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November 7, 2011

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

Dear Ms. Murphy:

Interactive Data is pleased to provide comments to the concept release on the Use of Derivatives by Investments Companies under the Investment Company Act of 1940 (RIN: 3235-AL22) that was issued by the Securities and Exchange Commission (Commission) on August 31, 2011.

As described in greater detail below, we believe that the use of derivatives by investment companies is integral to their ability to execute their investment strategies and to manage risk effectively. Given the diversity and complexity of derivatives and the related challenges in valuing these instruments, we believe that is appropriate for the Commission to provide investment companies with additional principle-based guidance on the valuation of derivatives. Related to this, we believe that the three key areas the Commission should consider in preparing such guidance are multiple sources of inputs; independence of sources; and transparency into key inputs.

Background on Interactive Data Corporation:

Interactive Data Corporation is a trusted leader in financial information. Thousands of financial institutions, including many of the world's leading investment companies, subscribe to our fixed income evaluations, reference data, real-time market data, trading infrastructure services, fixed income analytics, desktop solutions and hosted, web-based solutions. Interactive Data's offerings are used to assist clients with mission-critical functions, including portfolio valuation, regulatory compliance and risk management.

For over 40 years, Interactive Data's Pricing and Reference Data business has been collecting, editing, maintaining, and delivering financial data, and has established itself as a leading provider of evaluated pricing for 2.8 million fixed income securities, international equities and other hard-to-value instruments including OTC derivatives. These offerings are complemented by a comprehensive range of reference data for more than 10 million securities that encompasses listed markets pricing, identification information, corporate actions, and terms and conditions for current and historical fixed income securities. Interactive Data Pricing and Reference Data has built a strong presence within the U.S. mutual fund marketplace and now counts 50 of the top 50 U.S. mutual fund companies as customers.

In recent years, we have invested considerable resources to provide our clients with greater insight and transparency into the inputs used to derive our evaluated prices. We also have developed new services such as our Business Entity Service which identifies relationships between issues, issuers and parent entities, thereby helping clients meet their requirements for managing credit, market and operational risk, managing diversification, concentration and investment restrictions, and for compliance with a variety of global risk management and other regulations.

We believe that the use of derivatives by investment companies is integral to their ability to execute their investment strategies and to manage risk effectively. Given our expertise and experience as a leading provider of evaluated pricing services, we have focused our comments on Section VI Valuation of Derivatives. Please note that we have included our responses to some of the specific questions posed by the Staff in Section VI of the Concept Release in an Appendix to this letter.

<u>Valuation of Derivatives</u>

The Commission's general principle that the "fair value of a security or other asset held by a fund would be the amount that the fund might reasonably expect to receive for the security or other asset upon its current sale"[1] has underpinned the valuation practices of investment companies for decades. While this general principle has served investors and the investment fund industry well, the financial markets have undergone tremendous change since the Commission last provided guidance on valuation. The financial services industry has witnessed a proliferation of new asset classes and investment products, and in particular a boom in the variety and availability of derivative products. Given both the tremendous utility and prevalence of derivatives today, we believe that it is appropriate for the Commission to provide additional principle-based guidance on the valuation of derivatives that takes into account the diversity and complexity of these instruments. We believe that such principle-based guidance would help investment companies and investors more effectively and consistently assess valuations for these instruments.

When market quotations are not readily available for derivative instruments (i.e. for derivatives that do not trade on an exchange), investment companies must determine the fair value of derivatives that they hold. To do this, they may employ a wide range of approaches based on inputs related to actual trade activity, mathematical models, quotes and prices of other comparable securities, security-based swaps, or derivatives, or a combination thereof. For OTC derivatives, depending on the type of derivative and the availability of verifiable trading information, valuation techniques may include obtaining values from counterparties or others making a market in those securities, or using model-based valuations, either created by internal teams or provided by third-party sources. Valuation models themselves can vary widely from basic approaches, such as calculating the mean or average of contributor prices, to more sophisticated

[1] Use of Derivatives by Investment Companies under the Investment Company Act of 1940, Page 68

approaches using analytical software powered by complex mathematical models or by employing models that incorporate multiple market inputs. Interactive Data's valuation models for OTC derivatives utilize a broad range of market inputs from multiple sources, including benchmark curves from leading interdealer brokers, reference rates and trade details from both buy and sell-side market participants, as well as related trading activity from cash markets to develop independent valuations for credit default swaps.

