

THE FINANCIAL SERVICES ROUNDTABLE

Financing America's Economy



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By Electronic Mail (rule-comments@sec.gov)

March 28, 2011

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

**RE: Securities Ratings [Release No. 33-9186; 34-63874;
File No. S7-18-08] RIN 3235-AK18 (February 16, 2011)**

Dear Ms. Murphy:

The Financial Services Roundtable¹ (the “Roundtable”) respectfully submits these comments in response to the request for comments on the proposal (the “Proposal”) by the Securities and Exchange Commission (the “Commission”) to amend rules and forms under the Securities Act of 1933 and the Securities Exchange Act of 1934² pursuant to Section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”).³ Section 939A of the Dodd-Frank Act directs the Commission to review its regulations that refer to or rely on credit ratings of securities, remove those references or requirements, and substitute an appropriate creditworthiness standard.⁴

- I. The Roundtable believes the revision to eligibility requirements for use of Forms S-3⁵ and F-3,⁶ and removal of the safe harbor afforded by Rule 134(a)(17),⁷ would cause a material, adverse effect on certain issuers and market participants, and impose substantial costs and burdens on issuers that outweigh the benefits to investors of the proposed rules.**

¹ The Roundtable represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. Roundtable member companies provide fuel for America's economic engine, accounting directly for \$ 92.7 trillion in managed assets, \$ 1.2 trillion in revenue, and 2.3 million jobs.

² See Securities Act Release No. 9186, 76 Fed. Reg. 8946 (Feb. 16, 2011) (the “Proposing Release”).

³ Pub. Law No. 111-203, § 939A, 124 Stat. 1887 (July 21, 2010).

⁴ Pub. Law No. 111-203, § 939A(a)-(b), 124 Stat. 1887 (July 21, 2010).

⁵ 17 C.F.R. § 239.13 (2009).

⁶ 17 C.F.R. § 239.33 (2009).

⁷ 17 C.F.R. § 230.134(a)(17) (2009).

A. The Commission should preserve the eligibility of those entities that are currently eligible to use Form S-3 or Form F-3.

The requirement to remove credit rating references from the Commission's rules reflected Congress's concern about investors' inordinate reliance on credit ratings.⁸ We do not believe the change arose out of concern that the Commission's forms are being used by inappropriate entities or for inappropriate transactions. Indeed, the legislative goal was to "encourage[] investors to conduct their own analysis."⁹ Given this context, we do not believe it would be appropriate to deprive those entities that currently rely on short-form registration of the ability to continue to do so.

Moreover, we are concerned that a requirement based on the issuance of \$1 billion in aggregate principal amount of non-convertible securities (other than common equity securities) in the prior three years would make capital raising more difficult. Nor do we believe it would provide a meaningful alternative measure of "creditworthiness" or consistently demonstrate a wide following in the market. An issuer's ability to satisfy the proposed \$1 billion minimum offering history requirement could depend on something as arbitrary as when the three-year measuring period begins, and could exacerbate the effect of market disruptions. For example, the financial crisis that preceded enactment of the Dodd-Frank Act effectively shuttered the financial markets for some period of time. Issuers who lose access to capital markets during times of economic crisis should not also be at risk of losing Form S-3 or Form F-3 eligibility as a consequence, as would be the case if the Proposals were adopted. Such a result could impede capital formation and delay financial recovery at critical times.

We urge the Commission not to adopt rules that would deprive regulated, investment-grade entities of the use of Form S-3 or Form F-3 because they can no longer rely on the security rating criterion.

B. The Commission either should retain the reference to security ratings *disclosure* in Rule 134(a)(17), or provide interpretative guidance that disclosure of these ratings is permissible.

Section 939A of the Dodd-Frank Act requires the Commission to remove any reference to or requirement of reliance on credit ratings from the Commission's regulations and to substitute such standard of creditworthiness as the Commission deems appropriate. The purpose of Section 939A was to discourage "over-reliance" on security ratings information due to references in the Commission's regulations or any requirement in the Commission's regulations to use security ratings.¹⁰

Rule 134 affords a safe harbor from the definitions of "prospectus" in Section 2(a)(10) of the Securities Act¹¹ and "free writing prospectus" in Rule 405 under the Securities Act¹² for communications about a securities offering that comply with Rule 134. The information permitted in a Rule 134-communication is restricted to brief factual data, such as the name of the issuer and underwriters, the exchange where the securities are to be listed, and the ticker symbol.

