CreditSights

August 12, 2009

Ms. Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street N.E.
Washington D.C. 20549-1090

Re: Proposed Rules for Nationally Recognized Statistical Rating Organizations

<u>COMMENTS on Release No. 34-59343; File No. S7-04-09</u>

Re-proposed Rule for NRSROs
Enhanced Disclosure for Structured Finance and ABS Deals

As Congress, the Administration, and, most critically, the SEC consider the process of much-needed rating agency reform, the focus must remain on those structural changes that will promote transparency all along the information chain. That "chain" includes the *information and disclosure* required to actually rate securities or structured finance vehicles effectively and not just the *criteria* used in the ratings process itself. Too frequently the regulatory and legislative debates have completely ignored the former while narrowing the debate to the latter – much to the joy of those whose underlying agenda is to preserve the status quo. And once again, the current round of reforms appears to do little or nothing to ensure that aspiring NRSROs have access to information that is critical to the ratings process. The separation of the structured finance business— Moody's and S&P's gold mine — under the Credit Rating Agency Act of 2006 was bad enough. The push under new reform initiatives appears designed to preclude potential competition from gaining access to the data and disclosure that would allow them to even "start the three year clock" under 2006 legislation and tackle the mountain of misrated and mispriced toxic structured piles that the status quo system fostered. Such an unfortunate outcome would be fatal to meaningful reform of structured finance ratings and the goal of improving the independence, quality, and diversity of information in the marketplace—whether for use in ratings by "non-engaged" NRSROs or more broadly for direct use by institutional investors.

To date the reform process has been going down the track of exploring how to punish the incumbents rather than improve the system of information flows and enhance investors' ability to assess risk. The debate focuses more on the question of "**How can we sue these guys?"** rather than how the process of viable competition can be fostered after decades of a regulatory structure that allowed the stacking of unnatural barriers to entry. Unfortunately, meaningful change doesn't lend itself well to political sound bytes. If there is one thing that the Enron-to-subprime time frame (fall 2001 to today) drives home, it is that lasting change will not come from knee-jerk responses, angry speeches, and threats of punishment. Nor will lasting change come just from more backward-looking regulation, more paperwork, and more “administrative taxes.” The goal, instead, should be to tear down the unnatural barriers to competition that the current system has created and which contributed meaningfully (some would argue created) to the current financial crisis.

At the core of any ratings process is a level playing field of access to information. The whole exercise of credit rating industry reform will be one in futility if the process only focuses on ratings transparency and not the information needed by providers to rate issuers and instruments at the beginning of the process. There are bits and pieces of such initiatives in the proposals (e.g. in RMBS origination and documentation), but the low hanging fruit around readily available loans, documents, and data are all but absent. We cannot tell if this is by design, by accident, or due to intensive lobbying by those who seek to stymie meaningful change. Our overriding concern is that the myriad regulatory bodies and various Congressional Committees will once again opt for the politically expedient solution and embrace the status quo with a few extra bells and whistles rather than effecting structural change that will foster fair competition. That tendency toward focusing on short-term expedience over the past 7+ years since the March 2002 Enron Rating Agency hearings helped get the credit rating industry to where it is today. The missed opportunities may not have caused as many of the problems as the decades of artificial regulatory barriers to entry, but they sure are a close second.

The reform of disclosure and documentation is the most difficult to tackle effectively and yet this area of reform could promote more competition and attract more high quality, high-information-content ratings and research offerings to the marketplace. That can foster competition and makes investment in the space more attractive for larger strategic players with major brand power, technology, global reach, and data resources. It can also promote inflows of more financial capital that see opportunities to enter this space. As the SEC tries to develop a disclosure framework and information infrastructure that allows for more independent and conflict-free ratings and research products that better serve the needs of investors, there will be a compelling need to recognize the doubletalk that will be used by underwriters and the incumbent rating agencies to slow forward progress. We have seen an ample supply of misdirection plays being run in the comments in summer of 2008 on proposed changes, but that was before the whole financial house of cards came down. **There is a highly incentivized economic food chain of relationship bankers, law firms, vendors, and trade groups that will do as much as they can to change the debate while striving to preserve as much of the status quo as possible.**

