Annual Report on Nationally Recognized Statistical Rating Organizations

As Required by Section 6 of the Credit Rating Agency Reform Act of 2006

December 2016

This is a report of the staff of the U.S. Securities and Exchange Commission. The Commission has expressed no view regarding the analysis, findings, or conclusions contained in this report.

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As Required by Section 6 of the Credit Rating Agency Reform Act of 2006

I. INTRODUCTION

The staff (the "Staff") of the U.S. Securities and Exchange Commission (the "Commission" or "SEC") is providing this report ("Report") regarding nationally recognized statistical rating organizations ("NRSROs") pursuant to section 6 of the Credit Rating Agency Reform Act of 2006 ("Rating Agency Act").[1] This Report reflects solely the Staff's views. Section 6 of the Rating Agency Act requires the Commission to submit an annual report ("Annual Report") to the Committee on Banking, Housing, and Urban Affairs of the U.S. Senate and the Committee on Financial Services of the U.S. House of Representatives that, with respect to the year to which the Annual Report relates:

- identifies applicants for registration as NRSROs under section 15E of the Securities Exchange Act of 1934 ("Exchange Act");[2]
- specifies the number of, and actions taken on, such applications; and
- specifies the views of the Commission on the state of competition, transparency, and conflicts of interest among NRSROs.

This Report relates generally to the period from June 26, 2015 to June 25, 2016 (the "Report Period"). In addition to addressing the items specified in section 6 of the Rating Agency Act, this Report provides an overview of certain Commission and Staff activities relating to NRSROs.

Information regarding the topics covered in this Report with respect to prior periods can be found on the Office of Credit Ratings ("OCR" or the "Office") page of the Commission's website.[3]

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1 Pub. L. No. 109-291, 120 Stat. 1327 (Sept. 29, 2006). The Rating Agency Act, among other things, added section 15E to the Securities Exchange Act of 1934 (15 U.S.C. §78o-7) to establish self-executing requirements on NRSROs and provide the Commission with the authority to implement a registration and oversight program for NRSROs. In June 2007, the Commission approved rules implementing such a program. See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations, Release No. 34-55857, 72 FR 33564 (Jun. 18, 2007), available at: https://www.sec.gov/rules/final/2007/34-55857.pdf.

2 Unless otherwise noted, all references to specific statutory sections and rules in this Report are to sections in the Exchange Act and related rules.

3 Prior Annual Reports can be found under "Annual Reports to Congress" in the "Public Reports" section of the OCR webpage, available at: http://www.sec.gov/ocr.

II. STATUS OF REGISTRANTS AND APPLICANTS

Section 3(a)(62)(A) defines a "nationally recognized statistical rating organization" as a credit rating agency that issues credit ratings certified by qualified institutional buyers, in accordance with section 15E(a)(1)(B)(ix), with respect to:

(i) financial institutions, brokers, or dealers;
(ii) insurance companies;
(iii) corporate issuers;
(iv) issuers of asset-backed securities (as that term is defined in 17 CFR 229.1101(c));
(v) issuers of government securities, municipal securities, or securities issued by a foreign government; or
(vi) a combination of one or more categories of obligors described in any of clauses (i) through (v) above, and that is registered under section 15E.

As of the date of this Report, there are ten credit rating agencies registered as NRSROs. The NRSROs, categories of credit ratings described in clauses (i) through (v) of section 3(a)(62)(A) in which they are registered, and locations of their principal offices, as of the date of this Report, are listed below:[4]

NRSRO	Categories of Credit Ratings	Principal Office
A.M. Best Rating Services, Inc. ("A.M. Best")[5]	(ii), (iii), and (iv)	U.S.
DBRS, Inc. ("DBRS")	(i) through (v)	U.S.
Egan-Jones Ratings Company ("EJR")	(i) through (iii)	U.S.
Fitch Ratings, Inc. ("Fitch")	(i) through (v)	U.S.
HR Ratings de México, S.A. de C.V. ("HR Ratings")	(i), (iii), and (v)	Mexico
Japan Credit Rating Agency, Ltd. ("JCR")	(i), (ii), (iii), and (v)	Japan
Kroll Bond Rating Agency, Inc. ("KBRA")	(i) through (v)	U.S.

4 See the current Form NRSRO on each NRSRO's website for any updates to this information.

5 On January 12, 2016, A.M. Best Company, Inc. announced the completion of an organizational restructuring involving the creation of a subsidiary to operate its regulated rating-centric business. The subsidiary, A.M. Best Rating Services, Inc., became operational on January 1, 2016 and filed an update on Form NRSRO on such date. See A.M. Best Press Release dated January 12, 2016, available at: http://www3.ambest.com/ambv/bestnews/PressContent.aspx?altsrc=14&refnum=23512.

Moody's Investors Service, Inc. ("Moody's")	(i) through (v)	U.S.
Morningstar Credit Ratings, LLC ("Morningstar")	(i), (iii), and (iv)	U.S.
S&P Global Ratings ("S&P")[6, 7]	(i) through (v)	U.S.

While during the Report Period the Commission did not receive any complete applications for initial registration as an NRSRO or for registration by current NRSROs in additional ratings classes, after the end of the Report Period each of Morningstar and HR Ratings filed with the Commission in accordance with section 15E(a)(1) and Rule 17g-1 applications for registration in the financial institutions and corporate issuers ratings classes. Morningstar's application was approved by the Commission on August 24, 2016,[8] and HR Ratings' application was approved by the Commission on November 23, 2016.[9]

Applications for initial registration and for registration by current NRSROs in additional ratings classes are filed on Form NRSRO[10] ("Form NRSRO"). In addition, section 15E(b) requires NRSROs to promptly amend Form NRSRO if any information or document provided therein becomes materially inaccurate, and, on an annual basis, Form NRSRO must be amended to update ratings count and performance information, certify the continuing accuracy of the information and documents provided therein, and list any material change thereto during the previous calendar year. OCR Staff review such amendments to Forms NRSRO in light of the

6 In connection with a name change from McGraw Hill Financial, Inc. to S&P Global Inc., the company rebranded its credit rating business from "Standard & Poor's Rating Services" to "S&P Global Ratings." An update on Form NRSRO was filed on April 29, 2016 to reflect the name change of the NRSRO. See S&P Global Inc. Press Release dated April 27, 2016, available at: http://investor.spglobal.com/file/Index?KeyFile=34046145.

7 On January 21, 2015, S&P consented to a Commission order under which, among other things, S&P agreed to refrain from issuing preliminary or final ratings for any new issue U.S. conduit/fusion commercial mortgage-backed securities transaction for a period of twelve months from the date of the order. See In the Matter of Standard & Poor's Ratings Services, Release Nos. 33-9705 and 34-74104 (Jan. 21, 2015), available at: http://www.sec.gov/litigation/admin/2015/33-9705.pdf. The twelve-month period expired during the Report Period.

8 The order approving Morningstar's application is available at https://www.sec.gov/rules/other/2016/34-78671.pdf.

9 The order approving HR Ratings' application is available at https://www.sec.gov/rules/other/2016/34-79382.pdf.

10 Rule 17g-1 requires an applicant/NRSRO to use Form NRSRO for the following, as applicable:

- an initial application to be registered as an NRSRO;
- an application to register for an additional class of credit ratings;
- an application supplement;
- an update of registration pursuant to section 15E(b)(1);
- an annual certification pursuant to section 15E(b)(2); and
- a withdrawal of registration pursuant to section 15E(e).

See http://www.sec.gov/about/forms/formnrsro.pdf for additional information.

requirements of section 15E(b), Rule 17g-1, and the instructions to Form NRSRO, and may comment on such amendments and refer certain observations regarding such amendments to OCR examination Staff.

III. ACTIVITIES RELATING TO NRSROs

A. Activities

The creation of OCR was mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act")[11] and the Office was established in June 2012 with the appointment of its Director, Thomas Butler. OCR is responsible for the oversight of credit rating agencies registered with the Commission as NRSROs. OCR's Staff includes professionals with expertise in a variety of areas that relate to its regulatory mission, such as corporate, municipal, and structured debt finance.[12]

OCR's responsibilities – as mandated by the Dodd-Frank Act – include conducting an examination of each NRSRO at least annually in eight specified review areas.[13] Information regarding the examinations, including those that concluded during the Report Period, is included in OCR's annual examination reports.[14]

In connection with its regulatory mission, OCR also monitors trends and developments affecting the credit rating industry. For example, OCR Staff meets with each NRSRO to discuss rating and industry developments and meets with the board of directors of certain NRSROs to discuss, among other things, compliance and oversight matters. OCR Staff also meets with a variety of other market participants, including investors, issuers, and industry organizations, to discuss matters relevant to the credit rating industry. OCR Staff also attends various conferences, seminars, and other events addressing topics applicable to the industry. These monitoring activities are focused on informing Commission policy and rulemaking and NRSRO examinations.

During the Report Period, OCR Staff also continued to participate in meetings that involved rating agency regulators globally, including those of the International Organization of Securities Commissions ("IOSCO") Committee 6 on Credit Rating Agencies[15] and the supervisory colleges that were formed at IOSCO's recommendation for the largest

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11 See Pub. L. No. 111-203, 124 Stat. 1376 (2010).

12 See section 15E(p)(2) for a description of OCR staffing requirements.

13 See section 15E(p)(3) for a description of the scope of the required examinations.

14 The examination reports can be found on OCR's page of the Commission's website, which is located at http://www.sec.gov/ocr, in the "Public Reports" section under "Annual Examination Reports."

15 IOSCO Committee 6 was formed to evaluate and consider regulatory and policy initiatives relating to credit rating agencies' activities and oversight and facilitate regular dialogue between regulators and the credit rating industry. The SEC chairs Committee 6, and OCR Staff represents the SEC in this regard.

internationally-active credit rating agencies.[16] During the Report Period, the colleges held an in-person meeting and conducted quarterly calls. OCR Staff also conducted additional discussions with international regulators as appropriate.

B. Commission Orders and Releases and Staff Publications

From the beginning of the Report Period to the date preceding the issuance of this Report, the below-listed Commission orders and releases and Staff publications were issued relating to NRSROs or credit ratings in general.

- Order Granting Registration of HR Ratings de México, S.A. de C.V. for Two Additional Classes of Credit Ratings, Release No. 34-79382 (Nov. 23, 2016).[17] The Commission granted HR Ratings' registration for the following two additional classes of credit ratings: (1) the class of credit ratings described in clause (i) of section 3(a)(62)(A) (i.e., financial institutions, brokers, or dealers); and (2) the class of credit ratings described in clause (iii) of section 3(a)(62)(A) (i.e., corporate issuers).

- Order Granting Registration of Morningstar Credit Ratings, LLC for Two Additional Classes of Credit Ratings, Release No. 34-78671 (Aug. 24, 2016).[18] The Commission granted Morningstar registration for the following two additional classes of credit ratings: (1) the class of credit ratings described in clause (i) of section 3(a)(62)(A) (i.e., financial institutions, brokers, or dealers); and (2) the class of credit ratings described in clause (iii) of section 3(a)(62)(A) (i.e., corporate issuers).

- Order Granting Conditional Exemption of Morningstar Credit Ratings, LLC from a Requirement in Section 15E(a)(1)(C)(iv) of the Securities Exchange Act of 1934 and Item 6C of Form NRSRO, Release No. 34-78670 (Aug. 24, 2016).[19] The Commission granted Morningstar a conditional exemption from the requirement in section 15E(a)(1)(C)(iv) and Item 6C of Form NRSRO that an NRSRO applying to register for additional classes of credit ratings provide at least two certifications from qualified institutional buyers stating, among other things, that they have used the credit ratings of the applicant in such classes in the course of making some of their investment decisions for at least the three years immediately preceding the date of the certifications. An exemption was requested because the related credit ratings had been issued by a non-NRSRO affiliate of Morningstar. Under the order, Morningstar is required to file certifications from qualified institutional buyers as to the additional classes of credit

[16] The supervisory colleges were formed to enhance communication among credit rating agency regulators globally with respect to examinations of the relevant credit rating agencies. See Supervisory Colleges for Credit Rating Agencies, Final Report (July 2013), available at: http://www.iosco.org/library/pubdocs/pdf/IOSCOPD416.pdf. The SEC serves as chair of the colleges for S&P and Moody's, and OCR Staff represents the SEC in this regard. The European Securities and Markets Authority serves as chair of the college for Fitch.

[17] Available at: https://www.sec.gov/rules/other/2016/34-79382.pdf.

[18] Available at: https://www.sec.gov/rules/other/2016/34-78671.pdf.

[19] Available at: https://www.sec.gov/rules/exorders/2016/34-78670.pdf.

ratings by no later than four years following its registration in those classes of credit ratings.

