March 22, 2007

Ms. Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, N.E., Washington, D.C. 20549-1090

Re: Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations; Release No. 34-55231, File No. S7-04-07

Ladies and Gentlemen:

The American Securitization Forum ("ASF")[1] appreciates the opportunity to comment on the rules proposed by the Securities and Exchange Commission (the "SEC") to implement provisions of the Credit Rating Agency Reform Act of 2006 (the "Act").[2]

The comments in this letter relate to certain SEC proposed rules ("Proposed Rules") discussed in the SEC's proposing release (the "Proposing Release").[3] Specifically, the comments (i) request that certain conflicts of interest prohibited under the Proposed Rules be permitted if disclosed and adequately managed through policies and procedures, (ii) request that clarification be provided regarding the proposed prohibition on the inappropriate dissemination of pending credit rating actions, (iii) discuss the proposed requirement to disclose performance measurement statistics and the metrics used to derive the statistics, (iv) suggest that the proposed requirement that an NRSRO retain all external and internal communications relating to a credit rating is unnecessary, and (v) summarize different points of view within ASF's membership regarding ways in which the proposed anti-notching rule should be clarified and adjusted.

[1] ASF is a broadly-based professional forum through which participants in the U.S. securitization market express their common interests on important legal, regulatory and market practice issues. ASF's membership—over 330 organizations in all—includes securitization issuers, investors, financial intermediaries, rating agencies, legal and accounting firms and other market participants. Additional information about the ASF, its members and activities is available at www.americansecuritization.com.

[2] Pub. L. No. 109-291, § 3850, 120 Stat. 1327 (2006). The Act adds definitions to Section 3(a) of the Securities Exchange Act of 1934 (the "Exchange Act") and creates new Section 15E of the Exchange Act.

[3] *Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations*, Exchange Act Release No. 55231, 72 Fed. Reg. 6378 (Feb. 9, 2007) ("Proposing Release"), *also available at* http://www.sec.gov/rules/proposed/2007/34-55231.pdf.

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I. Conflicts of Interest

A. Proposed Rule 17g-5(c)(1)

Proposed Rule 17g-5(c)(1) would make it unlawful for a Nationally Recognized Statistical Rating Organization ("NRSRO") to issue or maintain a credit rating solicited by a person that, in the most recently ended fiscal year, provided the NRSRO and its affiliates with net revenue equaling or exceeding 10% of the total net revenue of the NRSRO and its affiliates for the year.

While ASF recognizes that an NRSRO would have a conflict of interest in issuing or maintaining a credit rating for a customer on which it relies for a significant portion of its net revenues, ASF also believes that the prohibition set forth in Proposed Rule 17g-5(c)(1) may make it difficult for an NRSRO that has not developed a broad customer base to conduct business. In light of the Act's goal of fostering competition in the credit rating industry[4] and its requirement that rules prescribed by the SEC be narrowly tailored, ASF believes that an NRSRO should be permitted to have such a conflict of interest if the NRSRO discloses the type of conflict of interest and implements policies and procedures to address and manage the conflict of interest.

B. Proposed Rule 17g-5(c)(2)

Proposed Rule 17g-5(c)(2) would make it unlawful for an NRSRO to issue or maintain a credit rating for a person where the NRSRO, a credit analyst who participated in determining the credit rating, or a person associated with the NRSRO 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.

While ASF agrees that Proposed Rule17g-5(c)(2) identifies relationships that could result in a conflict of interest for an NRSRO, ASF also believes that the prohibition set forth in Proposed Rule 17g-5(c)(2) would be unnecessarily broad[5] because it would prohibit some ordinary course transactions such that do not give rise to a material conflict of interest, *e.g.*, home mortgage loans entered into by a credit analyst with a financial institution that happens to be a rated person, or indirect ownership by a credit analyst of common stock of a rated person as a result of his or her mutual funds holdings. ASF respectfully requests that the SEC consider permitting an NRSRO to have such a conflict of interest if the NRSRO discloses the type of conflict of interest and implements policies and procedures to address and manage the conflict of interest.