Ground zero in the debate around reforming the rating and analysis of structured finance products is disclosure and information availability – Step 1 in the analytical chain. To date the proposal of the Administration, various Congressional bills, and the SEC are completely inadequate in this critical area. **Disclosure is a core competency of the SEC, and we see that as the body most capable of getting this done the right away.**

After all, Reg FD was an unqualified success and many of the groups opposed to that effort are the same ones lined up to preserve their fiefdoms now. The thrust of the debate right now across various bodies seems to be more about promoting liability and simply requiring everyone to register. The effort instead should be directed toward effecting change that will improve quality and not just generate better disclaimers at the end of reports.

Competition will increase if a clear and level playing field –and most notably in information access—is promoted and supported by Congress and the regulators. At this point, little that we have seen in the proposals promotes that level playing field. The SEC has opened the door with its re-proposal, and it is much more than Congress or the Administration has proposed, but it still falls well short. We in fact see the bulk of the proposals –most notably from the Administration and the Senate—as talking "competition" but in fact serving as a Trojan Horse for the status quo industry structure. Some of the proposals across the various legislative and regulatory bodies may be seeking to excuse historical inaction, dress up their special interest connections, or simply paper over past incompetent oversight by stating that the rating agency business is a "natural oligopoly." That can in turn promote the policy of leaning toward proposals that will make that view a self-fulfilling prophecy.

The difficult battle to effect change is amply evident during the 7+ years of missed opportunities in this area. The highly politicized and strangely partisan process around the Credit Rating Agency Reform Act of 2006 also set the stage for a different approach this time around given the stakes. In the end, the fact that the underwriters and the incumbent agencies will vigorously oppose such reform around disclosure (whether openly or away from the public relations rhetoric) is supposed to reinforce the assumption that such reform is the right thing to do and promote some additional research by the appropriate regulators. When those who caused the problem scream the loudest about a given change, chances are the regulators and legislators will be onto something. **We recommend a hard look at this neglected aspect of disclosure reform. It will shed a lot of light on motives. As it stands now, the proposals are shaping up as a giant step backward.**

Summary of the Disclosure Reform Problems Feeding the Crisis

The basic policy issues remain the same now as they have been before, during, and in the aftershocks of this unprecedented credit crisis:

- **Disclosure has been inadequate—**To make the information void more dangerous, the parties with the worst conflicts of interest control the information flow. "Information" by itself is an absolute barrier to entry in numerous asset classes and, most notably, in structured finance. We are still stunned how few seem to comprehend this simple fact among the regulatory and legislative bodies debating reform. **Take an issuer-pay structured finance product, add a closed information loop across the underwriters and incumbent ratings firms who in substance get to design the criteria, and you get to combine the very worst of conflicts of interest with the worst of *intentionally designed* barriers to entry.** That problem is not being tackled by anything out of Congress, the SEC, or the Treasury Department at this point although there still is hope at the SEC. The Administration to this point seems more intent on solidifying that information barrier to entry, which is perplexing.

The close control and limited availability of such information to third parties is still an obstacle that prevents those rating agencies, investors, and independent research firms who are outside the underwriting and rating agency "closed information loop" from making rigorous assessments on the quality of various assets and even entire asset classes for use in models. Thus truly independent firms cannot effectively challenge inflated "issuer paid" opinions in structured finance through use of their own analytics. At the very least, they will be forced to use less complete information in evaluating portfolio level aggregate risk. Similarly, they cannot challenge methodologies or assumptions armed with proper data and documents. They can play the boutique "town crier" role, but that is less effective and less useful and certainly is not a model for expanding a viable business that presents serious competition.

The disclosure requirements are daunting to address given the array of structures (RMBS, CMBS, various ABS structures, leveraged loans in CLOs, synthetic and cash structures, etc.). Nonetheless, mountains of data and documents exist intrinsically as part of the deal origination and the process of ongoing deal maintenance (whether for market-making by banks, ongoing ratings, or for portfolio evaluation by owners of assets). In the age of technology, the cost of such disclosure would be low despite the usual nonsense of how "burdensome" new disclosure rules would be. That said, the legal bills and lobbyist outlays by those that control the information to derail any enhanced disclosure would be rather costly to the obstructionists. The question should be "Why do they spend that money?" The answer is simple enough. There is profit in an unlevel information playing field. For the broader market, there is also heightened systemic risk when that is the case and the asset class origination gets taken to an extreme level. That is not an argument at this stage.

