

# The Investors' Working Group

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Via Facsimile

February 22, 2010

The Honorable Christopher J. Dodd  
Chairman  
United States Senate Committee on Banking,  
Housing and Urban Affairs  
534 Dirksen Senate Office Building  
Washington, DC 20510-6075

The Honorable Richard C. Shelby  
Ranking Member  
United States Senate Committee on Banking,  
Housing and Urban Affairs  
534 Dirksen Senate Office Building  
Washington, DC 20510-6075

Dear Chairman Dodd and Ranking Member Shelby:

It is our understanding that proposed legislative language is currently being circulated for consideration that would replace the existing provisions of Section 913 of the Committee Print of the "Restoring America's Financial Stability Act of 2009" ("Act") with new language requiring the Securities and Exchange Commission to study regulatory "gaps and overlaps" between brokers and investment advisers. We write to express our concern about this proposed change because Section 913 was designed to ensure that brokers who give investment advice adhere to the same fiduciary duty to act in the best interests of their clients already applicable to investment advisers and financial planners consistent with the findings and recommendations of the Investors' Working Group ("IWG").

An independent blue ribbon panel of industry and market experts created by the CFA Institute and the Council of Institutional Investors to study and report on financial regulatory reform from the viewpoint of investors, the IWG carefully considered the need to close the gaps in the regulation of brokers, investment advisers, and other intermediaries. That consideration resulted in a number of findings and specific recommendations included in the IWG's July 2009 report – *U.S. Financial Regulatory Reform: The Investors' Perspective* ("IWG Report").

IWG findings relevant to the provisions of Section 913 include the following:

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.

Consideration of the above findings led the IWG to propose the following specific recommendation that is, at least in part, addressed by Section 913 as currently drafted:

**4. 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.

More details regarding the background and basis for the above findings and recommendations can be found on pages 14-17 of the IWG Report available in electronic form at <http://www.cii.org/UserFiles/file/IWGreport.pdf>.

Thank you for your consideration of the IWG views in connection with this very important element of regulatory reform. As always, we would welcome the opportunity to have members of the IWG discuss these issues with you or your staff at your convenience. Please feel to contact Jeff Mahoney at 202.261.7081 or [jeff@cii.org](mailto:jeff@cii.org) to arrange for such a meeting or if you should have any questions or comments regarding this letter.

Sincerely,



Kurt N. Schacht, CFA  
Managing Director, CFA Institute Centre for  
Financial Market Integrity  
Co-Sponsor, Investors' Working Group



Joseph A. Dear  
Chair, Council of Institutional Investors  
Co-Sponsor, Investors' Working Group



Council of Institutional Investors  
The Voice of Corporate Governance



**About the Investors' Working Group:** The Investors' Working Group (IWG) is an independent, nonpartisan commission co-sponsored by the Council of Institutional Investors and the CFA Institute to recommend ways to improve the regulation of U.S. financial markets. The IWG was established to ensure that investor views are heard in debate about how to modernize the financial regulatory system. Co-chairs of the IWG are William H. Donaldson, CFA, and Arthur Levitt Jr.

**About the IWG sponsors:** The [Council of Institutional Investors](#) is a nonprofit association of public, union and corporate pension funds with combined assets that exceed \$3 trillion. The Council is a leading voice for good corporate governance, strong shareowner rights and related investment issues. [CFA Institute](#) is the global association for investment professionals. It administers the CFA and CIPM curriculum and exam programs worldwide; publishes research; conducts professional development programs; and sets voluntary, ethics-based professional and performance-reporting standards for the investment industry.