Our Shared Mission: Ensuring That Global Markets Work for Investors

"Our Shared Mission: Ensuring That Global Markets Work for Investors"

Opening Remarks
2011 Equity Markets Conference

Karrie McMillan
General Counsel
Investment Company Institute

December 6, 2011
New York Marriott Downtown
New York, NY

As Prepared for Delivery

Good morning, everyone. I'm Karrie McMillan, ICI's General Counsel, and it's my privilege to welcome you to our 2011 Equity Markets Conference.

Before I get into my remarks, I'd like to recognize the sponsors of this event: Bank of America Merrill Lynch, Investment Technology Group, Liquidnet, NASDAQ OMX, NYSE Euronext, and Rosenblatt Securities. Along with your participation and the hard work of ICI staff, these companies have made this conference possible. So we are grateful for their underwriting support and thank them for helping ICI continue its tradition of high-quality conference programming.

And we do have a high quality program ahead of us today. My colleague Ari Burstein has once again managed to sign up an excellent roster of speakers and panelists, and I am very much looking to all their insights.

But to start things off, I want to step back a bit and reflect on the significance of this event. In my mind, this is much more than just a gathering of smart people like yourselves—it's a conference that embodies a vital mission of the fund industry.

That mission is this: to ensure that global markets work as efficiently and as effectively as they can for investors. And this is a mission we all should share—buy side, sell side, and regulators.

So what's driving this mission?

For funds, the answer is clear. Funds are the gateway to the securities markets for tens of millions of Americans.

ICI members manage $12.5 trillion for 90 million shareholders. U.S. registered investment companies—mutual funds, exchange-traded funds, closed-end funds, and unit investment trusts—hold just over a quarter of all U.S. corporate equities.

Underlying those big numbers are some equally big principles.

One is that the relationship between funds and their investors extends well beyond simply treating customers nicely to keep their business. By law, funds have fiduciary responsibilities of loyalty and care toward their shareholders. That fiduciary obligation means that when funds go into the markets, they're driven to get the best execution possible for the benefit of shareholders.

So how do we go about this mission of ensuring that global markets work for investors? What do we need to do? I think you can

break it down to four key tasks:

- One, foster understanding of the markets, particularly from the buy-side's perspective;
- Two, improve the rules that govern the players in the markets;
- Three, avoid policy pitfalls; and
- Four, stay vigilant.

I'd like to take a moment to discuss each of these items. Right now, I think the second one—improving the rules—is especially on our minds with the impending rollout of the Volcker Rule. If regulators get that wrong, some very significant aspects of the market could go right off a cliff.

But before we even get into the rules, I think our mission begins with fostering understanding of the markets.

How are trading practices evolving? Do they benefit shareholders? Which market participants are affected by these changes? To ensure that global markets work for investors, you need a solid understanding of these developments.

As we'll discuss today, there are many places where we can work to deepen this kind of understanding. At ICI, one issue we're focused on intently is the ever-increasing globalization of our securities markets. Our last panel this afternoon will dive into this topic—I know there's always that fatigue that sets in at the end of a conference, but this panel is worth staying for.

At ICI, we have recently stepped up our efforts to address this globalization. In October, as I'm sure some of you have heard, we set up a new, London-based organization called ICI Global. This organization serves, among other things, as a conduit for an international dialogue around trading and market structure.

That kind of dialogue is critical. It enables us to help shape the rules, to improve them. And improving the rules is another key aspect of our mission.

Now, when I say "improving the rules," I'm not just talking about a job for regulators. Everyone in this room can provide input to help ensure that regulations are sensible and consistent; that they're harmonized as appropriate with the laws of other countries—and that they provide robust investor protections.

And, as I mentioned, we have to provide this input increasingly on a global basis. Earlier this year, for example, we at ICI gave a number of recommendations to the European Commission as it reforms its Markets in Financial Instruments Directive, or MiFID.

Our recommendations covered a wide range of issues, including automated and high-frequency trading, pre- and post-trade transparency, dark liquidity, and the need for a European consolidated tape.

