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U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
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Washington, D.C. 20549
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Attention: Jonathan G. Katz, Secretary

Re: File No. S7-33-97
Release No. 34-39457
Capital Requirements for Brokers or Dealers Under the 1934 Act
Proposal to Define the Term "NRSRO"

Ladies and Gentlemen:

This letter is submitted by MOODY'S INVESTORS SERVICE, INC. (***"MOODY'S"***) in response to the request of the Securities and Exchange Commission (***"SEC"*** or ***"Commission"***) for comments on its proposal set forth in Release No. 34-39457 (***"NRSRO Release"***) to amend Rule 15c3-1 under the Securities Exchange Act of 1934 (***"1934 Act"***) to define the term "nationally recognized statistical rating organization" (***"NRSRO"***).

BACKGROUND

As noted in MOODY'S letter, dated 5 December 1994 (***"Concept Letter"***), responding to the Commission's Concept Release (No. 33-7085, File No. S7-23-94), dated 31 August 1994 (***"Concept Release"***), soliciting public comment on the SEC's role, if any, in regulating NRSROs, MOODY'S objected then, and continues to object now, to the continuing extension and codification of the use in regulation of credit ratings in general and the NRSRO concept in particular, because any such extension and codification will inevitably:

- Erode the independence, objectivity, and integrity of rating agencies, thereby undermining their credibility and thus their utility in the capital formation process.

- Encourage issuers and intermediaries to shop among the few designated NRSROs for the most favorable or cheapest rating that will enable such issuers to clear some regulatory hurdle, irrespective of that rating's quality or credibility in the marketplace.

- Erode the First Amendment rights of *all* publishers of credit opinion, because the NRSRO concept by definition confers a privileged position on a limited number of such publishers at the expense of others.

MOODY'S has repeatedly emphasized that there exist practical and credible alternatives to the use of ratings in regulation. In a letter, dated 6 October 1995 (***"Wallman Letter"***), to then Commissioner Stephen M. H. Wallman, MOODY'S (i) enumerated the uses of ratings and of the NRSRO concept in the regulations of the SEC, (ii) noted that only one of many such uses was in fact consistent with the purposes for which credit ratings were originally intended, and (iii) proposed practical alternatives to all such uses. The comments set forth below presuppose the reader's familiarity with both the Concept Letter and the Wallman Letter. (*For ease of reference, copies of each are being filed with this letter.)*

SUMMARY

If, notwithstanding the recommendations set forth in the Concept Letter and the Wallman Letter and the comments set forth below, the Commission decides that it is desirable, as a matter of public policy, to define and formalize the concept of NRSRO and to continue the use of the ratings of NRSROs in its regulations, MOODY'S believes that:

- The proper and exclusive test for determining whether a rating agency deserves designation as an NRSRO, and therefore whether its ratings can be used for regulatory purposes, should be whether it is "nationally recognized" by active participants in the capital markets as a publisher of credible and reliable rating opinions on a broad set of securities. Such a test is the only criterion relevant to investors who use ratings and should, therefore, be the SEC's primary, if not exclusive, concern in this area. The fundamental determinants of "national recognition" of a rating agency are (i) an *impact* of its ratings on bond prices, (ii) a tight *correlation* over time between its ratings and actual default experience, and (iii) substantial *congruence* between its rating scale and those of rating agencies that already enjoy such recognition. Such determinants are essential to provide the SEC, as regulator, a high degree of assurance that the "currency", *i.e.*, the ratings, employed in its regulatory regime is reasonably uniform and not susceptible to easy debasement.

- NRSROs that confine their activities solely to the expression and publication of rating opinions and analyses should not be treated, or required to register, as investment advisors under the Investment Advisers Act of 1940 (***"IAA"***). Unlike investment advisors, NRSROs do not make buy, sell, or hold recommendations or invest the money of others. The regulatory system established for the latter under the IAA has no value in measuring the credibility or reliability of an NRSRO's ratings or any other characteristic reasonably related to a rating agency's fitness to be granted status as an NRSRO. Moreover, the proposed requirement that rating agencies be so registered would be inconsistent with the reasoning in the U.S. Supreme Court's decision in *SEC v. Lowe,* 472 U.S. 181 (1985), and mark the first time that the SEC had attempted to exercise broad regulatory oversight of rating agencies without an appropriate Congressional mandate.

