

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

March 25, 2009

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Re-proposed Rules for Nationally Recognized Statistical Rating Organizations (File Number: S7-04-09)

Dear Ms. Murphy:

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 birth of the SEC's NRSRO designation in the 1970s moved credit rating agencies from simply information suppliers to financial gatekeepers. NRSRO ratings are now woven into international and domestic laws and regulations, many of which directly impact the investment options of Council members, which on average invest 27.1 percent of their portfolios in fixed income securities. The quality of a rating is a vital concern to long-term shareowners such as Council members, 90 percent of which incorporate passive management strategies into their portfolios.¹

By registering as an NRSRO and accepting the quasi-governmental power associated with the title, credit rating agencies must also take on a responsibility to ensure that their ratings are arrived at fairly and are accurate. 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."² Council members approved the statement in response to the rating agencies' gross underestimation of the risks of complex mortgage-linked structured

¹ Council of Institutional Investors. *2008 Asset Allocation Survey*. Washington, D.C.: Council, 2008.

² 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>

March 25, 2009

Page 2 of 3

products. While credit rating agencies did not single-handedly create the credit crisis, their practices contributed to the debacle.

Consistent with that position, the Council supports provisions of the proposed rules that would enhance investors' and the SEC's ability to compare ratings and gauge the accuracy of ratings over time. The Council also lauds provisions that would increase competition within the industry by removing information barriers. With proper oversight and a system of accountability, the proposals will help repair the integrity of these financial gatekeepers.

Proposed Amendments to Rule 17g-2 – Disclosure of 100 Percent of Issuer-Paid Ratings

The Council generally supports the disclosure requirements, which we believe in the long term would help individual investors identify which NRSROs tend to be more accurate in their issuer-paid ratings and allow market participants to develop alternative performance measurement statistics. However, we encourage the Commission to consider strengthening the proposal in two areas.

First, the disclosure rule should apply to initial credit ratings issued on or after an earlier date. As proposed, only issuer-paid credit ratings determined on or after June 26, 2007, would be subject to disclosure. The Council is concerned that the 2007 start date would exempt a large number of now failing securitized products from appropriate market transparency. To ensure that investors and the marketplace at large have sufficient historical data to begin analyzing trends and NRSRO performance promptly, the Council believes an earlier start date is warranted.

Second, the rule should extend to unsolicited ratings issued by traditionally issuer-paid NRSROs and ratings produced by subscriber-paid NRSROs. These two types of ratings could serve as vital checks on agencies compensated by the issuers whose securities they rate. Without these checks, investors would lack the ability to compare ratings surrounded by issuer-pay conflicts with ratings independent of those conflicts.

The Council also believes that granting unsolicited and subscriber-paid ratings an exemption from disclosure would diminish the value of the proposed amendments to Rule 17g-5, which is intended to increase the ability of NRSROs to issue unsolicited ratings on structured products. For these reasons, the Council strongly encourages the Commission to consider extending the disclosure requirements to cover all ratings.

Re-Proposed Amendments to Rule 17g-5 – Disclosure of Structured Products' Underlying Information

The Council generally believes that with proper oversight the proposals to require the disclosure of structured products' underlying information could improve the transparency of the ratings process, quality of ratings and competition among NRSROs. In conjunction with the proposed amendments to Rule 17g-2, these proposals would provide investors with a broader range of views on the creditworthiness of securities, which in turn may also increase the likelihood that any inappropriate actions to favor an issuer could be exposed.

March 25, 2009

Page 3 of 3

As the re-proposed rules are written, access to structured products' underlying information would be limited to NRSROs only. Investors and other market participants, however, would be better served if the information were more broadly available, as the Commission first proposed in its June 16, 2008 release. The Council continues to support this level of transparency. In order to properly understand and analyze a structured security, as well as to evaluate the process and considerations an NRSRO took in determining its rating, market participants must be able to access the structured security's fundamental information.

At minimum, the Commission should grant all credit rating agencies, as defined by the Credit Rating Agency Reform Act of 2006, access to the information. Denying non-NRSROs the opportunity to evaluate these structured products would only serve to further entrench the select group of agencies that have already gained the title. With access to the information, smaller non-registered rating agencies could more easily establish track records, broaden their customer base and better position themselves to apply for registration with the SEC. By leveling the playing field, the Commission would lower barriers to entry and, in doing so, would provide investors with a wider range of views on the risk profiles of complex securities.

Finally, as stated in the proposing release, the Commission intends that the proposed disclosure requirements would apply to written communications only. At the very least, the Commission should require that an issuer certify, under penalty, that it will not provide any information, whether written or spoken, to a hired NRSRO without providing it to others. In addition to ensuring that all NRSROs have equal access to the information necessary to issue a quality rating on a structured product, the requirement would make it easier for both issuers and NRSROs to resist temptations to engage in anticompetitive behaviors.

We appreciate the opportunity to comment on these proposed rules. The Council encourages the Commission to continue its work to improve the transparency and independence of credit ratings and competition within the ratings industry. Please feel free to contact me with any questions at (202) 261-7086.

Respectfully,

A handwritten signature in black ink that reads "Laurel Leitner". The signature is written in a cursive, flowing style.

Laurel Leitner
Analyst
Council of Institutional Investors