



December 14, 2018

The Honorable Walter Jay Clayton  
Chairman  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

Re: Timing and Substantive Concerns Related to No-Action Relief for Dealing Commissions

Dear Chairman Clayton:

The Asset Management Group (the “**AMG**”) of the Securities Industry and Financial Markets Association (“**SIFMA**”)<sup>1</sup> appreciates the continued dialogue with the Securities and Exchange Commission (“**SEC**”) staff regarding our members’ concerns related to the cross-border implementation of Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (“**MiFID II**”).

We understand and recognize broader industry concerns related to ongoing regulatory requirements resulting from MiFID II, and believe that investors would be best served if asset managers were able to choose a payment arrangement for investment research that makes sense based on the individual circumstances. Currently managers may only pay cash to U.S. broker-dealers for research if they are required to do so by MiFID II or equivalent regulation. Even this exception will only continue to be an option if the SEC or its staff extends its temporary relief for payments for research from all ‘institutional investors’ through a formal rulemaking, interpretation or guidance, unless such broker-dealers elect to register as investment advisers. However, regardless of how the SEC chooses to proceed, our immediate and perhaps more pressing concern relates to the temporary nature of the dealer’s no-action relief letter that was issued by the staff last

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<sup>1</sup> SIFMA AMG is the voice for the buy side within the securities industry and broader financial markets, which serves millions of individual and institutional investors as they save for retirement, education, emergencies, and other investment needs and goals. The AMG’s members represent U.S. asset management firms whose combined assets under management exceed \$40 trillion. The clients of AMG member firms include, among others, registered investment companies, separate accounts, ERISA plans, and state and local government pension funds. Our members represent a significant and representative cross section of the registered open-end investment companies that are the subject of the Proposal.

fall.<sup>2</sup> We believe it is critical for the staff to provide clarity quickly regarding whether it plans to issue extended and/or permanent relief. As discussed in our meeting earlier this fall, should the SEC decide not to extend the relief, industry participants will need time to implement the changes necessary to meet regulatory requirements currently stayed by the SEC's temporary relief.

## Background

For many years, it has been common practice globally for asset managers to pay broker-dealers a single commission-based payment in exchange for research and brokerage in connection with the execution of a trade. Because no compensation is provided specifically for research, in the US this approach results in the research not being deemed "investment advice," and thus does not require that the broker-dealer be registered as an investment adviser.<sup>3</sup> However, under EU law, MiFID II now requires that asset managers who obtain research from broker-dealers pay for research with their own funds and/or through a client-funded research payment account ("**RPA**") alongside a separate payment for brokerage services. MiFID II also precludes asset managers and broker-dealers from structuring around this restriction by having a broker-dealer provide research for free to asset managers, as MiFID II deems this practice to be an illegal inducement.

Many asset managers that are subject to MiFID II seek to invest in markets where research coverage is provided by U.S. broker-dealers. However, absent SEC relief, MiFID II requirements would preclude an asset manager subject to MiFID II from using commission-based payments to acquire the research from U.S. broker-dealers and/or accepting "free" research from U.S. broker-dealers. At the same time, U.S. law prevents broker-dealers from accepting cash payments for research without registering with the SEC as investment advisers, which many are reluctant to do for legitimate business reasons.<sup>4</sup> Absent a solution, global asset managers with affiliates subject to MiFID II will not be able to benefit from research provided from broker-dealers registered with the SEC (regardless of whether they are in the U.S. or offshore).

In recognition of these issues, the staff issued three no-action letters on October 26, 2017.<sup>5</sup> The *SIFMA Letter* was time limited in nature, providing that, for thirty months from the implementation date of MiFID II, or January 3, 2018, U.S. broker-dealers may accept a specific payment for research alongside the brokerage fees without the research being deemed "investment advice." The expiration of the temporary no-action relief on or about July of 2020 will subject broker-dealers to potential immediate SEC enforcement action absent registration with the SEC as

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<sup>2</sup> *Securities Industry and Financial Markets Association*, SEC Staff No-Action Letter (pub. avail. Oct. 26, 2017) ("*SIFMA Letter*").

<sup>3</sup> Section 202(a)(11) of the Investment Advisers Act of 1940.

<sup>4</sup> *SIFMA Letter*, *supra* note 2.

<sup>5</sup> SEC Press Release: SEC Announces Measures to Facilitate Cross-Border Implementation of the European Union's MiFID II's Research Provisions (Oct. 26, 2017), *available at* <https://www.sec.gov/news/press-release/2017-200-0>.

an investment adviser, as the relief does not provide there will be any designated transition period post-expiration.