- Proposed Rule: Disclosure Update and Simplification, Release Nos. 33-10110, 34-78310, and IC-32175 (July 13, 2016), 81 FR 51607 (Aug. 4, 2016).[20] The Commission proposed amendments to certain disclosure requirements that may have become redundant, duplicative, overlapping, outdated, or superseded in light of other Commission disclosure requirements, U.S. Generally Accepted Accounting Principles ("U.S. GAAP"), International Financial Reporting Standards, or changes in the information environment. The proposed amendments relate to issuers of securities and other entities, including a proposed change to Rule 17g-3 to conform the financial statement reporting requirements applicable to NRSROs to U.S. GAAP.

- Staff Guidance sent to NRSROs in July 2016.[21] In July 2016, OCR sent letters to the compliance officers of the NRSROs designated under section 15E(j), setting forth OCR Staff's view on a particular aspect of section 15E(h)(4)(A) relating to required policies and procedures of NRSROs involving the conduct of "look-back" reviews with respect to certain former employees.

- Update to Rating History Files Publication Guide.[22] An update to technical guidance on the creation of files containing credit rating histories in accordance with the requirements of Rule 17g-7(b) was posted to the Commission's website on May 26, 2016.

- 2015 Summary Report of Commission Staff's Examinations of Each Nationally Recognized Statistical Rating Organization, dated December 2015, as required under section 15E(p)(3)(C).[23] The report summarizes essential findings of the examinations conducted by Staff under section 15E(p)(3)(C), generally focusing on the period from January 1, 2014 through December 31, 2014.

- Annual Report to Congress on Nationally Recognized Statistical Rating Organizations, dated December 2015, as required by section 6 of the Rating Agency Act.[24] The Annual Report addresses the matters described in the first paragraph under Section I hereof, generally covering the period from June 26, 2014 to June 25, 2015.

- Order Granting Temporary, Limited, and Conditional Exemption of Morningstar Credit Ratings, LLC from the Conflict of Interest Prohibition in Rule 17g-5(c)(1) of the Securities Exchange Act of 1934, Release No. 34-76766 (Dec. 24, 2015).[25] The Commission granted Morningstar a temporary, conditional exemption, until January 1, 2017, from the conflict of interest prohibition in Rule 17g-5(c)(1), which prohibits an

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20 Available at: https://www.sec.gov/rules/proposed/2016/33-10110.pdf.

21 Available at: https://www.sec.gov/about/offices/ocr/dear-dco-letter-15eh4a-071816.pdf.

22 Available at: https://www.sec.gov/structureddata/rocr-publication-guide.html.

23 Available at: http://www.sec.gov/ocr/reportspubs/special-studies/nrsro-summary-report-2015.pdf.

24 Available at: http://www.sec.gov/ocr/reportspubs/annual-reports/2015-annual-report-on-nrsros.pdf.

25 Available at: https://www.sec.gov/rules/exorders/2015/34-76766.pdf.

NRSRO from issuing or maintaining credit ratings solicited by a person that provided 10% or more of an NRSRO's total net revenue in the NRSRO's most recently ended fiscal year.

- Order Instituting Administrative and Cease-and-Desist Proceedings, Pursuant to Sections 15E(d) and 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order, Release No. 34-76261 (Oct. 26, 2015).[26] The Commission instituted settled administrative proceedings against DBRS regarding DBRS's surveillance methodology and practices with respect to residential mortgage-backed securities and re-securitized real estate mortgage investment conduits.

- Order Extending Temporary Conditional Exemption for Nationally Recognized Statistical Rating Organizations from Requirements of Rule 17g-5(a)(3) under the Securities Exchange Act of 1934 and Request for Comment, Release No. 34-76183 (Oct. 16, 2015) 80 FR 64031 (Oct. 22, 2015).[27] The Commission extended, until December 2, 2017, the order exempting NRSROs from complying with Rule 17g-5(a)(3) with respect to credit ratings for certain structured finance products where the issuer is a non-U.S. person and the NRSRO has a reasonable basis to conclude that the products will be offered and sold only in transactions outside the United States.

- Order Granting Temporary, Limited, and Conditional Exemption of Kroll Bond Rating Agency, Inc. from the Conflict of Interest Prohibition in Rule 17g-5(c)(1) of the Securities Exchange Act of 1934, Release No. 34-76129 (Oct. 13, 2015).[28] The Commission granted KBRA a temporary, conditional exemption, until January 1, 2017, from the conflict of interest prohibition in Rule 17g-5(c)(1), which prohibits an NRSRO from issuing or maintaining credit ratings solicited by a person that provided 10% or more of an NRSRO's total net revenue in the NRSRO's most recently ended fiscal year.

- Final Rule: Removal of Certain References to Credit Ratings and Amendment to the Issuer Diversification Requirement in the Money Market Fund Rule, Release No. IC-31828 (Sept. 16, 2015), 80 FR 58124 (Sept. 25, 2015).[29] The Commission adopted amendments to address provisions that reference credit ratings in Rule 2a-7 and Form N-MFP, under the Investment Company Act of 1940. Specifically, the amendments to Rule 2a-7 replace references to credit ratings in the rule with alternative standards designed to maintain a similar level of credit quality as under the rule prior to the amendments. The amendments to Form N-MFP require that a fund disclose any credit rating that the fund's board considered in determining the credit quality of a portfolio security. The amendments were adopted pursuant to section 939A of the Dodd-Frank Act.

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26 Available at: http://www.sec.gov/litigation/admin/2015/34-76261.pdf.

27 Available at: http://www.sec.gov/rules/exorders/2015/34-76183.pdf.

28 Available at: http://www.sec.gov/rules/exorders/2015/34-76129.pdf.

29 Available at: http://www.sec.gov/rules/final/2015/ic-31828.pdf.

- Order Granting Temporary Conditional Exemption for Japan Credit Rating Agency, Ltd. from Certain Requirements of Section 15E(t) of the Securities Exchange Act of 1934, Release No. 34-75747 (Aug. 20, 2015).[30] The Commission granted JCR a temporary, conditional exemption until August 20, 2018 from certain corporate governance requirements under section 15E(t).

- Final Rule: Adoption of Updated EDGAR Filer Manual, Release Nos. 33-9874, 34-75586, 39-2505, and IC-31735 (Aug. 3, 2015), 80 FR 51123 (Aug. 24, 2015).[31] The Commission adopted revisions to the Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system and related rules to reflect updates, including those enabling NRSROs to deliver certain forms and reports to the Commission electronically, as required under the rule amendments adopted by the Commission with respect to NRSROs on August 27, 2014.

IV. COMPETITION

A. Select NRSRO Statistics

Sections 1 through 3 below summarize and discuss certain information reported by NRSROs on Form NRSRO or pursuant to Rule 17g-3 that provides insight into the state of competition among NRSROs. While this information indicates that Moody's, S&P, and Fitch continue to account for the highest percentages of outstanding ratings, other information suggests that smaller NRSROs have been able to gain market share in certain rating categories.[32]

1. NRSRO Credit Ratings Outstanding

(a) Number of Outstanding Ratings in Statutory Rating Categories

Each NRSRO annually reports the number of credit ratings outstanding, as of the end of the preceding calendar year, in each rating category for which it is registered.[33] This information, for the calendar year ending December 31, 2015, is summarized in Charts 1 through 4 below and can be useful in determining the breadth of an NRSRO's coverage with respect to issuers and obligors within a particular rating class.

30 Available at: http://www.sec.gov/rules/exorders/2015/34-75747.pdf.

31 Available at: http://www.sec.gov/rules/final/2015/33-9874.pdf.

32 As discussed in Section IV.B.1. of this Report, information available on the websites of Commercial Mortgage Alert (https://www.cmalert.com/) and Asset-Backed Alert (https://www.abalert.com/) regarding NRSRO market shares in the asset-backed securities category indicates that some of the smaller NRSROs have developed significant market shares in such category over the past few years. In addition, Section IV.B.3. of this Report provides examples of certain asset classes in which it has been reported that smaller NRSROs have been able to gain market share and discusses other developments relevant to competition among NRSROs.

33 Annual certifications on Form NRSRO must be filed with the Commission on EDGAR pursuant to Rule 17g-1(f) and made publicly and freely available on each NRSRO's website pursuant to Rule 17g-1(i). The number of outstanding credit ratings for each class of credit ratings for which an NRSRO is registered is reported on Item 7A of Form NRSRO.

Chart 1 depicts the number of credit ratings each NRSRO had outstanding in each rating category for which it was registered as of December 31, 2015. Chart 2 shows the percentage of credit ratings each NRSRO had outstanding across all rating categories and also breaks out the percentages for each NRSRO in each of the rating categories. Chart 3 illustrates the relative size of each rating category based on the aggregate number of ratings reported outstanding by all NRSROs. Chart 4 depicts the percentage of ratings each NRSRO had outstanding across all rating categories other than the government securities category.

Comparing the number of ratings *outstanding* for established NRSROs and newer NRSROs may not provide as comprehensive a picture of the state of competition as comparing the number of ratings *issued* by such NRSROs in a given period. Certain NRSROs (particularly S&P, Moody's, and Fitch) have a longer history of issuing ratings and their ratings include those for debt obligations and obligors that were rated well before the establishment of the newer entrants.[34] Consequently, the information described in Section IV.B.1. of this Report (relating to recent market share developments in the asset-backed securities rating category) may provide additional insight regarding how well newer entrants are competing with more established rating agencies, specifically in the asset-backed securities rating category.

The number of outstanding ratings reported by the NRSROs provides insights into the state of competition in each rating class and in the aggregate, but assessing the state of competition based on this data has some limitations. For instance, during the Report Period some NRSROs have pursued business strategies to specialize in particular rating categories or sub-categories[35] and chosen not to issue ratings in certain of the other rating categories. Also, the reported information does not reflect any credit ratings being issued by NRSROs in classes of ratings in which they are not registered with the Commission, nor does it reflect ratings issued by an affiliate of an NRSRO unless the affiliate is identified as a credit rating affiliate on Item 3 of Form NRSRO.

Further, the outstanding ratings reported by the NRSROs are based on their own determinations of the applicable categories and number of ratings, which are not necessarily consistent among all the NRSROs. As NRSROs adjust their ratings count disclosures in accordance with the new instructions to Form NRSRO (which are designed to enhance

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[34] The ratings counts disclosed on Item 7A of Form NRSRO include outstanding credit ratings, regardless of when they were issued. As a result, the ratings counts of the more established NRSROs may include credit ratings that were issued before the newer entrants began issuing credit ratings. These earlier ratings will continue to be included in the disclosed ratings counts until the rated securities are repaid or the credit ratings are otherwise withdrawn. Because outstanding ratings are included in the ratings counts, historical results factor significantly into the disclosed number of ratings, making it more difficult to discern current-year trends and identify gains achieved by the newer entrants.

[35] For example, A.M. Best with respect to insurance companies and their affiliates; JCR with respect to Japanese issuers and securities; and HR Ratings with respect to Mexican securities.

comparability across NRSROs), comparisons to ratings counts disclosed in prior years may also be affected.[36]

Chart 1 provides the number of outstanding credit ratings reported by each NRSRO in its annual certification for the calendar year ending December 31, 2015, in each of the five categories identified in section 3(a)(62) for which the NRSRO is registered, as applicable.

Chart 1: Number of Outstanding Credit Ratings as of December 31, 2015 by Rating Category*						
NRSRO	**Financial Institutions**	**Insurance Companies**	**Corporate Issuers**	**Asset-Backed Securities**	**Government Securities**	**Total Ratings**
A.M. Best	N/R	7,710	1,445	18	N/R	9,173
DBRS	8,487	143	3,536	12,848	16,947	41,961
EJR	11,251	1,015	6,384	N/R	N/R	18,650
Fitch	43,798	3,077	16,734	41,517	198,375	303,501
HR Ratings	N/R	N/R	N/R	N/R	347	347
JCR	770	59	2,227	N/R	428	3,484
KBRA	443	4	4	4,259	55	4,765
Moody's	50,094	3,175	42,821	68,494	637,898	802,482
Morningstar	N/R	N/R	N/R	3,306	N/R	3,306
S&P	60,005	6,896	51,105	64,222	964,704	1,146,932
Total	**174,848**	**22,079**	**124,256**	**194,664**	**1,818,753**	**2,334,600**

* N/R indicates that the NRSRO was not registered in the applicable rating category as of the reporting date.
Source: NRSRO annual certifications for the 2015 calendar year, Item 7A on Form NRSRO

Chart 2 displays the percentage of each NRSRO's outstanding credit ratings of the total outstanding credit ratings of all NRSROs, for each rating category in which the NRSRO was registered, based on information reported by the NRSROs as of December 31, 2015.[37]

[36] Effective January 1, 2015, Item 7A of Form NRSRO and the corresponding instructions were amended to clarify the manner in which the number of outstanding credit ratings should be calculated and presented. The clarifying amendments are designed to ensure that disclosures on Item 7A of Form NRSRO are consistent across NRSROs. The change in instructions may have caused some NRSROs to modify the way they count ratings for purposes of Item 7A of Form NRSRO, which may affect comparisons to disclosures made in prior years. See Nationally Recognized Statistical Rating Organizations, Release No. 34-72936 (Aug. 27, 2014), 79 FR 55077 (Sept. 15, 2014) ("Adopting Release") at 55220-22 (discussing the clarifying amendments to Item 7A of Form NRSRO).

