Measuring and Rating Ethical Corporate Governance

January 18, 2011

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

By email: rule-comments@sec.gov

Re: SEC File Nos.: S7-22-10; S7-32-10; 4–619; S7-36-10; S7-34-10; S7-35-10

Dear Ms. Murphy:

Ethics Metrics LLC appreciates the opportunity to respond to the Securities and Exchange Commission's (the "SEC" or the "Commission") requests for comment listed below on proposed reforms by the President's Working Group on Financial Markets' ("PWG") study of possible money market fund reforms and proposed rules to implement certain provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act") and related federal securities laws.

- *Short Term Borrowing Disclosures,* SEC File No.: S7-22-10 (September 17, 2010). Due date for public comments: November 29, 2010.

- *Prohibition Against Fraud, Manipulation, and Deception in Connection with Security-Based Swaps*, SEC File No. S7-32-10 (November 3, 2010). Due date for public comments: December 23, 2010.

- *President's Working Group Report on Money Market Fund Reform*, SEC File No. 4–619, (November 8, 2010). Due date for public comments: January 10, 2011.

- *Implementing Amendments to the Investment Advisers Act of 1940,* SEC File No. S7-36-10; (November 19, 2010). Due date for public comments: January 24, 2011.

- *Regulation SBSR – Reporting and Dissemination of Security-Based Swap Information and Credit Default Swap Information,* File No. S7-34-10, (November 19, 2010). Due date for public comments: January 24, 2011.

- *Security-Based Swap Data Repository Registration Duties, and Core Principles,* File No. S7-35-10, (November 19, 2010). Due date for public comments: January 18, 2011.

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Ethics Metrics, Responsible Investing and Corporate Governance:

Ethics Metrics measures ethical corporate governance of U.S. financial companies and its impact on investment values by applying its Ethics Framework™ to evaluate undisclosed information for investors.

Factors evaluated range from the ethical and fiduciary standards for boards and senior management that include compliance by financial holding companies ("FHCs") with banking and securities regulations, which generates sustainable operations, to material compliance breaches and related audit risks that can lead to FHCs' reaching a troubled financial condition and generating ongoing systemic risk and investment risk.

Ethics Metrics' products and services include independent ratings, indices and reports that quantify the effect of FHCs' ethical and fiduciary conduct, including regulatory compliance, that is not disclosed to the public.

Ethics Metrics is a member of the UN PRI and the International Corporate Governance Network. (www.ethicsmetrics.com)

Summary of Comments:

Ethics Metrics is responding to the SEC's requests for comment cited in Addendum 3.

Our comments are offered in the spirit of the preamble of the Act, which states as its purpose "to promote the financial stability of the United States by improving accountability and transparency in the financial system, to end ''too big to fail'', to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices, and for other purposes."

Our comments also reflect the theme of Associate Director Mary Ann Gadzila's June 23, 2005 speech, "Rebuilding Ethics and Compliance in the Securities Industry." The theme of that speech is reinforced by the federal sentencing guidelines of 2010, as provided in §8B2.1 and in §8C2.5(f), by the United States Sentencing Commission. Both Ms. Gadzila's speech and the sentencing guidelines focus on ethics and compliance, as overseen by directors and senior management.

Our comments also respond to the concerns raised in the "Advance Notice of Proposed Rulemaking Regarding Authority To Require Supervision and Regulation of Certain Nonbank Financial Companies" by the Financial Stability Oversight Board, as published October 6, 2010 within the Federal Register (http://federalregister.gov/a/2010-25321). Please see Addendum 3 for a list of questions from this notice that are addressed in this letter.

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For an historical perspective on major events in the U.S. financial markets since the passage of the Gramm-Leach-Bliley Act ("GLBA") in 1999, please see Addendum 1. Addendum 2 contains the text of the determination of systemic risk on October 13, 2008 by the Secretary of the Treasury (after consultation with the President) upon the recommendation of the FDIC Board and the Federal Reserve Board, pursuant to the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA").

As things stand today, it is very difficult for shareholders and the general public to determine the true financial condition of FHCs. Are these institutions, so critical to the U.S. financial system and the American economy, operating safely and soundly within the parameters set by federal banking regulations? In many cases, inadequate FHC disclosure in public filings with the SEC has masked material financial weaknesses and corresponding violations of federal safety and soundness regulations that lead to FHCs' reaching a troubled financial condition that generates (1) systemic risk both for the institution and the financial system and (2) investment risks for investors, including securities law violations. Accurate and complete disclosure by FHCs ensures integrity and efficient pricing in valuation models and the capital markets. This enables reallocation of capital based on actual regulatory compliance, achieving the goals of the Act by preventing systemic risk and promoting institutional sustainability. Full disclosure will also enable money market funds ("MMFs"), registered investment advisers ("RIAs"), private funds ("PFs") and securities-based swap ("SBS") dealers to value securities more accurately, manage risk more effectively and comply fully with the Act's mandate, in Sections 404, 405, 763 and 766, to report on exposure to counterparty credit risks and systemic risk.

