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June 9, 2005

Via E-Mail (rule-comments@sec.gov)

Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
450 Fifth Street, NW
Washington, D.C. 20549

Re: Definition of Nationally Recognized Statistical Rating Organization
Release Nos.: 33-8570; 34-51572; IC 26834;
File No.: S7-04-05

Dear Mr. Katz:

On behalf of Rating and Investment Information, Inc. (“R&I”), thank you for the opportunity to comment on the Commission’s release (“Proposing Release”) proposing to define the term “nationally recognized statistical rating organization” (“NRSRO”). R&I particularly welcomes the Commission’s clarification in the Proposing Release of its intention to continue to use the no-action letter process to provide certainty to users of ratings, and the Commission’s position on allowing credit rating agencies to exercise self-regulation with regard to conflicts of interest and confidentiality obligations. We further appreciate the Commission’s indication that it will promptly review no-action requests, with a view to responding to such requests within 90 days after a rating agency’s submission of all necessary information. R&I also welcomes the Commission’s acknowledgement that credit rating agencies may be recognized as NRSROs if they are considered reliable in the marketplace in particular sectors of the debt market or particular geographic areas.

By way of background, with offices in Tokyo, Hong Kong, and New York, R&I is the largest rating agency in Japan, rating more yen-denominated issues than any other rating organization. R&I and its predecessors have twenty-seven years’ experience in providing rating and financial information to issuers, broker-dealers, and the financial marketplace. In 2004, R&I rated approximately 65% of all Japanese issuers.

Publicly Available Credit Ratings

R&I agrees with the Commission’s position that publishing credit rating symbols alone, without the detailed supporting analyses, on a credit rating agency’s Web site free of charge should satisfy the public availability component of the definition. R&I further believes, to provide “current assessments,” that rating agencies should also indicate, free of charge, the rating outlook and the commencement of review procedures when there is a material change of factors which is likely to affect the creditworthiness of issues or issuers.

General Acceptance in the Financial Markets

We agree that general acceptance in the financial markets would reflect the markets' belief in the reliability of a rating agency's ratings. As the Commission has done in the past, we believe it should continue to rely on information from predominant users of securities ratings. However, we believe the Commission should expand that group to include providers of electronic information, such as Reuters and Bloomberg. These electronic information services have become part of the infrastructure of the global securities markets, and their use of ratings by certain rating agencies should also be considered in determining market acceptance.

We also believe that general acceptance can be determined by additional means. The rating agency's penetration in the issuer market, which could be measured by the percentage of issuers who engage the rating agency to rate their securities, would be a useful measure because issuers typically are very familiar with the market for their securities and would most likely select rating agencies that their investors rely upon to rate their securities. Another method would be to measure the rating agency's reliability by evaluating the correlation between the agency's ratings and the spread of the issues over the yield of government issues (such as, U.S. Treasuries in the United States, or Japanese Government Bonds "JGBs" in Japan).

Limited Coverage NRSROs

Consistent with the Commission's view of "limited coverage NRSROs" in Section III.B.2.b. of the Proposing Release, we agree that a credit rating agency that has developed a general acceptance in the financial markets for a limited sector of the debt market or a limited geographic area could meet the NRSRO definition. Specifically, when a credit rating agency has demonstrated that it possesses unique expertise in rating particular securities, or securities of a particular currency denomination, investors and the marketplace should be able to receive the benefit of this expertise and utilize the ratings of that entity for regulatory purposes. Thus, recognition will be beneficial for U.S. investors who invest globally. In addition, the Commission's recognition of these credit rating agencies will encourage additional market participants and promote competition among NRSROs.

The Commission has posed four questions in connection with its consideration of limited coverage NRSROs, to which we respond below.

1. Should a credit rating agency that is recognized by the financial marketplace for issuing credible and reliable ratings within a limited sector or geographic area meet the NRSRO definition only for its ratings within such sector or geographic area, or more broadly?

We believe very strongly that a credit rating agency that is so recognized would meet the NRSRO definition for ratings beyond the limited sector or geographic area. As stated in the Proposing Release, the Commission designed the "nationally recognized" component to "ensure that credit ratings used for regulatory purposes are credible and reliable, and are reasonably relied upon by the marketplace." The Commission further states, "Such acceptance would reflect the markets' belief in the credibility and reliability of the ratings provided by the credit rating agency and should provide some level of assurance to those relying on ratings with regard to the dependability and consistency of the ratings for a variety of regulatory purposes."