Closer to home, there are plenty of proposals that we can improve. Let's look at a big one: the Volcker Rule. As you know, regulators will be accepting comments until mid-January on how to implement this very complex and controversial corner of the Dodd-Frank Act.

Now, the Volcker Rule is not directed at funds. But as investors, funds have good reason to worry about the market impact of its implementation.

One of our greatest concerns is that the proposed Volcker rules, as written, could impede the ability of market makers to operate in less liquid debt and over-the-counter markets. There's a very real risk that the Volcker rule will reduce liquidity in these markets, increase transaction costs, and, in the end, diminish returns to investors.

In fact, it's hard for me to imagine what the fixed income markets would look like if this rule were adopted as proposed. So I'm glad our first panel today will be spending some time exploring these challenging issues.

The Volcker framework was imposed by Congress, so the best we can do now is try to make sure that it works as well as possible.

But ensuring that global markets work for investors also can mean making sure some laws aren't adopted to begin with. I call this "avoiding policy pitfalls," and I'll mention one that's looming out there now—the potential imposition of financial transaction taxes.

Around the world, we see policymakers tempted to spring this tax on markets.

Here in the U.S., for example, members of Congress have introduced a bill that would place a tax of up to three basis points on the value of stock trades.

They call their bill the "Targeted Wall Street Trading Tax." But you can guess who also ends up in the crosshairs: investors. For now,

the bill would raise transaction costs for funds, costs that investors would bear. They'd also get taxed when they redeem their fund shares. So this tax would directly hit the returns of millions of American families saving to meet their goals for retirement, education, and other needs. Make no mistake—it will tax Main Street.

This tax will also hurt the broader economy. By reducing market efficiency and lowering investment returns, FTTs simply sap people's willingness to invest. And less investment means lower GDP in the long run.

It all sounds like quite the pitfall to me.

The last of my four dictates is to stay vigilant. Stay wary of the fact that some firms will chase profit in ways that work against investors.

The recent developments with Pipeline Trading Systems illustrate this point well.

This past October, Pipeline settled charges that it had failed to tell its dark pool customers that an affiliated broker-dealer filled the vast majority of its orders. According to the SEC, although Pipeline represented that all users of the dark pool were treated the same, it provided the affiliate with advantages over other users. It also failed in some cases to adequately protect customers' confidential trading information.

We'll have a robust discussion of these issues in our 10 o'clock panel on potential conflicts of interest. For me, the takeaway is vigilance. As I told this audience last year, funds must press their brokers and market centers for disclosure on order routing and execution. And while you can't always avoid bad actors, the vast majority of good firms can tell you information that will ultimately benefit investors.

The structure of our markets is under global regulatory review, while also changing dynamically as it rapidly innovates. So we've got our work cut out for us. I'll probably never stand at this podium with a big "mission accomplished" banner hanging up there behind me.

But that doesn't trouble me so much. If we relentlessly pursue our mission, investors will benefit and so will our businesses. Thank you.

Craig Donohue, chief executive officer of the CME Group, was scheduled to deliver our keynote this morning. Unfortunately, Craig was called away and can't be with us. Instead, it's our great pleasure to welcome Thomas LaSala, Managing Director and Chief Regulatory Officer of CME Group, to address us today.

CME's role in our conference reminds us that markets are not just global—they are interconnected.

Operating the world's largest futures platform, CME enables customers to manage the full range of risks, whether related to interest rates, equity indexes, foreign exchange, or commodities. The company managed an average 14.7 million contracts a day last quarter.

So Tom has quite the view of the interplay between markets. He's also well-suited to discuss how regulatory developments will ripple through those markets.

Tom came to CME through its 2008 merger with NYMEX, where he also had served as Chief Regulatory Officer. He joined NYMEX in 1984 as an analyst and director in market surveillance. In his current role, Tom is a director of the Futures Industry Association's Futures Services and Law and Compliance Divisions, and also serves on the Joint Compliance Committee of all of the U.S. futures exchanges.

Tom earned a bachelor's degree from Marist College in 1983, majoring in business administration with a concentration in finance and economics.

Ladies and gentlemen, Tom LaSala.

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.