

# INSIDE DEBT

PRODUCED BY REUTERS IN PARTNERSHIP WITH ICAP

Wednesday, March 24, 2010

## CHART OF THE DAY

### Euro/Dollar



An already weak euro fell to the day's low of \$1.3329, its lowest since early May 2009.

## TODAY'S TOP NEWS

- Euro slides on Portugal downgrade, Greek wrangling
- U.S. new homes sales fall, durable orders up in Feb
- Fed's Hoenig supports 'Volcker rule' limits on banks
- Financial reform tops Obama agenda post-healthcare
- Weak U.S. 5-yr debt sale intensifies supply worries
- Bank of America to offer home loan write-downs
- UK's Darling cuts debt forecast, sets election stage
- China official rejects U.S. complaints on currency

## ECON WATCH

FOR THURSDAY MARCH 25

ET	Indicators	Unit	Reuters	Prior
03:00	DE GfK consumer sentiment	ind	3.1	3.2
03:45	FR Consumer spending	mm %	0.3	-2.7
04:30	IT Business confidence	ind	84.5	84.0
05:00	EZ Money-M3 annual grwth	%	-0.1	0.1
05:00	EZ Money - Private loans	%	-0.4	-0.6
05:30	GB Retail sales mm	%	0.7	-1.8
05:30	GB Retail sales yy	%	3.2	0.9
08:30	US Initial Claims	k	450	457
08:30	US jobless contin claims	mln	4.55	4.579
19:30	JP CPI, core nationwide	%	-1.2	-1.3
19:30	JP CPI, core Tokyo	%	-1.7	-1.8
-	GR National Holiday			

### FACTBOX

#### House, Senate bills tighten swaps regulation

Over-the-counter derivatives would be brought under U.S. regulation in regulatory reform legislation pending in Congress. [For more please click here](#)

## MARKETS TODAY

**TODAY'S TOP STORY:** The euro tumbled to a 10-month low as European leaders wrangled on the eve of a summit over how to help debt-stricken Greece, while fellow euro zone weakling Portugal suffered a cut in its credit rating. [For more please click here](#)

**TREASURIES:** U.S. Treasuries fell pushing benchmark 10-year yields to the highest level in over one month, as strong economic data and weak demand in an auction of five-year notes left government debt out of favor.

- 10-yr notes fell 1-7/32 in price to yield 3.84 pct, the highest in over one month and up from 3.69 pct late Tuesday.
- 2-yr notes yielded 1.10 pct from a high yield of 1.00 pct in an auction of \$44 bln of the notes.
- 10-yr swap spread remained in negative territory for the second consecutive day.
- 5-yr notes fell 23/32 to yield 2.58 pct from 2.42 pct, while 30-yr bonds were 1-30/32 lower to yield 4.73 pct from 4.61 pct.
- 2-10's part of the yield curve steepened by about 8 bps to 274 bps.

**FOREX:** The U.S. dollar rose across the board, pushing the euro to a 10-mnth low after a rating downgrade for Portugal added to worries about debt levels and growth in the euro zone's smaller countries.

- The euro was last down 1.27 pct at \$1.3323. It was the biggest one-day move since Feb. 17.
- The dollar rose 1.92 pct to 92.16 yen after touching a session high of 92.23 yen. The greenback hit a two-week peak against the Swiss franc at 1.0716.
- The dollar index rose to its highest since May last year. It was last up 1.25 pct at 81.907.
- Sterling fell 1.02 pct to \$1.4882. Earlier it rose as high as \$1.5041.

**CORPORATES:** U.S. corporate bond markets were little changed after a month-long run as sovereign credit risk weighed on demand for corporate debt.

- Corporate credit spreads were little changed for the past four trading sessions after narrowing to about 168 bps, having traded as high as 191 bps in February.
- Wal-Mart Stores launched \$2 bln two-part debt sale.

**STOCKS:** U.S. stocks fell threatening to end a string of gains, after Fitch Ratings cut Portugal's credit rating on deficit concerns in the latest sign of worsening sovereign debt problems in Europe.

- Dow shed 0.48 pct to 10,836.23 S&P was down 0.55 pct to 1,167.77 and Nasdaq fell 0.68 pct to 2,398.76.
- Shares of Chevron fell 1.12 pct to \$73.93.
- BofA rose 2.57 pct to \$17.57. KBW bank index rose 0.42 pct.
- S&P financial index rose 0.19 pct, S&P energy index fell 0.66 pct.