- **Opposition to improved disclosure remains intense-** It is common knowledge that Wall Street makes more money in inefficient markets where the bid-offer is wider and the fees on underwriting such deals higher. Similarly, the incumbent NRSROs derive better margins and pricing power on such elaborately structured deals, and they want that franchise protected in the future. That is the case even if the size of the structured finance market will be much smaller in the future as the most complicated structures either die or go into a protracted hibernation period. The systemic risk issues that can accompany new waves of products also is hardly without some very recent precedent and especially where information or relationship control is a key driver of capturing fees. The highly damaging structured finance wave is in many regards a continuation of the same principles (or perhaps lack of principles) that we saw in the high-margin tech bubble and IPO boom that fell apart earlier in the decade. The deal flow dynamic is certainly similar as well. The hefty fees on such "deal booms"—whether internet stocks or structured finance products—attract even more deals and more variations of the theme. Unfortunately, the volume potential and fee structures in such new product deluges provide an incentive to compromise on quality and underwriting standards as the asset alternatives get closer to the bottom of the barrel. In the case of structured finance, the bottom of the barrel even had a trap door as we saw in subprime, CDOs squared, and CPDOs to name the more obvious toxic waste sites.

The checks and balances on such a process getting out of control could have been partially addressed through more and better disclosure to investors and also supported by more independent research and objective assessment from less conflicted voices. In the case of structured finance, however, the same parties that created the problem still control all the information and are the most vocal in opposition. It is notable that Fitch may mark a departure from that generalization based on their recent testimony. It does not take even a hint of skepticism or cynicism to see why the opposition from underwriters and most incumbents is so intense. Some of the objections to improving information availability to the market generally or to non-engaged NRSROs under new disclosure rules will—true to form—be resisted as a matter of profit and economics. That profit motive will be understandable as the incumbent agencies and underwriters (and their relationship law firms and supporting vendor chain) will want a structure that maximizes the potential to maximize deal volume. After all, Wall Street is a business about "maximizing," but apparently the goal is to minimize information availability.

Part and parcel with an industry structure that limits information flow is that it limits market entry and new competition (i.e. prevents them from getting information and data to rate structure finance vehicles effectively if at all). It also helps the incumbents control pricing (make the market a price-taker) and makes sure the stage is set where the same entrenched players that got us here can leverage long-established relationships for maximum franchise value (notably between underwriters, the established ratings oligopoly, and deal managers with established ties to the underwriters/agencies). The interesting point is that once any more sweeping structural changes are made, the underwriters and asset managers will immediately adapt. They always do. On the other hand, the incumbent NRSROs will face more competition, probably see their outsized, near-monopolistic profit margins narrow from *obscene* to just *very high*, and they will be in a position where they need to focus more on competing on quality and being more discriminating with the use of their rubber stamp (especially the one with the AAA on it in structured finance and the single B in leveraged loans).

Those who control the information do not want to share it given an understandable profit motive, and they will once again have a raft of eloquent reasons away from the profit and market leverage it brings as to why it cannot be shared. A parallel to this opposition to level field disclosure is in the corporate sector. If the rationale used by various opponents to structured finance disclosure applied the same rational to corporate issuers, the financial statements of companies would not be available either. Of course that is absurd and they would not try to make that case. For some reason, however, they believe they can oppose disclosure of the nuts and bolts input needed to be used in evaluating structured finance. We would remind everyone that the underwriters were among the most vocal opponents to Reg FD that leveled the information playing field in corporates. Their motives in structured finance are no different. Again, they will adapt to any changes that are made. The challenges to the incumbent ratings agencies will be more lasting, and it will be good for the market.