[37] For example, according to Chart 1, A.M. Best reported that it had 7,710 insurance company credit ratings, and the total of the credit ratings in that category reported by all NRSROs was 22,079. Dividing 7,710 by 22,079 equals (approximately) 0.349 or 34.9% (which is the percentage of NRSRO insurance company ratings attributable to A.M. Best, as shown on Chart 2).

Chart 2: Percentage by Rating Category of Each NRSRO's Outstanding Credit Ratings of the Total Outstanding Credit Ratings of all NRSROs, as of December 31, 2015*						
NRSRO	**Financial Institutions**	**Insurance Companies**	**Corporate Issuers**	**Asset-Backed Securities**	**Government Securities**	**Total Ratings**
A.M. Best	N/R	34.9%	1.2%	<0.1%	N/R	0.4%
DBRS	4.9%	0.6%	2.8%	6.6%	0.9%	1.8%
EJR	6.4%	4.6%	5.1%	N/R	N/R	0.8%
Fitch	25.0%	13.9%	13.5%	21.3%	10.9%	13.0%
HR Ratings	N/R	N/R	N/R	N/R	<0.1%	<0.1%
JCR	0.4%	0.3%	1.8%	N/R	<0.1%	0.1%
KBRA	0.3%	<0.1%	<0.1%	2.2%	<0.1%	0.2%
Moody's	28.7%	14.4%	34.5%	35.2%	35.1%	34.4%
Morningstar	N/R	N/R	N/R	1.7%	N/R	0.1%
S&P	34.3%	31.2%	41.1%	33.0%	53.0%	49.1%

* N/R indicates that the NRSRO was not registered in the applicable rating category as of the reporting date. Percentages have been rounded to the nearest one-tenth of one percent.
Source: NRSRO annual certifications for the 2015 calendar year, Item 7A on Form NRSRO

As illustrated in Chart 2, S&P, Moody's, and Fitch in the aggregate account for 96.5% of all the ratings outstanding as of December 31, 2015--slightly higher than 95.8% as of December 31, 2014.[38] This change is attributable to an increase in outstanding ratings for these NRSROs in the financial institutions and corporate rating categories, which was partially offset by a lower percentage in the asset-backed securities rating category.

Chart 2 also illustrates the relative percentages of ratings outstanding among the NRSROs. S&P accounts for the highest number of ratings outstanding with nearly half (49.1%) of the total number of ratings reported by all NRSROs. Moody's reported the second highest number of ratings outstanding, accounting for 34.4% of the total. Fitch was third and DBRS was fourth, with 13.0% and 1.8% of the total, respectively. Each other NRSRO reported less than 1.0% of the total number of ratings outstanding.

Finally, Chart 2 shows notably that, in the insurance category, A.M. Best had the most credit ratings outstanding. A.M. Best has consistently reported being one of the top three issuers of insurance ratings since this information began to be reported in 2007.

Chart 3 depicts the percentages of outstanding credit ratings attributable to each rating category, based on information reported by the NRSROs as of December 31, 2015.

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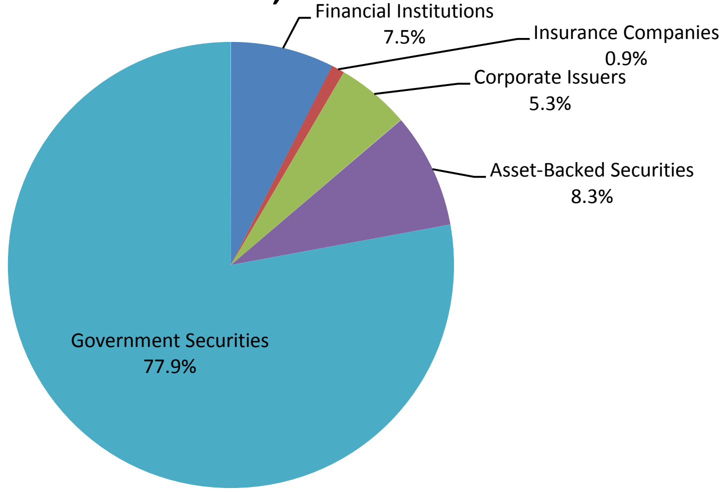
[38] In 2007, the year when NRSROs began reporting outstanding ratings on Form NRSRO, these NRSROs accounted for 98.8% of all outstanding ratings.

Chart 3: Breakdown of Ratings Reported Outstanding on December 31, 2015*



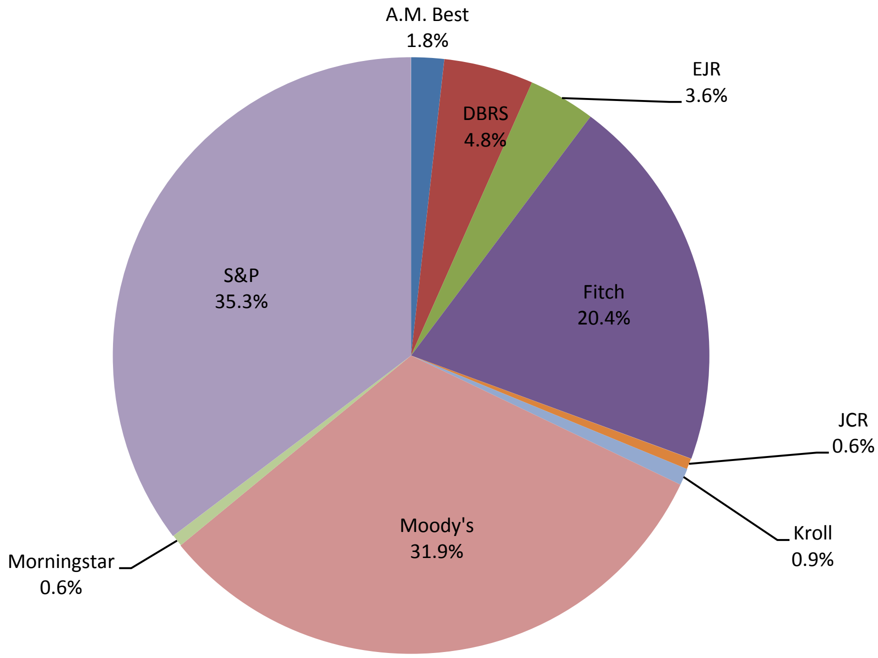
* Percentages have been rounded to the nearest one-tenth of one percent.
Source: NRSRO annual certifications for the 2015 calendar year, Item 7A on Form NRSRO

As illustrated by Chart 3, as of December 31, 2015, a disproportionate number of the aggregate credit ratings reported to be outstanding were in the government securities category, which may be attributable to the large number of government bond issuers and their multiple debt offerings. The government securities category accounted for 77.9% of the total number of credit ratings reported across all categories and, as shown on Chart 2, is also the most concentrated rating category, with Moody's and S&P accounting for 88.1% of all outstanding government ratings.

Given the disproportionate size of the government securities rating category relative to the other rating categories and the high concentration of NRSROs rating government securities, the inclusion of the government securities category in the calculation of total market share for each NRSRO may make it difficult to assess the relative market shares of the smaller NRSROs.

Chart 4 depicts the percentages of the credit ratings outstanding that are attributable to each NRSRO over all rating categories other than the government securities category, based on information reported by the NRSROs as of December 31, 2015. This chart includes all NRSROs which issue ratings in rating categories other than government securities.

Chart 4: Breakdown of Non-Government Securities Ratings Reported Outstanding on December 31, 2015*



* Percentages have been rounded to the nearest one-tenth of one percent.
Source: NRSRO annual certifications for the 2015 calendar year, Item 7A on Form NRSRO

A comparison of Chart 4 to Chart 2 (which shows each NRSRO's total market share over all rating categories, including government securities) illustrates that there is less concentration in the non-government securities rating categories. S&P's and Moody's percentage share of the overall market declines by 13.8 and 2.5 percentage points, respectively, when government securities are excluded. Fitch's percentage share of outstanding ratings, on the other hand, increases by 7.4 percentage points when government securities are excluded. The market share percentage for all the remaining NRSROs other than HR Ratings (which was registered only in the government securities category as of the applicable reporting date) also increases when government securities are excluded. Further, when government securities are included in the total calculation, all but one (i.e., DBRS) of the NRSROs aside from S&P, Moody's, and Fitch have less than 1.0% of the market share, making it difficult to assess their relative market shares. When government securities are excluded, a clearer picture of the relative market shares of the smaller NRSROs can be observed, as illustrated in Chart 4.

As discussed above, Charts 1 through 4 reflect the number of credit ratings outstanding as of December 31, 2015, which may include credit ratings that were issued years ago. For a discussion of recent market share developments in the asset-backed securities rating category and other developments that could impact NRSRO market share, see Section IV.B of this Report.

(b) Industry Concentration

Economists generally measure industry concentration, which indicates the competitiveness of an industry, by using the Herfindahl-Hirschman Index ("HHI").[39] The inverse of the HHI ("HHI Inverse") can be used to represent the number of firms with equal market share necessary to replicate the degree of concentration in a particular industry.[40] In other words, an industry with an HHI Inverse of 3.0 has a concentration that is equal to an industry where the entire market is evenly divided among three firms with a market share of one third each. A highly concentrated market will have a low HHI Inverse, whereas an unconcentrated market will have a high HHI Inverse.[41]

Calculations of the HHI and HHI Inverse for the NRSRO industry are consistent with the results included in Section IV.A.1(a) of this Report and further illustrate gains in market share made by smaller NRSROs in the asset-backed securities rating category. Based on the number of outstanding ratings included in such section,[42] the HHI Inverse indicates that the NRSRO industry constitutes a "highly concentrated" market, and has the equivalent concentration of an industry with approximately 2.65 firms with equal market share. This is consistent with the high proportion of outstanding ratings that have been issued by the three largest NRSROs. Although the industry remains highly concentrated, a comparison of the HHI Inverse calculations since 2010 shows that the asset-backed securities rating category has become less concentrated.

Chart 5 reports the HHI Inverses calculated from 2008 to 2015 for the ratings outstanding (as reported by the NRSROs) in each rating category, in total for all rating categories, and in total for all rating categories excluding government securities.

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39 See, e.g., U.S. Department of Justice and the Federal Trade Commission, Horizontal Merger Guidelines §5.3 (2010) (discussing how the Department of Justice and the Federal Trade Commission use HHI to measure the impact of a merger on market concentration); however, since the HHI calculation does not take into account that multiple NRSROs may rate a single issue, different considerations may be applicable to the use of the HHI calculation for NRSROs.

40 The HHI Inverse is calculated by dividing 10,000 (i.e., the highest possible HHI) by the HHI. For additional discussion of the HHI Inverse, see VERA PAWLOWSKY-GLAHN & ANTONELLA BUCCIANTI, COMPOSITIONAL DATA ANALYSIS: THEORY AND APPLICATIONS (2011); Toby Roberts, When Bigger is Better: A Critique of the Herfindahl-Hirschman Index's Use to Evaluate Mergers in Network Industries, 34 PACE L. REV. 894, 908 (2014).

41 A market with an HHI Inverse of less than 4.0 is considered to be highly concentrated; a market with an HHI Inverse between 4.0 and 6.67 is considered to be moderately concentrated; and a market with an HHI Inverse above 6.67 is considered to be unconcentrated. See generally U.S. Department of Justice and the Federal Trade Commission, Horizontal Merger Guidelines §5.3 (2010).

42 See Section IV.A.1(a) of this Report for a discussion of certain limitations involved in determining the number of outstanding ratings reported.

Chart 5: HHI Inverses for Each Rating Category

Year	Financial Institutions *	Insurance Companies **	Corporate Issuers**	Asset-Backed Securities *	Government Securities*	Total (all rating categories)	Total Excluding Government Securities
2008	3.72	4.05	3.79	2.82	2.83	2.99	3.56
2009	3.85	3.84	3.18	3.18	2.65	2.86	3.58
2010	3.99	3.37	3.17	3.20	2.69	2.88	3.55
2011	4.16	3.76	3.02	3.38	2.47	2.74	3.70
2012	4.04	3.72	3.00	3.44	2.50	2.75	3.68
2013	3.99	3.68	3.03	3.48	2.46	2.72	3.65
2014	4.30	3.83	3.35	3.34	2.40	2.68	3.81
2015	3.72	3.82	3.23	3.53	2.40	2.65	3.67

* Seven credit rating agencies were registered in this rating category as of the applicable reporting date. Therefore, the highest possible HHI Inverse (in a perfectly competitive market where all firms have an equal share of business) would be 7.0.

