September 8, 2008

U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549
Attention: Secretary

File No.: S7-17-08

Re: Realpoint LLC ("Realpoint") Comments to Release No. 34-58070 References to Ratings of Nationally Recognized Statistical Rating Organizations ("NRSROs")

Summary:

The Commission may accomplish its stated goals without also eliminating the benefits that independent NRSRO credit ratings may provide to investors and the public interest. The Commission’s reaction to the "recent turmoil in the credit markets" should not be to eliminate the systems of checks-and-balances provided by existing references to NRSROs.

The Commission’s proposals (published July 11, 2007), if adopted, will reduce investors’, broker-dealers’ and other market participants’ needs for credit ratings issued by NRSROs. The Commission’s proposals may therefore trigger a decrease in the number, and frequency of surveillance updates, of credit ratings. The Commission’s approach is not consistent with “[t]he purposes of the Credit Rating Agency Reform Act of 2006,” which “are to improve ratings quality for the protection of investors and in the public interest by fostering accountability, transparency, and competition in the credit rating industry.”

The Commission’s proposals, if adopted, will reduce the market for, and impair the liquidity and marketability of, asset-backed securities. The Commission’s approach may indirectly reduce yields because investors, broker-dealers and other market participants who wish to invest in asset-backed securities will need to incur additional staffing, data and other costs for review, analysis and surveillance thereof. Other investors may simply elect to forego investment in asset-backed securities. The Commission’s proposals for Regulation M will reduce the number of investors eligible to purchase asset-backed securities and reduce demand for public offerings of asset-backed securities.

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1 "[T]he Commission is considering whether the inclusion of requirements related to ratings in its rules and forms has, in effect, placed an ‘official seal of approval’ on ratings that could adversely affect the quality of due diligence and investment analysis. The Commission believes that today’s proposals could reduce undue reliance on credit ratings and result in improvements in the analysis that underlies investment decisions.” References to Ratings of Nationally Recognized Statistical Rating Organizations, Release 34-58070, SEC File Number S7-17-08, 73 Fed. Reg. 40088 (July 11, 2008) [hereinafter, “SEC File Number S7-17-08”].

2 Id. at page 40088.

3 Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations; Proposed Rule, Release 34-55231, SEC File Number S7-04-07, 72 Fed. Reg. 6378 (February 9, 2007) at page 6409. “Increased confidence in integrity of NRSROs and the credit ratings they issue could promote participation in the securities markets. Better quality ratings could also reduce the likelihood of an unexpected collapse of a rated issuer or obligor, reducing risks to individual investors and to the financial markets.” Id. at page 6410.
With respect to broker-dealers and the net capital rule\(^4\) and the customer protection rule\(^5\), the Commission should not eliminate references to credit ratings and opinions of credit risk by independent NRSROs. Instead, the Commission should require broker-dealers to: (i) separately consider independent credit rating(s) of independent NRSROs, (ii) document any determination of credit risk that is not supported by a similar determination by independent NRSROs (including the reasons for such determination), and (iii) file any such determination with the Commission and perhaps publicly disclose any such determination. This requirement would not conflict with the Commission’s goal of requiring broker-dealers to make independent determinations of credit risks. Broker-dealers would not be permitted to either place undue reliance on NRSRO credit ratings or choose to ignore NRSRO credit ratings. Given the inherent and potential conflicts of interest of a broker-dealer, when simultaneously considering and evaluating its net capital requirements and the credit risks of its various holdings, the Commission should not reduce its regulatory requirements for these determinations. The Commission should further require that the broker-dealers include in their determinations a reference to credit ratings of at least one unsolicited NRSROs not compensated by the issuer or other arranger. Further with respect to such rules, the Commission’s proposals will reduce the market for, and impair the liquidity and marketability of, asset-backed securities because broker-dealers may not be willing to undertake the extensive loan-level or collateral-level due diligence and review necessary to properly analyze and determine credit risk.

