



Council of Institutional Investors
The Voice of Corporate Governance

Statement on Financial Gatekeepers

The Council of Institutional Investors believes financial gatekeepers should be transparent in their methodology and avoid or tightly manage conflicts of interest. Robust oversight and genuine accountability to investors are also imperative. Regulators should remain vigilant and work to close gaps in oversight. Continued reforms are needed to ensure that the pillars of transparency, independence, oversight and accountability are solidly in place.

Auditors, financial analysts, credit rating agencies and other financial “gatekeepers” play a vital role in ensuring the integrity and stability of the capital markets. They provide investors with timely, critical information they need, but often cannot verify, to make informed investment decisions. With vast access to management and material non-public information, financial gatekeepers have an inordinate impact on public confidence in the markets. They also exert great influence over the ability of corporations to raise capital and the investment options of many institutional investors.

In recent years, the global financial crisis and financial scandals on Wall Street and at operating companies from Enron to Tyco have cast a harsh light on flawed structures and practices of gatekeepers. In many cases, poor disclosure, conflicts of interest, minimal oversight and lack of accountability helped mislead many market participants into making investment decisions that ultimately yielded huge losses. The crisis of confidence in the markets that followed spurred regulators and lawmakers to scrutinize and rein in gatekeepers.

The Sarbanes-Oxley Act of 2002 and the “global settlement” with Wall Street firms in 2003 bolstered the transparency, independence, oversight and accountability of accounting firms and equity analysts, respectively. For example, accounting firms now are barred from providing many consulting services to companies whose books they audit. And banks are not allowed to include analysts in investment banking “roadshows” and must make analysts’ historical ratings and price target forecasts publicly available.

Credit rating agencies largely escaped meaningful oversight until the passage of the Credit Rating Agency Reform Act of 2006. While the act has improved disclosure and

competition in the rating industry, more transparency, stronger regulation and genuine accountability are still needed. Investigations by Congress and the Securities and Exchange Commission (SEC) have uncovered repeated instances where credit raters inflated ratings on structured financial products to win business from firms that issued the debt. And rating agencies continue to face minimal accountability for the fairness or quality of their ratings. The Council welcomes further examination of financial gatekeepers by regulators, lawmakers, academics and others, to determine what changes, including new rules and stronger oversight, are needed.

(Adopted April 13, 2010)