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March 12, 2007

Via Email

Nancy M. Morris, Secretary
U.S. Securities & Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: S7-04-07 - Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations

Dear Ms. Morris:

We appreciate the opportunity to comment on the U.S. Securities and Exchange Commission's ("SEC" or "Commission") proposed rules governing the registration of Nationally Recognized Statistical Rating Organizations ("NRSROs"). Rating and Investment Information, Inc. ("R&I") generally supports the Commission's efforts to establish a registration process for credit rating agencies to obtain recognition as NRSROs, as mandated under the Credit Rating Agency Reform Act of 2006 (the "Act").[1] For the reasons described below, however, R&I disagrees with and/or requests clarification of certain required elements of the proposed rules.

Form NRSRO

Item 8

Item 8 of the Proposed Form NRSRO would require credit rating agencies to disclose on a disclosure reporting page whether a credit rating agency or person associated with the credit rating agency has "committed certain acts under Section 15(b)(4)(A), (D), (E), (G) or (H) of the Exchange Act, been convicted of certain offenses described in Section 15(b)(4)(B) of the Exchange Act, been convicted of certain other offenses, or if a person associated with the [credit rating agency] is subject to a Commission order suspending or barring the person from being associated with an NRSRO."[2] This information would be publicly available.

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[1] See Pub. L. No. 109-291 (2006).

[2] See NRSRO Proposing Release at 6386.

To the extent information with respect to arrests or accusations is disclosed, rather than a final adjudication of wrong-doing, R&I respectfully requests that such information be afforded confidential treatment.

Exhibit 1

Exhibit 1 of the Commission's Proposed Form NRSRO would require that credit rating agencies disclose their "credit rating performance measurement statistics over short-term, mid-term and long-term periods," as dictated by the Act.[3] Neither the Act nor the Commission define "short-term," "mid-term," or "long-term" periods.

R&I agrees with the Commission that historical default rates and rating transition matrixes that include clear definitions of default are important indicators of credit rating agency performance. R&I, however, does not believe that credit rating agencies should be required to measure, and therefore disclose, the performance of a credit rating by mapping it to the market value of the rated security. Unlike equity securities that are traded on an exchange and have a defined closing price, bonds are traded on the Over-the-Counter ("OTC") market where the market value (price) can vary among brokers and dealers. The market value of rated securities can also be influenced by the liquidity of such securities, as brokers and dealers might quote arbitrary prices for securities with low-liquidity.

Given the fact that the definition of default may vary according to the bankruptcy laws of different countries, R&I does not believe that it would be realistic for the Commission to establish a standard methodology to measure the performance of credit ratings. R&I, however, does not believe that NRSROs should be able to choose their own, undisclosed definitions of "short-term," "mid-term," and "long-term" periods. Therefore, R&I proposes that the Commission require credit rating agencies to disclose the criteria used in defining each time period and prevent NRSROs from arbitrarily changing such criteria over time.

Exhibit 3

Exhibit 3 of the Commission's Proposed Form NRSRO would require a credit rating agency to "furnish [to the Commission] its policies and procedures to prevent the misuse of material, nonpublic information established under Section 15E(g) of the Exchange Act and proposed Rule 17g-4."[4] This information would be publicly available.

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[3] See NRSRO Proposing Release at 6387.

[4] Id. at 6389.

R&I believes that to the extent the Commission decides to publicize any part of Form NRSRO or its exhibits, the Commission should afford confidential treatment to a credit rating agency's procedures regarding the prevention, detection and misuse of material, non-public information as this information should be considered proprietary business information. Furthermore, public disclosure of such information might hinder the effectiveness of such procedures.

Exhibit 4

Exhibit 4 of the Commission's Proposed Form NRSRO would require credit rating agencies to disclose their organizational structure, including "an organizational chart that identifies the credit rating agency's ultimate and sub-holding companies, subsidiaries, and material affiliates…."[5] The Commission does not propose a definition of "material affiliate."

R&I believes that a credit rating agency should not be required to disclose information with respect to affiliated entities if the ownership percentage is low and recommends that the Commission define "material affiliate."

Exhibit 7

Exhibit 7 of the Commission's Proposed Form NRSRO would require credit rating agencies to furnish to the Commission a copy of their "policies and procedures to address and manage conflicts of interest."[6] This information would be publicly available.

R&I believes that, to the extent the Commission decides to publicize any part of Form NRSRO or its exhibits, the Commission should afford confidential treatment to a credit rating agency's procedures regarding conflicts of interest as this information should be considered proprietary business information. Furthermore, public disclosure of such information might hinder the effectiveness of such procedures.