**Responses to Specific Questions:**

**Release Section IV; Request for Comment**

**Q.** On Page 40093, the three questions posed are as follows: (i) “Should we eliminate the NRSRO designation from all our rules or only from select rules? Commenters who believe that certain rules should retain references to NRSROs or NRSRO ratings should identify each rule they believe should retain the use of the NRSRO concept and explain the rationale for doing so. (ii) Does the use of the NRSRO designation in our rules cause investors to overly rely on NRSRO credit ratings? Would its

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4 “For the purposes of determining the haircut on commercial paper, [the Commission] propose[s] to replace the current NRSRO ratings-based criterion - being rated in one of the three highest rating categories by at least two NRSROs - with a requirement that the instrument be subject to a minimal amount of credit risk and have sufficient liquidity such that it can be sold at or near its carrying value almost immediately. For the purposes of determining haircuts on nonconvertible debt securities as well as on preferred stock, [the Commission] propose[s] to replace the current NRSRO ratings-based criterion - being rated in one of the four highest rating categories by at least two NRSROs - with a requirement that the instrument be subject to no greater than moderate credit risk and have sufficient liquidity such that it can be sold at or near its carrying value within a reasonably short period of time. This latter formulation would apply as well to long or short positions in securities issued by the United States or any agency thereof or nonconvertible debt securities having a fixed interest rate and a fixed maturity date and which are not traded flat or in default as to principal or interest. [The Commission] preliminarily believe[s] that these new standards would continue to advance the purpose the NRSRO ratings-based standards were designed to advance, which is to enable broker-dealers to make net capital computations that reflect the market risk inherent in the positioning of those particular types of securities.” SEC File Number S7-17-08 at page 40092.

5 “Note G to Exhibit A of Rule 15c3-3 under the Exchange Act (the ‘Customer Protection Rule’), which provides the formula for the determination of broker-dealers’ reserve requirements, allows a broker-dealer to include as a debit in the formula the amount of customer margin related to customers’ positions in security futures products posted to a registered clearing or derivatives organization that maintains the highest investment grade rating from an NRSRO. This standard, which is one of four different means by which a registered clearing or derivatives organization can be judged to meet the requirements of paragraph (b)(1) of Note G,55 is consistent with the customer protection function of Rule 15c3-3 and is necessary because of the unsecured nature of the customer positions in security futures products margin debit. [The Commission] propose[s] to replace this standard with a requirement that the registered clearing or derivatives organization to which customers’ positions in security futures products are posted has the highest capacity to meet its financial obligations and is subject to no greater than minimal credit risk.” SEC File Number S7-17-08 at page 40094.
A. The Commission should not eliminate any of the benefits that independent NRSRO credit ratings may provide to investors or the public interest. The Commission’s proposals, to eliminate references to NRSROs from existing rules, do not benefit investors or the public interest. Investors, and the public interest, would be better served by a requirement that investment companies and broker-dealers disclose when their determinations of credit risk deviate from those of an independent NRSRO.

As the Commission reduces or eliminates the regulatory purposes of NRSRO credit ratings, the Commission reduces the financial incentives for market participants to compensate NRSROs for credit ratings. The Commission’s proposals may trigger a decrease in the number, and frequency of surveillance updates, of credit ratings. The Commission’s approach may therefore cause investors, broker-dealers and other market participants to incur additional costs for review, analysis and surveillance. These additional costs will indirectly reduce investors’ yields from these securities.

The Commission bases its perceived need to eliminate the NRSRO designation from various rules on its assumption that investors and other participants in the capital markets place undue reliance on credit ratings. In making this assumption, the Commission appears to be making the assumption that investors only refer to letter-grade credit ratings published by NRSROs and ignore the various reports published by NRSROs in connection therewith. The Commission’s assumption in this regard is likely incorrect given that NRSROs often disclose letter-grade ratings for no or a relatively nominal charge while investors and broker-dealers purchase the analytical reports.