** Eight credit rating agencies were registered in this rating category as of the applicable reporting date. Therefore, the highest possible HHI Inverse (in a perfectly competitive market where all firms have an equal share of business) would be 8.0.

Source: NRSRO annual certifications for the 2008-15 calendar years, Item 7A on Form NRSRO

As mentioned in Section IV.A.1(a) of this Report, as of December 31, 2015, the government securities rating category (which includes sovereigns, U.S. public finance, and international public finance) was the largest class of ratings (comprising approximately 77.9% of all ratings outstanding). Given the disproportionate size of the government securities rating category relative to the other rating categories and the high concentration of NRSROs rating government securities, the inclusion of the government securities category in the calculation of the aggregate HHI Inverse may make it difficult to assess the level of market concentration in the other four rating categories.

The government securities category is the most concentrated rating category, as indicated by a HHI Inverse of 2.40. The other four rating categories are less concentrated than the government securities category.

Industry concentration in the asset-backed securities category is at its lowest point (i.e., having the highest HHI Inverse and reflecting the greatest historical competition) since NRSROs began reporting information regarding the number of ratings outstanding on Form NRSRO. This may reflect increased competition from some of the smaller NRSROs which have focused on rating securities in this category (see Section IV.B.1. of this Report for a discussion of recent NRSRO market shares in the asset-backed securities sector). The other rating categories were more concentrated in 2015 than they were in 2008, except for the financial institutions rating category, which is at the same level of concentration as in 2008.

2. NRSRO Analytical Staffing Levels

Chart 6 reports the number of credit analysts (including credit analyst supervisors) and the number of credit analyst supervisors employed by each of the NRSROs, as reported on Exhibit 8 of Form NRSRO, and the ratio of credit analyst supervisors to credit analysts.[43]

Chart 6: NRSRO Credit Analysts and Credit Analyst Supervisors

NRSRO	Credit Analysts (Including Credit Analyst Supervisors)	Credit Analyst Supervisors	Ratio of Credit Analyst Supervisors to Credit Analysts
A.M. Best	125	46	1 : 1.7
DBRS	171	41	1 : 3.2
EJR	12	4	1 : 2.0
Fitch	1,100	304	1 : 2.6
HR Ratings	44	8	1 : 4.5
JCR	62	31	1 : 1.0
KBRA	127	20	1 : 5.4
Moody's	1,601	197	1 : 7.1
Morningstar	68	12	1 : 4.7
S&P	1,453	168	1 : 7.6
Total	**4,763**	**831**	**1 : 4.7**

Source: NRSRO annual certifications for the 2015 calendar year, Exhibit 8 on Form NRSRO

The three largest NRSROs report employing 4,154 credit analysts (including supervisors), which is approximately 87.2% of the total number employed by all of the NRSROs. Although the smaller NRSROs in the aggregate employ only approximately 12.8% of all credit analysts employed by NRSROs, this percentage has increased steadily in recent years.[44] During this time, some of the smaller NRSROs have reported significant increases in their analytical staff.[45] The trend in the number of rating analysts employed by an NRSRO can indicate the state of the NRSRO's business or its business outlook–i.e., NRSROs that are increasing their staff may be experiencing or anticipating an increase in ratings volumes or

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43 Effective January 1, 2015, the instructions for Exhibit 8 of Form NRSRO were amended to clarify that NRSROs must include credit analyst supervisors in the total number of credit analysts disclosed on Exhibit 8. This amendment was designed to enhance consistency of the disclosures on Exhibit 8 of Form NRSRO. Prior to this amendment, some NRSROs may have excluded credit analyst supervisors from the total number of credit analysts disclosed.

44 Based on reports by the currently-registered NRSROs on their annual certifications for the applicable calendar year, the smaller NRSROs employed approximately 9.6% of all NRSRO analysts in 2013 and 11.4% of all NRSRO analysts in 2014.

45 For example, KBRA reported on its most recent annual certification that it employs 127 credit analysts and supervisors, as compared to 13 reported for 2010.

planning to enter new markets. In addition, comparing the breadth of staffing across NRSROs may provide insight into the adequacy of the managerial resources at each NRSRO.

3. NRSRO Revenue Growth

The total revenue reported to the Commission[46] by all of the NRSROs for their 2015 fiscal year was approximately $5.9 billion, which was about the same amount reported in the 2014 fiscal year. Chart 7 shows the percentage of total NRSRO revenues since 2012 that were accounted for by S&P, Fitch, and Moody's in the aggregate and by all other NRSROs in the aggregate.

Chart 7: NRSRO Revenue Information: Fiscal Year Percentage of Total Reported NRSRO Revenue

	2012	**2013**	**2014**	**2015**
S&P, Fitch, and Moody's	94.7%	94.5%	94.3%	93.2%
All Other NRSROs	5.3%	5.5%	5.7%	6.8%
Total	100.0%	100.0%	100.0%	100.0%

Source: Financial reports provided to the Commission under Rule 17g-3 for the fiscal years ended 2012-15

Further revenue information is available for NRSROs that are owned, in whole or in part, by public companies. The following information is from the 2015 Annual Report on Form 10-K and other annual reports of public companies with an ownership interest in an NRSRO:

- Moody's Corporation, the owner of Moody's, attributes a 3.0% increase in revenues at Moody's from the previous fiscal year to changes in the mix of fee type, new fee initiatives and certain pricing increases, primarily in the U.S., coupled with growth in rated issuance volumes for investment-grade corporate debt. The growth also reflects increases across all asset classes within the structured finance group and increased issuance of securities related to the banking sector.[47]
- S&P Global Inc. ("S&P Global"), which is S&P's parent company, indicated that revenue at S&P declined by 1.0% compared to its 2014 results and attributed the decline to the unfavorable impact of foreign exchange rates and a decline in structured finance revenue

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46 Under Rule 17g-3(a)(3), NRSROs are required to provide to the Commission annual unaudited reports that include revenue information. These reports are not required to be made publicly available.

47 See Moody's Corporation Annual Report on Form 10-K for the year ended December 31, 2015, available at: http://s21.q4cdn.com/431035000/files/doc_financials/annual/Annualreport.pdf.

driven by reduced global market issuance. These declines were partially offset by an increase in U.S. public finance issuance.[48]

- Fimalac, S.A., an equity investor in Fitch's parent, Fitch Group, Inc., attributed an 8.5% increase in revenues at Fitch compared to fiscal year 2014 to increases across most asset classes driven by favorable issuance trends, continued acceptance of Fitch's credit opinions and business development efforts worldwide.[49]
- Morningstar's parent company, Morningstar, Inc., stated that revenue increased at Morningstar due to higher new issuance volume for the year.[50]

The growth in revenues experienced by most of these NRSROs in 2015 did not continue during the first half of 2016. According to quarterly regulatory filings of their parent companies, revenues at Moody's and S&P decreased by 7% and 2%, respectively, during the first half of 2016, as compared to the first half of 2015.[51] Moody's Corporation attributes this revenue decline to declines in the issuance volumes of collateralized loan obligations ("CLOs"), residential mortgage-backed securities, and high-yield corporate debt.[52] S&P Global attributes its decline in revenue to the impact of foreign exchange rates, reduced corporate bond issuance in the U.S. and European region during the first quarter of 2016, and lower structured finance issuance. Additionally, Morningstar, Inc. reported that revenue at Morningstar had decreased during the second quarter of 2016 due to lower issuance volumes of commercial mortgage-backed securities.[53]

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48 See McGraw Hill Financial, Inc. Annual Report on Form 10-K for the year ended December 31, 2015, available at: http://investor.spglobal.com/Annual-Reports/Index?KeyGenPage=1073751495.

49 See Fimalac Presentation 2015 Results, available at: http://www.fimalac.com/items/files/6b5617113eb2116dbb25720f1d8f135f_Fimalac-comptes-au-31-dec-2015-v2-gb.pdf.

50 See Morningstar, Inc. 2015 Annual Report, available at: https://corporate.morningstar.com/us/documents/PR/Morningstar-Annual-Report-2015.pdf.

51 See Moody's Corporation Quarterly Report on Form 10-Q, dated June 30, 2016, available at: http://d1lge852tjjqow.cloudfront.net/CIK-0001059556/15f181d1-9d6c-4fbe-a4e9-814524387ce9.pdf?noexit=true; S&P Global Inc. Quarterly Report on Form 10-Q, dated June 30, 2016, available at: http://investor.spglobal.com/Cache/35267941.pdf.

52 For additional information on issuance trends during the Report Period, see http://www.sifma.org/research/reports.aspx.

53 See Morningstar, Inc. Quarterly Report on Form 10-Q, dated June 30, 2016, available at: http://files.shareholder.com/downloads/MORN/2562473419x0xS1289419-16-279/1289419/filing.pdf.

B. Recent Developments in the State of Competition among NRSROs

1. Market Share Developments in the Asset-Backed Securities Rating Category

Based on information from the websites of Commercial Mortgage Alert and Asset-Backed Alert,[54] some of the smaller NRSROs have developed significant market shares in the asset-backed securities rating category over the past few years. The market share data reported on these websites indicate that the growth trend the Staff has observed since the 2012 Annual Report for some smaller NRSROs in some asset-backed securities asset classes continued during the Report Period. Sections (a) and (b) below include market share information reported on these websites as to commercial mortgage-backed securities ("CMBS"), asset-backed securities ("ABS"), and mortgage-backed securities ("MBS"), as further described in the following paragraph.[55]

The following definitions from the Commercial Mortgage Alert and Asset-Backed Alert websites apply to the determination of reported market share statistics: (i) CMBS is comprised of transactions collateralized by mortgages or leases on commercial or multi-family income-producing properties;[56] (ii) the ABS category is comprised of securities that are collateralized by assets (excluding mortgages, issuances by municipalities (i.e., revenue bonds), tax exempt issues, issues that are fully retained by an affiliate of the deal sponsor, commercial paper, and other continuously offered securities such as medium-term notes);[57] and (iii) the MBS category is comprised of first lien mortgages on residential properties.[58]

According to a report published by S&P, issuance of structured finance transactions decreased by 28.4% during the first eight months of 2016 as compared to the same period in 2015.[59] Specifically, asset classes such as CLOs, residential mortgage-backed securities, and commercial mortgage-backed securities, in each case, as designated by S&P, experienced significant decreases in issuance volumes during this period (i.e., 47.9%, 37.1%, and 40.0%, respectively).

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54 See https://www.abalert.com/ and https://www.cmalert.com/. Although the information available on these websites may provide insight into recent developments regarding the state of competition among NRSROs in the asset-backed securities rating category, it has certain limitations. For instance, the information is self-reported by NRSROs. In addition, the information is presented using the number of transactions with respect to which an NRSRO has reported issuing a credit rating and the aggregate dollar amount thereof, rather than indicating where an NRSRO may have rated fewer than all tranches of a particular transaction.

55 References to U.S. ABS, MBS, and CMBS issuance and market shares in this Section IV.B.1. reflect securities issued for sale primarily in the U.S., which includes securities issued publicly and those issued under Rule 144A. See https://www.abalert.com/market/about_db.pl; https://www.cmalert.com/market/about_db.pl.

56 See https://www.cmalert.com/market/about_db.pl.

57 See https://www.abalert.com/market/about_db.pl.

58 See id.

59 See Ben Lane, S&P: Private mortgage bond well running dry, September 1, 2016, available at: http://www.housingwire.com/articles/37945-sp-mortgage-bond-well-is-running-dry.

The market shares of some of the NRSROs discussed below may have been affected by market volatility associated with such factors as declining oil prices and uncertainty regarding the direction of China's economy, Federal Reserve plans to increase interest rates, and the potential effects of new regulations.[60] However, since issuance of structured finance transactions has increased during the second half of 2016,[61] there may be some variation between the market shares that were reported for the first half of 2016 and those that will be reported for the second half of 2016.

(a) CMBS

The number of ratings recently issued by NRSROs may give a clearer picture of competition than the number of ratings each NRSRO currently has outstanding. For example, Chart 2 indicates that, as of December 31, 2015, S&P, Moody's, and Fitch have issued 89.5% of the ratings outstanding in the asset-backed securities class of ratings, which includes ratings on CMBS. However, information from the Commercial Mortgage Alert's website indicates that smaller NRSROs issued 46.2% of the CMBS ratings issued during the 2015 calendar year.[62]

Charts 8 through 10 provide information concerning U.S. CMBS ratings by NRSROs, as reported to Commercial Mortgage Alert.[63] NRSRO market share varies between the conduit CMBS and single borrower CMBS segments,[64] the two segments that account for most of the U.S. CMBS transactions rated by NRSROs. The charts include reported market share information for total U.S. CMBS transactions,[65] U.S. conduit CMBS transactions, and U.S. single borrower CMBS transactions for calendar year 2014, calendar year 2015, and the first half of calendar year 2016.

