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ASSOCIATION OF FINANCIAL GUARANTY INSURERS

Unconditional, Irrevocable Guaranty®

March 7, 2007

By E-Mail: rule-comments@sec.gov

Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090
Ref: File Number S7-04-07

Re: Applicability of Proposed Rule 17g-6 to Financial Guaranty Insurers

Dear Ms. Morris:

On behalf of the Association of Financial Guaranty Insurers ("AFGI"), I am writing to comment on Proposed Rule 17g-6 implementing the provisions of the Credit Rating Agency Reform Act of 2006 (the "Act"). Specifically, I respectfully submit on behalf of AFGI that the Securities and Exchange Commission (the "Commission") (1) extend the applicability of paragraph (a)(4) of Rule 17g-6 to financial guaranty insurers (including reinsurers), (2) explicitly include "shadow" ratings in paragraph (a)(4) of Rule 17g-6 and (3) modify the provisions intended to address the practice of notching so that they do not prevent a rating organization from assessing the creditworthiness of unrated assets and securities underlying a structured product transaction.

AFGI is the trade association representing monoline financial guaranty insurers and reinsurers of asset-backed securities and municipal bonds.[1] Financial guaranty insurance serves the interests of public investors in asset-backed and municipal bond transactions by irrevocably and unconditionally guaranteeing payments on asset-backed securities and municipal bonds in exchange for premiums. For more information about AFGI members, please visit AFGI's website, www.afgi.org.

The value of the financial guaranty insurance product is generally a function of the credit rating applied to the obligations insured. As such, financial guaranty insurers are highly

[1] Current AFGI member companies are ACA Financial Guaranty Corporation, Ambac Assurance Corporation, Assured Guaranty Corp., BluePoint Re Limited, CIFG Assurance North America, Inc., Financial Guaranty Insurance Company, Financial Security Assurance Inc., MBIA Insurance Corporation, Radian Asset Assurance Inc., RAM Reinsurance Company Ltd. and XL Capital Assurance Inc.

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dependent on the availability and integrity of credit ratings. Most financial guaranty insurers maintain a financial strength rating of "Triple-A" or "Double-A" (with one insurer being rated "Single-A" by design) from multiple nationally recognized statistical rating organizations. These rating agencies periodically review the financial guaranty insurer's business and financial condition, and apply their own capital adequacy models in assessing the financial strength of the financial guaranty insurer.

Rating agency capital adequacy models employed by certain NRSRO's typically require that every transaction insured by a financial guaranty insurer be rated, or have a "shadow" rating, by the rating agency that is assessing the insurer's financial strength. The shadow rating reflects the NRSRO's assessment of the creditworthiness of the transaction without giving effect to the insurance. If an insured transaction does not carry such a rating or shadow rating, but was rated by another NRSRO, the rating agency will generally "notch" down the rating assigned by the other NRSRO in assessing the financial guaranty insurer's capital adequacy. This practice is similar to the NRSRO's practices with respect to asset-backed and mortgage-backed pools addressed in paragraph (a)(4) of Proposed Rule 17g-6.

AFGI respectfully submits that the considerations expressed by the Commission in proposing Rule 17g-6 as it relates to asset-backed and mortgage-backed pools are applicable to the financial guaranty insurance industry. If a rating agency requires that each transaction in a financial guaranty insurer's book of business be rated (or shadow rated) by the rating agency in assessing the insurer's financial strength, or else be "notched" downwards, there is significant pressure on the financial guaranty insurer to obtain, from each rating agency that assesses its financial strength, a rating or shadow rating for every transaction it insures. AFGI believes that the balance struck by the Commission in paragraph (a)(4) of Proposed Rule 17g-6 would be appropriate to apply to an NRSRO's assessment of the capital adequacy of a financial guaranty insurer.[2]

In addition, in the event that an NRSRO has not rated a transaction insured by a financial guaranty insurer and therefore requires that a shadow rating be obtained for purposes of assessing the financial guaranty insurer's capital adequacy, AFGI assumes that the provisions of paragraph (a)(4) of Proposed Rule 17g-6 are intended to apply to the shadow rating as well. However, insofar as shadow ratings are of significant importance to financial guaranty insurers, AFGI respectfully requests that the Commission either confirm in the adopting release for the final rule that credit ratings include shadow ratings, or, preferably, explicitly reference shadow ratings in the final rule.

Finally, AFGI is concerned that Rule 17g-6, as proposed, would not permit an NRSRO to adequately evaluate the effect of unrated assets in rating a structured product. AFGI notes that

[2] In making this proposal, AFGI is not expressing an opinion on whether the threshold of 85% contained in the proposed rule is the optimal level. Accordingly, references herein to 85% or 15% are intended to refer to the appropriate percentages based on the Commission's ultimate determination.