- **Any changes made in structured finance deal disclosure has to include disclosure of legacy deals and allow for ongoing surveillance -** One of the glaring shortfalls of the current re-proposal presented by the SEC is that the ABS and structured finance disclosure rules is that they still only apply to *future deals* in ABS. The definitions also fall well short of what is needed to provide clarification around how they will apply to the full range of structured finance asset classes. Notably it is completely unclear what it means for CLOs. We cannot tell if that omission is an oversight or by design. Restricting the enhanced disclosure does damage to the value of reform from several vantage points. Among other shortfalls, it ignores the concept of deal surveillance under investor pay models and seems to assume that *new issue* ratings service is the only product offering the market needs. It also seems to cater to the issuer pay model. Lastly, that proposal ignores one of the foundations of structured finance ratings, namely, the need for ongoing modeling of asset classes and structures to refine ratings models. How does one refine models for future deals if the largest structured finance ratings issuance wave in history in the most volatile market in history is not accessible? How does one compete if assets cannot be reviewed in depth by third parties and evaluated by new or non-engaged NRSROs, academics, policy makers, or, even more broadly, investors that need to assess ongoing asset allocation strategies in the future? It is bad policy and at best inconsistent with the stated goals.

  A few major shortcomings of this proposal need some detailing. First, the massive amount of structures outstanding in terms of numbers of deals and in terms of dollar value outstanding need immediate attention now for purposes of surveillance. That is not just about assigning a few letters to a deal. It is about modeling loss exposure across tranches and the relative risk of loss across deals. That is true across the full range of CLOs, CDOs, subprime RMBS, and CMBS. **Directing aspiring NRSROs toward a distant mole hill (tomorrow's deals) and away from today's mountain (outstanding structured products of varied quality if not toxicity) is an astonishingly bad move from the vantage point of effecting meaningful change in the rating agency industry**. We are sure it will be celebrated by those that control the current deal information. The proposal is anti-competitive—plain and simple. It is a scrap relative to what is needed. That is especially the case for new market entrants given the 3-year "waiting period" in the 2006 act.

  The end game from those advocating limited data on new deals will direct new competitors to more plain vanilla sectors such as autos, cards, and RMBS. It will also direct them to a new issue focus and keep them out of some business lines such as asset backed commercial paper. A still largely untold story—at least in the mainstream financial media and on the Washington circuit—is how subprime mortgages and structured investment vehicles almost blew up the commercial paper market and how the rating agencies rubber stamped prime ratings on those structures as well. The decline from the 2007 peak in ABCP outstanding rivals the size of the TARP program itself.

Corporate-based structured products such as CLOs will remain closed under the current proposal. The surveillance business in such areas as legacy CDOs and subprime will allow for only limited entry. The ability for growing players to build a surveillance business to compete with the agencies and allow for more formidable competitors will be set back. The incumbents would very much like to keep for themselves the ability to enter new product lines such as valuation and risk analysis in structured products. **Having spent years selling tanks, they can now sell anti-tanks weapons.** Such a proposal will undermine the ability of new NRSRO entrants to even enter into the structured finance ratings space and certainly for those that do try, the unconscionably narrow sliver of data required to be disclosed will doom any that try if their goal is to be a high quality operations and not just a firm looking for some one-off new issue fees. The shackles will be placed on established research/ratings firms looking to expand in structured finance. After all, how are the more recent handful of approved NRSROs going to add value if they only get new issue information and nothing else?

Second, the ability to model the performance of various assets and structures for purposes of future ratings criteria and the next generation of ratings products requires that current deal data and documentation be made available for analysis. If innovation in ratings products is truly desired or improving the potential for new entrants to challenge entrenched incumbents on their assumptions, then the legacy deal disclosure also has to improve—not just the relative trickle of new issues in the more complex structures in coming years. Doing otherwise directly contravenes the stated policy goals of encouraging the market to rely less on the dominant, incumbent rating agencies. The idea that it is sound policy to concentrate the control of information in the hands of those that rated and underwrote the structures is dubious at best. At worst, other words clearly apply. If the SEC will aggressively move to require more information for use by investors, then the market will in the end benefit. The benefits will be evident in the fair and objective appraisal of current exposures but also in terms of future risk assessment decisions and the investor’s ability to make more informed judgments around ongoing asset allocation strategies.