By way of analogy, Rule 2370 of the National Association of Securities Dealers, Inc. permits associated persons of members to enter into commercial lending relationships with their customers where "the customer is a financial institution regularly engaged in the business of providing credit, financing, or loans, or other entity or person

[4] *See* preamble to the Act.

[5] Again, Section 15E(c)(2) of the Exchange Act requires that the SEC rules be narrowly tailored to meet the requirements of the Act.

that regularly arranges or extends credit in the ordinary course of business," provided the member has in place appropriate policies and procedures. ASF believes that such an approach would be appropriate for employees of NRSROs as well.

II. Policies and Procedures to Prevent Misuse of Material Nonpublic Information

Proposed Rule 17g-4(c) would require that an NRSRO establish, maintain and enforce written policies and procedures designed to prevent the inappropriate dissemination within and outside the rating organization of a pending credit rating action prior to making the action readily accessible.

Under current practice, in the context of certain nonpublic offerings of structured products, rating organizations communicate to prospective purchasers and the applicable issuer(s) the rating they expect to issue on the structured product prior to releasing the rating publicly.

ASF requests that the SEC confirm that this current practice would not be considered an "inappropriate" dissemination of material nonpublic information under Proposed Rule 17g-4(c).

III. Disclosure of Ratings Methods/Criteria

Form NRSRO would require an NRSRO or NRSRO applicant to publicly disclose in Exhibit 1 the performance measurement statistics it uses to determine credit ratings, including the metrics used to derive the statistics. The Proposing Release states that the SEC believes that such information would assist users of credit ratings in understanding how the measurements were derived and in making comparisons with the measurement statistics of other NRSROs.

ASF fully supports the SEC's proposed requirement to disclose performance measurement statistics and the metrics used to derive the statistics. In the Proposing Release, the SEC requested comments regarding whether the performance measurement statistics should use standardized inputs, time horizons and metrics to allow for greater comparability. ASF generally supports the goal of comparability that would be promoted by standardization of inputs, time horizons and metrics. However, ASF acknowledges the difficulty inherent in prescribing detailed standards given diversity among current (and, potentially future) NRSROs and their ratings methodologies, and the risk that overly prescriptive performance measurement standards could operate to inhibit that diversity and methodological independence. Accordingly, ASF believes that the goal of comparability would be adequately achieved by mandating detailed public disclosure of performance measurement statistics and the metrics used to derive the statistics.

IV. Recordkeeping

Proposed Rule 17g-2(b)(7) would require an NRSRO to retain all external and internal communications, including electronic communications, received and sent by the NRSRO and its employees relating to initiating, determining, maintaining, changing, or

withdrawing a credit rating. Proposed Rule 17g-2(c)(3) would require such communications be retained for three years. The SEC notes in the Proposing Release that the retention of written communications has played an important role in assisting the SEC in identifying legal violations and compliance issues with respect to regulated entities other than NRSROs.

While ASF understands the SEC's rationale for Proposed Rule17g-2(b)(7), we are concerned that the Proposed Rule could have a chilling effect on communications between an NRSRO and its issuers and subscribers. ASF notes that Proposed Rule 17g-2(b)(2) would require that an NRSRO retain its internal records, including non-public information and work papers, used to determine a credit rating and Proposed Rule 17g-2(c)(3) would require such internal records be retained for three years. ASF believes that the information required to be retained under Proposed Rule 17g-2(b)(2) would adequately assist the SEC with monitoring and enforcing NRSRO compliance. ASF believes that Proposed Rule 17g-2(b)(7) would involve overreaching in contravention of the Act's requirement that the rules prescribed by the SEC be narrowly tailored.[6] In this regard, issuers, and in particular foreign issuers, are very concerned about maintaining the strict confidentiality of the information they provide to NRSROs. ASF believes that the requirement to retain correspondence could have a chilling effect on the flow of information between issuers and NRSROs, ultimately to the detriment of investors.

V. **Anti-Notching Provision**

Proposed Rule 17g-6(a)(4) would make it unlawful for an NRSRO to issue or threaten to issue a lower credit rating, lower or threaten to lower an existing credit rating, withdraw an existing rating or refuse to rate securities or money market instruments issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction (collectively, a "structured product"), unless a portion of the assets within such pool or part of such transaction, as applicable, also is rated by that NRSRO. This requirement would be subject to an exception whereby the prohibition on withdrawing a rating or refusing to issue a rating would not apply if the NRSRO has rated less than 85% of the market value of the assets underlying the structured product.