- The SEC is the preeminent securities regulatory authority in the world. Its regulations often serve as a model for regulatory regimes around the world. It is clearly in the best interests of the United States and the global economy to encourage the development of vibrant and healthy capital markets on a world-wide basis. The history of the past century has demonstrated that sound rating agencies promote the healthy functioning of capital markets, but also that the health of the rating sector is, in turn, dependent upon an equilibrium that is fragile and easily upset by even well-intentioned public sector involvement.

- In order to preserve over time the efficacy and integrity of a standard for qualification based on national recognition and to mitigate the unintended consequences of its regulatory actions, the Commission should focus on and promote the following:

1. The transparency of information and the adequacy of the disclosure regime in the market in which rating agencies function, in order that the instruments and issuers rated by them, as well as their rating opinions, be susceptible of broad market critique and commentary.

2. The demonstrated commitment of a rating agency to express, for the benefit of investors, rating opinions that are independent and objective, irrespective of whether those opinions may at times be controversial or unwelcome to governments, issuers, regulators, or intermediaries operating in such agency's markets.

3. The public availability on an ongoing basis of those ratings that are eligible for use for regulatory purposes, in order to ensure that market participants are able to assess and compare the performance over time of ratings and rating agencies.

- The SEC should remain vigilant in assessing, on an ongoing basis, the unintended consequences of its regulatory actions. Rating shopping is a direct consequence of the use of ratings in regulation and should be an area of acute concern to the SEC, because it directly threatens the intrinsic value and integrity of the currency upon which the SEC's regulatory regime in this area is predicated.

COMMENTS

A. If Not Eliminated Altogether, NRSRO Qualification Should Be Determined Solely by "National Recognition"

Rating agencies are publishers of financial information and opinions. They express opinions about the relative credit quality of individual securities and the issuers thereof.

The SEC has traditionally demonstrated concern for greater transparency, including fuller disclosure and discussion of risks, and the broadest possible dissemination of all material information, a concern that MOODY'S fully shares. Unfortunately, the introduction and use of the NRSRO concept has — albeit unintentionally — produced in the rating sector precisely the opposite result: fewer domestic rating agencies, *de facto* restrictions on the ability of most non-U.S. rating agencies to achieve such status, and consequently less robust discourse, in the form of competing rating opinions, about credit in both the domestic and the global capital markets.

