Moody's Investors Service

7 World Trade Center at 250 Greenwich Street
New York, New York 10007

July 28, 2008

By Electronic Mail

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

Re: Proposed Rules for Nationally Recognized Statistical Rating Organizations (Release No. 34-57967; File No. S7-13-08) ("Proposing Release")

Dear Ms Harmon:

Moody's Investors Service ("**MIS**") appreciates the opportunity to provide comments to the Securities and Exchange Commission ("**Commission**") on the proposed amendments ("**Proposed Amendments**") to rules ("**Existing Rules**") implementing the Credit Rating Agency Reform Act of 2006 ("**Rating Agency Act**"). We support the broad objectives of the Rating Agency Act to foster accountability, competition and transparency in the credit rating agency ("**CRA**") industry and recognize the efforts undertaken by the Commission through this rule-making initiative to enhance confidence in the credit rating process.

MIS does not object in principle to the majority of the Proposed Amendments. There are, however, two proposed changes that we believe require substantial modification. First, proposed paragraph (a)(3) of Rule 17g-5 is intended to address rating shopping, where issuers of structured finance products can shop for the highest rating among CRAs. While we support the objective underlying the Commission's proposal, we believe that the mechanism chosen to address the Commission's concern is inappropriate. Proposed paragraph (a)(3) attempts to deal with rating shopping by making nationally recognized statistical rating organizations ("**NRSROs**") the linchpin of a new disclosure regime for structured finance transactions. A simpler way to address this concern would be for the Commission to specifically identify what constitutes appropriate information to meet market participants' needs and then revise the disclosure regime for structured finance issuers set out in Regulation AB, Rule 144A and other rules adopted the Securities Act of 1933 ("**Securities Act**") and Securities Exchange Act of 1934 ("**Exchange Act**"). Instead, the proposed rule unintentionally miscasts NRSROs as creators and enforcers of disclosure requirements in structured finance markets and thereby conflicts with the Commission's intention to reduce market participants' over-reliance on credit ratings and CRAs.

Second, it is unclear whether the requirement in proposed paragraph (d) of Rule 17g-2 that NRSROs make a machine-readable, electronic data file containing the rating history of each NRSRO's current ratings "publicly available" means that this file must be made freely accessible. We support the Commission's effort to enhance overall transparency and market participants' ability to compare rating performance across NRSROs. We believe, however, that this purpose can be achieved by permitting NRSROs to make the data available on a subscription basis. Requiring NRSROs to make the data freely accessible would unnecessarily force NRSROs to forego an important source of revenue while increasing their costs. Moreover, this requirement could be interpreted as reflecting a Commission policy preference for the issuer-pays model over the subscription-model to the extent that rating histories are or might become an important source of revenue under a subscription model.

In our Comment Letter below, we have set out a detailed discussion of these issues and our recommended revisions to these Proposed Amendments. In Annex A, we address important matters of a more technical nature. Among other things, we request in part 11 of Annex A that the Commission clarify that the final rules will apply on a prospective basis only. In Annex B, we respond to the substantive questions posed by the Commission that we do not otherwise address in the main text of our letter or Annex A. In Annex C, we discuss the costs associated with the Proposed Amendments. Please note that, while we have carefully considered all of the questions posed by the Commission in the Proposing Release, we have responded only to those questions that we believe we are well-positioned to address.

I. PROPOSED RULE 17G-5(a)(3): DISCLOSURE IN STRUCTURED FINANCE MARKETS

A. Summary of MIS's Response

MIS recognizes that rating shopping, in structured finance as well as other credit markets, is a harmful practice engaged in by issuers, underwriters and/or subscribers that can exacerbate the potential conflicts that CRAs face as a result of being paid to provide credit ratings. Accordingly, we do not object to disclosing the conflict that can be exacerbated by rating shopping and adopting measures to mitigate this conflict.

We also agree with the Commission that more extensive disclosure by issuers, and wider dissemination by them, of information relating to structured finance products may mitigate to some extent the adverse effects of rating shopping, *e.g.* by enabling investors to form their own opinions and facilitating unsolicited ratings. We strongly believe, however, that NRSROs should not be made the linchpin of any disclosure regime. Instead, the emphasis should be, as it is for other types of securities, on having the party wishing to access U.S. securities markets assume responsibility for disseminating all information that is material to investment decisions, regardless of whether or not it has been "provided to" or "used by" an NRSRO.

Consequently, we believe that paragraph (a)(3) overreaches the Commission's authority under the Rating Agency Act because it goes far beyond requiring NRSROs to disclose and manage a conflict of interest. It creates an entirely new disclosure regime for entities other than NRSROs, such as issuers and underwriters, and exposes NRSROs to substantial liability for the conduct of third parties, which NRSROs cannot and should not control. Furthermore, it miscasts NRSROs as creators and enforcers of disclosure requirements in structured finance markets. Moreover, the proposed rule presumes that all CRAs follow the same analytical approach and require the same information so that the information requested by one NRSRO is sufficient to meet the needs of any other CRA. We disagree with this premise.

Furthermore, while we cannot predict with certainty how the proposed rule will affect market participants' behavior, we believe that two scenarios are possible. First, the difficulties associated with determining whether an NRSRO has "used" information could result in NRSROs deeming all information provided to them to have been "used". This could lead to a disclosure regime characterized by "data dumping". An alternative (and more likely scenario) is that paragraph (a)(3) will have a chilling effect on issuers[1], reducing their willingness to provide information to NRSROs and encouraging them to "shop" for the CRA that will ask for the least amount of information. This could make it harder for other CRAs to assign unsolicited ratings. It is even possible that issuers will avoid having to disclose information provided to NRSROs by choosing not to obtain ratings for structured finance transactions. This could decrease transparency in structured finance markets and may affect adversely their depth and liquidity.

Finally, we believe that paragraph (a)(3) imposes unprecedented, harsh and unnecessary conditions upon NRSROs' freedom of speech.

We recommend instead that the burden of any new disclosure requirements fall upon issuers, who control or own most of the relevant information and are also the principal beneficiaries of access to U.S. securities markets. Any new disclosure regime should ensure that sufficient, relevant information is conveyed to all market participants and observers, including investors and other CRAs (regardless of whether they are registered as NRSROs), instead of inundating the market with volumes of information lacking the context and analysis otherwise found in mandated disclosures. The Commission should carefully determine and specifically identify what constitutes appropriate information to meet market participants' needs, instead of equating "materiality" and "relevance" with what an NRSRO "uses" in the rating process. Accordingly, we recommend that the Commission strike proposed paragraph (a)(3) and, instead, focus on revising the existing disclosure regime for structured finance issuers contained in Regulation AB, Rule 144A and other applicable rules.

If the Commission nevertheless decides to adopt a rule comparable to paragraph (3)(a), we urge the Commission to include a safe harbor for NRSROs that obtain representations from the participants in a rated offering stating that such participants have made or will make the required disclosure.

B. Detailed Analysis

1. Proposed Rule Not Narrowly Tailored

As indicated above, MIS agrees that rating shopping is a harmful practice engaged in by issuers, underwriters and/or subscribers that can exacerbate the potential conflicts that CRAs face as a result of being paid (by issuers or subscribers) to provide credit ratings. Accordingly, we do not object in principle to proposed paragraph (b)(9) of Rule 17g-5.[2] We believe, however, that proposed paragraph (a)(3) goes far beyond what Congress intended when it authorized the

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[1] To streamline our discussion in this Comment Letter, unless otherwise indicated, we use the term "issuer" to refer collectively to the originator and sponsor of structured finance products, as well as the special purpose vehicle ("**SPV**") to which the assets to be securitized are transferred and which issues the structured securities.

[2] However, as we discuss in more detail in part 10 of Annex A concerning proposed Rule 17g-7, we believe that the definition of structured finance transactions used in proposed Rules 17g-7 and 17g-5(b)(9) is insufficiently precise and that the Commission should provide clearer guidance as to which securities and instruments fall within the definition's scope.

Commission to adopt rules that are narrowly tailored to achieve the purpose of requiring NRSROs to disclose and manage conflicts of interest. Specifically, paragraph (a)(3) will create an entirely new disclosure regime for entities other than NRSROs, such as issuers, who will be required to disclose large volumes of information to the market solely because they have provided such information to an issuer-paid NRSRO as part of the credit rating process. We believe that any rules adopted by the Commission under the Rating Agency Act should address only the conduct of NRSROs (and applicants for NRSRO status).

If the Commission decides that more information about the assets or risks underlying structured finance products should be disseminated, it should determine in consultation with the structured finance industry and investors through the comment process which categories of information are material and relevant to the investment decision-making process and amend Regulation AB, Regulation 144A and other applicable rules as appropriate to require issuers to disclose such information. We believe this approach will be more effective at ensuring complete and accurate dissemination of the necessary information to investors and CRAs.

2. Proposed Rule Would Exacerbate Over-Reliance on NRSROs

MIS believes that paragraph (a)(3) is fundamentally inconsistent with the Commission's stated goal to reduce regulators' and market participants' over-reliance on credit ratings and NRSROs.[3] This is because paragraph (a)(3), if adopted, will establish NRSROs as creators and enforcers of disclosure requirements in structured finance markets.

Historically, issuers and a limited number of other participants in offerings, such as underwriters, have been responsible for making complete and accurate disclosures to investors about the securities being offered according to standards that focus on the information's materiality and relevance to the investment decision-making process. Specific disclosure items are otherwise based on disclosure rules adopted under the Securities Act and/or Exchange Act. If the Commission adopts paragraph (a)(3), it will, in effect, delegate to NRSROs the authority to define disclosure requirements for structured finance offerings, based on the information that NRSROs decide in their discretion to use in determining a credit rating. Ultimately, NRSROs, rather than the Commission, will determine what investors need to know and for which information issuers and underwriters can be held liable. NRSROs also will be required to enforce these disclosure requirements by withholding credit ratings unless the prescribed information is disseminated.

Encouraging market participants to rely upon NRSROs in this way is particularly inappropriate because credit ratings address just one characteristic of debt securities – their creditworthiness. Credit ratings do not take into consideration other factors such as market prices, liquidity, or an investor's investment objectives and risk parameters. We believe that proposed paragraph (a)(3) would contribute to the misperception that the information that NRSROs use in the credit rating process is sufficient for investment decision-making.

Proposed paragraph (a)(3) also incorrectly presumes that the information requested by one NRSRO is sufficient to meet the requirements of any other CRA. Credit ratings cannot be commoditized in this fashion. Different CRAs use different methodologies, ask for different types and amounts of information and carry out their rating analysis with varying degrees of

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[3] See, *e.g.* Christopher Cox, "Statement on Proposal to Increase Investor Protection by Reducing Reliance on Credit Ratings", June 25, 2008, available at www.sec.gov.

vigor. By contrast, proposed paragraph (a)(3) contributes to the misperception that one NRSRO is equivalent to another. In so doing, the proposed rule could discourage investors from carefully considering whether the information conveyed by a particular NRSRO's credit ratings is, in fact, useful for the investor's purposes.

3. Disclosure Regime May Lead to "Data Dumping"

Proposed paragraph (a)(3) also raises concerns about the unintended consequences of using a hard-to-apply disclosure standard focusing on the NRSRO's "use" of information to determine ratings or conduct surveillance. How will an NRSRO determine whether it has "used" information that it has received? For example, will any review by an NRSRO analyst of information constitute "use"? We believe that, in practice, the difficulties (and related liability risk) associated with determining "use" on a case-by-case basis will result in NRSROs deeming all information provided to them to have been "used". This could lead to a disclosure regime characterized by "data dumping", in stark contrast to the orderly and methodological presentation of relevant information required elsewhere under the securities laws. Accordingly, we recommend that, regardless of who is ultimately responsible for such disclosure, the Commission should specify precisely which categories of information should be disclosed instead of relying on the overly broad and vague standard of "used by an NRSRO".

4. Disclosure Regime Could Have a Chilling Effect

As we discuss in more detail in this section, a more likely, alternative scenario is that paragraph (a)(3) will discourage issuers from providing information to NRSROs and encourage them to shop for the CRA that will demand the least information. Presently, an MIS analyst can request, and typically receives, whatever information the analyst believes could be helpful in the analytical process. Depending on the asset class, much of the requested data goes beyond the specific line item requirements of Regulation AB. MIS analysts may also ask to speak to or meet with various individuals, including senior executives of issuers and arrangers, and may receive information through oral communications and/or onsite visits. Furthermore, some of the information that we receive from issuers and other participants in the structured finance transaction will have been provided to them by other parties.

The Proposing Release indicates that, in registered offerings, issuers will be subject to strict liability, and underwriters will have customary liability, under the Securities Act for any information that is required to be made public under paragraph (a)(3). Despite this, neither the issuer nor the underwriter will have control over the information provided to the NRSRO by sponsors, depositors or trustees. Also, they might not be able to obtain consents to disclose publicly certain kinds of information (such as legal opinions about the transaction structure or data subject to privacy laws) that historically they may have provided to the NRSRO, or they may be unwilling to assume any liability risk for such information. Therefore, issuers and underwriters could opt to refrain from providing any information to NRSROs that does not have to be disclosed under Regulation AB. They also might seek to discourage sponsors, depositors and trustees from providing non-public information to NRSROs. This could result in NRSROs providing less well-informed credit ratings.

Where an issuer subject to the Exchange Act's reporting requirements conducts a private or offshore offering, it is unclear what liability will attach to it under the Exchange Act for information required to be disclosed under proposed paragraph (a)(3) by persons other than the issuer. Even if the Commission clarifies that such information can be furnished rather than filed

on Form 8-K in such instances, so that the issuer will not be subject to liability under Section 18 of the Exchange Act, the issuer ordinarily would be liable under Rule 10b-5 for information so furnished and made public. We expect that exposure to such liability will have a chilling effect on issuers' willingness to provide information to NRSROs.

The potentially adverse consequences of adopting paragraph (a)(3) cannot be overstated. First, the rule could lead to less well-informed and more volatile credit ratings because of the chilling effect noted above. Second, the rule is likely to encourage many issuers and underwriters to shop for the CRA that will demand the least information, thereby undermining the Commission's goal of facilitating unsolicited ratings through the dissemination of more information. Third, the rule could lead to issuers raising less capital through structured finance transactions, which could have adverse consequences for the liquidity and depth of capital markets for structured finance securities. This in turn could adversely affect the broader economy, *e.g.* by reducing the availability of mortgage financing. Fourth, some issuers that proceed with structured finance transactions may do so through unrated, private placements, particularly in buoyant markets with high transaction volumes, when investors often focus on deal speed and are willing to make decisions based on less information. While, ultimately, it is up to investors to decide whether or not to insist upon receiving information (including credit rating opinions) about securities, the likely net result of proposed paragraph (a)(3) will be less, not more, transparency in public and private structured finance markets.