A. Two Viewpoints on the Anti-Notching Prohibition

Overall ASF strongly supports the goal of promoting more effective and meaningful competition among credit rating agencies and addressing any unfair, coercive or abusive practices that may operate to inhibit that competition. However, ASF's membership was not able to reach a consensus with respect to Proposed Rule 17g-6(a)(4). ASF members have expressed a range of divergent views on this topic, which we have categorized below into two principal groups. Some ASF members believe that the Proposed Rule should only apply when an NRSRO has acted with an unfair, coercive, or abusive intent (such members, "ASF Group 1"), and some members believe that the Proposed Rule should apply regardless of intent, and that the conduct prohibited under

[6] Section 15E(c)(2) of the Exchange Act

the Proposed Rule should be per se illegal (such members, "ASF Group 2"). Each of these viewpoints is explained below.[7] No priority or preference is intended in presenting the two competing views set forth in this letter, and each view is entitled to equal consideration and deference.

1. Intent-Based Application of the Anti-Notching Prohibition

ASF Group 1 believes that, although not explicitly stated in the Proposed Rule, the prohibitions of the Proposed Rule should apply only to situations in which an NRSRO has acted with an intent to coerce an issuer to use such NRSRO's services or to inhibit competition. ASF Group 1 is concerned that unless the Proposed Rule is modified to incorporate a scienter requirement, there may be circumstances in which one NRSRO may be required to rely upon ratings assigned by one or more other NRSROs, even if there is a legitimate basis for conducting independent analysis that may produce a different credit opinion. Members of ASF Group 1 believe that any such requirement would fundamentally undermine the ability of NRSROs to formulate and express independent credit opinions and would, at least in some circumstances, force credit ratings convergence where a diversity of opinions may exist.

ASF Group 1 believes that the goal of Section 15E(i)(1) of the Exchange Act, namely, to prevent abusive, coercive, or unfair practices, requires the SEC to adopt an intent-based standard, to avoid regulatory interference in ratings methodologies and the substance of ratings opinions. ASF Group 1 requests that the SEC clarify that, absent an intent to engage in an unfair, coercive, or abusive practice, an NRSRO would not be prevented from issuing or communicating an intent to issue a lower credit rating, lowering or communicating an intent to lower an existing credit rating, withdrawing an existing rating or refusing to rate a structured product, regardless of whether the NRSRO has rated at least 85% of the underlying assets. ASF Group 1 believes that such a clarification would be in accordance with the Act's requirement that the SEC issue rules to prohibit any act or practice relating to the issuance of credit ratings by an NRSRO that the SEC determines to be unfair, coercive, or abusive,[8] while also complying with the Act's prohibition against regulating the substance of credit ratings or the procedures and methodologies by which an NRSRO determines credits ratings.[9]

ASF Group 1 recognizes that, as with any scienter-based rule, establishing whether or not the requisite intent exists would be difficult, and would be based on the totality of facts and circumstances associated with an NRSRO's credit rating business practices. As a result, ASF Group 1 believes that if the Proposed Rule is clarified as

[7] ASF always seeks to identify and present a membership-wide consensus on significant regulatory policy issues affecting the securitization market. However, our membership is large and diverse, and those policy issues—as in the present case—are often complex. In situations where, despite our best efforts, a single consensus position cannot be established, ASF seeks to present the principal competing viewpoints within its membership, and the underlying arguments and rationale for each position.

[8] *See* Section 15E(i)(1) of the Exchange Act.

[9] *See* Section 15E(c)(2) of the Exchange Act.

described above, an NRSRO could nonetheless feel obligated to rate a structured product when the NRSRO has rated at least 85% (but less than all) of the underlying assets but has valid reasons (*i.e.*, reasons which are not based on an unfair, coercive, or abusive intent) for not rating the structured product (*e.g.*, if the NRSRO has made a good faith judgment that the nature the underlying assets that it has not rated makes rating the structured product inappropriate). Further, this same concern would exist where an NRSRO has not rated all of the underlying assets, but believes that a lower credit rating than that assigned by another NRSRO is appropriate.