Issuers and underwriters regularly rely on Rule 134 to disseminate information on public offerings. By relying on Rule 134, issuers and underwriters can provide summary factual information

⁸ See H.R. REP. NO. 111-517 at 871 (2010) (Conf. Rep.).

⁹ Wall Street Reform Conference Report Summary at 11 (July 1, 2010), available at http://banking.senate.gov/public/files/070110_Dodd_Frank_Wall_Street_Reform_comprehensive_summary_Final.pdf.

¹⁰ *Id.*

¹¹ 15 U.S.C. § 77(b)(a)(10) (2006).

¹² 17 C.F.R. § 230.405 (2009).

about the offering to investors without concern that these factual disclosures would constitute either a non-statutory prospectus under Section 10 of the Securities Act¹³ or a free writing prospectus that either was not permitted or not timely filed pursuant to Rule 433 under the Securities Act.¹⁴ Either of those failures could result in a violation of Section 5 of the Securities Act,¹⁵ which in turn can lead to some of the most onerous penalties under the Securities Act, including strict rescission liability.¹⁶

The Commission proposes to eliminate the safe harbor of Rule 134(a)(17) for any communication that includes any security rating for the offered securities that was assigned by a nationally recognized statistical rating organization. The Commission noted that “removing the safe harbor for this type of information would not necessarily result in a communication that included this information being deemed to be a prospectus or free writing prospectus . . . [but] would simply result in there no longer being a safe harbor for a communication that included this information.”¹⁷

The Roundtable is concerned that eliminating the Rule 134 safe harbor for disclosures of security ratings would effectively stifle the free flow of communications about security ratings information to investors and markets, but would not eliminate investor demand for ratings information. Given the onerous consequences associated with the dissemination of a non-statutory prospectus or the failure to file a free writing prospectus, we believe that eliminating the Rule 134(a)(17) safe harbor would have a chilling effect on issuers and underwriters who currently rely on the safe harbor to publish “tombstones” or other advertisements that disclose security ratings information that investors regularly use.

The Roundtable does not believe that permitting security ratings to be *disclosed* in Rule 134 communications provides the Commission’s *imprimatur* for such disclosures or otherwise makes the Commission (or any other governmental authority) an advocate for security ratings. Nor did Congress intend to chill or eliminate completely the ability of issuers or underwriters to communicate information on securities ratings that many knowledgeable investors and market participants insist on receiving.¹⁸

The Commission has broad authority to “exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of [the Securities Act] or of any rule or regulation issued under [the Securities Act].”¹⁹ Therefore, we ask the Commission either to: (a) exercise its exemptive authority to retain paragraph (a)(17) of Rule 134, or (b) provide clear interpretative guidance that the disclosure of security ratings would continue to be permissible without the risk of violating Section 5 of the Securities Act.

C. The costs and burdens imposed on issuers arising out of the revised eligibility standards for Forms S-3 and F-3 outweigh any potential benefit to investors.

The Commission acknowledged that many of the entities that would lose access to Form S-3 are regulated insurance companies and regulated energy utilities.²⁰ Yet the costs that would be imposed on regulated entities are not insignificant. For example, a Roundtable member company estimated that registering its non-variable annuity certificates on Form S-1²¹ (rather than on Form S-3) could increase

¹³ 15 U.S.C. § 77(j)(a) (2006).

¹⁴ 17 C.F.R. § 230.433 (2009).

¹⁵ 15 U.S.C. § 77(e) (2006).

¹⁶ 15 U.S.C. § 77l (2006).

¹⁷ Proposing Release at 8955.

¹⁸ Proposing Release at 8947 (recognizing that “credit ratings play a significant role in the investment decision of many investors”).

¹⁹ 15 U.S.C. § 77z-3 (2006).

²⁰ Proposing Release n. 58 and accompanying text.

²¹ 17 C.F.R. § 239.11 (2009).

its offering expenses by hundreds of thousands of dollars annually.²² This company's inability to avail itself of the shelf offering process pursuant to Rule 415 under the Securities Act²³ also would present logistical difficulties and practical restraints on capital raising activities. In addition, the loss of Form S-3 or Form F-3 eligibility may make domestic public offerings less desirable for issuers and may impede their timely access to necessary capital.