Release Section III.E; Proposed Amendments to Rules 101 and 102 of Regulation M

Q. On Page 40096, the second, fifth, seventh and eighth questions posed are as follows: “Should the Rule 101(c)(2) and 102(d)(2) exceptions be based on criteria other than the WKSI requirements for nonconvertible debt and nonconvertible preferred securities and Form S-3 registration for asset-backed securities? Do the proposed WKSI and Form S-3 benchmarks adequately identify nonconvertible debt, nonconvertible preferred securities, and asset-backed securities that are of high quality with low default risk? Please distinguish the characteristics of nonconvertible debt, nonconvertible preferred securities, and asset-backed securities that meet these proposed benchmarks and those that do not. Would persons other than issuers who are subject to Rules 101 and 102 have access to adequate information to determine if a particular security fits into the exceptions? Should asset-backed securities registered on Form S-3 be excepted from Rules 101 and 102 of Regulation M? Have there been developments in the asset-backed securities market that might indicate whether such securities should be eliminated from the proposed exceptions or should continue to be excepted from Rules 101 and 102?”

A. The Commission proposes to limit the exception from Regulation M for asset-backed securities to those registered on Form S-3 rather than those that have been rated “investment grade” by an NRSRO. At the same time, the Commission is reducing the desirability of Form S-3 registrations by proposing: (i) that offerings of securities registered on Form S-3 or issued under Rule 415 may only be sold in minimum denominations of $250,000; (ii) that initial sales thereof may only be made to qualified institutional

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6. n.1, supra

buyers; and (iii) “to eliminate the exclusion [under Rule 3a-7] for structured financings offered to the general public.” (The reduced utility of Form S-3 with respect to structured finance products is addressed in comments to Security Ratings, Release 34-58071, SEC File Number S7-18-08, 73 Fed. Reg. 40106 (July 11, 2008).) Unregistered securities are generally less liquid than registered securities. Thus, the Commission is proposing to limit the market for asset-backed securities rather than retain existing measures that support capital formation and liquidity based on such securities.

Realpoint and others who filed comments to SEC File No. S7-13-0810 opined that separate rating symbols should not be implemented to differentiate structured finance products from corporate debt securities. The Commission’s proposals to limit the potential investor base for asset-backed securities is a more subtle, but equally damaging, means to implement this differentiation. This differentiation will create confusion within the financial markets with respect to, and impair the value of, structured finance products.

Persons other than issuers who are subject to Rules 101 and 102 include “selling security holders, underwriters, brokers, dealers, other distribution participants, and any of their affiliated purchasers.”11 These persons, as sellers, may not know whether a potential purchaser is a qualified institutional buyer. The Commission’s proposal does not implement a standard, such as that available under private placements under Rule 144A, that permits a broker or dealer selling securities in reliance on Rule 144A to make offers to a person if it reasonably believes that person is a qualified institutional buyer. Thus, the Commission’s proposals for amending Regulation M, if adopted, will further limit the market for asset-backed securities.

Release Sections III.C, D; Proposed Amendments to Rules 15c3-1 and 15c3-3

Q. On Page 40093, the first question posed is as follows: “Would internal evaluations of individual debt securities by broker-dealers for purposes of determining the capital charges (“internal processes”) instead of reliance on NRSRO ratings accomplish the stated goals of the Commission’s net capital requirements?” On Page 40094, the second question posed is as follows: “What would be the potential consequences of using internal processes for purposes of the net capital rule and how could these be addressed? For example, one concern is that a broker-dealer would have an incentive to downplay the credit risk associated with a particular security in order to minimize capital charges. How could this concern be addressed?” On Page 40095, the second question posed is as follows: Is it appropriate to allow broker-dealers to make the determination of whether a clearing organization possesses the highest capacity to meet its financial obligations and is subject to no greater than minimal credit risk? If not, what are suggested ways that the proposed rule could be amended to address that concern? On Page 40095, the fourth question posed is as follows: What would be the potential consequences of allowing broker-dealers to determine whether a clearing organization possessed the highest capacity to meet its financial obligations and was subject to no greater than minimal credit risk and how could these be addressed? For

8 Id. at 40109-40110.
11 “Rules 101 and 102 of Regulation M specifically prohibit issuers, selling security holders, underwriters, brokers, dealers, other distribution participants, and any of their affiliated purchasers, from directly or indirectly bidding for, purchasing, or attempting to induce another person to bid for or purchase, a covered security until the applicable restricted period has ended.” Id. at 40095.
example, one concern is that a broker-dealer would have an incentive to downplay the credit risk associated with a particular clearing organization in order to be able to post customers' positions in security futures products to it. How could this concern be addressed?