5. Consequences for Private and Offshore Offerings

While certain private and offshore offerings undertaken by issuers currently are exempt from requirements to publicly disseminate information in the United States, proposed paragraph (a)(3) will require such issuers of rated structured finance securities to disseminate a significant amount of information. We believe that such a requirement could significantly reduce their willingness to issue rated securities.

The consequences of the proposed amendment on offshore offerings under Regulation S are particularly problematic. If implemented, paragraph (a)(3) will require dissemination of information for securities sold pursuant to Regulation S even where investors are located outside the United States and the issuer and underwriters are required to comply with the securities laws of their local jurisdictions and the jurisdictions where such offerings are made. Such a broad disclosure requirement might also conflict with the foreign securities laws or other laws (such as privacy laws) applicable to such transactions.

6. NRSROs Should Not Be Liable for Conduct beyond Their Control

MIS is also particularly concerned that NRSROs will be subject to penalties or sanctions for actions taken, or not taken, by issuers and other participants in structured finance transactions since NRSROs cannot control third parties' behavior. The Commission has suggested that NRSROs can obtain representations that the required information is being disclosed. The proposed rule, however, does not provide a safe harbor for NRSROs that obtain and rely in good faith upon such representations. While breach of a representation could give rise to a right of action in contract law against the provider of the representation, NRSROs could still face regulatory sanctions for a breach of the proposed rule.[4] Given that MIS monitors over 100,000

[4] Furthermore, the provider of the representation and warranty likely will be the SPV, since this is the entity with which the NRSRO has the rating relationship. Bringing an action in contract law against the SPV likely would

structured finance ratings, paragraph (a)(3) could impose an unprecedented and excessively burdensome obligation on us to monitor third parties' disclosures and litigate breaches of contract. We believe that NRSROs should not be subject to liability, especially regulatory sanctions, for the conduct of third parties since NRSROs cannot control such parties' behavior. We also believe that issuers, who control and/or own most of the relevant information and who benefit from access to U.S. securities markets, should bear responsibility for making any required disclosures and that it is the Commission's responsibility to set and enforce the appropriate disclosure standards.

7. Condition on Speech

MIS believes that the proposed disclosure regime set out in paragraph (a)(3) will impose unprecedented conditions on NRSROs' freedom of speech and effectively prohibit the publication of rating opinions unless third parties such as issuers and underwriters, which are outside the NRSROs' control, or the NRSROs themselves disseminate information in accordance with a broad and vaguely worded standard according to a prescribed timetable. In short, an NRSRO must relinquish its right to decide what, and when, to publish; otherwise, it will be in breach of the securities laws and subject to sanctions, with no safe harbor. These restraints would not, and could not, be imposed on a publisher of opinions in any other context.[5]

The costs of NRSRO registration, which are already significant, should not include this extraordinary condition on speech. The proposed restraint on an NRSRO's right to publish its opinion seems especially harsh and unwarranted because the Commission could achieve the same objective by imposing additional disclosure requirements directly upon issuers, to whom the information belongs in the first place and that are already subject to disclosure requirements under the securities laws. Moreover, it is significant that these restraints will apply only to NRSROs, while other CRAs will remain free to publish opinions regardless of whether or not the information they receive from issuers as part of the structured finance rating process is ultimately disclosed. By impeding NRSROs' core function in the market through restraints on their freedom to express opinions when they wish to do so, the Commission may discourage CRAs from becoming NRSROs. This outcome seems likely given that the proposed rule may create incentives for issuers to seek ratings from non-NRSRO CRAs, so that issuers can avoid the disclosure requirements arising under proposed paragraph (a)(3).

II. XBRL RATING ACTIONS DATABASE

A. Summary of MIS's Response

MIS does not object to a rule requiring NRSROs to make, retain and provide access to a data file containing the rating histories of their currently outstanding credit ratings. We do, however, have several concerns about the Commission's proposed rules and the questions it has posed for comment. First, it is unclear whether the proposed requirement that NRSROs make this data file "publicly available" means that the file must be freely accessible. If this is true, we

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be fruitless and, to the extent it was not fruitless, it likely would harm the SPV (and thereby, indirectly, the investors in the SPV's securities). Such an action also could result in rating downgrades.

[5] We note that, in the past, the Commission has acknowledged the similarity between the mission of CRAs and that of the media. See *Release Adopting Rules for Selective Disclosure and Insider Trading*, Securities Act Release No. 7881 (August 15, 2000) at II.B.1.a.

believe that the proposed rules do not sufficiently protect the revenues that NRSROs may derive from subscriptions to rating history databases. We believe that the Commission's objectives could be met by permitting NRSROs to make the required data file available on a subscription basis. Also, we would not object to a requirement to provide free access to this data file upon request by authorities and regulators for purposes such as the production and publication of independent research.

Second, while we have begun to identify and evaluate the potential advantages and disadvantages of providing the data in a format that is different from the manner in which we already make rating history data available, we have not had sufficient time to fully assess the incremental costs and benefits of the proposed rule. Consequently, we cannot express support now for proposed paragraph 17g-2(d) and would appreciate an opportunity to provide further feedback to the Commission when we complete our evaluation. We are willing, however, to explore with other NRSROs, users of our credit ratings and the Commission the potential advantages and disadvantages of creating and maintaining a structured, electronic data file that uses a common mark-up language such as XML or XBRL and an industry-agreed taxonomy and tags for the data. Also, if the Commission ultimately decides to require NRSROs to use a common mark-up language and taxonomy for these records, the taxonomy should not be permitted to impinge upon the meaning of the data, *e.g.* by imposing a universal definition on data that have different meanings for different NRSROs. The taxonomy and data tags should be developed by the NRSROs for approval by the Commission.

Third, since the proposed rules are intended to foster accountability and facilitate comparative analyses of NRSROs' ratings performance, then there is no need for continuous database updates. We believe that semi-annual updating would be sufficient.

B. Detailed Analysis

1. Proposed Rules Unnecessarily Require NRSROs to Forego Revenues

We do not object to a rule requiring NRSROs to make publicly available a data file containing the rating histories of their outstanding ratings. We agree that public disclosure of ratings performance over time is an important part of the NRSRO oversight framework. We already publish and make freely available various statistical ratings performance reports, a number of which are incorporated by reference into our Form NRSRO.[6] We also make our credit rating actions on public debt obligations and public debt issuers available to the public without cost. Furthermore, we continue to invest significant resources in developing and maintaining data products and analytical tools that leverage off our historical rating databases. While fees paid by issuers for ratings constitute the primary source of revenues for MIS's parent company Moody's Corporation ("**MCO**"), it also derives substantial revenue through subscription products. (The expected revenues derived from the subscriptions for ratings data may play an even larger role in the business models of some other NRSROs.)

We believe that it is unnecessary to require NRSROs to make this data available for free, even on a time-delayed basis. Historical rating information is valuable and many CRAs make it available on a subscription basis. While third parties already can track MIS's rating actions and construct historical rating databases, it is time-consuming and costly to do so. Accordingly, requiring NRSROs to invest significant resources to compile and maintain this data without

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[6] See, e.g. *Guide to Moody's Default Research: March 2008 Update* (Document #108157).

permitting them to derive value from their efforts is unreasonable. Our concerns will be exacerbated if we are required to include the entire ratings history for our current ratings, since this history extends back to the 1920s for some ratings.

Moreover, we believe that the Commission's proposal could be perceived as favoring the issuer-pays model over the subscription-based model. This implied policy preference could adversely affect NRSROs, such as MIS, that operate primarily under the issuer-pay model but seek to diversify their revenue sources by providing data on a subscription basis. That outcome seems at odds with other Commission proposals intended to increase competition in the CRA industry and reduce the influence of issuers on NRSROs that operate primarily under the issuer-pays model. Therefore, we suggest that NRSROs be permitted to provide the required data on a subscription basis. We would not object if NRSROs were required to make the data available for free to authorities and regulators upon request for purposes such as the production of independent research.

2. Insufficient Time to Assess Whether XBRL Is the Appropriate Standard

We acknowledge that there may be benefits associated with having NRSROs create and maintain rating history data files in a machine-readable electronic format. We also believe it is worth exploring the potential utility of an XML-type standard (including but not limited to XBRL), since XML is an open standard that is flexible and extensible. We believe that flexibility and extensibility are particularly important features that would enable us to convey more effectively any unique meanings associated with our data that are not captured by the industry-agreed tags. Finally, we recognize the value of presenting the data in an organized format, since this could enhance the usability of the data (particularly in automated applications). However, we do not have sufficient information and have not had enough time to evaluate fully the potential, incremental advantages and disadvantages (including costs) of providing the data in a format that is different from the format we already use to make rating history data available. Therefore, we cannot provide a definitive view on proposed paragraph 17g-2(d). We are, however, willing to explore with others the proposal's potential advantages and disadvantages.

3. NRSROs Should Take the Lead in Developing the Taxonomy and Tags

If the Commission decides to proceed with this proposal, we recommend that NRSROs collectively take the lead in creating any taxonomy and tags that are needed for whatever format is adopted, subject to Commission approval of the industry-agreed tags. This approach would take advantage of the NRSROs' understanding of their own data. We also believe that it would reduce the risk that the process of defining a taxonomy and tags for common use in the CRA industry could inadvertently restrict or change the meaning of the data, *e.g.* by inappropriately imposing common definitions of terms that different NRSROs define differently.[7]

4. Recommended Data Fields

MIS believes that the following data fields are appropriate:

- Unique, NRSRO-defined identifier for each issuer in the data

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[7] For example, the meanings of ratings differ across CRAs. MIS's credit ratings express an opinion about "loss given default", *i.e.* they reflect our view on both the probability of default and financial loss suffered in the event of default. Some other CRAs' credit ratings speak only to probability of default.

- Unique, NRSRO-defined identifier for each obligation in the data
- International Securities Identifying Number ("**ISIN**") for each obligation in the data (if available without cost to the NRSRO)[8]
- Credit rating date
- Credit rating
- Type of rating/rating scale
- Watchlist (*i.e.* whether rating is on a watchlist for upgrade or downgrade)
- Watchlist date
- Outlook (*i.e.* whether the medium-term outlook for the rating is positive, negative, stable or developing)
- Outlook date
- Rating expiration date

5. Update Frequency

According to the proposed rule, NRSROs will have to incorporate into the data file all credit rating actions within six months after the date the rating action is taken. Given the global nature of our business, we take rating actions every day. Consequently, the proposed language in the rule seems to indicate that MIS would have to update the required data file as a whole every day, on a rolling basis, to reflect any rating actions that were taken six months earlier. This daily updating process would be costly.

The rule is intended to foster accountability and facilitate comparative analyses of NRSROs' ratings performance, which can only be measured over time. We believe that semi-annual (instead of daily) updates should be sufficient to achieve the rule's intended purpose. We also recommend that the rule provide for a delay (*e.g.* three months) between the cut-off date for the actions to be included in the data file and the date the data file must be updated.

6. A Voluntary Pilot Program Could Lead to a Two-Tiered System

If the Commission proceeds with a voluntary pilot program, the volunteers could incur significant costs to develop the tags and prepare their data, while facing the risk that the Commission will delay implementation, decide not to adopt the rule or exempt smaller NRSROs from compliance with it. Our concerns would be exacerbated if the Commission expected the volunteers to make the interactive data file available for free. In our view, a pilot program could lead to a two-tiered registration system for NRSROs, to which we would strenuously object. If the Commission decides to proceed with this initiative, we believe that all NRSROs should start complying with the reporting requirements at the same time. An industry-wide test phase could be implemented through a moratorium on enforcement action for a specified period.

7. Data File Should Reside on Each NRSRO's Website with Access Facilitated through Industry Portal

We are concerned that if the data file is stored on a Commission-established database such as EDGAR, users of the data might mistakenly conclude that the information contained in the NRSROs' data files is comparable in nature to EDGAR filings. In essence, EDGAR filers such as registered, public companies attest to the truth of the information they file through

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8 This recommendation is discussed in more detail in our response to Question D in part 1 of Annex B.

EDGAR. By contrast, NRSROs' credit ratings constitute opinions, not statements of fact, about relative future creditworthiness of entities and obligations.

Accordingly, we recommend that each NRSRO maintain the data file on its own website. To facilitate easier access to this data, an NRSRO industry portal for performance statistics and data could be established. People seeking such information about different NRSROs could navigate to the portal, from where they could click on links that would take them directly to the relevant webpage of the NRSRO. Each NRSRO could still condition access to certain web pages by requiring a person to register, accept the associated terms and conditions[9] and, as appropriate, subscribe for the relevant data product or service.

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Once again, we appreciate the opportunity to comment on the Proposed Amendments. We would be pleased to discuss our comments further with the Commission or its staff.

Sincerely,

Michel Madelain
Chief Operating Officer
Moody's Investors Service

[9] MIS makes a variety of information publicly available for free on Moodys.com, subject only to the condition that a person who wishes to use our website register and accept the associated "Terms and Conditions" and "Privacy Policy". It is possible to become an anonymous, registered user. Additional information is available to subscribers who pay for certain products and services.

ANNEX A: TECHNICAL COMMENTS ON THE PROPOSED AMENDMENTS

In this Annex, we offer some technical comments on the Proposed Amendments.

1. PROPOSED RULE 17G-5(c)(5): RATING RECOMMENDATIONS

We do not object to the overall thrust of proposed paragraph 17g-5(c)(5) but, as we discuss in our response to Question 2 below, we believe that the prohibition could be more narrowly tailored and still achieve its intended purpose.

A. Responses to Selected Questions

1. ***Is this type of conflict one that could be addressed through disclosure and procedures to manage it instead of prohibiting it? Should the Commission, rather than prohibiting it, add this type of conflict to the list of conflicts in paragraph (b) of Rule 17g-5, which, under paragraph (a) of the rule, must be addressed through disclosure and procedures to manage them?***

MIS believes that a credit rating analyst cannot be an objective participant in the credit rating process if he or she has also provided advisory services to the issuer, underwriter or sponsor of the security. We agree, therefore, with the Commission that if credit rating analysts provided such services, it would be a difficult conflict to manage.[10] Accordingly, we do not object to a prohibition on persons within an NRSRO providing such services. As we discuss in our response to Question 3, MIS does not recommend, consult or provide advice to corporate or structured finance issuers.