**C & E:** Oil fell more than \$1 a barrel, weighed down by data showing a larger-than-expected rise in crude stocks and a stronger U.S. dollar.

- U.S. oil fell 1.87 pct to \$80.38 per barrel.
- Gold shed 1.43 pct \$1,085.85 per ounce.
- Reuters-Jefferies index was down 0.82 pct to 269.48.

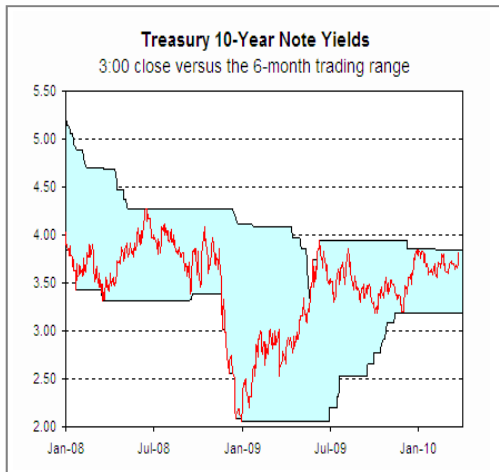
• [For MARKET SNAPSHOT click here](#)

• [For NEXT UP click here](#)

• [For DEEP DIVE click here](#)



MARKET SNAPSHOT as of 3:00 pm EST



**TREASURIES <5> <500>**

	BID	ASK	YIELD	CHANGE
1-Mo Bill	0.130	0.095	0.132	0.006
3-Mo Bill	0.140	0.130	0.142	0.007
6-Mo Bill	0.240	0.220	0.244	0.008
1-Year	0.403	0.400	0.409	0.023
2-Year	99.797	99.828	1.104	-0.125
3-Year	99.188	99.219	1.657	-0.324
5-Year	99.078	99.117	2.575	-0.707
7-Year	98.313	98.359	3.274	-0.961
10-Year	98.313	98.375	3.831	-1.148
30-Year	98.469	98.531	4.721	-1.797

**EQUITIES**

	INDEX	CHANGE
DJIA	10834.56	-54.57
NASDAQ	2399.37	-15.87
S&P 500	1167.42	-6.75

**OIL**

	PRICE	CHANGE
NYMEX	80.6	-1.3
BRENT	81.5	-0.5

**EURODOLLAR FUTURES**

	CLOSE	CHANGE
Apr-10	99.683	-0.003
Jun-10	99.610	-0.010
Sep-10	99.400	-0.035
Dec-10	99.090	-0.060

**REPURCHASE AGREEMENTS**

G/C		MORTGAGE REPOS	
O/N	0.230	O/N	0.250
2-Week	0.210	2-Week	0.240
1-Month	0.250	1-Month	0.270
3-Month	0.270	3-Month	0.300
AGENCY REPOS		i-REPO <sup>SM</sup> INDEX	
O/N	0.240	10:00 AM	0.170
2-Week	0.230	3:00 PM	0.168
1-Month	0.260		
3-Month	0.290		

**IR SWAPS <19901>**

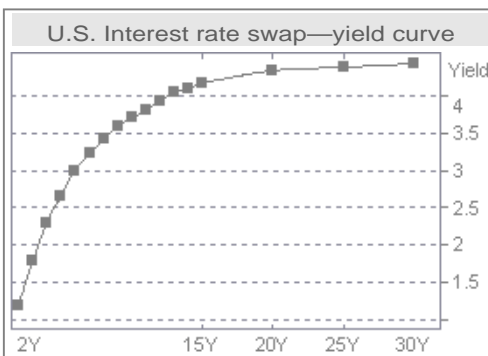
	SPREAD		RATE	
2-Year	9.00	13.00	1.19	1.21
3-Year	12.25	16.25	1.77	1.79
5-Year	10.25	14.25	2.67	2.67
7-Year	-3.00	1.00	3.24	3.23
10-Year	-10.25	-6.25	3.72	3.71
30-Year	-28.50	-24.50	4.43	4.41

