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**VIA ELECTRONIC MAIL at [rule-comments@sec.gov](mailto:rule-comments@sec.gov)**

April 25, 2011

Ms. Elizabeth M. Murphy, Secretary  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549-1090

**Re: References To Credit Ratings In Certain Investment Company Act  
Rules and Forms  
(File Number S7-07-11)**

Dear Ms. Murphy,

Invesco Advisers, Inc. is a registered investment adviser that, along with its affiliates, has managed and advised money market funds and other cash investment vehicles for over 30 years. As of March 31, 2011, Invesco had approximately \$54 billion in assets under management in its registered money market funds operated in compliance with Rule 2a-7 of the Investment Company Act of 1940, as amended ("Rule 2a-7").

We strongly endorse the ongoing efforts of the United States Securities and Exchange Commission (the "Commission") and other policymakers to bolster the resiliency of money market funds. Since its adoption, Rule 2a-7 has provided money market funds with a solid foundation of safety, liquidity, investment diversification, and a market based rate of return. The changes recently adopted by the Commission have strengthened these protections even further. Invesco understands the requirements placed upon the Securities and Exchange Commission ("SEC") by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act") with respect to the elimination from Rule 2a-7 of references to credit ratings as a standard of credit-worthiness. Nevertheless, Invesco has certain concerns regarding the changes to Rule 2a-7 that the Commission has proposed to implement these requirements (the "Proposed Changes").<sup>1</sup>

Credit ratings have long served an important purpose as objective, third-party standards by which money market fund boards and advisers can assess the risk associated with portfolio investments.<sup>2</sup> The uniformity of these standards across funds increases credit quality transparency and facilitates comparisons between funds. We believe that credit ratings, while not perfect, provide an important floor to prevent money market funds from taking undue risks to increase yield.

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<sup>1</sup> *References to Credit Ratings In Certain Investment Company Act Rules and Forms*, 76 Fed. Reg. 12896 (March 9, 2011).

<sup>2</sup> See Report of the President's Working Group on Financial Markets: Money Market Fund Reform Options (October 2010).

The removal of third-party credit ratings as a standard of credit-worthiness from Rule 2a-7 as required by the Dodd Frank Act will introduce a greater element of subjectivity in the evaluation and presentation of credit risk within money market fund portfolios. Our comments below reflect Invesco's strong belief that it is important to craft any changes to Rule 2a-7 with an eye toward ensuring that these more subjective standards do not create opportunities for money market funds to take on more credit risk than they are currently permitted. The new credit-worthiness standards therefore must be expressed clearly, understood widely, and interpreted uniformly by advisers, investors, and market participants. This imperative is acknowledged in the language of the Dodd Frank Act itself, which directs the Commission to "establish, to the extent feasible, uniform standards of credit-worthiness" to replace credit ratings.<sup>3</sup>

As discussed in more detail below, we believe that certain elements of the Proposed Changes should be revised to minimize the potential for increased risk and to maintain the strong existing board and adviser oversight framework established by Rule 2a-7.

#### **Definition of Eligible Security:**

The portfolio quality restrictions currently set forth in Rule 2a-7 require that all securities in a money market fund's portfolio be determined by the fund's board (or their delegate) to present "minimal credit risks (which determination must be based on factors pertaining to credit quality in addition to any rating assigned to such securities by a Designated NRSRO)..."<sup>4</sup> In addition, money market funds are limited to investing in securities that have received a rating in one of the two highest short-term rating categories (or, if unrated, have been determined to be of comparable quality by the fund's board of directors).<sup>5</sup> Securities meeting these requirements are considered "eligible securities." Securities rated within the highest short-term rating category (including any sub-categories) or unrated securities deemed by the board to be of comparable quality are considered "first tier" securities, while all other eligible securities are considered "second tier" securities.<sup>6</sup> Money market funds are required to invest no less than 97% of their assets in first tier securities.<sup>7</sup>

Under the Proposed Changes, a money market fund board would still be required to determine that all securities in the fund's portfolio present minimal credit risks. However, the objective NRSRO ratings criteria used in this analysis and in designating securities as first or second tier would be replaced by more subjective criteria. Under the revised rule, first tier securities would be those for which "the fund's board (or its delegate) determines that the issuer (or in the case of a security subject to a guarantee, the guarantor) has the 'highest capacity to meet its short term obligations.'"<sup>8</sup> As under the current rule, any eligible security that did not satisfy the requirements to be a first tier security would be considered a second tier security.<sup>9</sup>

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<sup>3</sup> Dodd-Frank Sec. 939A.

