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109. *See supra* notes 76-94 and accompanying text (analysis suggesting propriety of textual context approach to context clause); *see also supra* notes 76-94 and accompanying text (analysis demonstrating that textual construction of context clause makes '34 Act's definition of "bank" applicable unless preempted by specific provision of '34 Act).

110. *See* Marine Bank v. Weaver, 455 U.S. 551, 555-59 (1982) (applying context clause to determine whether FDIC-insured certificate of deposit was a security under '34 Act).

111. *Id.*

112. *Id.*; *see also* 15 U.S.C. § 78; (antifraud provisions of '34 Act generally applicable to securities transactions, including transactions executed by banks). In *Marine Bank v. Weaver*, Sam and Alice Weaver bought a $50,000 FDIC-insured certificate of deposit (CD) from Marine Bank, the Weavers pledged the CD to guarantee a $65,000 loan that Marine Bank had made to Columbus Packing Co., a slaughter house and meat market business that already owed Marine Bank $33,000. *Id.* By guaranteeing the $65,000 loan, the Weavers became entitled to 50% of Columbus' net profit plus $100 per month and additional consideration. *Id.* When the Weavers discovered that Columbus had filed for bankruptcy and that Marine Bank, thus, had become entitled to the Weavers' $50,000 CD, the Weavers claimed that bank officers of Marine Bank fraudulently had solicited the Weavers to guarantee the $65,000 loan. *Id.* The district court determined that the transaction did not involve the purchase or sale of a security as defined in the '34 Act. *Id.* Concluding that the '34 Act, therefore, did not apply, the District Court granted summary judgment for Marine Bank. *Id.*

The Third Circuit in *Marine Bank* determined that the FDIC-insured CD was functionally equal to the withdrawable capital shares of a savings and loan association. Weaver v. Marine Bank, 637 F.2d 157, 164 (3d Cir. 1980). The Third Circuit determined, therefore, that the CD was a security under the '34 Act because the Supreme Court earlier had held that withdrawable capital shares were securities under the '34 Act. *Id.*; *see* Tcherepnin v. Knight, 389 U.S. 332, 345-46 (1967) (withdrawable capital shares of savings and loan association are securities under '34 Act).

113. *See* Marine Bank v. Weaver, 455 U.S. at 552 (considering whether FDIC-insured CD was "security" under '34 Act).

114. *See id.* at 555-56 (definition of "security" under '34 Act includes unusual and irregular instruments); *see also supra* note 6 and accompanying text (Congress promulgated '34 Act to protect investors from unfair practices in securities market).

115. *See Marine Bank*, 455 U.S. at 556 (context clause qualified definition of "security"); *see also* 15 U.S.C. § 78c (context clause qualifying definitions of '34 Act).

investing in FDIC-insured certificates of deposit.[116] The *Marine Bank* Court reasoned, therefore, that extending the '34 Act's protection to the Weavers was unnecessary, even though the broad definition of "security" ordinarily would comprehend certificates of deposit.[117] Accordingly, the Supreme Court in *Marine Bank* dismissed the Weavers' claim under section 10(b) of the '34 Act.[118]

The *Marine Bank* Court may have construed the context clause factually by equating the word "context" with the existing regulatory scheme for the banking and securities industries.[119] The Court based its holding, however, on the independent ground that SEC regulation of the Weaver's certificates of deposit was inconsistent with the legislative history of federal banking and securities laws.[120] Therefore, the Court's references to the context clause arguably were dicta.[121] Moreover, the *Marine Bank* Court expressed no intention to depart from the textual approach that the Supreme Court in *National Securities v. SEC* had endorsed unequivocally.[122] Finally, prudential considerations militate against imputing to the *Marine Bank* Court a position inconsistent with Congress' probable intent in incorporating the context clause.[123] Consequently, whether the *Marine Bank* Court sanctioned factual construction of the context clause is unclear.[124] Thus, the proper construction of the context clause is unsettled.[125]

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116. *See Marine Bank,* 455 U.S. at 558-59. In *Marine Bank,* the Supreme Court noted the reporting, advertising, and inspection requirements that the federal banking regulators imposed on banks to assure the financial safety of banks. *Id.* The Court determined that regulation to assure financial safety coupled with FDIC protection of customer deposits adequately protected the Weavers in their purchase of an FDIC-insured CD. *Id. But cf. supra* note 14 and accompanying text (banking regulation inadequate to protect investors in securities).

