
**Report to Congress
Credit Rating Agency Independence Study**

**As Required by Section 939C of the
Dodd-Frank Wall Street Reform and
Consumer Protection Act**



November 2013

This is a report prepared by the Staff of the Office of Credit Ratings of the U.S. Securities and Exchange Commission. The Commission has expressed no view regarding the analysis, findings or conclusions contained in this report.

Table of Contents

Introduction.....	3
Part One	4
I. Dodd-Frank Independence Study Requirement and Annual NRSRO Examination Requirement.....	4
A. Independence Study.....	4
B. Annual NRSRO Examinations and Report.....	5
II. Current NRSROs.....	7
III. Current U.S. Regulatory Framework	8
A. Rule 17g-5(a) and Rule 17g-5(b) (Managed Conflicts of Interest)	9
B. Rule 17g-5(c) (Prohibited Conflicts of Interest).....	10
C. Rule 17g-6 (Prohibited Acts and Practices).....	11
D. Reporting Requirements	12
i. Form NRSRO.....	12
ii. Rule 17g-2(a)(5).....	13
IV. Applicable Proposed NRSRO Rules	14
V. IOSCO Code of Conduct and European Union Credit Rating Agency Regulations	15
A. IOSCO Code of Conduct	15
B. European Union Credit Rating Agency Regulations	16
Part Two.....	18
VI. Overview of NRSRO Ancillary Services and Potential Conflicts of Interest Involved.....	18
A. Ancillary Services Definition Used in this Report	18
B. Ancillary Services Provided by NRSROs.....	19
C. Potential Conflicts of Interest Involving Ancillary Services	21
VII. Description of NRSRO Ancillary Services and Policies and Procedures to Manage Potential Conflicts of Interest.....	24
A. A.M. Best.....	25
i. Products and Services.....	25
ii. Policies and Procedures.....	26
B. DBRS	26
i. Products and Services.....	26
ii. Policies and Procedures.....	27
C. EJR.....	28

i.	Products and Services.....	28
ii.	Policies and Procedures.....	28
D.	Fitch Ratings	29
i.	Products and Services.....	29
ii.	Policies and Procedures.....	30
E.	HR Ratings.....	31
i.	Products and Services.....	31
ii.	Policies and Procedures.....	31
F.	JCR.....	32
i.	Products and Services.....	32
ii.	Policies and Procedures.....	32
G.	Kroll	33
i.	Products and Services.....	33
ii.	Policies and Procedures.....	33
H.	Moody’s	34
i.	Products and Services.....	34
ii.	Policies and Procedures.....	36
I.	Morningstar.....	37
i.	Products and Services.....	37
ii.	Policies and Procedures.....	37
J.	S&P	38
i.	Products and Services.....	38
ii.	Policies and Procedures.....	40
VIII.	NRSRO Enforcement of Policies and Procedures; NRSRO Exam Report Findings	41
A.	NRSRO Enforcement of Policies and Procedures	41
B.	NRSRO Exam Report Findings	42
IX.	Comparable Conflicts of Interest	43
X.	Conclusions and Recommendations.....	46

Introduction

This report, prepared by the staff of the Office of Credit Ratings (the “Staff”) of the U.S. Securities and Exchange Commission (the “Commission”), is being submitted under Section 939C (“Section 939C”) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) to the Committee on Banking, Housing, and Urban Affairs of the U.S. Senate and the Committee on Financial Services of the U.S. House of Representatives (collectively, the “Congressional Committees”).

This report is divided into Part One and Part Two. Part One, including Sections I through V, describes the study (the “Dodd-Frank Independence Study” or the “Study”) required by Section 939C on the independence of nationally recognized statistical rating organizations (“NRSROs”) and how such independence affects ratings issued by the NRSROs; describes the annual examinations of NRSROs; identifies the current NRSROs; and reviews the U.S. and foreign regulatory backdrop for the provision of ancillary services by the credit rating industry and conflicts of interest with respect thereto.

