

MEMO# 15275

October 18, 2002

INSTITUTE COMMENT LETTER ON PROPOSED AIMR RESEARCH OBJECTIVITY STANDARDS

[15275] October 18, 2002 TO: SEC RULES MEMBERS No. 90-02 INVESTMENT ADVISER MEMBERS No. 43-02 COMPLIANCE ADVISORY COMMITTEE No. 90-02 RE: INSTITUTE COMMENT LETTER ON PROPOSED AIMR RESEARCH OBJECTIVITY STANDARDS The Association for Investment Management and Research ("AIMR") recently published for comment proposed Research Objectivity Standards ("Standards"). The proposed Standards are intended to be specific, measurable standards for managing and disclosing conflicts of interest that may impede a research analyst's ability to make objective recommendations. The Institute has filed a comment letter on the proposed Standards. The most significant aspects of the comment letter (a copy of which is attached) are summarized below. In general, the letter states that the Institute strongly opposes the application of the proposed Standards to investment management firms. The letter notes that investment management firms are subject to comprehensive rules and regulations under the Investment Advisers Act and the Investment Company Act and already have stringent internal procedures in place to address conflicts of interest. In addition, the letter notes that investment advisers owe their clients fiduciary duties that would preclude conflicts of interests from arising and whatever potential conflicts of interest may exist relating to investment management firms and research are greatly attenuated as compared to those presented by sellside firms. Finally, the letter notes that we are not aware of any reported cases of abuse in this area involving investment management firms and that the proposed Standards would create significant compliance burdens for such firms. The letter also contains specific comments on the proposed Standards. As a preliminary matter, the letter states that many of the definitions contained in the proposed Standards are ambiguous and/or overly broad. For example, the letter states that the definitions of "research analyst" and "research report" may unnecessarily sweep in personnel at investment management firms with little or no association to the "research report." The letter therefore recommends that AIMR revise these terms to appropriately narrow their scope. The letter also expresses several concerns regarding the Standards' proposed requirements and recommended procedures to implement those requirements. For example, the Standards would require firms to implement policies and procedures addressing the 2 working relationships that covered employees have with research analysts at sellside firms. One of these procedures recommends that firms monitor brokerage to verify that it is not inappropriately shifted from firms when research analysts change ratings or recommendations on corporate issuers in which the firm is invested or with which the firm has an investment advisory relationship. The letter states that this recommendation would create unnecessary burdens for investment management firms as such firms would have to constantly monitor not only

when a rating or recommendation is changed on a security the fund holds, but also whether brokerage has been shifted from that analyst's firm and the reasons for that shift. The letter therefore recommends that this recommendation be eliminated from the Standards. The letter also states that, given existing federal securities law requirements, as well as the stringent internal policies and procedures that investment management firms have in place relating to the personal investment and trading activities of investment management personnel, the Standard containing several requirements relating to a covered employee's personal investments and trading activities is unnecessary. Specifically, the letter notes that registered funds must adhere to Rule 17j-1 under the Investment Company Act. The letter also notes that substantially all funds groups have adopted the recommendations in the Institute's Report of the Advisory Group on Personal Investing addressing the personal investment and trading activities of investment personnel. The letter therefore states that AIMR should revise the Standard and follow an approach similar to that used in Rule 17j-1 to determine the scope of the Standard. The Standards also would require firms to provide full and fair disclosure of all conflicts of interest to which the firm or its covered employees are subject. The letter states that the Standard's recommended disclosures are unnecessary inasmuch as registered investment advisers are already subject to similar, and in some cases more extensive, disclosure requirements under the Investment Advisers Act. The letter also notes that the recommended disclosures are vague and may raise confidentiality concerns for investment management firms. The letter therefore states that the better approach would be for the Standards to make a strong affirmation of a firm's obligations to adhere to all applicable disclosure requirements of the SEC and other regulatory bodies. At a minimum, the letter recommends that AIMR not require the disclosure of the specific conflicts of interest to which the firm or its covered employees are subject, but instead only require a general statement about the conflicts. Finally, the Standards recommend that firms disseminate a list of potential violations of their policy and associated disciplinary sanctions to all covered employees, clients and prospective clients. The letter states that such a list could take away a firm's discretion to tailor and modify disciplinary sanctions based on the specific facts and circumstances of a violation and may result in firms drafting the list very generally to allow for flexibility. The letter therefore recommends that AIMR eliminate this recommendation. Ari Burstein Associate Counsel

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