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Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549-0609

RE: Governance of Self-Regulatory Organizations, File No. S7-39-04

Dear Mr. Katz

I am writing to you on behalf of the Board of Administration, California Public Employees' Retirement System (CalPERS). CalPERS is the largest public pension system in the U.S., with approximately $184 billion in assets.

CalPERS is pleased to provide comment on the Commission's proposed new rules and amendments pertaining to the governance, administration, transparency and ownership of self-regulatory organizations ("SROs"). CalPERS shares the SEC's concerns about the governance of SROs and views these proposals as a positive step toward addressing these concerns. The proposals on board composition, director independence, independence of the regulatory function, and transparency should help mitigate, though not resolve, the conflicts inherent in the self-regulatory model. We particularly applaud the Commission for ensuring investor representation on each SRO board and for enhancing the transparency of SRO governance and compensation practices.

CalPERS would, however, like to suggest several revisions to clarify and strengthen the proposed rules and amendments. We are concerned that the proposed rules do not require that the investor representative on an SRO board be "independent" within the meaning of the rules. While the proposed rules provide that such a representative may not be associated with any member or broker dealer, they permit the representative to be affiliated with a listed company. We believe that such an affiliation could compromise the investor representative's ability to protect adequately the interests of investors. Therefore, the final rule should require that the investor representative be independent.

We applaud the SEC's efforts to ensure the independence of the SROs' regulatory functions. However, the current proposal does not require enough specific action to separate the regulatory and business components of the organizations. Merely requiring the SROs to develop policies and procedures in this area will not be sufficient where the rules do not specify what policies and procedures are required, or even what criteria will be used to determine the independence of the regulatory function from the business unit.

Moreover, it is unlikely that any policy or procedure will be able to protect an SRO's regulatory operation from business pressures as long as it constitutes merely one function in an integrated corporate entity. Therefore we urge the Commission to adopt the proposal, suggested in the Concept Release (File No. S7-40-04), that SROs be required to place their regulatory and market operations in separate corporate subsidiaries, as the NASD does at present. Such a separation could define more clearly the division between the SROs' regulatory and market functions, and, as the Concept Release suggests, foster an "independent attitude" in the regulatory subsidiary.

We also applaud the proposals on transparency. However, we are concerned that they do not require SROs to disclose more about their nominating processes. More disclosure in that area is critical to ensuring that the SROs comply in their obligations regarding director independence and investor representation. We therefore urge the SEC to require that SROs include in their governance guidelines detailed information about their nominating procedures, including their policy on considering nominations by investors and issuers, their process for identifying and evaluating nominees, and any specific minimum qualifications they believe must be met by candidates for director.

With respect to the Concept Release, CalPERS shares the SEC's concerns about the inherent conflicts between SROs' regulatory functions and their business operations. However, we believe the markets are best served by evolutionary, rather than revolutionary, change. Therefore, except for requiring that SROs place their regulatory and market operations in separate corporate subsidiaries, the SEC should hold off on implementing the more stringent reforms the Concept Release suggests. Instead, it should implement the current SRO governance proposal and observe the results, revisiting the issue if problems with SRO governance continue.

In summary, the new rules as proposed are significant improvements and we compliment the Commission for taking the appropriate steps toward improving SRO governance structures. We support the SEC's efforts and hope that our comments can be helpful.

Sincerely,

Mark Anson
Chief Investment Officer – CalPERS

cc: CalPERS Board of Administration
Fred Buenrostro, Chief Executive Officer – CalPERS