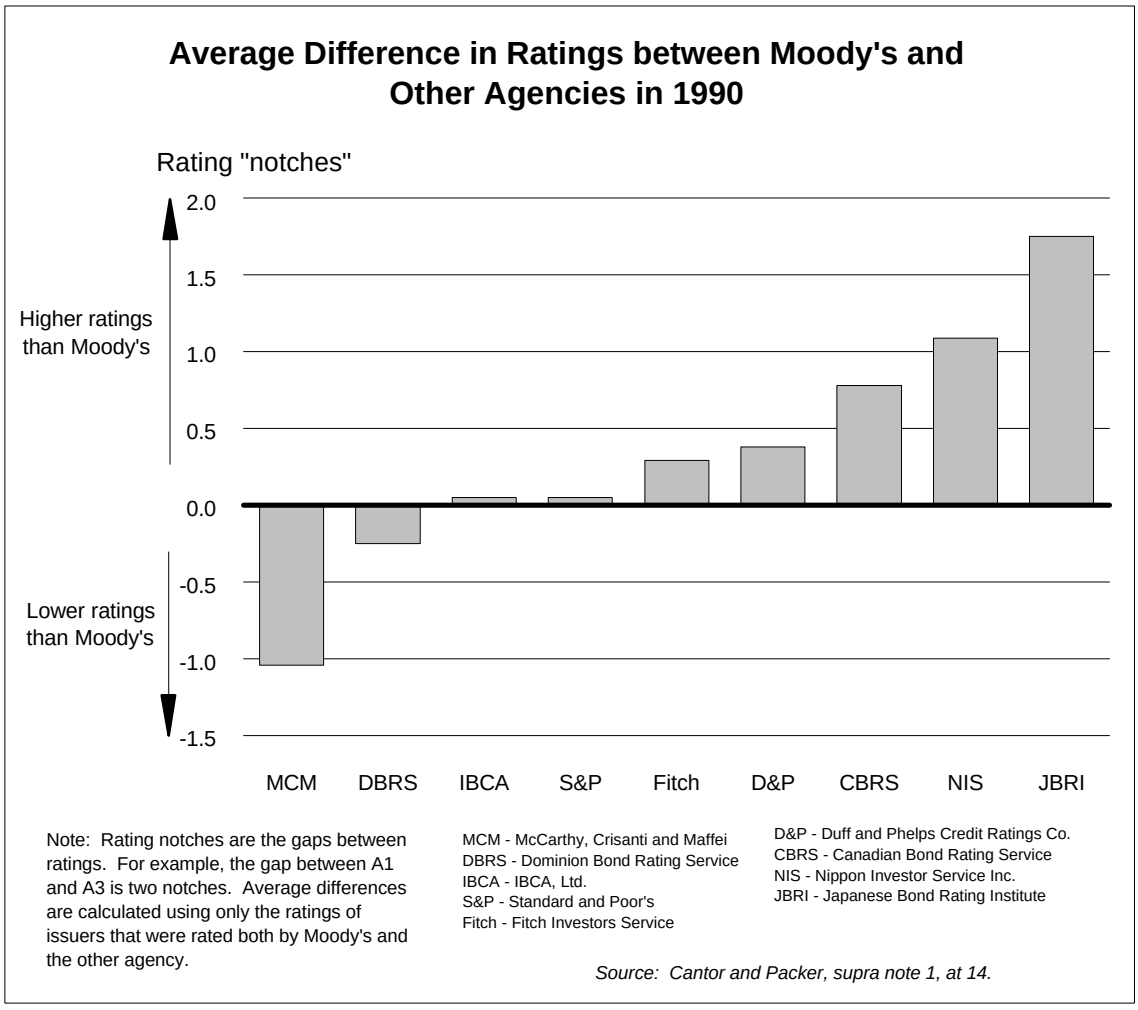
The SEC's granting of NRSRO status reflects, we suspect, a legitimate public policy interest in protecting investors, and the resulting regulatory regime has been erected with the intent to secure that interest, by policing the "quality" of rating opinions in the marketplace through careful screening of the providers of those opinions. The proposals contained in the NRSRO Release essentially seek, through definition, to make the new procedures more transparent than the existing ones while leaving this underlying principle untouched. The aims of both the current and the proposed procedures are laudable, but the methods employed to date have not produced the results desired, and there is no basis for believing that the proposed procedures will be any more successful in this regard.

The reason for this contradiction between purpose and result is not hard to find. Both the current approval process, as described in Section I. D. of the NRSRO Release, and the proposed process, as described in Section IV. B. of that Release, focus on rating *agencies* rather than rating *quality* as the basis for NRSRO status. Rating agencies are subject to competitive pressures, all the more so when demand for ratings is artificially stimulated by regulation. If there is not an equally strong motivation on the part of an NRSRO to achieve and maintain the quality of its ratings, then the SEC's fundamental interest in this area — investor protection — is undermined. Nothing in the current or proposed process indicates that the SEC has attempted, or will attempt, systematically to examine whether there exists, in the case of each applicant for NRSRO status, any of the fundamental determinants of "national recognition" of an agency that are in fact relied upon by the capital markets, *viz.*, (i) an *impact* of its ratings on bond prices that is independent of the impact thereon of regulation, (ii) a tight *correlation* over time between its ratings and actual default experience, and (iii) substantial *congruence* — or at least the absence of ***illusory*** congruence — between its rating scale and those of rating agencies that have already achieved such recognition. Correlation and congruence should, moreover, be capable of statistical demonstration. Such demonstration would require that those ratings of an agency that are eligible for use for

regulatory purposes — which might well be a subset of all ratings assigned by such agency — be *publicly available* and *sufficiently numerous* to permit market participants to conduct appropriate statistical testing.