Part Two of this report, including Sections VI through X, includes an overview of the ancillary services provided by the NRSROs and the potential conflicts of interest involved; reviews, on an entity-by-entity basis, the details of the ancillary services provided by the NRSROs and the applicable policies and procedures which have been publicly disclosed by the NRSROs; describes certain self-enforcement measures taken by NRSROs with respect to such policies and procedures; describes the results of relevant essential findings from recent annual NRSRO examinations; considers comparable conflicts of interest; and offers related conclusions and recommendations.

Part One

I. Dodd-Frank Independence Study Requirement and Annual NRSRO Examination Requirement

A. Independence Study

On July 21, 2010, President Obama signed the Dodd-Frank Act into law.¹ Title IX, Subtitle C of the Dodd-Frank Act, consisting of Sections 931 through 939H and titled “Improvements to the Regulation of Credit Rating Agencies,” amended Section 15E (“Section 15E”) of the Securities Exchange Act of 1934 (the “Exchange Act”)² to impose new self-executing requirements applicable to NRSROs and required the Commission to adopt rules applicable to NRSROs in a number of areas. The credit rating agencies which are currently registered as NRSROs are listed in Section II of this report.

One of the Congressional findings included in the Dodd-Frank Act was that rating agencies, in particular in advising arrangers of structured financial products on potential ratings of such products, face conflicts of interest that need to be carefully monitored.³ In light of this finding, the Dodd-Frank Act required, among other things, various studies to be conducted, including a Commission Study on Strengthening Credit Rating Agency Independence.⁴ Section 939C requires the Commission to conduct a study of the independence of NRSROs and how NRSRO independence affects the ratings issued by the NRSROs. In conducting this study, the Commission is required to evaluate the management of conflicts of interest raised by an NRSRO providing other services, such as risk management advisory services, ancillary assistance, or

¹ See Pub. L. No. 111-203, 124 Stat. 1376 (2010).

² 15 U.S.C. § 78o-7.

³ See Pub. L. No. 111-203 § 931(4). A Senate Report related to the Dodd-Frank Act noted, for instance, that conflicts of interest in the process of rating structured financial products contributed to the issuance of inaccurate ratings by rating agencies and accordingly to the mismanagement of risk by financial institutions and investors. See S. Report. No. 111-176 (2010).

⁴ See Pub. L. No. 111-203 §§ 939, 939C - 939F.

consulting services, and the potential impact of rules prohibiting an NRSRO that provides a rating to an issuer from providing other services to the issuer.

The Dodd-Frank Act further requires the Chairman of the Commission to submit a report on the results of the study, “including recommendations, if any, for improving the integrity of ratings issued by [NRSROs]” to the Congressional Committees not later than three years after the enactment of the Dodd-Frank Act.⁵

B. Annual NRSRO Examinations and Report

Section 15E(p)(3)(A) of the Exchange Act, which was added by the Dodd-Frank Act, requires the Commission’s Office of Credit Ratings to conduct an examination of each NRSRO at least annually.⁶ Each examination must include a review of eight areas,⁷ including the management of conflicts of interest by the NRSROs.⁸

The purpose of NRSRO examinations is, generally, to “facilitate [NRSRO] compliance with applicable laws and rules, identify potential violations of such laws and rules, and monitor for remedial action.”⁹ During the examination process, the Staff generally maintains ongoing communication regarding its findings with each NRSRO, and at the end of the process, the Staff provides a letter to each NRSRO summarizing the Staff’s findings and recommendations. Such findings and recommendations are discussed with each NRSRO.

Potential violations of U.S. securities laws discovered in an NRSRO examination have to date been, and may in the future be, referred for potential enforcement action, in order to

⁵ See Pub. L. No. 111-203 § 939C(c).

⁶ Section 15E(p)(3)(A).

⁷ Section 15E(p)(3)(B)(i)–(viii).

⁸ Section 15E(p)(3)(B)(ii).