Ethics Metrics respectfully submits the following points for consideration by the SEC with respect to the proposed rules listed above:

1. Five major, interconnected risks, listed below, hamper the ability of MMFs, PFs, RIAs, and SBS dealers to comply with the proposed regulations concerning efficient reporting and valuation of short term borrowing, commercial paper, counterparty credit risks, systemic risk, equity investment values, debt values, credit default swaps ("CDSs"), and SBSs for FHCs.

2. Post-trade transactions in SBSs should be disclosed, as recommended in Release No. 34-63347 under Proposed Rule 901(c), to all market participants in order to reveal counterparty credit risks and systemic risk and provide material information to eliminate inefficiencies in pricing FHC debt and equity in the U.S. capital markets.

3. Reporting and valuation models for counterparty credit risks and systemic risk should include independent, third-party data in order to (1) address the risk

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factors listed below and (2) provide an independent baseline to measure historical and future levels of systemic risk. This addresses the SEC's request for comments in the *President's Working Group Report on Money Market Fund Reform*, Release No. IC–29497 dated November 8, 2010, and the *Security-Based Swap Data Repository Registration Duties, and Core Principles,* Release No. 34-63347 dated November 19, 2010.

Five Major, Interconnected Risk Factors Impact the Proposed Rules:

The SEC should consider the following factors that complicate the common tasks of MMFs, PFs, RIAs and SBS dealers in measuring, managing and reporting on exposure to counterparty credit risks and systemic risk and to integrate these risks into valuation models:

1. Many FHC Boards of Directors are failing to govern in accordance with their ethical and fiduciary duty to achieve sustainable operations, as required by federal banking regulations, for the benefit of shareholders, investors and the national economy. At a minimum, fiduciary duty includes the obligation to operate in full compliance with applicable banking and securities regulations. Significantly, many FHCs do not disclose whether or not they are in compliance with federal safety and soundness banking regulations and, critically, whether or not they are in a troubled condition and require federal financial assistance to cease causing systemic risk. These are material disclosure omissions that qualify as material misstatements and a material weakness in internal controls over financial reporting ("ICFR"). Correcting such misstatements requires restatements of misleading financial statements, in itself another material weakness. FHCs have not disclosed the potential cost of restatements to investors. A third material weakness is the certification by the CEO and CFO that ICFR are effective, despite the presence of one or more material weaknesses. Doing so constitutes fraud, yet another material weakness. Collectively, these three material weaknesses reflect a fourth and final material weakness: ineffective oversight of FHC external financial reporting and ICFR by FHC audit committees. Material weaknesses of this kind lead to:
   a. Breaches of the fiduciary duty of FHC boards of directors to oversee compliance with safety and soundness regulations, the securities laws and the listing standards of the U.S. exchanges;
   b. Inefficient pricing in the capital markets of debt and equity securities issued by FHCs;
   c. FHCs' reaching a troubled condition, including contributing to the Treasury Secretary's systemic risk determination on October 13, 2008

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(see Addendum 2);

d. Violations of SEC Rule 10b-5. These include undisclosed violations of safety and soundness regulations that misrepresent the actual financial condition of FHCs, leading in turn to misrepresentations in FHC registration statements, mispricing in the capital markets and deepening the troubled condition of FHCs, in turn leading to systemic risk and federal bailouts provided by TARP, the FDIC Debt Guarantee Program, financing by the Federal Reserve, the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility ("AMLF") and the Temporary Guarantee Program for Money Market Funds.

e. Limitations on borrowing, including from the Federal Reserve's Discount Window and the special primary and secondary liquidity facilities, based on the actual regulatory compliance of each FHC. Due to the failure of FHCs to disclose their actual regulatory compliance with safety and soundness regulations, the public and the capital markets do not know the true financial condition or the legal borrowing capacity of FHCs.

f. Severe economic consequences for FHCs that fail to remain in compliance as a FHC. Federal Reserve Rule 12 §225.83 defines procedures to cure underlying violations of safety and soundness regulations that contribute to a troubled condition. These include required remediation of compliance violations within 180 days. If violations are not cured within 180 days, the Federal Reserve may, under section (e)1, force the FHC to divest ownership or control of any depository institution owned or controlled by the FHC. "A company may comply with an order issued under paragraph (e)(1) of this section by ceasing to engage (both directly and through any subsidiary that is not a depository institution or a subsidiary of a depository institution) in any activity that may be conducted only under section 4(k), (n), or (o) of the BHC Act (12 U.S.C. 1843(k), (n), or (o))." Section 4(k) refers to financial activities that were provided by investment banks prior to enactment of the GLBA.

