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December 13, 2005

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
100 F Street N.E.
Washington, D.C. 20549

Re: Proposed Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934 (File Number S7-09-05)

Members of the Commission:

On behalf of the Committee on Federal Regulation of Securities of the Section of Business Law of the American Bar Association (the "Committee"), we are writing to express our views on proposed Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934, as amended (the "1934 Act") issued by the Securities and Exchange Commission ("Commission").[1] This letter was drafted by a task force of members of the Committee whose names are set forth below, and the members are available to discuss the matters discussed herein with the Commission and its staff.

The comments expressed in this letter represent the views of the Committee only and have not been approved by the American Bar Association's House of Delegates or Board of Governors and therefore do not represent the official position of the ABA. In addition, they do not represent the position of the ABA Section of Business Law, nor do they necessarily reflect the views of all members of the Committee on every comment herein

[1] Securities Exchange Act Release No. 52635 (October 19, 2005) (the "Release").

As a preliminary matter, we commend the Commission and its staff for taking the initiative to clarify the circumstances under which money managers fall within the "safe harbor" provided by Section 28(e) when using client commissions to purchase "brokerage and research services".

Despite the Commission's past guidance, designed to define the scope of the safe harbor, there is still some uncertainty among money managers and broker-dealers who provide brokerage and research services. In addition to providing guidance to market participants, this additional guidance will benefit independent directors of registered investment companies, who appreciate clear guidance on how they can best fulfill their fiduciary responsibilities in overseeing the use of fund commissions to pay for brokerage and research services.

Process of Publishing Proposed Guidance

We commend the Commission for seeking public comment prior to issuing its final guidance on the Section 28(e) safe harbor. This process affords investment advisers and other money managers, broker-dealers, fund directors and others the welcome opportunity to identify areas of uncertainty or problematic issues before the guidance has been formalized.

Reasonableness of Commissions in Relation to Value of Brokerage and Research Services

The Commission has sought comment on whether its proposed guidance is adequate, or whether it should provide additional guidance concerning specific products and services. We suggest that the Commission provide greater detail as to how its guidance might be applied. That is, while the Release sharpens the focus of whether particular research or brokerage services fall inside or outside of the safe harbor, further guidance would be helpful. For example, should the Commission determine to permit certain mass market publications (*i.e.*, publications that are widely circulated to the general public and intended for a broad public audience) to be eligible for the safe harbor, we believe that it would be helpful to clarify the circumstances when such publications would be eligible.

We note at page 28 of the Release, the Commission states that "certain financial newsletters and trade journals. . .could be eligible research services if they relate to the subject matter of the statute." Question 9 also asks whether mass-marketed publications should be eligible for the safe-harbor protection of Section 28(e). *See also* discussion of NASD Recommendations with respect to newspapers, at page 18. The thrust of the discussion seems to suggest that it would be appropriate to distinguish mass-media publications from more narrowly focused publications, such as newsletters and trade

journals. In Section 28(e)(3)(B) of the Exchange Act, Congress stated that research services includes "analyses and reports concerning issuers, industries, securities, economic factors and trends, portfolio strategy, and the the performance of accounts. . . ." Accordingly, the legal standard in Section 28(e) is one of substantive content, not size of circulation. The Committee respectfully urges the Commission not to focus on whether a publication has a broad circulation, but on whether its substantive content is in furtherance of assisting money managers in making informed investment decisions.

The Committee appreciates the Commission's efforts to provide certainty regarding whether certain mixed use products and services, such as order management systems, are eligible brokerage services under Section 28(e). We are concerned, however, that the proposed "temporal standard" is at odds with the language of Section 28(e)(1) that a manager evaluate the value of brokerage and research services provided by a broker-dealer in light of either a particular transaction or the manager's overall responsibilities with respect to the accounts over which the manager has investment discretion. In other words, a service should not be evaluated in terms of when it is provided (*e.g.*, at the time an order is sent or at the conclusion of clearance and settlement), but in light of whether the service provides value to a manager in making an investment decision (*e.g.*, on-going market color and indications of interest that help a money manager assess whether and when to execute a trade for an account).

The Committee urges the Commission to provide clear guidance about how the safe harbor applies to correspondent arrangements, to provide certainty to the money managers and broker-dealers who structure those arrangements in order to fit within Section 28(e). In particular, guidance is needed regarding how the Commission's four proposed elements would apply in circumstances when a money manager provides orders to the clearing broker for execution, clearance and settlement, and the introducing broker is not notified of a trade until after execution.

Standards of Review by Investment Company Directors

The Release addresses issues that arise under Section 28(e) of the 1934 Act, which will be of particular help to money managers and broker-dealers. The Commission recognizes the role that the boards of directors of investment companies have in overseeing the companies' brokerage practices.[2] We believe it would be useful to the independent directors of investment companies if the Commission were to use the Release as an occasion to provide more specific guidance on both the scope of, and how directors can fulfill, their fiduciary duty under the Investment Company Act of 1940.

[2] "The directors of an investment company have a continuing fiduciary duty to oversee the company's brokerage practices." *See* Release at footnote 5.

Because commissions paid in exchange for research and brokerage services are fund assets, investment company directors must evaluate whether the fund investment advisers are using those assets in an appropriate manner. In addition, investment company directors consider the benefits to an investment adviser of receiving brokerage and research paid for with brokerage commissions when they consider the annual renewal of the adviser's contract. Yet, little, if any, guidance exists to help directors understand the standard of review that they should apply in evaluating research and brokerage services in relation to commissions paid by their funds.

We suggest that the Commission provide guidance under the Investment Company Act of 1940 to clarify that investment company directors are not required to substitute their own judgment or conduct a *de novo* review of the basis for the investment adviser's good faith determination that the amount of commissions was reasonable in relation to the value of brokerage and research services provided. It would also be constructive for the Commission to provide guidance with respect to the information and level of detail that (a) fund advisers should provide to fund boards, and (b) fund directors should review in evaluating arrangements that involve research and brokerage services in exchange for commissions.

Documentation

The Release highlights the type of documentation that would be appropriate for money managers to maintain to justify their determinations as to the reasonableness of the commissions paid in relation to the value of research and brokerage services received. We suggest that the Commission provide guidance on whether and to what extent investment company directors can rely on this documentation, or a summary of such documentation, in fulfilling their oversight responsibilities.

Conclusion

While we have not attempted to address every point on which the Commission has solicited public comment, we have attempted to raise some issues that we believe merit further consideration by the Commission. In particular, we strongly note the importance of clear guidance to provide certainty to money managers, fund directors, and broker-dealers. Members of the Committee, its Subcommittee on Investment Companies and Investment Advisers, its Subcommittee on Market Regulation, and the Drafting Committee are available to discuss these comments. If you believe that such discussions would be helpful, please contact the undersigned.

Respectfully submitted,

Committee on Federal Regulation of Securities

/s/ Dixie L. Johnson

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