

October 31, 2006

Office of the Secretary of the Commonwealth
Attention: Proposed Regulations
Securities Division, Room 1701
One Ashburton Place
Boston, MA 02108

Re: Request for Exemption—Proposed Rule 12.205(9)(c)(15)

Dear Sir or Madam:

CFA Institute¹ is writing you in reference to your proposed regulations that would prohibit broker-dealer agents and investment adviser representatives registered in Massachusetts from using certain credentials to market their services and to exempt certain designations.

As discussed more fully below, the Chartered Financial Analyst (CFA[®]) designation is obtained only with the type of course, examinations and experience that appear to form the basis for implementation of these new regulations. We therefore respectfully request the Massachusetts Securities Division (Division) to exempt the CFA designation for purposes of proposed regulation 12.205(9)(c)(15).

Summary

CFA Institute administers and maintains the CFA examination and designation. It is composed of a rigorous series of three exams that must be taken over a minimum of two years. After passing all three levels of the CFA exam, an individual must meet certain experience requirements and agree to comply with a strict code of ethics and standards, in order to receive the CFA designation. This examination is widely accepted throughout the world as the pinnacle of competency achievement for investment professionals.

Moreover, most of the individual states have recognized the CFA designation as meeting their competency requirements, and thus exempt CFA charterholders from their licensing exam for those seeking to register as investment advisers and investment adviser representatives. (See www.nasaa.org/content/Files/65%2D66Adoption.pdf). Massachusetts is one of these states.

¹ With headquarters in Charlottesville, VA and regional offices in New York, Hong Kong and London, CFA Institute, formerly the Association for Investment Management and Research[®], is a global, non-profit professional association of more than 94,700 financial analysts, portfolio managers, and other investment professionals in more than 130 countries of which more than 74,600 are holders of the Chartered Financial Analyst[®] (CFA[®]) designation. The CFA Institute membership also includes 134 Member Societies and Chapters in 55 countries and territories.

Below we provide an overview of the CFA Program. Second, we discuss the CFA examination process and the substantive knowledge areas tested by the three levels of the exam. Third, we address the experience component of the CFA designation process. Finally, we discuss the emphasis on integrity required of all CFA charterholders through adherence to ongoing ethical and professional standards.

Discussion of CFA Examination Program

A. Overview of the CFA Program

The CFA Program, which is developed and administered by CFA Institute, seeks to represent to the investing public, employers, and fellow investment professionals that a holder of the CFA designation possesses the fundamental knowledge and commits to adhere to ethical standards necessary to practice in the investment and securities profession. Accordingly, in order to obtain the CFA designation, a candidate must pass a rigorous series of exams designed to test the CFA candidate on a broad spectrum of subjects that are essential to the competent and ethical practice of investment management activities. These subjects include:

- Ethical and professional standards;
- Economics;
- Financial statement analysis;
- Analysis of equity investments;
- Analysis of debt investments;
- Portfolio management;
- Analysis of derivatives;
- Quantitative methods;
- Corporate finance; and
- Analysis of alternative investments.

Today, the CFA designation is a credential recognized throughout the world as signifying the highest achievement in the investment profession. Since the first CFA designation was awarded in 1963, more than 82,868 professionals have become CFA charterholders.

Each year, the number of candidates who take the CFA exams continues to grow. Over 42,000 candidates from 125 countries enrolled for the June 2006 CFA Exam, and over 41,700 enrolled for the December 2006 Exam. In the United States alone, over 43,000 individuals have received the CFA designation. The dramatic growth in the number of candidates pays tribute to the value investment professionals place on the CFA Program and their desire to achieve and maintain the highest standards of professional excellence and integrity.

In order to be awarded the CFA designation, a candidate must fully satisfy the program's requirements in three primary areas. First, a candidate must demonstrate comprehensive knowledge of securities analysis and valuation, and investment and portfolio management by sequentially passing a series of rigorous examinations that are administered over a minimum of three years—the Level I, Level II and Level III examinations. Second, the candidate must have accrued at least four years of acceptable professional experience in financial analysis, investment management, securities

analysis and other similar professions. Third, a candidate must agree to comply with a stringent code of ethical and professional standards—the CFA Institute *Code of Ethics* and *Standards of Professional Conduct*.