<sup>4</sup> Rule 2a-7(b)(3)(i).

<sup>5</sup> Rule 2a-7(a)(12).

<sup>6</sup> Rule 2a-7(a)(14), (24).

<sup>7</sup> Rule 2a-7(b)(3)(ii).

<sup>8</sup> *References to Credit Ratings In Certain Investment Company Act Rules and Forms*, 76 Fed. Reg. 12898 (March 9, 2011).

<sup>9</sup> *Id.*

We agree that the current two-tier classification of money market funds' portfolio securities should be maintained. However, we believe that the highly subjective nature of the replacement standards the Commission has proposed could create more risk within money market funds over time by potentially permitting them to "reach for yield" by holding securities that they are currently restricted from holding due to ratings criteria. This risk may be particularly acute in the current low interest rate environment. We also echo the concerns expressed by the Investment Company Institute ("ICI") in their comment letter that the new standard proposed by the Commission for first tier securities could potentially be interpreted to be higher than the current standard since it references the "highest capacity" whereas the existing first tier standard permits funds to hold securities within any of the sub-categories of the top rating categories.

We understand that the Dodd Frank Act mandates the removal of references to credit ratings as the standard of credit-worthiness in Rule 2a-7.<sup>10</sup> However, as noted earlier, the Dodd Frank Act itself requires that any new credit-worthiness standards be uniform.<sup>11</sup> It is therefore critically important that the new standards adopted for Rule 2a-7 be interpreted and applied by all funds in the same way.

In the absence of objective, third-party standards such as credit ratings, we believe that the best way to accomplish this goal is to use widely recognized and uniformly interpreted standards. We therefore propose that for purposes of Rule 2a-7, eligible securities would be defined as those for which the issuer demonstrates a very strong (first tier) or strong (second tier) ability to meet its short-term obligations and as to which there is a very low (first tier) or low expectation (second tier) of default. We believe that these standards are more consistently understood as they are similar to those used by ratings agencies currently. Since these standards more closely track those currently used by fund boards and advisers to evaluate their portfolio holdings, there is less likelihood that implementing them will result in funds weakening their current risk standards.

#### **Monitoring of Credit Risk:**

Rule 2a-7 currently requires that a money market fund "board of directors... reassess promptly whether such security continues to present minimal credit risks and...cause the fund to take such action as the board of directors determines is in the best interest of the money market fund and its shareholders" upon the occurrence of certain events.<sup>12</sup> These events include when a portfolio security ceases to be a first tier security (or the board has determined it no longer of comparable quality) and when the fund's adviser becomes aware that any unrated or second tier security has been downgraded or been given a rating by an NRSRO which is below the second highest short-term rating.<sup>13</sup>

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<sup>10</sup> Dodd Frank Sec. 939A.

<sup>11</sup> *Id.*

<sup>12</sup> Rule 2a-7(b)(7).

<sup>13</sup> Rule 2a-7(c)(7)(i)(A).

The Proposed Changes would amend Rule 2a-7 to require that in the event the fund's "adviser... *becomes aware of any credible information* about a portfolio security or an issuer of a portfolio security that *suggests* that the security is no longer a First Tier Security or a Second Tier Security, as the case may be, the board of directors shall reassess promptly whether such security continues to present minimal credit risks and shall cause the fund to take such action as the board of directors determines is in the best interests of the money market fund and its shareholders [emphasis added]."<sup>14</sup>

