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December 14, 2009

By Electronic Mail

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

Re: Credit Ratings Disclosure (File No. S7-24-09) (the "Release")

Dear Ms Murphy:

Moody's Investors Service ("**MIS**") appreciates the opportunity to provide comments to the Securities and Exchange Commission ("**Commission**") on the proposed amendments to rules ("**Proposed Rules**") that would require issuers to disclose information about credit ratings and credit rating agencies ("**CRAs**") in registration statements and on certain forms. In a separate letter ("**Related Comment Letter**"), we are also submitting comments on the *Concept Release on Possible Rescission of Rule 436(g) under the Securities Act of 1933* ("**Concept Release**").

The Commission has stated that the Proposed Rules are intended to reduce undue reliance on credit ratings by enhancing investors' ability to place ratings in their proper context, understand the appropriate uses of ratings, and appreciate the factors that affect the reliability of specific ratings. We agree with these objectives but believe that the Proposed Rules contradict them. We have summarized our principal concerns and alternative recommendations below:

- ***Commission rules should address the causes, rather than the symptoms, of potential over-reliance on ratings.*** While credit ratings can be useful in the investment decision-making process, they are simply one of many tools available. However, the widespread regulatory use of ratings and gaps in disclosure regimes (*e.g.*, for structured finance products), create conditions in which market participants may over-emphasize ratings. The Proposed Rules would mandate disclosure about ratings in structured finance markets, while key information upon which those ratings are based remains exempt from public disclosure. Adopting the Proposed Rules would perpetuate and exacerbate this artificial emphasis on ratings. Instead, the Commission should update the mandatory disclosure regime for structured finance products so that market participants can develop their own informed opinions about credit risk based on publicly available information. It also should eliminate or substantially reduce its use of ratings-based criteria in its rules.

- ***A materiality test focusing on disclosure of credit risks is more appropriate than tests focusing on whether the rating is "used" or "solicited".*** If the Proposed Rules are adopted, an issuer of a debt

security will have to disclose information about credit ratings that it uses in connection with the registered offering. "Used" ratings are most likely to be solicited ratings. The issuer also will have to disclose information about ratings that it solicited but chose not to use ("**Unused, Solicited Ratings**"). The combined effect of these proposals is to suggest that issuer-paid, solicited ratings are material, while investor-paid or other unsolicited ratings that are "unused" are not. This approach is likely to reinforce the issuer-pays model (since the ratings the issuer pays for are most likely to be used and therefore disclosed) and a new variant of rating shopping (since the issuer will be motivated to avoid formally soliciting ratings from CRAs that it fears may have more conservative views). Instead, issuers and investors should be encouraged to focus on information that is truly material, such as credit risk and other material risks and uncertainties that currently must be disclosed under existing Commission rules. In particular, we believe that issuers, and ultimately investors, would benefit if the Commission provided enhanced guidance about credit risk focusing on "risk factors", known trends and uncertainties, and what constitutes "material information" that should be disclosed pursuant to Rule 408 of Regulation C.[1]

- ***Mandating disclosure about Unused, Solicited ratings will not discourage rating shopping or provide meaningful information to investors about ratings quality.*** Even if issuers are required to disclose Unused, Solicited Ratings, the ability to work around the rule will exist. Rating shopping will still occur, with the added risk that the existence of the disclosure rule could leave investors with the mistaken understanding that shopping has not taken place. Furthermore, mere disclosure of Unused, Solicited Ratings will not tell the investor anything about the reliability of used and unused ratings. This is because there are many reasons why an issuer might choose one rating over another, and these reasons will not necessarily be disclosed. By contrast, enhancing the mandatory structured finance disclosure regime will make it more difficult for issuers to shop for ratings because CRAs and other market participants will have access to the information needed to form and publish their own opinions.
- ***The proposed disclosure regime could jeopardize the independence of the rating process.*** Requiring issuers to disclose the rating and non-rating fees paid to CRAs and their affiliates would undermine the firewalls many CRAs have established to bolster analytical independence. The Commission and other authorities have stressed the importance of insulating rating analysts and rating committees from commercial influences. Compiling and publicly disclosing fee information will expose analysts and rating committees to more commercial information about rated issuers than they ever had before. Also, requiring detailed disclosure about ratings and CRAs in the registration statement could lead investors to think that CRAs are participants in the offering process, which is inconsistent with their intended and expected role as impartial commentators.