ASF Group 1 therefore requests that the SEC further clarify the Proposed Rule to state that an NRSRO could establish a rebuttable presumption of compliance with the Proposed Rule's requirements if the NRSRO, based on the application of its established, quantitative and/or qualitative credit rating models and analytic methods, in good faith determines that it should issue or communicate an intent to issue a lower credit rating, lower or communicate an intent to lower an existing credit rating, refuse to rate or withdraw a rating in accordance with established policies and procedures for making such determinations, regardless of whether the NRSRO has rated at least 85% of the underlying assets.

ASF Group 1 believes that a number of interpretive issues would arise should the Proposed Rules not be clarified as suggested above. The Proposed Rule does not clearly provide that an NRSRO may subject assets underlying a structured product that it has previously not rated to a credit rating process without running afoul of the prohibition related to unsolicited credit ratings contained in Proposed Rule 17g-6(a)(5), especially if the NRSRO were to seek compensation for undertaking that process. Without clarification, the Proposed Rule may also lead an NRSRO to rely, without further analysis, on the ratings of another NRSRO with respect to the underlying assets it has not rated (in cases in which such underlying assets have been rated by another NRSRO) in rendering its credit rating on the structured product. At the extreme, the Proposed Rule could be interpreted to require an NRSRO to rate a structured product, even where up to 15% of the underlying assets are unrated by *any* NRSRO. ASF Group 1 is concerned that these circumstances would undermine competition among rating agencies and may not be consistent with the protection of investors, as each NRSRO's ratings would not represent a completely independent view of the credit, but instead would be the result of analysis that overlapped with analysis conducted by another NRSRO.

2. Non-Intent Based Application of the Anti-Notching Prohibition

ASF Group 2 believes that the conduct prohibited under Proposed Rule 17g-6(a)(5) should not incorporate a scienter standard.

ASF Group 2 believes that imposing a scienter requirement would be inconsistent with the Congressional mandate under Section 15E(i)(1) of the Exchange Act, and difficult to enforce in practice. Section 15E(i)(1) requires the SEC to prohibit any act or practice relating to the issuance of credit ratings by an NRSRO that the SEC determines to be unfair, coercive, or abusive, and does not limit the scope of the prohibition to situations in which an NRSRO has an unfair, coercive, or abusive intent.

The Proposing Release notes the SEC's understanding that several of the existing NRSROs have procedures under which they will undertake to issue a credit rating for a structured product where they have rated approximately 80% to 90% of the market value of the underlying assets.[10] ASF Group 2 believes that the 85% exception set forth in the Proposed Rule is consistent with the Act's objective of increasing competition in the credit ratings industry, but does not go far enough in prohibiting unfair, coercive or abusive conduct, or in altering the status quo. ASF Group 2 believes that it would be contrary to the spirit and intent of the Act for the SEC to implement a rule that permits NRSROs to refuse to rate or withdraw a rating on a structured product based on a subjective, intent-based standard.

ASF Group 2 believes that the Proposed Rule should be clarified to eliminate the proposed threshold 85% exception or, in the alternative, to state that if an NRSRO has rated at least 85% of the assets underlying a structured product, it cannot refuse to rate the structured product, and cannot systematically lower, or "notch" the ratings that other NRSROs have assigned to assets underlying the structured product, or use other direct or indirect means to require issuers of securities included in structured products to obtain their ratings. Some members of ASF Group 2 believe that if a percentage threshold exception is retained, that threshold should be lower—for example, 66%. In rating the structured product, the NRSRO would be required to recognize ratings assigned by other NRSROs, and, if it is so desired, rely on appropriate disclaimers.

To the extent that two NRSROs have rated such remaining underlying assets, ASF Group 2 believes that the NRSRO rating the structured product should be required to use the lower of the two ratings for purposes of rating the structured product. If three or more NRSROs have rated the underlying assets, the NRSRO rating the structured product should be required to use the average of such ratings. To the extent that no other NRSRO has rated such remaining underlying assets, ASF Group 2 believes that the NRSRO rating the structured product should be required to rate or otherwise assess such remaining underlying assets in accordance with its established policies and procedures without unreasonable delay.

