



October 1, 2008

Florence E. Harmon
Acting Secretary
Securities and Exchange Commission
100 F Street NE
Washington, D.C. 20549

**Re: Commission Guidance Regarding the Duties and Responsibilities
of Investment Company Boards of Directors with Respect to
Investment Adviser Portfolio Trading Practices (Release No. 34-
58264, File No. S7-22-08)**

Dear Ms. Harmon:

The Securities Industry and Financial Markets Association (“SIFMA”)¹ appreciates the opportunity to comment on proposed Commission guidance to Investment Company Board of Directors regarding oversight of fund advisers portfolio trading practices, including client commission and commission sharing arrangements.

INTRODUCTION

Given that mutual fund shares are a prominent holding of tens of millions of American households, providing fund directors with appropriate guidance for overseeing the activities of fund investment advisers is certainly an important undertaking. Therefore, SIFMA welcomes guidance that will enhance the ability of fund directors and advisers to fulfill their fiduciary duty to fund shareholders. However, we believe that the tone and focus of the proposed guidance in numerous respects fails to fully take into account many of the very positive developments that have taken place in the institutional brokerage marketplace in which fund advisers operate. These developments include technologically advanced alternative trading systems, declining commission rates, and the enhanced ability to enter into arrangements that better allow for allocation of commissions between execution costs and research and brokerage services. All of these help assure that client commission and similar arrangements better serve fund investors. The Commission has acknowledged these positive developments and in fact its 2006

¹ SIFMA brings together the shared interests of more than 650 securities firms, banks and asset managers. SIFMA’s mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services and create efficiencies for member firms, while preserving and enhancing the public’s trust and confidence in the markets and the industry. SIFMA works to represent its members’ interests locally and globally. It has offices in New York, Washington, D.C., and London, and its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong.

Interpretive Release on Section 28(e)² (“the 2006 Release”) was a major catalyst for some of these developments.

In that regard, at a recent SIFMA Institutional Brokerage Conference, SEC Division of Investment Management Director Andrew Donohue in discussing these developments stated that:

“...Other implications of the dramatic changes we are seeing appear to me to be very positive and are presenting market participants with some tremendous benefits. For example, client commission arrangements and commission sharing arrangements are allowing advisers to choose brokers solely on the basis of execution performance, while obtaining research from a number of other providers. Also the use of technology-driven trading mechanisms has led to an overall improvement in the efficiency of institutional trading. For example, algorithms help find the most efficient venues for executing different types of orders, and dark pools, particularly block crossing systems, allow buyers and sellers to find each other while avoiding costs that might arise from information leakage. In general, we are seeing lower transaction costs of large orders and, as I mentioned, commissions are overall becoming significantly lower...”³

In light of these positive developments we do not believe that the proposing release presents a properly balanced view of the current environment or of the positive contribution made by the 2006 interpretive guidance, including clarification that it applies to both proprietary and third-party research. In fact, the continuing references to “soft dollars” in the proposing release obfuscates the clarifications that were provided in the 2006 guidance. We are particularly concerned that the proposing release’s unwarranted negative connotations regarding portfolio trading practices and the scope of the inquiry that fund directors may conclude they must undertake, as reflected on pages 29-31 of the proposing release, will discourage directors from supporting beneficial arrangements, or fund advisers from pursuing them.

In sum, we believe that the proposed guidance does not set a proper context or perspective from which client commission and similar arrangements relating to portfolio trading practices should be evaluated. We discuss these below.

CONFLICTS OF INTEREST

SIFMA agrees that there are potential conflicts of interest inherent in a fund adviser’s use of fund commissions, as there are in numerous other aspects of the securities business. SIFMA also agrees that fund directors have a role to play in helping assure that conflicts are managed in a way that protects fund shareholders. However, we

² Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934. Exchange Act Release No. 54165 (July 18, 2006).

³ Remarks Before SIFMA Institutional Brokerage Conference, June 4, 2008.

believe that the proposing release's discussion regarding conflicts of interest is not reasonably balanced or characterizes certain activities as questionable or conflicts that are consistent with existing law, such as the ability to obtain research that generally benefits the investment selection process, rather than requiring allocation to particular accounts.

It is noteworthy that the proposing release contains no discussion of countervailing forces which tend to mitigate conflicts in a fund adviser's use of client commissions. One of the most important mitigating factors is that the bulk of an adviser's compensation comes from asset based fees so that the adviser has a major incentive to use client commissions to obtain research and brokerage services to enhance the net asset value of the fund to the mutual benefit of the fund shareholders and the adviser. Additionally, the ability to obtain research and brokerage services pursuant to Section 28(e) compliant client commission arrangements may also have a positive impact on the level of management fees – also to the benefit of fund shareholders. We would recommend that as part of a fund board's review and approval of management fees they obtain adviser input on the extent to which the receipt of research and brokerage services impacts the level of such fees.

