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Testimony of Linda L. Rittenhouse--CFA Institute

Department of Labor Hearings on Conflict of Interest-Definition of Investment Advice

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Good afternoon. I am Linda Rittenhouse, Director of Capital Markets Policy at CFA Institute. We appreciate the opportunity to offer our views today on the recent DOL fiduciary duty proposal. We know this has been a controversial endeavor and we commend the Department for stepping into the fray.

CFA Institute is a global membership organization of more than 133,000 members in 151 countries, with over 125,000 holding the Chartered Financial Analyst or CFA designation. Our membership is diverse, including investment analysts, portfolio managers, chief investment officers for mutual funds, private wealth, pension funds, and other investment professionals. It is as a representative of this diverse group that I am happy to provide comments on the DOL's effort to hold advice providers to a best interest standard when serving ERISA retirement plans and IRA accountholders.

Regardless of their profession, all CFA Institute members are bound by their commitment to abide by the CFA Institute Code of Ethics and Standards of Professional Conduct, which require them to act for the benefit of their clients and place their clients' interests before their employer's or their own. They also must act with loyalty, care and prudence. These are not light undertakings; members must attest to their compliance on an annual basis, or risk losing their charter. Thus, we strongly support DOL's aim to put clients' interests first. We have long said that all personalized investment advice should be held to the same standard—regardless of the title of the provider, for example, be it "broker" or "advisor" or "counselor." We applaud the DOL for taking this important first step to actualize this objective. Retail clients—all investors—should be able to trust that the advice they receive is impartial and not compromised by conflicts of interest that may arise from revenue sharing arrangements or limiting recommendations to certain firm products.

Otherwise, what happens to the integrity of our marketplace?

While the proposal is not perfect, it does start from a place that seeks to restore the original intent of ERISA that requires duties of prudence and loyalty.

We have been impressed with your stated willingness to consider all comments raised and to acknowledge areas that are in need of redraft or clarification. We also have appreciated the attitude we have heard on numerous occasions that your intent is not one of "gotcha" but instead of investor protection. Thus, your willingness to clarify areas that have been problematic—especially under the Best Interest Contract Exemption—bodes well for making the final rule more workable.

So—now to the actual proposal.

We wholeheartedly agree that the current 5-part test is inadequate, does not honor the statutory definition of fiduciary, and allows for conflicted advice, higher costs, and the sale of inappropriate investment products to investors. Committing to replace this test alone is a major step forward in providing investors with protections they deserve.

We also strongly support the rule's carve out from the definition of investment advice that allows a range of educational materials to be provided to investors. We have a longstanding position that investors must receive the information they need to make informed investment decisions. This is never so important as today, when individual investors have greater responsibility for understanding their retirement options, planning their future and managing their retirement assets through participant-directed plans; they need the educational tools. We encourage the final rule to retain the provisions that neither the frequency nor the form of these educational materials matter, as long as they do not include advice or recommendations as to specific investment managers or products.

We are not convinced that requiring all advice providers to adhere to a fiduciary duty or meet the conditions of the Best Interest Contract Exemption will eliminate all retirement advice for the smaller investor. Nor do we agree with the argument that conflicted advice is better than no advice at all. Instead, we believe that investors will continue to receive the retirement advice they need, and technology and providers will step in to fill whatever void is created.

We do have some concerns about the proposal, however, that fall primarily into three areas relating to the Best Interest Contract Exemption.

First, we do believe that the proposal, as written, is too complex. This complexity and the resulting confusion will lead to unnecessarily high compliance costs and ultimately dilute its effectiveness. When the duty to comply first arises, whether the advice provider can have preliminary conversations and how the sequence of events will work on a practical level, all need to be addressed. We urge the Department to specifically discuss the parameters of when certain actions will first trigger responsibilities under the Exemption. We also encourage a review of the numerous actions required under the Exemption with an eye to streamlining those that are not necessary for achieving a best interest standard. For example, we note in our letter that the proposed point of sale disclosures are too onerous as drafted and instead recommend consideration of the Surgeon-General-type warning discussed in the proposal.

Second, we also hope the Department will provide more comfort as to when legal liability will attach. We support the new private right of action for IRA accountholders but understand that this and the execution of contracts create concerns in the industry. We also understand the trepidation caused by entering into contracts, and the resulting legal costs to defend actions when recommendations are later questioned by investors, even if the contract was executed correctly. To that end, we encourage the DOL to issue separate Guidance or discuss more directly in the final rule areas that most likely will lead to legal liability so that the industry has more certainty about the rule's boundaries.

Third, we are concerned about the investor confusion that may arise from a standard of care that applies to the retirement arena, but not other areas. While the DOL is creating a best interests standard for all advice providers under ERISA, the SEC has yet to introduce a uniform standard that would apply to all who provide personalized advice to retail investors. As a consequence, investors may expect a broker-dealer providing retirement advice to also be honoring a best interest standard when advising as to non-retirement assets. We encourage the DOL to work closely with the SEC when finalizing this rule to reconcile to the degree possible, this investor confusion issue.

In sum, we support this undertaking. We suggest that the DOL consider all reasonable ways to simplify this exemption—to reduce the compliance costs, to better define the parameters of when duties kick in, and to clarify legal liability under the rule so as to more clearly define the risks. Finally, we hope that the Department and the SEC will consult closely in adopting the final rule.