ADVOCACY UPDATE

GLOBAL ADVOCACY NEWS AND UPDATE

SEPTEMBER 2020

IN THIS ISSUE

FOR COMMENTS OR QUESTIONS, CONTACT

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Amidst continuing complex economic, political, and social conditions around the globe, CFA Institute remains focused on investor protection and market integrity issues. This month we share updates from our key regions on making our voices heard on important regulatory, sustainability, and investment topics, including the following: in the United States, on the Department of Labor retirement rules, climate change, and short-termism; in Europe, on ESG disclosures, MiFID II, and leverage-related systemic risk; and in Asia Pacific on stewardship codes and ESG standards. You also will find highlights of our advocacy in action, media coverage, and global events. Please feel free to contact us with questions or comments.

—**Kurt N. Schacht, JD, CFA, CFA Institute Policy Director**

INVESTOR PROTECTION

CFA INSTITUTE TESTIFIES ON DOL RETIREMENT RULES

US Department of Labor (DOL) testimony: On 3 September, Jim Allen, head of Capital Markets Policy for the Americas, was invited by the DOL to testify before its staff to elaborate on the views of CFA Institute on the DOL's proposed retirement investment rules. This proceeding followed the issuance of our comment letter on 6 August.

Jim Allen's virtual testimony to the DOL

Investor confusion: The key concern conveyed in the testimony focused on the DOL's decision to reinstate its out-of-date "Five-Part Test," and its heavy reliance on the US Securities and Exchange Commission's Regulation Best Interest (Reg BI). The test confusingly determines when advisers are fiduciaries, while exempting them from those same obligations if they adhere to Reg BI, which does not impose a fiduciary duty on brokers. This would permit self-interested and conflicted advice from brokers, and thus is contrary to the Employee Retirement Income Security Act's (ERISA) fundamental purpose of protecting individuals in retirement and health plans by requiring disclosure and reporting.

Our position: CFA Institute expressed support for the DOL's plans to interpret advice on the rollover of institutional retirement funds to individual retirement accounts as fiduciary investment advice and therefore subject to fiduciary obligations. We recommended, however, that DOL define *all* rollover advice as fiduciary advice and subject that advice to limited and narrowly defined exemptions from fiduciary standards. We concluded by calling on the DOL to grant investors a private right of action to remedy fraudulent advice, and we recommended it mandate that advisers "eliminate conflicts where possible," not just "mitigate" them.

ADVOCACY IN ACTION

IMPACT METRICS

The CFA Institute Advocacy Group is affiliated with many key industry organizations, committees, societies, and associations around the globe to represent the investment community and advocate on behalf of our members. Here is an overview of our "Seats at the Table" numbers as of August 2020:

- Service on Regulatory or Stakeholder Advisory Committees: 30
- Days of Service: 117
- Citations, Speeches, and References: 189

MEDIA ATTENTION

Barron's (11 September): Kurt Schacht, policy director at CFA Institute, provided criticisms of the Department of Labor's (DOL) latest proposal to undo a major landmark of fiduciary duty for proxy voting.

The Asset (HKG) (11 September): CFA Institute Capital Markets Policy Director Sara Cheng commented on the power of nudges in financial advice.

XBRL (11 September): Mohini Singh, director of financial reporting policy at CFA Institute, discussed whether blockchain can be used as a distribution mechanism for financial data.

Risk (7 September) covered Systemic Risk Council Chair Paul Tucker's warnings on large bank bail-ins.

Forbes (3 September) quoted CFA Institute Capital Markets Policy Head Jim Allen on a proposed DOL rule.

Expert Investor (3 September) covered CFA Institute Advocacy Head Olivier Fines' comments on alternative ways of investing in UK funds.

Financial Advisor Magazine (1 September) reported on the CFA Institute survey on the COVID-19 stimulus.

Advisor Perspectives (31 August) featured Jim Allen, head of the Americas Capital Markets Policy Group at CFA Institute, on the "Gaining Perspective" podcast covering the Investment Advisers Act of 1940.

The Hindu Business Line (IND) (31 August) CFA Institute India Head Vidhu Shekhar discussed career opportunities in investment management.

China Daily (28 August) quoted Mary Leung, head of advocacy at CFA Institute, Asia Pacific, on ESG integration and disclosure.

NASDAQ (27 August): CFA Institute Capital Markets Policy Head Jim Allen discussed the recent CFA Institute COVID-19 impact survey.