117. *See Marine Bank,* 455 U.S. at 559 (applying context clause to preempt specific definition of "security" in '34 Act); *see also* 15 U.S.C. § 78c(a)(10) (definition of "security" qualified by context clause).

118. *See Marine Bank,* 455 U.S. at 559 (*Marine Bank* Court reversed Third Circuit's decision).

119. *See Marine Bank,* 455 U.S. at 559 (adequacy of federal banking regulations to cover FDIC-insured CDs was a context that made definition of security inapplicable).

120. *See Marine Bank,* 455 U.S. at 559 (applying '34 Act to FDIC-insured CDs would be inconsistent with legislative history of federal banking and securities laws).

121. *See id.,* 560 n.11 (articulating decisional basis independent of context clause).

122. *See id.* (articulating decisional basis independent of context clause); *see also SEC v. National Sec.,* 393 U.S. 453, 466 (1969) (Congress prefaced definitions in '33 and '34 Acts with context clause because same words may have different meanings in different parts of statute).

123. *See Marine Bank,* 455 U.S. at 559 (articulating decisional basis independent of context clause); *see also supra* notes 76-85 and accompanying text (legislative history suggesting that Congress intended textual construction of context clause).

124. *See supra* notes 119-123 and accompanying text (analysis demonstrating that whether *Marine Bank* Court adopted factual context approach to context clause is unclear).

125. *See supra* notes 76-94 and accompanying text (legislative history and *National Securities* favor textual construction of context clause); notes 95 & 124 and accompanying text (federal courts have construed context clause factually, and whether *Marine Bank* Court adopted factual context approach to context clause is unclear).

Significantly, though, *Marine Bank* created a legitimate basis for the SEC's factual construction of the context clause.[126] Indeed, several federal courts have cited *Marine Bank* as the Supreme Court's approval of the factual context approach to the context clause.[127] The Supreme Court's decision in *Chevron,* therefore, suggests that the judiciary should defer to the SEC's reasonable construction of the context clause.[128]

Authorized by *Marine Bank* to look outside the text of the '34 Act to interpret the context clause, the SEC in adopting rule 3b-9 equated the word "context" with the adequacy of existing regulation to preserve the investor protection function of the '34 Act.[129] Thus, in adopting rule 3b-9, the SEC determined that the proliferation of banks engaged in unregulated securities activities was a factual context that required SEC protection of investors trading securities through banks.[130] Opponents of rule 3b-9, however, maintain that the *Marine Bank* Court interpreted the context clause narrowly to restrict the SEC's jurisdiction and, thus, to prevent overlapping in the jurisdictions of the federal regulatory agencies.[131] The opponents of rule 3b-9 argue that the word "context" in the context clause simply requires the SEC to abstain from regulating industries that are already subject to regulation by other agencies.[132]

The Supreme Court's opinion in *Marine Bank,* however, requires analysis beyond the simple inquiry whether SEC regulation of banks would create multiple regulation of the banking industry.[133] In interpreting the context clause, the *Marine Bank* Court tempered its discussion of dual regulation by addressing the adequacy of federal banking regulations to protect persons investing in FDIC-insured certificates of deposit.[134] Thus, in *Marine Bank,* the relevant "context" was the adequacy or inadequacy of federal banking

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126. *See Marine Bank,* 455 U.S. at 556-59 (citing context clause in determining whether FDIC-insured CDs were securities).

127. *See, e.g.,* Wolf v. Banco Nacional de Mexico, S.A., 739 F.2d 1458, 1462 (9th Cir. 1984) (*Marine Bank* Court construed context clause factually); Daily v. Morgan, 701 F.2d 496, 500 (5th Cir. 1983) (citing *Marine Bank* as support for factual construction of context clause); Crownair Systems, Inc. v. Wolf, 598 F. Supp. 1478, 1480-81 (D. Puerto Rico 1984) (citing *Marine Bank* as authority to construe context clause factually).

128. *See Chevron,* 104 S.Ct. at 2782 (court may not substitute its interpretation of ambiguous statute for reasonable interpretation of agency); *see also supra* notes 44-54 and accompanying text (analysis of judicial review of agency interpretations of statutes).