g. Delisting of securities by U.S. securities exchanges due to violations of exchange corporate governance listing standards. Violations include ineffective internal controls over financial reporting as well as violations of the Code of Ethics referred to in Section 406 of the Sarbanes-Oxley Act.

h. Claw backs of excess executive compensation based on restatements of material misstatements in FHC financial statements and annual reports;

i. Material disclosure omissions on the part of FHCs. These undermine a

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primary objective of the Act: that RIAs, PFs and SBS dealers report their exposure to systemic risk and counterparty credit risk and, in the case of PFs and RIAs, explain how they incorporate these risks into their valuation models.

i. Release No. 34-63346, *Regulation SBSR – Reporting and Dissemination of Security-Based Swap Information and Credit Default Swap Information*, states that the Act is intended to bring transparency to information asymmetries that create an opaque and inefficient capital market for pricing the systemic risk and counterparty credit risk of FHCs.

ii. Release No. 34-63236, *Prohibition Against Fraud, Manipulation, and Deception in Connection with Security-Based Swaps*, is "intended to prevent fraud, manipulation, and deception in connection with the offer, purchase or sale of any security-based swap, the exercise of any right or performance of any obligation under a security-based swap, or the avoidance of such exercise or performance."

j. Audit risks as defined in paragraph 2 below;

k. "Falsification of accounting records" under the U.S. Foreign Corrupt Practices Act;

l. Violations of the compliance and ethics provisions of the federal sentencing guidelines of 2010; and

m. Required remediation of compliance violations by FHCs so that:

i. FHCs and federally insured depository institutions act ethically and in a sustainable manner thus preventing FHCs' reaching a troubled condition and generating systemic risk;

ii. FHCs remain in compliance as a FHC and not suffer the consequences of non-compliance; and

iii. FHCs remain in compliance with the corporate governance listing standards of U.S. securities exchanges thereby avoiding the risk of delisting of securities by those exchanges.

2. Audit risks mask the true financial condition of FHCs due to the inherent limitations of generally accepted accounting principles ("GAAP") and internal controls over financial reporting ("ICFR") in detecting and reporting material compliance violations and related material misstatements. For relevant definitions please see SAS 107, AU Section 312.02[1]; SAS 107, AU Section 312.17[1]; GAAP by SAS 54, 317.07[2] and ICFR by Sarbanes-Oxley 404[3].

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a. The basic definition of audit risk is that GAAP and ICFR do not include an analysis of regulatory compliance, except when the auditor detects, in the course of the audit, material compliance violations or illegal acts that represent material misstatements. In the case of material misstatements, auditors have an obligation to report them to management and the board of directors, and if those material misstatements are not remedied, then to the SEC.

[1] www.aicpa.org/Research/Standards/AuditAttest/DownloadableDocuments/AU-00312.pdf
[2] www.aicpa.org/Research/Standards/AuditAttest/Pages/SAS.aspx
[3] http://www.sec.gov/rules/final/33-8238.htm#P167_36196

b. The Basel Committee on Banking Supervision cites audit risks as a material risk for the quality of audits in *External audit quality and banking supervision*, dated December 2008. The paper (www.bis.org/publ/bcbs146.pdf) states that:

i. "A perceived lack of transparent financial information from banks and across the financial system as a whole was a major factor of the current market crisis. It also has the potential to widen the expectations gap[12] for audits." Footnote 12 defines expectations gap as follows:

1. [12] "The expectations gap refers to the gap between an auditor's required standard of performance during a financial statement audit and public expectations of the auditor's performance during the audit. Some examples include the mistaken expectations that: 1) auditors should accept primary responsibility for the financial statements, 2) a *clean* or unqualified opinion guarantees the accuracy of financial statements, 3) auditors check all transactions, 4) auditors must provide early warnings about the possibility of business failure and 5) auditors have a responsibility to detect all fraud."

ii. "Currently, no tool exists to measure audit quality, but there are recent efforts to evaluate how to measure audit quality."

3. The Act's definition of systemic risk does not incorporate the elements of systemic risk and related safety and soundness contained in FDICIA and the GLBA. In addition, the proposed rules do not refer to or quantify historical trends of systemic risk within the U.S. banking system since 2001, either for the purpose of restating misleading financial statements or as a benchmark for the measurement and valuation of systemic risk. The lack of a clear definition of systemic risk in the Act and the lack of historical metrics on the sources of systemic risk in the Act and the proposed rules mask the

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fundamental source of systemic risk. The proposed rules do not address the core source of systemic risk. The core source of systemic risk is FHCs' failure to operate in compliance with federal safety and soundness regulations and failure to disclose non-compliance. The proposed rules increase the risk that MMFs, RIAs and PFs will be subject to additional regulation if the Financial Stability Oversight Council should determine that they are a source of systemic risk and thus "pose a threat to the financial stability of the United States."

