MORNINGSTAR®

22 West Washington Street
Chicago
Illinois 60602

Telephone: +1 312 696-6000
Facsimile: +1 312 696-6001

May 18, 2012

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

RE: Comments on File Number S7-12-10

Dear Ms. Murphy,

Morningstar, Inc. ("Morningstar") appreciates the opportunity to comment on the Securities and Exchange Commission's proposed amendments to rule 482 and 156 under the Securities Act of 1933 and rule 34b-1 under the Investment Company Act of 1940 regarding target-date retirement funds. We support the Commission's efforts to ensure target-date funds are presented in a manner that promotes understanding and transparency. Morningstar specifically commends the Commission's goal to improve and expand the information provided to target-date investors through marketing materials. Our response recognizes the positive features outlined in the proposal and also suggests sections that would benefit from additional review or deliberation.

Morningstar offers various products and services relating to target-date retirement funds through several research and business groups that operate independently from one another. This letter reflects the collective views of these entities.

- Morningstar's Fund Research Group offers Morningstar Target-Date Series Ratings and Reports, which are issued quarterly, as well as the annual Morningstar Target-Date Series Research Paper, which includes a section that specifically evaluates series' disclosure practices (http://corporate.morningstar.com/us/documents/MethodologyDocuments/MethodologyPapers/TargetDateFundSurvey_2012.pdf).
- Ibbotson Associates, a subsidiary of Morningstar, works directly with retirement-plan providers and individual plan sponsors to develop asset-allocation investment solutions for plan participants, writes practitioner-oriented papers, and publishes a quarterly report on the target-date industry.
- Morningstar's Investment Profiles team provides fact sheets and other tools to help retirement-plan participants make well-informed choices.
- Morningstar's Data unit collects data from target-date providers that appear in Morningstar's software, including Morningstar.com, and is delivered in data feeds to institutions, media outlets, and academics.

Target-date funds have become a key feature of employer sponsored defined-contribution plans. According to a recent study from Vanguard, one of the industry's largest target-date providers and retirement-plan record keepers, 82% of its retirement plans offer target-date funds (https://institutional.vanguard.com/VGApp/iip/site/institutional/researchcommentary/article/InvCommTDFPrevalent). The Pension Protection Act of 2006 allows target-date funds to be designated as Qualified Default Investment Alternatives Assets, which has accelerated the asset growth of these funds. At year-end 2011, Morningstar estimates that target-date mutual funds held approximately $378 billion, and billions more are invested in institutional and private target-date accounts, such as collective investment trusts, that are not yet required to disclose their assets under management.

The diversity of target-date funds has also grown. There are now 48 distinct target-date mutual fund series, each with their own interpretation of how a target-date fund should be constructed. While some target-date series are relatively straightforward, many of the industry's newest entrants are notable for their very distinctive designs.

Given the prominence of target-date funds in investors' retirement portfolios and the complexity of these investments, it's critical that target-date funds be held to a high standard for disclosure. Importantly, the disclosures need to be clear enough for beginner investors to comprehend, while also providing easy access to detailed information such that financial advisors, consultants, and plan sponsors can adequately assess the funds' potential risks and rewards. We believe a more comprehensive set of disclosure guidelines would improve investors' understanding of target-date funds.

Below please find our detailed comments which we hope will assist the Commission in further clarifying the proposal.

Not All Disclosures Are Made Equal

Morningstar supports the Commission's effort to improve investors' understanding of a target-date fund's asset allocation, but that goal would not be met by requiring each target-date fund to disclose its asset allocation at the target date adjacent to the first use of the fund's name in marketing materials. To be sure, Morningstar maintains that the series' asset-allocation at all points along the glide path be disclosed clearly as part of the funds' prospectus. Our objection specifically pertains to the proposed naming convention in the funds' marketing materials. Highlighting this one data point would be misleading. The proposed rule would overemphasize the importance of one point in time for an investment that's designed to change in order to serve investors well for decades. This disclosure would discount the significance of how the fund invests before and after that point, which collectively are more important to the funds' long-term performance and the investors' success. The single asset allocation at the target date does not provide sufficient insight into the broader glide path.