**FUTURES**

	PRICE	CHANGE
CBOT 5 yr	115.73	-0.66
CBOT 10 yr	118.45	-0.31
CBOT 30 yr	119.19	-0.25

**EURODOLLAR DEPOSITS & OIS STRIPS (ASKED)**

	BID	ASK	BID	ASK
O/N	0.200	0.250	-	-
1-Month	0.220	0.280	0.187	0.197
3-Month	0.240	0.400	0.197	0.207
6-Month	0.350	0.450	0.235	0.245
12-Month	0.700	1.050	0.418	0.428



**CURRENCIES**

	BID	ASK
Euro	1.3335	1.3338
Sterling	1.4884	1.4890
JP Yen	92.07	92.10
Swiss Franc	1.0720	1.0724
Can Dollar	1.0241	1.0246
Mexico	12.5782	12.5838

**FED FUNDS NYFR<sup>SM</sup> - 10AM**

Open	0.1700	1m	0.2275
High	0.2400	3m	0.2794
Low	0.1200		

**ACTIVE FANNIE MAE AGENCIES**

TERM	COUPN	MATURITY	YIELD-SPREAD	YIELD
2-Year	1	12/04/2012	11 10	1.22
3-Year	1.625	15/04/2013	19 0	1.75
5-Year	2.875	09/02/2015	23.5 0	2.73
7-Year	5.125	18/10/2016	19 0	3.46
10-Year	-	-	- -	-
30-Year	6.625	15/11/2030	35.5 33.5	5.1

**ACTIVE FREDDIE MAC AGENCIES**

TERM	COUPN	MATURITY	YIELD-SPREAD	YIELD
2-Year	1.125	15/12/2011	-5 -7	1.05
3-Year	1.75	07/05/2013	21.5 19.5	1.86
5-Year	2.625	20/11/2014	13.5 0	2.63
7-Year	5.25	15/09/2016	14 11	3.41
10-Year	3.75	27/03/2019	21 20	4.04
30-Year	6.25	15/07/2032	42.75 39.75	5.15

**Active MBS 15YR**

	CPN	BID	ASK	YIELD
FNMA	4.0	101.1150	101.1210	3.659
FHLMC	4.0	101.1400	101.1400	3.586

**Active MBS 30YR**

	CPN	BID	ASK	YIELD
FNMA	4.5	100.1600	100.1600	4.360
FHLMC	4.5	100.1860	100.1920	4.345
GNMA	4.5	101.0600	101.0600	4.213

**Wrightson ICAP<sup>SM</sup> Chart of the Day**

**Nondefense Capital Goods Ex-Aircraft: Orders and Shipments**  
3-month moving averages in blns of dollars



## TODAY'S TOP NEWS

**Euro slides on Portugal downgrade, Greek wrangling**

The euro tumbled to a 10-month low as European leaders wrangled on the eve of a summit over how to help debt-stricken Greece, while fellow euro zone weakling Portugal suffered a cut in its credit rating.

The latest jitters to hit the common currency underlined the risk of market contagion if European Union leaders, meeting on Thursday and Friday, fail to agree on a credible financial safety net for Greece.

Diplomats said euro co-founders Germany and France were negotiating intensively on conditions for a last resort support mechanism for Greece, with Berlin demanding a central role for the IMF. European Commission President Jose Manuel Barroso appealed to euro zone leaders to find a fallback solution this week for Greece, whose huge budget deficit has prompted investors to dump its debt. A German government official said he did not expect any decisions on aid for Greece at the two-day Brussels summit but added that support for IMF involvement was growing among EU governments.

Fitch Ratings downgraded Portugal's sovereign debt rating by one notch to AA-, citing budgetary underperformance. The move put Fitch in between fellow credit watchdogs Moody's and S&P's, but had a stronger psychological impact due to the climate of uncertainty.

**Fed's Hoenig supports 'Volcker rule' limits on banks**

U.S. financial reform should include some form of the "Volcker rule," which would limit large financial firms' ability to engage in speculative trading, Thomas Hoenig, president of the Kansas City Federal Reserve Bank said.

Hoenig argued the country's mammoth investment conglomerates had not served the broader economy well.

Hoenig said some of the push toward deregulation during the 1990s had been detrimental to financial stability, and needed to be reversed.