B. CFA Examinations

(a) Competency

The CFA program is designed so that, by the time a charter is awarded, the CFA charterholder has not only mastered the basic competency areas, but has a substantial breadth of investment knowledge. Unlike many other designations, the CFA program is not solely academic. A candidate will not receive the CFA designation until he/she has at least three years of relevant experience in the investment profession. The exam's focus on practical applications of investment management and financial analysis, coupled with practical experience in these fields, allows the CFA charterholder to *apply* his/her education in a meaningful manner. Thus, the process of becoming a CFA charterholder demands a candidate demonstrate broad, substantive knowledge and understanding of all aspects of the investment profession.

(b) Requirements of the CFA Examination Program

To be awarded the CFA designation, a candidate must pass three comprehensive examinations – Level I, Level II and Level III. Each Level exam is administered once a year. Given the degree of difficulty of the exams, candidates do not always pass the exams in successive years. Examination pass rates have varied over time and across exam levels. For example, over the entire history of the examinations, the average pass rate has been 47% for Level I, 52% for Level II, and 68% for Level III. In 2006, the pass rate was 40% for Level I candidates, 48% for Level II candidates, and 76% for Level III candidates.

(i) Sitting for the Exam

To enroll and sit for the CFA exam, an applicant must, in addition to other requirements: (i) have a bachelor's degree or the equivalent in qualified investment work experience; and (ii) complete an CFA Institute professional-conduct inquiry form demonstrating that the individual understands, maintains, and adheres to the CFA Institute *Code* and *Standards* and that he/she has not been convicted of any felony or, within the last ten years, a misdemeanor for a crime of moral turpitude (e.g., lying, cheating, stealing).

Each exam is prepared at CFA Institute in conformity with industry testing standards. Exams are printed under secure conditions, sealed prior to delivery, and stored in a locked and access-controlled storage area until distributed to candidates at the exam. Exam site supervisors and proctors ensure the integrity of the testing process in accordance with the CFA Institute "Security Controls and Procedures" manual specifically prepared for the CFA Institute CFA Program by security experts.

(ii) Content – The Candidate's "Body of Knowledge"

All three levels of the CFA exam require the candidate to demonstrate a thorough understanding of, and the ability to apply, a substantial amount of information on a broad range of topics. Since the CFA curriculum is grounded in the practice of investment analysis, valuation, and management, CFA Institute periodically conducts a “job analysis” by surveying CFA charterholders throughout the world on the “elements of the body of investment knowledge” that are most important in their practice. These surveys contribute to the development and maintenance of the CFA “Candidate Body of Knowledge” (“CBOK[®]”) and help determine the appropriate emphasis each subject matter receives on the examination.

The CBOK is the basis of the CFA exam curriculum. Each of the three levels of the exam tests candidates on their knowledge of specific subjects contained within the CBOK. It is organized along functional lines to track changes in the investment decision-making process and is updated regularly.

The major functional areas of the CBOK are:

- ethical and professional standards;
- tools and inputs for investment valuation and management (investment tools);
- asset valuation; and
- portfolio management.

(iii) Selection of Questions

Questions for each CFA Level exam are written by a CFA Institute standing committee called the “Council of Examiners” (COE). The COE consists of prominent practitioners and academicians, all CFA charterholders. In writing questions, the COE uses learning outcome statements (“LOS”) developed by another CFA Institute standing committee, the “Candidate Curriculum Committee” (CCC). The CCC, also composed of CFA charterholders, selects the appropriate texts and readings to address the topics in the CBOK, which the candidate will use in studying for the exam. LOS are provided for each assigned reading and indicate the specificity and level of knowledge that is expected for each topic area. The COE writes the exam questions to test the specific “learning outcomes” designed for each reading.