A. Potential consequences of relying solely on internal processes include: (i) increased costs to broker-dealers to make credit risk determinations; and (ii) a loss of transparency in the rating process. Broker-dealers have inherent and potential conflicts of interest when determining their net capital requirements. Thus, there are no advantages to relying solely on broker-dealers to determine whether a security “is subject to a minimal amount of credit risk,” “is subject to no greater than moderate credit risk,” or “is subject to subject to no greater than minimal credit risk.” The Commission should also not rely on broker-dealers voluntarily implementing procedures to refer to NRSRO credit ratings. Given that the Commission intends to retain the requirement to refer to NRSRO ratings as part of the customer protection rule, the Commission should retain the requirement to refer to NRSRO ratings as part of the net capital rule. Further, instead of eliminating requirements to refer to NRSRO ratings, the Commission should consider revising Rule 15c3-1 and Rule 15c3-3 to require broker-dealers to separately consider credit rating(s) of independent NRSROs and document or publish when their determinations deviate therefrom. Such a requirement would support the Commission’s stated goals without authorizing a complete disregard for readily-available NRSRO credit ratings.

Further with respect to such rules, the Commission’s proposals will reduce the market for, and impair the liquidity and marketability of, asset-backed securities. With respect to issuances of asset-backed securities, and, in particular, commercial mortgage-backed securities (“CMBS”), broker-dealers may not be willing to undertake the extensive loan-level or collateral-level due diligence and review necessary to properly analyze and determine credit risk. An NRSRO needs the period of approximately four to six weeks to review and analyze property-level due diligence items (including operating statements, leases, appraisals, inspection and other reports) and forecast defaults and losses in part by means of quantitative analytical models. That information may include ABS informational and

12 With respect to Rule 15c3-1, the Commission has not proposed a requirement of disclosure of the “internal processes.” See id. at 40093. Under Rule 15c3-3, all that the Commission intends to require is that “[the broker-dealer] would have to be able to explain how the registered clearing or derivatives organization to which customers’ positions in security futures products are posted meets the standard in the proposed amendment.” Id. at 40094.

13 SEC File Number S7-17-08 at page 40092.

14 Id.

15 Id. at 40094.

16 [The Commission] believe[s that] it would be appropriate, as one means of complying with the proposed amendments, for broker-dealers to refer to NRSRO ratings for the purposes of determining haircuts under the [n]et [c]apital [r]ule. As such, if [the Commission] adopts the proposed amendments, after considering comments, [it] expect[s] to take the view in the adopting release that securities rated in one of the three highest categories by at least two NRSROs would satisfy the requirements of proposed new paragraph [17 CFR §240.15c3-1](c)(2)(vi)(E) and securities rated in one of the four highest rating categories by at least two NRSROs to satisfy the requirements of proposed new paragraphs [17 CFR §240.15c3-1](c)(2)(vi)(F) and (c)(2)(vi)(H). [The Commission] emphasize[s], however, that references to such NRSRO ratings would be just one means of satisfying the requirements of the proposed amendments but would not be the only means of doing so. Id. at 40093.