2. ***Would there be practical difficulties for an NRSRO that is part of a large conglomerate in monitoring the business activities of persons associated with the NRSRO such as affiliates located in other countries to comply with the proposed requirement? If so, given the greater separation between the NRSRO and these types of persons associated with the NRSRO, should the Commission require instead that, for these types of persons associated with the NRSRO <u>only</u>, the NRSRO disclose this conflict and manage it through information barriers rather than prohibit it?***

The Rating Agency Act requires that the Commission's rules be narrowly tailored to achieve its requirements. However, as presently drafted, paragraph (c)(5) seeks to regulate and constrain the activities of entities other than NRSROs (and their CRA affiliates). MCO owns two legally and operationally separate subsidiaries, MIS and Moody's Analytics. MIS is the CRA and registered NRSRO. Moody's Analytics brings together all of MCO's other commercial activities, including the provision of a range of analytical and technical products and services.[11] As indicated in our response to Question 3, MIS does not recommend, consult or provide advice to corporate or structured finance issuers. Also, although Moody's Analytics offers certain consulting services,[12] at present it does not offer a rating advisory service.

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[10] Proposing Release at 36226.

[11] Moody's Analytics' products and services are intended to provide clients with the means to: (1) assess and manage the credit risk of individual exposures as well as portfolios; (2) price and value holdings of debt instruments; (3) analyze macroeconomic trends; and (4) enhance their risk management skills and practices.

[12] For example, Moody's Analytics assists customers in developing, validating and calibrating internal risk scoring models.

Consequently, no enterprise within the MCO family advises, or provides consulting services to, issuers about how to obtain a desired credit rating from any NRSRO, including MIS. However, MIS does not exercise control over Moody's Analytics. In addition, we believe that it would be inappropriate for MIS to dictate how a legally separated, sister subsidiary should conduct its business. Moreover, we believe that legally separated subsidiaries of corporate parents of NRSROs should be allowed to make independent business decisions, including the decision to provide recommendations or advice about how best to achieve a desired credit rating, provided that this potential conflict is disclosed and effectively managed. We disagree with the Commission's assertion that it would be difficult for the NRSRO to remain objective where an affiliate of the NRSRO provided a rating advisory service.[13] We believe that the potential conflict can be managed through appropriate and robust policies and procedures, including but not limited to:

- information fire-walls between the entities;
- a base and cash bonus compensation structure for credit rating analysts that is not connected to the success of the affiliated entity; and
- the rating committee process.

Accordingly, we believe that the Commission's and the Rating Agency Act's objectives can be met by revising the proposed rule as follows. The prohibition in paragraph (c)(5) should apply only to the NRSRO and any "person within the NRSRO", as that term is defined in the Existing Rules. With respect to persons who are "associated" with the NRSRO within the meaning of the Exchange Act but who are not persons "within the NRSRO", the potential conflict should be prohibited in paragraph (b) unless it is disclosed and managed. We recommend that the Commission revise paragraph Rule 17g-5(b) by adding a new sub-paragraph (11) and revise Rule 17g-5(c) by modifying proposed sub-paragraph (5) as follows:

> (b)(11) Issuing or maintaining a credit rating with respect to an obligor or security where a person associated with the nationally recognized statistical rating organization, other than a person within the nationally recognized statistical rating organization, made recommendations to the obligor or the issuer, underwriter, or sponsor of the security about the corporate or legal structure, assets, liabilities or activities of the obligor or issuer of the security;
>
> (c)(5) The nationally recognized statistical rating organization issues or maintains a credit rating with respect to an obligor or security where the nationally recognized statistical rating organization or a person ~~associated with~~ within the nationally recognized statistical rating organization made recommendations to the obligor or to the issuer, underwriter, or sponsor of the security about the corporate or legal structure, assets, liabilities or activities of the obligor or issuer of the security;

3. The Commission recognizes that the line between providing feedback during the rating process and making recommendations about how to obtain a desired rating may be hard to draw in some cases. Consequently, should the Commission specify the type of interactions between an NRSRO and the person seeking the rating that would and would not constitute recommendations for the purposes of this rule?

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13 Proposing Release at 36226.

The terms "making recommendations", "consulting services" and "advisory services" are commonly understood as involving the provision of advice, in the form of proposed solutions or recommended plans of action relating to the issuer's strategy, structure, management and/or operations. With respect to the goal of "obtaining a desired credit rating during the rating process",[14] investment banks often have rating advisory divisions, which provide such services to corporate issuers, and structured finance underwriting divisions, which provide such services to structured finance originators. There are also firms that specialize in providing advice about ratings. These underwriters and rating advisors often work with law firms and other service providers to offer advice to meet a particular issuer's overall financial and strategic objectives. Some advisors and consultants also assist in implementing the solutions they have recommended. Consequently, those who make recommendations or who provide consulting or advisory services are actively involved in creating, endorsing and sometimes implementing proposals.

The credit rating process, in contrast, is essentially reactive. At MIS we do not structure or design structured finance products, nor do we recommend one structure over another. Structures are designed by arrangers and investment bankers to fit the needs of particular investors. We are not privy to many of the discussions that contemplate features of a securitization (especially non-credit related features) and in most situations we do not know who the ultimate investors in the transaction will be.

MIS believes that additional guidance beyond the Commission's discussion in the Proposing Release[15] is neither necessary nor appropriate. We appreciate the Commission's understanding that the rating process is essentially reactive. We recognize that rating analysts should not make recommendations to issuers, regardless of whether the issuer is a corporate entity or a structured finance sponsor. We also recognize that NRSROs must remain transparent about their rating methodologies and rating processes. To this end, we believe a principles-based rule will enable NRSROs and market participants to strike the appropriate balance between these two seemingly contradictory, yet parallel, objectives.

In particular, we are concerned that if the Commission provides examples of what it considers to be permissible interactions, the Commission could unintentionally stifle our ability to have robust analytical conversations with issuers of debt securities. It is possible that such examples, and only those examples, will be considered acceptable and that any deviations, regardless of how slight, could cause apprehension among analysts, issuers and their representatives. Such an outcome could hamper our ability to have thorough discussions with issuers and inevitably lead to a less transparent rating process.

While MIS does not structure or design securitization products or recommend one proposed structure over another, in rating any structured security we do provide our opinion on the credit risks associated with various features of the transactions proposed by issuers or their advisors. In so doing, we may hold numerous, in-depth analytical discussions. These discussions do not transform us into investment bankers, consultants or advisors. Instead, they serve the dual purposes of: (i) helping us better understand the particular facts of the transaction as proposed by the issuer; and (ii) clarifying to the issuer the rating implications of our methodologies for that transaction and its specific characteristics. Similar discussions take place with corporations contemplating changes in financial structures and business strategies (*e.g.* the

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[14] Ibid.

[15] Proposing Release at 36226.

potential rating implications of a share buy-back program) or new corporate issuers to whom MIS has not previously assigned a rating. We believe that these discussions enhance overall market transparency and stability since they provide issuers with a better understanding of our analytical thinking and enable us to provide better-informed ratings to investors and other market participants. In this regard, we believe that the guidance the Commission has provided in the Proposing Release is clear and allows for a back-and-forth dialogue that is appropriate and sufficient for each given circumstance.

2. PROPOSED RULE 17G-5(c)(6): INVOLVEMENT IN FEE DISCUSSIONS

While MIS supports the objective underlying proposed paragraph (c)(6), we believe it is unworkable as drafted. As we discuss in more detail below, we recommend that the Commission adopt a rule that: (i) works for all NRSROs regardless of their size; (ii) recognizes that it is impracticable and undesirable to expect NRSROs to completely separate analytic functions from the function of determining and discussing fees with issuers and subscribers; and (iii) deals with this potential conflict as it arises both for issuer-pay and subscriber-pay NRSROs. Consequently, we suggest that the proposed prohibition in paragraph (c)(6) be replaced with a requirement for NRSROs to disclose and manage this potential conflict, as follows:

> "(b)(*) The nationally recognized statistical rating organization issues or maintains a credit rating where ~~the fee paid for the rating was negotiated, discussed, or arranged by~~ a person within the nationally recognized statistical rating organization who ~~has responsibility for participating~~ participated in determining the credit ratings or ~~for~~ developing or approving applicable procedures or methodologies initiated or participated in discussions regarding the fees payable by the issuer, investors or subscribers;"

A. Responses to Selected Questions

1. Should the proposed prohibition also be extended to cover participation in fee negotiations by NRSRO personnel with supervisory authority over the NRSRO personnel participating in determining credit ratings or developing or approving procedures or methodologies used for determining credit ratings?

As discussed in our response to Question 2 below, MIS believes that it is more appropriate to deal with this conflict through a requirement to disclose and manage it instead of prohibiting it. At a certain level in the hierarchy of the NRSRO, it is appropriate and necessary for some individuals to be involved both in the rating process and the business decisions, such as decisions about fee schedules for issuers and/or subscribers.

The MIS Code states that "MIS will not have Analysts who are directly involved in the rating process initiate, or participate in, discussions regarding fees or payments with any entity they rate."[16] In practice, this means that credit analysts and their immediate supervisors do not participate in discussions with issuers about fees. A wholly separate group within MIS is responsible for discussing fees and liaising with issuers on payment matters. At the same time, we believe that it is appropriate for more senior managers to participate in the rating process (including the development and approval of methodologies) even though they also are involved in matters such as setting fee schedules and, occasionally, discussing fees with a particular issuer.

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[16] See Provision 2.12. The MIS Code defines the term "Analyst" to mean "an Employee whose primary function is participation in the Credit Rating analysis process". The term encompasses Analysts who supervise or manage teams of Analysts. An "Employee" is "any individual who works for MIS in any capacity".

If a senior manager discusses fees with an issuer, however, it is MIS's practice for that senior manager to recuse himself or herself from any rating committee concerning that issuer.

We believe that these practices enable us to manage effectively the potential conflict that arises by separating as much as possible the function of discussing fees and putting in place fee schedules from the credit rating analytical function. At the same time, it is essential for MIS's senior managers to understand both the credit markets and the rating business and to let their knowledge of one inform the other. We also believe, therefore, that complete segregation of these functions at the highest levels of the organization could impair our capacity to operate.

2. Instead of prohibiting this conflict outright, would disclosure and procedures to manage the conflict adequately address the conflict? If so, what specific disclosures should be required? What other measures should be required in addition to disclosures?

MIS believes that this conflict can be addressed effectively through disclosure and procedures to manage it. This approach would obviate any need to adopt a two-tiered regulatory approach since a "disclose and manage" requirement can be adapted to suit different NRSROs.

We recommend that NRSROs describe generally whether employees with analytic responsibilities (including the development or approval of methodologies) also participate in the development of fee schedules or policies for, or fee discussions with, rated issuers. Likewise, NRSROs also should describe generally whether such employees participate in developing fee schedules or policies for, or fee discussions with, subscribers who pay for access to the NRSRO's ratings. NRSROs should also describe generally how individuals at different levels in their organization (*e.g.* credit analysts, credit analyst supervisors and senior managers) are permitted to, or not permitted to, participate in internal discussions about fees paid by issuers or subscribers and/or discussions directly with issuers or subscribers.

3. Would there be practical difficulties in separating analytic and fee discussions for a small NRSRO, including one that has limited staff, that are significant enough that the Commission should consider a different mechanism to address the conflict? If so, what sort of mechanism and with what conditions?

If the Commission revises proposed paragraph (c)(6) as we have recommended, we believe that the same requirement to disclose and manage the conflict should apply to all NRSROs regardless of their size. We would strongly object to rules that created a two-tier system of NRSROs, with some NRSROs being exempted from provisions such as the proposed rule, as it would unjustly allocate regulatory burdens and frustrate the regulatory purpose of minimizing conflicts. We also believe that the Commission should recognize through its rule-making that it is impracticable and undesirable to expect an NRSRO to completely separate these two functions at the highest levels of its management.

3. PROPOSED RULE 17G-5(c)(7): RECEIVING GIFTS

A. Responses to Selected Questions

1. Instead of prohibiting this conflict outright, should the Commission require that NRSROs disclose it and establish procedures to manage it? If so, what specific disclosures should be required?

We recognize that receiving gifts from entities that have or are seeking a rating from an NRSRO or that subscribe to an NRSRO's rating service can influence, or appear to influence,

that NRSRO's judgment. We believe that this conflict can be handled either by: (i) a requirement to disclose and manage it; or (ii) an easy-to-apply prohibition.

While we agree that a cap on the value of gifts may be one appropriate approach, we are concerned that the proposed prohibition (in the form of a per analyst/per meeting $25 cap) raises practical implementation concerns. For example, at meetings with issuers or their representatives, analysts likely will have to obtain itemized lists setting out the value of every single item received during the course of the meeting, including pens, paper, trinkets, refreshments and meals. Such requests likely will embarrass or even offend some issuers, particularly those from other cultures, with whom analysts interact. Moreover, to facilitate compliance with the proposed rule, an NRSRO likely will require its analysts to make and retain records with respect to every activity (including receipt of food or drinks), however insignificant, that could be interpreted as involving a gift.

Furthermore, a $25 aggregate limit per meeting per analyst likely will prevent analysts in cities such as New York, London and Tokyo where we do business from eating a modest meal at a meeting. MIS analysts also sometimes participate in full-day or multi-day onsite meetings with issuers. It is unclear how the "per meeting" cap will apply in such circumstances. We believe that receiving meals and refreshments during normal business activities (such as meetings) does not raise a potential conflict of interest. In this respect, therefore, we believe that the proposed rule is overbroad.

Finally, the proposed rule may be too narrow because it does not appear to capture gifts provided to analysts by persons other than issuers, underwriters and sponsors. A subscriber might also seek to influence an analyst by providing the analyst with gifts or favors. We believe that such activities also should be subject to a requirement to disclose and manage the conflict or an appropriately tailored prohibition on the activities.

If the Commission decides to require disclosure and management of the conflict, we would not object to a rule requiring the NRSRO to describe generally: (i) the kinds of gifts its analysts typically receive; (ii) the categories of people from whom they typically receive gifts; (iii) how the NRSRO characterizes certain items or activities (*e.g.* as gifts or otherwise); and (iv) how analysts are expected to handle certain types of items or activities, such as:

- meals, refreshments and incidental items provided during business meetings;
- meals that take place outside the context of a business meeting;
- entertainment; and
- reimbursement or direct payment of the personal travel, meal or other expenses (including conference fees) incurred by an analyst to attend a conference or similar event.