For these reasons, we believe the Commission should not adopt the Proposed Rules. Instead, we urge the Commission to first address the conditions in the regulatory environment (*i.e.*, gaps in the disclosure regime for structured finance products and regulatory use of ratings) that create incentives for market participants to over-emphasize credit ratings. Then, the Commission could adopt guidance outlining: (i) the circumstances in which it believes that enhanced disclosure about credit risk is likely to constitute material information that should be disclosed in the registration statement; and (ii) the

[1] Rule 408 requires an issuer to disclose "... such further material information, if any, as may be necessary to make the required statements [in the registration statement], in light of the circumstances in which they are made, not misleading."

information that likely would be considered material if an issuer were required to, or chose to, disclose a credit rating in the registration statement. Subject to the caveats outlined in the Annex,[2] MIS would not object to guidance stating that, if an issuer discloses a credit rating in a registration statement, it also should disclose:

- the identity of the CRA whose credit rating is disclosed, whether it is an NRSRO and its website address;
- the identity of the person who paid for the credit rating;
- a general description of the types of any non-rating services the CRA or its CRA affiliates provided to the issuer or its affiliates;
- a disclaimer about the limitations of credit ratings, the fact that a CRA can change or withdraw a rating at any time, and the fact that an NRSRO must disclose in its Form NRSRO the nature of the conflicts it faces; and
- the differences between the terms of the security as considered or assumed by the CRA and those actually offered or marketed to prospective investors.

The issuer and underwriter should not face liability for such disclosures except to the extent they present the required information inaccurately (*e.g.*, disclosing that the securities received a Aaa rating when in fact they received a Aa rating) and/or fail to include the required information. As we discuss in more detail in the Related Comment Letter, Rule 436(g) should not be rescinded and CRAs should not be exposed to liability in respect of an issuer's disclosures about credit ratings.

In the attached Annex, we provide a more detailed analysis of the Proposed Rules.

Once again, we appreciate the opportunity to comment on the Release. 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

[2] See footnote 8.

Annex - Detailed Analysis

The Commission believes that the Proposed Rules will help reduce undue reliance on credit ratings by providing investors with information about what a credit rating is, and is not, and other information bearing on the rating's reliability so that the rating can be placed in its proper context. In particular, the Commission is concerned that investors may not:

- be provided with sufficient information to understand the scope or meaning of ratings used to market securities in registered offerings;
- be receiving even basic information about what the Commission considers to be a potentially key element of their investment and voting decisions (*i.e.*, a security's credit rating and/or changes in that rating);
- have access to information allowing them to appreciate fully the potential conflicts of interest faced by CRAs and how these conflicts may have an impact on ratings;
- have been informed about the practice of "rating shopping"; and
- be routinely monitoring CRA press releases and therefore may not know that a rating has been changed or withdrawn.

In Part A below, we discuss the limited role of credit ratings in financial markets and suggest that a "materiality" test for disclosure is more appropriate than tests focusing on whether a rating is "used" or "solicited". We also discuss how regulatory use of credit ratings and gaps in the disclosure regime for structured finance products create incentives for market participants to over-emphasize ratings and that the Proposed Rules would aggravate this problem. In Part B, we discuss how situating disclosures about credit ratings in the registration statement could make it harder, not easier, for investors to properly contextualize credit ratings. Finally, in Part C, we explain how adopting the Proposed Rules likely would have undesirable consequences, such as undermining the independence of the rating process and competition based on ratings quality, reducing the amount of information available to the market, and making the capital-raising and capital allocation processes less efficient and more costly.

A. Commission Rules Should Treat the Causes, Rather than the Symptoms, of Potential Over-Reliance on Credit Ratings

1. Limited Role of Credit Ratings in Financial Markets

CRAs occupy a narrow niche in the information industry. We express opinions about the relative creditworthiness of entities, credit commitments, and debt or debt-like securities and thereby help to level the playing field by reducing informational asymmetry between borrowers (debt issuers) and lenders (debt investors). Our opinions are about the relative credit risk of one MIS-rated bond versus other MIS-rated bonds and are intended for use by institutional, not retail, investors.

We believe it is essential for investors and other market participants to understand the role of CRAs and what credit ratings can and cannot do. MIS has always been clear that our credit ratings should be used primarily as a gauge of default probabilities and expected credit loss. We explain that our credit ratings should not be used as indicators of price, as measures of liquidity, or as recommendations to buy, sell or hold securities – all of which are regularly influenced by factors unrelated to credit. MIS's credit

ratings are not designed to address any risk other than credit risk and should not be assigned any other purpose.

It is also important for investors to understand that CRAs do not participate in the capital-raising process. Issuers choose their capital structures, transaction structures and business strategies independently of CRAs and then present them to rating analysts. Issuers and their advisers draft the appropriate disclosure documents and marketing materials used in the offering process. CRAs, like investors, are consumers of the information provided by issuers and others and react to that information by formulating and disseminating independent credit opinions.