ASF Group 2 believes that clarifying the Proposed Rule so that it may be consistently applied in this manner would avoid the uncertainties associated with an intent-based standard. While acknowledging that such a clarification could, to a limited degree, create increased reliance on disclaimers, or partial reliance on ratings of other NRSROs, ASF Group 2 believes that the clarification described above is necessary to promote competition among NRSROs. As the Proposing Release notes, currently two NRSROs represent over 80% of the credit rating industry market share as measured by revenues.[11]

Members of ASF Group 2 acknowledge some diversity of opinion among NRSROs regarding ratings of structured products and their underlying assets. However,

[10] *See* Proposing Release fn. 278, 72 Fed. Reg. at 6403.

[11] *See* Proposing Release fn. 9, 72 Fed. Reg. at 6379.

they believe historical evidence suggests that those ratings are comparable. More importantly, they believe the policy goal of facilitating competition within an industry where two NRSROs currently enjoy a dominant market share outweighs the countervailing policy goal of preserving full independence of ratings opinions in all circumstances. ASF Group 2's suggested clarification is designed to prevent dominant NRSROs from further reinforcing their market dominance by, in the circumstances described above, prohibiting them from effectively forcing structured product issuers to permit them to rate the relatively few underlying assets that they have not already rated.

ASF Group 2 believes that its suggested clarification to the Proposed Rule is an essential refinement to the 85% exception formulated by the SEC that would be in accordance with the Act's mandate that the SEC prohibit unfair, coercive, or abusive acts or practices. It would prevent an NRSRO that has rated a specified percentage threshold percentage of a structured product's underlying assets from (i) refusing to rate, or withdrawing its rating on, a structured product, (ii) notching ratings assigned to underlying assets by other NRSROs as a condition of rating the structured product, or (iii) insisting on rating the remaining underlying assets rated by another NRSRO as a condition of rating the structured product.

ASF Group 2 notes that instances in which an NRSRO rating is based partially upon ratings of one or more other NRSROs, the extent of any such reliance should be disclosed in the offering documents for structured product offerings.

B. Other Comments on the Anti-Notching Provision

ASF also believes that the following clarification and adjustment to Proposed Rule 17g-6(a)(4) is necessary to help enable NRSROs to comply with the Proposed Rule requirements.

1. Clarification of Proposed Rule 17g-6(a)(4)'s Prohibition on Issuing or Threatening to Issue a "Lower" Credit Rating

ASF notes that Proposed Rule 17g-6(a)(4)'s prohibition on issuing or threatening to issue a lower credit rating does not provide guidance on the standard against which such rating should be compared to determine whether the rating is "lower." As proposed, "lower" may be interpreted alternatively with reference to the rating assigned by another NRSRO, or to the rating that an NRSRO would have assigned, had it actually issued ratings for assets not rated by it. ASF requests that clarification be provided regarding this aspect of the Proposed Rule as well.

2. Use of Par Value Instead of Market Value to Determine 85% Threshold

As written, the 85% exception is based on the market value of the assets underlying the structured product. Market value is constantly fluctuating and may be difficult for the NRSROs to determine as of a particular point in time. ASF therefore recommends that the SEC to base the 85% exception on the par value of the underlying assets, rather than on the market value.

Further, even if par value is used for purposes of establishing a percentage threshold for rated assets, ASF urges the SEC to clarify that this value, and the corresponding portions of rated versus unrated assets, be measured only at the time that a credit rating is initially solicited from an NRSRO. The composition of assets underlying a structured product may change over time, as a result of routine amortization of those assets and substitution of collateral pursuant to contractual terms of the transaction. ASF believes that it would be unduly burdensome for NRSROs, issuers, investors and other parties to be required to monitor dynamic changes to the composition of structured product asset pools over time for purposes of determining the validity of ratings actions that depend upon the availability of this exemption.

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ASF thanks the SEC for this opportunity to comment on the Proposed Rules. If you have any questions concerning these comments, or would like to discuss these comments further, please feel free to contact the undersigned at 646.637.9216 (telephone), or at gmiller@americansecuritization.com (e-mail).

Sincerely,

George P. Miller
Executive Director