



December 22, 2006

Matt Daigler
Office of the Chief Counsel
Division of Market Regulation
The Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Dear Matt,

At our conference call with you, the Chief Counsel and other colleagues on the 30th November, the Chief Counsel indicated that she would prefer us to submit queries in writing. We requested queries from our member firms on the issue of Rule 15a in the context of foreign regulated firms producing eligible research, and have included a summary of these queries below.

For the benefit of your colleagues' information, EuroIRP is the European trade association for independent research firms, which seeks to: enhance the awareness and reputation of independent research; work with regulators and investors to promote the awareness and acceptance of payment structures; improve the regulatory and fiscal environment in which independent research firms operate.

We are grateful for the opportunity to submit these queries and look forward to hearing from you.

Kind regards,

Nick Paulson-Ellis

EuroIRP Member queries for the Securities and Exchange Commission

The objective of these queries is to obtain an understanding of the Securities and Exchange Commission's (the "Commission") interpretation of Rule 15a-6 in the context of foreign regulated firms producing eligible research, as defined in Section 28(e), as a core activity, for distribution to major US institutional investors ("MUSII").

Specifically the foreign regulated firms being considered, are regulated in their local jurisdictions to provide investment advice, including research. The production of research is the core business activity and as such these firms are referred to as independent research providers. Section 28(e) refers to them as "third party" producers of research. They may have some or no capability to "execute" transactions, however, this is incidental to their core business activity.

Whether or not they have this capability it is understood that all such parties are considered by the Commission to fall within the definition of a foreign broker dealer ("FBD") as defined within 15a-6. This is based upon an assessment that they are inducing or attempting to induce transactions as a result of submitting research reports and have an understanding that they will be remunerated by receiving a proportion of commission paid by the fund manager for resulting transactions, whether they execute the transaction or not .

In Europe, the arrangements between the fund manager (mainly themselves regulated) and the executing broker are documented in a "commission sharing agreement" ("Agreement"). This agreement is normally initiated by the fund manager. Consequently, the fund manager retains control upon broker and third party research selection and the monetary value they attach to research. The Agreement clarifies the roles and responsibilities of the parties and can include provisions fulfilling fiduciary and other regulatory obligations, including that the executing broker must provide best execution.

Specifically the interpretation and practical application of 15-6(a) (2) (ii)-+ and (iv) and 15-6(a)(3) are relevant to this analysis.

The Application of 15-6(a) (2) – Gratuitous Research

Considering 15-6(a) (2) first. This section allows the submission of gratuitous research reports subject to the following four conditions:-

- i. The research reports may not recommend the use of the FBD to effect trades in any security;
- ii. The FBD cannot initiate contact to follow up on the research reports;
- iii. If the FBD is “associated” with an SEC-registered broker-dealer (“USRBD”), then any trades with the recipients of the research in the securities the subject of the research must be effected through the USRBD; and
- iv. The FBD cannot provide research pursuant to any implied understanding that the USMII receiving the research will in turn direct commission income to the FBD (i.e. there may not be a “soft dollar” arrangement).

There is no further discussion on (i) and (iii).

With reference to the restrictions in (ii) and (iv) above, this precludes the initiation of contact with MUSIIs to follow up on the research. In the Nine Firms no Action Letter dated April 9, 1997, footnote 6, the commission’s staff clarified that 15-6(a) (2) (ii) would not prohibit a foreign broker-dealer from initiating follow-up contacts with MUSIIs to which it has furnished research reports, if such follow-up contacts occur in the context of a relationship between a foreign broker-dealer and a US intermediary broker dealer under the Rule. This refers to the “chaperoning arrangements” in 15-6(a)(3). It also prevents the entering into of Agreements between the USRBD selected by the money manager (who are also MUSIIs).