4. Section 939 of the Act further complicates the reporting and pricing of counterparty credit risk by removing the requirement of credit ratings of securities issues from all federal statutes. Compounding this problem is that the quality of credit ratings on the senior debt of FHCs has been compromised by undisclosed material weaknesses in ICFR that mask the true financial condition of FHCs. In the short term, removing the credit rating requirement will generate confusion in the capital markets due to the lack of a reliable, independent standard to assess the credit-worthiness of FHCs. These risk factors contribute to mispricing in short-term debt, long-term debt and credit default swaps and the potential for liquidity events in the case of material downgrades of credit ratings for certain FHCs should the true financial condition of those FHCs become widely known.

5. A fundamental concept that is missing in the proposed rules is that systemic risk results from undisclosed material violations of safety and soundness regulations on the part of FHCs and banks, in violation of securities regulations including Rule 10b-5. These violations impede efficient pricing in the capital markets of the equity and debt securities, CDSs, and SBSs issued by FHCs.

In closing, we wish to thank the Commission for providing the public the opportunity to comment on these very important issues. We would be pleased to discuss any of our comments with you at your convenience.

Respectfully submitted,

/s/ Beckwith B. Miller, CEO

Enclosures:

Addendum 1: Timeline of Events
Addendum 2: October 13, 2008 – Systemic Risk Determination
Addendum 3: List of Requested Comments

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Addendum 1: Timeline of Events

1	Congress	Gramm-Leach-Bliley Act (GLBA) Approved	11/12/1999
2	FRB	Primary Credit, Secondary Credit, effective 1-9-03	1/9/2003
3	FRB	Term Auction Facility (TAF) approved	12/17/2007
4	FRB	FRBNY extended credit to Maiden Lane LLC (Bear Stearns and JPMorgan Chase)	6/26/2008
5	FRB	Approves Discount Window Lending to Fannie Mae, Freddie Mac	7/13/2008
6	U.S. Treasury	Fannie Mae Conservatorship	9/7/2008
7	U.S. Treasury	Freddie Mac Conservatorship	9/7/2008
8	News	Bankruptcy of Lehman Brothers Holdings Inc.	9/15/2008
9	Congress	Emergency Economic Stabilization Act (EESA) and TARP Approved by Congress	10/3/2008
10	President, U.S. Treasury, FDIC, FRB:	Systemic Risk Determination (SRD): The FDIC's establishment of the TLG Program was preceded by a determination of systemic risk by the Secretary of the Treasury (after consultation with the President), following receipt of the written recommendation of the Board on October 13, 2008, along with a similar written recommendation of the Board of Governors of the Federal Reserve System (FRB).	10/13/2008
11	FRB	FRB Board Approval of Systemic Risk Determination (SRD)	10/13/2008
12	FDIC	Systemic Risk Determination (SRD) as part of TLGP	10/13/2008
13	FDIC	FDIC Announces Plan to Free Up Bank Liquidity: TLGP: No SRD	10/14/2008
14	FDIC	Statement by FDIC Chairman Bair: No SRD	10/14/2008
15	FDIC, FRB, Treasury	Joint Statement by Treasury, Federal Reserve, and FDIC: Systemic Risk Determination (SRD); Healthy Institutions	10/14/2008
16	FDIC	Temporary Liquidity Guarantee Program (TLGP) Approved	10/14/2008
17	U.S. Treasury	Secretary Paulson: nine healthy institutions - TARP	10/14/2008
18	FRB	FRBNY: Begins extending credit to Maiden Lane III LLC (AIG)	11/28/2008
19	FRB	Announces Term Asset-Backed Securities Loan Facility (TALF)	11/28/2008
20	FRB	FRBNY: Begins extending credit to Maiden Lane II LLC (AIG)	12/12/2008
21	Congress	Dodd-Frank Act (DFA) Approved	7/21/2010

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Addendum 2: Systemic Risk Determination, Dated October 13, 2008

"Section 141 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), Pub. L. No. 102-242 (Dec. 19, 1991), added Section 13(c)(4)(G) to the Federal Deposit Insurance Act (FDI Act), 12 U.S.C. 1823(c)(4)(G). That section authorizes action by the federal government in circumstances involving a systemic risk to the nation's financial system. On October 13, 2008, in response to the unprecedented disruption in credit markets and the resultant effects on the abilities of banks to fund themselves and to intermediate credit, the Secretary of the Treasury (after consultation with the President) made a determination of systemic risk following receipt of the written recommendation of the FDIC Board, along with the written recommendation of the Federal Reserve Board, in accordance with Section 13(c)(4)(G). The systemic risk determination allows the FDIC to take certain actions to avoid or mitigate serious adverse effects on economic conditions or financial stability. Pursuant to the systemic risk determination, the FDIC Board established the Temporary Liquidity Guarantee (TLG) Program.[1]"