Exhibits 8 and 9

Exhibit 8 of the Commission's Proposed Form NRSRO would require credit rating agencies to "disclose information about the responsibilities, experience and employment history of its credit analysts and supervisors," including post-secondary education.[7]

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[5] See Proposed Instructions to Form NRSRO, Exhibit 4.

[6] NRSRO Proposing Release at 6390.

[7] Id. at 6391.

Likewise, Exhibit 9 of the Commission's Proposed Form NRSRO would require credit rating agencies to disclose "information about the experience and employment history of the designated compliance officer and persons assisting the officer," including such persons' responsibilities and post-secondary education.[8]

R&I does not believe that disclosing such information is appropriate because the responsibilities, employment history, and post-secondary education of R&I's analysts, supervisors, compliance officer, and persons assisting the compliance officer is personal data, which belongs to each individual employee. In lieu of disclosing personal information about such persons, R&I respectfully proposes that the Commission require NRSROs to disclose their recruitment criteria, training policies and training track records. If the Commission determines that disclosure of the aforementioned information is necessary, R&I respectfully proposes that such information be afforded confidential treatment.

Exhibit 10

Exhibit 10 of the Commission's Proposed Form NRSRO would require credit rating agencies to submit to the Commission "a list of the 20 largest issuers and subscribers that use the credit rating services provided by the credit rating agency by amount of net revenue…. [and] certain large obligors…and underwriters…if they are determined to have provided at least as much net revenue as the 20th largest issuer or subscriber."[9] It is unclear why credit rating agencies must first rank their 20 largest issuers and subscribers and then add to the list an unlimited amount of underwriters and obligors of a particular size. R&I respectfully proposes that the Commission simply require credit rating agencies to inform the Commission of their 20 largest issuers, subscribers, underwriters and obligors.

Exhibit 12

Exhibit 12 of the Commission's Proposed Form NRSRO would require credit rating agencies to disclose, among other things, the amount of revenue generated from subscribers.[10] Neither the Act nor the Commission defines the term "subscriber."

R&I publishes all of its ratings, together with a summary of R&I's rating rationale, on its web site, which is free of charge to the public, so long as its customers have agreed to

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[8] Id.

[9] Id.

[10] See NRSRO Proposing Release at 6393.

such disclosure. R&I also maintains a fee-based web site in which customers pay a fee to access more detailed information on each individual rating. R&I respectfully requests clarification that such revenue from a fee-based website would not be considered "revenue from subscribers" for purposes of Exhibit 12 of the Proposed Form NRSRO.

R&I also respectfully proposes that the Commission either define the term subscriber or provide an interpretation of what they understand the term to include. R&I respectfully requests clarification that "revenue from subscribers" would only apply to those credit rating agencies that employ the "subscriber business model," in which agencies only disclose their ratings to its subscribers, as opposed to the public.

Rule 17g-1(f)

Section 15E(b)(1) of the Act states that "[e]ach nationally recognized statistical rating organization shall promptly amend its application for registration … if any information or document provided therein becomes materially inaccurate…."[11] Although neither the Act nor the Commission has proposed a definition of "promptly," the Commission has stated that it believes amendments should be made "as soon as reasonably practicable," which they believe "should not take more than two days."[12]

R&I believes that amending materially inaccurate documents is not practicable within two days for non-resident credit rating agencies, especially since such materials must be prepared in an agency's native language and then translated into English. R&I respectfully proposes that the Commission allow non-resident credit rating agencies ten business days to prepare amendments to materially inaccurate documents.

Rule 17g-2(b)(6)

Proposed Rule 17g-2(b)(6) would require NRSROs to "retain all marketing materials relating to the business of operating as a credit rating agency."[13] It is our understanding that this provision as drafted would include all internal and external materials prepared for purposes of marketing. R&I believes this provision is too broad and does not address whether a credit rating agency would be required to maintain, for example, internal memos within the marketing department. R&I respectfully proposes that the Commission define "marketing materials" to ensure that all credit rating agencies are aware of what materials they need to retain. R&I also respectfully proposes that the

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[11] 15 U.S.C. § 78o-7(b)(1) (2006).

[12] See NRSRO Proposing Release at 6383.

[13] Id. at 6395.

Commission narrow the scope of the rule to require credit rating agencies to retain marketing materials distributed to customers for the purpose of soliciting or retaining credit agency ratings.

Rule 17g-2(c)(2)

Proposed Rule 17g-2(c) provides that "the records with respect to customers would need to be retained for three years after the NRSRO's business relationship with the customer ended."[14] An NRSRO oftentimes has relationships with customers that can span decades. It would be untenable to maintain all customer records for decades. R&I respectfully proposes that the Commission require NRSROs to maintain customer records for a period of three years after the conclusion of the business relationship up to a maximum of six years from the time of creation.