At its core, the NRSRO concept, and its utility as a regulatory tool, depend upon the validity of its implicit assumptions that (i) the ratings of all NRSROs' correlate essentially equivalently with actual default experience over time and (ii) the rating scales of all NRSROs' are essentially congruent. The assumption of correlation is easily susceptible of testing for any applicant, and such a test over an appropriate time horizon should be a prerequisite for consideration for NRSRO status. The assumption of congruence of rating scales has, with the exception of those of MOODY'S and its competitor Standard & Poor's, been found by academics and other researchers to be incorrect, at least historically.[1] As the following chart demonstrates, there exist significant departures from congruence:

[1] *See* Cantor & Packer, Richard Cantor and Frank Packer, *The Credit Rating Industry*, 19 FRBNY Q. REV. 1 (Summer-Fall 1994), at 14 ("[t]his rough equivalence in the rating standards of Moody's and Standard and Poor's does not seem to extend to other rating agencies"). Since 1997, three years after this study was published, Mr. Cantor has been employed by Moody's Investors Service. Vivien Beattie and Susan Searle, *Bond Ratings and Inter-Rater Agreement*, J. OF INT'L. SECS. MARKETS 167 (Summer 1992) , at 170 (finding that differences between pairs of rating agencies to be generally statistically significant and in some cases highly significant; Moody's and S&P ratings were found to be most closely correlated).



Despite this evidence, the SEC's existing and proposed regulations treat as equivalent ratings from different NRSROs that are not in fact equivalent. This illusion of equivalence among the various agencies, their ratings, and their rating standards creates the opportunity for rating shopping. In addition, because of the manner in which the SEC uses NRSRO ratings in its regulations, investors may be led — fallaciously — to conclude that all NRSRO ratings of a certain level express opinions denoting equivalent levels of risk. The SEC should not assume, without more, that it may use the ratings of different NRSROs interchangeably, and should not, by regulation, encourage investors to do so.

As MOODY'S suggested in the Concept Letter, no process, whether transparent or opaque, for evaluating providers of credit opinion that fails to focus primarily on the fundamental determinants of "national recognition" can ultimately succeed. No system premised on the notion of na-

tional recognition can function effectively over time without clearly identifying the defining characteristics of that recognition and making those criteria paramount in any approval process.

If investor protection is in fact the Commission's primary motivation for proposing the new definition and procedures set forth in the NRSRO Release, then it should pause to consider that rating agencies provide a formidable private sector mechanism for enhancing investor protection, at least against credit risk, that functions best when disciplined only by market forces, *e.g.*, market recognition for credibility and reliability. Public sector "involvement" in, oversight of, and ultimately influence over, the rating process has distorted the otherwise healthy functioning of this private sector mechanism in the past and will continue to do so under the proposals now under consideration, unless NRSRO status is conferred on only those agencies that meet the definition of "national recognition" referred to above, rigorously applied.

Assuming it adopts "national recognition" as the appropriate standard for qualification of a rating agency as an NRSRO, the Commission should, in order to preserve the efficacy and integrity of that standard over time and to mitigate the unintended consequences of its actions, *viz.*, rating shopping, erosion of rating agency independence, and narrowing of competition of ideas and opinions in the marketplace, focus on and promote the following:

1. The transparency of information and the adequacy of the disclosure regime in the market in which such rating agency functions concerning specific issues, issuers, and markets, in order that the instruments and issuers rated by it, as well as its rating opinions, be susceptible of broad market critique and commentary.

2. The demonstrated commitment of a rating agency to express, for the benefit of investors, rating opinions that are independent and objective, irrespective of whether those opinions may at times be controversial or unwelcome to governments, issuers, regulators, or intermediaries operating in such agency's markets — a practice that MOODY'S has maintained since 1909.

3. The public availability on an ongoing basis of those NRSRO ratings that are eligible for use for regulatory purposes, in order to ensure that market participants are able to assess and compare the performance over time of ratings and rating agencies.

MOODY'S is concerned that the rating shopping and other abuses of the rating system that are fostered by NRSRO status of the type apparently now envisioned by the SEC (contrary to Moody's recommendation) will encourage attempts to impose consistency among NRSROs' rating opinions by "harmonizing" their rating scales, standards, or methodologies — an attempt that, while doomed to ultimate failure, would nevertheless in the process sacrifice not only the innovation in rating analysis that is essential to dynamic capital markets, but also the independence of rating agencies that is essential to their credibility.

