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Re: Standards of Conduct for Investment Advisers and Broker-Dealers – Follow-up Questions from Staff

Dear Messrs. Gilbride, Timura and Ryan:

CFA Institute[1] appreciates the opportunity to have met with staff (the "Meeting") of the Securities and Exchange Commission ("SEC" or the "Commission") to discuss the response submitted on 10 January[2] by CFA Institute (the "Response") to the Chairman's request for information on standards of conduct for investment advisers and broker-dealers (the "Original Request"). This letter is to respond to questions raised at the Meeting.

[1] 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 and territories, of which more than 150,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 151 member societies in 70 countries and territories.

[2] https://www.cfainstitute.org/Comment%20Letters/20180110.pdf

At what point does CFA Institute believe advice should be considered personalized? As noted in our letter, the Investment Advisers Act of 1940 (the "Act") describes what is "impersonal investment advice" — oral statements or written material that do "not purport to meet the objectives or needs of specific individuals or accounts." It does not, however, describe what constitutes personalized investment advice. We called upon the SEC to add clarity to these matters by describing what is and is not personalized advice.

During the Meeting, however, Commission staff inquired as to how CFA Institute believes personalized investment advice should be defined. This was seen as important because calling for this definition and for calling for clarity on titles (discussed in a later question) was apparently seen by staff as fundamentally changing the nature of the securities brokerage business.

We view this more as returning to the place where the Act was originally contemplated by asking the Commission to clarify its interpretation of "incidental to" and to address the steady creep by salespersons from suitable recommendations to full-fledged investment advice requiring registration under the Act. We do not believe that unlawful business practices should continue because they have been permitted in the past. If this leads, in turn, to an adjustment for the securities brokerage industry, then the implication would be that through their evolving business models, these firms and their representatives are engaging in activities that are not consistent with what the Act permits. We think that is the case.

We certainly wish there was a "bright-line" in this situation. We recognize there are varying circumstances that may place brokers in the position of providing investment recommendations that could be either ancillary or more essential to their clients' financial well-being. We also recognize that determining which side of this divide the recommendations fall is an issue that has bedeviled the Commission for many years.

What we do suggest in the Response is that personalized investment advice goes beyond suitable investment recommendations and is intended to be and comes across as advice "intended to influence the investment decisions and actions of specific individuals or accounts." It has become indistinguishable from the advice of an RIA operating under a legal fiduciary duty.

Consequently, we believe basic clarity on definitions and titles is needed to help make this distinction clearer in the minds of investors. While we recognize the difficulty of creating bright lines to achieve this, we believe determining when advice exceeds incidental should consider the frequency of such advice, the holding out as an advisor, if the advice is personal and said to be in the best interests of the client and, in the latest nuance, being given with a fiduciary "mindset." Doing so we believe will allay the intentional blurring of distinctions that is costing US savers. We hope these are some useful points and stand ready to comment and support your efforts to reaffirm basic and appropriate delineations in this context.

What benefits would come from changing enforcement around the incidental advice exemption?

We see three primary benefits arising from additional clarity about what constitutes investment advice triggering registration as investment advisers and investment adviser representatives.

First, we believe clarity will give brokers greater awareness of what is and is not permitted under the standard of suitable investment recommendations. This will inform brokers and prevent some brokers from engaging in practices that exceed the boundaries of suitable and incidental. While we generally agree that most brokers intend to be fully honorable in their service to clients, they are squarely (and legally) in the service of the firms they represent.

Second, clarity in these matters will ensure the law is enforced as it is written. Currently, the titles brokers use, combined with the advice they provide, give investors the impression that the brokers are trusted investment advisers rather than securities salespeople. By clarifying what constitutes personalized advice and when a broker must register will further enhance investors' understanding of what brokers do, how they get paid, and how they address real and potential conflicts of interest.

And finally, clarity in what constitutes personalized advice and when adviser registration is required will lead to consistency between what the law and regulation say and the way brokers operate. Ultimately, this, we believe, will lead to reduced confusion for investors and thus increased investor protection.

Why did CFA Institute choose broker disclosure rather than a higher standard of care for broker-dealers?

As stated in the Response and above, we believe securities brokers play an important and efficient role in helping U.S. securities markets function. Our goal in suggesting the approaches given in the Response was, first, to provide distinction and clarity between investment advisory and securities brokerage activities, and, second, to preserve as much as possible the securities brokerage business model.

We believe that one group of investment professionals operating under a fiduciary duty rule is sufficient to provide investors with advice based on a high standard of care. In contrast, we also support investors having the option to transact with securities brokers who offer sales pitches of suitable transactions, together with efficient transaction execution.

Merely raising the bar somewhat for securities brokers, by contrast, without completely reaching a fiduciary standard of care would have had two likely negative outcomes. First, it might further reduce the availability of lower-cost (often, but not always) investment options for investors. We believe that retaining this option is more valuable than incrementally raising the standard of care bar. Second, and perhaps most importantly, a third standard would only exacerbate the circumstance revealed in every study done by the Commission to understand investor literacy. Confusion is further aggravated as demonstrated by the complexity of the similar DOL approach.

Conclusion

We believe the SEC has the authority and a timely opportunity to clarify the legal contours of investment advisers, personalized investment advice, the incidental exemption and titles used in the financial services industry by using administrative guidance. We strongly encourage such action. We believe these actions will go far to address the confusion among investors surrounding the roles of broker-dealers, restore investor trust, and restore the intended use of the incidental exclusion under the Advisers Act.

Should you have any questions about our positions, please do not hesitate to contact James Allen, CFA james.allen@cfainstitute.org.

Sincerely,

/s/ James Allen

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