The only potential benefit to investors that the Commission identified as a result of its Proposal was that investors would not have to "seek out Exchange Act reports," because issuers would not be able to incorporate these reports by reference into their prospectuses.²⁴ In view of the ready availability of an issuer's full reporting on Form 10-K,²⁵ 10-Q²⁶ and 8-K²⁷ (in the case of a domestic issuer), and Forms 20-F²⁸ and 6-K²⁹ (in the case of a foreign private issuer), the availability of a short-form registration statement does not reduce the information available to investors. Indeed, investors have at their fingertips substantially all the information that would be included in a long-form registration statement. The availability of the short-form registration statement would, however, ease substantially the burdens on capital formation.

The Roundtable believes these substantial costs and burdens on issuers would outweigh any potential benefits to investors. We believe that these consequences, as collateral damage from legislation aimed at over-reliance on security ratings, are inappropriate.

II. The Roundtable recommends other alternatives that it believes would more effectively accomplish both Congressional intent and the Commission's regulatory program.

A. The Roundtable recommends that the Commission "grandfather" during the transition period all existing users of Form S-3 or Form F-3.

We believe the Commission should provide a transition period prior to full implementation of the new eligibility rules. This would enable affected issuers to update information technology and other systems, compliance and supervisory controls, and other operational functions so that issuers could meet the requirements of the new rules.

During the transition, each current user of Form S-3 and Form F-3 would be "grandfathered" for all types of securities transactions that they would currently be eligible to register on Form S-3 or Form F-3.³⁰ One possible approach would be to allow a grandfathered issuer to certify for each new Form S-3 or Form F-3 registration statement that "it has reasonable grounds to believe that: (i) it was eligible to use Form S-3 or Form F-3 at the time of the adoption of the new eligibility rules; and (ii) based on the standards in existence prior to adoption of the new eligibility rules, it would have been eligible to file the

²² These additional costs would include 250 hours of in-house legal time, 150 hours of business personnel time, outside legal counsel expenses, and independent auditor expenses.

²³ 17 C.F.R. § 230.415 (2009).

²⁴ Proposing Release at 8957. However, investors can easily obtain an issuer's Exchange Act reports either from the Commission's EDGAR site or from an issuer's website.

²⁵ 17 C.F.R. § 249.310 (2009).

²⁶ 17 C.F.R. § 249.308a (2009).

²⁷ 17 C.F.R. § 249.308 (2009).

²⁸ 17 C.F.R. § 249.220f (2009).

²⁹ 17 C.F.R. § 249.306 (2009).

³⁰ We ask the Commission to allow issuers who have effective Form S-3 or Form F-3 registration statements at the time the final rules take effect to use the remaining capacity on those registration statements through the expiration date of the applicable registration statement.

new registration statement.”³¹

B. The Roundtable recommends that the Commission consider compliance with regulatory requirements as an alternative indicator of creditworthiness.

The Roundtable believes a large portion of issuers affected by the Proposal are regulated entities (e.g., insurance companies and public utilities). Therefore, we recommend that the Commission consider compliance with regulatory capital or other requirements as an alternative condition for short-form registration eligibility for regulated entities. For example, U.S. insurance companies are subject to comprehensive regulation (including capital requirements) by insurance commissioners of each jurisdiction where they conduct business. Relying on a comprehensive regulatory system would be analogous to the comprehensive federal banking regulatory scheme applicable to federally insured certificates of deposit issued by banks.³² We believe an eligibility requirement based on a regulated entity’s compliance with state or federal regulatory standards would be consistent with Congress’s goal to use other *indicia* of creditworthiness.

C. The Roundtable further recommends that the Commission adopt an eligibility requirement based on an issuer’s Exchange Act reporting history and compliance with the conditions in General Instruction I.A. of Form S-3.

The Commission did not propose alternative *indicia* of creditworthiness, but instead focused on *indicia* of a “wide following in the market” for purposes of eligibility to use Form S-3 or Form F-3. The Commission stated its belief that “a wide following in the marketplace makes Form S–3 and Form F–3 appropriate for these issuers because information about them is generally readily available.” In our view, there is no reason to rely on an eligibility requirement premised on an issuer’s “market following” because investors and market participants have real-time access to information on every Exchange Act reporting company³³ (a “reporting company”).