Regardless of the approach, we believe that valuing complex derivatives with limited market activity is inherently difficult. Given these dynamics, we would like to emphasize three key areas that we believe are particularly important for the Commission to consider in preparing valuation guidance for derivative instruments:

1. Multiple Sources of Inputs
2. Independence of Sources
3. Transparency

It should be noted that our August 29, 2011 comment letter to the Commission on Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants also emphasizes these same points.

- ***Multiple Sources of Inputs:*** Relying on a single set of inputs introduces both valuation risk and operational risk, should that source become unreliable or unavailable. As noted above, Interactive Data's derivative valuation service is underpinned by models that utilize a broad range of market inputs from multiple sources. We believe that our approach is consistent with the Commission's guidance that "all indications of value that are available must be taken into account."[2] In addition, using multiple sources enhances a firm's business continuity and reduces operational risk by limiting single points of failure.

- ***Independence of Sources:*** We believe that independent data is fundamental to the valuation responsibilities of the fund's board of directors. In order to determine fair value, investment companies need to assess the independence of the sources of input data, the valuation methodology and the resulting valuations. We believe that independent third-party valuation service providers with models that incorporate a broad range of inputs produce higher-quality valuations than those resulting from automated, mathematically driven models based on unobservable data. In addition, we believe data obtained from independent third-party sources can be invaluable in resolving valuation disputes between investment companies and their counterparties.[3] When market data is not readily available or reliable, we recommend that the SEC encourage the utilization of

[2] Ibid, page 68.

[3] For further details, please reference the Company's Comment Letter, submitted on August 29, 2011, regarding Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants (File Number S7-25-11), which was proposed by the Securities and Exchange Commission (Commission) on June 29, 2011.

independent sources of data by investment companies as inputs into their valuation models and/or as an integral part of their valuation methodologies.

- ***Transparency:*** Because there is no uniform way to determine valuation when market quotations are not readily available, we recommend greater levels of disclosure between counterparties as to how the valuation of a derivative was determined. By indicating whether the valuation was calculated based on inputs related to actual trade activity, using mathematical models, quotes and prices of other comparable securities, swaps, or derivatives, or a combination thereof, and whether those inputs were sourced directly or through third-party valuation service providers, the counterparty will be in a better position to assess the overall quality of the valuation. In addition, such disclosures would be in keeping with the Commission's proposed new rules relating to external business conduct standards for security-based swap dealers and major security-based swap participants (File Number S7-25-11). Related to this, we believe that this information could be cost-effectively and securely shared along with the valuation through a website or electronic platform that each counterparty could access.[4]

<u>Summary</u>

Interactive Data appreciates the opportunity to respond to the concept release on the Use of Derivatives by Investments Companies under the Investment Company Act of 1940 (RIN: 3235-AL22). We support the Commission in its mission to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. We believe that utilizing multiple sources of inputs, leveraging independent data sources, and providing transparency into derivative valuations are important elements for the Commission to consider should it formulate additional guidance for valuing derivatives.

We believe that third-party valuation service providers like Interactive Data will continue to play an important role in helping investment companies value derivatives. We would be happy to meet with the Commission staff to discuss our comments or our approach to OTC derivative valuations. We look forward to working with the Commission and the investment management industry on this important issue.

Sincerely,

Mark Hepsworth

Mark Hepsworth
President, Institutional Business
Interactive Data Corporation

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[4] Ibid

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Appendix

Comments to the Questions Posed in Section VI. Valuation of Derivatives of the Concept Release:

- **How do funds determine the fair values of derivatives that they hold? To what extent do valuation determinations depend upon the type of derivative, reference asset, trading venue, and other factors?**

In our experience, funds employ a variety of methods to determine the fair value of the derivatives that they hold. As the Commission noted, valuations for derivatives traded on a regulated exchange are generally far more straightforward to determine because market values for those securities are readily available. Those values may be sourced directly from the exchange by the fund or the fund may obtain values from a third-party provider who aggregates data from the exchanges along with other pricing and/or reference data. When market quotations are not readily available, however, funds must determine the fair value of derivatives that they hold. To do this, they may employ a wide range of approaches based on inputs related to actual trade activity, mathematical models, quotes and prices of other comparable securities, security-based swaps, or derivatives, or a combination thereof. For OTC derivatives, depending on the type of derivative and the availability of verifiable trading information, valuation techniques may include obtaining values from counterparties or others making a market in those securities, or using model-based valuations, either created by internal teams or provided by third-party sources. Valuation models themselves can vary widely from basic approaches, such as calculating the mean or average of contributor prices, to more sophisticated approaches using analytical software powered by complex mathematical models or by employing models that incorporate multiple market inputs.