2. Instead of prohibiting gifts outright, should the Commission establish a yearly limit on the aggregate value of gifts that would be permitted under the prohibition? For example, the Commission could provide in the rule that the prohibition would not be triggered until the aggregate value of all gifts received from a particular person in a twelve month period exceeded $100, $500 or $1,000 or some other amount.

If the Commission decides to prohibit gifts, a prohibition in the form of an annual limit would be easier to implement than the proposed $25 per meeting limit. We recommend that the

prohibition exclude meals or refreshments provided during normal business activities, such as meetings.

4. PROPOSED RULE 17G-2(a)(2)(iii): RECORD OF RATIONALE FOR MATERIAL DEVIATION FROM MODEL OUTPUT

A. Detailed Responses to Selected Questions

1. Would this proposal have the impermissible effect of regulating the substance of credit ratings in any way?

MIS believes that the proposed rule, either as drafted or in the revised form we recommend in our response to Question 2, would not necessarily result in the Commission regulating the substance of credit ratings. There is a risk, however, that the Commission could inadvertently interpret and apply paragraph (a)(2)(iii) from time to time in a way that could have such an impermissible effect. For example, an examiner might question the validity of the reasoning set out in the record, instead of focusing on whether or not the record showed that the rating committee followed its stated policies, procedures and methodologies in determining the rating. MIS believes it will be important for the Commission to provide clear guidance to its staff on the scope of what is, and is not appropriate, to question in the examination process.

2. Should the Commission define in the rule when the use of a model would be a "substantial component" in the process of determining a credit rating? Commenters endorsing the adoption of such a definition should provide specific proposals.

MIS supports the Commission's goal of enhancing the NRSROs' recordkeeping processes so that the NRSRO and the Commission's examiners can generally perceive how a particular credit rating was determined.[17] We believe, however, that this recordkeeping requirement should not focus on deviations from the outputs of quantitative models. While we use quantitative models to assist our analysis and enhance consistency in our decision-making, our ratings take into account qualitative as well as quantitative factors and are intended to reflect the exercise of judgment about the expected creditworthiness of an obligation or entity. Moreover, each rating committee member is expected to apply his or her own independent judgment in the decision-making process. Ultimately, ratings are subjective opinions that reflect the majority view of the rating committee's members.

If the Commission focuses on deviations from ratings implied by quantitative models, we are concerned that the Commission as well as users of ratings will attach too much weight to those models. This might lead them to discount the significance of qualitative factors[18] in their assessment of credit risk, mistakenly treat NRSROs' credit opinions as statements of fact, and/or view deviations from models as evidence of a failure in the model or a failure to follow appropriate procedures. In effect, the proposed rule could create a presumption that the model output is the "right" rating and that any other opinion is "wrong" unless it is justified. As a consequence, the rule could discourage analysts and rating committees from considering qualitative factors or exercising judgment in determining ratings. Ultimately, NRSROs might

[17] Proposing Release at 36230.

[18] There are many other factors, such as macro-economic considerations, the regulatory environment and management quality that cannot be reduced to inputs for a quantitative model but that can have a significant impact on the relative creditworthiness of an issuer or obligation.

determine that there was little or no value in considering such factors or exercising such judgment, with the result that they might publish only their models without providing additional insight or perspective on the relative creditworthiness of obligations or entities. In our view, this would negatively affect the quality and usefulness of our credit ratings.

For these reasons, we recommend that the Commission revise the proposed rule to require NRSROs to make and retain for each current credit rating a record indicating the principal quantitative and qualitative factors considered, and the principal methodologies used, in determining the credit rating as well as the rationale for the rating assigned. Such a recordkeeping requirement will apply in more circumstances than the Commission's proposed rule, thereby enhancing NRSROs' recordkeeping and facilitating the Commission's examinations of NRSROs. Such a rule also will eliminate any requirement for the Commission or NRSROs to define subjective concepts such as "substantial component" or "material difference", making the rule easier for NRSROs to apply consistently and for the Commission to enforce. We suggest that the proposed rule be revised to require NRSROs to make and retain a record of:

> "(a)(2)(iii) The ~~If a~~ principal quantitative and qualitative factors considered, and the principal methodologies used, ~~to model was a substantial component in the process of~~ in determining the credit rating ~~any material difference between the credit rating implied by the model and the final credit rating issued~~ and the rationale for the rating assigned; ... ."

If the Commission nevertheless decides to adopt the rule as drafted, MIS believes that the rule should provide that each NRSRO may determine in its discretion which of its rating methodologies use a quantitative model as a substantial component of the rating process. First, each NRSRO is in the best position to know how and to what extent quantitative models are used in its rating process. Second, we are concerned that if the Commission defines "substantial component" or second-guesses the NRSRO's determination in this regard, the Commission may inadvertently regulate the substance of an NRSRO's methodologies and procedures for determining credit ratings by substituting its own opinion of what constitute the key components of the rating process and thereby devaluing other components of the methodology, contrary to the Rating Agency Act.

3. Should the Commission require that the information about material deviations from the rating implied by the model be publicly disclosed by the NRSRO in the presale report or when the rating is issued?

The Commission has stated that this recordkeeping requirement is intended to enhance the NRSROs' recordkeeping and facilitate the Commission's examination process. Extending the proposed rule to require public disclosure about material deviations from a rating implied by a model is unnecessary to achieve the Commission's stated purposes.

We believe that NRSROs should explain in their rating announcements the key elements underlying the rating.[19] If a quantitative model forms a substantial component of the rating process, such an explanation likely will encompass the key quantitative and qualitative factors underlying the credit rating. By contrast, for the reasons set out in our response to Question 2, we believe that requiring public disclosure of material deviations from ratings implied by

[19] See provision 3.6 of the MIS Code.

quantitative models will inappropriately encourage users of ratings to misunderstand the nature of credit ratings and over-estimate the relevance of models in the rating process.

5. PROPOSED RULE 17g-2(a)(8): RECORDS OF COMPLAINTS ABOUT ANALYSTS

MIS acknowledges that the Commission has a legitimate interest in assessing the reasons for analyst re-assignments or terminations to determine whether or not the NRSRO is following its own stated policies and procedures and making human resource allocation decisions for reasons unconnected to conflicts of interest. We note that potential conflicts exist under any business model and should be managed appropriately.

At the same time, it is important to emphasize that there are many appropriate business reasons for analyst re-assignments. For example, an analyst might marry a person associated with an issuer in the analyst's portfolio, might relocate or simply might wish to learn a new subject area. The nature of an issuer's business might change (*e.g.* it might acquire or dispose of a line of business), so that it makes sense to assign a new lead analyst with industry expertise that matches the issuer's new business profile. MIS's principal contacts at a foreign issuer might change, so that an analyst who speaks the same language as the new contacts might be assigned to serve as the lead analyst. Also, MIS might decide to re-balance a group of analysts' portfolios to distribute work more equitably in light of increases or decreases in the number of rated entities in a particular sector or asset class, or for training and development purposes.

While we do not object to the proposed rule requiring us to retain communications that contain complaints about analysts' performance, we have a few concerns and requests for clarification, which we address in our responses to the Commission's questions below.

A. Detailed Responses to Selected Questions

1. In addition to the proposed recordkeeping requirement, should the Commission require the NRSROs to publicly disclose when an analyst has been re-assigned from the responsibility to rate an obligor or the securities of an issuer, underwriter, or sponsor?

The Commission has stated that the proposed rule is intended to facilitate its examination process. We believe that retaining records is sufficient to achieve this objective, whereas a requirement for NRSROs to publicly disclose all re-assignments of analysts would not be narrowly tailored to achieve the objectives of the Rating Agency Act. Furthermore, we believe that public disclosure of analyst re-assignments might create or exacerbate a misperception among market participants and other users of credit ratings that individuals determine ratings. At MIS, individuals may be assigned to serve as lead or back-up analysts for a particular issuer or transaction, but all rating decisions are made collectively by rating committees, according to a majority vote. Finally, we believe that a public disclosure requirement of this nature could create incentives for NRSROs to avoid re-assigning analysts wherever possible, even in circumstances where the NRSRO believed that rating quality and/or the job satisfaction and intellectual capital of one or more analysts could be enhanced through re-assignments.

2. Should the Commission require NRSROs to retain any communications containing a request from an obligor, issuer, underwriter, or sponsor that the NRSRO assign a specific analyst to a transaction in addition to the proposed requirement to retain complaints about analysts?

MIS would not object to such a rule. We believe, however, that the record-keeping requirement should apply in respect of any third party request. The potential for conflict of

interest is not restricted to NRSROs that operate under an issuer-pays model. Such a conflict may arise if anyone outside the NRSRO, including obligors, their representatives, investors, subscribers or government authorities, makes such a request.

B. Request for Clarification

We also ask the Commission to clarify the meaning of the phrase "communications that contain complaints". It is unclear whether this phrase encompasses only recorded complaints (*e.g.* letters or voicemails) or whether it is also intended to capture complaints that are made orally but not recorded. If the broader interpretation is intended, then it would appear necessary for the NRSRO to make (and be required to make) a record and then retain it. We also observe that it may be difficult in practice to determine whether or not certain communications contain complaints. This would be particularly true in respect of informal, oral communications.

6. PROPOSED RULE 17G-2(b)(7): CLARIFYING AMENDMENT

A. Detailed Responses to Selected Questions

1. Should the Commission delete the term "maintaining" from paragraph (b)(7) and proposed new paragraph (b)(8) of Rule 17g-2 as it has the same meaning as "monitoring?"

We consider "monitoring" to be an internal function that involves regularly reviewing the creditworthiness of an entity or obligation. We consider "maintaining" a rating to be an externally oriented function that is akin to "continuing to express a credit opinion externally". As the words have different meanings, we do not object to retaining both terms.

7. PROPOSED AMENDMENTS TO THE INSTRUCTIONS FOR EXHIBIT 1 OF FORM NRSRO

MIS does not object to most of the Commission's proposed amendments. We believe, however, that the proposed instruction requiring applicants for NRSRO status ("**Applicants**") and NSRSOs to incorporate into their performance statistics defaults that have occurred after a rating is withdrawn is not narrowly tailored to achieve its intended purpose. A rating that has been withdrawn is, by definition, a rating that the NRSRO does not monitor. Requiring an NRSRO to monitor entities and obligations even after the NRSRO has publicly announced that it has ceased to do so intrudes upon the substance of the NRSRO's rating procedures. Such a requirement, therefore, seems to fall outside the scope of the Commission's authority.

From a practical perspective, many rating withdrawals occur because an issuer's debt is fully retired, so that a default is no longer possible.[20] In other circumstances, once a credit rating is withdrawn, MIS typically has limited access to information about the obligation and the issuer.[21] We would not be in a position to certify with confidence that our performance statistics incorporate all defaults with respect to withdrawn credit ratings. Therefore, a positive obligation for NRSROs to monitor issuers and obligations after a rating has been withdrawn is inappropriate.

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[20] Generally, ratings on bonds with shorter maturities will be withdrawn sooner (because the debt is retired sooner) than they will be for bonds with longer maturities.

[21] This is especially true in jurisdictions where it is difficult for the public to obtain copies of companies' financial statements.

We agree, however, with the Commission that it is possible that an NRSRO might manipulate its performance results by intentionally withdrawing ratings when the credit is performing contrary to the NRSRO's expectations. To address this concern, MIS takes into account the impact of rating withdrawals on its default rate statistics. We believe that failing to do so could result in understated default rates for a particular CRA.[22] We recommend, therefore, that the Commission amend Rule 17g-6 to prohibit NRSROs from withdrawing credit ratings with the intent to manipulate the performance statistics they disseminate or provide to the Commission. In addition or alternatively, the Commission might also wish to consider amending the instructions to Form NRSRO to require Applicants and NRSROs to certify that they have not withdrawn ratings with the intention of manipulating their performance statistics. We also would not object to requirements that NRSROs describe generally: (i) whether and how they take into account the impact of rating withdrawals on their performance statistics; and (ii) whether and in what circumstances they monitor ratings after they have been withdrawn.

Also, if the Commission decides to require NRSROs to show defaults relative to initial ratings in their performance statistics, for the following reasons we recommend that NRSROs also be required to show defaults relative to the ratings held as of the beginning of the one-year, three-year and ten-year periods for which performance statistics are being provided. First, we question whether users of credit ratings will find the Commission's proposed performance measure useful for all classes of credit ratings. It may be more relevant, for example, for structured finance securities than for other classes of credit ratings. Relative to structured securities, the creditworthiness of corporations can change for many unforeseen reasons after an initial rating is published.[23] Over-emphasizing initial ratings as a performance metric may be misleading. It also could lead to unintended consequences. For example, over-emphasizing initial ratings could lead rating committees to be overly conservative when they assign initial ratings.

Second, statistics that track defaults only with respect to original ratings could lead to results based on very small data sets, thereby making the statistics less reliable and relevant. Third, an attractive feature of cumulative default rate statistics is that they capture defaults associated with all ratings, including initial ratings.

A. Responses to Selected Questions

1. Should the Commission prescribe specific standards for the performance statistics, such as requiring an NRSRO to disclose how its credit ratings performed relative to metrics such as credit spreads?

MIS believes that disclosure of ratings performance over time is an important part of the NRSRO oversight framework because such disclosure provides objective criteria for assessing whether an NRSRO's ratings are suitable for use in regulation. MIS publishes and makes freely

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[22] See R. Cantor and D. Hamilton, "Adjusting Corporate Default Rates for Rating Withdrawals", Journal of Credit Risk, Vol. 3 (2), Summer 2007.

[23] For example, the economics of the industry may change, the issuer's debt leverage or equity levels may increase or decrease, the issuer may be acquired or acquire other businesses, and/or its management or strategy may change. Any of these changes may lead to material changes in the issuer's creditworthiness that were unforeseen when the initial rating was published and that should properly result in rating changes.

available various statistical ratings performance reports.[24] We believe measures of this nature provide valuable performance data for users of MIS's ratings.

We believe, however, that the Commission should not prescribe specific standards for performance statistics beyond those already set out in the instructions to Exhibit 1, as those instructions would be modified by the Commission's proposed amendments. Prescribing standardized performance statistics may imply direct comparability among the ratings of different NRSROs and thereby mislead users of ratings. It may also advantage certain NRSROs, giving rise to a mistaken impression that some NRSROs' methodologies may result in better ratings performance solely because their methodologies are better suited to the standardized performance metrics endorsed by the Commission. Moreover, prescribing standardized performance statistics may result in regulatory encouragement of a more standardized industry approach to the substance of ratings. This is because NRSROs would have an incentive to alter their rating methodologies, procedures and definitions, not to improve their ratings' predictive content, but to maximize performance under standards prescribed by regulators.

