



September 22, 2017

Hon. W. Jay Clayton, Chairman
Hon. Michael S. Piwowar, Commissioner
Hon. Kara M. Stein, Commissioner
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

RE: Implications and Recommendation Related to MiFID II Implementation

Dear Commissioners:

Colorado Public Employees' Retirement Association ("PERA") is a large U.S.-based asset owner, with approximately \$47 billion in assets under management. As a large asset owner that is also a direct equity investor, internally managing over \$18 billion in U.S. and non-U.S. equities, we are a unique market participant (i.e. we directly consume sell-side research, while also paying for such research via external managers).

On behalf of PERA, we respectfully request that the staff of the Securities and Exchange Commission ("SEC") consider granting no-action relief to broker-dealers under the Investment Advisers Act of 1940 ("Adviser Act"), thus allowing U.S. investment managers and asset owners to "unbundle" their trade execution from research. As you are aware, the European Union has adopted the Markets in Financial Instruments Directive II ("MiFID II"), which requires investment managers to pay for research services directly, via either their own money, or from a research payment account ("RPA") funded by its clients and/or its own money. We understand that certain broker-dealers are asking the SEC to refrain from taking enforcement action under the Adviser Act with specific regard to clients bound by MiFID II. These same broker-dealers have informed us that they will not allow U.S. investors, who are not subject to MiFID II, to pay directly for research. By foregoing universal no action relief, broker-dealers are forcing the continued practice of bundling research with execution (i.e. using commissions to pay for research), outside of MiFID II jurisdictions. We believe an urgent need exists to align market practice in this arena with our European peers, thus we advocate for the authorization of direct payment for research for all investors, including those not subject to MiFID II.

Investor Impact of MiFID II

As MiFID II separates the cost of trade execution from research, investors will benefit from increased transparency and price discovery for the cost of research. Pricing is already becoming more transparent, and a new competitive pricing dynamic is occurring globally. These developments foster more efficient allocation of resources related to research and trading, benefitting investors and asset owners. In addition, the unbundling of research costs and trading will facilitate independent research, thus improving market efficiency. This is all broadly positive

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for European-domiciled investors, as the overall cost of research as well as trade execution (i.e. commission rates) should decline, post-MiFID II.

Our major concern is that U.S.-based investors, who are not subject to MiFID II, will be at a disadvantage relative to their European peers. Whereas Europe's investors will benefit from the unbundling and transparency dictated by MiFID II, U.S. investors will not realize these benefits unless they are permitted to purchase research in an unbundled and direct manner. We understand this requires the SEC granting relief from Section 28(e) of the Securities Exchange Act of 1934 which provides a safe harbor for managers to pay for research with commission dollars generated by account transactions. Under the Advisers Act, broker-dealers are prohibited from accepting direct payments for research, as defined under Section 202(a)(11), as this would be deemed "special compensation" and likely considered a "separate and identifiable charge".¹ We believe the method of payment, whether direct or commission-based, neither defines the research services provided by broker-dealers, nor represents "special compensation"; the same research is provided regardless of payment choice. The difference is that, under the requirements of MiFID II, the explicit price of the research is established in advance, and paid for using clear, direct payments. In contrast, under the current bundled structure favored by U.S. broker-dealers, the price of research is embedded in the cost of the trade and thus opaque to the investor. This likely will remain the case in the U.S. unless there is action, clarification, or declaration of "no-action" status.

Requiring the continued bundling of research and commissions for U.S. investors creates a competitive disadvantage relative to our European peers. We envision and believe a scenario will exist whereby an investment manager trades with a broker and is required to use hard dollars for their European client, yet is "required" (based on current interpretation) to use soft dollars for a U.S. client. The manager is making the same trade on behalf of both clients, and utilizing the same research. However, due to the transparency associated with the hard dollars, the U.S. investors could ultimately end up subsidizing research for European clients, as U.S. investor payment into the "research pool" is opaque and less objective. This clearly puts U.S. investors at an unnecessary disadvantage.

Recommendation

We believe that U.S. investment managers and asset owners should be able to separately identify and pay for the most valuable research, while also seeking best execution on their equity orders. We urge the staff of the SEC declare no-action relief under the Adviser Act related to broker-dealers who accept direct compensation solely in exchange for research. Additionally, we recommend that the Commission require consistent treatment of clients by broker-dealers (i.e. if accepting direct payments for research, including from MiFID II-subject customers, the broker-dealer must accept direct payments from all customers including U.S. managers and asset owners). Thus global investment managers and asset owners, as well as global research providers, would share a level playing field.

¹ https://www.sec.gov/about/offices/oia/oia_investman/rplaze-042012.pdf, II(B)(3)

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We recommend that at a minimum, the SEC declare temporary no-action relief as requested above, and immediately proceed to seek public comment on the topic. This very important issue has broad and significant ramifications for the modernization and efficiency of the capital markets in the U.S. and deserves discussion and feedback to consider multiple perspectives.

Please contact me with any questions at 303-832-3709. Thank you for your consideration.

Sincerely,

A handwritten signature in cursive script that reads "Amy C. McGarrity" followed by a circled number "4".

Amy C. McGarrity, CFA
Chief Investment Officer
Colorado Public Employees' Retirement Association