⁹ See 2012 Summary Report of Commission Staff’s Examinations of Each Nationally Recognized Statistical Rating Organization, Commission staff (Nov. 2012), at 3, available at <http://www.sec.gov/news/studies/2012/nrsro-summary-report-2012.pdf>.

investigate and take further action when appropriate, such as in a Federal court or an administrative action.¹⁰

The Commission is required under Section 15E(p)(3)(C) of the Exchange Act to make publicly available an annual report summarizing: (i) the essential findings of the NRSRO examinations as deemed appropriate by the Commission; (ii) responses by the NRSROs to any material regulatory deficiencies identified by the Commission under such findings; and (iii) whether the NRSROs have appropriately addressed the Commission's recommendations from previous annual examination reports.

Since the enactment of the Dodd-Frank Act, the Commission has issued two examination reports under Section 15E(p)(3)(C) (the "NRSRO Exam Reports") in September 2011, generally covering the period from December 1, 2009 through August 1, 2010 (the "2011 NRSRO Exam Report")¹¹ and in November 2012, generally covering the period from August 1, 2010 through September 30, 2011 (the "2012 NRSRO Exam Report").¹²

Essential findings relating to the NRSROs' management of conflicts of interest involving ancillary services appear in the NRSRO Exam Reports. Such findings are described in Section VIII.B of this report.

¹⁰ For example, in April 2012, the Commission instituted administrative proceedings against Egan-Jones Ratings Co. ("EJR") and Sean Egan, EJR's founder, President, owner, and primary analyst. In the Order Instituting Proceedings, the Commission alleged that EJR and Mr. Egan committed numerous violations of Sections 15E and 17(a) and the rules thereunder. On January 22, 2013, the Commission announced that EJR and Egan agreed, among other things, as part of a settlement of the administrative action brought by the Commission, to be barred for at least 18 months from rating asset-backed securities and government securities as an NRSRO. *See In the Matter of Egan-Jones Ratings Company and Sean Egan*, Release No. 66854 (April 24, 2012), *In the Matter of Egan-Jones Ratings Company and Sean Egan*, Release No. 68703 (January 22, 2013) and Commission press release at <http://www.sec.gov/news/press/2013/2013-7.htm>.

¹¹ See 2011 Summary Report of Commission Staff's Examinations of Each Nationally Recognized Statistical Rating Organization, Commission staff (Sep. 2011), available at http://www.sec.gov/news/studies/2011/2011_nrsro_section15e_examinations_summary_report.pdf.

¹² See 2012 Summary Report of Commission Staff's Examinations of Each Nationally Recognized Statistical Rating Organization, Commission staff.

II. Current NRSROs

As of the date of this report, ten credit rating agencies are registered as NRSROs: A.M. Best Company, Inc. (“A.M. Best”), DBRS, Inc. (“DBRS”), EJR, Fitch Ratings, Inc. (“Fitch Ratings”), HR Ratings de México, S.A. de C.V. (“HR Ratings”), Japan Credit Rating Agency, Ltd. (“JCR”), Kroll Bond Rating Agency, Inc. (“Kroll”), Moody’s Investors Service, Inc. (“Moody’s”), Morningstar Credit Ratings, LLC (“Morningstar”), and Standard & Poor’s Ratings Services (“S&P”). The following table identifies each such NRSRO, the classes of credit ratings in which it is currently registered, and the date of its initial registration:

