



DIVISION OF  
MARKET REGULATION

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

February 24, 2003

Mari-Anne Pisarri  
Pickard and Djinis LLP  
1990 M Street, N.W.  
Washington, D.C. 20036

Re: Dominion Bond Rating Service Limited

Dear Ms. Pisarri:

This responds to your request, on behalf of Dominion Bond Rating Service Limited ("DBRS"), that the Division of Market Regulation ("Division") provide you with written assurance that it will not recommend enforcement action to the Securities and Exchange Commission ("Commission") against broker-dealers that consider credit ratings issued by DBRS to be credit ratings from a nationally recognized statistical rating organization ("NRSRO") for purposes of the net capital rule, Rule 15c3-1 under the Securities Exchange Act of 1934 ("Exchange Act") (17 CFR 240.15c3-1).<sup>1</sup>

In correspondence and conversations with Division staff over the past two years, you have represented certain facts relating to DBRS's business to be as follows:

I. ORGANIZATIONAL STRUCTURE

Since its inception in 1976, DBRS has been a privately owned Canadian-based credit rating agency incorporated under the Ontario Business Corporations Act. DBRS issues assessments on the creditworthiness of obligors with respect to specific securities and also provides a subscription service for persons interested in following DBRS

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<sup>1</sup> To be recognized as an NRSRO, a rating agency must first request written assurance from the Division that it will not recommend enforcement action against broker-dealers that consider ratings by the rating agency to be ratings from an NRSRO. Before the Division will issue the requested no-action letter, it must first determine that the rating agency satisfies certain established criteria. The single most important criterion is that the rating agency is widely accepted in the U.S. as an issuer of credible and reliable ratings by the predominant users of securities ratings. The staff also reviews the operational capability and reliability of the rating agency, including: (1) the organizational structure of the rating agency; (2) the rating agency's financial resources (to determine, among other things, whether it is able to operate independently of economic pressures or control from the companies it rates); (3) the size and experience and training of the rating agency's staff (to determine if the entity is capable of thoroughly and competently evaluating an issuer's credit); (4) the rating agency's independence from the companies it rates; (5) the rating agency's rating procedures (to determine whether it has systematic procedures designed to produce credible and accurate ratings); and (6) whether the rating agency has internal procedures to prevent the misuse of non-public information and whether those procedures are followed.

research. DBRS operates primarily from its Toronto office, though it also maintains an office in New York, New York. DBRS does not directly or indirectly control any financial institution, nor is it so controlled by such an institution. DBRS is registered with the Commission as an investment adviser under the Investment Advisers Act of 1940.

DBRS currently employs a total staff of 61 persons, 41 of whom are analysts. Generally all DBRS analysts have degrees in business administration or accounting, and many have professional degrees and/or professional designations (*e.g.*, MBAs, JDs, CFAs). DBRS staff work within one of the following four operating groups: Finance and Administration, Systems Development, Business Development, and Research and Analysis. Analysts in DBRS's Research and Analysis group generally work within one of the following eight industry groups: Financial Services, Consumer Products and Automotive, Media and Communications, Government Finance, Natural Resources and Manufacturing, Real Estate, Energy and Utilities, and Securitization and Structured Finance. Each industry group is comprised of approximately three to four analysts, including a manager who is typically a senior vice president or executive vice president.

## II. RATING PROCESS

DBRS has credit ratings and rating reports currently outstanding on debt and preferred stock issued by over 400 different companies and on securities issued by over 120 special purpose entities. DBRS has been hired by these issuers, which include more than 60 large U.S.-based corporations, to rate their financial obligations on an ongoing basis. In addition, DBRS has issued "benchmark reports" on an additional 250 companies. Benchmark reports generally contain all of the information included in a DBRS rating report, but do not contain credit ratings. DBRS credit ratings are not recommendations to buy, sell, or hold a particular security, but rather are forward-looking assessments of an entity's ability to make timely payments of interest and principal. DBRS does not perform an audit in connection with any credit rating and on occasion relies on unaudited financial information. In all cases, DBRS uses information from sources that it considers reliable.

With regard to ratings categories and definitions applied to long-term debt, DBRS uses the same categories and definitions as are used by the Standard & Poor's division of the McGraw-Hill Companies, Inc., and Fitch, Inc. (*i.e.*, AAA, AA, A, BBB, BB, B, CCC, CC, C, D). However, standing within a particular rating category is generally reflected by DBRS with the terms "high," "middle," and "low" rather than with the characters "+" and "-" (*e.g.*, BB (high), BB (middle), and BB (low)). With the exception of ratings on structured products, DBRS appends each rating with a "Positive," "Stable," or "Negative" classification to provide users of its ratings with a better understanding of DBRS's opinion regarding the outlook for a particular security.

DBRS generally begins the rating process by gathering information from an issuer and/or from other sources that provide DBRS with a better understanding of the issuer and the industry in which it operates. DBRS normally requires that the issuer provide its last five annual reports, year-to-date interim results, any recent prospectuses or offering memoranda, and other information that the issuer has made available to the financial community. DBRS also requests confidential information from issuers, which generally includes information relating to future earnings and balance sheet projections, outstanding bank lines, and future strategic planning.

DBRS generally uses an issuer's financial statements to perform an initial credit analysis and generate a preliminary rating opinion. Once DBRS and the issuing entity are prepared for a more detailed discussion, the relevant DBRS analysts will generally visit the issuer's headquarters to meet with senior management and to learn more about the issuer and the planned financing. The analysts who visited the issuer prepare a report, generally four to six pages long, which is prepared in a standard DBRS format. This report forms the basis for the analysts' presentation to the DBRS rating committee.