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60 See Expectations for 2016 CMBS Issuance Slashed Sharply, March 2, 2016, available at: http://www.crenews.com/general_news/general/expectations-for-2016-cmbs-issuance-slashed-sharply.html.

61 See "US ABS Issuance and Outstanding," and "US Mortgage-Related Issuance and Outstanding," available at: http://www.sifma.org/research/statistics.aspx.

62 According to the Commercial Mortgage Alert's database, KBRA, Morningstar, and DBRS issued 19.3%, 15.4%, and 11.5%, respectively, of the CMBS ratings issued during calendar year 2015. See https://www.cmalert.com/db/cmbs_db.pl.

63 The charts reflect market share percentages based on dollar amounts of issuance. The market shares of individual NRSROs do not add up to 100% since more than one NRSRO may rate a particular transaction or obligor. CMBS market share data is from the Commercial Mortgage Alert, available at: https://www.cmalert.com/rankings.pl?Q=78.

64 The term "conduit," which had been previously referred to by Asset-Backed Alert as "conduit /fusion," refers to a financial intermediary that functions as a link, or conduit, between the lender(s) originating loans and the ultimate investor(s). The conduit makes loans to, or purchases loans from, third parties under standardized terms, underwriting, and documents and then, when sufficient volume has been accumulated, pools the loans for sale to investors in the CMBS market. See http://www.crefc.org/uploadedFiles/CMSA_Site_Home/Industry_Resources/Research/Glossary.pdf. In contrast, a single borrower transaction includes commercial mortgage loans made to a single borrower.

65 Total U.S. CMBS ratings include conduit CMBS, single-borrower CMBS, and other types of CMBS, such as distressed/non-performing CMBS transactions and re-securitizations of CMBS transactions.

Chart 8: Rating Agencies for CMBS Issued in 2014, 2015, and First Half of 2016 Total U.S. CMBS*										
1H 2016 Rank	**NRSRO**	**1H-2016 Issuance ($Mil.)**	**No. of deals**	**Market Share (%)**	**2015 Issuance ($Mil.)**	**No. of deals**	**Market Share (%)**	**2014 Issuance ($Mil.)**	**No. of deals**	**Market Share (%)**
1	Moody's	$22,895.6	29	74.6	$71,525.7	77	70.8	$62,036.7	66	65.9
2	Fitch	21,776.6	30	70.9	55,720.2	67	55.2	45,406.6	48	48.3
3	KBRA	12,793.3	19	41.7	58,557.6	70	58.0	53,790.1	65	57.2
4	DBRS	8,542.1	12	27.8	28,429.5	35	28.1	37,183.5	43	39.5
5	S&P	6,368.1	16	20.7	25,900.9	43	25.6	31,614.2	53	33.6
6	Morningstar	4,680.6	9	15.2	44,179.0	56	43.7	31,129.7	45	33.1
	Total Rated Market	**$30,707.4**	**71**		**$101,008.5**	**160**		**$94,084.4**	**134**	

Source: https://www.cmalert.com/rankings.pl?Q=78

Chart 9: Rating Agencies for CMBS Issued in 2014, 2015, and First Half of 2016 U.S. Conduit*										
1H 2016 Rank	**NRSRO**	**1H-2016 Issuance ($Mil.)**	**No. of deals**	**Market Share (%)**	**2015 Issuance ($Mil.)**	**No. of deals**	**Market Share (%)**	**2014 Issuance ($Mil.)**	**No. of deals**	**Market Share (%)**
1	Moody's	$19,005.5	23	100.0	$62,118.7	60	100.0	$54,027.6	47	94.0
2	Fitch	17,539.3	21	92.3	39,001.9	38	62.8	39,008.6	33	67.8
3	KBRA	10,895.3	13	57.3	45,093.4	43	72.6	39,096.4	33	68.0
4	DBRS	7,367.5	9	38.8	23,769.3	22	38.3	32,523.3	29	56.6
5	Morningstar	3,085.3	4	16.2	27,568.4	26	44.4	14,464.3	13	25.2
6	S&P	0.0	0	0.0	0.0	0	0.0	5,070.3	4	8.8
	Total Rated Market	**$19,005.5**	**23**		**$62,118.7**	**60**		**$57,497.4**	**50**	

Source: https://www.cmalert.com/rankings.pl?Q=78

Chart 10: Rating Agencies for CMBS Issued in 2014, 2015, and First Half of 2016 U.S. Single Borrower*										
1H 2016 Rank	**NRSRO**	**1H-2016 Issuance ($Mil.)**	**No. of deals**	**Market Share (%)**	**2015 Issuance ($Mil.)**	**No. of deals**	**Market Share (%)**	**2014 Issuance ($Mil.)**	**No. of deals**	**Market Share (%)**
1	S&P	$5,028.2	12	73.9	$24,285.2	40	79.1	$20,510.9	35	81.7
2	Moody's	3,659.9	5	53.8	7,012.0	9	22.8	4,763.9	7	19.0
3	Fitch	2,707.8	3	39.8	13,977.6	19	45.5	4,701.1	8	18.7
4	KBRA	1,102.0	3	16.2	10,171.7	15	33.1	7,555.4	13	30.1
5	DBRS	944.5	2	13.9	3,378.6	8	11.0	3,225.0	6	12.8
6	Morningstar	800.0	2	11.8	14,560.9	25	47.4	13,809.6	25	55.0
	Total Rated Market	**$6,801.2**	**13**		**$30,690.7**	**51**		**$25,099.8**	**43**	

Source: https://www.cmalert.com/rankings.pl?Q=78

* Charts 8-10 reflect market share percentages based on dollar amounts of issuance. The market shares of individual NRSROs do not add up to 100% since more than one NRSRO may rate a particular transaction or obligor.

As the charts above indicate, some of the smaller NRSROs continue to report significant market shares in the U.S. CMBS sector.[66] KBRA's market share of 41.7% during the first half of 2016 was the third highest in the sector, while DBRS' market share of 27.8% was the fourth highest. The market shares of these two NRSROs were particularly significant in the U.S. conduit CMBS sector, where KBRA and DBRS had the third (57.3%) and fourth (38.8%) highest market shares during the first half of 2016. Additionally, Morningstar's market share in the U.S. CMBS sector was 15.2% in the first half of 2016, reflecting market shares of 16.2% in the U.S. conduit CMBS sector and 11.8% in the single borrower CMBS sector.

As previously mentioned, difficult market conditions, which negatively affected CMBS issuance volumes, may have also adversely affected the market shares of some of the smaller NRSROs. According to one report, as market volatility rises and liquidity tightens, some CMBS issuers include ratings from at least two of the larger NRSROs on their deals.[67] This may have caused the market shares of some smaller NRSROs to decline in the first half of 2016 as compared to 2015. For example, KBRA's U.S. CMBS market share declined from 58.0% in 2015 to 41.7% in the first half of 2016. During the same period, Morningstar's market share in this sector declined from 43.7% to 15.2%.

The market share results from 2015 and the first half of 2016 for U.S. conduit CMBS may have also been affected by a settlement, dated January 21, 2015, between S&P and the Commission regarding charges relating to S&P's ratings on certain conduit CMBS.[68] The settlement terms include a twelve-month restriction from marketing or rating new issue conduit CMBS transactions. As shown in Chart 9, S&P did not rate any U.S. conduit CMBS transactions in 2015 or the first half of 2016. However, now that the restriction has ended, it has been reported that S&P may be re-entering this sector.[69]

(b) ABS/MBS[70]

Charts 11 and 12 provide information concerning U.S. ABS and U.S. MBS ratings by NRSROs. The charts show rankings for the rated public and Rule 144A ABS and MBS markets in the U.S.

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66 For example, KBRA's market share of the U.S. CMBS sector rose from 2.4% in the first half of 2011 to 41.7% in the first half of 2016. During the same period, DBRS' market share of the U.S. conduit CMBS sector rose from 23.9% to 38.8%. These represent the largest increases in market shares in these sectors among the NRSROs for this period.

67 See Moody's Tops Ranking; Fitch Overtakes Kroll, Commercial Mortgage Alert, July 15, 2016.

68 See In the Matter of Standard & Poor's Ratings Services, Release Nos. 33-9705 and 34-74104 (Jan. 21, 2015), available at: http://www.sec.gov/litigation/admin/2015/33-9705.pdf; SEC Announces Charges Against Standard & Poor's for Fraudulent Ratings Misconduct, Release No. 2015-10 (Jan. 21, 2015), available at: http://www.sec.gov/news/pressrelease/2015-10.html.

69 See Conduit Dealers Bringing S&P Out of Exile, Commercial Mortgage Alert, July 29, 2016.

70 ABS/MBS market share data is from the Asset-Backed Alert. See https://www.abalert.com/rankings.pl. Charts 11 and 12 reflect market share percentages based on dollar amounts of issuance. The market shares of individual NRSROs do not add up to 100% since more than one NRSRO may rate a particular transaction or obligor.

Chart 11: Rating Agency Market Shares for U.S. Public and Rule 144A ABS Issued in 2014, 2015, and First Half of 2016*

1H 2016 Rank	NRSRO	1H-2016 Issuance ($Mil.)	No. of deals	Market Share (%)	2015 Issuance ($Mil.)	No. of deals	Market Share (%)	2014 Issuance ($Mil.)	No. of deals	Market Share (%)
1	S&P	$61,919.9	102	57.6	$128,651.4	212	60.3	$149,757.0	241	67.9
2	Moody's	59,011.2	88	54.9	123,620.2	182	57.9	129,352.5	175	58.7
3	Fitch	58,669.8	80	54.6	115,824.6	169	54.2	121,224.8	170	55.0
4	DBRS	25,493.6	63	23.7	44,913.1	97	21.0	24,557.7	65	11.1
5	KBRA	16,527.4	49	15.4	21,572.0	63	10.1	19,556.2	46	8.9
6	Morningstar	1,433.4	5	1.3	7,317.8	16	3.4	6,751.1	12	3.1
7	A.M. Best	0.0	0	0.0	115.0	1	0.1	88.8	1	0.0
	Total Rated Market	**$107,469.8**	**195**		**$213,518.2**	**380**		**$220,426.9**	**363**	

Source: https://www.abalert.com/rankings.pl?Q=102

Chart 12: Rating Agency Market Shares for U.S. MBS Issued in 2014, 2015, and First Half of 2016*

1H 2016 Rank	NRSRO	1H-2016 Issuance ($Mil.)	No. of deals	Market Share (%)	2015 Issuance ($Mil.)	No. of deals	Market Share (%)	2014 Issuance ($Mil.)	No. of deals	Market Share (%)
1	Moody's	$2,250.2	7	67.7	$7,266.5	21	23.6	977.1	3	4.5
2	Fitch	1,235.1	4	37.2	7,614.3	26	24.7	5,025.9	16	23.0
3	DBRS	1,001.9	4	30.2	20,921.3	76	67.8	16,445.2	71	75.3
4	Morningstar	585.6	4	17.6	4,585.5	9	14.9	0.0	0	0.0
5	S&P	565.8	2	17.0	3,370.6	10	10.9	9,003.4	27	41.3
6	KBRA	344.9	1	10.4	6,890.5	22	22.3	4,183.1	13	19.2
	Total Rated Market	**$3,321.8**	**14**	**100.0**	**$30,842.9**	**103**		**$21,826.2**	**86**	

Source: https://www.abalert.com/rankings.pl?Q=102

* Charts 11 and 12 reflect market share percentages based on dollar amounts of issuance. The market shares of individual NRSROs do not add up to 100% since more than one NRSRO may rate a particular transaction or obligor.

As Chart 11 shows, while S&P, Moody's, and Fitch continue to report the largest market shares in the U.S. ABS sector, the smaller NRSROs appear to have built significant market share over the past few years. For example, the reported market shares of DBRS and KBRA increased between 2014 and the first half of 2016.[71]

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[71] DBRS increased its market share from 11.1% in 2014 to 23.7% during the first half of 2016. KBRA increased its market share from 8.9% to 15.4% during the same period.

Chart 12 shows reported NRSRO market share information for the MBS sector. According to a report by the Securities Industry and Financial Markets Association, U.S. MBS issuance decreased by about 40.0% during the first half of 2016 compared to the first half of 2015.[72] Similar to the CMBS sector, lower MBS issuance volumes may have also affected the market shares of some of the NRSROs during the first half of 2016.

During the first half of 2016, while Morningstar had the fourth largest market share in the MBS sector, it was the only smaller NRSRO to experience growth in its market share since 2015.[73] DBRS and KBRA both had decreases in their market shares during the first half of 2016. DBRS had a market share of 30.2%, which was the third highest market share during the first half of 2016.[74] KBRA's market share decreased to 10.4% in the first half of 2016 from 22.3% in 2015.

