

December 8, 2009

By Electronic Delivery and Federal Express

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

Re: Rel. Nos. 34-60790 and 34-58070; File Nos. S7-17-08, S7-18-08 and S7-19-08
References to Ratings of Nationally Recognized Statistical Rating Organizations

Dear Chairman Schapiro:

We submit this letter in response to the request of the Securities and Exchange Commission (“SEC” or “Commission”) for comments on its proposed amendments to eliminate references to ratings of Nationally Recognized Statistical Rating Organizations (“NRSROs”) in certain SEC rules and forms. Specifically, we are commenting on the SEC’s proposed changes that would remove references to NRSRO ratings in Regulation M (“Proposal”).¹ The Proposal would eliminate all references to NRSRO ratings in Rules 101 and 102 of Regulation M and substitute new exceptions for nonconvertible debt securities and nonconvertible preferred securities based on the “well-known seasoned issuer” or “WKSI” definition included in Rule 405 under the Securities Act of 1933.

If the Proposal is adopted in its present form, foreign sovereign issuers that issue investment grade debt securities would be adversely affected because such securities would no longer be excepted from the provisions of Rules 101 and 102 of Regulation M. The Proposal’s new exception for securities issued by WKSIs would not be available to foreign sovereign issuers because sovereign issuers file on Schedule B rather than on Forms S-3 or Form F-3 and therefore do not qualify as WKSIs. In addition, many foreign

¹ The amendments were originally proposed in Release No. 34-58070, 73 Fed. Reg. 40088 (July 11, 2008). Although comments on the Proposed Release were originally due on September 5, 2008, in Release No. 34-60790, 74 Fed. Reg. 52374 (Oct. 9, 2009), the comment period was re-opened and extended to December 8, 2009.

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sovereign issuers whose securities do not currently qualify for an exception under Regulation M based on an investment grade rating rely on no-action letters that are based on the similarities between the trading markets for such issuers' securities and the markets for investment grade securities. If the Proposal is adopted as written, the continued reliance on such letters by foreign sovereign issuers would be uncertain.

I. Foreign Sovereign Issuers Would Lose the Benefits of the Current Exceptions from Rules 101 and 102 of Regulation M

We are commenting on this Proposal because Schedule B issuers, including our foreign sovereign clients (i.e., foreign governments or governmental entities), would be severely and negatively impacted by the Proposal. Because Schedule B issuers are not eligible to use Form S-3 or Form F-3 to register primary offerings of securities, foreign sovereigns do not fall within the definition of a WSKI even though the foreign sovereign may have been active in the U.S. capital markets and may be widely followed in the United States. Thus, if the Proposal is adopted, foreign sovereign issuers that issue investment grade securities in U.S. markets will lose the benefit of the exceptions for such securities in Rules 101 and 102 of Regulation M.

The purpose of Regulation M is to protect the integrity of the securities trading market by prohibiting activities that could artificially influence the market for an offered security. Rules 101 and 102 of Regulation M are anti-manipulation rules that, subject to certain exceptions, prohibit persons participating in a distribution of securities from bidding for or purchasing, or attempting to induce other persons to bid for or purchase, a covered security until they have completed their participation in the distribution.

Rules 101 and 102 of Regulation M currently except from the requirements of Regulation M nonconvertible debt securities, nonconvertible preferred securities, and asset-backed securities that are rated by at least one NRSRO in one of its generic rating categories that signifies investment grade. The SEC's consistent rationale for the current exceptions (and their predecessors) has been that investment grade securities trade on the

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basis of yield and spread to comparable securities, and are generally fungible with other, similarly rated securities. Based on these qualities, such securities are less susceptible to manipulation.²

In addition, the Staff has consistently granted no-action letters to foreign sovereign issuers of non-investment grade securities based in part on the important similarities of such securities to investment grade securities, including that they trade in a manner similar to that of investment grade securities.³ For example, in connection with a global bond offering of non-investment grade securities by the United Mexican States, the Staff issued a no-action letter that relieved both the issuer and the underwriters from compliance with Rules 101 and 102 of Regulation M on the basis that such securities “are expected to trade primarily on the basis of a spread to a United States Treasury security in a manner similar to trading in investment grade debt securities.”⁴ Therefore, adoption of the Proposal not only affects foreign sovereign issuers of investment grade securities, but it could also result in uncertainty regarding those foreign sovereign issuers that do not issue investment grade securities but instead act in reliance on no-action letters that effectively exempt them from compliance with Rule 101 or Rule 102 of Regulation M.

II. *Foreign Sovereign Issuers Would Be Adversely Affected by the Proposal*

The lack of an exemption under Rule 102 of Regulation M would disrupt the ability of foreign sovereign issuers and their affiliates to purchase any of such issuer’s securities in connection with the sovereign’s own general trading and investment activities, or for other public purposes, during the applicable restricted period. As a result, foreign sovereign issuers and their affiliates that do not make a market in foreign sovereign issued securities would be unable to participate in the purchase of these securities during the restricted period even when permitted by their local laws. For example, central banks of foreign sovereigns may be permitted by their local laws to

² See Section III.E.2 of Release No. 34-58070, *supra* n. 1 (“The current exceptions for certain investment grade debt and preferred securities rated by a NRSRO were originally based on the premise that these securities are traded on the basis of their yields and credit ratings, are largely fungible and, thus, are less likely to be subject to manipulation.”)

