Written Statement
Prepared For: Securities and Exchange Commission
Field Hearing on the State of the Municipal Securities Market
Ratings – Impact and Practices

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Thank you for the opportunity to provide comments on Ratings in the Municipal Securities Market. My name is Dan Kiefer and I am a Portfolio Manager for Opportunistic Investments in the Global Fixed Income Unit of the California Public Employees' Retirement System (CalPERS). We welcome the SEC's information gathering efforts and look forward to working with them in the future.

CalPERS is the largest public pension fund in the United States with approximately $206 billion in global assets. CalPERS provides retirement benefits to more than 1.6 million public workers, retirees, their families and beneficiaries. As a large institutional investor with a long-term investment time horizon, CalPERS has a vested interest in maintaining the integrity and efficiency of the capital markets. We rely on the quality and integrity of market information to allocate capital on behalf of our beneficiaries and we believe that credit ratings provide a critical contribution to those decisions.

CalPERS maintains a limited but meaningful involvement with the Municipal Securities Market. In 2003, the CalPERS Board approved the Credit Enhancement Program (CEP) to provide credit and liquidity enhancements to States & municipalities nationwide. These letters and lines of credit allow municipalities to access short term debt markets and lower the overall borrowing costs.

CEP uses conservative underwriting standards to diversify the exposure to municipalities geographically and across sectors. As of August 31, 2010, CEP provides enhancement for 19 issues across eight States in the amount of $1.89 billion.

CalPERS CEP has two points of interaction with rating agencies in the context of the CEP and the Municipal Securities Market:

1) CalPERS is itself rated by the credit rating agencies, and
2) CalPERS requires each municipality it enhances to have, at a minimum, an investment grade rating from at least two credit rating agencies

We believe the rating agencies provide a valuable service in each of these regards, but there is always room for improvement.

Additionally, CalPERS Board endorses the principal that major rating agencies should rate municipal securities on a scale which is uniform, fair and consistent with other rated products, e.g. Global Ratings Scale. CalPERS encourages the SEC to use the authority under Dodd-Frank to require rating agencies to develop a uniform, risk based ratings standard that ends the differential treatment between municipal and corporate issuers.

In relation to recent calls for financial reform in general, CalPERS has proposed five specific reforms to the credit rating agencies. Current legislation through the Dodd-Frank Act takes action on 4 of the 5 recommendations and has provisions for further studies of alternative means to compensating credit ratings agencies that reduces conflicts of interest and provides incentives for accuracy and integrity.

CalPERS has provided the SEC with their specific suggestions for creating an alternative compensation system in other forums.

The Dodd-Frank Act addresses each of the other four recommendations for credit rating agencies (also referred to as Nationally Recognized Statistical Rating Organizations or NRSOs) as outlined below:

Congress and the Administration should bolster the SEC's position as a strong, independent overseer of credit rating agencies.

The Securities and Exchange Commission is the primary financial regulatory agency, as defined in section 2 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Section 932 (8) states the Commission shall establish within the Commission an Office of Credit Ratings to administer rules of the Commission –

(i) with respect to practices of NRSRO in determining ratings, for the protection of users of credit ratings and in the public interest

(ii) to promote accuracy in credit ratings issued by NRSRO and

(iii) to ensure that ratings are not unduly influenced by conflict of interest.

Credit rating agencies should be required to manage and disclose conflicts of interest and create an executive level compliance officer position.

Section 932, Enhanced regulation, Accountability and Transparency of NRSROs laid out numerous initiatives, rules and commission studies that are directed at mitigating conflict of interest risk. We support, at a minimum, the attestation requirement that each NRSO submit to the Commission on an annual basis an internal controls report. In the end, however, I am skeptical that a ratings analyst can be truly insulated from conflicts of interest in the present issuer-pays system. For, if you do not have a sales target, but your boss does, then you have a sales target.

Credit rating agencies should be held to a higher standard of accountability under federal law.

Section 931 (3) recognizes that credit rating agencies are gatekeepers and are fundamentally commercial in character and should be subject to the same federal standards of liability and oversight as apply to auditors, securities analysts, and investment bankers in connection with the offering and sale of securities.

Credit rating agencies should not rate products for which they lack sufficient information and expertise to assess.

Section 932 (r) Credit Ratings Methodology states the Commission shall prescribe rules for the protection of investors and in the public interest with respect to the procedures and methodologies including qualitative and quantitative data and models used by the NRSRO that require the NRSRO to in section (s) Transparency of Credit Methodologies and information reviewed, requiring disclosures on rating assumptions and methodologies.

Along with the full disclosure of the methodology employed by credit rating agencies, the credit rating agencies should comment on all factors identified in the process of making a decision to rate or not to rate a security or product. Further, the Office of Credit Ratings within the Commission should consider additional transparency requirements including a "ratings scorecard" to assess the practices, accuracy and effectiveness of the rating process via historical rating outcomes.

Thank you for this opportunity to share our comments on Ratings in the Municipal Securities Markets.