B. Rating Agencies Are Not Investment Advisers

As stated above, rating agencies are publishers of financial information and opinions. Unlike many other financial publishers, however, rating agencies do not usually consider or opine upon the relative price or yield of the securities in respect of which they are making credit assessments — leaving it to investors, intermediaries, investment advisers, or others to comment upon and determine whether the yield on any security adequately compensates the individual investor for the level of credit risk inherent in that security. Absent some determination by an investor of his tolerance for credit and other risk, *e.g.*, currency risk, interest rate risk, etc., a credit rating by itself is insufficient to permit one to make an informed investment decision — and therefore cannot constitute "investment advice".

The foregoing constitutes a fundamental distinction between the opinions of rating agencies and the recommendations of investment advisers. Although its rating opinions may be of great interest to investors, MOODY'S does not provide advice or recommendations as to whether to buy, sell, or hold any securities, nor does it provide an analysis of whether any security is over- or under-valued. It does not hold investors' funds, manage portfolios, or perform other investment advisory functions, and believes that to do so would raise serious issues of conflict of interest.

Although MOODY'S has continued voluntarily to register with the SEC under the IAA for many years, even after selling its investment advisory business more than 25 years ago, it does not now carry on an investment advisory business and objects to any attempt to make such registration mandatory for rating agencies for four reasons.

First, because the activities of rating agencies and those of investment advisers are so different, the regulatory system established for the latter under the IAA has no value in measuring the credibility or reliability of an NRSRO's ratings or any other characteristic reasonably related to a rating agency's fitness to be granted status as an NRSRO. Moreover, although it explicitly disclaims in all its publications any intent to provide investment advice, MOODY'S is very concerned that any requirement that rating agencies, acting only as publishers of impersonal opinions, register as investment advisers would tend, without justification, to equate the activities of such agencies with those of entities that are in fact performing investment advisory functions. This, in turn, may further encourage some investors mistakenly to believe that credit ratings can be relied upon as a proxy for an assessment of overall investment quality, which they cannot.

Second, mandatory investment adviser registration would, by requiring rating agencies to register as something they are not in order to obtain or maintain NRSRO status, permit the SEC to assert broad regulatory oversight and influence over them for the first time. The U.S. Supreme Court in *SEC v. Lowe* rejected the Commission's effort to expand its regulatory authority to pub-

lishers of impersonal investment advice.[2] Under the Court's reasoning in *Lowe*, publishers of impersonal credit opinions that do not rise to the level of "investment advice" should even more clearly not be subjected to such an extension of SEC authority. The SEC should not undertake regulation of rating agencies without an express grant of authority.

Third, if the Commission succeeds in requiring rating agencies to register under the IAA, it will soon find itself forced to mediate between issuers and rating agencies disputes that are inherently political rather than financial. In so doing, it will expose itself to the risk of serious damage to its reputation, with no commensurate public benefit. Rating agencies' opinions are inherently controversial, often taking unpopular positions on matters of public concern that frequently attract the ire of politicians and regulators. Ratings often reflect concerns in the capital markets regarding the safety and soundness of banking systems or particular industries, the competence of state and local governments, and even the strength of sovereign nations. If rated entities are politically well-connected, pressure can be brought to bear on regulators to use their regulatory oversight to "encourage" rating agencies to reach "appropriate" rating conclusions or otherwise modify their activities to reach results that are politically palatable. Such influence — or even the appearance of such influence — would quickly destroy the utility of ratings as a mechanism for improving the efficiency of the capital markets.

Fourth, the SEC's regulations are often emulated by other U.S. and non-U.S. regulators when developing their own regulatory regimes. There is unfortunately no guarantee, however, that similar regulations adopted elsewhere will be implemented with the same sensitivity, even-handedness, and appreciation for the benefits of freedom of speech that have to date characterized the Commission's approach to this area. Given the role its regulations thus play, the SEC should set a clear and unmistakable example for other regulators around the world by (i) avoiding any exercise of regulatory authority that could be interpreted as regulatory oversight of, or influence upon, the rating process, and (ii) making it explicit, through deed as well as word, that regulatory interference in the rating process exacts an unacceptably high price by undermining the independence and credibility of rating agencies, thereby destroying their ability to enhance the efficiency of the capital formation process.