Moreover, the target-year allocation disclosure could be confusing. Most investors choose target-date funds within their defined-contribution plan, which typically offers just one target-date series. As a result, every fund in the series that precedes its target date would have the same asset allocation at the target date, even though the funds are designed for participants of varying ages and may have vastly different allocations at the time of enrollment. Also puzzling would be the current allocations disclosed on the funds that are past their target dates.

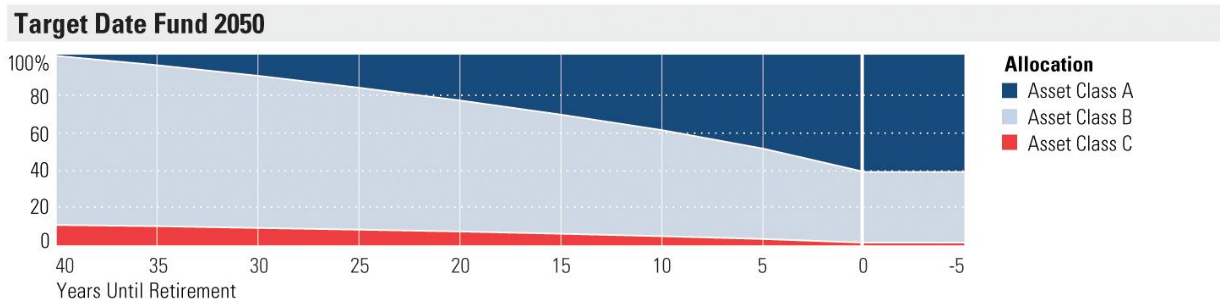
These asset-allocation numbers cited with the funds' name would lack meaningful context. Most plan participants are not familiar with a comparable industry average, or the expected returns and volatility associated with such an allocation. In addition, listing the allocation at the target date could be misinterpreted as a fund's final allocation, even though many target-date funds continue to change the asset allocation after the target date.

Visual Representation Is Better

Instead of highlighting the funds' asset allocations at a single point, Morningstar supports requiring marketing materials for target-date funds to include a graphical depiction of the asset allocation over time (a "glide path"). The Commission's sponsored study found that respondents who reviewed documents containing a glide path illustration better understood target-date funds than those who reviewed documents without the illustration. Most of the industry already perceives the glide-path graphic as an important part of disclosure.

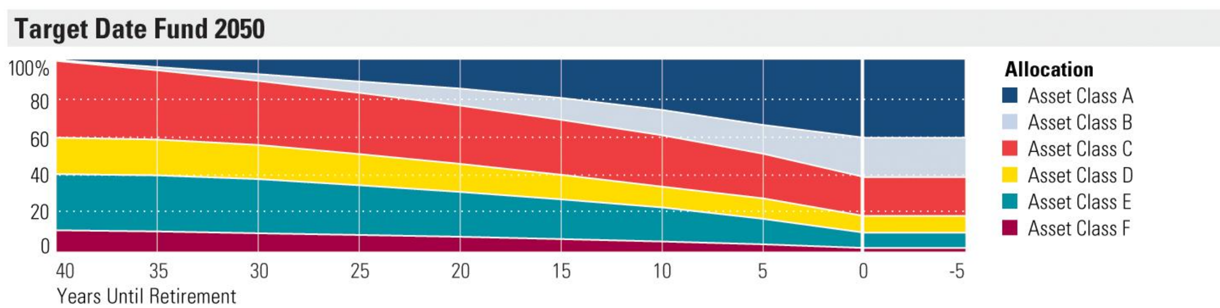
This disclosure would be even more effective if detailed guidelines for glide-path disclosure were provided. For example, based on our experience, we see that it is common for series' current disclosure to outline expected allocations to stocks and bonds, but not necessarily allocations to non-traditional asset classes, including commodities and alternative strategies. Target-date providers should retain some flexibility as to how they graphically represent their glide paths, but meaningful asset class exposures need to be clearly disclosed to investors. Allocations to those less-traditional asset classes can have a significant impact on series' risk profiles. As such, Morningstar suggests that target-date funds disclose intended allocations to broad asset classes representing more than 10% of a fund's assets, and such exposures should be included in the glide-path graphic. The target-date industry would benefit from clear guidelines from the Commission, outlining what types of investments constitute each broad asset class.

