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26 March 2009

Elizabeth Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Security Ratings, File No. S7-18-08; References to Ratings of Nationally Recognized Statistical Rating Organizations, File No. S7-17-08; References to Ratings of Nationally Recognized Statistical Rating Organizations, File No. S7-19-08

Dear Ms. Murphy:

The CFA Institute Centre for Financial Market Integrity (the "CFA Institute Centre")[1] appreciates the opportunity to comment on certain aspects of the three releases referenced above that propose to revise the treatment of credit references in the Securities Act of 1933, Securities Act of 1934, Investment Company Act of 1940 and Investment Advisers Act of 1940 (collectively, Securities Acts) and related forms.

Executive Summary

Rule 2a-7 of the Investment Company Act of 1940

Minimum credit risk. We generally support the proposed elimination of references to credit ratings in determining minimal credit risk, especially given that boards can still rely on ratings issued by NRSROs in making their determination.

Portfolio liquidity. We believe heightened awareness of liquidity needs is warranted and support amendments that would prohibit a fund from holding more than 10 percent of the fund's assets in securities considered illiquid when they were purchased. We also recommend that the final rule include a clearer definition of what it believes makes a security "liquid."

[1] The CFA Institute Centre for Financial Market Integrity is a part of CFA Institute. With headquarters in Charlottesville, Virginia, USA, and regional offices in London, Hong Kong, and New York, CFA Institute is a global, not-for-profit professional association of more than 94,900 financial analysts, portfolio managers, and other investment professionals in 131 countries and territories, of whom 83,200 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 136 member societies in 57 countries and territories.

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Monitoring minimal credit risks. We recommend that the final rule provide more guidance as to what will trigger the need to reassess whether a security continues to provide minimal credit risk.

Affiliated transactions. We support the proposed reporting of when a fund's affiliate purchases a security from the fund that is no longer an "Eligible Security" as providing an additional degree of transparency.

Rule 10f-3 of the Investment Company Act of 1940

We generally support the proposed change from relying on credit ratings to using other means for measuring liquidity and credit-quality conditions, particularly given that boards would be allowed to incorporate into their approval of procedures NRSRO ratings, reports, analyses and other assessments.

Rule 10b-10 under the Securities Exchange Act of 1934

We do not support the proposed elimination of any reference to whether the security is rated. Instead, in keeping with the current rationale that whether a security is unrated by an NRSRO may prompt a dialogue between investors and their brokers, we favor the alternative proposal that would require the confirmation to disclose whether or not the security is rated, as opposed to only stating that it is not rated.

Rule 134 of the Securities Act of 1933

We support the proposed amendment that would allow references to ratings by any credit rating agency, not just NRSROs, in certain communications that are not deemed to be a prospectus, so long as the communication describes the rating agency and its rating methodologies.

Discussion

We agree that the investing public and certain market participants have suffered a false sense of security because of ratings assigned by nationally recognized statistical ratings organizations (NRSROs). We therefore generally agree with the objectives of these three proposals to eliminate, modify or substitute references to ratings assigned by an NRSRO in an effort to reduce reliance on ratings that may have inadvertently conveyed an "official seal of approval". We do, however, question the breadth of certain of the proposed changes and urge retention of the current regulation for several of the rules.

Investment Company Act of 1940—Amend References to Credit Ratings

Rule 2a-7

Minimal Credit Risk

As it currently stands, Rule 2a-7 limits portfolio investments to securities that have received credit ratings from NRSROs in one of the two highest short-term rating categories or comparable unrated securities (an "Eligible Security"). Furthermore, the rule limits money market fund investments to

securities that the fund's board determines present minimum credit risks, a determination that usually relies on the advice of the fund adviser and is based, in part, on the ratings assigned by the NRSRO.

Proposed amendments to Rule 2a-7 would continue to require money market funds to invest only in securities that present minimum credit risks, but would no longer require them to limit their investments to securities that are assigned ratings in the top two categories by NRSROs. References to NRSRO ratings would be eliminated from the rule and "Eligible Securities" instead would be determined by the board.

Specifically, under the proposed amendments, the fund board would determine whether a security is an "Eligible Security" based on whether it presents minimal credit risks and whether the issuer is able to meet short-term financial obligations. In making this determination, the SEC notes that boards would "still be able to use quality determinations prepared by outside sources, including NRSRO ratings that they conclude are credible". In the release, the SEC also notes its expectation that fund boards "would understand the basis for the rating and make an independent judgment of credit risk."

We believe that eliminating explicit references to credit ratings in Rule 2a-7 is acceptable. If fund boards and the managers working on their behalf fulfill their obligations under the proposed rule, then we do not believe the elimination of reference to NRSROs will cause investors in money market funds material harm. Given that the board could still rely on ratings by NRSROs in making a determination that a security presents a minimal credit risk, this appears to signal only a moderate shift from current oversight duties. However, we do recognize that there is an accompanying expectation that boards would understand the basis for ratings that are assigned and make "independent judgments of credit risks." We believe that this responsibility is required by the current rule.

It is implicit in the existing rule that a board, either on its own or, more likely, with the assistance of the fund manager's staff, has the ability to make independent assessments of the credit quality of securities that are considered for investment. This is because the rule limits investments to securities with NRSRO-credit ratings in one of the two highest categories or in ***comparable unrated securities***. To be able to determine that an unrated security is comparable to a rated one requires, first, that the board or its agents be able to conduct their own credit analyses on the unrated security and, second that they understand the NRSRO's rating methodologies well enough to recreate the NRSRO's analyses in order to determine comparability. Considering that the boards or their agents are expected to be able to make these determinations, we believe there is no need to require an NRSRO rating.