In particular, he said big financial holding companies should not be allowed to trade for their own accounts, so-called proprietary trading. He said they should be forbidden from investing in or sponsoring their own hedge funds. He also stressed the need for greater transparency in derivatives markets, which many blame for bringing the global financial system to the brink of collapse in late 2008. He added that the implicit guarantee by government of the dominant banking interests gave them an unfair advantage in the market, including cheaper borrowing costs and higher credit ratings.

**Weak U.S. 5-yr debt sale intensifies supply worries**

A poor five-year debt sale stoked anxiety over investors' appetite for U.S. government securities as the U.S. Treasury Department sought cash to fund its massive deficit.

Perception of weak demand accelerated a sell-off in U.S. Treasuries, sending benchmark yields to their highest levels since early January. The five-year debt sale was sandwiched between Tuesday's \$44 billion two-year auction and Thursday's \$32 billion seven-year note sale. Overall bidding at the latest five-year auction was the lowest in six months. The auction's bid-to-cover ratio was 2.55, down from 2.75 at the February auction.

Indirect bidders which include foreign central banks bought only 39.7 percent of the five-year notes offered. This was the smallest percentage this group had purchased since July 2009.

A separate report showed, benchmarks on U.S. longer-term corporate borrowing costs fell due to appetite for higher-yielding assets and hedging on government and corporate bond supply.

**U.S. new homes sales fall, durable orders up in Feb**

Sales of newly built U.S. homes fell for a fourth straight month to a record low in February, but another rise in new orders for durable goods offered assurance that the economic recovery was on course.

Single-family home sales fell 2.2 percent to a 308,000 unit annual rate, the Commerce Department said, surprising markets that had expected a 320,000 unit pace.

In a second report, the department said new orders for long-lasting manufactured goods increased 0.5 percent in February, rising for the third straight month, and January's figures were revised higher to show a 3.9 percent increase. Markets had expected orders to gain 0.7 percent in February from the previously reported 2.6 percent rise. Durable goods inventories rose 0.3 percent, the biggest gain since December 2008, after rising 0.1 percent in January.

Last month, new durable goods orders excluding transportation rose 0.9 percent in February after falling 0.6 percent the previous month.

Non-defense capital goods orders excluding aircraft rebounded 1.1 percent last month after a 3.9 percent fall in January.

**Financial reform tops Obama agenda post-healthcare**

Financial regulation reform vaulted to the top of President Barack Obama's post-healthcare agenda, with both Democrats and Republicans upbeat about passing legislation soon.

After a meeting with Obama, Democratic Senate Banking Committee Chairman Christopher Dodd said the president wants results soon from Congress on proposals to tighten U.S. government oversight of banks and capital market.

Obama, at the meeting with Dodd and Frank, reiterated a commitment to working to strengthen reforms and to fight attempts to weaken a proposal to set up a new government watchdog for financial consumers, a White House official said.

Separately, U.S. financial reform should require the reporting of all trades in the \$450 trillion swaps market and mandatory clearing for some standardized swaps, a key Senate committee chairman said.

Meanwhile, U.S. Deputy Treasury Secretary Neal Wolin sharply criticized the U.S. Chamber of Commerce for launching what he called a "misleading" \$3 million advertising campaign against financial reform bills championed by the Obama administration.

**Bank of America to offer home loan writedowns**

Under pressure from Massachusetts Attorney General Martha Coakley, Bank of America said it would offer about \$3 billion in loan forgiveness to about 45,000 troubled homeowners.

Bank of America pledged to offer an "earned principal forgiveness" of up to 30 percent for homeowners nationwide who owe more than 120 percent of the value of their home.

The plan, to begin in May, is among the first by a U.S. mortgage lender that takes a systematic approach to reducing mortgage principal to tackle the thorny issue of preventing foreclosures when home values drop well below the amount owed.

The forgiveness would be offered in two stages for the riskiest loans, including subprime loans and loans which offered borrowers multiple options for how much to pay each month. Ineligible are 30-year fixed rate loans. The lender will first offer an interest-free forbearance of principal that the homeowner can turn into forgiven principal annually over five years, provided they stay current on their payments. The forgiveness can allow a homeowner to bring the loan value back down to 100 percent of the home's value over five years.