All DBRS rating decisions must be approved by a DBRS rating committee. DBRS rating committees consist of some or all of the following persons: DBRS's three executive vice presidents, three senior vice presidents, and the analysts involved in assessing a particular credit (who have no voting authority with regard to the committee's decision). Rating committee meetings are normally chaired by DBRS's president or a DBRS executive vice president. Among other considerations, an issuer's strengths, weaknesses, profitability, balance sheet, liquidity, and industry conditions are discussed in rating committee meetings. A comparison of the issuer is made with other companies in the issuer's industry, including a comparison of credit ratings. Thereafter, a final rating for the issuer is agreed upon. DBRS rating committees attempt to reach a consensus, and if there is a major disagreement in the first meeting, the response is normally to procure more information and/or add more DBRS senior staff to the next discussion. DBRS documents the discussions of its rating committees.

After a rating and report have been approved by DBRS's rating committee, a copy is provided to the issuer to ensure that the information contained in the draft report is both factually correct and devoid of confidential information provided to DBRS to assist in the determination of the rating. In the event an issuer takes exception to an indicated rating, DBRS is prepared to listen to an appeal. After receiving comments from the issuer and making any appropriate changes to the draft report, the report is finalized and prepared for public distribution. Unless the issuer has requested that its rating and rating report be kept private, the rating becomes publicly available after DBRS issues a press release containing the rating and basic rationale underlying the rating. DBRS's full rating report is then made available to subscribers on DBRS's website.

Generally, at least two analysts are familiar with, and responsible for, all current and recent events for an entity that DBRS rates. Under normal circumstances, a rating is fully reviewed and a meeting arranged with an issuer's senior management on at least an annual basis. However, a rating may be changed based upon an event that materially affects an entity. DBRS expects the cooperation of the issuer in keeping DBRS up-to-date with any significant developments affecting the issuer, providing DBRS with continuing financial information as released, and being ready to respond to questions that DBRS has as they arise. Under normal circumstances, DBRS would expect to have at least one two to four hour meeting with the issuer's senior management each year to obtain a formal update on the Company's performance. It is DBRS policy that, in most cases, DBRS will continue to provide a rating for an issuer as long as the issuer has debt outstanding.

If there is a high uncertainty regarding the outcome of a significant event which directly impacts the credit quality of an issuer or group of issuers, and DBRS is unable to provide an objective forward looking opinion, then DBRS will place the rating of the issuer "Under Review." Ratings that are "Under Review" by DBRS are qualified with one of the following three provisional statements: "negative implications," "positive implications," or "developing implications."

DBRS represented that it generally does not offer a separate ratings advisory service from which it generates revenue. If an issuer wants to know how a potential event would impact its rating, and substantial work is required by DBRS, DBRS will typically charge a one-time fee.

DBRS also represented that it generally does not issue unsolicited ratings. However, if DBRS is unable to obtain the full cooperation of an issuer, and sufficient information is publicly available, DBRS may issue either a benchmark report or a report with a rating. If DBRS issues a report with a rating, it appends the rating with a "p" to reflect that the rating process did not include discussions with the issuer's management and was based only on public information. DBRS represented that it uses unsolicited ratings only as a last resort and that, to date, it has issued unsolicited ratings in only a handful of instances.

### III. INTERNAL PROCEDURES TO PREVENT MISUSE OF INFORMATION

DBRS prohibits its analysts, employees, and consultants from investing in or advising on securities of any company or subsidiary that DBRS rates or benchmarks. DBRS also instructs its staff not to inform an issuer of any definite rating action until DBRS's rating committee has reached a decision on the issuer's rating. Up to that time, DBRS can inform an issuer of concerns, but always with the caveat that the rating has not yet been finalized until the analyst has completed his or her analysis and the

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recommendation has been settled by the rating committee. Further, DBRS prohibits its staff from discussing nonpublic information with non-DBRS staff other than relevant persons from the specific issuer under review.

DBRS represented that its staff and consultants must annually review and sign an "Annual Statement of Understanding of DBRS Policy Concerning Code of Conduct, Ethics, and Employee (or Consultant) Investment Related Activities." In addition to stating that DBRS employees and consultants are prohibited from investing in or advising on securities of any company or subsidiary that DBRS rates, benchmarks, or is on DBRS's restricted list, the statement also contains sections on confidentiality, nonpublic information, and monitoring (*e.g.*, that DBRS will randomly request and review copies of an employee's brokerage account statements at least once a year).

#### IV. CONCLUSION

Based on the foregoing, and facts and representations made to the Division in connection with DBRS's request, the Division will not recommend enforcement action to the Commission if DBRS is considered by broker-dealers to be a "nationally recognized statistical rating organization" for purposes of applying the relevant provisions of Exchange Act Rule 15c3-1. Note, however, that this position is conditioned on DBRS not representing in any of its ratings, marketing, or similar literature that the Commission considers DBRS to be recognized as an NRSRO.

You should understand that the position expressed herein is a staff position with respect to enforcement only and does not purport to express any legal conclusion on this matter. The Division's position is confined to the facts as you have represented them; any material change therein may warrant a different result and should be brought to the Division's attention.

Sincerely,



Annette L. Nazareth  
Director