### **Harm to Markets without Clarity**

It is currently unclear whether the staff plans to extend or make permanent the temporary no-action relief or potentially extend the relief beyond its current reach. In the event the staff does not extend the relief, U.S. broker-dealers will be unable to accept cash payments unless/until they register as investment advisers. As a result, asset managers may have challenges acquiring research on behalf of clients globally, including U.S. clients. For example, many global asset managers have investment operations in the EU serving MiFID clients who wish to invest in U.S. markets. Without the current relief, or extended relief, firms would not have any way of acquiring research from a U.S. broker-dealer on behalf of these clients (i.e. there would be no means to pay for such research and it would be an inducement to accept it for free). To complicate matters further, global asset managers often conduct their research and manage their investments on a global basis, and would often have challenges preventing or limiting research obtained from U.S. broker-dealers from also being used on behalf of MiFID clients. Some asset managers may also be forced to limit the research they acquire, to the immediate detriment of all of their clients. In addition, limitations on the acquisition of research may interfere with the efficient functioning of markets as a price discovery mechanism, as the artificial impediments to the acquisition of research may well result in less information being capitalized into the trading prices of both equity and debt securities.

Working through these alternatives will take time. If U.S. broker-dealers elect to register as investment advisers, they will be required to complete (or modify) and file Form ADV, modify their practice policies to reflect newly assumed fiduciary duties, and comply with expanded reporting and disclosure requirements. Asset managers will need to assess whether their research providers will register before considering their options. Depending on how they elect to allocate expenses, they may also need to revise investment management agreements to reflect new payment arrangements.

Further, some U.S. broker-dealers may determine that the regulatory burden imposed by registration as an investment adviser is not worth the profit made from research, and refuse to accept cash payments or payments from RPAs for research (thereby making their services unavailable to asset managers who are required to pay cash) or discontinue their research offerings. For some markets, there are currently few research providers. In the event one of these research providers decides to discontinue their offerings, it would be helpful for the industry to have more time to find and/or solicit alternative providers. Relatedly, some asset managers may seek to expand their internal research departments. If the SEC does not plan to extend their temporary relief, the asset management industry would benefit from having more time for these efforts as well.

## **The Thirty-Month Period Will Provide Little Additional Insight for the SEC**

SEC staff noted that, in connection with the temporary no-action relief, the staff would monitor and assess the impact of MiFID II's requirements on the research marketplace.<sup>6</sup> In the months that have passed, SIFMA AMG has provided the SEC with information reflecting our member firms' procurement and usage of research, and the SEC has also reached out individually to asset managers and broker-dealers. We believe this outreach has already given the SEC a better understanding of how the industry utilizes broker-dealer research. However, we do not believe additional time will provide the SEC with further clarity regarding whether permanent no-action relief is warranted.

The SEC has long recognized the value of accessible research provided by broker-dealers, identifying it as a "fundamental element of a brokerage function."<sup>7</sup> Access is best preserved by allowing asset managers to continue to have choice by permanently extending the current relief to all institutional investors irrespective of whether an institutional investor is required under MiFID II to pay for external research from its own money and/or from a separate RPA. Should the SEC determine, however, to sunset the relief, the expiration of the no-action relief without a long enough period to formulate a response to these significant regulatory changes threatens the strength of the research marketplace. While we believe the SEC should continue to monitor and evaluate marketplace reactions to MiFID II, this oversight should not delay the SEC from making their determination on how best to proceed at this point. Regardless of the SEC's decision, the markets will function better with regulatory clarity.

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<sup>6</sup> SEC Press Release, *supra* at note 5.

<sup>7</sup> See Future Structure of Securities Markets, 37 F.R. 5286, 5290 (Mar. 14, 1972). In this interpretive release, the SEC also attributed the status of the U.S. capital market as the "best capital market in the world" in part to the quality and availability of research (at 5286) and noted that "vigorous enforcement" of the suitability of a trade by a broker-dealer includes the provision of research (at 5290).

## Conclusion

SIFMA AMG sincerely appreciates your consideration of these views and concerns. We stand ready to provide any additional information or assistance that the Commission might find useful. Please do not hesitate to contact either Timothy Cameron at 202-962-7447 or [tcameron@sifma.org](mailto:tcameron@sifma.org) or Lindsey Keljo at 202-962-7312 or [lkkeljo@sifma.org](mailto:lkkeljo@sifma.org) with any questions.

Sincerely,

A handwritten signature in black ink, appearing to be 'TC', followed by a long horizontal line.

Timothy W. Cameron, Esq.  
Asset Management Group – Head  
Securities Industry and Financial Markets  
Association

A handwritten signature in blue ink, appearing to be 'LW Keljo'.

Lindsey Weber Keljo  
Asset Management Group – Managing  
Director and Associate General Counsel  
Securities Industry and Financial Markets  
Association

cc: Honorable Kara M. Stein, Commissioner, U.S. Securities and Exchange Commission  
Honorable Hester M. Peirce, Commissioner, U.S. Securities and Exchange Commission  
Honorable Robert J. Jackson, Jr., Commissioner, U.S. Securities and Exchange Commission  
Honorable Elad L. Roisman, Commissioner, U.S. Securities and Exchange Commission  
Ms. Dalia Blass, Director, Division of Investment Management, U.S. Securities and Exchange Commission  
Mr. Brett Redfearn, Director, Division of Trading and Markets, U.S. Securities and Exchange Commission