2. A Materiality Test Focusing on Credit Risk is More Appropriate

Issuers currently must disclose the most significant factors that make an offering speculative or risky. In a debt offering, this surely includes the credit risks associated with the securities. Issuers also must disclose in "Management's Discussion and Analysis of Financial Condition and Results of Operations" ("**MD&A**") any known trends, demands, commitments, events or uncertainties that may affect liquidity or results of operations. Furthermore, Rule 408 states that, in addition to the information expressly required to be disclosed in a registration statement, an issuer must disclose "such further material information, if any, as may be necessary to make the required statements, in light of the circumstances in which they are made, not misleading." The anti-fraud rules also prohibit omission of material facts. Consequently, the current rules already require an issuer to disclose credit ratings if the issuer believes the rating is material information.

The fact that an issuer, underwriter or selling party member refers to a credit rating in the context of an offering does not mean that the rating, standing alone, is material to an investment decision. MIS intends that its credit ratings be used as amplifying information on relative credit risk that institutional investors can use to gauge the opinion they have formulated themselves based on publicly available information. A credit rating, therefore, may convey (in the investor's opinion) useful information, but that information is not necessarily material.

If the Proposed Rules are adopted, however, they will encourage investors to consider all ratings that have been solicited by the issuer to be material. This is because issuers are most likely to "use" ratings that they have solicited, and because the only *unused* ratings that must be disclosed are the solicited ones. The Proposed Rules also will contribute to the impression that investor-paid or other unsolicited ratings that have not been "used" are immaterial, a result that seems inconsistent with recent Commission initiatives to facilitate unsolicited ratings. In fact, many investors are unlikely to learn about the existence of such ratings because issuers will not have to disclose them. The Proposed Rules, therefore, are likely to reinforce the issuer-pays model (since the ratings the issuer pays for are most likely to be used and therefore disclosed) and a new variant of rating shopping (since an issuer will be motivated to avoid formally soliciting ratings from CRAs that it fears may have more conservative views), instead of encouraging issuers and investors to focus on the information that is truly material, *e.g.*, credit risk.

Instead of a specific disclosure requirement that focuses on whether a rating is "used" or "solicited", we believe the Commission could provide enhanced guidance about the circumstances in which better disclosures about credit risk are likely to be material information that should be disclosed as risk factors, in MD&A or pursuant to Rule 408. Typically, an issuer should be able to satisfy the disclosure requirements

by disclosing either: (i) additional information about credit risk; or (ii) the credit rating and certain other information about the rating and the CRA.[3]

One advantage of this approach is its adaptability. Commission staff's interpretations of what is material could evolve as market practices and the regulatory environment change.

3. Credit Ratings Should Not Be Used to Fill Gaps in the Structured Finance Disclosure Regime

Credit ratings likely play a more important role in structured finance markets, but that is because there is insufficient public information for market participants to develop their own, informed opinions about credit risk. Indeed, under this limited information disclosure model, CRAs must ask for additional information to analyze and rate structured finance products. This contrasts with the disclosure regime for U.S. corporate issuers, which are required to make a substantial amount of information publicly available. We note that the Proposed Rules would mandate disclosure about ratings in structured finance markets, while key information upon which those ratings are based remains exempt from public disclosure. In our view, credit ratings should not be used as a substitute for disclosure of essential information to investors.

Instead, as we have stated in other submissions,[4] we urge the Commission to amend the disclosure regime for registered offerings of structured finance products. If this regime is amended, issuers will be required to disclose sufficient information about credit and other risks to enable potential investors and other market participants to conduct their own analysis of the securities in question.

4. Minimizing the Regulatory Use of Ratings Will De-Emphasize Them

In an environment where the use of credit ratings is not affected by regulation, CRAs would not be significantly different from other market commentators who express credit opinions. They simply would be offering opinions for market participants, in their discretion, to consider or ignore. In the current environment, however, regulators have leveraged the market's use of ratings by incorporating them into regulation. Official recognition of ratings weakens incentives for investors to conduct their own credit analysis and use ratings as just one of several inputs in their decision-making process.

We believe that requiring issuers to disclose information about credit ratings in registration statements, Form 8-K and Form 20-K will further over-emphasize the ratings' significance and draw attention away from other, generally more important information. We are particularly concerned that retail investors, who typically are less sophisticated and under no duties regarding their decision-making, may be even more likely than institutional investors to rely on credit ratings instead of conducting their own analysis or seeking advice from a professional. Boilerplate disclosures by the issuer about the limitations of credit ratings are unlikely to discourage investors from over-emphasizing ratings.

This result is inconsistent with the Commission's and other authorities' efforts to reduce the risk of over-reliance on ratings. We believe that the more appropriate solution is for the Commission to eliminate

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[3] In Part B.1 we list the disclosure items to which MIS would not object if an issuer chose, or were required, to disclose a credit rating.