Each of the three larger NRSROs experienced growth in their market shares in the MBS sector. Moody's and Fitch had the first and second largest market shares, respectively, in this sector, while S&P had the fifth largest market share.[75]

2. NRSRO Registration in Additional Rating Categories

As mentioned in Section II of this Report, Morningstar and HR Ratings registered in the rating categories of financial institutions and corporate issuers after the Report Period ended. Morningstar's president was quoted in an article as saying that the NRSRO designation will allow Morningstar's ratings in these categories to be more acceptable to certain market participants.[76] The article further stated that Morningstar intends to compete with the larger rating agencies on rating new debt issuances by being more forward-looking than its rivals, and by incorporating emerging trends into its analysis.[77] Morningstar also stated that it intends to increase the number of analysts that focus on these two sectors.[78]

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72 See http://www.sifma.org/research/statistics.aspx.

73 Morningstar's MBS market share increased to 17.6% during the first half of 2016 compared to 14.9% in 2015.

74 DBRS previously had market shares of 67.8% and 75.3% in 2015 and 2014, respectively, which were the largest market shares in the MBS sector during those years.

75 Moody's MBS market share was 67.7% during the first half of 2016, which is an increase from its market share of 23.6% in 2015. Fitch's MBS market share in this sector increased to 37.2% from 24.7%, and S&P's MBS market share increased to 17.0% from 10.9%, during the same period.

76 See Kendall Baer, Morningstar Authorized to Rate Financial Institutions by SEC, available at: http://www.dsnews.com/daily-dose/09-05-2016/morningstar-authorized-rate-financial-institutions-sec.

77 See Lynne Market, Morningstar to rate corporate debt, August 29, 2016, available at: http://www.chicagobusiness.com/article/20160829/NEWS01/160829855/morningstar-to-rate-corporate-debt.

78 Prior to registering as an NRSRO in the corporate issuers and financial institutions rating categories, Morningstar's parent company, Morningstar, Inc. issued non-NRSRO ratings in these sectors.

HR Ratings has indicated that its registration as an NRSRO in the financial institutions and corporate issuers rating classes will enable it to expand the services it provides its clients.[79] The chairman of HR Ratings' board of directors was quoted as saying that such registration "marks the beginning of a new and important period of growth" for HR Ratings.[80]

As depicted in Chart 2, S&P, Moody's, and Fitch in the aggregate account for 88.0% and 89.1% of the financial institutions and corporate issuers ratings, respectively, which were outstanding as of December 31, 2015 and, as shown in Chart 5, both of these rating categories are highly concentrated. The introduction of Morningstar and HR Ratings operating as NRSROs in these rating categories would give market participants more sources of credit opinions and may increase the level of competition in these sectors. Increased competition in the corporate ratings sector may also bring more competition to the CLO sector since the ratings of the underlying corporate debt are a key input in determining CLO ratings. Due to this, NRSROs that have more corporate ratings tend to also rate more CLOs.

According to one report, issuance of corporate debt is projected to increase by about 46.5% between the end of 2015 and the end of 2020.[81] Reports have cited an increased investor interest in securities issued by financial institutions, which could lead to increased issuance of these securities.[82] Accordingly, registration in these rating categories may present market share opportunities for NRSROs so registered. However, it may take several years before the full effects of increased competition can be fully observed.

3. Other NRSRO Developments

As described in Section IV.B.1. of this Report, some of the smaller NRSROs have reported success in gaining market share in the asset-backed securities rating category. Some of these market share gains result from smaller NRSROs rating newer asset classes (such as single-family rental ("SFR") securitizations[83] and marketplace lending securitizations[84]).

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79 HR Ratings Press Release dated November 29, 2016, available at: http://www.prnewswire.com/news-releases/hr-ratings-expands-scope-of-international-operations-with-sec-registration-for-corporate-and-financial-institution-ratings-in-the-united-states-300369909.html.

80 Id.

81 See Terry E. Chan, et al., 2016 Global Corporate Debt Demand, July 2016, available at: https://www.spratings.com/documents/20184/1481001/Global+Corp+Credit_0718_HomeSector/f66b581b-c4e5-420e-abba-1ccc0ac28ca8.

82 See Will Caiger-Smith, Investors likely to welcome new US bank bonds, January 15, 2016, available at: http://www.reuters.com/article/usa-corpbonds-banks-idUSL1N14S2FU.

83 SFR securitizations are collateralized by rental income from residential rental properties and proceeds from the sale of residential rental properties. Ratings of the first rated SFR securitization were issued in November 2013.

84 The assets collateralizing marketplace lending securitizations are generally loans that were made through online platforms that connect borrowers with lenders. The first rated marketplace lending securitization was issued in December 2013.

KBRA and Morningstar have rated a very high percentage of the SFR securitizations issued.[85] During the Report Period, there were seven rated SFR securitizations issued. Of these deals, Morningstar issued ratings on all of them and KBRA issued ratings on five of them. Among the larger NRSROs, Moody's and Fitch are also active in this sector, having rated six and one, respectively, of the rated SFR transactions issued during the Report Period.

Research conducted by a credit risk analytics firm serving the peer-to-peer sector indicates that competition for rating marketplace lending transactions increased during the Report Period.[86] Both KBRA and Fitch issued their first ratings on these types of transactions during the Report Period. Other NRSROs active in this sector during the Report Period include S&P, Moody's, and DBRS. During the Report Period, DBRS, KBRA, and Moody's were the most active in this sector, having rated 28.6%, 25.0%, and 25.0% of the 28 rated marketplace lending transactions issued.[87] Fitch and S&P rated 7.1% and 3.6% of these deals, respectively.[88]

Smaller NRSROs are also rating other new types of asset-backed securities and issuances commonly referred to as "esoteric" asset-backed securities.[89] For example, during the Report Period, smaller NRSROs rated cell-tower leases securitizations,[90] small business loan securitizations,[91] railcar equipment notes,[92] aircraft lease bonds,[93] property assessed clean energy securitizations,[94] and franchise fee securitizations.[95]

Some smaller NRSROs continue to pursue expansion in more traditional types of asset-backed securities as well. For example, during the Report Period, Morningstar rated a non-

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85 According to the Asset-Backed Alert's database, as of June 30, 2016, there have been 30 rated SFR securitizations issued. Of these deals, 27 were rated by Moody's, KBRA, and Morningstar, two were rated by Fitch and Morningstar, and one was rated by Moody's and Morningstar.

86 See Marketplace Lending Securitization Tracker Q2 2016, available at: http://www.peeriq.com/research/.

87 Id.

88 Id.

89 According to some reports, esoteric asset classes such as aircraft leases and whole business securitizations are attracting more attention from traditional investors in high yield corporate bonds because some of these asset classes have higher ratings than high yield bonds with similar yields. See Glen Fest, ABS Vegas: Junk Bond Market's Pain is Esoteric's Gain, March 1, 2016 available at: http://www.asreport.com/news/abs/abs-vegas-junk-bond-markets-pain-is-esoterics-gain-260031-1.html.

90 See, e.g., LMRK Issuer Co. LLC, Series 2016-1, June 16, 2016, available at: https://www.krollbondratings.com/show_report/4282.

91 See, e.g., Oxford Finance Funding 2016-1 LLC, June 14, 2016, available at: https://www.krollbondratings.com/show_report/4375.

92 See, e.g., NP SPE II LLC, April 29, 2016, available at: https://www.krollbondratings.com/show_report/4104.

93 See, e.g., Apollo Aviation Securitization Equity Trust 2016-1, April 6, 2016, available at: https://www.krollbondratings.com/show_report/3927.

94 See, e.g., HERO Funding Trust 2016-2, June 6, 2016, available at: http://www.dbrs.com/research/295382/hero-funding-trust-2016-2-rating-report.pdf.

95 See, e.g., Arby's Funding, LLC, November 16, 2016, available at: https://www.krollbondratings.com/show_report/3155.

performing MBS transaction[96] and an auto loan securitization.[97] Morningstar also expanded its MBS re-REMIC rating business, as it rated eleven such transactions in the Report Period compared to one in the prior Report Period.[98]

Smaller NRSROs also continue to pursue rating opportunities outside of the asset-backed securities rating category. For example, during the Report Period, KBRA published criteria articles that describe its methodologies for rating global insurer and insurance holding companies and for rating non-profit higher education entities.[99]

Some smaller NRSROs entered in alliances with other entities or opened foreign offices, which may help the NRSROs compete in foreign markets. For example, JCR and HR Ratings entered into an alliance to collaborate with each other as strategic business partners.[100] JCR also entered into a strategic alliance with Credit Analysis and Research Ltd., a rating agency in India.[101] KBRA announced plans to build its presence in the European markets by establishing itself in Europe and becoming a full service and locally staffed regulated rating agency.[102] DBRS opened an office in Mexico as part of its plans to expand globally.[103]

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96 See Bayview Opportunity Master Fund IVb Trust 2016-RN1, April 28, 2016, available at: https://ratingagency.morningstar.com/mcr/ratings-surveillance/transaction-detail/Bayview%20Opportunity%20Master%20Fund%20IVb%20Trust%202016-RN1.

97 See ThunderRoad Motorcycle Trust 2016-1, April 11, 2016, available at: https://ratingagency.morningstar.com/PublicDocDisplay.aspx?i=A7fAjJ5dKW0%3d&m=i0Pyc%2bx7qZZ4%2bsXnymazBA%3d%3d&s=LviRtUKXqs8kml5dHt7FTeE2SZmY0Fvqd4iX49Mk%2f9UapyiFTEO6TA%3d%3d.

98 See https://ratingagency.morningstar.com/mcr/ratings-surveillance/structured-finance.

99 See https://www.krollbondratings.com/ratings/methodologies/.

100 See HR Ratings Signs a Strategic Alliance with Japan's JCR, August 30, 2016, available at: http://www.prnewswire.com/news-releases/hr-ratings-signs-a-strategic-alliance-with-japans-jcr-300319824.html.

101 See CARE Ratings enters into a strategic alliance with Japan Credit Rating Agency, Ltd. (JCR), December 29, 2015, available at: http://www.careratings.com/upload/pr/Press%20Release%20-%20CARE%20Ratings%20&%20JCR.pdf.

102 See Kroll Bond Rating Agency Announces Addition of Mauricio Noé, September 9, 2016, available at: https://www.krollbondratings.com/announcements/2741.

103 See DBRS Opens Office in Mexico as Part of Global Expansion; Names Head of Business Development & Compliance Officer for Mexico, June 30, 2016, available at: http://www.dbrs.com/research/296602/dbrs-opens-office-in-mexico-as-part-of-global-expansion-names-head-of-business-development-compliance-officer-for-mexico.html.

C. Barriers to Entry

Despite the notable progress made by smaller NRSROs in gaining market share in some types of asset-backed securities over the past few years (see Section IV.B. of this Report), economic and legal or regulatory barriers to entry continue to exist in the credit ratings industry, making it difficult for the smaller NRSROs to compete with the larger NRSROs.[104]

One such potential barrier that is consistently referred to by certain smaller NRSROs is the minimum ratings requirements that specify use of the ratings of particular rating agencies in the investment management contracts of institutional fund managers and the investment guidelines of fixed income mutual fund managers, pension plan sponsors, and endowment fund managers.[105] The effect of these requirements can be to increase the demand and liquidity for securities bearing the ratings of specified rating agencies.[106] Historically, many of these guidelines refer to the ratings from the larger NRSROs by name (i.e., S&P, Moody's, and Fitch). However, there have been reports that some investors are changing their guidelines to include ratings from other NRSROs.[107] Some smaller NRSROs have stated that they are continuing to reach out to investors that have not changed their guidelines to ask them to consider broadening their rating requirements.[108] Some smaller NRSROs published open letters to investors or pension board members asking them to broaden the applicable investment guidelines to include ratings from all NRSROs.[109]

Another potential barrier to entry is the inclusion requirements of some fixed income indices. To be included in many of these indices, securities must be rated by specific NRSROs. These indices are used to evaluate the performance of investment managers, which often try to mimic the performance of the indices by purchasing the securities included in them. These

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104 See Shankar Ramakrishnan and Philip Scipio, Big three in credit ratings still dominate business, May 4, 2016, available at: http://www.reuters.com/article/uscorpbonds-ratings-idUSL2N17U1L4.

105 See letter from KBRA to the Commission, dated August 19, 2014, available at: http://www.sec.gov/comments/s7-18-11/s71811-88.pdf. This barrier to entry was also mentioned during the SEC's Credit Ratings Roundtable held on May 14, 2013. At the roundtable, a representative of Morningstar mentioned that, according to a study conducted by Morningstar, approximately 42% of the fixed income funds have investment guidelines referring to ratings of S&P, Moody's, or a "major NRSRO." See Credit Rating Roundtable, May 14, 2013, available at: http://www.sec.gov/spotlight/credit-ratings-roundtable.shtml.