Law360 (26 August): CFA Institute Managing Director Kurt Schacht and Capital Markets Policy Manager Karina Karakulova wrote an opinion piece against SEC proxy rules.

FN London (UK) (26 August) cited CFA Institute EMEA Managing Director Gary Baker on asset management post-COVID-19.

Business Standard (IND) (26 August) cited CFA Institute India Head Vidhu Shekhar's comments on the need to slow down the pandemic in the Indian market.

City AM podcast (26 August) covered CFA Institute EMEA Managing Director Gary Baker comments on recent market disruptions and reactions.

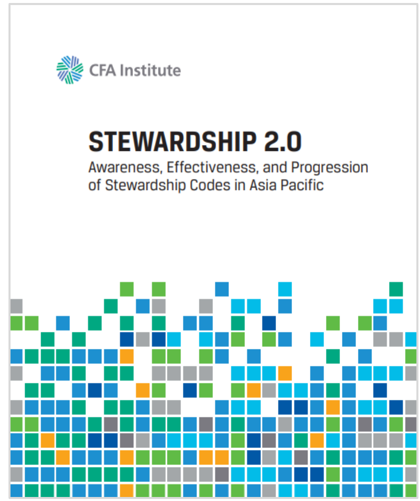
Financial Standard (AUS) (25 August) reported that CFA Institute is seeking feedback from the investment industry on a consultation paper for a proposed disclosure standard for ESG investments.

Wealth Management (20 August) reported that CFA Institute filed negative comments with the DOL over the ESG rule for 401(k) plans.

Financial Advisor Magazine (19 August) covered CFA Institute Managing Director Kurt Schacht's comments on SEC's use of fake Fiduciary Rule comments.

MARKET INTEGRITY & TRANSPARENCY

STEWARDSHIP 2.0 IN ASIA PACIFIC



Enhancing investor transparency and engagement: CFA Institute released a new report, *Stewardship 2.0: Awareness, Effectiveness, and Progression of Stewardship Codes in Asia Pacific*, in August that gauged the adherence to stewardship codes requiring institutional investors to be transparent about their investment processes in Australia, Hong Kong SAR, India, Japan, Malaysia, Singapore, South Korea, Taiwan, and Thailand. The report offers recommendations to increase the awareness and effectiveness of stewardship codes and provides insights from institutional investors to guide the development of future codes.

Our position: CFA Institute supports an outcomes-focused update of stewardship codes and encourages shareowners to participate in exercising their rights. Stewardship codes guide institutional investors and encourage a higher level of engagement with listed companies, such as voting their shares, in accordance with institutional investors' fiduciary duties. Our recommendations in revising and applying stewardship codes include maintaining flexibility as a comply-or-explain standard with sufficient monitoring. A need for global differences and leading from the top are also key best practices for establishing stewardship codes.

MARKET INTEGRITY & TRANSPARENCY

CREATING ESG DISCLOSURE STANDARDS FOR INVESTMENT PRODUCTS

New standards: In August, CFA Institute issued its *Consultation Paper on the Development of the CFA Institute ESG Disclosure Standards for Investment Products*, which aims to develop and publish a set of global standards for investment managers to communicate the environmental, social, and governance (ESG)–related features of their products to provide greater transparency and comparability for investors. The consultation paper asks for industry input on the initial draft of the ESG disclosure standards.

Disclosure and transparency: Importantly, CFA Institute is not seeking to define an ESG or sustainable investment product or strategy or compare different ESG-related investment approaches. Rather, the standard will establish disclosure requirements so that investors can more easily understand the features offered by a particular investment product and make comparisons among investment products.

Our ESG position: As stated in our policy paper, *Positions on Environmental, Social, and Governance Integration*, CFA Institute believes consideration of relevant and material ESG information and risks should be a fiduciary duty and integral in the analytical and investment decision-making process.

We need your input: Setting industry standards is integral to the mission of CFA Institute, and we encourage industry professionals and standard setters to provide their views to help shape the standard. Responses are due by 19 October and can be entered on our site.

MARKET INTEGRITY & TRANSPARENCY

WEIGHING IN ON EU ESG DISCLOSURES

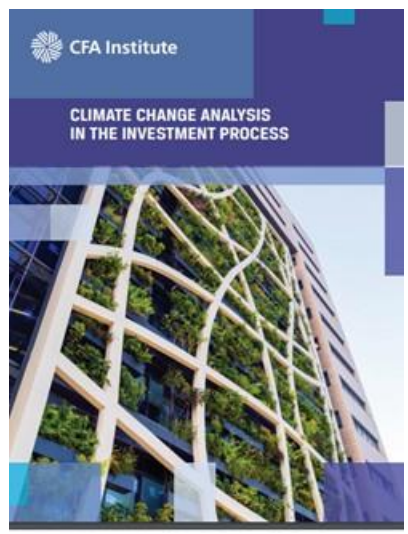
Response to the European Supervisory Authority's (ESA) proposal: On 1 September, CFA Institute responded to ESA's public consultation seeking input on proposed environmental, social, and governance (ESG) disclosure standards for financial market participants, advisers, and products.