8. PROPOSED AMENDMENTS TO INSTRUCTIONS FOR EXHIBIT 2 OF FORM NRSRO

MIS does not object to the proposed amendments to the instructions for Exhibit 2.

9. PROPOSED RULE 17G-3(a)(6): ANNUAL REPORT OF RATING ACTIONS

A. Responses to Selected Questions

> ***1. Could the performance statistics currently required in Exhibit 1 to Form NRSRO, as well as the proposed enhancements to those statistics, be used to target potential problem areas in an NRSRO's credit rating processes in the same manner as this proposed report thereby making the report redundant?***

MIS does not object to providing the Commission with an annual report of rating actions, aggregated by asset class for structured finance securities and otherwise by broad rating category. We believe, however, that such a report is redundant because it will not convey any meaningful information about whether or not an NRSRO's rating processes have been compromised beyond the data that: (i) are already conveyed by the performance statistics required by Exhibit 1 (as it would be amended); and (ii) what will be made available in an electronic data file if the Commission amends Rule 17g-2.

Furthermore, we are concerned that a rule focusing attention solely on a single feature of rating performance (*e.g.* the frequency of rating changes year-to-year) sends a signal to users of credit ratings that a single dimension of rating stability (*i.e.* frequency of rating changes) is the most important factor to consider in assessing the quality and usefulness of an NRSRO's ratings and the integrity of its rating processes. By contrast, we believe that the performance of our ratings should be measured by rating accuracy (*i.e.* the correlation between ratings and defaults) as well as rating stability (*i.e.* the frequency and magnitude of rating changes as well as the frequency of rating reversals).[25] Furthermore, we believe that stability should be measured over

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[24] See, e.g. our *Guide to Moody's Default Research: March 2008 Update* (Document No. 108157).

[25] MIS, *Measuring the Performance of Corporate Bond Ratings*, April 2003 (Document No. 77916) and *Analyzing the Tradeoff between Rating Accuracy and Stability*, September 2006 (Document No. 99100).

multiple time periods (not just year-to-year). To the extent that rating performance is relevant to an assessment of the integrity of our rating processes, all these factors would be relevant.

2. Should the Commission also require NRSROs to furnish an "early warning" report to the Commission when the number of downgrades in a class of credit ratings passes a certain percentage threshold (e.g., 5%, 10%, 15%, or 20%) within a number of calendar or business days (e.g., 2, 5, 10, or 15 days) after the threshold is passed, similar to the broker-dealer notification rule (See 17 CFR 240.17a-11)?

If the Commission adopts proposed paragraphs (a)(8) and (d) of Rule 17g-2 in an amended form as we have recommended, the Commission will have free access to a data file of rating action history, including the most recent rating actions, for current ratings. Commission staff could search the data file to identify recent rating trends. Such access would render an early warning reporting requirement redundant.

More importantly, MIS believes that an early warning reporting requirement is inappropriate. First, as the Commission noted in the Proposing Release, a significant and sudden increase in the number of rating actions may be the result of factors broadly affecting an asset class or industry sector and, therefore, is not a strong indicator of a failure in the rating process. We appreciate that the Commission has acknowledged this fact in the Proposing Release. Nevertheless, we are concerned that the mere existence of an early warning reporting requirement may aggravate a misperception held by some market participants and authorities that downgrades in ratings necessarily indicate that the ratings were wrong in the first place. We are also concerned that such an early warning reporting requirement could create incentives for NRSROs to avoid having to file such reports, *e.g.* by being excessively conservative in assigning initial ratings and/or manipulating the timing of rating decisions to avoid triggering reporting thresholds. Such behavior would undermine the objectives of the Rating Agency Act, which include enhancing transparency and fostering accountability in the CRA industry.

In addition, if the Commission wishes to consider trends in rating actions as part of its analysis of whether or not rating processes have been compromised, we believe it should use metrics that take into account a wider range of factors relating to accuracy and stability. By contrast, the proposed early warning reporting requirement focuses on only one aspect of rating stability (downgrades), considered over a very short time period.

B. Does Paragraph (a)(6) Belong under Rule 17g-3?

Section 15(E)(k) of the Exchange Act authorizes the Commission to adopt rules requiring NRSROs to furnish to the Commission "financial statements" and "information concerning [their] financial condition". In our view, the proposed annual report on the number of credit rating actions taken during the preceding fiscal year does not appear to fall within the scope of "financial statements" or information concerning an NRSRO's "financial condition". Instead, it seems to fall more appropriately within the scope of the Commission's authority under Section 17(a)(1) of the Exchange Act, which authorizes the Commission to adopt rules requiring, among others, NRSROs, to make and keep records for prescribed periods and furnish copies thereof to the Commission. It would seem more appropriate, therefore for this record to be provided for under Rule 17g-2, which sets out NRSROs' record-keeping requirements.

C. Which Rating Actions Should Be Included in the Report?

As drafted, proposed paragraph (a)(6) may be overly broad or unclear as to its scope because it calls for the NRSRO to provide the Commission with an annual report on the number of "credit rating actions" taken during the preceding fiscal year. When MIS issues or revises a credit rating with respect to an obligation, it may take rating actions with respect to one or more obligations of the issuer as well as the issuer itself. It is unclear which credit rating actions should be included within the scope of the report and whether and how multiple credit rating actions with respect to a single issuer should be aggregated for purposes of the annual report and any early warning reporting requirement.

10. PROPOSED RULE 17G-7: DIFFERENTIATING STRUCTURED FINANCE RATINGS

A. Responses to Selected Questions

1. ***Is the proposed rule sufficiently clear about the types of securities and money market instruments to which it applies? Are there securities to which the proposal applies that should not be subject to the requirement of a report or a differentiated symbol?***

The lines of demarcation for what is and is not structured finance are blurry. According to one academic text on the topic,[26] there is no universally accepted definition for the term "structured finance". As a result, while there is agreement that asset-backed securities, commercial mortgage-backed securities, residential mortgage-backed securities and collateralized debt obligations are structured finance products, there is no broad consensus that other types of instruments, such as project financings or credit default swaps, are structured finance products. Some have argued that the term "structured finance" includes "any financial transaction that is not standard, or in market jargon, 'plain vanilla', in terms and conditions."[27] Consequently, hybrid debt securities, trust preferred securities, warrants and convertible bonds could be construed as a form of structured financing and fall within proposed Rule 17g-7.[28]

For these reasons, some people have suggested that structured financing refers to a technology rather than a class of discrete and identifiable securities. In other words, structured financing encompasses "… techniques employed whenever the requirements of the originator or owner of an asset, be they concerned with funding, liquidity, risk transfer, or other need, cannot be met by an existing, off-the-shelf product or instrument. Hence, to meet this requirement, existing products and techniques must be engineered into a tailored-made product or process. Thus, structured finance is a flexible engineering tool."

MIS believes that the proposed definition of structured finance securities and instruments in proposed Rule 17g-7 is insufficiently precise and that, if the Commission adopts Rule 17g-7, it

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[26] F.J. Fabozzi *et al.* (2006), *Introduction to Structured Finance* (Wiley: Hoboken, NJ).

[27] Ibid.

[28] We note that the definition of structured finance product in proposed rules 17g-7 and 17g-5(b)(9) is broad enough that it could encompass a wide range of asset-backed or mortgage-backed securities that generally are not considered to be structured finance securities. For example, state housing authorities may issue bonds that are secured by a pool of mortgage loans or rental revenues from a housing authority in circumstances where the mortgages or assets remain on the housing authority's balance sheet instead of being transferred to an SPV. These bonds are not ordinarily considered to be structured finance securities.

should provide clear guidance as to which types of securities and instruments fall within the scope of the rule.

2. Would the reports or differentiated symbols achieve the Commission's stated goal of encouraging investors to perform more internal risk assessments of structured finance products? Could the reports cause investors to ignore other relevant disclosures or lead to confusion?

MIS cannot speak for investors but we can share with the Commission the results of a Request for Comment ("**RFC**") that we published to solicit market views on whether we should differentiate structured finance and corporate ratings.[29] We undertook this initiative in response to the growing debate about the appropriateness of using a single rating scale for both structured and non-structured securities. The RFC solicited comments on five possible options:

1. move to a completely new rating scale for structured finance securities;
2. use the same rating scale but add a modifier (*e.g.* Aaa.sf) to all structured finance ratings;
3. use the same rating scale but add a suffix that contained additional information, such as an estimate of multi-notch rating transition risk (*e.g.* Aaa.v1, Aaa.v2);
4. use the same rating scale but provide additional analytical information in a separate scale that would exist in a separate data field; or
5. make no changes to the rating scale, but provide additional information and commentary through written research.

We received over 200 submissions from institutions representing more than $9 trillion in fixed income assets under management. About three quarters of all respondents (both by number and assets under management) voted for no change to the rating scale currently used by MIS for rating structured securities. Many respondents also expressed the view that using the same rating scale but adding a modifier to all structured finance ratings would be merely a cosmetic change. Instead, a large majority of market participants who responded to the RFC believe that MIS should enhance the analysis and transparency of our structured finance ratings.

Based on these survey results, it is our understanding that rating symbols or other identifiers (such as an .sf suffix) that merely label a rating as a structured finance rating rather than a corporate rating have little information content. We doubt that such labeling would help achieve the Commission's goal of encouraging investors to perform their own risk assessments of structured finance products. By contrast, we understand that market participants would like us to enhance our analysis and the transparency of our structured finance ratings. Based on the responses we received in relation to our RFC, we are introducing two new risk measures, model assumption volatility scores ("**V Scores**") and loss sensitivity analysis.[30] These measures seek to address the two distinct questions that users of our credit ratings have repeatedly posed:

- What is the degree of uncertainty around the assumptions that underlie our credit ratings of structured finance securities?

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[29] See *Should Moody's Consider Differentiating Structured Finance and Corporate Ratings*?, February 2008 (Document No. 107318).

[30] See *Introducing Assumption Volatility Scores and Loss Sensitivities for Structured Finance Securities*, May 2008 (Document No. SF132669). MIS has begun to roll out these new risk measures. See *Assumption Volatility Scores and Loss Sensitivities in the U.S. ABS Vehicle Sector*, July 2008 (Document No. SF138274).

- How sensitive are MIS's credit ratings to our collateral pool loss expectation assumptions?

V Scores are intended to rank transactions by the potential for significant rating changes owing to uncertainty around the assumptions and the modeling that underlie the ratings. The V Score applies to the entirety of a transaction (rather than individual tranches) and is derived from an analysis of: (i) historical performance; (ii) data adequacy; (iii) complexity and market value sensitivity; and (iv) governance. Loss sensitivity analysis is intended to measure the number of notches that an MIS-rated structured finance security would likely move downward if the underling collateral pool's assumed loss expectations increased substantially. For this analysis, we will "re-rate" different transactions assuming a uniform level of stress. Specifically, we will assume that the expected loss rate on each transaction's underling collateral pool rises from its original level to a level consistent with a 95th percentile loss level stress; *i.e.* expected losses will rise to a level that would normally be assumed to occur with a one-in-twenty probability.

While we have concluded based on feedback from market participants that we should introduce V Scores and loss sensitivity analysis, we do not believe it is appropriate for the Commission to require NRSROs to publish certain types of opinion or analysis, such as those MIS has chosen to provide. We believe that such a rule falls outside the scope of the Commission's authority as it would regulate the substance of NRSROs' credit ratings and/or the procedures and methodologies by which they determine credit ratings. This is because it could require NRSROs to employ particular methodologies to produce the required assessments and disclosure. The fact that the proposed rule offers NRSROs the options of providing a prescribed report or using a different symbol system does not, in our view, prevent the rule from being inconsistent with paragraph (c)(2) of Section 15E of the Exchange Act, since both options would affect the substance of credit ratings, methodologies and/or procedures.

3. ***Should the rule be expanded to require reports or different ratings symbols for each class of credit ratings identified in Section 3(a)(62)(B) of the Exchange Act (15 U.S.C. 78c(a)(62)(B)); namely: (1) financial institutions, brokers, or dealers; (2) insurance companies; (3) corporate issuers; (4) issuers of asset-backed securities; and (5) issuers of government securities, municipal securities or securities issued by a foreign government? Alternatively, should the rule be expanded to require reports or different ratings symbols for only certain of these classes or subclasses such as for municipal securities?***

MIS believes that having a different rating nomenclature for different asset classes could lead to confusion in the market and could significantly and adversely affect the usefulness of our opinions. We are interested, however, in market participants' perspectives on this question and will consider modifying our rating scales if market participants indicate to us that such differentiation would be useful.

Nevertheless, for the reasons set out in our response to Question 2 above, we believe that a rule requiring NRSROs to use different rating symbols or provide prescribed information in a report is inappropriate and falls outside the scope of the Commission's rule-making authority. That is because prohibiting the use of common symbols for different types of debt securities or issuers would preclude the NRSRO from expressing the opinion, if it wished to do so, that two different types of debt security with the same rating were similarly creditworthy.

4. Should the rule prohibit an NRSRO from using a common set of symbols (e.g., AAA, AA, A, BBB, BB, B, CCC, CC, C) to rate different types of obligors and debt securities (e.g., corporate debt and municipal debt) where the NRSRO uses different methodologies for determining such ratings? Would such a proposal raise any questions relating to the scope of the Commission's legal authority in this area?

For the reasons set out in our response to Question 2 above, we believe that such a requirement would fall outside the scope of the Commission's rule-making authority.

11. AMENDMENTS SHOULD APPLY ONLY ON A PROSPECTIVE BASIS

A number of the Proposed Amendments refer to past conduct, thereby raising certain questions about the retrospective reach of the final rules. For example, the proposed amendments to paragraph (c) of Rule 17g-5 provide that an NRSRO cannot issue or maintain a rating if a credit analyst who participated in determining a rating "received" a gift whose value exceeded $25 from the rated issuer. Read literally, these provisions would seem to prohibit an NRSRO from issuing or maintaining a rating after the date the rules come into force if, for example, an analyst received a gift worth $40 before the proposed rule came into effect. Such an interpretation of paragraph (c) of Rule 17g-5 would impose an excessive burden on NRSROs, issuers and users of credit ratings.

We have assumed that all of the Proposed Amendments, if implemented, will apply on a prospective basis only. We ask the Commission to clarify that the final rules will apply only on a prospective basis by expressly stating the effective date of the final rules.