106 The effect of including particular NRSROs in investment guidelines was highlighted in an article concerning a loan securitization. In the article, an issuer referred to the fact that many institutional buyers are limited to purchasing securities rated by one of the larger NRSROs, and that a larger NRSRO's rating expanded the number of entities which could purchase the rated securities. See Tracy Alloway, Peer-to-Peer Lender Wins Landmark Rating, Fin. Times, July 10, 2014 at Companies and Markets, p. 18.

107 See, e.g., Matt Scully, Bond Buyers Easing Rating Requirements to Shop for More Deals, Bloomberg Business, June 22, 2015, available at: http://www.bloomberg.com/news/articles/2015-06-22/bond-buyers-easing-rating-requirements-to-shop-for-more-deals.

108 See Moody's Tops Ranking; Fitch Overtakes Kroll, Commercial Mortgage Alert, July 15, 2016.

109 See http://images.mscomm.morningstar.com/Web/MorningstarInc/%7B84b496ba-a04e-4164-91f3-2e0ffcfc081b%7D_MCR_Letter.pdf; https://www.krollbondratings.com/media_files/pension_and_investments_final_letter.pdf.

inclusion requirements increase the demand and liquidity for securities bearing the ratings of specific NRSROs. Although some indices have changed their requirements to include ratings from smaller NRSROs,[110] other major indices continue to require ratings from specified NRSROs.[111]

Certain entities may use credit ratings of specified NRSROs. For example, the National Association of Insurance Commissioners ("NAIC")[112] uses credit ratings of certain NRSROs, called "Credit Rating Providers" ("CRPs"), to determine an equivalent NAIC designation for reporting and reserving purposes.[113] Only the credit ratings of NRSROs that have applied to provide credit rating services to the NAIC and have been accepted by the NAIC as CRPs can be used for such purpose. Smaller NRSROs have made progress in gaining acceptance as CRPs. As of June 23, 2016, eight NRSROs, including DBRS, A.M. Best, EJR, Morningstar, and KBRA, had been approved as CRPs in one or more rating categories.[114] On August 27, 2016, HR Ratings was approved by the NAIC as a CRP to provide credit ratings on government securities.[115]

With respect to potential regulatory barriers to entry, the Commission received public comments regarding the effect that the proposed rules implementing the NRSRO mandates of the Dodd-Frank Act (the "Proposed Rules") would have on competition.[116] Generally, these comments expressed concerns that certain of the Proposed Rules could have negative effects on competition because they would be burdensome for smaller NRSROs to implement and could raise barriers to entry for credit rating agencies that seek to register as NRSROs.[117] The Commission adopted a final version of these rules ("Final NRSRO Rules"), however, with various changes intended to address such comments. For example, it modified certain disclosure

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110 See Jody Shenn, Ratings Shopping in CMBS Prompts Changes to Derivative Indexes, Bloomberg Business, January 20, 2015, available at: http://www.bloomberg.com/news/articles/2015-01-20/ratings-shopping-in-cmbs-prompts-changes-to-derivative-indexes.

111 For example, the rules for inclusion in the Barclays Global Aggregate Index specify that securities must be rated investment grade using the middle rating of Moody's, S&P, and Fitch. See Barclays Global Aggregate Index Fact Sheet, available at: https://index.barcap.com/Home/Guides_and_Factsheets.

112 The NAIC is a standard setting and regulatory support organization for insurance regulators. It is governed by elected or appointed government officials from the 50 states, the District of Columbia, and 5 U.S. territories. See http://www.naic.org/index_about.htm.

113 See http://www.naic.org/cipr_topics/topic_rating_agencies.htm.

114 See http://www.naic.org/documents/svo_naic_aro.pdf.

115 See http://www.naic.org/meetings1608/committees_e_vos_2016_summer_nm_summary.pdf. See also http://www.prnewswire.com/news-releases/hr-ratings-included-on-national-association-of-insurance-commissioners-naic-credit-rating-provider-list-in-us-300342176.html.

116 See Nationally Recognized Statistical Rating Organizations, Release No. 34-64514 (May 18, 2011), 76 FR 33420 (Jun. 8, 2011), available at: https://www.sec.gov/rules/proposed/2011/34-64514.pdf. See also comment letters submitted with respect to the Proposed Rules, available at: http://www.sec.gov/comments/s7-18-11/s71811.shtml.

117 See Adopting Release, 79 FR at 55090, 55154, 55161, and 55254-55.

and reporting requirements in ways that could reduce the impact on smaller NRSROs, while maintaining the usefulness of the information to users of credit ratings.[118]

V. TRANSPARENCY

Congress described the Rating Agency Act as an act to improve ratings quality "by fostering accountability, transparency, and competition in the credit rating agency industry."[119] Section 932 of the Dodd-Frank Act is entitled "Enhanced regulation, accountability, and transparency of NRSROs." Both Acts contain various provisions designed to increase the transparency—through clear disclosure open to public scrutiny—of, among other things, NRSROs' credit rating procedures and methodologies, business practices, and credit ratings performance.

The Final NRSRO Rules improved and expanded the disclosure requirements applicable to NRSROs. Additional sources of information that can be beneficial to investors and others are now required to be made publicly available under requirements of the Final NRSRO Rules. These requirements are designed to enhance the transparency of NRSRO credit ratings by reducing information asymmetries that may adversely affect users of credit ratings.[120] Specifically, the Final NRSRO Rules require an NRSRO to disclose:

(1) standardized performance statistics;[121]
(2) consolidated and increased information about credit rating histories;[122]
(3) information about material changes and significant errors in the procedures and methodologies used to determine credit ratings;[123]
(4) information about specific rating actions;[124] and
(5) clear definitions of each symbol, number, or score in the rating scale used by the NRSRO.[125]

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118 See Section VI. of the Adopting Release. For example, the Commission modified the instructions for Exhibit 1 to Form NRSRO by narrowing the scope of credit ratings included in the performance statistics for four of the five classes of credit ratings, which is expected to substantially reduce the amount of historical information that an NRSRO is required to analyze. The Commission also modified Rule 17g-7(a) by narrowing the scope of rating actions that will trigger the disclosure requirement, exempting certain rating actions involving credit ratings assigned to foreign obligors or securities issued overseas, and significantly reducing the reporting requirements relating to representations, warranties, and enforcement mechanisms. These modifications from the Proposed Rules were described in the Adopting Release as reducing the impact on small NRSROs. See Adopting Release, 79 FR at 55255-56.

119 See the preamble to the Rating Agency Act.

120 See Adopting Release, 79 FR at 55091.

121 See Instructions for Exhibit 1 to Form NRSRO; Adopting Release, 79 FR at 55295-302.

122 See Rule 17g-7(b); Adopting Release, 79 FR at 55266-67.

123 See Rule 17g-8(a)(4); Adopting Release, 79 FR at 55267-68.

124 See Rule 17g-7(a); Adopting Release, 79 FR at 55264-66.

125 See Rule 17g-8(b)(2); Adopting Release, 79 FR at 55268.

An objective of these requirements is to improve the information provided to users of credit ratings in order to facilitate external scrutiny of NRSRO activities, enable ratings users to make more informed investment and credit-related decisions and allow users to compare the performance of credit ratings by different NRSROs.[126]

In accordance with the Final NRSRO Rules, each NRSRO must now disclose certain information in connection with each rating action it takes.[127] Such information includes, among other things, the version of the procedure or methodology used to determine the credit rating, a description of the types of data that were relied upon for purposes of determining the credit rating, an assessment of the quality of information available and considered in determining the credit rating, and information on the sensitivity of the credit ratings to assumptions made by the NRSRO.[128] These requirements are designed to promote transparency of the process for determining credit rating actions, allowing users of credit ratings to better understand how credit ratings are produced and the information content of credit ratings, including how these factors vary across NRSROs.[129]

A. Consideration of Environmental, Social, and Governance Factors in Credit Ratings

As discussed in Section III.A of this Report, OCR Staff monitors trends and developments affecting the credit rating industry. Some of the trends and developments observed by OCR Staff during the Report Period have the potential to provide more information about the factors used in the ratings process.

For example, during the Report Period, S&P and Moody's joined an initiative to consider environmental, social, and governance ("ESG") factors in a more systematic and transparent way.[130] The goal of the initiative is to bring investors and credit rating agencies together in a series of forums to discuss links between ESG factors and creditworthiness. In a joint statement with other non-NRSRO global credit rating agencies, S&P and Moody's affirmed their commitment to, among other things, publish views on the ways in which ESG factors are considered in credit ratings, participate in industry-wide efforts to develop consistent public disclosure by issuers on ESG factors that could impact their creditworthiness, and participate in dialogue with investors to identify and understand ESG risks to creditworthiness.[131]

126 See Adopting Release, 79 FR at 55091.

127 See Rule 17g-7(a).

128 See Rule 17g-7(a)(1)(ii).

129 See Adopting Release, 79 FR at 55180.

130 The initiative is part of a two-year program by the Principles for Responsible Investment, which is funded by The Rockefeller Foundation. See Credit Ratings Embrace More Systematic Consideration of ESG, May 26, 2016, available at: https://www.unpri.org/press-releases/credit-ratings-agencies-embrace-more-systematic-consideration-of-esg.

131 See Statement on ESG in Credit Ratings, available for download at https://www.unpri.org/press-releases/credit-ratings-agencies-embrace-more-systematic-consideration-of-esg.

Subsequent to joining the ESG initiative, S&P published a proposal for an ESG assessment tool.[132] S&P indicated that the proposed ESG assessments would be separate from its credit ratings and designed to provide greater transparency into ESG risk by evaluating "a company's impact on the natural and social environments it inhabits, the governance mechanisms it has in place to oversee those effects, and potential losses it may face as a result of its exposures to such environmental and social risks."[133]

During the Report Period, Moody's launched a new green bond[134] assessment service.[135] The assessments are not considered credit ratings by Moody's. Rather than assess credit risk, the green bond assessments evaluate the management and administration of, allocation of proceeds to, and reporting on, environmental projects financed by green bond offerings.[136] The assessments are intended to promote further disclosure and transparency of green bond issuances and to create a consistent and transparent approach for evaluating such bonds. Moody's has indicated that its green bond assessments are part of a broader strategy to address ESG risk more systematically and consistently.[137]

B. Unsolicited Ratings and Commentaries

Beyond the disclosures required under section 15E and the Commission's rules, transparency may be increased if NRSROs that are not hired to rate a security published their views of the credit quality of such a security, such as by issuing an unsolicited rating or publishing unsolicited commentaries. Certain NRSROs have issued unsolicited ratings in rating

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132 See Proposal for Environmental, Social, and Governance (ESG) Assessments, September 5, 2016, available at: https://www.globalcreditportal.com/ratingsdirect/renderArticle.do?articleId=1705169&SctArtId=399709&from=CM&nsl_code=LIME&sourceObjectId=9783018&sourceRevId=2&fee_ind=N&exp_date=20260906-19:11:59.

133 Id.

134 A "green bond" is a debt security issued to raise capital specifically to support climate-related or environmental projects. See What are Green Bonds?, 2015, available at: http://treasury.worldbank.org/cmd/pdf/What_are_Green_Bonds.pdf.

135 See Moody's launches new Green Bond Assessment service, March 30, 2016, available at: https://www.moodys.com/research/Moodys-launches-new-Green-Bond-Assessment-service--PR_346590. S&P also recently proposed a green bond evaluation tool. See Proposal for a Green Bond Evaluation Tool, September 2, 2016, available at: https://www.globalcreditportal.com/ratingsdirect/renderArticle.do?articleId=1704625&SctArtId=399652&from=CM&nsl_code=LIME&sourceObjectId=9777755&sourceRevId=1&fee_ind=N&exp_date=20260905-21:28:10.

136 See Green Bonds Assessment (GBA), March 30, 2016, available at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_188333.

137 See Lynn Hume, Moody's Issues First Muni Green Bond Assessment in U.S., August 11, 2016, available at: http://www.bondbuyer.com/news/washington-infrastructure/moodys-issues-first-muni-green-bond-assessment-in-us-1110691-1.html.

classes, outside of structured finance, where there is lower issuer concentration and where sufficient information is publicly available upon which to base a rating.[138]

For structured finance transactions, however, much of the information on the underlying assets necessary to produce a rating is not publicly available. Rule 17g-5(a)(3) was intended to encourage the issuance of unsolicited ratings by NRSROs that are not hired to rate a structured finance transaction by making the information necessary to rate such transactions available to such NRSROs.[139] However, no unsolicited initial ratings of structured finance transactions have apparently been produced in reliance on the information provided in the websites created under such rule,[140] and the rule contemplates that such information be used only for credit ratings (and not for other types of publications, such as rating commentaries).

As mentioned in the Staff's 2014 and 2015 Annual Reports, some NRSROs have published unsolicited commentaries in which they express their viewpoints on particular securities, ratings, or asset classes (including with respect to structured finance asset classes).[141] Several such commentaries were issued over the course of the Report Period.