Accordingly, if an agency's ratings are recognized as "credible and reliable," even in a limited sector or region, that is a verifiable reflection of the agency's standards and procedures in place to ensure the credibility and reliability of the ratings. These standards and procedures do not change simply because the agency rates securities outside of its limited recognition. Certainly, with the growth and globalization of the securities markets, there exist today numerous additional debt securities than existed in 1975 when the NRSRO concept was first used. The Commission has shown no indication that it believed the original NRSROs were incapable of issuing credible and reliable ratings on new types of securities as they were introduced. Likely, this is because the original NRSROs were found to have appropriate standards and procedures in place to ensure they issued credible and reliable ratings on all ratings they issued despite never having issued a rating on a particular type of security in the past.

The same should be true for NRSROs originally recognized for their ratings in limited categories. That is, once an agency has demonstrated its wide acceptance for issuing credible and reliable ratings in certain sectors, there is no reason to believe they will begin issuing incredible and unreliable ratings on other issues merely because they expand into an area they have not covered in the past. Furthermore, from a commercial and business perspective, a credit rating agency's reputation for credibility and reliability is paramount to its business. It would be nonsensical for an agency to spend years establishing and maintaining that credibility only to discard it by haphazardly expanding into a new or different business area.

2. If a credit rating agency meets the NRSRO definition only with respect to its ratings within a particular sector or geographic area, would the NRSRO classification interfere with the credit rating agency's ability to expand its business?

This question reflects the larger "chicken and egg" problem the Commission faces with the NRSRO concept as a whole. The technical answer to this question is probably "no." That is, a credit rating agency technically is free to expand its business in any direction it chooses. The realistic and practical answer, however, is "yes," limitations in recognition would impede a credit rating agency's natural business expansion into areas beyond the limited scope that the Commission originally recognizes.

Certainly, the staff of the Division of Market Regulation considered this impediment to competition in 1999 when it removed the limitation on Thomson BankWatch's recognition for ratings on debt of financial institutions to recognition as a full NRSRO.[1] In its letter to the Division staff requesting full-recognition, Thomson BankWatch stated that its limited designation "has failed to keep pace with the significant developments in the banking industry and with the resultant expansion in type of rating activities that [Thomson] BankWatch's clientele demands." It also stated that the limited designation imposed an "unwarranted burden on the firm's ability to fully compete in the ratings arena, despite its overwhelming qualifications to do so." Thus, the evolution of Thomson BankWatch is empirical evidence that reveals the natural outcome of limited recognition. Using Thomson BankWatch as a case study, limited recognition does indeed interfere with an agency's ability to remain competitive in a continually evolving industry.

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[1] *See* Letter from Lee A. Pickard to Michael A. Macchiaroli, dated November 4, 1998, and letter from Michael A. Macchiaroli to Lee Pickard, dated January 25, 1999.

3. How should ratings from such an NRSRO be identified so that broker-dealers and other users of NRSRO ratings for regulatory purposes can determine which credit ratings from the NRSRO may be used for regulatory purposes?

If the Commission determines that credit rating agencies can be recognized as NRSROs for limited categories, to minimize confusion, we suggest that these types of rating agencies indicate which ratings can be used for regulatory purposes with a footnote.

4. We noted above that commenters mentioned that it would be difficult for limited coverage NRSROs to provide a full and accurate assessment of credit risks without a broader expertise in credit risk assessment. We request further comment on this view given our proposal to permit limited coverage NRSROs.

It seems impractical and without merit to suggest that an entity with a particular expertise is incompetent to practice that expertise because it is not a recognized "generalist." An analyst must master the fundamental skills of credit analysis before fine-tuning those skills into a particular area of expertise. The analyst's acquired expertise in a particular area is not undermined by a lack of expertise in other areas. To the contrary, such a level of focus would enhance the chosen expertise.

Analyst Experience and Training

We believe that the Commission should not set any criteria or rules with respect to a rating agency's employment decisions. Although an individual analyst's analytical ability and expertise can affect the quality of ratings, a rating agency's opinions generally should be determined by a committee involving several analysts. Using a committee to determine ratings helps ensure objectivity and risk analysis from diverse viewpoints, and it helps avoid conflicts of interest. Thus, an evaluation of analyst qualifications should focus more on the rating agency as a whole rather than on the individual analyst. Accordingly, we believe it would be unnecessary to impose rules or restrictions on analyst qualifications.