129. *See SEC Rule, supra* note 8, at 1269-70 (SEC's determination that proliferation of unregulated bank securities activities was context requiring implementation of rule 3b-9).

130. *Id.*

131. *See* American Bankers Ass'n v. SEC, [July-Dec.] SEC. REG. & L. REP. (BNA) No. 43, at 1916 (Oct. 30, 1985) (ABA arguing that *Marine Bank* supported narrow interpretation of context clause to discourage overlapping regulation).

132. *Id.*

133. *See Marine Bank,* 455 U.S. at 558-59 (considering regulatory context in applying context clause to determine meaning of "security" under '34 Act).

134. *Marine Bank,* 455 U.S. at 556-58 (considering adequacy of banking regulations to protect investors in FDIC-insured CDs).

regulations to satisfy the investor protection function of the '34 Act.[135] Applying the context clause, the *Marine Bank* Court determined that the adequacy of federal banking regulations to protect investors in FDIC-insured certificates of deposit was a "context" requiring departure from the '34 Act's specific definition of "security" which otherwise would include FDIC-insured certificates of deposit.[136] Conversely, the inadequacy of federal banking regulations to protect investors that trade securities through banks offering brokerage services is a context indicating that banks doing brokerage business are not banks within the bank exemption of the '34 Act.[137] Therefore, under the *Marine Bank* Court's analysis, the SEC properly interpreted the context clause as authority for adopting rule 3b-9 requiring banks doing brokerage business to register as broker-dealers.[138]

As the SEC determined in adopting rule 3b-9, imposing the broker-dealer registration requirement on banks doing brokerage business fills the void in federal protection of investors trading securities.[139] Banks attempting to side-step the broker-dealer registration requirement by affiliating a broker-dealer or by establishing a subsidiary will not compromise the investor protection purpose of the '34 Act, because the '34 Act imposes the registration requirement on bank subsidiaries and affiliates.[140] Moreover, by reducing the economic incentives for banks to conduct brokerage business, rule 3b-9 may provide the unintended benefit of deterring banking practices that arguably violate the Glass-Steagall Act which prohibits banks from engaging in most securities activities.[141] In this sense, rule 3b-9 may do double duty in guarding the integrity of the financial industry.[142]

Notwithstanding the possible benefits of rule 3b-9, the propriety of its adoption depended upon factual construction of the context clause, a practice that Congress probably did not intend and that contradicts the Supreme Court's unchallenged textual construction of the context clause in *National Securities.*[143] Congress, therefore, should clarify the SEC's power to regulate

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135. *See id.* at 556-59 (*Marine Bank* Court concerned with investor protection and overlapping federal regulation).

136. *See id.* (determining that banking regulation of FDIC-insured CDs adequately served investor protection purpose of '34 Act).

137. *See supra* note 14 and accompanying text (federal banking regulation is inadequate to regulate bank securities activities).

138. *See supra* notes 111-37 and accompanying text (analysis of *Marine Bank* opinion relevant to SEC's power under context clause to adopt rule 3b-9).

139. *See SEC Rule, supra* note 8, at 1264 (uniform regulation of securities activities best serves investor protection function of '34 Act); *see also supra* note 17 and accompanying text (identifying regulation-by-function approach to securities regulation); note 14 and accompanying text (suggesting deficiency of bank regulations to regulate bank securities activities).

140. *See* 15 U.S.C. § 78o(a)(1) (1982) (persons doing brokerage business must register with SEC).

141. *See supra* notes 23-25 and accompanying text (rule 3b-9 reduces brokerage revenues of banks whether banks handle brokerage accounts internally or through affiliates or subsidiaries).

142. *Id.*

143. *See supra* notes 76-94 and accompanying text (legislative history and *National Securities* suggesting impropriety of factual context approach to context clause).

banks doing brokerage business by repealing or narrowing the bank exemption from the broker-dealer registration requirement of the '34 Act. Further, the Supreme Court should clarify its position on the proper construction of the context clause in light of the Court's inconsistent approaches to the clause in *National Securities* and *Marine Bank*. By declaring the proper construction of the context clause, the Supreme Court will help the lower federal courts applying the clause perpetuate Congress' intent. In the meantime, rule 3b-9 is valuable as an interim measure to reconcile the dynamics of the banking industry with the investor protection function of the '34 Act.

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