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November 14, 2008

The Honorable Christopher Cox
Chairman
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Commission Request for Comment on Mark-to-Market Accounting
File No. 4-573

Dear Chairman Cox:

The Investment Company Institute[1] appreciates the opportunity to respond to the Commission's request for comment on mark-to-market accounting.[2] The Emergency Economic Stabilization Act of 2008 requires the Commission, in consultation with the Federal Reserve and the Treasury, to conduct a study on mark-to-market accounting as provided in FAS No. 157 and to submit a report to Congress within 90 days ("Study"). The Study must consider, among other things, the impact of FAS No. 157 on the quality of information available to investors, alternatives to FAS 157, and the advisability of modifying FAS No. 157.

Mark-to-market accounting (also called fair value accounting) refers to the use of market prices to measure the value of financial assets and liabilities in financial reporting. Depending on its application, fair value accounting may also require firms to report the periodic change in the fair value of positions they currently hold as unrealized gains and losses on their income statements.

As investors in more than $5.3 trillion of domestic equity and fixed-income securities, the Institute strongly supports the efforts of the Commission and the Financial Accounting Standards Board to ensure that the U.S. financial reporting system provides investors with information that fairly presents the financial position and results of operations of companies accessing our capital markets and therefore is useful to investment decision making. For the reasons described below, we believe financial reporting that requires the use of mark-to-market or fair value accounting to

[1] The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors and advisers. Members of ICI manage total assets of $11.2 trillion and serve almost 90 million shareholders.

[2] SEC Study of Mark-to-Market Accounting, SEC Release Nos. 33-8975, 34-58747 (October 8, 2008), 73 Fed. Reg. 60737(October 14, 2008).

measure financial instruments better serves the interests of investors and our capital markets than alternative cost-based measures.

Measurement Attributes

The goal of a fair value measurement is to estimate the price at which a financial instrument would trade in an orderly transaction based on current information and conditions. When market prices for the same or similar instruments are available, FAS 157 generally requires firms to use these prices to estimate fair value. If market prices for the same or similar instruments are not available, firms must estimate fair values using valuation models. FAS 157 requires these models to maximize the use of observable market inputs. If observable market inputs are not available, FAS 157 permits use of unobservable inputs, thereby allowing for situations in which there is little, if any, market activity at the measurement date.

The alternative to fair value accounting is amortized cost. Amortized cost uses historical information from the purchase or inception of the position to value the financial instrument and report its cash flows over its holding period. Unlike fair value accounting, changes in the value of the position are ignored for financial reporting purposes until they are realized through disposal, impairment or the passage of time.

Objectives of Financial Reporting

Financial reporting should provide information that is useful to current and potential investors, creditors and other financial statement users in making rational investment, credit, and similar decisions.[3] Such information should enable investors, creditors, and other financial statement users to assess the amounts, timing and uncertainty of prospective net cash inflows to the business. Further, financial reporting should provide information about the economic resources of the business, and claims against those resources.

Financial information must be relevant, reliable, and comparable in order to be useful to investors, creditors and other financial statement users.[4] Relevant information enables users to form predictions about the outcomes of past, present and future events or to confirm or correct prior expectations. Reliable information is that which is free from error and faithfully represents what it purports to represent. Comparable information facilitates comparison across time periods or to other businesses.

Fair Values Better Serve the Interests of Investors

The fair value of financial instruments is more relevant to investors, creditors and other financial statement users than amortized cost in that it reflects the market's current assessment of

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[3] *See* Statement of Financial Accounting Concepts No. 1, Objectives of Financial Reporting by Business Enterprises (November 1978).

[4] *See* Statement of Financial Accounting Concepts No. 2, Qualitative Characteristics of Accounting Information (May 1980).

the value of the financial instrument. Such assessment incorporates market participants' judgments as to the likelihood that contracted cash flows on the financial instrument will ultimately be realized. In contrast, amortized cost fails to reflect the likelihood that contracted cash flows may not be realized. Deterioration in credit quality is not reflected until such time as the financial instrument is deemed to be impaired.

Financial instruments that are traded actively provide reliable measures of value. When identical positions trade in liquid markets, fair value is the most accurate and least discretionary measurement attribute. Fair values may involve greater discretion where markets are inactive or market prices are not available. However, FAS 157 addresses these situations by requiring firms to disclose qualitative information about how they estimate fair values as well as quantitative information about the financial instruments they hold. Such quantitative disclosures include gain/loss for the reporting period attributable to financial instruments valued through reference to internal assumptions (*i.e.*, Level 3).

Fair value accounting provides more comparable measures of value than amortized cost. All businesses that hold a particular financial instrument will rely on the market-based price to determine the value of that instrument, or at the very least, will apply the same valuation principles prescribed by FAS 157 to estimate the value of the instrument. In contrast, the amortized cost of a particular financial instrument is a function of the position's cost at inception or purchase. Where different businesses purchase the same financial instrument at different times and at different costs, their amortized cost will also differ, causing these businesses to report the same financial instrument at differing values in their financial statements.

For the reasons described above, we believe fair value based measures better achieve the objectives of financial reporting and better serve the interests of investors, creditors and others that rely on financial reporting. Any suspension of fair value accounting would reduce transparency and could cause investors to lose confidence in financial reporting.

Modifications to FAS 157

We fully support the recent clarifications issued jointly by the Commission's Chief Accountant and the FASB staff on the determination of fair values in inactive markets.[5] This guidance appropriately recognizes that the determination of fair value often requires significant judgment and that trades or quotes from inactive markets may be an input when measuring fair value, but that they are not determinative.[6] We also support recent clarifications issued by the

[5] *See* SEC Office of Chief Accountant and FASB Staff Clarifications on Fair Value Accounting, SEC Press Release No. 2008-234 (September 30, 2008).

[6] The SEC's Division of Investment Management recently provided no-action relief to the Institute enabling money market funds to value certain securities at amortized cost for purposes of "shadow pricing" their portfolios as required by rule 2a-7 under the Investment Company Act of 1940. In particular, such funds may use amortized cost to value securities that (i) have a remaining maturity of 60 days or less, (ii) are rated in the highest short-term rating category by an NRSRO, and (iii) the fund reasonably expects to hold to maturity, unless the issuer's creditworthiness has been impaired. Such relief recognizes that amortized cost better represents fair value than prices from dislocated markets for short-term, high-quality paper that will be held to maturity. This no-action relief

FASB.[7] The FASB guidance describes how management's internal assumptions (e.g., expected cash flows and appropriately risk-adjusted discount rates) should be considered when measuring fair value when relevant observable inputs do not exist. The determination to pursue any further modifications to FAS 157 should reside with the FASB and should be subject to its normal due process procedures, including notice and appropriate opportunity for comment.

We appreciate the opportunity to respond to the Commission's request for comment and would be pleased to provide any additional information you may require. Please contact Greg Smith at 202/326-5851 if you have any questions on our comments or if we can be of assistance.

Sincerely,

Paul Schott Stevens
President & CEO
Investment Company Institute

cc: The Honorable Kathleen L. Casey
The Honorable Elisse B. Walter
The Honorable Luis A. Aguilar
The Honorable Troy A. Paredes

Florence E. Harmon
Acting Secretary

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expires January 12, 2009. *See* letter from Robert E. Plaze, Associate Director, Division of Investment Management to Karrie McMillan, General Counsel, Investment Company Institute (October 10, 2008). The Commission, or the FASB, may wish to consider enabling broader use of amortized cost in similar circumstances.

[7] *See* FSP 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is not Active (October 10, 2008).