The existing rules, and their subsequent interpretation, require that follow up by means of telephone calls and other contacts and specifically Agreements can only operate where chaperoning arrangements are in place. This approach does not seem consistent with section 28(e) recognition of the value of independent third party research to money managers and the emphasis on their fiduciary responsibilities. A fundamental issue here is that chaperoning arrangements are entered into at the initiation of the FBD whereas the commission sharing arrangements are initiated by the money managers in pursuance of their fiduciary and regulatory, including best execution, obligations. The need for chaperoning arrangements exerts a pressure for the money manager to utilise the broker with whom the FBD has its chaperoning arrangements, although we appreciate that they cannot be directed to do so. This arrangement echoes the notion of inappropriate “directed commission” arrangements which the Commission is correctly seeking to guard against. Regarding MUSIIs, by definition professional, often regulated organisations managing a significant amount of assets, the lack of the ability for the FBD not to follow up quality independent research and subsequently not to be in a position to put in place an Agreement to receive a fair remuneration for any resulting purchases or sales seems an unnecessary layer of regulatory protection and may restrict access to quality research.

A relaxation of 15-6(a) (2) (ii) and (iv) in the circumstances indicated would, we believe, be in the best interests of all parties including, most importantly the ultimate underlying investor.

Q: Would the Commission consider relaxing 15-6(a) (2) (ii) and (iv) where dealings involve MUSIs and regulated independent research providers?

Q: Would this analysis alter if the executing broker, issuing the contract note and maintaining transaction records was itself a US registered broker dealer without formal chaperoning arrangements being in place?

Q: Would this analysis alter if the FBD was a registered SEC investment adviser and/or the securities were foreign securities?

The Application of 15-6(a) (3) – Chaperoning Arrangements

If these arguments are not persuasive, in the alternative we consider the requirements of 15a-6(3), the “chaperoning” requirements together with the requirements under 28(e) as they relate to dealings involving MUSIIs. In theory the arrangements could be initiated by the MUSII money manager although in practice, given the responsibilities undertaken by the USRBD selected, is more likely to be limited in number and at the initiation of the FBD. Inevitable conflicts arise in establishing chaperoning arrangements with good quality brokers who themselves produce a competing research product which do not seem in the best interests of the MUSII fund manager and the ultimate investor.

Listed below are all the elements required to comply with both of these rules, as interpreted. It is our view that all these elements could be fulfilled, in practice, under a single agreement dealing with both the chaperoning and commission share arrangements.

- 1) the execution of all transactions have be to effected through the USRBD;
- 2) the USRBD must maintain books and records;
- 3) the USRBD must confirm the transaction i.e. in its own name as principal or agent;
- 4) the USRBD must be responsible for clearing and settlement;
- 5) the investor is a MUSII;
- 6) the FBD and its employees consent to the service of process in the US;
- 7) foreign associated persons visiting the US can make contacts with MUSII up to 30 days per annum;
- 8) The USRBD pays the FBD directly for research. This can be at the direction of the money manager;
- 9) The USRBD ensures that the research is “eligible research” in accordance with 28e;
- 10) The USRBD develops and maintains procedures so that research payments are documented and paid for promptly.

Q: Is this the correct interpretation of the requirements relating to 15a-6(3) and 28(e)?

Q. For the avoidance of doubt, provided all the other requirements in 15a-6(3) are fulfilled, please confirm that the FBD is exclusively responsible for the content of each research report. This seems consistent with the provision in 15a-6(3) (iii) B whereby oral communication between the FBD and a MUSII may occur directly without the involvement and vetting of the “chaperone”. In addition, visits to a MUSII, again without the specific involvement of the “chaperone”, for up to 30 days per annum are permitted in accordance with Nine Firms No Action Letter referred to above. The “chaperone” should therefore concern themselves with ensuring that distribution of the research is only to MUSIIs, the research constitutes “eligible research” as defined in 28(e) and have access to the reports in the event of enquiry, but do not otherwise need to take responsibility for the contents of the research produced by a FBD.