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[2] In *SEC v. Lowe*, 472 U.S. 181 (1985), the Supreme Court held that the IAA did not permit the SEC to regulate publishers of impersonal investment advice. At present, Moody's is voluntarily registered as an investment adviser. Moody's does not, however, concede that its publication of ratings constitutes investment advice within the meaning of the Advisers Act or that it is required to register as an adviser. The definition of "investment adviser" in S. 3580, the original bill that became the Advisers Act, excluded publishers of newspapers of general and regular circulation. After hearing testimony that the definition would continue to include rating agencies, such as Moody's, the exclusion was extended to business and financial publications. *See id*. at 194-95; *see also* Richard Y. Roberts, *Formal Regulatory Handle Needed for NRSRO Designation*, Speech Before the SIA Compliance & Legal Seminar, at 14 (Apr. 6, 1992) (in speaker's opinion, the Advisers Act does not authorize the SEC to regulate rating agencies).

In short, MOODY'S is extremely concerned that, weighed against the considerable cost in attenuation of rating agency independence and credibility that will inevitably result from any attempt by the Commission or its staff to expand its jurisdiction under the IAA to exercise oversight of, and therefore influence upon, rating agency opinions or the process by which they are reached, no case has ever been articulated, much less established, for the benefits that such an extension of authority might produce.

C. Specific Changes to Proposed Rule

1. Rating Agencies Rate Obligations As Well As Obligors

Subparagraph (A) of Section (c)(13)(i) should be amended to read:

> "Issues ratings that are current assessments of the creditworthiness of obligations or obligors, whether generally or with respect to specific securities, money market instruments, bank deposits, insurance claims, or other obligations; and…"

Most ratings assigned by MOODY'S constitute expressions of opinion about individual securities, rather than about obligors, whether generally or with respect to specific obligations. A rating assigned to a particular security reflects the individual characteristics of that security, including priority of payment in the event of insolvency or other default, and other bond covenants. Some ratings, on the other hand, such as bank deposit ratings and insurance financial strength ratings, may constitute assessments of the overall financial strength of an obligor without regard to "specific securities or money market instruments" at all. The terminology used in subparagraph (A) should be broad enough to encompass all ratings assigned by NRSROs.

2. Registration as an Investment Advisor

Subparagraph (A) of Section (c)(13)(i) should, for the reasons stated above in Paragraph B of this letter, be amended to delete the requirement that NRSROs be registered under the IAA. Such registration bears no reasonable relation to a rating agency's qualifications to be an NRSRO and undermines rating agencies' credibility in the marketplace with no commensurate public benefit by granting, or appearing to grant, the SEC and its staff authority to exercise influence over the rating process.

3. Recognition as Issuer of Credible and Reliable Ratings Is Only Criterion

Paragraph (ii) of Section (c)(13) should be amended to delete paragraphs (B) through (D). As noted above, "[r]ecognition of the rating organization in the United States as an issuer of credible and reliable ratings by users of securities ratings" is the only relevant criterion for any inquiry by the SEC or any other body as to whether that rating agency should be granted NRSRO status. All of the other listed criteria are either secondary to that inquiry or irrelevant. The criteria listed in subparagraphs (B) through (D) should therefore be deleted.

4. Staffing and Financial Resources

The levels of staffing[3] and financial resources that are "adequate" to create and operate a rating agency that can assign and publish credible ratings are nominal in today's technological environment. These criteria should therefore be eliminated.

5. Use of Systematic Rating Procedures

MOODY'S believes that any agency that has in fact achieved national recognition will almost certainly have systematic rating procedures in place and that its ratings will have a demonstrable track record of default prediction. MOODY'S does not, however, believe that it is the province of the SEC to determine the appropriateness of particular rating procedures in designating an NRSRO because the market, in conferring national recognition on an agency, has already assessed those procedures in a manner far more efficient than any that the SEC could adopt through regulation. Finally, it is well known that existing NRSROs have very different rating approaches and analytic methodologies, and that these approaches and methodologies change continuously over time. Yet several NRSROs share some level of national recognition, irrespective of their particular rating methodologies. The SEC should not attempt to codify appropriate rating procedures or to suggest to an applicant for NRSRO status that one particular rating methodology is more appropriate than any other.