## TODAY'S TOP NEWS

**UK's Darling cuts debt forecast, sets election stage**

Britain's Labour government set the stage for the coming election with a budget that promised a 2.5 billion pounds (\$3.75 billion) package to boost growth, higher taxes for the well-off and lower borrowing than predicted only three months ago.

Labour has said it would halve the deficit in four years but fiscal tightening would only start next year as the recovery remains too fragile. The Conservatives said that is too late and they would act this year.

Darling said he would scrap duty on house purchase on homes worth less than 250,000 pounds for first-time buyers but pay for that with a one percentage point rise in duty to 5 percent for houses worth more than 1 million pounds. He said he was able to revise down his forecasts for the budget deficit in the current and next fiscal year. Public sector net borrowing in 2009/10, Darling said, would come in at 166.5 billion pounds, or 11.8 percent of GDP, compared with a December pre-budget report forecast of 177.6 billion pounds. In 2010/11, borrowing is expected to come in at 163 billion pounds versus 176 billion previously forecast. Future years have also been revised down.

**China official rejects U.S. complaints on currency**

A Chinese official said China would reform its currency policy gradually and keep the exchange rate stable, rejecting U.S. calls for it to rise more quickly.

Chinese Vice Commerce Minister Zhong Shan, in Washington at a time of heightened U.S.-China trade and political tensions, told business leaders that changing the exchange rate was not the way to fix a huge bilateral trade imbalance.

A growing number of U.S. economists estimate China's currency is undervalued by up to 40 percent. They say that gives China an unfair price advantage in international trade, takes jobs away from other countries and adds to global financial distortions. The economists' views on the currency have been taken up by U.S. lawmakers, who are crafting legislation that would slap import duties on Chinese goods to offset the price advantage China enjoys from suppressing the value of its currency.

## NEXT UP

**POLL-Rates and liquidity drain to drive bond yield rise**

A slow economic recovery and the prospect of rises in official interest rates will ensure major government bond yields rise back to where they were before the financial crisis, a Reuters poll showed on Wednesday.

Median forecasts from nearly 100 bond strategists showed 10-year bond yields in the U.S. and Britain surging far past 4 percent in a year's time, reflecting the risk in their status as the most fiscally overburdened of "AAA"-rated nations.

The 10-year Bund yield is expected to reach 3.88 percent in 12 months, compared to 4.23 percent and 4.5 percent for the equivalent U.S. and British bonds, according to the poll taken between last Friday and Wednesday.

With the latest Reuters polls showing a roughly 60 percent chance of interest rate hikes by end-2010 from the U.S., euro zone and British central banks, forecasters upgraded their benchmark bond yield predictions from January's poll.

The Fed and BoE became major players in the U.S. and UK bond markets last year through their QE programs, which further depressed bond yields.

But their effect on yields is on the wane -- the Fed's scheme to

**Dealmakers meet to sort \$26 bln Dubai World debt**

Bankers met in Dubai to hammer out a \$26 billion debt plan with state-owned Dubai World as a repayment deadline loomed, adding to pressure on the glitzy emirate to settle the conglomerate's debt.

Core creditors representing 97 banks met to finalise months of talks on how Dubai World can restructure the debt, about a quarter of Dubai's estimated total debt of \$101 billion.

Before the meeting ended at around 1600 GMT, a spokeswoman for Dubai World said the talks were "very positive".

Sources earlier told Reuters that former British minister Shriti Vadera had also been in Dubai for weeks, despatched quietly by the UK government after British banks raised concerns about the process to London. The sources said Vadera, an abrasive character who was nicknamed "Gordon Brown's representative on Earth" for her long and close alliance with him as finance and prime minister, had played a key role in hammering out the debt proposal. The Dubai government later said it had invited Vadera to provide strategic advice.

**Japan approves record \$1 trln budget amid debt concerns**

Japan's parliament approved a record \$1 trillion budget for the fiscal year from April, with an all-time high of 44.3 trillion yen (\$490 billion) in new bond issuance underlining its public finance troubles. The government is resisting pressure to spend more on stimulating its domestic economy, saying it should now manage to avoid sinking back into recession. But Prime Minister Yukio Hatoyama said it should still be ready to act if necessary given lingering downside risks such as unemployment. Finance Minister Naoto Kan said it was too early to mention additional stimulus spending but that the government may consider tapping reserves set aside in 2010/11 budget to support a fragile economy without boosting fresh debt issuance. Fitch, Moody's and S&P's have all warned Japan it faces a ratings downgrade, which could raise the borrowing costs for the most indebted of the industrialised nations and rattle investors who are already nervous about Greece's debt and the sovereign risk facing other European nations.

buy \$300 billion in Treasuries finished in October and the BoE has left its QE program at 200 billion pounds (\$300 billion), although policymakers have reserved the right to extend it.