[4] See *Moody's Comment Letter re: Proposed Rules for Nationally Recognized Statistical Rating Organizations* at 3-4 (July 28, 2008); and *Moody's Comment Letter re: Re-proposed Rules for Nationally Recognized Statistical Rating Organizations* at 11-13 (March 28, 2009).

or reduce significantly the use of credit ratings for regulatory purposes.[5] This could help eliminate or reduce the impact of artificial factors affecting the importance of credit ratings to market participants and restore the influence of natural market demand for high quality credit ratings.

B. Proposed Disclosure Regime Is Unlikely to Improve Investor Understanding of Ratings

1. Situating Disclosures about the Nature of Ratings in the Registration Statement Could Make It Harder, Not Easier, for Investors to Consider Ratings in Their Proper Context

We believe that any assessment of the incremental benefits of the Proposed Rules should take into account developments that already have enhanced the ability of investors and other market participants to easily obtain information about credit ratings, the rating process and CRAs, including the following:

- ***Dissemination of Information through the Internet***: While MIS has made its credit ratings available to the public for free since the mid-1970s, our website, moodys.com, has greatly enhanced accessibility to our credit ratings and other publications we distribute for free. Mechanisms, including web links, exist to assist investors in readily locating information that may be of use to them in the investment decision-making process, even if it is not material and therefore not included in the registration statement itself.
- ***Ten CRAs Subject to Formal Oversight as Nationally Recognized Statistical Rating Organizations ("NRSROs")***: There are now ten NRSROs subject to the formal oversight regime established by the Credit Rating Agency Reform Act of 2006 ("**Reform Act**") and associated rules. They are required to make their credit ratings available through the internet or other readily accessible means, either for free or a reasonable fee. In particular, of the ten NRSROs, seven (including MIS) operate primarily under the issuer-pays model and disseminate their credit rating announcements for free. According to the Commission, these seven NRSROs account for approximately 99% of the total, currently outstanding credit ratings of NRSROs.[6] Each NRSRO also must disclose on Form NRSRO: a description of its rating methodologies and procedures; a copy of its code of ethics (or an explanation of why it does not have one); a description of the material conflicts of interest it faces in the rating process; copies of its policies and procedures to manage such conflicts; rating histories; and ratings performance statistics. An NRSROs must make its Form NRSRO available on its website.
- ***Public Commitment to Greater Transparency in Line with International Standards***: The *IOSCO Code of Conduct Fundamentals for Credit Rating Agencies* ("**IOSCO Code**") was adopted in 2004. It calls upon CRAs to meet high standards regarding the quality, integrity, independence and transparency of the credit rating process. The IOSCO Code includes recommendations about, among other things: (i) the timely, public dissemination of non-private credit ratings for free where the ratings are determined using non-public information; (ii) information that should be included in credit rating announcements so that users can understand the rationale for the rating, identify the relevant rating methodology and determine when the

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[5] See, *e.g.*, *MIS Comment Letter re References to Ratings of Nationally Recognized Statistical Rating Organizations – Files S7-17-08, S7-18-08 and S7-19-08* (Sept. 5, 2008) and *MIS Comment Letter re Money Market Fund Reform – File S7-11-09* (Sept, 8, 2009).

[6] See Commission, *Annual Report on Nationally Recognized Statistical Rating Organizations* (September 2009) at 9-10.

rating was last updated prior to the current rating action; (iii) disclosure of methodologies, ratings performance metrics and the meaning of rating symbols; (iv) disclosure about the attributes and limitations of ratings; and (v) disclosure about potential conflicts of interest and how they are managed. The IOSCO Technical Committee has concluded that the four largest CRAs (including MIS) have substantially incorporated the revised IOSCO Code into their own codes.

Because of these developments, we believe that the Commission's concerns that potential investors in registered offerings are not being provided with sufficient information about credit ratings generally[7] are not supported by evidence. While there may be CRAs that are not NRSROs, we believe that issuers' use of non-NRSRO ratings in connection with registered offerings is minimal.

We also understand that the Commission believes that potential investors should be able to find all of the information about the issuer and its securities that is material to their investment decision in a single document. As discussed earlier, however, we are concerned that mandating extensive disclosures about solicited ratings in registration statements will exacerbate incentives for investors to over-rely on such ratings instead of encouraging them to focus on the material information about the issuer and its securities that is supposed to be contained in the registration statement. Also, the requiring the issuer to include the disclosures outlined in the Proposed Rules could create the mistaken impression that CRAs are participants in the offering, rather than independent commentators. By contrast, measures (*e.g.*, references to a CRA's website) that help investors locate amplifying, properly contextualized information about credit risk and the nature of the rating process without deeming all such information to be material are more likely to achieve the Commission's stated objectives than the Proposed Rules.

