



June 26, 2019

Via Electronic Delivery

Hon. Jay Clayton, Chairman  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20002

Re: Concerns Regarding Best Execution and Research Payments Issues

Dear Chairman Clayton,

We write jointly<sup>1</sup> to urge you to consider taking prompt action to address significant risks to US investors posed by the implementation of MiFID II and its impact on investment research and best execution. In particular, we urge you to revise guidance under Section 28(e) of the Securities Exchange Act of 1934 to:

1. require investment managers and advisers who seek to rely on the safe harbor to disclose amounts paid for research from client assets; and
2. require investment managers and advisers who seek to rely on the safe harbor to have procedures to ensure research benefits the asset owners who pay for it.

Enhancing transparency into the costs of research and the use of client commissions to pay for it are essential components of any Securities and Exchange Commission (SEC

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<sup>1</sup> The Healthy Markets Association is an investor-focused not-for-profit coalition working to educate market participants and promote data-driven reforms to market structure challenges. Our members, who range from a few billion to hundreds of billions of dollars in assets under management, have come together behind one basic principle: Informed investors and policymakers are essential for healthy capital markets. For more information about Healthy Markets, please visit our website at [healthymarkets.org](http://healthymarkets.org). The Council of Institutional Investors (CII) is a nonprofit, nonpartisan association of public, corporate and union employee benefit funds, other employee benefit plans, state and local entities charged with investing public assets, and foundations and endowments with combined assets under management of \$4 trillion. Our member funds include major long-term shareowners with a duty to protect the retirement savings of millions of workers and their families. Our associate members include a range of asset managers with more than \$35 trillion in assets under management. For more information about CII, including its members, please visit CII's website at <http://www.cii.org/members>. CFA Institute is a global, not-for-profit professional association of nearly 160,000 investment analysts, advisers, portfolio managers, and other investment professionals in 165 countries, of whom more than 152,000 hold the Chartered Financial Analyst® (CFA®) designation. Its membership also includes 151 member societies in 73 countries and territories. CFA Institute speaks on behalf of its members and advocates for investor protection and market integrity before standard setters, regulatory authorities, and legislative bodies worldwide. Its focus is on issues affecting the profession of financial analysis and investment management, education and competencies for investment professionals, and on issues of fairness, transparency, and accountability of global financial markets. For more information about CFA Institute, please visit our website at <https://www.cfainstitute.org/>.

or Commission) response to MiFID II. Failure by the Commission to address these concerns will continue to put US investors at significant risk.<sup>2</sup>

### ***Transparency To Asset Owners***

Each of our organizations has called for greater transparency into soft dollar research payments for years. For example, in 1998, the Council of Institutional Investors instituted a policy that:

[I]ike any other expense of the plan, trading costs need to be managed to minimize the cost and ensure that maximum value is received. But current brokerage industry practices of bundled pricing for services make it difficult to break out the exact costs of services (for trade execution, research or other things), may be antithetical to the fiduciary obligation of obtaining best execution, and hold too much potential for conflicts of interest and abuses.

We support and urge full unbundling of pricing for investment management, brokerage and research services, so that institutional investors can purchase and budget for these services as they do any other expense of the plan.<sup>3</sup>

Similarly, the CFA Institute has long had a policy that:

[i]t is the duty of investment managers to seek best execution for their clients, to ensure that any benefits accruing from the payment of commission fees beyond execution costs belong to the clients, and to inform their clients about how the benefits derived from those execution costs are invested.<sup>4</sup>

Our members, who regularly work as fiduciaries for US retirement funds, endowments, foundations, and other asset owners, frequently do not know how much of their own assets are being used to pay for investment research, nor can they be confident that the research they are buying even benefits their funds. While other parts of the developed

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<sup>2</sup> If the Commission were to separately consider a potential exemption from the Advisers Act to permit broker-dealer research providers to accept “hard dollars” for research without having to register as investment advisers, we urge you to carefully review the contours of such exemption so that it does not materially weaken the protections afforded by the Act. Further, such a change would still not provide asset owners with transparency into how their assets may be used to pay for research.

<sup>3</sup> Council of Institutional Investors, *Policies on Other Issues, Guiding Principles for Trading Practices, Commission Levels, Soft Dollars and Commission Recapture*, Mar. 31, 1998, available at [http://www.cii.org/policies\\_other\\_issues#principles\\_trading\\_commission\\_softdollar](http://www.cii.org/policies_other_issues#principles_trading_commission_softdollar).

<sup>4</sup> CFA Institute, *Investment Management Policies: Fair Dealing. Accord*, CFA Institute, *Soft Dollar Standards: Guidance for Ethical Practices Involving Client Brokerage*, at 8, 2011.

world have adopted research cost transparency (or gone further in the name of protecting investors), the US regulatory regime has not changed in decades.

Correcting US policy to provide greater transparency and flexibility in the payments for research has never been more essential. With the implementation of MiFID II and the PRIIPS regimes in Europe, many European asset owners are no longer being asked to pay for research.<sup>5</sup> This trend appears to be spreading globally.

If a global adviser were to want to continue to use its clients' commissions to pay for research, it can. But that would now often include mostly (or only) US asset owners. Put simply, US retirement funds, endowments, foundations, and other asset owners are now at risk for subsidizing research for others around the world. And they generally have no transparency into those additional costs.

### ***Adviser Choice***

Some research providers, including broker-dealers, have asserted that the Investment Advisers Act of 1940 and subsequent interpretations of it impede their ability to accept payments that are not explicitly tied to transactions or commissions. Further, some pensions and investment managers and advisers have expressed concerns that these provisions may impede their abilities to price competitively, and separately, shop for the best research and trading services.<sup>6</sup>

In particular, as interpreted, the law may require research providers to register as investment advisers if they directly receive a "hard dollar" payment from their customers. While many research providers are registered as investment advisers or are otherwise willing to accept "hard dollar" payments, many are not. Further, we understand that some broker-dealer research providers who currently do not accept hard dollar payments have indicated that they may decrease or eliminate their provision of research if they were to be forced to register as investment advisers.

We understand that the Commission is considering various mechanisms to permit research providers to accept payments from adviser (as opposed to asset owner) funds.

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<sup>5</sup> While MiFID II permits client funds to be used to pay for research through a Research Payment Account, we understand that the overwhelming majority of asset managers have declined to utilize this framework.

<sup>6</sup> We also note that some research providers don't provide their customers with clear pricing of costs for research, even upon request.

As part of the consideration of those mechanisms, we respectfully urge the Commission to protect asset owners by revising the contours of Section 28(e) to ensure that asset owners will (1) know what they are paying for research and (2) have confidence that their payments for research benefit them.

Thank you for your consideration.

Sincerely,



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Executive Director  
Healthy Markets Association



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Jeff Mahoney  
General Counsel  
Council of Institutional Investors



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Kurt Schacht  
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