We suggest that series present glide-path graphics that include a minimum of three asset-class exposures, such as the example below:



Source: Morningstar, Inc.

Even better would be a graphic that includes a more-detailed depiction of asset-class exposures at all points along the glide path. The example below reflects a chart with six asset classes.



Source: Morningstar, Inc.

Glide-path illustrations are a useful way to explain target-date funds to investors, but those who are choosing a target-date series for a retirement plan--advisors, consultants, and plan sponsors--need additional detail to fully assess the series' potential risks and returns. Below is an example from an existing target-date fund prospectus. It includes this table which we believe provides information that can be used to support that assessment process:

Years to Target Retirement Date	40	35	30	25	20	15	10	5	0	-5	-10
Equity	85.0%	85.0%	85.0%	85.0%	77.5%	70.0%	60.0%	49.0%	31.0%	31.0%	31.0%
U.S. Large Cap Equity Funds	41.0%	41.0%	41.0%	41.0%	37.0%	33.5%	29.0%	24.0%	16.0%	16.0%	16.0%
U.S. Small/Mid Cap Equity Funds	9.5%	9.5%	9.5%	9.5%	9.0%	8.0%	7.0%	5.5%	3.5%	3.5%	3.5%
REIT Funds	6.0%	6.0%	6.0%	6.0%	5.5%	5.0%	4.5%	4.0%	2.5%	2.5%	2.5%
International Equity Funds	18.5%	18.5%	18.5%	18.5%	17.0%	15.0%	12.5%	10.5%	7.0%	7.0%	7.0%
Emerging Markets Equity Funds	10.0%	10.0%	10.0%	10.0%	9.0%	8.5%	7.0%	5.0%	2.0%	2.0%	2.0%
Commodities & Global Natural Resources	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	1.5%	3.5%	3.5%	3.5%
Commodities Funds	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.5%	1.5%	1.5%	1.5%
Global Natural Resources Funds	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	1.0%	2.0%	2.0%	2.0%
Fixed Income	15.0%	15.0%	15.0%	15.0%	22.5%	30.0%	40.0%	49.5%	55.5%	55.5%	55.5%
U.S. Fixed Income Funds	9.0%	9.0%	9.0%	9.0%	15.5%	22.0%	31.0%	35.5%	33.5%	33.5%	33.5%
Inflation Managed Funds	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	4.0%	10.0%	10.0%	10.0%
High Yield Funds	4.0%	4.0%	4.0%	4.0%	4.5%	5.0%	5.5%	6.0%	7.5%	7.5%	7.5%
Emerging Markets Debt Funds	2.0%	2.0%	2.0%	2.0%	2.5%	3.0%	3.5%	4.0%	4.5%	4.5%	4.5%
Money Market Funds/Cash and Cash Equivalents	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	10.0%	10.0%	10.0%
Money Market Funds/Cash and Cash Equivalents	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	10.0%	10.0%	10.0%

Source: Securities and Exchange Commission

In addition to disclosing the target asset allocations, target-date fund marketing materials should clearly note whether the fund’s investment manager(s) will tactically adjust the allocations. For target-date fund series that do incorporate a tactical strategy, we believe it's important that the marketing materials describe the constraints on their allocations. Below is an example of such disclosure:

