

MEMO# 22953

October 2, 2008

Institute Comment Letter on SEC Proposed Soft Dollar Guidance

[22953]

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TO: CHIEF COMPLIANCE OFFICER COMMITTEE No. 14-08
CLOSED-END INVESTMENT COMPANY MEMBERS No. 49-08
COMPLIANCE MEMBERS No. 52-08
EQUITY MARKETS ADVISORY COMMITTEE No. 52-08
FIXED-INCOME ADVISORY COMMITTEE No. 29-08
INTERNATIONAL MEMBERS No. 15-08
SEC RULES MEMBERS No. 112-08 RE: INSTITUTE COMMENT LETTER ON SEC PROPOSED
SOFT DOLLAR GUIDANCE

As we previously informed you, the Securities and Exchange Commission has proposed guidance for boards of directors of registered investment companies to assist them in fulfilling their fiduciary responsibilities with respect to overseeing the trading of portfolio securities. [\[1\]](#) The Proposed Guidance focuses on the role of the board in overseeing the best execution obligations of the investment adviser in connection with soft dollar arrangements. The Commission requested general and specific comments on the Proposed Guidance. The Commission also solicited comments on whether to propose new disclosure requirements for investment advisers to fund shareholders and other investment advisory clients addressing the use of client commission arrangements. The Institute's comment letter is attached and summarized below.

The Institute's Comment Letter

The Institute's letter states that it supports the goal of the Commission's proposed guidance – to provide assistance to fund boards of directors regarding their duties with respect to investment adviser portfolio trading practices. The letter explains that the

Institute has three concerns with respect to the Proposed Guidance.

First, the letter states that despite the Commission's statement that it did not seek to impose new or additional requirements on directors in this area, certain aspects of the Proposed Guidance could be interpreted to impose additional responsibilities on fund boards, some of which go beyond boards' traditional oversight role. The Proposed Guidance states, among other things, that directors should "scrutinize the payment of transaction costs" and "demand" certain information. These directives appear to prescribe, rather than suggest for consideration, a specific list of tasks for directors, some of which are more consistent with board micromanagement than with traditional oversight. The letter also expresses the Institute's concern with the "checklist" approach of the Proposed Guidance, noting that the "suggested" factors to be considered are likely to become de facto required. The letter recommends that any final guidance reiterate throughout the Commission's intention to provide "guidance for fund directors to consider" in performing their responsibilities, and that the guidance clarify that the role of directors is to evaluate the adviser's policies and procedures, and to periodically review compliance with such policies and procedures, rather than to make specific findings about individual transactions.

Second, the letter explains that certain language in the Proposed Guidance, and the overall tone of the Guidance itself, may create an impression that certain portfolio trading practices, particularly soft dollar practices, are per se unsuitable for funds, and that fund boards should therefore prohibit such practices. The letter urges the Commission to present a more balanced discussion of these issues in its final guidance.

Finally, the letter expresses the Institute's concern that the Proposed Guidance appears to articulate a new standard for compliance with Section 28(e) of the Securities Exchange Act of 1934, at least with respect to registered investment companies. Section 28(e) explicitly permits an adviser to consider the value of soft dollar benefits to all accounts for which it exercises investment discretion. The Proposed Guidance, on the other hand, suggests that directors have an obligation to undertake a fund-specific analysis of soft dollar arrangements. In suggesting that fund directors must conduct such an analysis, the Commission appears to be imposing restrictions on the availability of the safe harbor for advisers to registered investment companies. The letter states that the Commission may not retract Section 28(e) through guidance. Directors' fiduciary obligations to act in the best interests of the fund and its shareholders can and should be met not by scrutinizing individual transactions, but by considering whether, on the whole, the soft dollar services acquired by the adviser are in the best interests of the fund.

In response to the Commission's request for comments on whether to require additional disclosures to fund shareholders and investment advisory clients regarding the use of client commission arrangements, the letter states that while the Institute supports disclosure of useful and relevant information to fund investors, we do not believe that additional disclosure is warranted at this time.

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[Attachment](#)

endnotes

[\[1\]](#) See Commission Guidance Regarding the Duties and Responsibilities of Investment Company Boards of Directors with Respect to Investment Adviser Portfolio Trading Practices, SEC Release Nos. 34-58624, IC-28345 (July 30, 2008), 73 Fed. Reg. 45646 (Aug. 6, 2008) (“Proposed Guidance”).

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