Included in the proposing release's description of various conflict of interest is the following statement:

“...The availability of soft dollar benefits that an adviser may receive from fund brokerage commissions creates an incentive for an adviser to use broker-dealers on the basis of their research services provided to the adviser rather than the quality of execution provided in connection with fund transactions...”⁴

We find this statement both puzzling and to a degree ironic. It implies that research services and quality execution are “either/or” concepts, when in fact, the use of beneficial research is an important component of a quality execution in its broadest sense. Additionally, to the extent the Commission is construing quality of execution more narrowly, the concept of “paying up” for research services is specifically embraced by Section 28(e) of the Securities Exchange Act of 1934. Furthermore, and most significantly, the updated interpretive guidance which the Commission adopted in its 2006 release on Section 28(e) largely eliminated any potential source of conflict by modifying earlier interpretive guidance that had required research services to be obtained only from broker-dealers who were involved in “effecting the transaction.” This gave rise to the development of client commission arrangements and commission sharing arrangements which Division of Investment Management Director Donohue stated at the SIFMA Institutional Brokerage Conference “are allowing advisers to choose brokers solely on the basis of execution performance, while obtaining research from a number of other providers.”

⁴ Proposing release at p. 24.

FIDUCIARY DUTY

It is a given that brokerage commissions are a fund asset and therefore a potential conflict of interest exists when fund advisers utilize such commissions to obtain research and brokerage services. Clearly, in reviewing and approving such arrangements, fund directors have a fiduciary duty to satisfy themselves that these arrangements and the potential conflicts they pose are managed in a way that serves the best interest of the fund and its shareholders.

We submit that it is also a given that as a fund asset, it is perfectly appropriate for fund advisers to seek to maximize the value of that asset by utilizing commissions to obtain important research and brokerage services which have the potential to enhance investment performance and execution quality for the benefit of the fund. We believe that the proposed guidance should also emphasize the positive aspects of this use of fund assets so that fund advisers and directors do not conclude that they are placing themselves at greater risk in entering into or approving such arrangements, even when they clearly benefit the fund and its shareholders.

FOCUS OF DIRECTOR REVIEW

A recent telephone survey conducted at the request of the Commission in conjunction with its summary prospectus proposal reflects that by a wide margin fund investment performance was the information that fund investors most looked for when reading a prospectus.⁵ To put this in perspective, 50 percent of survey respondents cited investment performance whereas only 10 percent cited cost information. Since investment performance appears to be what investors care most about, it is surprising that the proposed guidance makes no reference to it. We believe that investment performance should also be considered by fund directors in helping to determine whether fund commissions are being utilized in a manner that benefits the fund. Good performance relative to market conditions and similar types of funds would not excuse advisers placing their interests above those of the fund. However, good performance may help demonstrate the value of research and brokerage products and services obtained with fund commissions and the fund adviser's effective use of those products and services. We also respectfully suggest that investment performance, which is a value concept, may be as useful a barometer for evaluating execution quality as applying commission rates or measuring implicit costs, which the Commission has noted are difficult to quantify.⁶

CONCLUSION

We appreciate the Commission's efforts to provide guidance to fund boards on the oversight of an adviser's use of fund brokerage commissions. However, as stated in

⁵ Abt. SRBI Mandatory Disclosure Documents Telephone Survey, p. 61 (July 30, 2008)

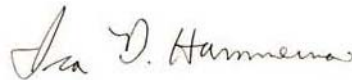
⁶ Investment Company Act Release No. 26313 (December 18, 2003)

this letter, we believe that the context within which these activities are evaluated should be set forth in a less pejorative and more balanced manner. Indeed, fund brokerage commissions can be a powerful tool for helping a fund adviser obtain valuable services that enhance investment performance and their usage in that manner needs to be encouraged. There should be a recognition in the guidance, similar to pronouncements in other SEC releases, underscoring the important and vital role that research of all kinds provides to the investment process, leading to more efficient markets and better performance. Therefore, fund advisers and boards should not be placed in a position where they believe they are at greater risk if they enter into or approve arrangements that they truly believe are beneficial to fund shareholders.

We also believe that positive developments such as the evolvement of client commission arrangements and commission sharing arrangements, which have been facilitated by the Commission's excellent 2006 interpretive release, have further mitigated potential conflicts regarding the use of fund brokerage commissions by fund advisers.

If you have any questions regarding the contents of this letter or related matters, please contact the undersigned at (202) 962-7300.

Sincerely,

A handwritten signature in dark ink, appearing to read "Ira D. Hammerman". The signature is fluid and cursive, with the first name "Ira" being more prominent.

Ira D. Hammerman
Senior Managing Director and
General Counsel

CC: Luis A. Aguilar, Commissioner
Kathleen L. Casey, Commissioner
Robert Colby, Deputy Director, Division of Market Regulation
Christopher Cox, Chairman
Andrew Donohue, Director, Division of Investment Management
Troy A. Paredes, Commissioner
Elisse B. Walter, Commissioner