NRSRO	Current Registered Classes of Credit Ratings	Initial Registration Date
A.M. Best	<ul style="list-style-type: none"> • Insurance companies • Corporate issuers • Issuers of asset-backed securities 	9/24/2007
DBRS	<ul style="list-style-type: none"> • Financial institutions • Insurance companies • Corporate issuers 	9/24/2007
	<ul style="list-style-type: none"> • Issuers of asset-backed securities • Issuers of government securities 	
EJR¹³	<ul style="list-style-type: none"> • Financial institutions • Insurance companies • Corporate issuers 	12/21/2007
Fitch Ratings	<ul style="list-style-type: none"> • Financial institutions • Insurance companies • Corporate issuers 	9/24/2007
	<ul style="list-style-type: none"> • Issuers of asset-backed securities • Issuers of government securities 	
HR Ratings	<ul style="list-style-type: none"> • Issuers of government securities 	11/5/2012
JCR	<ul style="list-style-type: none"> • Financial institutions • Insurance companies • Corporate issuers 	9/24/2007
	<ul style="list-style-type: none"> • Issuers of government securities 	
Kroll	<ul style="list-style-type: none"> • Financial institutions • Insurance companies • Corporate issuers 	2/11/2008
Moody’s	<ul style="list-style-type: none"> • Financial institutions • Insurance companies • Corporate issuers 	9/24/2007
	<ul style="list-style-type: none"> • Issuers of asset-backed securities • Issuers of government securities 	
Morningstar	<ul style="list-style-type: none"> • Issuers of asset-backed securities 	6/23/2008
S&P	<ul style="list-style-type: none"> • Financial institutions • Insurance companies • Corporate issuers 	9/24/2007
	<ul style="list-style-type: none"> • Issuers of asset-backed securities • Issuers of government securities 	

¹³ See *supra* note 10 for a description of an administrative action brought by the Commission against EJR and Sean Egan. Prior to January 22, 2013, EJR was registered as an NRSRO in the ratings categories of asset-backed securities and government securities.

III. Current U.S. Regulatory Framework

NRSROs are regulated by the Commission primarily pursuant to Section 15E, which was added to the Exchange Act by the Credit Rating Agency Reform Act of 2006 (the “CRARA”)¹⁴ and amended by the Dodd-Frank Act. The CRARA established Commission oversight over credit rating agencies that register with the Commission as NRSROs.¹⁵ In June 2007, the Commission adopted a series of rules implementing a registration and oversight program for credit rating agencies that register as NRSROs.¹⁶

Section 15E(h)(1) of the Exchange Act requires each NRSRO to establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of its and its affiliates’ business, to address and manage any conflicts of interest that can arise from such business. Section 15E(h)(2) requires the Commission to issue rules to prohibit or require the management and disclosure of such conflicts of interest. The Commission adopted Exchange Act Rule 17g-5 to implement Section 15E(h)(2).

Sections A through D below describe the Commission’s rules and statutory requirements relevant to the management of conflicts of interest involving ancillary services.

¹⁴ See Pub. L. No. 109-291, 120 Stat. 1327 (2006).

¹⁵ Prior to the enactment of rules in June 2007 to implement provisions of the CRARA, the process of identifying NRSROs had historically been undertaken by the Commission staff through the issuance of no-action letters where the staff had determined, among other things, that the credit rating agency was recognized nationally by the predominant users of credit ratings as issuing credible and reliable ratings. See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 34-55857 (Jun. 5, 2007), 72 FR 33564 (Jun. 18, 2007), available at <http://www.sec.gov/rules/final/2007/34-55857.pdf> (“2007 Adopting Release”).

¹⁶ See 2007 Adopting Release, 72 FR 33564. The Commission adopted rules that prescribe: how a credit rating agency must apply to the Commission for registration as an NRSRO (Rule 17g-1 (17 CFR 240.17g-1)); the form of the application and the information that must be provided in the application (Form NRSRO and the Instructions to Form NRSRO (17 CFR 240.249b.300)); the records an NRSRO must make and maintain (Rule 17g-2 (17 CFR 240.17g2)); the reports an NRSRO must furnish to the Commission annually (Rule 17g-3 (17 CFR 240.17g-3)); the areas that must be addressed in an NRSRO’s procedures to prevent the misuse of material nonpublic information (Rule 17g-4 (17 CFR 240.17g-4)); the types of conflicts of interest an NRSRO must disclose and manage or is prohibited from having (Rule 17g-5 (17 CFR 240.17g-5)); and certain unfair, coercive, or abusive practices an NRSRO is prohibited from engaging in (Rule 17g-6 (17 CFR 240.17g-6)).