[1]http://edocket.access.gpo.gov/2008/E8-30555.htm

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Addendum 3: List of Requested Comments by SEC for File Nos.: S7-22-10; S7-32-10; 4–619; S7-36-10; S7-34-10; S7-35-10 and the Financial Stability Oversight Council's *Advance Notice of Proposed Rulemaking Regarding Authority To Require Supervision and Regulation of Certain Nonbank Financial Companies*

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Short Term Borrowing Disclosures
Date of Proposed Rule: September 17, 2010
File No.: S7-22-10
Release Nos. 33-9143; 34-62932;
Federal Register Publication Date; September 28, 2010
Dodd-Frank Sections 721(b), 761(a), 774
Comments due by November 29, 2010
SUMMARY: We are proposing amendments to enhance the disclosure that registrants provide about short-term borrowings. Specifically, the proposals would require a registrant to provide, in a separately captioned subsection of Management's Discussion and Analysis of Financial Condition and Results of Operations, a comprehensive explanation of its short-term borrowings, including both quantitative and qualitative information. The proposed amendments would be applicable to annual and quarterly reports, proxy or information statements that include financial statements, registration statements under the Securities Exchange Act of 1934, and registration statements under the Securities Act of 1933. We are also proposing conforming amendments to Form 8-K so that the Form would use the terminology contained in the proposed short-term borrowings disclosure requirement.
Requests for Comments: 1. Is information about short-term borrowings and intra-period variations in the level of short-term borrowings useful to investors? If so, should we require specific line item disclosure of this information in MD&A, as proposed, or would existing MD&A requirements for disclosure of liquidity and capital resources provide sufficient disclosure about these issues? If a specific MD&A requirement would be appropriate, does the proposed requirement capture the type of information about short-term borrowings that is important to investors? If not, how should we change the proposed requirement? 34. Should bank holding companies be required to include the same level of disclosure of leverage and capital ratios for quarterly financial statements as they do for annual financial statements, rather than quarterly reporting of material changes? Should additional disclosures be required to accompany existing ratio disclosure that would make it more meaningful? III. GENERAL REQUEST FOR COMMENT We request and encourage any interested person to submit comments on any aspect of our proposals, other matters that might have an impact on the

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amendments, and any suggestions for additional changes. With respect to any comments, we note that they are of greatest assistance to our rulemaking initiative if accompanied by supporting data and analysis of the issues addressed in those comments and by alternatives to our proposals where appropriate.

Advance Notice of Proposed Rulemaking Regarding Authority To Require Supervision and Regulation of Certain Nonbank Financial Companies
Date of Proposed Rule: October 6, 2010
Federal Register Publication Date; October 6, 2010 (http://federalregister.gov/a/2010-25321).
Comments due by: November 5, 2010
SUMMARY: Section 113 of the Dodd- Frank Wall Street Reform and Consumer Protection Act (the ''DFA'') gives the Financial Stability Oversight Council (the ''Council'') the authority to require that a nonbank financial company be supervised by the Board of Governors of the Federal Reserve System (''Board of Governors'') and subject to prudential standards if the Council determines that material financial distress at such a firm, or the nature, scope, size, scale, concentration, interconnectedness, or mix of the activities of the firm, could pose a threat to the financial stability of the United States. This advance notice of proposed rulemaking (ANPR) invites public comment on the criteria that should inform the Council's designation of nonbank financial companies under the DFA.
Requests for comments: II. Criteria for Designation 1. What metrics should the Council use to measure the factors it is required to consider when making determinations under Section 113 of DFA? a. How should quantitative and qualitative considerations be incorporated into the determination process? b. Are there some factors that should be weighted more heavily by the Council than other factors in the designation process? 2. What types of nonbank financial companies should the Council review for designation under DFA? Should the analytical framework, considerations, and measures used by the Council vary across industries? Across time? If so, how?

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4. Are there simple metrics that the Council should use to determine whether nonbank financial companies should even be considered for designation?

5. How should the Council measure and assess the scope, size, and scale of nonbank financial companies?

> c. How should the Council take managed assets into consideration in making designations? How should the term ‘‘managed assets’’ be defined? Should the type of asset management activity (e.g., hedge fund, private equity fund, mutual fund) being conducted influence the assessment under this criterion? How should terms, conditions, triggers, and other contractual arrangements that require the nonbank financial firm either to fund or to satisfy an obligation in connection with managed assets be considered?

6. How should the Council measure and assess the nature, concentration, and mix of activities of a nonbank financial firm?