(iv) Exam Preparation

In order to prepare for each level of the CFA exam, a candidate receives a Study Guide that provides basic information on the CFA program, organizes the assigned readings into separate “study sessions”, and provides the required reading list for the relevant level exam. Primary Readings are the core of the study program and form the basis for exam questions. For the 2006 exams, the required readings for Level I and Level II were assembled into self-contained volumes, allowing a “modular curriculum” approach for these levels (in lieu of Study Guides). LOS or “expected learning outcomes,” which indicate the level of knowledge a candidate should demonstrate with respect to each reading, as well as the relevant CBOK that the candidate is

expected to master remains an integral part of the exams at each level. Each level exam requires an average of over 250 hours of individual study time.

(v) *Grading*

The CFA Level I exam is a multiple-choice exam and is scored by computer. The format of both the Level II and Level III CFA exams consists of 50% “item set” questions and 50% essay/short answer questions that are assigned maximum point values based on the number of minutes allocated to the question. Item set questions are also scored by computer. The essay/short answer questions on both Level II and Level III exams are graded by a carefully selected group of approximately 300 CFA charterholders from around the world who are practitioners or academics. Each grader is assigned to a grading team that grades a single question which helps to ensure consistency in grading and allows each grader a greater degree of specialization.

Each exam question is graded in accordance with a guideline answer and grading key that are developed by the Council of Examiners and members of CFA Institute senior professional staff. Each grading team captain receives statistical reports during grading about the work of his/her team to ensure that grading is done consistently and in accordance with the grading key. Senior graders re-grade marginal exams in their entirety during the second week of grading.

The CFA Institute Board of Governors determines the “minimum passing score” (MPS) for each level of the exam. The goal of the Board of Governors in determining the appropriate MPS for each level is to maintain the integrity of the CFA charter. With that goal in mind, the Board considers, among other factors

- The top-scoring exam responses as an indication of the difficulty of the examinations;
- Recommendations from a panel of CFA charterholders who review the examinations and the quality of candidate responses (Level I only)
- Feedback from those involved in the grading process on the examinations and the quality of candidate responses; and
- Actual candidate responses in papers above and below the minimum passing scores (Levels II and III only).

Level I Examination – Knowledge and Comprehension

The CFA Level I exam is the foundation for the CFA program, focusing on ethical practices and the tools and concepts that apply to investment valuation and management. It also provides an overview of asset valuation and portfolio management. This six-hour exam concentrates on:

- ethical and professional standards;

- investment tools;
 - ♣ financial statement analysis
 - ♣ quantitative analysis/techniques
 - ♣ macro- and micro-economics
- corporate finance;
- asset valuation (equity, fixed income, derivatives, and alternative investments); and
- portfolio management.

Level II Examination – Financial Analysis and Application

The Level II CFA exam builds on the breadth of knowledge obtained from the Level I exam and emphasizes asset valuation, including applications of the tools and inputs (economics, financial statement analysis and quantitative techniques) to the practice of asset valuation. Specifically, the Level II CFA exam tests a candidate’s ability to:

- analyze and value debt, equity, and derivative securities and recommend those with the most (or least) attractive expected return/risk characteristics for purchase (or sale);
- apply a top-down valuation approach based on global trends, national economies, industry- and company-specific factors and individual assets characteristics;
- apply an alternative (bottom-up) valuation approach based on the identification of those companies and industries/sectors that are undervalued regardless of the macroeconomics forecast;
- use a variety of valuation techniques and the duPont approach to financial analysis;
- incorporate international factors in asset valuations; and
- apply a knowledge of applicable laws and regulations and the CFA Institute *Code* and *Standards* to recognize and avoid unprofessional practices and violations of standards where issues are not clear (e.g., conflicts of interest, compensation, inside information, corporate governance, proxies, and the “prudent expert rule”).