ANNEX B: ADDITIONAL RESPONSES TO THE COMMISSION'S QUESTIONS ABOUT THE SUBSTANCE OF THE PROPOSED AMENDMENTS

In this Annex, we respond to the substantive questions posed by the Commission that we are well-positioned to answer and did not otherwise address in our Comment Letter or Annex A.

1. PROPOSED RULE 17G-2(a)(8) AND (d): XBRL RATING ACTIONS DATABASE

A. Is the six-month delay before publicly disclosing a rating action sufficiently long to address the business concerns of the subscriber-based NRSROs and the issuer-paid NRSROs? Should the delay be for a longer period such as one or two years or even longer? Alternatively, is six months too long and should it be a shorter period of time such as three months or even shorter?

Please see our response in section B.1 of part II of our Comment Letter.

B. Should the rule require that a notice be published along with the XBRL Interactive Data File warning that because of the permitted delay in updating the record some of the credit ratings in the record may no longer reflect the NRSRO's current assessment of the creditworthiness of the obligor or debt security? For example, the notice could explain that the information in the record is six months old and state that the credit ratings contained in record may not be up-to-date.

MIS would not object to a rule requiring that such a notice be published. We believe, however, that the exact content of the notice should not be prescribed exhaustively because NRSROs may wish to include other disclosures and explanations about the data file.

C. Are there ways in which the NRSROs should be required to sort the credit ratings contained on the record such as by asset class or type of ratings?

MIS can sort the data in the record in whatever order is called for by the Commission and users of our credit ratings. If, however, the electronic data file uses machine readable code, a common mark-up language such as XBRL and a common taxonomy, we do not see why it would be necessary for the Commission to prescribe the way the data is sorted.

D. What mechanisms are appropriate for identifying rated securities? Are there other identifiers in addition, or as an alternative, to CUSIP or CIK number that could be used in the rule?

MIS recommends that ISINs be used, rather than CUSIP numbers, since CUSIP numbers are available only for North American securities while the ISIN system is international. An NRSRO should not have to provide an ISIN, however, unless the NRSRO is permitted to use ISIN numbers in the data file without having to pay a fee. We also believe that NRSROs should not be required to include externally recognized identifiers, such as CIKs, to identify the issuers of the rated obligations. Requiring an NRSRO to add and populate a CIK data field is unnecessarily burdensome, since disclosure of the ISIN and the NRSRO's own identifier for the issuer should be sufficient.

We also wish to draw the Commission's attention to the fact that MIS relies upon external sources of information regarding data fields such as the "name of the security", as well as ISINs. We are aware of numerous situations where different NRSROs and other firms identify the same security differently. Also the way in which a security is identified can change over time (*e.g.* because of transactions such as mergers and acquisitions). Accordingly, while

MIS seeks to resolve any discrepancies in the identifying information it uses, we cannot always have complete confidence in the accuracy of these aspects of the data we use (particularly with respect to older, historical data). We recommend, therefore, that the proposed rule provide each NRSRO with the option of including its own, unique identifiers for securities and issuers in the data file, together with ISINs where these are available to the NRSRO without cost.

E. Should the Commission allow the ratings action data to be provided in a format other than XBRL, such as pipe delimited text data ("PDTD") or eXtensible Markup Language ("XML")? Is there another format that is more widely used or would be more appropriate than XBRL for NRSRO data? What are the advantages / disadvantages of requiring the XBRL format?

Please see our response in section B.2 of part II of our Comment Letter.

F. Should the Commission require that the information on the assets underlying a structured finance products discussed in Section II.A.1.a above be provided in a specific format such as PDTD, XML, or XBRL? Again, is there another format that is more widely used or would be more appropriate for such data? What are the advantages/disadvantages of requiring a specific format?

As set out in more detail in part II of our Comment Letter, MIS supports the objective of having greater public disclosure about the assets underlying structured finance securities but opposes the Commission's adoption of proposed paragraph (a)(3) of Rule 17g-5.

Since MIS does not produce the information concerning assets underlying structured finance securities, we are not well-positioned to express an opinion about the appropriate format and standard to be used to communicate that information.

G. Should the Commission take the lead in creating the new tags that are needed for the XBRL format or should it allow the tags to be created by another group and then review the tags? How long would it take to create new tags?

Please see our response in section B.3 of part II of our Comment Letter.

H. The Commission anticipates that the data provided by NRSROs would be simple and repetitive (i.e., the data would be name, CUSIP, date, rating, date, rating, etc.). Is there a need for more detailed categories of data?

Please see our response in section B.4 of part II our Comment Letter.

I. Should the Commission institute a test phase for providing this information in an XBRL format (such as a voluntary pilot program, similar to what it is currently doing for EDGAR filings)? How long should this test phase last?

Please see our response in section B.6 of part II of our Comment Letter.

2. PROPOSED RULE 17G-2(a)(2)(iii): RECORD OF RATIONALE FOR MATERIAL DEVIATION FROM MODEL OUTPUT

A. Are there certain types of rated products (e.g., corporate debt, municipal bonds) which generally employ a quantitative model as a substantial component of the ratings process? Commenters should identify the types of bonds and a general description of the models used to rate them.

As explained in our response to Question 2 in part 4 of Annex A, MIS believes that the proposed rule should not focus on deviations from model outputs.

B. Should the Commission define in the rule when the divergence from a model would be "material"? Commenters endorsing the adoption of such a definition should provide specific proposals.

As discussed in our response to Question 2 in part 4 of Annex A, we believe that the proposed rule should require NRSROs to make and retain for each current credit rating a record indicating the principal quantitative and qualitative factors considered, and the principal methodologies applied, in determining the rating as well as the rationale for the rating assigned. If the Commission nevertheless decides to adopt the rule as drafted, we believe, for the reasons set out in our response to Question 2 in part 4 of Annex A, that each NRSRO should determine what constitutes a "material divergence" from a rating implied by a quantitative model. We expect that the concept of "material divergence" will vary from sector to sector and methodology to methodology. Accordingly, we doubt that it would be possible for an NRSRO or the Commission to develop a one-size-fits-all definition of "material divergence". Moreover, we believe that the Commission's adoption of a binding interpretation would intrude upon the substance of NRSROs' rating methodologies and practices.

C. Is the hypothetical scenario of the RMBS rating process used to illustrate when a divergence would be material for purposes of the proposed amendment reasonable? For example, is the adjustment of the subordination level from 20% to 19% for a $1 billion loan pool a material divergence? Would a lesser adjustment of the subordination level (e.g., 20% to 19.5%) also be material?

As discussed in more detail in part 4 of Annex A, MIS believes that the proposed recordkeeping requirement should not focus on deviations from the outputs of quantitative models. With respect to the hypothetical scenario set out above, the quantitative outputs that we consider in determining RMBS, or any other, credit rating, are just one factor in our analysis. Consequently, we do not consider the hypothetical scenario set out in the Proposing Release to be an appropriate illustration of how ratings are determined.

D. Are there alternative types of records that may be created or retained by an NRSRO that would allow the Commission to understand when and why an NRSRO's final rating differed materially from the rating implied by the model?

Existing Rule 17g-2(b)(2) requires an NRSRO to retain "Internal records, including non-public information and work papers, used to form the basis of a credit rating" issued by the NRSRO. Accordingly, if an NRSRO typically records the principal quantitative and qualitative factors considered, and the principal methodologies used, in determining a rating as well as the rationale for the rating assigned, that record will fall within the scope of Rule 17g-2(b)(2). It does not appear, however, that the NRSRO is required to make such a record. MIS could easily adapt its documentation to specifically and systematically capture such a record.

3. PROPOSED RULE 17G-5(a)(3) AND (b)(9): DISCLOSURE IN STRUCTURED FINANCE MARKETS

A. Would the information proposed to be required to be disclosed sufficient to permit the determination of an unsolicited credit rating? Conversely, would the proposed amendment require the disclosure of more information than would be necessary to permit the determination of an unsolicited credit rating?

Please see our response in Part I of our Comment Letter.

B. The proposed amendment would require the disclosure of information provided to an NRSRO by the "issuer, underwriter, sponsor, depositor, or trustee" based on the Commission's preliminary belief that these would be the parties relevant to an NRSRO's performance of the ratings process, i.e., that taken together, these are the parties that would provide all relevant information to the NRSRO. Are there other entities that should be included in this category?

As part of the structured finance rating process, MIS may receive information provided by various participants including, among others, those identified in Question B above as well as originators, accountants, due diligence firms, lawyers and monoline insurers for certain transactions. Ultimately, however, the issuer is in control of who provides information and which information is provided to us. This fact reinforces our view that the Commission should focus on determining which categories of information are relevant and material to the investment decision-making process and then clearly place the disclosure obligation on the issuer.

C. Should the Commission provide a "safe harbor" so that an NRSRO that obtained a representation from one or more parties to a transaction to disclose the required information would not be held in violation of the rule if the party did not fulfill its disclosure obligations under the representation?

Yes. Please see our response in section A of part I of our Comment Letter.

D. Should the Commission also require the disclosure of information about the steps, if any, that were taken by the NRSRO, issuer, underwriter, sponsor, depositor, or trustee to verify information about the assets underlying or referenced by the security or money market instrument, or, if no such steps were taken, a disclosure of that fact?

E. Should the Commission also require the disclosure of the results of any steps taken by the NRSRO, issuer, underwriter, sponsor, depositor, or trustee to verify information about the assets underlying or referenced by a structured finance product? Alternatively, should the Commission require a general disclosure of whether any steps were taken to verify the information and, if so, a description of those steps?

We do not object to a requirement that NRSROs describe generally in Exhibit 2 to Form NRSRO the steps, if any, they take to satisfy themselves as to the sufficiency and quality of the information they use in the credit rating process for different broad classes of credit ratings and structured finance asset classes. We believe that this disclosure would be more relevant and helpful to users of our credit ratings than disclosure about the steps we take, or results of the steps we take, to verify information about the assets underlying structured finance products since it is not a part of our role as a CRA to verify the quality of the information we receive.

With respect to a requirement that NRSROs provide such disclosure on a transaction-by-transaction basis, we are concerned that it could contribute to over-reliance on the NRSROs' rating process and a misperception that an NRSRO credit rating constitutes a "seal of approval"

with respect to accuracy of the information disseminated to market participants in connection with the transaction. MIS's credit ratings are opinions about the relative creditworthiness of entities and obligations, not factual statements.

We believe that issuers and other participants in structured finance transactions are better-positioned to describe, on a transaction-by-transaction basis, what steps they have taken to verify information about the assets underlying the offered securities. Furthermore, such verification is implicit in the liability of offering participants with respect to the disclosure materials. Regulation AB also currently requires each party involved in servicing a publicly offered, structured finance transaction to assess and certify periodically its compliance with Regulation AB's servicing criteria. Each servicer must also arrange for a registered, public accounting firm to examine the servicer's operations and deliver an annual attestation regarding the servicer's compliance with the servicing criteria. These certification and examination/attestation requirements could be extended and modified, as appropriate, to apply to one or more of the other participants in the securitization process, such as the originator, sponsor, seller and/or issuer. Certifications and third-party examinations/attestations could enhance market confidence in the information provided by these market participants.

If the Commission nevertheless decides to require NRSROs to provide such disclosure on a transaction-by-transaction basis, we believe the Commission should expressly acknowledge in a note forming part of the rule that NRSROs, unlike underwriters, do not have any statutory duty under federal securities laws to verify any of the information submitted to them in connection with the credit ratings they provide.

F. Would the disclosure of the initial information on the pricing date provide enough time for other NRSROs to determine unsolicited ratings before the securities were sold to investors? If not, would it be appropriate to require that this information be disclosed prior to the pricing date? Alternatively, would it be more appropriate to require NRSROs hired by the arranger to wait a period of calendar or business days (e.g., 2, 4, 10 days) after the asset pool is settled upon by the arranger before issuing the initial credit rating in order to provide other NRSROs with sufficient time to determine an unsolicited rating?

As discussed in part I of our Comment Letter, we believe that the Commission should strike proposed paragraph (a)(3) of Rule 17g-5 and focus instead on revising the disclosure regime for issuers provided for in Regulation AB, Rule 144A and other applicable rules. We have assumed for purposes of this Question that the Commission proceeds as we have recommended and imposes a disclosure obligation on the issuer, with such disclosure having to occur at the times specified by the Commission in proposed paragraph (a)(3). We believe that requiring disclosure of the initial information on the pricing date may not provide enough time for mother CRAs to determine unsolicited ratings before the securities are sold to investors. It likely would take at least a week for a CRA to determine a rating, even in circumstances where the structured finance product is relatively commoditized, the CRA is familiar with the product, and is rating and monitoring a number of similar transactions so that it already has a comprehensive, up-to-date view of credit trends affecting the asset class. Even then, the lead analyst might spend a week analyzing the data before scheduling a rating committee and it could take several days for appropriate participants with the requisite experience and diversity of views to meet. The rating committee might also adjourn after asking the lead analyst to consider and then present to the rating committee further analysis. It could take much longer for a CRA to determine a credit rating for a novel product or a product with which it is unfamiliar.

However, we also believe it would be inappropriate for the Commission to prohibit an NRSRO hired by the arranger to wait for a prescribed period after the asset pool is settled upon before issuing an initial credit rating. Imposing such a condition, especially in light of the fact that a similar condition would not apply to CRAs that had not been hired to rate the transaction, would be a harsh and unwarranted imposition on the NRSRO's freedom of speech.[31]

G. Do NRSROs obtain information about the underlying assets of structured products – particularly in the surveillance process – from third-parties such as vendors rather than from issuers, underwriters, sponsors, or trustees? If so, would it be necessary to require the disclosure of this information as proposed or can the goals of the proposed amendments in promoting unsolicited ratings be achieved under current practices insomuch as the information necessary for surveillance can be obtained from third-party vendors, albeit for a fee?

Typically, MIS does not receive non-public information about the assets underlying structured products directly from third parties such as vendors with whom MIS has a direct relationship. We may receive such information, however, indirectly from issuers, arrangers or their agents. This reflects the fact that it is the issuer who ultimately determines who provides information to MIS and which information is provided. This is one of the reasons why we recommend that the Commission strike proposed paragraph (a)(3) of Rule 17g-5 and focus instead on revising the existing disclosure regime for structured finance issuers contained Regulation AB, Rule 144A and, as appropriate, other rules. If there is information about the underlying assets that the Commission believes should be disclosed, the Commission should require the issuer to disclose it.