7. How should the Council measure and assess the interconnectedness of a nonbank financial firm?

> a. What measures of exposure should be considered (e.g., counterparty credit exposures, operational linkages, potential future exposures under derivative contracts, concentration in revenues, direct and contingent liquidity or credit lines, cross-holding of debt and equity)? What role should models of interconnectedness (e.g., correlation of returns or equity values across firms, stress tests) play in the Council's determinations?
>
> b. Should the Council give special consideration to the relationships (including exposures and dependencies) between a nonbank financial company and other important financial firms or markets? If so, what metrics and thresholds should be used to identify what financial firms or markets should be considered significant for these purposes? What metrics and thresholds should be used in assessing the importance of a nonbank financial company's relationships with these other firms and markets?

10. How should the Council take into account the fact that a nonbank financial firm (or one or more of its subsidiaries or affiliates) is already subject to financial regulation in the Council's decision to designate a firm? Are there particular aspects of prudential regulation that should be considered as particularly important (e.g., capital regulation, liquidity requirements, consolidated

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supervision)? Should the Council take into account whether the existing regulation of the company comports with relevant national or international standards? 11. Should the degree of public disclosures and transparency be a factor in the assessment? Should asset valuation methodologies (e.g., level 2 and level 3 assets) and risk management practices be factored into the assessment? 13. Please provide examples of best practices used by your organization or in your industry in evaluating and considering various types of risks that could be systemic in nature. a. How do you approach analyzing and quantifying interdependencies with other organizations? b. When and if important counterparties or linkages are identified, how do you evaluate and quantify the risks that a firm is exposed to? c. What other types of information would be effective in helping to identify and avoid excessive risk concentrations that could ultimately lead to systemic instability? 14. Should the Council define ''material financial distress'' or ''financial stability''? If so, what factors should the Council consider in developing those definitions? 15. What other risk-related considerations should the Council take into account when establishing a framework for designating nonbank financial companies?

Prohibition Against Fraud, Manipulation, and Deception in Connection with Security-Based Swaps
Date of Proposed Rule: November 3, 2010
File No.: S7-32-10
Release No. 34-63236
Federal Register Publication Date: November 8, 2010
Dodd-Frank Sections 721(b), 761(a), 774
Comments due by December 23, 2010
SUMMARY: The Securities and Exchange Commission (''Commission'') is proposing for comment a new rule under the Securities Exchange Act of 1934 (''Exchange Act'') that is intended to prevent fraud, manipulation, and deception

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in connection with the offer, purchase or sale of any security-based swap, the exercise of any right or performance of any obligation under a security-based swap, or the avoidance of such exercise or performance.
Benefits: Proposed Rule 9j-1 would specify that it is unlawful for any person, directly or indirectly, in connection with the offer, purchase or sale of any security-based swap, the exercise of any right or performance of any obligation under a security based swap, or the avoidance of such exercise or performance, to: (a) to employ any device, scheme, or artifice to defraud or manipulate; (b) to knowingly or recklessly make any untrue statement of a material fact, or to knowingly or recklessly omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; (c) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or (d) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.33 Thus, proposed Rule 9j-1 would prohibit the same misconduct as Exchange Act Section 10(b) and Rule 10b-5 thereunder, and Securities Act Section 17(a)34 but would also explicitly reach misconduct that is in connection with the “exercise of any right or performance of any obligation under” a security-based swap. In other words, proposed Rule 9j-1 would apply to offers, purchases and sales of security-based swaps in the same way that the general antifraud provisions apply to all securities but would also explicitly apply to the cash flows, payments, deliveries, and other ongoing obligations and rights that are specific to security-based swaps. This would include, for example, misconduct that affects the market value of the security-based swap for purposes of posting collateral or making payments or deliveries under a security-based swap. Thus, the proposed rule would, among other things, prohibit a person who is a party to a security-based swap from later engaging in fraudulent conduct (<u>e.g.</u>, knowingly making a false or misleading statement) that affects the value of cash flow, payments, or deliveries, such as triggering the obligation of a counterparty to make a large payment or to post additional collateral.
Request for comments: On Page 15, Please discuss how and to what extent the proposed rule may affect issuers, broker-dealers, security-based swap dealers, major security-based swap participants, and other swap market participants.

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On Pages 15 and 16, Although much of the activity that would be prohibited by the proposed rule is already prohibited by the general antifraud and anti-manipulation provisions of the federal securities laws (e.g., Exchange Act Section 10(b) and Rule 10b-5 thereunder, and Securities Act Section 17(a)), to what extent, if any, would the proposed rule affect the nature of the security-based swap market in general, including the extent or nature of information shared between market participants? If so, in what ways and to what degree? Are there any legitimate market activities that the proposed rule could have the effect of discouraging? Commenters are invited to provide specific examples of any such activities and any such potential effect. On Page 16, Are there any specific issues with respect to the application of the proposed rule to fraudulent, manipulative, or deceptive activity involving security-based swaps (including the reference underlying of such security-based swaps) that are or will be effected on or through security-based swap execution facilities or national securities exchanges, or over-the-counter?