6. Contact With Management of Issuers

The credibility of ratings does not depend upon the "[e]xtent of contacts with the management of issuers, including access to senior level management of issuers". It is the *quality* of the information obtained and analyzed by a rating agency rather than its *source* that determines the credibility and reliability of the rating opinion expressed. This criterion should be eliminated.

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[3] MOODY'S believes that the location of staffing is similarly irrelevant.

A common misconception is that rating agencies, through some sort of privileged access to senior management of an issuer, can and do gain insights that are not available through any other means. While MOODY'S meets with management of most issuers of securities it rates, it does not view this practice as indispensable to the formation of an accurate rating opinion. This misconception rests on a troubling set of assumptions:

- That the SEC's disclosure rules are, where applicable, inadequate to allow investors and others to make a credible and reliable assessment of the risk of a security.

- That information provided by senior management to rating agencies is always accurate, credible, reliable, and complete, and never self-serving.

- That unless investors have the same access to senior management that MOODY'S does, they will always have to rely on ratings for reliable assessments of risk.

- That withdrawal by an issuer of access to senior management results in a second-class rating.

We strongly disagree with all of the foregoing assumptions and with the Commission's unsupported assertion in footnote 13 of the NRSRO Release that "rating organizations that have access to senior management are better able to make subjective opinions regarding the risks associated with [an] issue".

MOODY'S finds that meetings with senior management tend to *accelerate* the analytic process, because much of the information needed can be gathered quickly from one source and the answers to certain questions easily obtained, but not to change the substance of such process. If such a meeting is not available, the analyst usually has access to public filings, industry publications, and information from the issuer's competitors, suppliers, and customers through its normal course of business. The analyst may have followed the company for many years as part of an ongoing analysis of the industry. In the U.S., accounting and disclosure rules for public companies, and publicly available information about governmental issuers, are extremely useful in fulfilling the analytic needs of a rating agency analyst. In short, a meeting with senior management may facilitate an analyst's understanding of information otherwise available, but such a meeting is not an adequate substitute for information gathered from other sources.

The Commission would ill serve investors or other market participants by adopting a definition of NRSRO that encourages such participants to believe, contrary to fact, that rating agencies have access to material or privileged information as a result of their contacts with senior management that is greater than that available to a skilled and experienced rating agency analyst from other sources or that provided by offering documents whose form and content are dictated by the SEC's own regulations.

D. Other Comments

1. Sliding Scale Rating Fees

MOODY'S does not believe that rating fees should play any role in the definition or designation of NRSROs, since rating fees play no role in determining national recognition.

Rating fees should be left to the discretion of each NRSRO and to the effective discipline of natural competitive pressures in the marketplace. Each rating agency attempts to create value for issuers and investors by expressing rating opinions and charging a fee for such services commensurate with the value so created. The SEC should not attempt to substitute its judgment as to the value of such services for that of issuers or the investors who, by accepting lower yields from issuers, ultimately pay the agency's fees. Regulatory constraints upon NRSROs' business relationships with issuers and investors are not an appropriate method to encourage rating agencies to perform their socially useful role in improving the efficiency of the capital formation process. Disciplined by market forces alone, rating agencies that cease to render services at a price that market participants choose to pay will soon cease to be "nationally recognized".

Investors derive greater benefit from ratings of certain types of securities — perhaps because of the complexity of their structure or a rating agency's sophistication in the analysis of those instruments — and might therefore be expected to have a greater incentive to induce rating agencies to rate them. Moreover, as noted in the Concept Letter, forbidding a sliding scale of fees would result in the reallocation from larger issuers to smaller issuers of a portion of the costs of providing ratings. Such a result would obviously impede capital formation by small issuers without any commensurate public benefit.

