

MEMO# 19405

November 28, 2005

ICI COMMENT LETTER ON PROPOSED SEC SOFT DOLLAR GUIDANCE

©2005 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. [19405] November 28, 2005 TO: BOARD OF GOVERNORS No. 58-05 CLOSED-END INVESTMENT COMPANY MEMBERS No. 61-05 EQUITY MARKETS ADVISORY COMMITTEE No. 41-05 INVESTMENT COMPANY DIRECTORS No. 27-05 INVESTMENT ADVISER MEMBERS No. 23-05 SEC RULES MEMBERS No. 120-05 SMALL FUNDS MEMBERS No. 94-05 RE: ICI COMMENT LETTER ON PROPOSED SEC SOFT DOLLAR GUIDANCE

The Institute has filed a comment letter on the Securities and Exchange Commission's proposed interpretive guidance concerning the use of soft dollars under Section 28(e) of the Securities Exchange Act of 1934. A copy of the letter is attached and is briefly summarized below. The letter recognizes that the use of soft dollars by investment advisers raises complex policy and practical issues that have been the subject of widespread debate and divergent opinions for many years. The letter refers to the potential benefits of soft dollar arrangements to investors and also acknowledges the conflict of interest concerns that have led many in the mutual fund industry – including independent fund directors – to recommend that soft dollar practices be curtailed. It mentions the ICI's 2003 recommendations for tightening restrictions on soft dollars, including the recommendation to prohibit the use of soft dollars to pay for third-party research. Given that the SEC has decided not to distinguish between proprietary and third-party research, the ICI's comments address those issues raised by the guidance in the form proposed by the SEC. The letter observes that, based on the proposed interpretation, it appears that the SEC has concluded that the Section 28(e) safe harbor and related guidance remain an acceptable way to preserve the benefits of "client commission arrangements" for investors while subjecting these arrangements to appropriate safeguards. It expresses support for the proposed guidance, subject to the following comments on specific issues:

- The SEC should take steps to level the playing field by prohibiting the use of soft dollars outside of the Section 28(e) safe harbor by all investment advisers, regardless of the type of client account involved. This change will ensure that all advisers treat investors equitably in connection with the adviser's use of brokerage, and that broker-dealers will not have financial incentives to favor hedge fund and other advisers who are permitted to use soft dollars outside the safe harbor.
- The SEC should modify the proposed guidance to:
 - o Exclude from the safe harbor publications that are marketed to the general public.
 - o Permit money managers to treat order management systems and proxy voting services as mixed use items in appropriate circumstances.
- The SEC should clarify that the proposed guidance concerning commission-sharing arrangements does not place any affirmative obligations on money managers with respect to the responsibilities of introducing brokers under the guidance and applicable law, and should ensure that any responsibilities placed

on brokers are appropriate and workable. • The SEC should make clear that any final guidance applies on a prospective basis, and should provide a one-year transition period for money managers to unwind or modify, as necessary, existing soft dollar arrangements and to use credits earned under existing arrangements. Elizabeth Krentzman General Counsel Attachment (in .pdf format) Note: Not all recipients receive the attachment. To obtain a copy of the attachment, please visit our members website (<http://members.ici.org>) and search for memo 19405, or call the ICI Library at (202) 326-8304 and request the attachment for memo 19405.

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.