MIS would not object[8] to guidance that, if a credit rating constitutes material information or where an issuer elects to disclose a credit rating in the registration statement, it also should disclose:

- the name of the CRA whose rating is being used and whether or not it is an NRSRO;
- the credit rating assigned;
- the identity of the person paying for the credit rating;
- the nature of any non-rating services provided by the CRA and/or its CRA affiliates to the issuer and/or its affiliates;[9]

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[7] We agree that investors may not be sufficiently aware of the practice of rating shopping. As we discuss below, however, the Commission's proposed disclosure rule about Unused, Solicited Ratings is unlikely to curb the practice or improve investor understanding of it.

[8] This expression of non-objection is qualified as follows. First, we remain concerned that requiring issuers to disclose information about credit ratings in registration statements could perpetuate and exacerbate incentives for market participants to over-rely on credit ratings. Second, as discussed in the Related Comment Letter, we do not believe that CRAs should be subject to liability under Section 11 of the Securities Act of 1933 ("**Securities Act**") for disclosures about credit ratings in registration statements. Third, any reference in a registration statement or other disclosure document to a CRA's website should not constitute an incorporation by reference into the registration statement or disclosure document of the cross-referenced information for liability purposes.

[9] We believe, however, that proposed Item 202(g)(7) is overly broad because it would require the issuer to describe any non-rating services provided by the CRA's *non-rating affiliates* in addition to its CRA affiliates. Some CRAs are part of corporate groups that include non-CRA entities which may provide a range of non-rating services and products to issuers and their affiliates in the ordinary course of business. For example, the three largest NRSROs, including MIS, are affiliated

- the website address where an interested person can obtain a description of the CRA's rating system, the credit rating and any available ratings history for the rating, any other published designation reflecting the results of any other evaluation the CRA has conducted, and a description of the potential conflicts of interest it faces in its rating business;[10]
- any material differences between the terms of the securities as assumed or considered by the CRA and: (i) the minimum obligations of the security as specified in the governing instruments of the security; and (ii) the terms of the securities as used in any marketing or selling efforts; and
- the disclaimer statement set out in proposed Item 202(g)(12).

We believe, however, that issuers should not make the other proposed disclosures about credit ratings because of the risk that the information could be presented inaccurately or out of context. In particular, we believe that the issuer should not be the entity that discloses the information called for in paragraphs (g)(3), (5), (8), (9) and (10) of Item 202(g). These disclosure items would require issuers to have an in-depth knowledge of the credit rating system of each CRA whose rating they use and create explanatory narratives for opinions that are not their own.

With respect to disclosures on Form 8-K and 20-K about changes in credit ratings, we do not believe that additional rules are necessary. Also, since CRAs generally publish, and markets process, information about rating changes on nearly a real-time basis, the benefits associated with requiring Form 8-K disclosure four business days after the CRA advises an issuer of a rating change are negligible. Subject to the caveats expressed in footnote 8, however, MIS would not object to requirements that the issuer disclose:

- the date it was notified by the CRA of the CRA's decision to change the rating;
- the name of the CRA and whether or not it is an NRSRO;
- the new credit rating, the rating action (*e.g.*, upgrade, downgrade, change in outlook or placement on review), and the date the rating action was taken;
- the prior credit rating; and

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with non-CRA entities that publish and distribute a wide variety of materials, ranging from materials that focus specifically on credit markets, to general interest newspapers and magazines, to school textbooks and *Seventeen* magazine. While it is unlikely that an issuer will be purchasing school textbooks or *Seventeen* magazine, requiring it to collect information about and describe all of the non-rating services that non-CRA affiliates of the CRA provide to the issuer and its affiliates seems unnecessary, overly burdensome and irrelevant to the investment decision-making process. A more appropriate requirement would be for the issuer to describe any non-rating services provided by the CRA and/or any of its *CRA* affiliates.

We also are strongly opposed to any requirement that the issuer disclose the fees paid to the CRA and its affiliates for rating and non-rating services. We discuss our concerns in more detail in Part C.1 below.

[10] We also note that, if issuers disclose only the information about potential conflicts that the Proposed Rules require them to disclose, investors could be left with the mistaken impression that a particular CRA does nothing to manage those potential conflicts and, as a consequence, its ratings are not credible. By contrast, if the investor is directed to the CRA's website, he or she will have access to significantly more detailed information about the range of potential conflicts the CRA faces and how it manages them. Requiring the issuer to make detailed disclosures about how the CRA manages conflicts would be inappropriate because the placement of this information the registration statement could encourage investors to see CRAs as agents of the issuer and participants in the offering.

- the website of the relevant CRA where further information about the rating action can be found.