Need for global standard: In our response, CFA Institute emphasized that the current ESG disclosure practices in the EU need improvement as the ESG data lack quality, comparability, and consistency for investors. To develop greater sustainability practices in the financial sector, we believe that a global standard is necessary to ensure that ESG data are comparable and audited.

Our position: Overall, we agree with the ESA's proposed template on the description of the factors that lead to adverse impact of the investment decisions made by financial market participants on sustainability factors. CFA Institute believes that their approach and indicators are appropriate, but these metrics should be periodically reviewed to meet investor expectations. The final regulatory technical standards are expected to be finalized by 30 December 2020, and the new Sustainable Finance Disclosures Regulation rules will enter into force on 10 March 2021.

INVESTOR PROTECTION

CFA INSTITUTE SHEDS LIGHT ON CLIMATE CHANGE ISSUES IN INVESTING



New report: CFA Institute provides an important and incisive examination of the issue of climate change in the financial industry in its new report, *Climate Change Analysis in the Investment Process*. The report highlights the physical and transition risks brought about by climate change, explores carbon markets, and presents current resources and best analysis practices available to investors concerning climate change.

Survey results: Based on a survey of CFA Institute members, the report brings to life the views of investment professionals on this all-important topic. Results show that about 75 percent of global C-level executives in the investment industry surveyed believe that climate change is an important issue, but only about 40 percent of survey respondents incorporate climate change information into their investment process.

Best practices: The report also includes a series of illustrative case studies from global investment management firms demonstrating best practices for fitting climate change analysis into the investment process. These case studies cover a diverse set of investment themes, such as carbon markets, quantitative analysis, and engagement around climate issues. The goal is to provide practical instruction and examples to guide organizations on how this crucial area can be incorporated into its investment process.

MARKET INTEGRITY & TRANSPARENCY

CFA INSTITUTE PUSHES BACK ON RELAXATION OF MIFID II

Disagree on EC rule reduction: On 10 September, CFA Institute provided comments on the recent European Commission proposed rules on investment research under the Markets in Financial Instruments Directive (MiFID) II regulatory framework. CFA Institute does not agree with the EC's proposed overall simplification and relaxation of rules, as it could negatively affect transparency and investor protection, and it may not work to improve investment research coverage. Evidence is not yet clear that the new rules on unbundling under MiFID II have directly caused the ongoing reduction of research coverage and quality, especially for small and midsize enterprises (SMEs).

Recommendations: CFA Institute believes that alternative measures could be put in place to stimulate investment research on SMEs, such as subsidizing research funding for this segment or focusing on the impact of large competitive organizations on the emergence of new independent research firms. Setting out clear disclosure rules to address conflicts of interest is another way to improve the dissemination of SME's research.

Our position: Overall, we argue that this is not the right time to lighten the rules on investment research as markets are still adjusting on the implementation of MiFID II requirements.

INVESTOR PROTECTION

REVISITING SHORT-TERMISM IN 2020

New report: In July, CFA Institute published *Short-termism Revisited,* which reexamines the important topic of short-termism, the focus on short-term results at the expense of long-term interests (first analyzed in 2006 in *Breaking the Short-term Cycle*). For this new report, CFA Institute convened an expert panel to evaluate both the improvements and remaining challenges related to short-termism and also provided recommendations for moving forward.

Recommendations: Many improvements in the short-termism and long-termism landscape have been made over the past 15 years, such as better engagement and communication between issuers and investors, but more work remains to be done. Recommendations include encouraging issuers and investors to focus on long-term strategy and agreed-upon metrics, simplifying executive compensation, and standardizing data around ESG sustainability.

High costs: For this report, CFA Institute partnered with renowned research firm, Fund Governance Analytics, for a quantitative analysis to better understand short-termism behaviors and affects. Interestingly, our research estimated that the agency costs (foregone earnings) of short-termism were $1.7 trillion over the 22-year period (1996–2018) covered by our analysis, or about $79.1 billion annually. We will have to wait and see if lessons have been learned by both issuers and investors, and if this agency cost of short-termism will mitigate over the long term.

