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September 13, 2011

VIA E-MAIL: ***rule-comments@sec.gov***

Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090
Attn: Elizabeth M. Murphy, Secretary

Re: Release No. 34-64456; File No. 4-629

Dear Ms. Murphy:

Kroll Bond Rating Agency (KBRA) appreciates the opportunity to respond to the Securities and Exchange Commission (the "Commission") request for comment regarding Release No. 34-64456; File No. 4-629 (the "RFC"), to assist the Commission in carrying out a study on the feasibility of establishing a system in which a public or private utility or a self-regulatory organization ("SRO") assigns nationally recognized statistical rating organizations ("NRSROs") to determine credit ratings for structured finance products.

Rating Shopping

It is our understanding that the proposed utility/SRO mechanism is designed to minimize conflicts of interest associated with rating shopping. Rating shopping occurs when issuers of securities "shop" for a rating agency that offers the highest rating or, in the case of structured finance, the lowest enhancement levels for rated tranches. Rating shopping is not about searching for the lowest cost ratings

In the past, rating agencies cooperated with shoppers by lowering rating standards, thereby issuing misleading ratings and putting investors at risk of loss. Such cooperation contributed greatly to erroneous ratings being issued to residential mortgage-backed securities and derivative securitizations leading up to the recent credit crisis. The goal of the Commission should therefore be to assure that safeguards are in place to prevent deterioration in rating standards in the future.

In our opinion, the problem with rating shopping is not that an issuer is able to select and compensate a rating agency. Issuers should be free to work with any rating agency that best meets their needs. Instead, the problem stems from a lack of transparency around the rating agency selection process. This lack of transparency potentially allows a slippage in standards to occur well out of the sight of investors, regulators and others.

Proposed Rating Assignment Board

The Dodd-Frank Act introduces a proposal in which structured finance ratings would be assigned by a public or private utility or SRO (collectively the "Board"). In addition to assigning rating agencies to rate each structured transaction, the Board would have a say in their methodological developments, the measurement and monitoring of rating accuracy and in the fees paid to rating agencies. It is our view that such a bureaucratic solution risks damaging the market for structured products, because it:

1. May lead to uneconomic enhancement levels: In order to obtain assignments from the Board, rating agencies will provide enhancement levels that satisfy the Board's standards, rather than based on the merits of the security. If standards are unduly conservative, the cost of funds would be unnecessarily increased and issuers could possibly choose to forego securitization altogether. This would impair an important means of capital formation, and reduce the investment options available to investors in asset-based securities. Additionally, ratings may lose credibility as an independent source of information, thereby causing significant damage to NRSROs and, ultimately, to the structured finance market.

2. May give false confidence in Board-selected ratings: The investing public may look at the Board as providing a government-sponsored or government-approved rating. The inclusion of a disclaimer (as suggested in the proposal) will likely be insufficient to counteract this view.

3. May increase the liability of the U.S. government for ratings by selected NRSROs: By insinuating itself into the rating process, including assessments of the accuracy and effectiveness of rating methodologies, the Board will likely assume the liabilities of a rating agency. This unintended, but predictable, outcome will harm both the independence and perception of ratings published by NRSROs and the Commission's ability to conduct independent regulatory oversight.

4. May further entrench the largest incumbents: An appointment mechanism that requires an established track record could also correspondingly limit the ability of new NRSROs to compete in structured finance. This will constitute an additional barrier to entry and maintain the hegemony of the largest NRSROs.

5. May not prevent deterioration in rating standards: By creating a standard against which NRSROs are measured, the Board would effectively superimpose its own standard on all NRSROs. Uniform, board-approved rating criteria will likely become increasingly remote from market conditions. Rating agencies will have little incentive to innovate and improve upon board-sanctioned standards. Rather than preventing a degradation in rating standards, the Board mechanism raises the risk that standards will become monolithic and at odds with market reality.

In sum, we have grave doubts about the consequences, both intended and unintended, that would follow from the creation of a Board whose decisions will replace the discipline of the marketplace. Among others, we question how the Board will evaluate the performance of a new NRSRO, such as KBRA, in a way that enables it to obtain assignments based on merit.

Proposed Alternative

We propose that the Commission strongly consider a market-based solution to the problems associated with rating shopping. In particular, we advocate an increase in transparency around the rating selection process. Initial steps were taken in this respect when the Commission introduced Rule 17g-5 for NRSROs in an effort to promote unsolicited ratings. We propose modifying Rule 17g-5 by converting it into a mechanism for full market disclosure. This can be accomplished by taking the following steps:

- Dispense with the requirement of issuing unsolicited ratings after 10 or more "looks" at issuer data. Imposing this requirement potentially forces a new NRSRO to deploy valuable resources to provide a rating for which it will not be compensated, and for which there will be limited market interest. To date, rating agencies have avoided this forced application of resources by refraining from accessing issuer data. Removing the 10-look limit will encourage rating agencies to access issuer data, and thereby improve awareness of trends in capital formation, leading to improved methodologies and more accurate ratings.

- Open the 17g-5 mechanism to all market participants, not just NRSROs. This will increase the market's ability to compare the rating issued with the NRSRO's published rating standards.

A 17g-5 system that is modified in the ways described above will shine a light on the rating creation and selection process, at no additional cost to the Commission or to taxpayers. Most importantly, it will allow market participants to compare assigned enhancement levels against published methodologies. Any deterioration in standards – observed as deviations from published criteria – would be open for public scrutiny.

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Thank you for giving us the opportunity to provide our comments. We hope you find them useful, and that you will give them due consideration. Please call me at (212) 702-0707 with any questions that you might have or to discuss this matter further at your convenience.

Very truly yours,

James Nadler
President
Kroll Bond Rating Agency, Inc.