2. Rating Shopping Disclosures Will Not Cure the Problem or Improve Investor Understanding

Rating shopping is a harmful practice engaged in by some issuers, sponsors, arrangers and/or subscribers for ratings. MIS has discussed this concern in public forums on numerous occasions and we have noted that rating shopping stems from issuers' exclusive control over the dissemination of the information needed to analyze an obligation. It is particularly endemic in markets, such as structured finance markets, with limited disclosure obligations for issuers. Such opaque markets can facilitate rating shopping by hampering the ability of CRAs (regardless of whether they are paid by the issuer), other analysts and, most importantly, investors to assess independently the creditworthiness of issuers or debt issuances. We share the Commission's concern about this practice and have recommended that the mandatory disclosure regime for structured finance products be enhanced, since greater transparency in this market would make it more difficult for issuers to shop for ratings. We believe, however, that the proposed disclosure rule will not achieve the Commission's objectives for the following reasons.

If an issuer discloses an Unused, Solicited Rating, all that an investor might learn is that rating shopping *might* have occurred. Such disclosure, however, would not definitively indicate that the issuer selected the ratings used in the offering solely because they were the highest ones. There are other reasons why an issuer may choose one CRA's credit rating over another, such as: the CRA's track record with respect to the predictive power of its ratings, views about the quality of the CRA's methodologies and its analysts' understanding of the relevant sector or asset class, and considerations relating to the integrity of the ratings process, rating fees, or the efficiency of the CRA's rating processes. Consequently, merely disclosing the existence of an Unused, Solicited Rating could lead an investor to conclude wrongly that the ratings used in connection with the offering are less reliable than the Unused, Solicited Rating. Also, disclosing Unused, Solicited Ratings that are not based on full and final information could exacerbate the problem, since potential investors might conclude that the Unused, Solicited Rating, which the investor might not realize is based on outdated or incomplete information, is more reliable than the rating selected by the issuer. In the end, disclosing Unused, Solicited Ratings will not help investors identify which credit ratings are credible.

If this disclosure rule is adopted, it is more likely to create the inaccurate impression that no rating shopping has occurred. While the requirement might deter the most egregious forms of rating shopping, some issuers will find ways to avoid triggering the requirement. For example, instead of seeking preliminary ratings from a number of CRAs and then selecting one or more ratings to use in connection with the offering, issuers are more likely to refrain from approaching CRAs that are known to have more conservative methodologies. (This practice already occurs but the new disclosure requirement would reinforce the incentives to do so.) Issuers also will be less likely to engage in initial conversations with smaller or newer CRAs, or CRAs that are starting to build up a new practice area, because the issuer is less likely to be familiar with such CRAs' methodologies and rating procedures. In effect, issuers will be more inclined to window shop for a rating without entering the store. This could adversely affect competition based on ratings quality in the CRA industry, *e.g.*, by making it harder for CRAs to enter the market or expand their scope of coverage and/or making it harder for more conservative CRAs to compete for business. Alternatively, issuers could simply present "hypotheticals" to CRAs and claim that they did not seek a preliminary rating. Simply put, it is more than likely that issuers will continue shopping for ratings,

but they will move their rating shopping activity to an earlier point in the process that does not trigger disclosure requirements.

Furthermore, since the proposed disclosure rule will require disclosure only of Unused, *Solicited* Ratings, market participants might not be made aware of unsolicited credit ratings that are less favorable than the credit ratings disclosed by the issuer. Since, for the reasons noted above, issuers will be much less likely to solicit ratings from CRAs with more conservative methodologies, it is likely that credit ratings determined using more conservative methodologies will not be brought to market participants' attention.

Moreover, the Commission's proposed rule also may have a negative and unintended consequence. Specifically, it is possible that the rule could deter issuers and underwriters, out of a concern that they will trigger accidentally the disclosure requirement and possibly taint the offering, from engaging in analytical discussions with CRAs that otherwise would help them understand better the CRA's methodologies and help CRAs remain well-informed about market developments. We are concerned about any rule that would hamper such discussions, since they promote transparency in the rating process, help improve market participants' understanding of CRAs' methodologies, and help CRAs improve the quality of their methodologies and rating analysis.

Also, because the Proposed Rules would, in effect, label solicited ratings (whether used or unused) as material and investor-paid or other unsolicited ratings as immaterial, the issuer-pays model would be reinforced. This result seems to be inconsistent with the Commission's stated interest in promoting unsolicited ratings.

For these reasons, we strongly believe that issuers should not be required to disclose Unused, Solicited Ratings. If the Commission nevertheless decides to require issuers to disclose Unused, Solicited Ratings, it also should require them to disclose *unsolicited* ratings that are material and that have been communicated to the issuer or underwriter by, for example, the CRA or an investor that solicited the rating.