President's Working Group Report on Money Market Fund Reform
Date of Proposed Rule: November 3, 2010 http://www.sec.gov/rules/other/otherarchive/other2010.shtml
File No. 4–619
Release No. IC–29497
Federal Register Publication Date: November 8, 2010 http://edocket.access.gpo.gov/2010/pdf/2010-28241.pdf
Comments due by January 10, 2011
Summary: "The Securities and Exchange Commission (''Commission'' or ''SEC'') is seeking comment on the options discussed in the report presenting the results of the President's Working Group on Financial Markets' study of possible money market fund reforms. Public comments on the options discussed in this report will help inform consideration of reform proposals addressing money market funds' susceptibility to runs."
Requests for Comments: We request comments on the options described in the Report both individually and in combination. Commenters should address the effectiveness of the options in mitigating systemic risks associated with money market funds, as well as their potential impact on money market fund investors, fund managers, issuers of short-term debt and other stakeholders. We also are interested in comments on other issues commenters believe are relevant to further money market fund

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reform, including other approaches for lessening systemic risk not identified in the Report.

Implementing Amendments to the Investment Advisers Act of 1940
Date of Proposed Rule: November 19, 2010
File No. S7-36-10
Release No. IA-3110
Federal Register Publication Date: December 10, 2010: Link http://www.federalregister.gov/articles/2010/12/10/2010-29956/rules-implementing-amendments-to-the-investment-advisers-act-of-1940
Dodd-Frank Sections 404, 405
Comments due by January 24, 2011
Background: Dodd-Frank Section 404 states (*emphasis added*): (3) REQUIRED INFORMATION.—The records and reports required to be maintained by an investment adviser and subject to inspection by the Commission under this subsection shall include, for each ***private fund*** advised by the investment adviser, a description of— (A) the amount of assets under management and use of leverage, including off-balance-sheet leverage; (B) **counterparty credit risk exposure;** (C) **trading and investment positions;** (D) **valuation policies and practices of the fund;** (E) types of assets held; (F) side arrangements or side letters, whereby certain investors in a fund obtain more favorable rights or entitlements than other investors; (G) trading practices; and (H) such other information as the Commission, in consultation with the Council, determines is necessary and appropriate in the public interest and for the **protection of investors** or for the assessment of **systemic risk,** which may include the establishment of different reporting requirements for different classes of fund advisers, based on the type or size of private fund being advised.
SEC request for comments: On pages 22 and 23, the SEC requests "comment on our proposed changes to the instructions relating to the calculation of "regulatory assets under management." Are changes to the rule and instructions necessary? Should we

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instead consider different changes? If so, in what way should we amend them?

Regulation SBSR – Reporting and Dissemination of Security-Based Swap Information and Credit Default Swap Information
Date of Proposed Rule: November 19, 2010
File No. S7-34-10
Release No. 34-63346
Federal Register Publication Date: December 2, 2010: Link http://www.federalregister.gov/articles/2010/12/02/2010-29710/regulation-sbsrreporting-and-dissemination-of-securitybased-swap-information
Dodd-Frank Sections 763, 766
Comments due by January 18, 2011
Background: Security-Based Swaps (SBS) On page 21, the Commission discusses below the SBS data that would be required to be reported in real time, and which would be publicly disseminated. 1. Asset class Proposed Rule 901(c)(1) would require the reporting party to report the asset class of the SBS and, if the SBS is an ***equity derivative***, whether the SBS is a total return swap or is otherwise designed to offer risks and returns proportional to a position in the ***equity security or securities*** on which the SBS is based. Proposed Rule 900 would define "asset class" to mean those SBSs in a particular broad category, including, but not limited to, ***credit derivatives, equity derivatives, and loan-based derivatives.*** The Commission believes that identifying the asset class would provide market participants with basic information about the SBS transaction to identify the type of SBS being publicly reported. In addition, requiring the reporting party to indicate whether the SBS is an equity total return swap or is otherwise designed to offer risks and returns proportional to a position in the equity security or securities on which the SBS is based would enable a registered SDR to know if the SBS was excluded from being a block trade. 1. "Valuation models" – cited 6 times. a. The SEC states on pages 226 and 227 that, "***Valuation models*** could be improved to the extent that they consider last-sale reports of the

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asset to be valued, reports of related assets, or reports of benchmark products that include the asset to be valued or closely related assets, even if those reports are dated. There is evidence to suggest that post-trade transparency helps reduce the range of valuations of assets that trade in illiquid markets.[314] Thus, post-trade transparency in the SBS market could result in more accurate valuations of SBSs generally – particularly if trade information is used as an input to, rather than a substitute for, independent valuations by other market participants – as it would allow all market participants to know how SBS counterparties priced the SBS at a specific point in time. ***<u>Especially with complex instruments, investment decisions generally are predicated on a significant amount of due diligence to value the instruments properly.</u>*** A post-trade transparency system permits other market participants to derive at least some informational benefit from obtaining the views of the two counterparties who did a particular trade.

