Securities and Exchange Commission
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- Credit Ratings Roundtable

Dear Sir.

Thank you for giving us the opportunity to provide comment to your roundtable discussion on Credit Ratings.

You will host a one day roundtable to discuss various matters related to credit ratings. The roundtable will consist of three panels. The first panel will examine issues in connection with the possibility of developing a credit rating assignment system. The second panel will discuss the effectiveness of the Commission's current system under the Securities Exchange Act of 1934 for encouraging unsolicited ratings of asset-backed securities. The third panel will focus on other potential alternatives to the current issuer pay business model. I will comment generally here and on the first panel's issues in connection with the possibility of developing a credit rating assignment system.

It is clear that there are fundamental conflicts of interest in the current dominant issuer pay business model. Given the importance of credit rating agencies (nationally recognized statistical rating organizations or NRSROs) in financial markets, and the reliance that investors and other parties place upon their ratings, it is important that regulators should place more emphasis on the fitness and appropriateness of NRSROs' senior management and other key officers, their lines of responsibility, and on their monitoring, managing and mitigating conflicts of interest, in order to reduce the possibility of disruptive or abusive behaviour, manipulation and other deceptive, misleading or fraudulent activities. This is critical in order to improve confidence in the veracity and integrity of NRSROs, and public perception in the integrity of the credit rating process and system. From the public point of view, it is very important that the credit rating process and system is both *perceived* and *seen* to be independent and objective.

Establishing an assignment system for credit ratings has certain merits. At first glance, the proposed Section 15E(w) system seems both practicable and reasonable. However, this system would suffer from intractable flaws: it would entrench a super-select few NRSROs and reduce competition and choice; it would create an implicit government stamp of approval on such ratings; investors could even view the system as an implicit government guarantee; it would therefore potentially increase, not reduce, investor reliance on credit ratings; it would create new conflicts of interest in that it would further blur the boundaries between NRSROs' private business and government control of that business;[1] it could reduce transparency and accountability if the processes are not clear and credible; it is operationally complex, given that large numbers of structured products would need to be rated on an ongoing, timely basis; and it is questionable legally.

I would much rather suggest that you should lever the existing rules in order to reduce conflicts of interest within the credit rating system. I would start by amending Exchange Act Rule 17g-5 to remove the 10% requirement,[2] or as a minimum, allow NRSROs to count own commentary towards the 10% requirement. This would maximise the possibility of non-hired NRSROs finding cases on which their views differed from the hired NRSROs, increase the pool of ratings on which to measure relative and absolute accuracy, and would therefore provide a market pressure towards more objective and appropriate ratings. The key point is that this would act to reduce conflicts of interest within the credit rating system in a reasonable and practicable manner.

Yours faithfully

Chris Barnard

[1] This government stamp of approval, increase in investor reliance on credit ratings, and new conflicts of interest would create significant moral hazard within the system.

[2] See Exchange Act Rule 17g-5(e).