For example, one larger NRSRO published a report comparing its own financial strength ratings on insurance companies with financial strength ratings from a smaller NRSRO.[142] The report concluded that, due to differences in methodologies among the NRSROs, the ratings were not comparable. This larger NRSRO also published a commentary on the subprime auto loan sector in which it discussed potential risks associated with the increased number of deals from newer, less established issuers, leading to increased competition in the sector.[143] The commentary mentioned that investors are concerned that these issuers are not adhering to their underwriting guidelines and lack sufficient ability to fund their servicing platforms. Another

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138 For example, S&P maintains unsolicited ratings on Tesla Motors, LinkedIn Corp., and Yahoo! Inc. See, e.g., LinkedIn Corp. Unsolicited Ratings Placed on CreditWatch Positive on Acquisition by Microsoft, June 13, 2016, available at: https://www.standardandpoors.com/en_US/web/guest/article/-/view/type/HTML/id/1655155.

139 See Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Release 34-61050 (Nov. 23, 2009), 74 FR 63831 (Dec. 4, 2009), available at: http://www.sec.gov/rules/final/2009/34-61050.pdf.

140 Some of the reasons for the lack of unsolicited initial ratings using such information are noted in the Report to Congress on Assigned Credit Ratings. See Report to Congress on Assigned Credit Ratings, December 2012, at 58-59, available at: http://www.sec.gov/news/studies/2012/assigned-credit-ratings-study.pdf.

141 As noted above, information obtained pursuant to Rule 17g-5(a)(3) may not be used to produce commentaries. Commentaries on specific structured finance transactions have largely been based on public information and/or offering materials for the transaction. In other cases, NRSROs have produced commentaries that discuss a structured finance asset class more generally, without commenting on a particular transaction.

142 See White Paper on Lack of Comparability of A.M. Best's 'A-' IFS Ratings to Those of Fitch, July 2016, available at: https://www.fitchratings.com/site/insurance/ifsratings.

143 See Fitch: Rising Delinquencies Not Main Concern among U.S. Subprime Auto Investors, May 5, 2016, available at: https://www.fitchratings.com/site/pr/1004026.

larger NRSRO also published a commentary on the subprime auto sector, which highlighted some of the credit risks associated with subprime auto transactions.[144]

A smaller NRSRO published a commentary on the CMBS sector discussing trends observed in the number and types of commercial mortgages being removed from preliminary CMBS asset pools.[145] The NRSRO found that the percentage of loans being dropped from preliminary CMBS pools has been increasing since 2013. The NRSRO described the characteristics of the loans most commonly dropped from pools, which may provide investors with more insights into the types of loans that are ultimately included in CMBS, as well as the selection process. The same smaller NRSRO published another commentary on the conduit CMBS market in which it stated that the credit quality of conduit CMBS transactions that it has rated in 2016 has improved as compared to the conduit CMBS transactions it rated in 2015.[146] Another smaller NRSRO commented about risks associated with CMBS backed by loans on hotel properties.[147]

Some larger NRSROs published commentaries on the marketplace lending sector. One larger NRSRO discussed the potential effects of a class action lawsuit filed against the developer of a consumer marketplace lending platform.[148] The suit relates to the applicability of state usury laws to such loans. Another larger NRSRO discussed how recent events in the marketplace lending sector could increase regulatory scrutiny and may have adversely affected investor confidence.[149] Both NRSROs mentioned that the events discussed in the commentaries were not expected to affect the NRSROs ratings on the marketplace securitizations that they rate.

Commentaries such as those mentioned above highlight differences in opinions and ratings criteria among NRSROs, and may concern matters such as the sufficiency of the credit enhancement for the transactions. This type of information can serve to enhance investors' understanding of the differences in ratings approaches used by the NRSROs.

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144 See Longer-Term Subprime Auto Loans Are Leading To More Back-Loaded Losses, May 23, 2016, available at: https://www.globalcreditportal.com/ratingsdirect/renderArticle.do?articleId=1641052&SctArtId=389508&from=CM&nsl_code=LIME&sourceObjectId=9646108&sourceRevId=1&fee_ind=N&exp_date=20260527-21:31:01.

145 See Not All Loans Make the Final Cut, April 15, 2016, available at: https://www.krollbondratings.com/show_report/4098.

146 See Is the Tide Turning for Conduit Credit?, June 9, 2016, available at: https://www.krollbondratings.com/show_report/4478.

147 See Ballooning Supply Looms Over $3.68 Billion in CMBS Backed by Manhattan Hotels, May 2016, available at: https://ratingagency.morningstar.com/PublicDocDisplay.aspx?i=IfxEGHtt7Zo%3d&m=i0Pyc%2bx7qZZ4%2bsXnymazBA%3d%3d&s=LviRtUKXqs8kml5dHt7FTeE2SZmY0Fvqd4iX49Mk%2f9UapyiFTEO6TA%3d%3d.

148 See Moody's: Lending Club class action case is credit negative for marketplace loan ABS, May 6, 2016, available at: https://www.moodys.com/research/Moodys-Lending-Club-class-action-case-is-credit-negative-for--PR_348477.

149 See Fitch: Confidence in US Marketplace Lending ABS Takes a Hit, May 16, 2016, available at: https://www.fitchratings.com/site/pr/1004557.

VI. CONFLICTS OF INTEREST

NRSROs operate under a combination of two business models, and there are potential conflicts of interest inherent in both. Most of the NRSROs, including the largest NRSROs, primarily operate under the "issuer-pay" model, which is subject to a potential conflict in that the credit rating agency may be influenced to determine more favorable (i.e., higher) ratings than warranted in order to retain the obligors or issuers as clients.[150, 151] This conflict could affect an entire asset class if, for example, an NRSRO becomes known for issuing higher credit ratings with respect to such class, resulting in that NRSRO's retaining or attracting business from most or all issuers of securities in such class. The potential for such a conflict to influence the ratings process may be particularly acute with respect to structured finance products, where transactions are arranged by a relatively concentrated group of sponsors, underwriters, and managers, and rating fees are particularly lucrative.[152]

The other business model is the "subscriber-pay" model which means that investors pay the rating agency a subscription fee to access its ratings. This model is also subject to potential conflicts of interest. For example, an NRSRO may be aware that an influential subscriber holds a securities position (long or short) that could be advantaged if a credit rating upgrade or downgrade causes the market value of the security to increase or decrease or that a subscriber invests in newly issued bonds and would obtain higher yields if the bonds were to have lower ratings.

Another example of a conflict in a "subscriber-pay" model is that the NRSRO may be aware that a subscriber wishes to acquire a particular security but is prevented from doing so because the credit rating of the security is lower than internal investment guidelines or an applicable contract permit. An upgrade of the credit rating of the security by the NRSRO could remove this impediment to investing in the security. These potential conflicts could be mitigated

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150 For example, in 2015, the U.S. Department of Justice and 19 states and the District of Columbia announced that they had entered into a settlement agreement with S&P to resolve certain allegations regarding S&P's ratings on MBS and collateralized debt obligations. One such allegation was that S&P falsely represented that its ratings were objective, independent, and uninfluenced by S&P's business relationships with the investment banks that issued the securities. See Justice Department and State Partners Secure $1.375 Billion Settlement with S&P for Defrauding Investors in the Lead Up to the Financial Crisis, February 3, 2015, available at: http://www.justice.gov/opa/pr/justice-department-and-state-partners-secure-1375-billion-settlement-sp-defrauding-investors. In addition, the Commission announced a separate settlement agreement with S&P in January 2015. Among other things, the agreement settled charges that S&P loosened its CMBS rating criteria to obtain more business but did not properly disclose the criteria changes to investors. See SEC Announces Charges Against Standard & Poor's for Fraudulent Ratings Misconduct, Release No. 2015-10 (Jan. 21, 2015), available at: http://www.sec.gov/news/pressrelease/2015-10.html.

151 Some authors have written about the effect of reputational concerns on the motivation of rating agencies to provide accurate ratings. See, e.g., Steven L. Schwarcz, Private Ordering of Public Markets: The Rating Agency Paradox, 2002 U. ILL. L. REV. 1 (2002); Harold Cole and Thomas F. Cooley, Rating Agencies, NBER working paper No. 19972 (Mar. 2014).

152 A Senate Report related to the Dodd-Frank Act noted, for instance, that conflicts of interest in the process of rating structured financial products contributed to the issuance of inaccurate ratings by rating agencies and, accordingly, to the mismanagement of risks by financial institutions and investors. See S. Report No. 111-176 (2010).

to the extent that an NRSRO has a wide subscriber base and subscribers have different interests with respect to an upgrade or downgrade of a particular security.

In addition to conflicts of interest that stem from an NRSRO's business model or otherwise may exist at an institutional level, conflicts may also arise involving individual credit analysts. Two academic articles published during the Report Period provide examples of potential conflicts of interest applicable to individual analysts. One of these articles discusses the potential bias an analyst may have when participating in the rating of municipal bonds of an issuer from the state in which the analyst grew up.[153] The other article discusses issues involving credit analysts who seek employment at a rated entity.[154]

Section 15E and the related Commission rules contain provisions addressing conflicts of interest. For example, Rule 17g-5 identifies certain conflicts of interest that are prohibited under all circumstances[155] and other conflicts of interest that are prohibited unless an NRSRO has publicly disclosed the existence of the conflict and has implemented policies and procedures reasonably designed to address and manage such conflict.[156] Among the conflicts of interest identified in Rule 17g-5 are conflicts involving individual credit analysts or other employees of the NRSRO. For example, an NRSRO is prohibited from issuing or maintaining a credit rating for a person where an employee of the NRSRO that participated in determining, or is responsible for approving, the credit rating directly owns securities or is an officer or director of the person that would be subject to the credit rating.[157]

Rule 17g-5(c)(8) is another example of a prohibited conflict of interest involving persons within an NRSRO. Under the Rule, adopted as part of the Final NRSRO Rules, an NRSRO is prohibited from issuing or maintaining a credit rating where a person within the NRSRO who participates in determining or monitoring the rating, or developing or approving procedures or methodologies used for determining the rating, also (a) participates in sales or marketing activities of the NRSRO or its affiliate or (b) is influenced by sales or marketing considerations.[158]

Other statutory provisions and Commission rules address potential conflicts of interest that may arise when a credit analyst seeks employment outside the NRSRO. Each NRSRO is required to have policies and procedures in place to provide for an internal "look-back" review process in order to determine whether any conflict of interest of a former employee influenced a

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153 See Kimberly R. Cornaggia, et al., Where the Heart Is: Information Production and the Home Bias, June 7, 2016, available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2518040.

154 See Elisabeth Kempf, The Job Rating Game: The Effects of Revolving Doors on Analyst Incentives, November 16, 2015, available at http://faculty.chicagobooth.edu/workshops/finance/pdf/KempfRevolvingDoors%20(JMP).pdf.

155 See Rule 17g-5(c).

156 See Rule 17g-5(a)(1)-(2); Rule 17g-5(b); and Form NRSRO, Exhibits 6-7. Additional requirements apply to the "issuer-pay" conflict of interest in the context of credit ratings of asset-backed securities. See Rule 17g-5(a)(3).

157 See Rule 17g-5(c)(2) and Rule 17g-5(c)(4).

158 See Rule 17g-5(c)(8).

credit rating in certain instances.[159] In July 2016, OCR Staff issued letters to the designated compliance officers of the NRSROs to provide the Staff's view that an NRSRO's policies and procedures should provide for a look-back review in those instances where a former analyst participated in determining credit ratings with respect to his or her new employer during the one-year period preceding the most recent rating action taken by the NRSRO prior to the analyst's departure.[160]

Rule 17g-8(c), adopted as part of the Final NRSRO Rules, requires an NRSRO's policies and procedures to address instances in which a "look-back" review determined that a conflict of interest influenced a credit rating. Such policies and procedures are required to be reasonably designed to ensure that the NRSRO will promptly determine whether a credit rating must be revised and promptly publish a revised credit rating or an affirmation of the credit rating, along with certain disclosures about the existence of the conflict.[161] This rule enhances the statutory requirement to conduct a look-back review by requiring the NRSRO to act promptly and to disclose information about the conflict of interest. The Commission noted in the Adopting Release that these requirements will provide users of credit ratings with information to assess an NRSRO's ability to address conflicts of interest and to compare NRSROs with respect to their ability to manage the conflicts.[162]

VII. CONCLUSION

The Staff will continue to conduct its oversight function with respect to NRSROs, including the performance of Staff examinations, and engage in other initiatives with respect to NRSROs.

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159 See section 15E(h)(4)(A).

160 The content of these letters was also published on the OCR page of the Commission's website. See "Dear DCO" Letter, July 2016, available at https://www.sec.gov/about/offices/ocr/dear-dco-letter-15eh4a-071816.pdf.

161 See Rule 17g-8(c); Adopting Release, 79 FR at 55268.

162 See Adopting Release, 79 FR at 55124.