The valuation determinations depend on a number of factors, including the type of derivative and reference asset. For OTC derivatives, there are a variety of inputs and sources that could also be considered, including benchmark curves from leading interdealer brokers, reference rates and trade details from both buy and sell-side market participants, and related trading activity from cash markets. The trading venue is generally not regarded as a relevant factor when valuing OTC derivatives. Interactive Data's derivative valuation services utilize a broad range of market inputs from multiple sources. In addition, for OTC derivatives in particular, Interactive Data has traditionally delivered valuations for these instruments that reflect a mid market approach, although valuation approaches may vary across the industry.

- **How do funds, when fair valuing derivatives, assess the accuracy and reliability of pricing information that is obtained from their counterparties or from other sources?**

In our experience, funds assess the accuracy and reliability of pricing information obtained from counterparties or other sources in several ways. Funds may employ more than one source to validate the fair value of a security when a market quotation is not readily available. For example, by obtaining valuations from two or more service providers, funds can assess the accuracy and reliability of the data they receive by comparing and contrasting the valuations from each source, as well as against pricing information received from counterparties or from internal valuation resources. In addition, this practice enables funds to mitigate operational risk should one of the service provider's reliability or quality be compromised. As mentioned above, Interactive Data's derivative valuation services utilize a broad range of market inputs from multiple sources.

When trying to assess the accuracy and reliability of pricing information, funds can significantly benefit from greater transparency into the inputs and processes used to determine those valuations. To that end, we are now providing our clients with a broader range of tools and information sources that offer greater transparency into the available market information and inputs considered in determining valuations. For example, our new Vantage℠ web application enables clients to visualize Interactive Data's evaluated prices within the context of a broad range of relevant market information, including public and proprietary market data inputs used in the evaluated pricing process.[1] Our efforts to improve transparency into fixed income markets also includes our collaboration with the Financial Industry Regulatory Authority (FINRA) to develop a set of reports providing transparency into U.S. structured securities, including an aggregate summary of daily transactions in U.S. structured securities by asset class.[2]

Furthermore, funds that obtain pricing information from a third-party valuation provider should be able to ask questions about those valuations. At Interactive Data, we provide clients with both traditional and online forums to support our clients' valuation inquiries – what we refer to as the "challenge process." This process is mutually beneficial – clients gain a better understanding about the inputs used in the valuation process while we may gain additional insight about the factors that market participants consider for valuation.

[1] For more information about Vantage, please visit http://www.interactivedata.com/VantageEvaluatedPricing/
[2] Please see Interactive Data's October 18, 2011 press release for more information about the Company's work with FINRA (http://news.interactivedata.com/press-release/product-news/interactive-data-and-finra-provide-transparency-structured-securities-mar).

- **Some derivatives held by funds may have negative values due to, among other things, changes in the value of the reference assets underlying the derivatives. Do funds calculate the values of such derivatives in the same manner as they value derivatives that have positive values? If not, why not?**

Interactive Data's OTC derivative valuations reflect either positive or negative values as a result of applying our methodologies and models consistently across the relevant coverage universe.

- **Should the Commission issue guidance on the fair valuation of derivatives under the Investment Company Act? If so, what issues should be addressed by that guidance?**

For the reasons outlined in our letter, Interactive Data believes that it is appropriate for the Commission to consider issuing additional principle-based guidance on the valuation of derivatives that takes into account the diversity and complexity of these instruments. We believe that principle-based guidance, rather than detailed prescriptive requirements, would help investment companies and investors more effectively and consistently value these instruments.

- **Are there special considerations that need to be taken into consideration for smaller funds? How might taking such considerations into account impact investor protection?**

The effective valuation of all assets within the fund's portfolio, regardless of the fund's size, is fundamental to protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation. We are not aware of any special considerations that should be taken into account for smaller funds should the Commission provide new guidance on the fair valuation of derivatives. With that said, firms of all sizes may be concerned about increased costs that could result from potential changes in valuation practices in order to comply with updated guidance. Nonetheless, we believe that there are currently many cost-effective valuation methods for funds of all sizes, including the availability of independent third-party valuation services.