Rule 17g-2(e)

Proposed Rule 17g-2(e) would require NRSROs to furnish "the Commission with a written undertaking of [any third-party record] custodian" if an NRSRO's records are made or retained by a third-party record custodian.[15] R&I believes that it may not be feasible in Japan to obtain such an undertaking from a third-party record custodian because of business practices established in the record custodian industry. R&I respectfully proposes that in lieu of an undertaking by a third-party custodian, the SEC require the NRSRO to make a pledge to the same effect.

Rule 17g-2(f)

Proposed Rule 17g-2(f) would require non-resident NRSROs to "undertake to send books and records to the Commission and its representatives upon request…and the proposed undertaking would require a translation [into English] if the Commission requested it" within 14 days of receipt of a request, or within a longer period of time with Commission consent.[16] It is extremely burdensome and costly for a non-resident NRSRO to translate a large volume of documents into English. R&I believes that 14 days is not a sufficient period of time to prepare and translate such documents into English and respectfully proposes that the time period be extended to 30 days or longer with Commission consent. Further, R&I respectfully requests that the Commission keep its requests for translated

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[14] Id. at 6396.

[15] Id. at 6396.

[16] Id.; Proposed 17 CFR § 240.17g-2(f) (2007).

documents as narrow as possible, in recognition of the time and expense involved in such requests.

Rule 17g-2(h)

In its proposal, the Commission clearly has recognized that foreign credit rating agencies will seek to become registered as NRSROs. R&I respectfully suggests that, when applying the proposed rules to non-resident rating organizations, the Commission fully respect the competitive environments in individual countries, foreign capital market business practices, and the relevant rules and regulations non-resident rating organizations must follow beyond those of the U.S.

Rule 17g-3(a)

Proposed Rule 17g-3 would require NRSROs, on an annual basis, to submit to the Commission their audited financial statements prepared in accordance with Generally Accepted Accounting Principles ("GAAP") and Regulation S-X, within 90 calendar days after the end of an NRSRO's fiscal year. R&I respectfully requests clarification that the Commission would accept financial statements prepared in accordance with foreign GAAP, such as Japanese GAAP. If an NRSRO submits its financial statements in accordance with Japanese GAAP, such financial statements would still provide sufficient information to determine whether an NRSRO is financially sound enough to maintain the independence and subjectivity of its credit rating business. R&I also respectfully requests that non-resident credit rating agencies be permitted to use an alternative to Regulation S-X in preparation of their financial statements.

Further, R&I believes 90 calendar days after the end of the fiscal year is not a sufficient period of time for a non-resident NRSRO to prepare and translate its financial statements and certification from an independent public accountant into English. R&I respectfully proposes that non-resident NRSROs be given 120 calendar days after the end of their fiscal year to furnish their financial statements to the Commission.

Rule 17g-5(a)

Proposed Rule 17g-5(a) would state that it is "unlawful for a[n NRSRO] or a person associated with [an NRSRO] to have a conflict of interest relating to the issuance of a credit rating…" unless the NRSRO has disclosed such conflicts on Form NRSRO and has "implemented policies and procedures to address and manage conflicts of interest…."[17]

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[17] Proposed 17 CFR § 240.17g-5 (2007).

R&I does not believe that the use of the term "unlawful" is appropriate in the context of Proposed Rule 17g-5(a) since the proposed rule does not prevent a credit rating agency from having the enumerated conflicts. R&I respectfully proposes that the Rule state that NRSROs may only have the conflicts of interest enumerated in paragraph (b) if: (1) the rating organization has disclosed the type of conflict of interest on Form NRSRO in accordance with Section 15E(a)(1)(B)(vi) of the Act; and (2) the rating organization has implemented policies and procedures to address and manage conflicts of interest in accordance with Section 15E(h) of the Act.

Rule 17g-5(c)(1)

Proposed Rule 17g-5(c)(1) would prohibit an NRSRO from issuing or maintaining "a credit rating solicited by a person that, in the most recently ended fiscal year, provided the rating organization and its affiliates with net revenue…equaling or exceeding 10% of the total net revenue of the rating organization and its affiliates for the year."[18]