A. Rule 17g-5(a) and Rule 17g-5(b) (Managed Conflicts of Interest)

Rule 17g-5(a) prohibits NRSROs from having a conflict of interest identified in Rule 17g-5(b)¹⁷, relating to the issuance or maintenance of a credit rating, unless it is disclosed in Exhibit 6 to Form NRSRO and the NRSRO has established, and maintains and enforces, policies and procedures to address and manage the conflict.¹⁸

Certain of the conflicts of interest listed in Rule 17g-5(b) relate to an NRSRO's provision of ancillary services. For example, Rule 17g-5(b)(3) identifies the following conflict of interest: "Being paid for services *in addition to* [italics added] determining credit ratings by issuers, underwriters, or obligors that have paid the [NRSRO] to determine a credit rating."¹⁹

Rule 17g-5(b)(4) identifies the following conflict of interest relating to services other than credit ratings which are paid for by subscribers: "Being paid by persons for subscriptions to receive or access the credit ratings of the [NRSRO] and/or for *other services offered by the [NRSRO]* [italics added] where such persons may use the credit ratings of the [NRSRO] to comply with, and obtain benefits or relief under, statutes and regulations using the term nationally recognized statistical rating organization."²⁰

¹⁷ The conflicts of interest listed in Rule 17g-5(b) include, without limitation, those relating to the payment for ratings or ratings subscriptions; relationships between persons within NRSROs and entities rated by the NRSROs; brokers or dealers associated with NRSROs; and asset-backed securities ratings paid for by issuers.

¹⁸ See 17 CFR 240.17g-5(a). Rule 17g-5(a)(3) contains additional requirements that apply to certain conflicts of interest relating to issuing or maintaining a credit rating for certain other securities, including those issued as part of an asset-backed securities transaction.

¹⁹ See 17 CFR 240.17g-5(b)(3).

²⁰ See 17 CFR 240.17g-5(b)(4). Rule 17g-5(b)(5) identifies an additional conflict of interest involving payment by persons for subscriptions to receive credit ratings and/or for "other services offered by the NRSRO." See 17 CFR 240.17g-5(b)(5).

In Exhibit 6 of their most recent Forms NRSRO, all of the NRSROs except for DBRS and HR Ratings identified the conflict referred to in Rule 17g-5(b)(3) and also disclosed in Exhibit 7 to Form NRSRO their policies and procedures addressing such conflict of interest.²¹

B. Rule 17g-5(c) (Prohibited Conflicts of Interest)

In contrast to Rule 17g-5(a), an NRSRO is absolutely prohibited from having the conflicts of interest listed in Rule 17g-5(c).²² Such conflicts include the conflict identified in Rule 17g-5(c)(5)²³: an NRSRO’s issuing or maintaining a credit rating as a credit rating agency “with respect to an obligor or security where the [NRSRO] or a person associated with the [NRSRO] made recommendations to the obligor or the issuer, underwriter, or sponsor of the security about the corporate or legal structure, assets, liabilities, or activities of the obligor or issuer of the security.”²⁴

The purpose of Rule 17g-5(c)(5) is to address the potential lack of impartiality that could arise when an NRSRO determines a credit rating based on a corporate structure that was developed after consultations with the NRSRO or its affiliates on how to achieve a desired credit rating. “In simple terms,” the Commission has explained, “the rule prohibits an NRSRO from rating its own work or the work of an affiliate.”²⁵

²¹ EJR also disclosed in such exhibits the conflicts of interest referred to in Rules 17g-5(b)(4) and 17g-5(b)(5). See Exhibits 6 and 7 to Form NRSRO for all currently registered NRSROs, and Section III.D of this report for a description of Exhibits 6 and 7 to Form NRSRO.

²² 17 CFR 240.17g-5(c).

