

August 4, 2006

Memorandum to Our Investment Management Clients and Friends

SEC Issues Interpretive Guidance on Soft Dollars

Introduction

On July 18, 2006, the Securities and Exchange Commission (the "SEC") published a guidance release with respect to the soft dollar safe harbor found in Section 28(e) of the Securities Exchange Act of 1934 (the "Release").¹ The SEC stated that its particular goal was to clarify for purposes of the safe harbor the scope of brokerage and research services in light of evolving technologies and industry practices.

Section 28(e) provides a safe harbor that protects a discretionary money manager of a client account from liability for breaching fiduciary duties owed to the client account solely based on the account paying more than the lowest commission amount for brokerage and research services received from a broker-dealer when the manager determines in good faith that the commission amount was reasonable relative to the brokerage and research services received. The safe harbor was enacted in 1975 and, since then, has been the subject of frequent guidance and reports issued by the SEC and self-regulatory organizations. The Release provides guidance that modifies, but largely repeats, past guidance and the SEC's proposed guidance issued on October 19, 2005. The Release is effective as of July 24, 2006, but market participants may continue to rely on the SEC's prior interpretations of Section 28(e) until January 24, 2007.

Set forth below is a summary of the SEC's guidance.

SEC's Interpretive Guidance

Eligibility. In order for brokerage and research services to be eligible for safe harbor protection, the manager must determine (i) whether the product or service constitutes research or brokerage under Section 28(e), (ii) whether the product or service in fact provides lawful and appropriate assistance in the investment decision-making function, and (iii) that the amount of commissions paid is reasonable in light of the products or services provided.

Research Services. Under the Release, to qualify as research a product must reflect the "expression of reasoning or knowledge" either through (i) advice relating to the value of securities, the advisability of investing in securities and the availability of securities or their buyers or sellers or (ii) analyses or reports about issuers, industries, securities, economic factors and trends, portfolio strategy and the performance of accounts. The form of the research may be electronic, paper or oral discussions. Exhibit A is a non-exclusive list of items that would be

¹ The Release may be found on the web at <http://www.sec.gov>.

eligible under the safe harbor if they cover the subjects identified above. Exhibit B is a non-exclusive list of items that do not constitute “research” and are not eligible under the safe harbor.

Brokerage Services. Under the Release, to qualify as brokerage a service must be provided to effect securities transactions during the period beginning when orders are first transmitted to broker-dealers and ending at the conclusion of clearance and settlement of the transactions covered by the orders. The Release refers to the use of this period as a “temporal” approach to identifying brokerage services. Exhibit C is a non-exclusive list of items that constitute brokerage services and are eligible under the safe harbor. Exhibit D is a non-exclusive list of items that do not constitute brokerage services and are not eligible under the safe harbor.

Mixed-Use Items. The Release affirms the continued propriety of following a mixed-use approach to allocate the value of products or services that are used only partially for activities within the safe harbor and emphasizes that a money manager must keep adequate books and records to substantiate the money manager’s allocations. To the extent a product or service includes a function that is not eligible research or brokerage under the safe harbor, or if the money manager does not use certain functions of the product or service in a manner that provides lawful and appropriate assistance in investment decision-making, the money manager should make an appropriate allocation as a mixed-use item. As further described below, examples of mixed-use items include order management systems and trade analytical software, as well as proxy services.

● ***Order Management Systems (“OMS”) and Trade Analytical Software.*** Under the Release, certain functions provided through OMS and trade analytical software may be eligible research or brokerage under the safe harbor. For example, research related to the market for securities and advice on market color and execution strategies (including pre- and post-trade analytics) constitutes research and is eligible under the safe harbor. In addition, trading software used to route orders, provide algorithmic trading strategies or transmit orders to direct market access systems may constitute brokerage services and be eligible under the safe harbor. In contrast, compliance mechanisms do not constitute research or brokerage and are not eligible under the safe harbor.

● ***Proxy Services.*** Under the Release, certain proxy services (which may include research and voting products and services provided by proxy service providers) may be eligible as research under the safe harbor. For example, reports and analyses on issuers, securities, and the advisability of investing in securities that are transmitted through a proxy service may constitute research to the extent they are used for investment decision making (and not for voting). In contrast, products or services offered by a proxy service provider that handle mechanical aspects of voting (such as casting, counting, recording and reporting votes) do not constitute research and are not eligible under the safe harbor.

Extent of Broker-Dealer Involvement. The Release reiterates past guidance that broker-dealers receiving commissions must be involved in “effecting” the transaction and must be responsible for the brokerage and research services “provided by” them (even when the services are the products of a third party). The Release, however, provides significantly greater flexibility than past guidance in determining whether a broker-dealer is involved in “effecting” a transaction and whether the broker-dealer is responsible for “providing” the services.