H. Does the information provided to NRSROs by issuers, underwriters, sponsors, depositors, or trustees about assets underlying structured products (e.g., mortgage loans, home equity loans, consumer loans, credit card receivables) commonly include personal identifying information about individuals such as names, social security numbers, addresses, and telephone numbers? If so, are there practical ways to ensure that this information is not disclosed?

Typically, MIS does not receive this type of information. We believe that the appropriate way to prevent this information from being disclosed is for the Commission to amend Regulation AB, Rule 144A and, as appropriate, other applicable rules to specify the types of information that should be (and should not be) broadly disseminated in connection with structured finance transactions.

I. Does any of the information provided to NRSROs by issuers, underwriters, sponsors, depositors, or trustees about assets underlying structured products contain proprietary information?

MIS treats all information that we receive from issuers, arrangers and their agents as confidential, unless it clearly constitutes publicly available information (such as a public filing or published article or study). The MIS Code also contains several provisions dealing specifically with the treatment of confidential information. Accordingly, we rarely receive requests on behalf of issuers to treat particular types of information as proprietary and confidential.

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[31] Such a condition also could adversely affect the timing of an offering and could cause an issuer to choose between obtaining a rating and pricing a transaction during a favorable market window.

J. Do we need to give more guidance on the relationship between the proposed disclosure requirements regarding information about the underlying assets provided to, and used by, the NRSRO to perform ratings surveillance and the requirements of Regulation FD?

If the Commission concludes that additional disclosures to the market are appropriate, we believe that it should amend Regulation AB and Rule 144A to prescribe the types of information that should be disclosed by issuers. Regulation FD also could be amended to supplement this disclosure regime. Regulation FD generally requires simultaneous public disclosure whenever an issuer (as that term is defined for purposes of Regulation FD), or a person acting on its behalf, discloses any material nonpublic information regarding that issuer or its securities, but there is an exception for information provided to CRAs that publish their ratings. The exception under Rule 100(b)(2)(iii) could be modified to apply only until the information must be disclosed under the proposed rule. This would help ensure that issuers disclose such information publicly by making them directly responsible under the securities laws rather than pursuant to a contractual obligation with the NRSRO rating their securities.

K. The proposed disclosure requirements regarding information about the underlying assets provided to, and used by, the NRSRO to perform ratings surveillance may be the same as the information required to be disclosed on Form 10-D for so long as the issuer has an Exchange Act reporting obligation. Given that the Form 10-D reporting obligation is typically suspended for most asset-backed issuers after the first year of reporting, does the proposed disclosure requirement raise any issues regarding Exchange Act reporting?

As discussed in more detail in part I of our Comment Letter, a disclosure standard based on the vague standard of what is "used" by an NRSRO to determine a rating could result in "data dumping", instead of the orderly and methodical presentation of relevant information required elsewhere under the securities laws. Accordingly, we recommend that the Commission specify precisely in Regulation AB, Rule 144A and, as appropriate, other applicable rules and forms which categories of information should be disclosed by issuers in connection with an offering and on an ongoing basis.

L. ABS informational and computation materials, as defined in Item 1101 of Regulation AB, can include, among other things, factual information regarding the pool assets underlying the asset-backed securities, including origination, acquisition and pool selection criteria, information regarding any prefunding or revolving period applicable to the offering, information regarding significant obligors, data regarding the contractual and related characteristics of the underlying pool assets (e.g., weighted average coupon, weighted average maturity, delinquency and loss information and geographic distribution) and other factual information concerning the parameters of the asset pool appropriate to the nature of the underlying assets, such as the type of assets comprising the pool and the programs under which the loans were originated. As noted above, the Commission believes that at least some of the proposed Paragraph (a)(3) Information could fall within this category and therefore constitute ABS informational and computational materials. Since there may be a wide variety of information that is provided to an NRSRO, it is not clear that all information provided would fit within the definition of ABS informational and computation materials, or in the various categories of free writing prospectus. Should the Commission provide additional interpretation regarding what types of material that could be provided and would be required to be disclosed to fit within this category? Is there information that is likely to be provided and disclosed that does not appear to fit within these definitions? Should the Commission instead revise the definitions to specifically include the information required to be disclosed?

We believe that the Commission's goal would be better achieved by broadening and/or clarifying Regulation AB to require more detailed disclosure by issuers of information relating to structured finance products and/or the underlying assets. We believe that specific guidance under Regulation AB, which focuses on disclosure requirements for issuers, is a better mechanism to address the Commission's goal of ensuring that sufficient, relevant information reaches investors and other CRAs to allow for more transparent offerings and ratings.

M. Is there any need for the Commission to revise Securities Act Rules 426 or 433 to clarify when the materials need to be filed?

To answer this question, it is useful to contrast the "everything that is used by a NRSRO must be disclosed" regime contained in proposed paragraph (a)(3) of Rule 17g-5 with the tailored disclosure requirements in Rules 426 and 433 under the Securities Act. Under Rule 426, ABS information and computational material is required to be disclosed in certain circumstances. Item 1101 of Regulation AB defines ABS information and computational material with specificity to include well-defined factual information regarding offered, asset-backed securities and underlying assets; the identities of key transaction participants; static pool data; and certain other statistical information related to the offering. Additionally, Rule 426 specifies when such ABS information and computational material need not be filed, such as when it relates to abandoned structures or is furnished to prospective investors that have not indicated to the issuer or underwriter their intention to purchase, prior to the time the final terms of an offering have been set. Similarly, Rule 433 precisely defines a "free writing prospectus" to include "any written communication as defined in [the Securities Act Rules] that constitutes an offer to sell or a solicitation of an offer to buy the securities relating to a registered offering that is used after the registration statement in respect of the offering is filed…." Rule 433 also contains clear exceptions specifying when this material need not be filed, such as when it contains a description of terms of the offered securities that do not reflect the final terms.

By contrast, the "everything that is used by an NRSRO must be disclosed" regime is an indiscriminate disclosure requirement. It is neither based on specific line item disclosure nor offering materials. Moreover, it requires far more disclosure than what has been required historically of issuers. As we discuss in more detail in part I of our Comment Letter, we believe the approach to disclosure taken in proposed paragraph (a)(3) of Rule 17g-5 is fundamentally at variance with the established principles of disclosure under federal securities laws. Instead of making the issuer the party ultimately responsible for ensuring that complete, accurate, material and relevant information is provided to investors, the proposed rule would make NRSROs and all other providers of information used in the rating process responsible for publicly disclosing that information. We think this approach is fundamentally misguided, and it is therefore no surprise to us that it gives rise to timing concerns under Rules 426 and 433 as well.

The timing concerns could be resolved by specifying that any information made publicly available under paragraph (a)(3) in accordance with the specific timing requirements of the new proposed rule would not constitute information required to be filed under Rules 426 and 433. However, we consider the new proposed disclosure regime to be fundamentally flawed. Consequently, we recommend that the Commission amend Rule 426 (and Regulation AB) to specify what additional information should be provided by issuers, rather than to create a parallel disclosure regime involving multiple persons that the NRSRO cannot control.

N. Are there any additional requirements in Regulation AB or under the Securities Act that are implicated by the proposed amendments? Is there any information that would typically need to be disclosed under this proposed amendment that is not already generally disclosed in filings with the Commission?

As discussed above, we believe it is inappropriate to create a disclosure regime for structured finance products based on whether NRSROs use that information in the rating process. We also expect that such a standard, if adopted, will be interpreted broadly and therefore require disclosure of far more information than currently is required to be disclosed under securities laws. We recommend instead that the Commission amend Regulation AB, Rule 144A and other applicable rules to specify precisely which categories of information should be disclosed by an issuer or its agents in an offering and on an ongoing basis.

O. Should the Commission amend Regulation AB to require that the Paragraph (a)(3) Information be disclosed?

Please see our response to Question L above.

P. Are there other parties besides credit rating agencies and investors that should be eligible to access Paragraph (a)(3) Information in the context of a private offering without raising issues of general solicitation?

Q. Is expanding the categories of parties who can access the information that would be contained in the proposed Paragraph (a)(3) Information consistent with the purposes of the Securities Act?

R. Is there any Paragraph (a)(3) Information that should remain accessible only to credit rating agencies and investors, rather than, as proposed, disclosed to the public on the business day after the offering has closed?

S. Should the requirement to publicly disclose the Paragraph (a)(3) Information on the first business day after the offering has closed also permit the NRSRO, depositor, etc. to omit deal-specific information relating to the transaction such that only "generic" information is provided to the public?

T. Should any of the foregoing guidance regarding the use of Paragraph (a)(3) Information be codified?

MIS does not believe that expanding the class of the parties who will have access to the information that would be contained in the proposed Paragraph (a)(3) Information would be consistent with the purpose of the Securities Act. The purposes of the Securities Act include protecting investors by requiring issuers to disclose sufficient, relevant information to enable investors to make informed investment decisions. We understand that the purpose of proposed paragraph (a)(3) is to increase the availability of diverse rating opinions by facilitating unsolicited ratings. Given these two sets of objectives, it is unclear how disclosure to parties other than CRAs and investors would be helpful.

4. PROPOSED RULE 17G-5(c)(7): RECEIVING GIFTS

A. Is the proposed $25 aggregate value an appropriate threshold for incidentals provided at meetings, or should a higher or lower threshold be applied?

Please see our response to Question 1 in part 3 of Annex A.

B. Should the Commission adopt a recordkeeping requirement with respect to the receipt of gifts by analysts and persons responsible for approving credit ratings in addition to the prohibition? For example, the Commission could require an NRSRO to document for each gift the identity of the person providing the gift, the recipient, and the nature of the gift.

MIS would not object to the Commission's adoption of a rule requiring an NRSRO to keep a record documenting the identity of the person providing the gift, the recipient and the nature of the gift, provided that the receipt of meals and refreshments received in the course of normal business, such as meetings and conferences, would not have to be recorded.

5. PROPOSED RULE 17G-7: CREDIT RATING REPORTS

A. Should the rule allow the use of a common set of symbols only if the NRSRO determines additional types of ratings to distinguish the different risk characteristics of the different types of obligors and debt securities? For example, the rule could require the determination of ratings to distinguish the potential volatility of the credit ratings of different classes of obligors and debt securities or the differing levels of market and liquidity risk associated with different classes of debt securities. Would such disclosures raise any concerns regarding liability if they were found to be deficient?

Please see our response to Question 2 in section 11 of Annex A above.

6. PROPOSED AMENDMENTS TO INSTRUCTIONS FOR EXHIBIT 1 OF FORM NRSRO

A. Should the Commission require performance statistics in a more granular form than by class of credit ratings?

MIS does not object in principle to the Commission's proposal requiring performance statistics on an asset class-by-asset class basis for structured finance products. We recommend, however, that the Commission define the disclosure requirement in such a way that the performance data that NRSROs are required to provide remain statistically significant. For example, it might be appropriate to call for performance data for the U.S. asset-backed securities market as a whole (but not for a subset of this market, such as airplane lease securitizations).

It also should be noted that NRSROs do not necessarily classify transactions in the same way and may change their classifications over time. For example, one NRSRO may classify a sub-category of transactions as RMBS while another NRSRO may classify them as ABS. This may reduce the comparability of performance statistics. Nevertheless, we do not believe it would be appropriate for the Commission to prescribe how various types of transactions should be classified. Instead, we believe that this variability in the classification of transactions can be addressed through appropriate disclosure by NRSROs (*e.g.* explanations of which transactions fall within particular asset classes) in the performance statistics they provide on Form NRSRO.

B. Should the Commission prescribe different time periods for the short, medium, and long term statistics than 1, 3, and 10 years, respectively. For example, should the periods be 6 months, 2 years and 7 years or 2, 5, and 15 years or some other set of time periods?

MIS does not object to the Commission's proposal to prescribe one, three and ten year time periods, or any other time periods, for the prescribed performance statistics.

ANNEX C: ESTIMATED RECORDKEEPING BURDENS AND OTHER COSTS

To assist the Commission in its evaluation of the incremental benefits and costs of the Proposed Rules, we have conducted preliminary assessments of a number of the anticipated, incremental recordkeeping burdens and other costs that MIS would incur if the Proposed Amendments were adopted as drafted. We emphasize, however, that we have not had sufficient time to thoroughly assess and quantify the potential impact of the Proposed Amendments and that the estimates set out below are based upon incomplete information. We would appreciate an opportunity to provide further feedback to the Commission once we complete our evaluation.

(1) PROPOSED AMENDMENTS TO INSTRUCTIONS FOR FORM NRSRO

(a) Would the proposed additional disclosure requirements increase the [collection of information] burden hours from the amount currently budgeted for Rule 17g-1 and Form NRSRO?

We disagree with the Commission's conclusion that there will be no additional, one-time or ongoing collection of information costs for NRSROs to provide the additional information called for in Exhibit 2 of Form NRSRO. For example, each of the practices specified above in the new instructions for Exhibit 2 is likely to vary to some extent by rating category and asset class. Accordingly, we would need to conduct a survey of our practices, synthesize and summarize the results of our survey, and incorporate that information into Exhibit 2. We estimate that it would take at least 100 hours to complete this task on a global basis and that the task would involve compliance personnel as well as senior analysts and their supervisors.[32]

Also, on an ongoing basis, we will have to develop mechanisms to collect data about any significant change in practices and introduce compliance procedures (*e.g.* such as periodic assessments of whether our practices conform to the general descriptions incorporated into Exhibit 2). We expect that we would spend, on average, at least an additional 24 hours per year to collect such information and another 12 hours per year to incorporate descriptions of the changes into our annual Form NRSRO and have the revised text reviewed and certified. In addition to the estimated 36 hours associated with this new collection of information burden, we estimate that we have to spend an additional 24 hours conducting compliance assessments. We do not consider, however, such one-time and ongoing compliance costs to be excessive.[33]

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[32] We estimate that currently, it already takes us approximately 50 hours to update and check the list of methodologies included in Exhibit 2. By contrast, the Commission estimated that it would take only 10 hours, on average, each year for an NRSRO to update its entire Form NRSRO.

[33] We believe, however, that the Commission significantly under-estimated some of the ongoing compliance costs associated with the Existing Rules. For example, we believe that the average, aggregate annual burden of preparing two amendments to Form NRSRO (25 hours each) and an annual certification on Form NRSRO (10 hours) exceeds 60 hours. In MIS's experience, a more accurate estimate would be 10-30 hours per amendment (depending on the scope of the amendment) and 80 hours to revise the annual Form NRSRO and have it certified. Our estimate takes into account the time needed to collect and assess information, revise and update our Form NRSRO and have the proposed revisions reviewed and approved by managers and, in some instances, senior executives.