Level III Examination – Synthesis and Evaluation

The Level III CFA exam emphasizes portfolio management, including strategies for applying the tools and inputs in managing equity and fixed-income securities. Specifically, the Level III CFA exam tests a candidate’s ability to:

- develop suitable investment policies that meet the specific requirements and circumstances of different types of individual and institutional investors;
- incorporate domestic and international economic forecasts and market conditions into portfolio investment strategies;

- determine asset allocations that are consistent with investment policies and strategies;
- implement portfolio strategies that take into consideration the costs and benefits of timely execution of trades;
- monitor and evaluate portfolio performance and respond to change; and
- design and administer a program of professional and ethical standards within an organization.

Critical regulatory topics, such as fiduciary duty, misrepresentation, disclosure of conflicts, personal trading, insider trading, performance presentation, use of soft dollars, suitability of investments, supervisory responsibility and trade allocation are all tested repeatedly at each level of the CFA exam.

A Level I candidate is expected to demonstrate a thorough knowledge of these topics. Candidates at Level II are expected to differentiate between acceptable behavior in these subject areas and conduct that violates best practices. At Level III, candidates are expected to be able to critique and revise compliance guidelines and policy statements with regard to these subjects. By the time the candidate has completed the CFA Program, he or she is well versed in those subject areas and professional practices involved in the investment-decision making process that are subject to intense regulatory scrutiny.

C. Relevant Work Experience

Successfully completing all three levels of the CFA exam is a major part of achieving the CFA designation. However, to become a CFA charterholder, a candidate must also have four years of acceptable professional experience working in the investment decision-making process. This work may be accrued before or during the study and examination period or after completion of all three level exams. Moreover, work experience that will qualify for the eventual award of the CFA charter must consist of activities substantially related to the investment decision-making process, the supervision of those who engage in such activities, or the teaching of such activities.

D. Ethical and Professional Standards

High ethical and professional standards are the cornerstone of the CFA Program. Accordingly, they are tested at each level of the CFA examination. The Ethical and Professional Standards section of the CBOK in each Study Guide sets forth four separate topics that the candidate must master. In addition, each Study Guide for Level II and Level III exams devotes two study sessions solely to ethical and professional standards.

To reflect the importance that the CFA Program places on high ethical and professional standards, the Level I exam allocates 15% to Ethical and Professional Standards; and Level II and III exams each allocate 10%. In addition, candidate responses to the ethics questions are a material factor in the review of marginal examinations.

Moreover, each CFA candidate, prior to receiving the CFA designation, must:

- sign and submit a professional conduct statement;
- sign and submit a certification form agreeing to comply with the CFA Institute rules and regulations, and acknowledging the authority of the CFA Institute Professional Conduct Program to enforce the *Code of Ethics* and *Standards of Professional Conduct*; and
- exhibit a high degree of ethical and professional conduct.

Every year thereafter, each CFA charterholder and candidate must file a Professional Conduct Statement in which they renew their pledge to comply with the *Code* and *Standards* and voluntarily disclose any ethics-related complaints that may have been lodged against them. Each disclosure is reviewed independently and may result in an inquiry by the CFA Institute Professional Conduct Program. Sanctions entered against those candidates found to have violated the *Code* and *Standards* may include suspension or permanent dismissal from the CFA Study and Examination Program.

Conclusion

We understand that the purpose of proposed regulation 12.205(9)(c)(15) is to deter unscrupulous use of designations by entities to mislead and harm investors—particularly the senior population. We submit that those who have obtained the CFA designation not only have the requisite expertise and knowledge to serve this population, but also embody the high ethical standards in the investment industry that this regulation intends to foster. We therefore request the Division to exempt CFA charterholders under this regulation.

We appreciate the opportunity to provide you with this information on the CFA Program and your consideration of our request for exemption. If you have any questions, or need additional information, please do not hesitate to contact Linda Rittenhouse at 434.951.5333 or at linda.rittenhouse@cfainstitute.org.

Sincerely,

/s/Linda L. Rittenhouse
Linda L. Rittenhouse
Senior Policy Analyst