MARKET INTEGRITY & TRANSPARENCY

IFRS CONSIDERING ACTION ON SUSTAINABILITY

New task force: As global demand for high quality and consistent sustainability reporting grows, the International Financial Reporting Standards (IFRS®) Foundation, a not-for-profit international organization responsible for developing high-quality global accounting standards and overseeing the International Accounting Standards Board (IASB), has created a task force to consider if, and how, the Foundation might engage on the issue of sustainability. Kurt Schacht, policy director at CFA Institute, who serves as a trustee on the Foundation noted, "Calls from a variety of global stakeholders including investors, corporate issuers, and market regulators asking the Foundation to help create a more coordinated approach have intensified in recent months."

Results coming: This swelling demand for a global set of standards in the sustainability area has prompted the IFRS task force to study an assortment of options. The Foundation is expected to announce within the coming weeks the results of the task force review, including a potential public consult seeking comment on a range of proposals and options for a more harmonized approach to sustainability reporting.

INVESTOR PROTECTION

A RESPONSE TO ESMA GUIDELINES ON LEVERAGE RISK

Responding to systemic risk: CFA Institute issued a response to the ESMA's public consultation on the proposed guidelines on the Alternative Investment Fund Managers Directive (AIFMD), which focuses on leverage-related systemic risk and leverage limits for Alternative Investment Funds (AIFs). CFA Institute has a long history of working on systemic risk in financial services, including our sponsorship of the Systemic Risk Council, a private sector body of experts committed to addressing regulatory and structural issues relating to global systemic risk.

Our position: CFA Institute believes a balance needs to be found between the industry and regulators when it comes to risk mitigation that may stifle innovation and unrestricted risky financial activities. We also feel that the systemic nature of the asset management sector does not bring about as many relevant risks as the banking sector. Nevertheless, it is important to monitor and control risk accumulation through leverage, and especially those organizations that wield leverage through the funds they manage.

ESMA support: We support the ESMA approach, which correctly identifies gross leverage as the main factor distinguishing the vast majority of funds from a very small minority of highly leveraged vehicles employing specific instruments, such as interest rate and foreign exchange derivatives. We would stress, however, that a blanketed approach to leverage restriction should be avoided as measures should be taken only if they are supported by a thorough assessment of firms' risk management systems and processes.

GLOBAL EVENTS & ACTIVITIES

KEY ENGAGEMENTS

Non-GAAP Financial Reporting, CFA Society of New York (8 September): Sandra Peters, senior head, Global Financial Reporting Policy, CFA Institute, participated in a discussion during the CFA Society of New York's event on Non-GAAP Financial Reporting, focused on the strengths and weaknesses of non-GAAP measures, how to analyze past and future corporate performance, and how to review new non-GAAP measures.

ESG Disclosure Standards for Investment Products initiative (25 August): Mary Leung, CFA, head of advocacy for Asia Pacific; Sara Cheng, senior director of capital markets policy for Asia Pacific; Piotr Zembrowski, CFA, manager of advocacy research and content for Asia Pacific; and Scott Lee, director of Asia Pacific Research Exchange, participated in ESG standards briefing meetings with the Hong Kong Exchanges and Clearing Limited, the Securities and Futures Commission (Hong Kong SAR), the Securities and Exchange Board of India, the Singapore Exchange, the Financial Services Agency (Japan), the Asia Securities Industry and Financial Markets Association, and KPMG.

Sustainable Finance Collective (28 August): Sivananth Ramachandran, CFA, director of capital market policy for India at CFA Institute, participated in two sessions of the Sustainable Finance Collaborative, a newly launched initiative of the Indian Ministry of Finance and the United Nations Development Programme. The sessions, on corporate financial disclosure and financial sector sustainability, were part of a three-day series of panel discussions with the objective of bringing together leading experts and organizations to boost the country's efforts to mobilize sustainable and green finance. The events were attended by Indian and global regulators, development agencies, investors, corporations, and ESG standard setters, including the Global Reporting Initiative, Sustainability Accounting Standards Board, and Climate Bonds Initiative.

UPCOMING EVENT

CFA Institute and the Systemic Risk Council Present

Ensuring Financial Stability: Relaunching the Reform Debate after Pandemic Dislocation

Hosted by Sir Paul Tucker, Chair, Systemic Risk Council

VIRTUAL EVENT

Wednesday, October 14, 2020

9:00 AM to 11:30 AM EDT