b. Furthermore, better valuations could create a benefit in the form of more efficient capital allocation, which is premised on accurate knowledge of asset prices. Asset prices that are too high could result in a misallocation of capital, as investors demand more of an asset that cannot deliver an economic risk-adjusted return. By the same token, assets that are inappropriately undervalued could represent investment opportunities that will likely not receive enough capital because investors do not realize that a good risk-adjusted return is available. To the extent that post-trade transparency of SBS transactions enables asset valuations to move closer to their fundamental value, capital could be more efficiently allocated.

c. Better valuations resulting from post-trade transparency of SBSs also could reduce prudential and systemic risks. Some financial institutions, including many of the most systemically important financial institutions, have large portfolios of SBSs. The financial system could benefit if the portfolios of these institutions were more accurately valued. To the extent that post-trade transparency affirms the valuation of an institution's portfolio, regulators, the individual firm, and the market as a whole could be more certain as to whether the firm would or would not pose prudential or systemic risks. In some cases, however, post-trade transparency in the SBS market might cause an individual firm to revalue its positions and lower the overall value of its portfolio. The sooner that accurate valuations can be made, the more quickly that regulators and the individual firm could take appropriate steps to

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minimize the firm's prudential risk profile, and the more quickly that regulators and other market participants could take appropriate steps to address any systemic risk concerns raised by that firm."
SEC request for comments: On page 18, the "Commission requests comment generally on all aspects of the categories of information that would be required to be reported in real time (under Proposed Rule 901(c)(1)) for public dissemination. On page 28, the SEC asks, "13. Do commenters agree with the proposed categories of information that would be required to be reported in real time for public dissemination? If not, what additional specific categories of information should be required to be reported in real time for public dissemination, and why? How would public dissemination of such additional information enhance price discovery or market liquidity?" On page 280, the SEC states that, "It is difficult at this stage to ascertain how proposed Regulation SBSR and other measures to implement the Dodd-Frank Act might increase or decrease participation in the SBS market, and what impacts such an increase or decrease might have on efficiency, competition, and capital formation. However, the Commission requests comment on those impacts."

Security-Based Swap Data Repository Registration Duties, and Core Principles
Date of Proposed Rule: November 19, 2010
File No. S7-35-10
Release No. 34-63347
Federal Register Publication Date: December 10, 2010: Link http://www.federalregister.gov/articles/2010/12/10/2010-29719/securitybased-swap-data-repository-registration-duties-and-core-principles
Dodd-Frank Section 763(1), 712(d), 712(a)(2), 728
Comments due by January 24, 2011
SEC request for comments: On pages 54 and 55, the Commission requests comment on the following specific issues: 1. In addition to the data already subject to the Commission's request, are there additional reports or sets of data that the Commission should consider

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obtaining from SDRs to evaluate systemic risk or that could be used for prudential supervision? (Page 54)

2. Besides the FDIC, should the Commission specify in its rules any other appropriate person to have access to all data maintained by an SDR (e.g., the Federal Reserve Bank of New York)? (Page 55)
3. Are there alternative ways that the Commission could address the indemnification provision while being consistent with Exchange Act Section 13(n)(5)(H)? (Page 55)
   a. Exchange Act Section 13(n)(5)G states[1]:
      i. (G) on a confidential basis pursuant to section 24, upon request, and after notifying the Commission of the request, make available all data obtained by the security-based swap data repository, including individual counterparty trade and position data, to—
         1. (i) each appropriate prudential regulator; (ii) the Financial Stability Oversight Council; (iii) the Commodity Futures Trading Commission; (iv) the Department of Justice; and (v) any other person that the Commission determines to be appropriate, including— (I) foreign financial supervisors (including foreign futures authorities); (II) foreign central banks; and (III) foreign ministries.
      ii. (H) CONFIDENTIALITY AND INDEMNIFICATION AGREEMENT.— Before the security-based swap data repository may share information with any entity described in subparagraph (G)—
         1. (i) the security-based swap data repository shall receive a written agreement from each entity stating that the entity shall abide by the confidentiality requirements described in section 24 relating to the information on security-based swap transactions that is provided; and
         2. (ii) each entity shall agree to indemnify the security-based swap data repository and the Commission for any expenses arising from litigation relating to the information provided under section 24. (ii) each entity shall agree to indemnify the security-based swap data repository and the Commission for any expenses arising from litigation relating to the information provided under section 24.

[1]Web site for Securities Exchange Act of 1934
http://www.sec.gov/about/laws/sea34.pdf

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