²³ Other prohibited conflicts of interest referred to in Rule 17g-5(c) include, without limitation, an NRSRO’s issuing or maintaining a credit rating where the person soliciting the rating provided the NRSRO with 10% of more of the NRSRO’s total net revenue; the NRSRO or credit analyst having an ownership interest in the rated entity; the rated entity being a person associated with the NRSRO; the NRSRO or a credit analyst being an officer or director of the rated entity; the fee paid for the rating having been negotiated, discussed or arranged by persons within the NRSRO responsible for credit ratings; and the credit analyst involved with the rating having received gifts from the rated entity. See 17 CFR 240.17g-5(c).

²⁴ See 17 CFR 240.17g-5(c)(5).

²⁵ Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 34-59342 (Feb. 2, 2009), 74 FR 6456, at 6466 (Feb. 9, 2009), available at <http://www.sec.gov/rules/final/2009/34-59342.pdf>.

The Commission has noted that the rule would be violated if the feedback process turns into recommendations by the NRSRO about changes to the structure, assets, liabilities or activities of the obligor or security that the person seeking the rating potentially could make to obtain a desired credit rating.²⁶

Another conflict of interest prohibited by Rule 17g-5(c) that could apply to an NRSRO's provision of ancillary services is Rule 17g-5(c)(1), which prohibits an NRSRO from issuing or maintaining a credit rating as a credit rating agency solicited by a person that provided the NRSRO with net revenue²⁷ equal to or exceeding 10% of the total net revenue of the NRSRO for the most recently ended fiscal year.

C. Rule 17g-6 (Prohibited Acts and Practices)

Rule 17g-6 prohibits an NRSRO from engaging in any of the following unfair, coercive, or abusive practices:²⁸

(1) Conditioning or threatening to condition the issuance of a credit rating on the purchase by an obligor or issuer, or an affiliate of the obligor or issuer, of any other services or products, including pre-credit rating assessment products, of the [NRSRO] or any person associated with the [NRSRO].

²⁶ Id. at 6466.

²⁷ See 17 CFR 240.17g-5(c)(1). Net revenue means “revenue earned by the applicant or NRSRO for any type of service or product, regardless of whether related to credit rating services, and net of any rebates and allowances paid or owed to the person by the applicant or NRSRO.” See 2007 Adopting Release, 72 FR at 33580.

²⁸ See 17 CFR 240.17g-6. Rule 17g-6(a)(4) also prohibits the following practice: Issuing or threatening to issue a lower credit rating, lowering or threatening to lower an existing credit rating, refusing to issue a credit rating, or withdrawing or threatening to withdraw a credit rating, with respect to securities or money market instruments issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction, unless all or a portion of the assets within such pool or part of such transaction also are rated by the NRSRO, where such practice is engaged in by the nationally recognized statistical rating organization for an anticompetitive purpose.

(2) Issuing, or offering or threatening to issue, a credit rating that is not determined in accordance with the [NRSRO's] established procedures and methodologies for determining credit ratings, based on whether the rated person, or an affiliate of the rated person, purchases or will purchase the credit rating or any other service or product of the [NRSRO] or any person associated with the [NRSRO].

(3) Modifying, or offering or threatening to modify, a credit rating in a manner that is contrary to the [NRSRO's] established procedures and methodologies for modifying credit ratings based on whether the rated person, or an affiliate of the rated person, purchases or will purchase the credit rating or any other service or product of the [NRSRO] or any person associated with the [NRSRO].

D. Reporting Requirements

i. Form NRSRO

Section 15E(b)(2) of the Exchange Act requires each NRSRO to file with the Commission annually an amendment to its registration certifying that certain information and documents in its application for registration continue to be accurate and to list any material changes that occurred to the information or documents during the previous calendar year. Paragraph (a) of Rule 17g-1 requires that the initial application for registration be furnished to the Commission on Form NRSRO and paragraph (f) of Rule 17g-1 requires that the annual certification be furnished to the Commission on Form NRSRO. NRSROs are required to make publicly available Exhibits 1 through 9 of Form NRSRO.²⁹ Exhibits 10 through 13 and the financial reports under Rule 17g-3 are not required to be made publicly available.