17 The Commission believes “that it would be appropriate, as one means of complying with the proposed amendment [to Note G to Exhibit A of Rule 15c3–3 under the Exchange Act (the “Customer Protection Rule”)] for broker-dealers to refer to NRSRO ratings for [such] purposes. . . . [The Commission] expect[s] to . . . continue to consider a registered clearing agency or derivatives clearing organization that maintains the highest investment-grade rating from an NRSRO to satisfy the requirements of that provision. We emphasize, however, that the references to such NRSRO ratings would be just one means of satisfying the requirements of the proposed amendments and would not be the only means of doing so.” Id. at 40094.
computational materials such as: (i) underlying property information and other loan-level information (which may, in the future, be provided by the issuer or other arrangers under the Commission’s proposed disclosure requirements under amended 17 CFR § 240.17g-5(a)(3)), (ii) additional data, research or due diligence reports purchased or developed by the NRSRO, and (iii) analyses developed therefrom. Thereafter, an NRSRO performs surveillance of the underlying loans and collateral. If broker-dealers are required to undertake their own, separate reviews, and in so doing incur additional costs, the resulting CMBS yields net of those costs will reduce the attractiveness of these structured finance products in the capital markets.

Release Section III.B; Proposed Amendments to Rule 10b-10

Q. On Page 40092, the second question posed is as follows: “Are there any possible alternatives to deletion that would address concerns about undue reliance on NRSRO ratings or avoid confusion about the significance of those ratings? For example, should the confirmation disclose that the security is rated or not rated by an NRSRO, as the case may be, instead of just that the security is not rated?”

A. Investors benefit from, and broker-dealers are not materially burdened by, the existing requirement to disclose whether a corporate debt security is not rated by an NRSRO. The Commission should therefore, at a minimum, retain the existing requirement rather than rely on investor demand for this information or on broker-dealers “voluntarily continuing to include this information in transaction confirmations.” Further, given the Commission’s estimated increase in the number of NRSROs, the Commission should also strongly consider requiring that the confirmation disclose whether the security is rated by an NRSRO who was not and is not being compensated for such rating from the original issuance or otherwise by the issuer or other arrangers.

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18 “Paragraph (a)(8) of Rule 10b–10 requires transaction confirmations for debt securities, other than government securities, to inform the customer if the security is unrated by an NRSRO. When [the Commission] adopted paragraph (a)(8) in 1994, it was intended to prompt a dialogue between the customer and the broker-dealer if the customer had not previously been informed of the unrated status of the debt security. [The Commission] stated that this disclosure was not intended to suggest that an unrated security is inherently riskier than a rated security. Upon further consideration and in light of present concerns regarding undue reliance on NRSRO ratings and confusion about the significance of those ratings, [the Commission] believe[s] it would be appropriate to delete this requirement. . . . [The Commission] do[es] not mean to suggest that information about an issuer’s creditworthiness is not a relevant subject for discussion and consideration prior to purchasing a debt security. [The Commission] would encourage investors to seek to understand all of the risks of securities, including credit-related risks, before buying. In addition, [the Commission] notes that deleting this requirement would not prevent broker-dealers from voluntarily continuing to include this information in transaction confirmations.” SEC File Number S7-17-08, 73 Fed. Reg.40088 (July 11, 2008) at page 40092.

19 “In adopting the final rules under the Rating Agency Act, the Commission estimated that approximately 30 rating agencies would be registered as NRSROs.” Proposed Rules for Nationally Recognized Statistical Rating Organizations, SEC File Number S7-13-08, 73 Fed. Reg. 36212 (June 25, 2008) at page 36237. At the time of the Commission’s adoption of Rule 10b–10(a)(8), six rating organizations were “designated as NRSROs for purposes of the net capital rule,” one of which was “designated as an NRSRO only for the purposes of rating debt issued by banks, bank holding companies, United Kingdom building societies, broker-dealers, broker-dealer parent companies and bank-supported debt.” Nationally Recognized Statistical Rating Organizations, Release No. 34-34616 (August 31, 1994), 59 FR 46314 (September 7, 1994).
Thank you for the opportunity to comment on the above-referenced proposed amendments. Please do not hesitate to contact us if you have any questions.

Very truly yours,

Robert Dobilas
CEO and President
Realpoint LLC