³ See Federative Republic of Brazil, SEC No-Action Letters (October 15, 2003, September 9, 2003, July 3, 2003, April 29, 2003 and January 21, 2000).

⁴ See United Mexican States, SEC No-Action Letter (February 17, 1999).

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make acquisitions of foreign sovereign issued bonds as part of open market operations that are implemented to control their nation's money supply. The Proposal would limit such acquisitions thereby hampering a foreign sovereign's ability to support the markets and its economy. This is of special concern given the current international financial crisis and the need for governments to have the tools to prevent financial and economic catastrophes.

Rule 101 of Regulation M generally prohibits a distribution participant (e.g., an underwriter, prospective underwriter, broker, dealer, or other person that has agreed to participate or is participating in a distribution) and its affiliated purchasers from bidding for, purchasing, or attempting to induce any person to bid for or purchase, a covered security during the specified restricted period. Thus, in the absence of an exemption from Rule 101, underwriters of securities issued by foreign sovereigns will be forced to be absent from the market for, and be unable to make a market in, such securities from the time of their issuance through the time the underwriters complete their participation in the distribution of the securities. Underwriters attempt to keep an orderly market by trying to balance the bids and asks and they also trade securities on their own account to maintain a stable price during times when there is no match of sellers to buyers. Without this exemption, the underwriters will likely have difficulty in providing additional liquidity during the first few hours and, even, days of trading in the securities, disrupting an otherwise orderly market with potentially serious consequences.⁵ Only a limited number of broker-dealers make a market in foreign sovereign debt securities. Therefore, the absence from the market of any underwriters during the restricted period would limit the opportunity to make a market in these securities and adversely affect foreign sovereign issuers.

III. *If the Proposal is Adopted, Foreign Sovereign Issuers May Limit Their Participation in the U.S. Public Markets. As a Result, U.S. Investors May Have Limited Opportunities to Diversify their Investments with Foreign Government Debt*

Adoption of the Proposal in its current form may impact the willingness or ability of foreign sovereign issuers to publicly issue securities in U.S. capital markets. Foreign

⁵ See Federative Republic of Brazil, SEC No-Action Letter (October 16, 2003) and incoming letter of October 15, 2003.

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sovereigns may turn instead to the private placement and Rule 144A markets, or to the Euro or other foreign markets. Consequently, the availability of foreign sovereign securities to U.S. investors may be limited, which would hamper the ability of most U.S. investors to invest in the debt of foreign sovereign governments and agencies.

IV. Conclusion

Because foreign sovereigns do not fall within the definition of a WKSI, they would be unable to continue to rely on the exceptions in Rule 101 or Rule 102 of Regulation M even though they may have been active in the U.S. capital markets and may be widely followed in the U.S. We believe that the elimination of the current exceptions for investment grade foreign sovereigns under Rules 101 and 102, and the calling into question of related no-action letters, would be an unintended consequence of the Proposal, and we are aware of no reason why the current exceptions should be denied to foreign sovereign issuers. We also believe that the loss of these exceptions would adversely affect foreign sovereign issuers' willingness or ability to issue in the U.S. public capital markets, and that an ancillary effect of the Proposal would be to limit the ability of most U.S. investors to invest in foreign sovereign debt.

We therefore urge the Commission to reject the Proposal. However, in the event that the Commission determines to adopt the Proposal, we urge that it also adopt a separate exemption under Regulation M for offerings by foreign sovereign issuers that file on Schedule B whether or not such issuers issue investment-grade securities. Alternatively, we urge the Commission to (1) adopt a separate exception for offerings of securities by foreign sovereign issuers that issue investment-grade debt securities, and (2) confirm that foreign sovereign issuers that do not issue investment-grade securities may continue to rely on, or apply for, no-action letters relieving them from compliance with Rule 101 or Rule 102 of Regulation M in the future, notwithstanding the Commission's adoption of the Proposal.

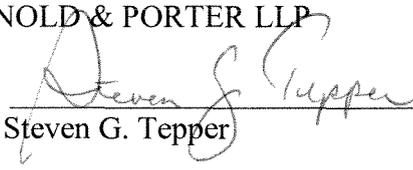
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We thank you for this opportunity to provide our comments. We would be happy to discuss the concerns of foreign sovereign issuers related to the Proposal at your convenience. Please feel free to contact the undersigned at (212) 715-1140, Gregory Harrington at (202) 942-5082, Laura Badian at (202) 942-6302, or Dermond Thomas at (212) 715-1041.

Very truly yours,

ARNOLD & PORTER LLP

By: 

Steven G. Tepper

cc: The Honorable Luis A. Aguilar, Commissioner
The Honorable Kathleen L. Casey, Commissioner
The Honorable Troy A. Paredes, Commissioner
The Honorable Elisse B. Walter, Commissioner
Elizabeth M. Murphy, Secretary
Josephine J. Tao, Assistant Director, Division of Trading and Markets
Elizabeth A. Sandoe, Branch Chief, Division of Trading and Markets
Bradley Gude, Special Counsel, Division of Trading and Markets