



Via Facsimile

April 27, 2010

The Honorable Robert Menendez
United States Senate
Washington, DC 20510

The Honorable Daniel K. Akaka
United States Senate
Washington, DC 20510

Dear Senators Akaka and Menendez:

I am writing on behalf of the Council of Institutional Investors ("Council"), a non profit association of public, union and corporate pension funds with combined assets that exceed \$3 trillion. Member funds are major long-term investors with a duty to protect the retirement savings of millions of American workers across the country. Significantly affected by the financial crisis, Council members have a deep, abiding interest in strong regulatory reform.

The purpose of this letter is to respond to your inquiry about the Council's views on your proposed "the honest broker amendment" to S. 3217, the *Restoring American Financial Stability Act of 2010* ("Act"). It is our understanding that the proposed amendment would replace Section 913 of the Act with a provision that would harmonize the fiduciary duties and regulation of brokers and investment advisers. We support the proposed amendment.

Our views on the regulation of brokers and investment advisers are informed by the recommendations of the Investor's Working Group ("IWG"). A blue ribbon panel of industry and market experts, the IWG is an independent, nonpartisan commission sponsored by the CFA Institute and the Council to provide an investor perspective on ways to improve the regulation of U.S. financial markets.

After months of deliberations, the findings and specific recommendations of the IWG were published in its July 2009 report *U.S. Financial Regulatory Reform: The Investors' Perspective* ("IWG Report").¹ Following its issuance, the IWG Report was reviewed and subsequently endorsed by the Council board and membership.²

¹ Investors' Working Group, *U.S. Financial Regulatory Reform: The Investors' Perspective* 1-27 (July 2009),

[http://www.cii.org/UserFiles/file/resource%20center/investment%20issues/Investors%20Working%20Group%20Report%20\(July%202009\).pdf](http://www.cii.org/UserFiles/file/resource%20center/investment%20issues/Investors%20Working%20Group%20Report%20(July%202009).pdf) [Hereinafter IWG Report].

² See Council of Institutional Investors, Investors' Working Group, <http://www.cii.org/iwgInfo> (Apr. 27, 2010).

Among its many findings, the IWG reached the following conclusions about the regulation of investment advisers and brokers:

Oversight of the intermediaries that investors rely on in making investment decisions has failed to keep pace with dramatic changes in the industry. These changes include the development and rapid growth of the financial planning profession and changes in the full-service brokerage business model to one that is, or is portrayed as being, largely advisory in nature. Nevertheless, a series of decisions by regulators over the years allowed brokerages to call their sales representatives “financial advisers,” offer extensive personalized investment advice and market their services based on the advice offered, all without regulating them as advisers.

As a result, investors are forced to choose among financial intermediaries who offer services that appear the same to unsophisticated eyes, but who are subject to very different standards of conduct and legal obligations to the client. Most significantly, investment advisers are required to act in their clients’ best interest and disclose all material information, including information about conflicts of interest, whereas brokers are subject to the less rigorous suitability standard and do not have to provide the same extensive disclosures.

Meanwhile, although investors are encouraged to place their trust in “financial advisers,” compensation practices in the industry are riddled with conflicts of interest that may encourage sales of products that are not in clients’ best interests. The disclosures that investors are supposed to rely on in making investment decisions are often inadequate and overly complex and typically arrive after the sale—long past the point when they could have been useful to investors in analyzing their investment options.³

³ IWG, *supra* note 1, at 15.

The IWG findings led to the following recommendation—which we interpret to be consistent with your proposed amendment:

Investment advisers and brokers who provide investment advice to customers should have to adhere to fiduciary standards. Their compensation practices should be reformed and their disclosures improved. All investment professionals, including broker-dealers who provide personalized investment advice, should be subject to a fiduciary duty to act in their clients' best interests and to disclose material information. Compensation practices that encourage investment professionals to make recommendations that are not in their clients' best interests should be reformed. Disclosures should also be improved to ensure that investors receive pre-engagement disclosure to aid them in selecting an investment professional and clear, plain English, pre-sale disclosure of key information about recommended investments. This would provide an added level of protection to both retail and institutional clients.⁴

Thank you for your interest in the Council's views on this issue. Please feel to contact me at (202) 261-7081 or jeff@cii.org should you have any questions or comments regarding the contents of this letter.

Sincerely,



Jeff Mahoney
General Counsel

cc: The Honorable Christopher J. Dodd, Chairman, Committee on Banking, Housing, and Urban Affairs
The Honorable Richard C. Shelby, Ranking Member, Committee on Banking, Housing, and Urban Affairs

⁴ *Id.* at 16-17.