When the Commission adopted the integrated disclosure system over 30 years ago,³⁴ information about reporting companies was far less widely disseminated. For example, an investor had to submit his or her request for a company’s filings at the Commission’s Public Reference Desk, because the EDGAR system did not exist. Documents the company was required to deliver to its shareholders usually were sent *via* U.S. Mail. Form 8-K had far fewer disclosure items and much longer filing deadlines, instead of the “real-time” disclosure the Form now requires.³⁵ Research analyst calls with the company’s senior management generally were closed to the public. Beginning in the early 1990s, investors used a home or office Internet connection to access financial information—now, they can access financial

³¹ Our proposed registrant certification would be an alternative to the current registrant certification requirement. This approach is similar to one that the Federal Deposit Insurance Corporation (“FDIC”) has applied in one of its safe harbors. *See* Treatment by the Federal Deposit Insurance Corporation as Conservator or Receiver of Financial Assets Transferred by an Insured Depository Institution in Connection With a Securitization or Participation After September 30, 2010, 12 C.F.R. §360.6, 75 Fed. Reg. 60287 (2010). The predecessor to that safe harbor had been tied to an accounting standard that was revised by the Financial Standards Accounting Board. The FDIC grandfathered some issuers so long as they could continue to meet the conditions of the predecessor accounting standard.

³² *See* *Marine Bank v. Weaver*, 455 U.S. 551 (1982).

³³ *See* Sections 13(a) and 15(d) of the Exchange Act, 15 U.S.C. §§ 78m(a) and 78o(d) (2006).

³⁴ Adoption of Integrated Disclosure System, Securities Act Release No. 6383, 47 Fed. Reg. 11380 (Mar. 2, 1982).

³⁵ The Commission noted the salutary effect of these changes on the regulatory environment when it modernized its rules for public offerings. *See* Securities Offering Reform, Securities Act Release No. 8591, 70 Fed. Reg. 44722, 44726 (August 3, 2005) (The increasing role of technology in the dissemination of information and the Commission’s own actions “have enhanced significantly the disclosure included in issuers’ Exchange Act filings and accelerated the filing deadlines for many issuers.”).

information on mobile phones, tablet computers and other mobile electronic devices. Today, virtually every reporting company has *a wide market following* because of changes to disclosure rules and innovations in technology and communications.

We believe the conditions in General Instruction 1.A. to Form S-3 would be a more appropriate eligibility requirement for an issuer registering a primary offering of non-convertible securities (excluding common equity) on Form S-3 or Form F-3. A minimum one-year reporting history³⁶ (including the company's Form 10-K obligation) would help investors and other market participants understand the company's business and material trends. A reporting company also should be able to register primary offerings of nonconvertible securities (excluding equities) on Form S-3 or Form F-3 without regard to the amount of securities it has outstanding or its public float.³⁷

We believe an eligibility requirement based on the public company's Exchange Act reporting history would be an appropriate alternative to criteria that reflect the credit quality of non-convertible securities as determined by third party credit rating agencies. Therefore, we ask the Commission to adopt an alternative creditworthiness standard that relies on the issuer's Exchange Act reporting history for purposes of Form S-3 or Form F-3 eligibility.

* * * * *

³⁶ Of course, the Commission could establish a longer minimum reporting period if that were in the public interest and necessary to protect investors.

³⁷ Foreign private issuers also should be eligible to use Form F-3 as long as the information they make available to US investors is comparable to that which they would have made available had they been US companies.

The Roundtable and its members appreciate the opportunity to comment to the Commission on its Proposals to remove requirements and references in rules and forms to securities ratings and substitute an appropriate creditworthiness standard under the Securities Act and Exchange Act. If it would be helpful to discuss the Roundtable's specific comments or general views on this issue, please contact me at Rich@fsround.org. Please also feel free to contact the Roundtable's Senior Regulatory Counsel, Brad Ipema, at Brad.Ipema@fsround.org.

Sincerely yours,

A handwritten signature in black ink that reads "Richard M. Whiting". The signature is written in a cursive, slightly slanted style.

Richard M. Whiting
Executive Director and General Counsel
The Financial Services Roundtable

With a copy to:

- The Honorable Mary L. Schapiro, Chairman
- The Honorable Kathleen L. Casey, Commissioner
- The Honorable Elisse B. Walter, Commissioner
- The Honorable Luis A. Aguilar, Commissioner
- The Honorable Troy A. Paredes, Commissioner

Meredith Cross, Director, Division of Corporation Finance
Eileen Rominger, Director, Division of Investment Management