Proposed Rule 17g-6 is intended to address, somewhat differently, the practice whereby an NRSRO refuses to rate a structured product for which it has not rated all the underlying assets, and whereby an NRSRO discounts the rating for a structured product because it has not rated all the underlying assets. The second sentence of paragraph (a)(4) of Proposed Rule 17g-6 provides that an NRSRO cannot refuse to initiate a rating or withdraw an existing rating so long as it has rated at least 85% of the underlying assets or securities. This sentence, therefore, creates a 15% "basket" for underlying assets that have not been rated by the NRSRO, whether because such assets are unrated or rated by another NRSRO. However, as noted in the proposing release, this provision does not apply to an NRSRO issuing or threatening to issue a lower credit rating or lowering or threatening to lower an existing credit rating. In other words, once an NRSRO is required to provide or maintain a rating under the second sentence of the proposed rule, the first sentence of the proposed rule then prohibits an NRSRO from taking into account the assets or securities that it has not rated to derive a lower rating.

AFGI respectfully suggests that paragraph (a)(4) of Proposed Rule 17g-6 be modified such that an NRSRO can lower or threaten to lower an existing credit rating of a structured product transaction where the underlying assets or securities have not been rated by any NRSRO. AFGI believes that it would be detrimental to the integrity of the credit ratings of structured products for NRSRO's not to be able to apply their own methodologies, which may include lower credit ratings, where there has been no assessment at all of the creditworthiness of assets or securities underlying a structured product. At the same time, AFGI believes that the Commission's goals would be fully supported by the modification that AFGI is proposing. First, it would not be coercive or abusive for an NRSRO rating a structured product to require some analysis of all underlying assets or securities, so long as it is not requiring that such NRSRO be employed to perform such analysis. Second, the modified rule would address the practice of notching because the NRSRO rating the structured product transaction could not lower the credit rating provided by another NRSRO. However, the modified rule would continue to protect the integrity of the ratings of an NRSRO by permitting it to refuse to rate or withdraw its rating of a structured product transaction where more than 15% of the assets have not been rated at all (or have been rated by another NRSRO).

The net effect of the modifications proposed by AFGI would be that, when an NRSRO rates the claims-paying ability or financial strength of a financial guaranty insurer, (1) the NRSRO could not refuse to issue the rating, or withdraw its rating, as a result of the insurer's outstanding obligations not having been shadow rated by that NRSRO, so long as that NRSRO has provided a shadow rating for at least 85% of the insurer's outstanding insured obligations, and (2) the NRSRO would be prohibited from notching the rating, if any, assigned by another NRSRO of the insured obligations, without giving effect to the insurance, for those transactions that the NRSRO has not shadow rated. AFGI believes that these modifications would support the Commission's goals in proposing Rule 17g-6, and, at the same time, create greater transparency of the credit rating process for both financial guaranty insurers and the large segment of investors who rely on their claims-paying and financial strength ratings.

For the reasons described above, we respectfully request that the Commission (1) include financial guaranty insurers in paragraph (a)(4) of Proposed Rule 17g-6, (2) explicitly include "shadow" ratings in paragraph (a)(4) of Rule 17g-6 and (3) modify the provisions intended to address the practice of notching so that they do not prevent a rating organization from assessing the creditworthiness of unrated assets and securities underlying a structured product transaction. For your convenience, these modifications to paragraph (a)(4) of Proposed Rule 17g-6 are shown in attachment 1 hereto. If you have any questions or would like to discuss our comments further, please feel free to contact me (telephone: 212-339-3482; e-mail: BStern@FSA.com).

Respectfully submitted,

Bruce E. Stern,
Chairman, AFGI Government Affairs Committee
General Counsel, Financial Security Assurance Inc.

Attachment 1

(4) Issuing or threatening to issue a lower credit rating, or lowering or threatening to lower an existing credit rating, or refusing to issue a credit rating or withdrawing a credit rating, with respect to securities or money market instruments issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction, **or with respect to the claims-paying ability or financial strength of a financial guaranty insurer,** unless a portion of the assets which comprise the asset pool or the asset-backed or mortgaged-backed securities, **or a portion of the outstanding obligations insured by the financial guaranty insurer,** also are rated by the rating organization. The prohibitions on refusing to issue a credit rating or withdrawing a credit rating shall not apply if the rating organization has rated less than 85% of the market value of the assets underlying the asset pool or the asset-backed or mortgage-backed securities**, or of the outstanding obligations insured by the financial guaranty insurer. The prohibitions on issuing or threatening to issue a lower credit rating, or lowering or threatening to lower an existing credit rating, shall only apply if the assets underlying the asset pool or the asset-backed or mortgage-backed securities or the insured obligations, as applicable, have been rated by another rating organization. As used in this paragraph (4), "credit rating" shall include an assessment of the creditworthiness of an insured obligor as an entity or with respect to specific insured securities or money market instruments, without giving effect to such insurance.**