In some of the recent regulatory commentary, there also appears to have been a notable attempt to push the discussion back toward plain vanilla ABS structures (e.g. RMBS, cards, and auto retail) and avoid raising the issue of leveraged loans and CLOs. We see this as possibly part of an intentional strategy to avoid tackling the thorny issues of private loan transactions that boomed in the recent LBO wave. It may also be an attempt in some quarters to avoid the inevitable turf wars that are every bit as characteristic of Washington as they are of Wall Street. Who regulates the loans and related disclosure? Who regulates structures created from loans and related disclosure? Does it require clarification in legislation or will that be taken under advisement for a year only to request legislation when the furor may have died down and election year distractions will table it until 2011? The reform around structured finance and loan disclosure is needed now and not just ahead of the oncoming maturity peak in 2012 and beyond. The challenge will not go away and the issues around CLOs and leveraged loan disclosure will be the next critical proving grounds for how serious the revamped regulation will be around tackling the next great credit crisis, which will be the massive refinancing wave of leveraged loans and especially those covenant lite loans generated in 2006-2007. A majority of these loans found their way into structured finance deals that remain outstanding. We refer the Commission to our earlier comments on the CLO issue last summer and those we filed in connection with hearings of this past April 15 in Washington.

SELECT COMMENTS ON OPPOSITION FROM LIMITED COMMENTERS

Below we make some additional commentary on some select opposition to enhanced disclosure referenced in the re-proposal.

Surveillance Information

"One commenter stated that the surveillance information called for under the proposed amendment is already available to the public for a fee through third party vendors." (page 28-29)."

The surveillance information needed to meet the analytical needs across the various structured finance instruments is *most decidedly and absolutely not available from vendors*. There are some very high quality vendors providing some very valuable information for purposes of rating and monitoring some—but not certainly not all—ABS products, but even in those cases there is a next layer of documentation and structural details that would not be available from the vendor. There is also the historical unwillingness of vendors to provide data to subscription based research firms that serve institutional investors and the added reality that the incumbent agencies can procure such data as part of their issuer-pay process. In other words, it is a natural barrier that has been stacked higher by the longstanding unnatural regulatory barriers that have been so frequently discussed over the years.

The SEC should also be fully aware that vendors can refuse to sell such data to research firms and will also often use such tactics as discriminatory pricing to keep third party research firms from gaining access to structured finance tranche data. Are commenters who are also vendors pledging to not engage in such conduct or recommending that the SEC regulate such behavior? The motive to completely withhold or only offer prohibitive, discriminatory pricing to new NRSROs or aspiring NRSROs is particularly targeted at subscriber-pay/investor-pay research firms on the theory that rigorous analysis of structured products and the underlying assets by third party firms could cannibalize their revenue base. We understand the vendors have a business need, but that hardly justifies preventing new NRSROs from gaining access to the information the engaged NRSROs and entrenched incumbents have routine access to**. So we would caution the Commission around believing that third party vendors can be a substitute for disclosure in many areas of ABS or structured finance.** That view is inaccurate and not borne out in the trenches. Anyone who represents such is the case is either taking liberties with the facts or making some broad generalizations that do not hold up to scrutiny.

There is also a motive on the part of the major incumbent agencies themselves to build data businesses from their entrenched and historically protected position as issuer-pay NRSROs. The NRSROs have multiple motives for vehement opposition to more disclosure and third-party access to structured finance and ABS disclosure. Not only are they looking to limit competition and protect their issuer-pay franchise revenue stream, but they are also looking to use that position to generate increased non-ratings revenues using the inputs from the ratings process. That is another reason the agencies want to narrow the debate solely to ratings as they look to keep regulatory eyes averted from the reality of the how the “ratings agency” businesses have evolved into data, analytics, consulting, asset valuation, and research subscription businesses. They have entered those product areas by leveraging the historically entrenched position of their narrower ratings business. **The seriousness of the SEC and Congress in promoting competition will get a critical test in whether they tackle the information barriers.** So far it is not looking good.