If the Commission in fact believes that sliding scale rating fees are distorting the ratings of any NRSRO, it should first examine whether the impetus for such distortion is not demand for ratings that has been artificially stimulated by the regulatory use of those ratings. Having harnessed to a public purpose an otherwise well-functioning private sector mechanism with an established reputation under the existing fee structure, regulators should hesitate before citing problems arguably introduced by the regulatory use of ratings as a pretext to justify intrusion into business relationships among rating agencies, issuers, and investors. The Commission has to date made no case, in either the NRSRO Release or elsewhere, for assuming a "rate regulation" role in this area.

2. Ratings Available Only to Subscribers

MOODY'S believes that the SEC should proceed extremely cautiously before attempting to dictate, as part of the process for designation of NRSROs or otherwise, that rating agencies express and disseminate, on a current basis, their opinions to the general public without charge. Although, as stated above, those ratings of an NRSRO that are eligible for use for regulatory purposes need to be publicly available on an historical basis to permit statistical testing of correlation and congruence, free public access on a timely basis to all ratings of an NRSRO is not one of the determinants of national recognition. While MOODY'S existing practice is to disseminate all monitored ratings when issued, revised, suspended, or withdrawn through certain broad-based wire services and other media outlets to the public at large, it believes that any attempt to enshrine such practice in a regulatory mandate would be inappropriate. In making decisions about the opinions that it expresses and the manner in which it expresses them, MOODY'S and other rating agencies should be able to respond to market demands and other competitive pressures, without regard to the possible impact of their decisions upon their status as NRSROs.

Most importantly, however, this proposal again appears to be predicated upon some perceived need for ongoing oversight or control by the Commission of rating agencies' activities — a control that MOODY'S believes to be unjustified, inappropriate, and un-Constitutional, as well as far beyond any oversight exercised over other financial media. Such control would also, not inconsequentially, constitute substantive regulation of rating agencies' activities that is at variance with the Commission's announced intention merely to "define" the concept of NRSRO. If substantive regulation of rating agencies' activities is, in fact, that which is contemplated by the Commission or its staff, such a wholesale shift in policy should be straightforwardly proposed and subjected to open and vigorous public debate.

3. Revocation of NRSRO Status

MOODY'S believes that the only basis on which NRSRO status, once conferred, should be questioned or revoked is if an NRSRO has lost its national recognition. Any revocation proceeding or investigation that is based on any rating action taken by an NRSRO, on any change in staffing levels, rating methodologies or practices, or on any enumerated criterion other than such recognition, would be inappropriate and would, in addition, have a chilling effect on the rating industry. It would also raise serious Constitutional issues, precisely as it would if another government agency attempted to classify newspapers, and grant privileged access to distribution channels to certain thereof, on the basis of how many reporters they employed or how "correct" their editorial opinions were in the eyes of the overseeing agency.

CONCLUSION

MOODY'S believes that, absent some compelling and well-articulated need, which has been neither discussed nor demonstrated in the NRSRO Release, it is unwise public policy artificially to narrow the range of informed public discourse about the creditworthiness of issuers and securities in the capital markets by (i) creating a select class of entities, such as those designated NRSROs, and then (ii) conferring regulatory benefits upon the use of their ratings. Since neither the existing nor the proposed approval process addresses the conceptual inconsistency inherent in the NRSRO concept or the unintended consequences of the regulatory use of ratings, the proposal should be abandoned or substantially revised. Moody's has proposed, in both the Concept Letter and the Wallman Letter, a way to eliminate the NRSRO concept and the inconsistencies attendant upon its use in the Commission's regulations. If the Commission is unable or unwilling to accept that proposal, it should use for its regulatory purposes the ratings of only those agencies that display the fundamental characteristics of "national recognition" — correlation, congruence, and an impact on bond prices — so that it can have a high degree of assurance that the currency employed in its regulatory regime is reasonably uniform and not susceptible to easy debasement.

Should you have any questions or need additional information with respect to any of the comments set forth above, please contact the undersigned at (212) 553-7958 or Donald Selzer, Managing Director, at (212) 553-1068.

Very truly yours,

MOODY'S INVESTORS SERVICE, INC.

By Matthew C. Molé

Matthew C. Molé