R&I recognizes that, in the case of corporate issuers or obligors, the receipt of a substantial portion of a credit rating agency's total revenue from a single person could be problematic. It is not burdensome for a credit rating agency to identify who paid the fee for corporate issuers and obligors. However, in the structured financial products area, net revenue resulting from an arranger can be deceptively large, even though there may be many actual payers of the fee behind the transactions. As a result, it may very well be unreasonably costly and burdensome to identify who paid the fee. Although the actual beneficiaries of structured financial product transactions are often originators, rating fees for structured products are usually paid by the arranger, after negotiations between the originator and the arranger. It would be highly costly and virtually impossible to identify the actual beneficiaries behind each transaction and to monitor the revenue that flowed from each beneficiary. Prohibiting a single person from comprising in excess of 10% of an NRSRO's net revenue could have a materially adverse impact on the structuring of financial products and the ability of issuers to raise capital through the arranger of their choice. For example, an arranger may be precluded from participation in a structured transaction, depending on the amount of revenues received by a credit rating agency from such arranger year to date. Therefore, R&I respectfully proposes that the Commission only apply the aforementioned 10% revenue prohibition to revenues from corporate issuers and obligors, and not to revenue from the arrangers of structured finance products. R&I respectfully further proposes that the Commission consider requests for exemptive relief from the aforementioned prohibitions, should there be material changes in the financial or economic environments or in the structure of the capital markets which

[18] Proposed 17 CFR § 240.17g-5(c)(1) (2007).

threaten to increase the possibility that the revenue from one single person could exceed 10% of the total revenue of rating organizations.

Rule 17g-5(c)(2)

Proposed Rule 17g-5(c)(2) would prohibit a credit rating agency from issuing or maintaining "a credit rating with respect to a person where the rating organization, a credit analyst who participated in determining the credit rating, or a person associated with the rating organization responsible for approving the credit rating, owns securities of, or has any other ownership interest in, the rated person or is a borrower or lender with respect to the rated person."[19]

R&I respectfully proposes that the aforementioned prohibited conflict of interest should contain an exception for indirect ownership of rated securities, such as investments in mutual funds and personal borrowing from rated financial institutions, such as home mortgage loans.

Rule 17g-6(a)(4)

Proposed Rule 17g-6(a)(4) prohibits NRSROs from "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, unless a portion of the assets which comprise the asset pool or the asset-backed or mortgage-backed securities also are rated by the rating organization. [The Rule provides that] "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."[20]

R&I believes that a rating organization may have other legitimate reasons for refusing to issue, withdrawing, or lowering a credit rating, beyond the enumerated 85% exception. A rating organization may have to refuse to issue or withdraw a credit rating on a structured product if another product issued out of the same vehicle is not rated by the same rating organization. For example, in order to issue a credit rating on a structured product an NRSRO might need to review the agreements with respect to other products issued out of the same vehicle that are not rated by the rating organization. However, if the arranger of the unrated product refuses to allow the rating organization to review the

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[19] See Proposed 17 CFR § 240.17g-5(c)(2) (2007).

[20] See Proposed 17 CFR § 240.17g-6(a)(4) (2007).

agreements, the rating organization has no choice but to refuse to issue a credit rating as it would have insufficient information upon which to issue a new credit rating.

Furthermore, it is common in the Japanese structured finance market for agreements to provide that a new series can only be issued so long as it does not negatively affect the ratings of the existing series (when a series of products are issued out of the same issuing vehicle). Therefore, if such an issue of a new series is made, credit ratings on the existing series might be required to be lowered or withdrawn.

R&I respectfully proposes that Rule 17g-6(a)(4) allow an NRSRO to lower, refuse to issue or withdraw a credit rating so long as there is a legitimate rationale behind the action and the NRSRO maintains the records of such action in accordance with Rule 17g-2(b)(8).

Rule 17g-6(a)(5)

Proposed Rule 17g-6(a)(5) would prohibit a credit rating agency from "issuing an unsolicited credit rating and communicating with the rated person to induce or attempt to induce the rated person to pay for the credit rating or any other service or product of the rating organization or a person associated with the rating organization."[21]

R&I, in principle, agrees that credit rating agencies should be prohibited from soliciting payment for unsolicited credit ratings. However, as the Commission suggested, some credit rating agencies wish to maintain active credit ratings on all major issuers in a given industry. When a credit rating agency's business model includes issuing credit ratings on all active issues within an industry, R&I believes that the Commission should not prohibit such a credit rating agency from soliciting payment for such ratings. R&I respectfully proposes that credit rating agencies, whose business models include issuing active credit ratings on all major issuers within an industry, should be exempted from the prohibition on soliciting payment for a credit rating, but should not be permitted to solicit payment for other credit rating services.

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[21] See Proposed Rule 17 CFR § 240.17g-6(a)(5) (2007).

Please do not hesitate to call me with any questions you might have.

Thank you.

Sincerely yours,

Yasuhiro Harada
President
Rating and Investment Information, Inc.

cc: Neal E. Sullivan, Esq., Bingham McCutchen LLP
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