C. Proposed Rules Likely to Have Unintended, Adverse Consequences

1. Fee Disclosure Rule Would Undermine Firewalls Designed to Promote Analytical Independence

The Commission and other authorities have stressed the importance of insulating rating analysts and rating committees from commercial influences. Consistent with the revised IOSCO Code and recently adopted Commission Rule 17g-5(c)(6), MIS prohibits anyone who participates in determining or monitoring credit ratings or developing or approving rating methodologies from participating in discussions regarding the fees paid for the rating. A separate team within MIS handles discussions about fees and payment of fees for rating services, while Moody's Analytics ("**MA**") sells MIS's credit ratings and research to subscribers. These arrangements are intended to bolster analytical independence and ensure that rating quality is not diminished by commercial interests. The extension, strengthening and ongoing maintenance of these firewalls have involved a significant investment of time and resources.

If, however, the Proposed Rules are adopted as proposed, information about fees paid by particular issuers to MIS for rating services and to MA for non-rating services will become publicly available. Compiling and publicly disclosing fee information will expose our analysts and rating committees to more commercial information about rated issuers than they ever had before. Access to such information would undermine our efforts and those of regulators globally to shield analysts from such information in order to

promote independence in the credit rating process. Accordingly, we strongly oppose any rule[11] requiring public disclosure of fees paid to the CRA and/or its affiliates for rating or non-rating services.

As an alternative to the proposed rule, the Commission could require issuers to disclose what proportion of the aggregate revenues received by the CRA and its CRA affiliates from the issuer and its affiliates constitute revenues for non-rating services. This information could help potential investors identify situations where a CRA might be facing a potential conflict of interest because it, or its CRA affiliates, receive a significant proportion of their revenues from a particular issuer for non-rating services. Disclosing such information, however, would not undermine CRAs' existing firewalls.

2. Liability Concerns Could Lead to Behaviors That Jeopardize CRA Objectivity and Reduce Diversity of Opinions in the Market

CRAs are consumers of information, including, most particularly, information filed by issuers with the Commission. Even if Rule 436(g) is not rescinded, requiring issuers to disclose detailed information about ratings in registration statements would transform CRAs from consumers of the information in such documents into participants in the documents' preparation, since issuers would expect CRAs to draft or vet disclosures about such matters as the meaning of the credit rating and material limitations on the credit rating's scope. Converting CRAs from impartial observers to participants in this process would jeopardize their independence, thereby directly undermining the usefulness of their credit ratings. Rescinding Rule 436(g) would aggravate this risk, since the prospect for CRAs of liability under Section 11 would provide even greater incentives for CRAs to become involved in preparing the registration statement.

Moreover, the issuer and underwriter likely would be particularly concerned about being sued for disclosing ratings that investors considered to be "wrong".[12] Consequently, we expect that they and their counsel would want to become involved in preparing and determining the substantive content of CRAs' ratings and rating announcements, so that they could conclude that the rating and related announcement accurately reflected (at least in their opinion) the relative creditworthiness of the issuer and/or its securities. This could result in pressure on CRAs to change the substance of their opinions and/or methodologies.

It is true that the issuer and underwriter already face the risk of being sued for a "wrong" rating when a rating is disclosed in a registration statement. We believe, however, that adoption of the Proposed Rules, which would require more extensive disclosures about ratings and effectively deem all solicited ratings to be material, would focus even more investor attention on ratings and tempt them to treat highly rated securities as "no-risk" investments. Inevitably, some investors would be disappointed and be more likely to sue issuers, underwriters and, if Rule 436(g) were rescinded, NRSROs.

Not only would the issuer and underwriter have incentives to second-guess the substance of the CRA's opinion and its rating methodologies, they also could be motivated to ask the CRA to express its

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[11] We have similar concerns about any of the alternatives described by the Commission at pages 53094-53097 of the Release that would require public disclosure about fees for rating or non-rating services. Likewise, we have similar concerns about any requirement to disclose publicly that the issuer, underwriter and/or their affiliates account for a significant proportion of the revenues of the CRA and/or its affiliates.

[12] If the Proposed Rules are adopted, we expect that claims will be filed in which it is alleged that the registration statement included a material misstatement or omission about the issuer's or the securities' creditworthiness. In other words, some investors will seek to hold the issuer and underwriter liable for credit ratings that the investors characterize as "wrong", and not just for inaccurately recording or characterizing the credit rating.

opinion in a more qualified manner or even to change the nature of the opinion it expressed, in order to reduce the risk of a suit alleging that the rating materially misstated the issuer's creditworthiness. For example, the issuer and underwriter might prefer the CRA to express a credit opinion that was more qualified or less granular with respect to its predictions about relative creditworthiness. This could make it more difficult for CRAs to maintain their objectivity (or the appearance of objectivity) in the rating process. As we discuss in the Related Comment Letter, the pressure on CRAs would be even greater if Rule 436(g) were rescinded.