The practice of limiting information flows by vendors extends across loan data/documents, CDO tranche information, and various ABS structures. To the extent that the incumbent rating agencies such as Moody’s, S&P, and Fitch receive such information as part of a rating a transaction and they in effect thus receive it for free, the effect is just the creation of one more barrier to entry. To the extent the availability is restricted from third parties, the parties who limit the availability of such information are in effect engaged in anti-competitive practices. That is the case with vendors if the vendor is “plugged into the street” and they—along with the incumbent rating agencies—are part of a mutually beneficial relationship to limit data availability. **Numerous vendors are in fact married to the status quo of a closed information loop and will continue to oppose all evolution of the information and disclosure rules.** They have developed business lines under a system that promotes inefficient information flows and an unlevel playing field. It is this very approach that led to catastrophic, systemic losses and they should not be allowed to impede improved disclosure for the markets and more competition in ratings products.

We agree purchasing vendor data can be a perfectly cost-effective way of procuring data and information that can be used in the ratings process. The trick will be determining where there are abuses in the system and where new NRSROs or investor-pay/subscriber-pay models are refused access or prevented from utilizing the information—either prevented outright from a refusal to sell such data or are in substance prevented from gaining access by the use of discriminatory, punitive pricing.

“These commenters were concerned that if issuers and underwriters were forced to disclose proprietary information, they would instead choose not to share this information with the NRSROs, which could affect the accuracy of the rating.” (page 29).

In reviewing the relatively few comments that indicated issuers and/or underwriters would choose not to share information, we would highlight that one of the parties subsequently filed bankruptcy and another one is living by the graces of TARP and Fed and taxpayer largesse. We would thus argue that the status quo was certainly not the optimal solution and did not yield the desired outcome for those organizations either. With a range of structured finance vehicles and asset classes (RMBS, CMBS, SIVs, CDOs, leveraged loans etc.) at the root of the commenters' problems, we see their dismal credit trend during this past structured finance cycle as more an endorsement of radical change. Their written opposition to change as late as the summer of 2008 is more than a little ironic.

We consider withholding information as somewhat of a hollow threat and a bad bluff given the risks such action would entail not only for the parties withholding the information but also for any major rating agency that went ahead and gave a rating without demanding the requisite information. Any such action by an underwriter would signal a desire not to do a deal (and pass on a fee-generating opportunity), and perhaps that would be for sound reasons seldom exercised in 2005-2007. Alternatively, printing a deal without procuring the needed information would signal an egregious lack of ethics. To the extent NRSRO's would rate structures with inadequate disclosure, they should be held accountable for such conduct either to the SEC or even face liability for such negligence.

Under a new disclosure system where the subscriber-paid NRSRO has *equivalent disclosure*, the less conflicted investor-pay model for structured finance would even be in a position to publish for "investor clients" that there was not adequate disclosure and detail that was missing. That would yield direct benefits to the market including checking the tendency of arrangers or issuers from "information shopping" (a first cousin of ratings shopping). In information shopping, the deal only gets awarded to underwriters that demand less disclosure. As far as "withholding" information, any deal arrangers and/or intermediaries that refused to share material information would face numerous risks as well. Knowingly withholding information that would preclude accurate ratings would raise many questions around their conduct. If the rating agencies lacked the competence to request the proper scope of information, then they have not conducted remotely adequate due diligence and care in developing an analytical opinion.

In a real world context, it is also critical to walk through what the enhanced disclosure would mean—either through a deal-specific NRSRO "web portal" or through a major ongoing overhaul of ABS and structured finance disclosure. The practical impact would be that under a potentially enhanced disclosure system, the other competing agencies—including investor-pay models— would have access to what was in fact provided to the "engaged NSRO." That is hardly controversial. If there was a material omission of critical data to make a reasoned assessment, that independent firm could highlight as much to investor-clients. The "rap" on unsolicited opinions from investor-pay models traditionally has been that they "lack information." That is the classic trap that the underwriters and issuer-pay incumbents set for new market entrants to undermine their products. More often than not, the information that *the incumbents do not have* may be the problem, but the opacity of the process keeps outsiders from challenging the process. Making such information broadly available would upgrade the level of debate and could generate some investor pushback on the ratings methodologies. In the case of subprime RMBS, it may have slowed the tsunami or warned more of those who drowned even if it did not prevent the wave. Subscriber-pay models would be in a position to highlight what information is missing and that would at the very least raise questions. After all, in structured finance asset classes there is more to the "ratings" than assigning letters. There is also a major high-information-content research component of ratings that tends to get buried in the debate around what new NRSRO's would offer.

