CFAI Letter to the SEC: Addressing the Fiduciary Standard of Conduct

By

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Advisers at Copley Investment Management unconditionally believe all persons giving investment advice should adhere to the fiduciary standard of conduct. The issue is not as complicated as some would like to make it. What is the problem, we wonder, for an investor to clearly understand whose best interest is being served: the person giving the advice or the person receiving it?

Recently, the Department of Labor issued a rule saying all persons giving investment advice on assets held in a retirement account must adhere to the fiduciary standard of conduct. After several postponements the DOL rule will go into effect in 2019. We believe such a fiduciary rule should cover all investment advice—whether an account consists of retirement assets or non-retirement assets. Fair play is fair play for everyone. Period.

The Securities Exchange Commission (SEC) has listened to us who have raised our voices; they are now considering adopting a rule requiring all persons giving investment advice on any type of account to adhere to the fiduciary standard of conduct. I have written on the issue in prior columns. Clearly, common sense dictates passage of such a universal rule. A fiduciary rule for everyone would delete conflicts of interest and raise the level of integrity for the entire industry.

To not follow a fiduciary rule is equivalent to allowing persons giving investment advice to legally manipulate the recipient of the advice. Market integrity is the cornerstone on which the industry is built, and integrity requires transparency. Can anyone make sense of a non-fiduciary rule that allows a person giving financial advice to gain from selling a product that's not in the client's best interest? It makes no sense! Still, the brokerage industry promotes that kind of argument and says the fiduciary standard unnecessarily cuts into its already fat profits. The argument is nonsensical!

In a letter to the SEC dated June 18, 2018, Paul Smith, CFA, president and chief executive officer of the CFA Institute, says a survey of Institute members (I am a member) shows the fiduciary rule as the highest priority facing the industry. Mr. Smith states, "CFA Institute strongly supports a fiduciary standard for all who provide personalized investment advice to retail investors."

He further says, "At the same time, we believe commission-based sales activities serve important client needs and give investors options for how they wish to conduct their investment activities. Whether commissioned brokers provide investment ideas or execute trades, we support their permission to pursue their business activities, so long as they are clear about their roles vis-a-vis their clients. Specifically, we recommend the commission require they refer to their roles with the title, "salespersons." For too long sales staff have blurred the lines between what they do—selling investment ideas to generate commission-base transactions—and what investment advisers do (advising clients on investment strategies and tactics to achieve their financial goals."

Mr. Smith concludes, “We believe once the issue of titles is addressed, the SEC will have a clearer idea of what kind of rules are needed to address other aspects of the standard-of-care issue. We stand ready to help make these changes, changes that we believe will have long-term benefits for investors and U.S. capital markets.”

In speaking for its members who represent the foundation of the investment management industry with a long history of professionalism, the president of the CFA Institute carries high credibility. The institute is a global, not-for- profit professional association of over 149,000 investment analysts, advisers, portfolio managers, and other investment professionals in 163 countries.

Over 143,000 professionals hold the coveted Chartered Financial Analyst (CFA) designation, which requires candidates pass three rigorous exams involving stock analysis, bond analysis, portfolio construction, and a multitude of related financial issues. The linchpin of the CFA designation is the code of ethics and professional conduct each member accepts as part of his/her responsibility to the profession. The designation is the gold standard in the investment management industry. I have taught CFA review courses for candidates preparing for the exam in nine countries.

Having been a proud member of the institute for 30 years, I am confident Mr. Smith’s letter reflects a great deal of research conducted in a balanced and thoughtful manner. Whether the SEC adopts his recommendations or not, the letter focuses attention on the standard-of-care issue.

As part of its mission statement, the institute has responsibility for educating the public when making investment decisions, to which this column is also devoted. An easy step every investor can take is to ask their advisers if they adhere to the fiduciary standard of conduct. The question deserves a simple unqualified answer. LOL

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