Furthermore, the prospect of liability for disclosing credit ratings that some investors consider to be "wrong", combined with a requirement to disclose Unused, Solicited ratings, likely would strengthen incentives for issuers and underwriters to avoid contacting CRAs that were considered to have more conservative methodologies or that were considered "new entrants" with respect to the industry sector or asset class in question. This could reduce competition in the CRA industry and lead to fewer, diverse opinions being disseminated.

3. Increased Transaction Costs and Inefficiencies in the Capital-Rating and Credit Rating Process

Once an issuer is required to include prescribed information in a registration statement, the persons who could be held liable for that disclosure will be motivated to conduct their own investigation so that they can: (1) satisfy themselves that there are no material misstatements or omissions; and (2) where available, take advantage of a "due diligence" defense. Consequently, if the Proposed Rules are adopted as proposed, the issuer and underwriter will want to have their respective counsel review the proposed disclosure, and any available documentary support, and have their counsel contact the CRA's staff to discuss the disclosure and documentation. This will take time and money. Moreover, identifying and collecting information about any non-rating services provided by the CRA and its affiliates and then preparing appropriate disclosures, which would be vetted by the CRA and each entity's counsel, will also be a time-consuming process.

In addition, because detailed ratings-related disclosures will be included in the registration statement, CRAs will want to review the draft registration statement and have their outside counsel review it. This would be a change in practice since CRAs historically have not participated in the offering process and have not reviewed and commented on draft disclosure. Involving CRAs and their counsel in the preparation and review of the registration statement would slow down, and increase the cost of, the capital-raising process. It also would slow down the dissemination of credit rating opinions.[13]

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[13] For the reasons set out above, we believe the Commission has significantly underestimated the time required to prepare the proposed disclosures. Its estimate that it would take one hour of the issuer's time and three hours of outside professionals' time does not appear to take into account, for example: (1) the time required for the issuer and underwriter to investigate the appropriateness of the CRA's rating opinion; and (2) collect information and prepare disclosure about non-rating services provided by the CRA and its affiliates to the issuer and its affiliates. It also does not appear to include an estimate of the time required for the CRA and its outside counsel to: (1) respond to queries from the issuer, underwriter and respective counsel about the credit rating, rating announcement and other source documents for the prescribed disclosures; (2) vet the proposed disclosures for the registration statement; and (3) collect information about and vet disclosures regarding non-rating services provided by the CRA and its affiliates to the issuer and its affiliates. We think that a more appropriate estimate of "burden hours per registered offering" would be at least four to five times higher than the Commission's estimate.

As discussed above, we also believe the Proposed Rules could motivate issuers to ask CRAs to adopt rating scales with fewer gradations and/or include more qualifiers in their predictive opinions. If CRAs acceded to these requests, there would be a decrease in the amount of useful information disclosed in the market about relative credit risk. This would decrease the efficiency of the capital allocation process and likely increase the cost of capital for many issuers.

For these reasons we recommend that, if the Commission adopts either a materiality-based test for disclosure or the Proposed Rules, it make it clear that issuers and underwriters cannot be held liable under Section 11 or Section 12(a) for disclosing a credit rating that is considered to be an inaccurate prediction of the issuer's or the securities' credit risk. In addition, as we discuss in the Related Comment Letter, Rule 436(g) should not be rescinded and CRAs[14] should not be exposed to liability in respect of an issuer's disclosures about credit ratings.

Likewise, we believe that requiring issuers to disclose all changes in credit ratings previously required to have been disclosed in registration statements would impose greater record-keeping burdens and costs on issuers and CRAs than the Commission has estimated. The Commission estimates that it would take five hours for an issuer and its outside advisers to complete and file an 8-K disclosing a change in a credit rating. We believe this estimate does not take into account: (1) the time the issuer and its counsel likely would spend investigating the appropriateness of the CRA's rating opinion; (2) the increased likelihood that an issuer would appeal rating agency decisions, either out of a concern that the change in rating was inappropriate or in order to delay having to disclose the change in rating; and (3) the time the CRA and its outside counsel would spend responding to queries from the issuer and its counsel, dealing with additional appeals of ratings and vetting the proposed disclosures on Form 8-K or 20-F. We believe that a more appropriate estimate of "burden hours per 8-K or 20-F" filing would be three to four times as high as the Commission's estimate.

[14] CRAs that are not NRSROs currently fall outside the safe harbor provided by Rule 436(g). As we state in the Related Comment Letter, to the extent the safe harbor creates competitive disadvantages, the better solution is to level the playing field by expanding Rule 436(g) to include *all* CRAs, whether or not they are NRSROs, as the Commission proposed in 2008.