While some of the commenters tossed around the much-overused terms "chill" and "chilling effect" in describing what could happen to communications between arrangers and NRSROs, we would argue that the most recent crisis has gone beyond "chill." There has been a deep freeze in disclosure, communication and issuance volumes on what only can be viewed as freeze-dried investor confidence levels. This is partly a function of a lack of faith in the underwriting and ratings process, but also it remains heavily tied to ongoing inadequate information flows. More independent voices and higher levels of information-intensive analysis would help restore confidence in higher quality deals.

"Some commenters suggested that instead of requiring the information to be disclosed to a range of market participants, it should only be disclosed to other NRSROs that seek to undertake an unsolicited rating. The commenters stated that NRSROs would be subject to the same confidentiality agreements that arrangers make with NRSROs they hire to rate structured finance products." (page 29)

One of the techniques that intermediaries, arrangers, and the incumbent NRSROs use to close off information flows is in the area of confidentiality agreements. The confidentiality agreement problem is a particular problem in the area of leveraged loans of private companies (LBOs, etc.) that flow into CLO transactions. As we detailed in our April 10, 2009 formal statement filed with the SEC, the lack public disclosure is essentially a prohibitive barrier to rating some structures.

To the extent the threat is made by debtors to not allow their loans to be placed into CLOs, the logical response should "so that is your decision. We will not put it in a CLO." We see such threats as hollow and for most rational firms a bluff. If borrowers are so secretive as to prevent a subscriber-paid NRSRO from seeing their loan documents and financial statements to evaluate the risk of that asset in a broader pool (or to rate on a stand-alone basis), then they should also bear the economic risks of such intransigence. Under such a policy, that borrower will find more onerous terms and pricing on the loan if the lender is prevented from using the loan in structured finance deals. Since the bank will need to hold that loan or run the risk it cannot be syndicated or offloaded into a CLO, he will want to get paid for that risk. In essence, the borrower is likely to see that it is much more cost-effective to be cooperative. If the LBO borrower cooperates, that borrower most likely gets better execution, more favorable pricing, and most likely a less demanding set of covenants. After all, the lender is passing that leveraged credit risk exposure along to investment grade investors via a structured finance vehicle.

In the end, the confidentiality flag gets waved all too frequently by underwriters and arrangers when in substance this confidential information is already in the hands of the lenders, many of the largest institutional investors, and also the major rating agencies. In other words, it is a red herring. The hands that don't hold the information are the investment grade buyers of the structured finance paper and the rating agencies and independent research firms that have no role in the deal. In other words, the parties that cannot gain access are the owners and objective arms-length raters not engaged in the transaction for a fee as part of the issuer-pay fold.

SUMMARY

If the end game for regulators and legislators is a fresh round of short-term punishment for the last round of bad behavior rather than making more sweeping changes to the industry structure, then this process will be by and large a waste of time. The basic changes in disclosure that are most vigorously opposed by the ones who caused this mess are usually the right initiatives since it eats into their control of information, promotes transparency in risk assessment and thus erodes their ability to print high fees and maximize profits while transferring risk. Most importantly, impaired information flows allow their issuing client base to transfer mispriced risks to those in the market that do not have the information. It also prevents those ratings firms who might objectively tackle the information and promote innovation or differentiated views or analytical frameworks from being able to compete effectively. That information element is being largely ignored in this process. We can assume it is being heavily lobbied away by those that see the power and or profit in controlling it themselves.

We wish the Commission well in its effort to take on that many entrenched and powerful opponents to disclosure and a level information playing field. Some of that opposition comes from within the regulatory framework itself. Based on what we have witnessed the past 7+ years in this process, the turf battles in Washington (Treasury vs. SEC , Committee vs. Committee in Congress, etc.) make Wall Street look like a Boy Scout Camp. That reality has tended to cloud the debate and slow *meaningful* change.

Sincerely,

/s/ Glenn Reynolds	/s/ Peter Petas
Glenn Reynolds CEO CreditSights, Inc.	Peter Petas President CreditSights, Inc.