In addition, it would be difficult to set parameters on a rating agency's employment decisions because an agency needs to be flexible enough to make changes to its staff to accommodate for changes in the market. For example, the natural evolution of structured finance transactions may result in a surge in real estate-related transactions. This might result in an agency's decision to hire a real estate appraisal expert to join a team of a structured finance analysts. Such an employee may be a necessary addition to a rating agency, but may not have the same skill set that would be attributed to a traditional credit rating analyst. Thus, if regulatory guidelines limited an agency to only hiring analysts with finance or accounting backgrounds, it might actually be detrimental to the quality of the ratings. Accordingly, we believe the best way to ensure credible and reliable ratings is to maintain flexibility and allow rating agencies to make appropriate employment decisions and avoid even broad generalizations as to who should be considered "qualified" as an analyst.

Number of Ratings Per Analyst

We agree that a single analyst should be responsible for a reasonable and limited number of issues or issuers. However, the number that each analyst covers must take into account the complexity and volatility in creditworthiness of those issues or issuers. The more complex the issue or issuer, the fewer an analyst should cover at one time. Likewise, the more volatile the creditworthiness of a particular issue or issuer, the more time it will consume to effectively monitor it and make appropriate rating changes.

These complexities can change over time with the evolving market, which may require the rating agency to make adjustments in its analyst coverage. The rating agency should not be restricted from making such necessary adjustments to its operations. Accordingly, we agree with the Commission's position to refrain from imposing such restrictions or parameters.

Conflicts of Interest

We agree with the Commission that rating agencies should establish policies and procedures to minimize potential conflicts of interest. We believe rating agencies can address potential conflicts by establishing firewalls and implementing written procedures for information management. A rating agency's disclosure of its measures to minimize potential conflicts would allow users of its ratings to make business decisions after evaluating the strength of those policies. We believe this market-driven system would be an effective means of ensuring that each rating agency keeps pace with market changes to the extent they affect policies concerning conflicts of interest. Accordingly, it would be unnecessary for the Commission to establish specific guidelines for these policies and procedures.

Misuse of Information

We agree that rating agencies should be required to have policies and procedures in place that are designed to effectively protect nonpublic information provided by issuers.

Financial Resources

We agree that rating agencies should make available their audited financial statements to ratings users. We also share the concern that a rating agency's over-dependence on revenues generated by particular clients may lead to conflicts of interest. However, we believe that rating agencies should not be required to disclose the amount of revenue generated by specific issuers. In particular, some clients request work from rating agencies on a confidential basis. These clients typically request non-disclosure agreements prior to engaging the agency's services. Thus, disclosure of the clients' identities would violate the express agreements they request of the agencies. In addition, revealing the identity of clients of a rating agency who generate the highest revenues would unnecessarily reveal both the agency's confidential business secrets and the clients' privacy. To address both concerns, we believe that rating agencies should have policies and procedures in place to limit the percentage of total revenues they receive from any one issuer. We believe that placing a limitation on the total revenues generated by an issuer, as compared to an agency's total revenues, will minimize the potential for over-dependence on a particular issuer while maintaining confidences of the agency's clients and business.

Standardized Rating Symbols

We agree with the Commission that rating agencies should continue to use market-based rating symbols.

90-Day Review of No-Action Requests

The Rule Proposal indicates that the Commission staff would act on a no-action request within "90 days after a credit rating agency has submitted all necessary information." We agree that the Commission should retain the no-action process and implement a time limit for the staff to issue a response. To effectively implement the 90-day review and enhance transparency of the process, we believe that the Commission or staff should identify a definite set of documents or information that will trigger

commencement of the 90-day review period. Without such specific guidelines, the 90-day period could result in further confusion and delays for requesters of NRSRO no-action relief.

Again, thank you for the opportunity to comment on the Proposing Release. If you would like further information on, or clarification of, the foregoing, please contact me at yharada@r-i.co.jp or +81-90-1777-8171.

Sincerely yours,

Yasuhiro Harada
President
Rating and Investment Information, Inc.

cc: The Hon. William H. Donaldson, Chairman
The Hon. Paul S. Atkins, Commissioner
The Hon. Roel C. Campos, Commissioner
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