We believe that the Proposed Changes represent a significant, though perhaps unintentional, change to the current credit monitoring requirements under Rule 2a-7. Under the existing rule, a fund board's or adviser's obligation to take action is triggered not only when a security is no longer deemed to represent a minimal credit risk but also by the occurrence of a discrete and clearly definable event: the downgrade of a portfolio security.<sup>15</sup> Such a downgrade would occur only after the ratings agency had obtained and analyzed information sufficient to cause the agency to alter its assessment of the security in question. Under the proposed new rules, however, advisers and boards would be obligated to take action upon becoming aware of *any credible information that suggests* that a portfolio holding is no longer a first or second tier security.<sup>16</sup>

Given the risk of potential litigation or regulatory enforcement in the event that a seemingly innocuous piece of information could be argued later to have "suggested" that the security was no longer first or second tier, we believe that the Proposed Changes would have the practical effect of creating an overly sensitive trigger. The implications are even more troubling given the subjectivity of the new first tier and second tier definitions under the revised Rule 2a-7. We are concerned that the imposition of the Proposed Changes could lead fund boards and advisers to become overly reactive and to liquidate otherwise solid portfolio holdings at the first rumor of problems in an effort to avoid being second-guessed at a later date by others who enjoy the benefit of hindsight. This may result in unintended adverse consequences for the normal functioning of short-term debt markets. Finally, we concur with the concern noted in the release for the Proposed Changes that the ambiguity inherent in the terms "credible information" and "suggest" would greatly complicate enforcement of the rule if the Commission believed that a fund board had failed to satisfy its credit monitoring obligations.

Given the subjectivity of the credit-worthiness standards that will be applied under the revised Rule 2a-7, we concur with the ICI's recommendation that Rule 2a-7 be amended to require fund boards (or their delegates) to monitor their funds' securities on an ongoing basis with reference to these standards rather than relying on the occurrence of an ambiguous event to trigger reassessment of a security.

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<sup>14</sup> Proposed Rule 2a-7(c)(7)(i)(A).

<sup>15</sup> Rule 2a-7(b)(7)

<sup>16</sup> Proposed Rule 2a-7(c)(7)(i)(A).

## **Stress Testing**

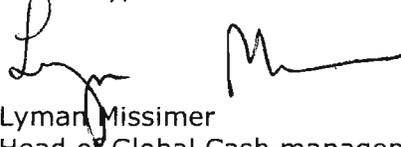
Rule 2a-7 requires a money market fund to test and report to the board the fund's ability to maintain a stable net asset value following the occurrence of certain hypothetical events, including a ratings downgrade. The Commission proposes to modify the stress testing requirement by replacing the assessment of the hypothetical impact of a ratings downgrade with an assessment of the hypothetical impact of "an adverse change in the ability of a portfolio security issuer to meet its short term financial obligations."<sup>17</sup> Such a measurement would prove extremely difficult in practice due to the subjective nature of the judgments involved and, as a result, the reliability of the stress testing results would be significantly undermined.

As previously noted, Section 939A of the Dodd-Frank Act requires the removal of references to credit ratings as a standard for measuring the credit-worthiness of a security or money market instrument.<sup>18</sup> We do not believe that the statute requires the elimination of all references to credit ratings, however. The references to a credit rating downgrade in the stress testing provisions of Rule 2a-7 are not related to assessing the credit-worthiness of the underlying issuer. Rather, these provisions focus on the *impact to the portfolio* of a hypothetical downgrade, as measured by pricing spreads between similar securities with different ratings. Since credit ratings in this context are not used as a credit-worthiness standard we agree with the ICI that removing references to them from the stress testing provisions of Rule 2a-7 is unwarranted and unnecessary.

## **Conclusion**

In conclusion, while we acknowledge that the Dodd Frank Act mandates the replacement of certain references to credit ratings in Rule 2a-7 with new credit-worthiness standards, we believe that the Commission should seek to maintain the integrity of the existing rule where possible. Where changes are required we urge the Commission to adopt clear and widely embraced standards in order to avoid inconsistent interpretation, which could undermine existing risk controls and hinder portfolio transparency for investors and regulators.

Sincerely,



Lyman Missimer  
Head of Global Cash management

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<sup>17</sup> Proposed Rule 2a-7(c)(10)(v)(A).

<sup>18</sup> Dodd-Frank Sec. 939A.