Portfolio Liquidity

We support proposed amendments that would require a money market fund to hold securities that are liquid enough to meet reasonably foreseeable redemptions in light of the fund's commitments. However, as we have seen in the past 18 months, instruments once considered liquid can quickly

become illiquid. Consequently, we urge the Commission to provide a clear definition of what it considers "liquid."

We also support the provisions that would prevent a fund from holding more than 10 percent of its assets in securities considered illiquid (under the Commission's definition of "liquid") when they were purchased. Particularly in light of recent market volatility, we believe that heightened awareness of liquidity needs is warranted.

Monitoring Minimal Credit Risks

Under the current rule, a money market fund must reassess whether a security continues to present minimal credit risks and take appropriate action when a security has been downgraded by an NRSRO. Proposed language would instead impose an obligation to reassess minimal credit risk whenever the board "becomes aware of any information about a portfolio security or an issuer of a portfolio security that may suggest that the security may not" continue to present such risks and then to take appropriate action. Staff commentary notes that while advisers do not have to subscribe "to every rating service publication in order to comply with this proposal", they are expected to exercise "reasonable diligence" in monitoring relevant information about portfolio securities.

While we appreciate the proposal's attempt to replace current requirements under Rule 2a-7 with language that eliminates express reliance on NRSRO ratings, we recommend that the final rule provide more guidance as to what will suffice under this language. Requiring an adviser to take action whenever it becomes aware of "any" information that "may" suggest a change in a security casts an overly broad net. Instead, we suggest that the obligation pivot on whether there is "credible" information that "reasonably suggests" a change in portfolio quality. Even with such modifications, however, we believe that the adviser needs additional guidance as to its monitoring obligations. Moreover, we question whether the adviser's obligation to stay "abreast of new information" about a portfolio security that is reported in the national financial press *or* publications subscribed to by the adviser provides adequate investor protections.

Notice of Affiliated Transactions

We support aspects of the proposal that would require a fund to notify the SEC when an affiliate (or its promoter or principal underwriter) purchases a security from the fund that is no longer an "Eligible Security" under Rule 17a-9 of the Investment Company Act of 1940. We believe that this adds an added degree of transparency and is warranted in light of recent events in the market that tended to disguise actual risk.

Rule 10f-3

Currently, Rule 10f-3 defines certain conditions under which funds that are affiliated with members of an underwriting syndicate may purchase securities from the syndicate. Municipal securities that may be purchased in reliance upon the rule must be rated investment grade by at least one NRSRO

or, for less-seasoned securities, in one of the three highest ratings by an NRSRO. Fund directors are charged with the responsibility for approving procedures for purchases made under the rule and determining that purchases comply with those procedures.

As proposed, reliance on credit ratings would be replaced with a requirement that eligible municipal securities be those that are "sufficiently liquid that they can be sold at or near their carrying value within a reasonably short period of time." The securities would also have to be either "subject to no greater than moderate credit risk" or, if seasoned securities, "subject to a minimal or low amount of credit risk." In keeping with its duties under the current rule, the board would be required to approve procedures to ensure that municipal securities would meet the proposed liquidity and credit-quality conditions. The release notes that the board could incorporate into their approval of procedures NRSRO ratings, reports, analyses and other assessments.

In general, we support the proposed changes to Rule 10f-3. While the duty to make credit determinations (in this case, approve the procedures for purchases and determine compliance) may appear to require expertise beyond typical board experience, boards would be allowed to rely on information and assessments provided by other sources.

Securities Exchange Act of 1934—Remove References to NRSROs

Rule 10b-10

As noted in the release, paragraph (a)(8) of Rule 10b-10 requires that transaction confirmations for most debt securities must inform investors whether a security is unrated by an NRSRO as a means for prompting a dialogue between investor and broker about the security. We believe this rationale remains valid.

In proposing elimination of paragraph (a) (8), staff reaffirms that an issuer's creditworthiness is a relevant topic for discussion and encourages investors to understand all credit-related risks before investing. The release also allows broker-dealers to volunteer in their confirmations the information that is proposed to be deleted.

We believe that the logic for deleting the reference to credit ratings in this case is questionable on two levels. First, noting that a security is unrated does not in and of itself unduly convey a judgment on that security. It simply allows the investors to raise relevant questions with their brokers. Second, without a prompt, the typical retail investor may not know to query the broker about the credit status of an issuer, thereby losing the ability to gain all the information he deserves in order to make informed investment decisions.

Accordingly, we support the alternative raised in the release whereby the confirmation would disclose whether or not the security is rated, as opposed to only stating when it is not rated. We believe that this approach serves the underlying purpose to put the investor on notice of any issues he may consequently want to raise with his broker.

Securities Act of 1933—Replace Requirements that Rely on Security Ratings with Alternative Requirements

Rule 134

Currently, Rule 134(a) (17) allows security ratings by NRSROs to be disclosed in certain communications that are not a prospectus or free writing prospectus. A proposed amendment would expand this disclosure to include ratings by any credit-rating agency, not just NRSROs. We support this amendment, provided that the communication includes a description of the credit-rating agency and its rating methodologies.

Conclusion

The CFA Institute Centre appreciates the opportunity to comment on these three releases relating to various references to credit ratings in the securities acts. In most part, we agree with, or do not object to, the proposed changes to and deletions of such references. However, as noted above, we believe that several proposed amendments exceed what is good for the market and the investing public and should not be implemented.

Should you have any questions about our positions, please do not hesitate to contact Kurt N. Schacht, CFA at kurt.schacht@cfainstitute.org or 212.756.7728; or Linda Rittenhouse at linda.rittenhouse@cfainstitute.org or 343.951.5333.

Sincerely,

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