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January 16, 2008

IOSCO Issues Final Report on Soft Commission Arrangements for Collective Investment Schemes

[22130]

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TO: EQUITY MARKETS ADVISORY COMMITTEE No. 2-08
INTERNATIONAL COMMITTEE No. 3-08
INVESTMENT ADVISERS COMMITTEE No. 1-08
SEC RULES COMMITTEE No. 5-08 RE: IOSCO ISSUES FINAL REPORT ON SOFT COMMISSION ARRANGEMENTS FOR COLLECTIVE INVESTMENT SCHEMES

The Technical Committee of the International Organization of Securities Commissions ("IOSCO") has issued its final report on Soft Commission Arrangements for Collective Investment Schemes (the "Report"). [1] In November 2006, IOSCO released a Consultation Report on Soft Commissions (the "Consultation"). [2] Fifteen organizations, including the Institute, submitted comments on the Consultation. No significant changes were made in the Report as a result of the comments. A summary of the comments is included as an appendix to the Report.

In the Report, IOSCO concluded that it was not appropriate at this time to develop general principles regarding soft commission arrangements because relevant law in many jurisdictions was changing. Instead, the Report identifies key issues related to soft commissions and includes the results of a survey regarding the soft commission regulatory regimes of 19 IOSCO member organizations that participate in IOSCO's Standing Committee on Investment Management ("SC5"). SC5 will monitor regulatory developments related to soft commission arrangements over the next two years to determine whether or how general principles can be developed, including whether it can develop a common list of goods and services that may be purchased using soft commissions and a common approach to periodic disclosure regarding soft commission arrangements.

While the Report notes that most jurisdictions have no legal definition for soft commissions, soft commission arrangements are commonly understood to be an arrangement in which a fund operator receives a benefit in connection with a fund's payment of commissions on fund portfolio securities transactions. Many jurisdictions surveyed specifically limit by law or regulation the benefits that may be obtained with soft commissions, however several jurisdictions surveyed do not have any specific limitations. The Report explicitly recognizes that each IOSCO member must choose its own approach to limiting the benefits that fund operators may receive from soft commission arrangements.

The primary conflict of interest identified in the Report is the possible incentive for a fund operator to generate portfolio securities transactions for a fund to increase soft commission benefits to the operator. The Report also notes that soft commission arrangements may provide incentives for fund operators to direct fund brokerage based on the benefits provided to the operators instead of the most favorable execution for the fund. The Report recognizes that soft commission arrangements can provide benefits to fund investors provided that conflicts of interest are adequately addressed.

Susan Olson
Senior Counsel - International Affairs

endnotes

[1] Final Report – Soft Commission Arrangements for Collective Investment Schemes, Report of the Technical Committee of IOSCO (Nov. 2006), available at http://www.iosco.org//library/pubdocs/pdf/IOSCOPD255.pdf.

[2]

For a summary of the consultation, see Memorandum 20721 to Equity Markets Advisory Committee No. 28-06, International Committee No. 31-06, Investment Advisers Committee No. 8-06 and SEC Rules Committee No. 56-06, dated December 22, 2006. The consultation is available online at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD227.pdf.

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