

State of Connecticut



Hartford

DENISE L. NAPPIER
TREASURER

July 25, 2008

Christopher Cox
Chairman
U.S. Securities and Exchange Commission
100 F Street N.E.
Washington, D.C. 20549

Re: File S7-13-08: Proposed Rule for Nationally Recognized Statistical Rating Organizations

Dear Chairman Cox,

As Treasurer of the State of Connecticut, my office has responsibility for the State's issuance of debt obligations and management of its \$16 billion debt portfolio and serves as principal fiduciary of the State's \$25 billion Connecticut Retirement Plans and Trust Funds. Through the management and operation of the State's \$5 billion Short Term Investment Fund, the State Treasury additionally provides an important investment vehicle for many of Connecticut's municipalities and public enterprises. As the State's largest public issuer and investor, the State Treasury has perhaps a unique perspective as a seller and purchaser of securities in the marketplace. It is in that context that we are responding to the Commission's request for comments on its Proposed Rules for Nationally Recognized Statistical Rating Organizations (NRSROs).

We wholeheartedly support the Commission's efforts to enhance the integrity of the credit ratings process and ensure that NRSROs are effectively meeting the needs of all market participants. The NRSROs can assist in improving market efficiency and market access, particularly for little-known issuers and unsophisticated investors, and the Commission can render an important public service by exercising its authority with respect to the NRSROs in order to instill greater confidence and transparency in the buying and selling of securities.

In our view, the Commission and its staff have done a commendable public service by advancing very specific proposals. Rather than responding to each of the Commission's proposed amendments and related questions, however, we would like to provide my feedback at a more "macro" level. This is significant because many of the basic objectives of your proposed rules, while properly focused on structured finance vehicles -- particularly residential mortgage-backed

securities and collateralized debt obligations -- should be applied to all types of bond ratings, including municipal and corporate ratings.

Significantly, the proposals relating to asset-backed securities could be interpreted to apply to other types of securities, including municipal obligations that are pooled financing vehicles such as housing bonds, student loan bonds, or conduit revenue bonds. Extending those proposals to such municipal securities, should be considered through separate rulemaking supported by an analysis tailored to the specifics of the municipal finance market.

My comments are focused on four critical areas:

1. The need for greater transparency in rating assignments as well as for the structured products themselves;
2. The opportunity for new NRSROs to emerge in the marketplace by encouraging greater competition;
3. The creation and enforcement of conflict-of-interest policies; and
4. Development of a single unified rating scale that applies to all types of debt, including structured products, municipal bonds, and corporate bonds.

Greater Transparency in Rating Assignments

Given the impact of a credit rating on an issue's pricing, marketability and future outlook of credit performance, it is critical that all parties have a clear understanding of how the rating is derived. I believe that the key to achieving greater transparency in the rating process is greater disclosure. I support your Proposed Rules to increase disclosure by the NRSROs about their credit screening and monitoring criteria, their analytical methodology, their quantitative and qualitative models, their surveillance practices, and their ratings performance and trends. I endorse more granularity by asset classes and explanations of differences in ratings awarded versus those generated by the model. In addition to tracking ratings changes over time, I concur with the recommendation to establish records of ratings performance by each NRSRO and believe that comparing against credit spreads is appropriate. Given that the purpose of these proposed changes is to provide greater access to potential investors, I strongly support a centralized web-based database and immediate availability of ratings changes. Discerning investors will seek to compare rating outcomes and performance of the security.

Your rules will also require disclosure of the information on which the rating is based, and that indirectly may result in greater disclosure responsibilities for the obligor. I fully support this proposal and would like to see external sources used by the NRSROs identified. As a governmental issuer, I am committed to full disclosure of all material information and would support additional disclosure responsibility that would contribute to a more efficient market with a broadened and more informed investor base. I encourage the Commission to extend these basic disclosure principles in a separate rulemaking customized for the municipal market.