The spread between British 10-year gilts and Bunds, which hit zero last March as the BoE started QE, will grow to 85 basis points in three months, be at 80 in six months but fall to 63 in 12 months, the poll showed.

With central banks gradually withdrawing the vast sums of liquidity from money markets, forecasters predicted 3-month money rates to rise steeply in the U.S., euro zone and Britain.

The growing scarcity of this ultra-cheap money, coupled with a good chance of an interest rate hike later in the year, will push the 3-month euro LIBOR rate to 173 basis points in a year's time, according to the poll. This would be more than double the current level of 58 basis points.

Median forecasts from 32 responses to an extra question showed a 10 percent chance that the UK would lose its coveted "AAA" debt rating over the next year.

Fears that an election due by June would fail to produce a government with a strong mandate to cut Britain's vast budget deficit have hit sterling and caused gilts to underperform Bunds in recent months.



## DEEP DIVE Commentary and Analysis

**FACTBOX-House, Senate bills tighten swaps regulation**

Over-the-counter derivatives would be brought under U.S. regulation in regulatory reform legislation pending in Congress.

The House passed its version of the bill last fall. In April, the Senate may debate a bill written by Banking Committee chairman Chris Dodd. The Senate Agriculture Committee is also preparing a bill dealing with derivatives, but has not yet revealed its draft.

While having many similarities, the House and Dodd bills differ on when swaps would be required to go through central clearing and on margin requirements for customized swaps.

Here are highlights of the bills:

**CLEARING AND TRADING OF SWAPS ON EXCHANGES**

Dodd: "Standardized" swaps must go through clearinghouses, which would set margin requirements and guarantee payment. Noncash collateral would be allowed. Clearinghouses could propose to regulators the swaps they would handle; CFTC and SEC can require particular swaps or group, category, type or class of swaps to go through clearing.

If a swap is cleared, trading will move onto regulated exchanges or electronic platforms.

Regulators can exempt a swap from mandatory clearing and on-exchange trading if one party is not a dealer or major swap participant or is not eligible for clearinghouse membership.

House: If a clearinghouse will accept it, a swap will go through clearing. CFTC and SEC review and decide if a swap or a group, category, type or class of swaps must go through clearing. Clearinghouses can propose swaps for clearing.

Clearing is not required for swaps where one party is not a swap dealer or major swap participant, uses swaps to hedge "commercial risk, including operating or balance sheet risk," and tells regulators how it meets obligations associated with non-cleared swaps.

Swaps that go through clearing must trade on regulated exchanges or electronic platforms.

**CUSTOM SWAPS**

Dodd: Deals in custom swaps must be reported to trade repositories or to regulators. "Substantially higher" capital requirements for swaps that do not go through clearing.

Regulators will set margin requirements for swaps that are not cleared; may allow exemptions if one party is not a dealer or major swaps participant, uses the swap "as part of an effective hedge" and is "predominantly engaged in activities that are not financial in nature."

House: Custom swaps are allowed. Swaps that are not accepted for clearing must be reported to a repository or to regulators.

**CLEARINGHOUSES**

Dodd: CFTC and SEC would regulate clearinghouses; would consult with Federal Reserve. "Fair and open" access to membership would be required and boards must include market participants.

House: CFTC and SEC regulate clearinghouses. Boards must include market participants.

**REGULATION OF DEALERS AND MAJOR SWAP PARTICIPANTS**

Dodd and House each say swaps dealers and major swaps participants must register with SEC or CFTC, which would set capital, margin, recordkeeping, business conduct and reporting rules in most cases. Financial regulators would set minimum margin and capital standards for bank swap dealers and major

swap participants.

**DEFINING MAJOR SWAP PARTICIPANTS**

Dodd: Entities that are not dealers and that maintain substantial positions in outstanding swaps, excluding positions held primarily for hedging, reducing, or otherwise mitigating commercial risk or "whose failure to perform under the terms of its swaps would cause significant credit losses to its swap counterparties."

