COUNCIL OF INSTITUTIONAL INVESTORS

Suite 500 • 888 17th Street, NW • Washington, DC 20006 • (202) 822-0800 • Fax (202) 822-0801 • www.cii.org

Via Email

July 24, 2008

Florence E. Harmon,
Acting Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: *Proposed Rules for Nationally Recognized Statistical Rating Organizations (File Number: S7-13-08)*

Dear Ms. Harmon:

I am writing on behalf of the Council of Institutional Investors, a nonprofit association of more than 140 public, union and corporate pension funds with combined assets that exceed $3 trillion. Member funds are major shareowners with a duty to protect the retirement assets of millions of American workers. As a leading voice for long-term, patient capital, the Council welcomes the opportunity to comment on the Securities and Exchange Commission's (SEC) proposed enhancements to its rules for Nationally Recognized Statistical Ratings Organizations (NRSROs).

The Council's general statement on financial gatekeepers encompasses rating agencies and asserts that the Council supports financial gatekeepers that are "transparent in their methodology, avoid or tightly manage conflicts of interest and have robust oversight."[1] Council members approved the statement in response to the rating agencies' gross underestimation of the risks of complex mortgage-linked structured products. While credit rating agencies did not create the credit crisis, their practices contributed to the debacle.

Consistent with that position, the Council generally supports provisions in the proposed rules that would enhance investors' and the SEC's understanding of NRSRO ratings on structured finance products. The Council also lauds provisions that would curb or manage conflicts of interest between rating agencies and entities that purchase ratings from them. Credit rating agencies have long maintained that their ratings are merely opinions. But in practice, the agencies wield considerable influence over market participants. Such clout carries a responsibility to ensure that ratings are arrived at fairly, that the ratings methodology is appropriate and transparent and that market participants can evaluate the performance of ratings over time.

Proposed Amendments to Rule 17g-5 - Disclosure and Management of Conflicts of Interest

Disclosure of information provided to and used by an NRSRO in rating a structured product
The Council appreciates that the provision aims to manage the conflicts of interest of an issuer-pays rating, increase the transparency of the ratings process and foster competition. We generally support the amendment and

[1] Council of Institutional Investors, Other Council Governance Policies: Transparency, Independence and Oversight of Financial Gatekeepers http://www.cii.org/UserFiles/file/council%20policies/05-22-08%20final%20Council%20statement%20on%20financial%20gatekeepers.pdf

urge that the scope of the information covered include the methodologies and underlying assumptions used by the rating agency, rather than just the raw data.

The amendment does not make clear, however, who is responsible for disclosing the information about the assets underlying a structured product. We think NRSROs should make the information available; otherwise, investors may be forced to hopscotch around the Web sites of the issuer, underwriter, sponsor, depositor or trustee to find it. In response to questions in the release, we also recommend that the SEC require the disclosure of any steps taken by any of the parties (NRSOR, issuer, underwriter, sponsor, etc.) to verify information about the assets underlying a structured product and the results of those efforts. If no attempt was made to verify the information, that should be disclosed, too.

Prohibition on an NRSRO rating a structured finance product that it has helped structure
For credit ratings to be objective and to be viewed as objective, the rating agency must be independent of the client issuer or obligor. Toward that end, an NRSRO should not rate its own work. For similar reasons, the Sarbanes-Oxley Act bars auditors from providing several types of non-audit services to their audit clients.[2] The Council supports the prohibition on rating agencies advising issuers or obligors on how to structure products in order to receive a specific rating. However, we recognize that it may not be possible to draw a clear line between acceptable explanation and feedback during the rating process and recommendations about how to obtain a desired rating. The SEC should consider requiring NRSROs to establish an executive-level compliance officer charged with monitoring such discussions.

Prohibition on credit rating analysts or rating committee members from participating in fee discussions
We strongly support this amendment. It would guard against the temptation for rating agencies to put business interests ahead of the objectivity and quality of ratings.

Proposed Amendments to Rules 17g-2 - Disclosure of records

Requirement that NRSROs keep records of all rating actions and make them publicly available on their Web sites
The Council supports the requirement, which we think would help market participants evaluate the accuracy of ratings over time and across agencies. It would be more efficient for investors to view the data in a central registry in EDGAR or elsewhere on the SEC's Web site. Hence, we encourage the SEC to consider establishing a central registry for this information and requiring NRSROs to submit the data to the Commission. We understand that a time lag would be needed to avoid undermining the subscriber-pays business model of some NRSROs.

Requirement that NRSROs keep a record of any material deviation in a rating
The Council strongly supports the proposal that a rating agency document the rationale for any material difference in the rating implied by the quantitative model and the actual rating issued. This could help the SEC determine whether a rating agency veered improperly from its rating procedures. The recordkeeping would be extremely valuable to investors, too; a growing pile of "deviation from the model" documents could signal unreliability of ratings, shoddy practices, pressure from issuers for specific ratings or a desire on the part of the NRSRO to curry favor with certain issuers or arrangers. The SEC should require NRSROs to publicly disclose the records, which would be valuable to investors.

[2] Sarbanes-Oxley Act of 2002, Section 201(a)

Requirement that NRSROs keep records of complaints about analyst performance
The Council supports the proposed requirement that NRSROs keep records of complaints about the performance of a credit analyst in relation to a rating. Such records could reveal how the rating agency handles pressure from issuers interested in obtaining specific ratings and might deter NRSROs from caving in to pressure to reassign an analyst. The SEC should require the records, or a sanitized version of them, to be disclosed publicly so investors could also get a clearer picture of how well an NRSRO manages conflicts of interest.

Proposed Amendments to Instructions for form NRSRO

Requirement to disclose enhanced ratings performance measurement statistics
The Council welcomes the proposal for greater specificity about performance statistics; requiring performance statistics for 1, 3 and 10 year periods for each asset class would enhance investors' ability to compare trends and evaluate the performance of NRSROs over time.

Proposed New Rule 17g-7 - Differentiated Ratings or Special Report for Structured Products

The SEC's proposal to differentiate ratings for structured products via a separate ratings nomenclature is more problematic for the Council to address as it is beyond the scope of our policies. An informal survey of Council members found that some favored a different ratings system for structured products while others opposed it. For these reasons, the Council takes no position on the use of differentiated ratings for structured products.

We do find value in a report that alerts investors to the different rating methodologies and risk characteristics associated with structured finance products. According to reports, many investors did not fully appreciate the extent to which structured products differed from corporate bonds until the market for complex mortgage-linked securities screeched to a halt. Some sort of red flag could be helpful. The danger, as the SEC has noted, is that such reports could become boilerplate and eventually ignored over time. However, requiring NRSROs to include the specific assumptions underlying the rating methodology used and any deviations from the methodology that were incorporated in the rating would make the reports relevant to market participants.

The Council appreciates the opportunity to comment on these proposals. Thank you for your efforts to improve the transparency of the credit rating process and the agencies' management of conflicts of interest.

Sincerely,

Amy Borrus
Deputy Director