New NRSROs in the Marketplace

I agree with the Commission's view that increasing the availability of the information on which a rating is based will allow any NRSRO, including those not hired by the issuer, to conduct a credit analysis. This will create opportunity for other NRSROs and benefit market participants by providing more options for obtaining credit assessments. It may also increase the development of specialty NRSROs, with in-depth credit analysis expertise in a particular area. The increased competition will not only improve the integrity of ratings, but could potentially reduce the influence of the three major firms such that the market impact of a policy change or rating action by any single firm will be less dramatic.

Conflict-of Interest Policies and Enforcement

The Proposed Rules address certain basic conflicts of interest between NRSROs and their clients; specifically, the receipt of gifts by credit analysts, and analyst participation in fee discussions, and consideration of the revenue impact on the NRSRO of their rating conclusion. It is appropriate for these conflicts of interest to be addressed in the Proposed Rules, and I support the Commission's ongoing efforts to ensure that the actions of the NRSROs are consistent with their policies in regard to these basic matters of business ethics. Given the market influence the largest of these firms enjoy, I believe that they must be held to the highest of standards, and for that reason I recommend an outright prohibition in these two areas rather than the alternative approach of allowing NRSRO disclosure with procedures to manage the conflict.

With regard to the proposed SEC prohibition on the NRSRO's making structuring or other recommendations pertaining to a security they are being asked to rate, I believe that a distinction should be made between an NRSRO analyst providing valuable feedback to an issuer about what structure or credit characteristics are viewed favorably vs. an analyst promising to provide a specific rating if recommended changes are implemented. I believe that the former should be allowed and the latter prohibited, as it does create the perception that the analyst is effectively rating his or her own work. Analyst feedback can be useful to efficient structuring of an issue. Credit analysts at rating agencies often have the same concerns and independent perspectives as institutional investors. Giving the issuer an opportunity to hear and address those potential concerns before bringing an issue to market can enhance the marketability of the offering and ultimately reduce the cost of funds to the borrower – a key concern of governmental issuers.

Another conflict is the "issuer/underwriter-pay" conflict which you propose to address by using a disclosure-based approach. I generally support that concept; but as I noted in the second paragraph of this letter, application of these rules to municipal securities should be addressed in a separate rulemaking.

Development of a Single Unified Rating Scale

The Commission is proposing that NRSROs have the option of either publishing a report with each structured finance rating that describes how "the ratings procedures and methodologies and credit risk characteristics for structured finance products" differ from those of other types of debt instruments, or using ratings symbols that differentiate structured finance ratings from the ratings for other types of debt.

I am a proponent of a single rating scale for all types of debt and believe that a single scale will facilitate the comparison of debt instruments across sectors. For municipal issuers in particular, I believe that a single scale will help level the playing field with corporate borrowers and broaden the investor base for our offerings. I believe that investors are seeking uniformity in rating symbology so that they can more clearly evaluate investment options. I urge you to consider promulgating a future rule requiring a single rating scale across all market sectors as I believe that it would be in the public interest and for the protection of investors.

If a single rating scale is in place, but additional symbols (such as “sf”) are added to the ratings associated with structured finance products, then I believe that the significance of that distinction must be clearly explained to investors each time such a rating is issued. Additionally, there must be a clear definition of a structured finance product. As previously mentioned, certain types of municipal bonds would fall into the category of asset-backed securities as referenced in the Proposed Rules. Making those types of bonds carry an “sf” label would likely affect their marketability and unfairly increase the cost of funds for municipal borrowers.

Thank you for providing this opportunity to share my thoughts with the Commission. I applaud your efforts to ensure that our securities markets function as fairly and efficiently as possible. If I can be of any further assistance to you in your endeavors, please do not hesitate to contact me.

Sincerely,

A handwritten signature in black ink that reads "Denise L. Nappier". The signature is written in a cursive style with a large initial "D".

Denise L. Nappier
Treasurer
State of Connecticut