● *“Effecting” a Transaction.* Broker-dealers are involved in “effecting” a trade if they execute, clear or settle the trade or perform at least one of the following four functions: (i) take financial responsibility for customer trades until the clearing broker-dealer has received payment (or securities), (ii) make and/or maintain records relating to customer trades, including blotters and memoranda of orders, (iii) monitor and respond to customer comments concerning the trading process, or (iv) monitor trades and settlements. The broker-dealer must also take steps to see that the other functions have been reasonably allocated to one or another of the broker-dealers in the arrangement.

● *Research “Provided By” a Broker-Dealer.* Under the Release, a broker-dealer “effecting” a transaction has satisfied the “provided by” element if the broker-dealer (i) prepares the research, (ii) has a direct legal obligation to pay for the research, or (iii) pays the research preparer directly for research that it is not directly obligated to pay for and takes steps to assure itself that the client commissions are used for eligible brokerage and research. Such steps include (i) reviewing the description of services to be paid for with client commissions for red flags that indicate the services are not within the safe harbor, (ii) agreeing with the money manager to use client commissions to pay only for those items that reasonably fall within the safe harbor and (ii) developing and maintaining procedures so that research payments are documented and made promptly.

The Release notes that in multiple broker arrangements, which would include correspondent and step-out relationships, the safe harbor is available if only one of the brokers involved satisfies both the “effecting” and “provided by” requirements.

The Release solicits comments from interested persons by September 7, 2006 on the appropriate extent of required broker-dealer involvement in Section 28(e) transactions and states that the SEC may supplement this guidance in the future.

If you have any questions regarding the foregoing, please contact your primary attorney in the Investment Management Group at Seward & Kissel LLP.

Seward & Kissel LLP

Exhibit A
Eligible Research

- Research reports (including market research)
- Certain financial newsletters and trade journals intended to serve the interests of a narrow audience with specified interests rather than the general public
- Software providing analysis of securities portfolios
- Corporate governance research (including corporate governance analytics) and rating services
- Attendance at certain seminars and conferences
- Discussions with research analysts
- Meetings with corporate executives
- Consultants' advice on portfolio strategy
- Data services (including services providing market data such as stock quotes, last sales prices and trading volumes; company financial data; and economic data such as unemployment and inflation rates or GDP figures)
- Advice from brokers on order execution
- Certain functions of order management systems*
- Certain functions of trade analytical software*
- Certain proxy services*

Exhibit B
Ineligible Research

- Mass-marketed publications intended to serve the interests of a broad public audience and offered at a low cost
- Consultants' advice on manager's operations
- Office equipment
- Office furniture
- Business supplies
- Computer hardware (including computer terminals)
- Computer accessories and related peripherals and delivery mechanisms
- Telephone and cable lines
- Utilities
- Internet service
- Website design
- Electronic mail software
- Administrative software and operating systems
- Word processing
- Equipment maintenance and repair services
- Overhead including rent
- Salaries (including research staff)
- Personnel management
- Travel, entertainment and meal expenses relating to a seminar or a trip to meet a corporate executive or analyst
- Marketing (including analysis of account performance for marketing purposes)
- Professional licensing fees
- Legal expenses
- Accounting fees and software
- Membership dues
- Back-office costs

*See discussion under "Mixed-Use Items" on page 2.

Exhibit C
Eligible Brokerage Services

- Communication services related to the execution, clearing and settlement of securities transactions and functions incidental thereto, i.e., connectivity services between a manager and a broker-dealer and other relevant parties such as custodians including: (i) dedicated lines between the broker-dealer and the money manager's order management system, (ii) lines between the broker-dealer and order management systems operated by a third party vendor, (iii) dedicated lines providing direct dial up service between the money manager and the trading desk at the broker-dealer, and (iv) message services used to transmit orders to broker-dealers for execution
- Trading software operated by a broker-dealer to route orders to market centers
- Software that provides algorithmic trading strategies
- Software used to transmit orders to direct market access systems
- Clearance and settlement in connection with a trade
- Short-term custody related to effecting a trade
- Electronic communication of allocation instructions between institutions and broker-dealers
- Routing settlement instructions to custodian banks and broker-dealers' clearing agents
- Post trade matching of trade information
- Services required by the SEC or a SRO such as comparison services, electronic confirms or trade affirmations
- Certain functions of order management systems*
- Certain functions of trade analytical software*

Exhibit D
Ineligible Brokerage Services

- Computer hardware, computer terminals and telephones (including those used in connection with an order management system)
- Software used for recordkeeping or administrative purposes
- Analytical software used to test "what if" scenarios related to adjusting portfolios, asset allocation or portfolio modeling
- Long-term custody (post-settlement custody)
- Trade financing (such as stock lending fees)
- Capital introduction services
- Margin services
- Error correction trades or related services
- Compliance mechanisms and responsibilities
- Surveillance systems

*See discussion under "Mixed-Use Items" on page 2.