> These strategic target allocations represent [the fund advisor's] view of how the Fund's investments should be allocated over the long term. The Fund's actual allocations may differ due to tactical allocations. The Adviser will use tactical allocations to take advantage of short to intermediate term opportunities through a combination of positions in underlying funds and direct investments, including derivatives. As a result of these tactical allocations, the Fund may deviate from its strategic target allocations at any given time by up to +/- 15% for fixed income, +/- 10% for equity, +/- 20% for money market/cash and cash equivalents and +/- 5% for commodities and global natural resources. These ranges apply to both the asset classes and types of underlying funds. Updated information concerning the Fund's actual allocations to underlying funds and investments is available in the Fund's shareholder reports and on the Fund's website from time to time.

No Guarantees

Morningstar supports the proposal to require a statement that target-date funds are not guaranteed investments. The Commission's study found that many investors wrongly believe target-date funds provide guaranteed income in retirement. To better set investors' expectations, marketing materials should clearly disclose that target-date funds are not guaranteed investments.

Morningstar also supports the Commission's proposal to require a statement that a target-date fund’s asset allocations may be subject to change. Many fund companies have made adjustments to the asset allocations of their target-date funds over the years. In 2011, Ibbotson Associates introduced a new measure of glide path changes called the Glide Path Stability Score, or GPSS. The calculations for GPSS can be found in the paper "Bait and Switch: Glide Path Instability" (Idzorek, Stempien, and Voris, 2011), available at http://corporate.morningstar.com/ib/documents/MethodologyDocuments/IBBAssociates/Bait_and_Switch_Glide_Path_Stability_Final_091211.pdf and forthcoming in the *Journal of Investing*. The scores suggest some target-date funds have exhibited significant glide-path changes, while others have been extremely stable. Glide-path changes are not inherently bad, but frequent changes can be cause for concern and can lead to poor investor experiences.

Align Shareholder Expectations with Series' Intentions

Morningstar recognizes that the target-date industry is diverse and that investment innovation, risk, and investment analysis and theory can change. Thus, there is no consensus as to whether a series' glide path should freeze at retirement--presumably because investors will withdraw their savings soon after--or continue to shift through the retirement years. To better inform investors as to whether a target-date fund is designed to be held to retirement or through retirement, we believe the proposal should require target-date funds to clearly disclose their assumptions in that regard. For example, if a target-date fund is managed in a way that assumes that investors will redeem their shares at the target date, then investors need to be aware so that they can take that into consideration when they are assessing what investment(s) may serve them well during their retirement.

Target-date funds are an important part of investors' retirement savings. While the design of these investments is complex, they still provide a relatively straightforward way for investors to broadly diversify their savings and better meet their retirement-savings goals. Again, Morningstar commends the Commissions' efforts to improve investors' understanding of target-date funds. Well-informed investors are more likely to avoid costly mistakes. We appreciate the opportunity to comment on this important topic and are happy to further discuss our views at the Commission's convenience.

Sincerely,

Morningstar, Inc.

David Falkof, Mutual Fund Analyst, Fund Research Group
Josh Charlson, Ph.D., Senior Mutual Fund Analyst, Fund Research Group
Laura Pavlenko Lutton, Editorial Director, Fund Research Group
Jeremy Stempien, Director of Investments, Retirement Solutions, Investment Management Division
Thomas Idzorek, Global Chief Investment Officer, Investment Management Division
Mary Beth Glotzbach, Senior Vice President, Institutional Software, Retirement Solutions
Avery Armour, Senior Data Analyst, Data Division
Chris Kielion, Data Analyst, Data Division

cc: Honorable Mary L. Schapiro, Chairman
Honorable Luis A. Aguilar, Commissioner
Honorable Daniel M. Gallagher, Commissioner
Honorable Troy A. Paredes, Commissioner
Honorable Elisse B. Walter, Commissioner