House: Entities that are not dealers and that maintain "a substantial net position in outstanding swaps, excluding positions held primarily for hedging, reducing and otherwise mitigating its commercial risk, including operating and balance sheet risk" and whose outstanding swaps "create substantial net counterparty exposure among the aggregate of its counterparties that could expose those counterparties to significant credit losses."

**POSITION LIMITS**

Dodd and House bill say CFTC could set position limits on swaps that affect trading on regulated markets. It also could set aggregate limits across all markets and on swaps that affect prices.

**ANALYSIS-Dodd bill takes pass on key broker reforms**

By Helen Kearney

As Senator Christopher Dodd's financial regulatory reform bill heads to the full Senate, brokerages for now have escaped tougher regulation thanks largely to fierce lobbying by insurers.

A bill approved by the Senate Banking Committee on Tuesday took a pass on two big issues affecting financial advisers -- a uniform fiduciary standard for all professionals advising investors and rules that mandate brokerage customers take disputes to an industry arbitration panel.

While the terms of the legislation are likely to change during debate by the full Senate and when Rep. Barney Frank's House Financial Services Committee weighs in, both issues for now will only be the subject of further study.

"The provision for another study is not warranted or wanted," said Knut Rostad, chairman of the lobbying group Committee for the Fiduciary Standard.

Rostad, who is also regulatory and compliance officer at Falls Church, Virginia, investment advisory firm Rembert Pendleton Jackson, said he was disappointed Dodd's committee only recommended that the Securities and Exchange Commission conduct a one-year study of the impact of a common fiduciary standard.

"We're worried that by postponing action for one or two years, it will be very difficult to bring it back," he said.

Rostad contends that committee members were swayed by aggressive lobbying by the insurance industry, which claimed a fiduciary standard would mean brokers could no longer charge commissions or recommend proprietary products -- both of which could hurt sales of insurance products like annuities.

Financial advisers currently must abide by the fiduciary standard under the Investment Advisers Act of 1940, which requires them to act in the best interests of their clients.

Series 7-licensed registered representatives, stockbrokers who charge clients on a commission basis, by comparison must ensure that the products they recommend are "suitable."

The issue has been muddied in recent years by a number of advisers who obtained both licenses, meaning they can act as an adviser with a fiduciary responsibility in some situations, or as a registered rep under the less strict suitability standard.

Further clouding the situation, almost every Wall Street firm now refers to its brokers as advisers, even though many of them are



## DEEP DIVE Commentary and Analysis

bound by the suitability standard.

A 2007 Rand Corp study revealed most clients do not understand the distinction between the two standards.

The fight for a common standard is far from over, said Neil Simon, a lobbyist for the Investment Adviser Association. The trade group intends to lobby members of the Senate and hopes the committee's bill will be amended.

Simon points to a provision in the House bill that gives the SEC authority to extend the fiduciary duty to brokers.

"I'm hopeful (the House version) will pass," he said.

The Securities Industry and Financial Markets Association, the brokerage industry's main lobbying group, agrees there is a need for a uniform standard. It objected, though, to Dodd's proposal to subject brokers to all provisions of the '40 Act.

"We believe this is the best way to protect investors and end the patchwork system that currently exists," a SIFMA spokesman said.

Investor groups had hoped that Dodd's regulatory reforms also

would tackle mandatory arbitration. As a matter of course, brokerage customers must agree to take any dispute to a FINRA arbitration panel rather than go through the court system.

Critics complain that the Financial Industry Regulatory Authority is controlled by Wall Street and historically has favored brokerages.

The Dodd bill delegates a decision on mandatory arbitration to the SEC and sets no deadline.

"We do not believe this needs to be studied any further," said Brian Smiley, a former president of investor lobbying group the Public Investors Arbitration Association and a member of its board. "We believe the law should make an arbitration forum available for those who want it, but the court system should also be available."

The Arbitration Fairness Act of 2009, introduced in the House 13 months ago, bans mandatory arbitration clauses in consumer disputes. The legislation appears to have stalled, Smiley said.

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(Compiled by Anil Kumar, Pronita Naidu and Mowna Ravikumar in Bangalore)

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