(2) Proposed Amendments to Rule 17g-2

(a) Are the estimates that these amendments would result in an increase to the current total one-time and annual recordkeeping burdens of 10% and 5% accurate? If not, should they be higher or lower?

(b) What would be the costs to an NRSRO to provide data in the XBRL format? Would there be a cost burden on smaller NRSROs? Is there another format that would cost less but still allow investors and analysts to easily download and analyze the data?

(c) Are the estimates that the requirement to make records of rating actions publicly available in an XBRL Interactive Data File would result in an increased one-time [collection of information] burden for each NRSRO of approximately 30 hours to publicly disclose the history of its rating actions for each credit rating in an XBRL Interactive Data File and, thereafter, 10 hours per year to update this information accurate? If not, should they be higher or lower?

(d) Is the estimate that the NRSROs would incur no additional costs (or that any additional costs would be de minimis) to update recordkeeping systems to comply with the proposed new recordkeeping requirements accurate? If not, what would the additional costs be?

We understand that the Commission has estimated that the proposed amendments to Rule 17g-2 would result in an increase in the average, one-time and ongoing recordkeeping burdens for an NRSRO of 30 hours and 13 hours, respectively. We believe that the Commission has significantly under-estimated the initial and ongoing recordkeeping burdens associated with its proposed changes to NRSROs' recordkeeping requirements.

XBRL Rating Actions Database: We believe that the Commission has significantly under-estimated the initial and ongoing costs associated with providing the required data in XBRL format.[34] While we already maintain databases that contain most of the information we would be required to include in the data file, a number of steps would have to be taken to provide this data in a format such as XBRL. We have described some of these steps below to assist the Commission in revising its cost estimates.

First, we anticipate that the process of developing and agreeing upon the taxonomy and tags for the data file would take at least several hundred hours of our time, expended over several months to a year or more. XBRL is a standard that is being developed to communicate financial information. While some tags that have already been developed in XBRL or another XML-based standard likely could be adapted for certain fields in a rating actions database (*e.g.* tags to identify rated entities), a number of other tags would have to be developed and agreed.

Hypothetically, if we developed the required taxonomy and tags on a stand-alone basis (*i.e.* without needing to consult others, agree on standards or obtain Commission approval for the tags), we estimate that it would take an XBRL specialist familiar with MIS's data and ratings at least 5-10 working days. In reality, of course, we would work with other NRSROs to develop the tags. We note that those developing and approving the tags need to be very careful that the tags do not inadvertently impinge upon the substance of the credit ratings themselves (*e.g.* by imposing common meanings on the rating symbols). Consequently, the process of developing and agreeing upon tags is likely to take longer than might otherwise be expected. Also, since the

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[34] The Commission has estimated that, on average, an NRSRO would spend approximately 30 hours to disclose publicly the required ratings history information in an XBRL format and, thereafter, 10 hours per year to update the data file. See Proposing Release at 36238 and 36245.

proposed rule is intended to facilitate easier access to NRSROs' performance data, we believe that it would be important to consult with users of our credit ratings as part of the process. Conducting such a consultation process could take several weeks of effort, expended over the course of several months. Finally, we would need to seek the Commission's approval of the taxonomy and tags.

Once the taxonomy and tags for the ratings history data had been developed and agreed to, we likely would have to:

- Determine which IT systems within MCO to source the data from, given the required fields, frequency of updates and output format;
- Evaluate the data source(s) for errors and/or missing data and determine how to correct the data source(s);
- Map the data source(s) to the desired output format;
- Build an automated process to extract the data and transform it to the required output format; and
- Establish monitoring and validation systems and procedures to maintain the integrity of the output data.

Ongoing maintenance costs would depend on variables such as where the data would be hosted (*e.g.* on moodys.com or an external website) and on support requirements. If the data were hosted on moodys.com, we could incur significant costs for additional hardware and associated support personnel to support increased traffic to our website, especially if the Commission required NRSROs to make the data available for free and required the database to be updated daily. If the data were to be hosted on an external website and we were held responsible for ensuring that the external website had the correct data, we would incur significant costs to check and correct continuously any errors that occurred with respect to the transmission, uploading and maintenance of data on the external website. Regardless of where the data file was hosted, we would need to know whether we were responsible for assisting consumers of the data who had questions or problems. We could incur significant costs in responding to user requests. Finally, the automated process for extracting the data would need regular maintenance, especially when changes were made to our systems. Even assuming that we had no responsibility to provide ongoing user support, the burden associated with ongoing maintenance could easily exceed two months per year.

Finally, we note that the Commission's estimate of the costs associated with this proposal does not include the cost of the foregone revenues an NRSRO receives, or might receive, for subscription products that contain historical rating data. While we have not had sufficient time to provide an estimate of the revenue implications for our business, we believe that these foregone revenues could be very significant for NRSROs and that the Commission should consider the revenue implications when it evaluates of the costs and benefits of the proposed rule. We would be happy to advise the Commission of our conclusion once we have fully assessed the potential impact of this proposal on our revenues.

Record of Rationale for Material Deviation from Model Output: We also believe that the Commission has significantly under-estimated the initial and ongoing recordkeeping burdens and compliance associated with proposed rule 17g-2(a)(2)(iii). To implement this rule as drafted, MIS would have to conduct a review of all the quantitative models it uses in

determining ratings and decide which, if any of them, constituted a "substantial component" in determining ratings. Such an exercise easily could take 150 hours or more and involve credit analyst supervisors, chief credit officers, our credit policy team and senior management. In addition, we would have to draft a policy regarding the recordkeeping practice, amend the schedules for rating committee memoranda and modify our systems to ensure that the absence of such a record was flagged as a deficiency. These processes would require the input and approval of the individuals mentioned above, as well as compliance staff, the legal department and our IT department. It could easily take 200 hundred hours or more to complete these tasks. If the Commission decides to adopt the revisions to proposed rule 17g-2(a)(2)(iii) that we have recommended, we would not have to conduct the survey of models referred to above but would still spend at least 200 hours or more to develop the policy, amend the schedules and modify our systems. Finally, we would need to develop compliance procedures and a training program for this requirement and train all of our analysts (as well as key administrative staff). We estimate that the one-time compliance burden associated with the development of the compliance procedures and this training requirement could exceed 1,500 hours (*e.g.* one hour per individual who participates in the training program, plus the time required to develop the training module).

On an ongoing basis, we estimate that, for each rating committee where such a record was required, it likely would take at least 60-90 minutes to draft the required record, have it reviewed and approved by the rating committee chair and file it in our systems. In addition to this recordkeeping burden, we also would have to introduce compliance procedures (such as periodic assessments of whether our practices conform to our policy), train new staff and provide refresher courses to existing staff. We estimate that compliance reviews might take 40-80 hours per year and that we would spend at least 200 hours per year on training.

If the Commission decides to adopt the revisions to proposed rule 17g-2(a)(2)(iii) that we have recommended, we expect that the per-rating committee recordkeeping burden would be similar (but the record would have to be created for each rating committee so that the aggregate recordkeeping burden per year would be higher). The compliance burden would be similar.

We believe that the compliance costs of the Commission's proposed rule as drafted are unjustified because, for the reasons outlined in Part 4 of Annex A: (i) the proposed record would not capture the nature of the rating committee process; and (ii) the proposed recordkeeping requirement could create disincentives for analysts and rating committees to consider qualitative factors and exercise appropriate judgment in determining ratings. While the compliance costs of implementing the recordkeeping requirement we have recommended are also significant, we would not consider such costs to be excessive in light of the expected benefits.

Retain Communications Containing Complaints about Analysts: We believe that the Commission has under-estimated the one-time and ongoing recordkeeping burdens and compliance costs associated with proposed rule 17g-2(b)(8). To implement the proposed rule, we would have to draft a policy and have it approved, as well as modify our systems to capture the required record. We estimate that it could take 100 hours or more to complete these tasks. In addition to these recordkeeping burdens, we would to develop compliance procedures and a training module for the proposed rule. We estimate that the development of compliance procedures and a training module would take at least 1,500 hours (taking into account the time spent by each individual who is required to attend training). On an ongoing basis, we would need to follow up on complaints and document our follow-up procedures, conduct compliance reviews, train new staff and provide refresher courses. We estimate that follow-up procedures

and documentation per complaint typically could range from 10-100 hours, compliance reviews might take 40-80 hours per year and that we would spend at least 150 hours per year on training.

(3) PROPOSED AMENDMENTS TO RULE 17G-5

(a) Would the proposed amendments to paragraph (c) of Rule 17g-5 impose training and restructuring costs?

Rating Recommendations: If the Commission revises proposed paragraph (c)(5) and introduces a new paragraph (b)(11) as we have suggested, we believe that the compliance costs associated with implementing the amended rule would be an appropriate cost of business for an NRSRO. NRSROs likely would have to: (i) enhance the training programs for their analytical staff; (ii) put in place, or reinforce, robust information fire-wall policies; and (iii) put in place measures to assess compliance with such information firewalls.

Since no enterprise within the MCO family currently engages in such activities, it is unlikely that implementing the broadly worded prohibition in the proposed rule as originally drafted would cause the MCO family to incur significant restructuring or training costs. As discussed in more detail in our response to Question 2 in part 1.A of Annex A, however, we believe that a rule prohibiting non-NRSRO affiliates from providing recommendations, advice or consulting services to issuers is not narrowly tailored to meet the Rating Agency Act's objectives and, therefore, over-reaches the Commission's rule-making authority.

Fee Discussions: If the Commission revises proposed paragraph (c)(6) as we have recommended, then we believe that this provision would not impose significant, additional training and restructuring costs for MIS.

If, however, the Commission adopts paragraph (c)(6) as originally drafted and MIS is expected to exclude senior managers from participating in the credit rating process as needed, our rating quality likely will suffer due to the loss of valuable input currently provided by senior management as part of process of approving methodologies. Likewise, if MIS senior management were prohibited from providing their views on fee schedules or other business-related matters, it would significantly hamper our ability to operate our business. Moreover, we believe that implementation of paragraph (c)(6) as originally drafted would create an artificial dissociation of credit analysis from credit markets.

(b) Would the proposed amendments to paragraph (c) of Rule 17g-5 impose personnel costs?

Rating Recommendations: If the Commission revises proposed paragraph (c)(5) and introduces a new paragraph (b)(11) as we have suggested, we believe that the personnel costs associated with implementing the new rules would be minimal. With respect to the potential impact on MCO if the proposed rule is implemented as drafted, please see our response to Question 3(a) above.

Fee Discussions: If the Commission revises proposed paragraph (c)(6) as we have recommended, then we believe that this provision would not impose significant, additional training and restructuring costs for MIS or other NRSROs that comply with the IOSCO Code. If, however, the Commission adopts paragraph (c)(6) as originally drafted, we expect to incur significant, additional personnel costs. For example, we likely would have to create a number of new positions for senior chief credit officers so that drafting, approving and implementing methodologies could be handled exclusively by individuals with no involvement in the business

of running an NRSRO. It also would be necessary to create additional, senior positions in our issuer and intermediary relations team for individuals, such as former analysts, who were deeply familiar with the technicalities of our methodologies and procedures and could assist with fee negotiations. On an ongoing basis, we would have to transfer former credit analysts to this team regularly so that this team retained sufficient and current technical knowledge to handle fees.

(c) Would the proposed amendments to paragraph (c) of Rule 17g-5 impose any additional costs on an NRSRO that is part of a large conglomerate related to monitoring the business activities of persons associated with the NRSRO, such as affiliates located in other countries, to comply with the proposed requirement?

Rating Recommendations*:* If the Commission revises proposed paragraph (c)(5) and introduces a new paragraph (b)(11) as we have suggested, we believe that the costs associated with monitoring the activities of CRA affiliates in other countries would be an appropriate cost for an NRSRO to bear. With respect to the potential impact on MCO if the proposed rule is implemented as drafted, please see our response to Question (3)(a) above.

(4) PROPOSED RULE 17G-7

(a) Is the Commission incorrect in its belief that NRSROs would opt to use a different rating symbol rather than to publish a report with each structured product rating? If so, what percentage of NRSROs would be likely to opt to publish a report?

From our perspective, what is of paramount importance is that we can express our opinions about the relative creditworthiness of securities and obligors in a manner that users of our credit ratings find helpful. The associated symbol system through which our opinions are made available is of secondary importance.

Regardless of the costs, we would be reluctant to choose an option that respondents to our RFC have indicated would exacerbate existing liquidity and market confidence concerns. Thus, if we had to choose between a different symbol set and publishing an accompanying report,[35] at this time and based on existing market sentiment, we would publish a report.

Based on the commentary in the Proposing Release, it is difficult for MIS estimate the recordkeeping burden and other costs associated with providing such reports because there are a number of unresolved issues regarding the Commission's proposal. For example, we would need clarity on the following questions, among others:

- Would the reports be required only in respect of credit ratings assigned in the future or would the requirement to provide reports be applied retroactively?
- Would the reports be required to accompany or co-exist with the ratings? In other words, if MIS provided data feeds of our ratings to investors, how would these reports be transmitted with the structured ratings for the purposes of the data feed?
- Pursuant to proposed rule17g-2(8), certain ratings data would have to be provided in an electronic data file that uses machine-readable code such as XBRL. Would the reports be put into this interactive data base? If so, how?

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[35] As noted earlier, we question the Commission's authority to impose such an alternative.

- At present, our ratings are displayed by other data service providers, such as Bloomberg, and there is no specific area or field for the proposed reports. How would these service providers accommodate the reports? If they did not accommodate the reports, would MIS be considered to have violated Rule 17g-7? As discussed above, MIS is concerned about any proposed rules that expose NRSROs to liability risk for the conduct of third parties that the NRSRO does not control.

(b) Would there be costs in addition to those identified above, such as costs arising from systems changes and restructuring business practices to account for the new reporting requirement?

If the Commission adopts Rule 17g-7 and MIS decides to comply with the rule by using different symbols for credit ratings of Structured Products, MIS and its parent company, MCO, will significant incur costs. Among other things, we would have to make changes to a number of systems, products and the data feeds between them and use both internal resources and consulting services. We estimate that it would take approximately eight to thirteen months at a total cost of approximately $1.8 to $2.9 million. As indicated in our response to question (4)(a) above, we would need clarity on a number of issues before we could estimate the systems costs and other costs associated with providing the report referred to in proposed rule 17g-7.