Exhibit 4 to Form NRSRO requires an NRSRO to provide the Commission and make public information regarding the organizational structure of the NRSRO, including an organizational

²⁹ See Section 15E(a)(3) and paragraph (i) of Rule 17g-1.

chart showing the divisions, departments, and business units of the NRSRO.³⁰ Such information is intended to assist credit ratings users and the Commission in understanding where potential conflicts of interest relating to ancillary business activities might arise.³¹

Exhibit 6 to Form NRSRO requires an NRSRO to identify the types of conflicts of interest relating to the issuance of credit ratings that are material to the NRSRO. Exhibit 7 to Form NRSRO requires an NRSRO to provide its written policies and procedures that address and manage conflicts of interest, except for information that is proprietary or would diminish the effectiveness of a specific policy or procedure if made publicly available.³²

Rule 17g-3(a)(3) requires an NRSRO to provide the Commission on an annual basis with unaudited information as to the amount of revenue generated from certain enumerated services and products, including revenue from determining and maintaining credit ratings (Rule 17g-3(a)(3)(i)), revenue from subscribers (Rule 17g-3(a)(3)(ii)), revenue from granting licenses or rights to publish credit ratings (Rule 17g-3(a)(3)(iii)), and revenue from “all other services and products” (Rule 17g-3(a)(3)(iv)). The NRSRO must include descriptions of any major sources of the revenue from “other services and products.”³³

ii. Rule 17g-2(a)(5)

Rule 17g-2(a)(5) requires an NRSRO to make and retain a record listing the general types of services and products it offers. Such record is intended to provide the Commission with details of the ancillary business activities of the NRSRO, to be useful in identifying potential conflicts of interest that arise from such activities and to enable Commission examiners to review whether the NRSRO has implemented procedures to manage such potential conflicts.³⁴

³⁰ See Exhibit 4 to Form NRSRO and Instructions to Exhibit 4.

³¹ See 2007 Adopting Release, 72 FR at 33576.

³² See Exhibits 6 and 7 to Form NRSRO and the Instructions to Form NRSRO.

³³ See Rule 17g-3(a)(3).

³⁴ See 2007 Adopting Release, 72 FR at 33585.

IV. Applicable Proposed NRSRO Rules

The Commission proposed certain NRSRO rules in May 2011 relevant to ancillary services and conflicts of interest.³⁵ Proposed Rule 17g-7(a)(1)(ii)(J) would require an NRSRO to provide an information disclosure form when taking a rating action, which form would include information relating to conflicts of interest of the NRSRO, including a classification of the relevant rating as either “solicited sell-side,” “solicited buy-side,” or “unsolicited” and, if the credit rating was solicited, a disclosure of whether the NRSRO provided services other than determining credit ratings to the person that paid for the rating during the most recently ended fiscal year.³⁶

Proposed Rule 17g-7(a)(1)(iii) would require such disclosure form to be accompanied by an attestation, by a person within the NRSRO responsible for the rating action, to the effect that (i) no part of the credit rating was influenced by any other business activities; (ii) the credit rating was based solely upon the merits of the obligor, security or money market instrument being rated; and (iii) the credit rating was an independent evaluation of the risks and merits of the obligor, security or money market instrument being rated.³⁷

In addition, a new prohibited conflict of interest is proposed to be added to Rule 17g-5, which would prohibit an NRSRO from issuing or maintaining a credit rating where a person within the NRSRO who participates in sales and marketing of a product or service of the NRSRO (or a product or service of a person associated with the NRSRO) also participates in determining or monitoring the credit rating, or developing or approving procedures or methodologies used to determine the credit rating.³⁸

³⁵ See Proposed Rules for Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 34-64514 (May 18, 2011), 76 FR 33420 (Jun. 8, 2011), available at <http://www.sec.gov/rules/proposed/2011/34-64514.pdf>.

³⁶ Id. at 33461-33462.

³⁷ Id. at 33465.

³⁸ Id. at 33513-14.

Commission staff continues to consider the comments received on these proposals as it formulates its final recommendations to the Commission.

V. IOSCO Code of Conduct and European Union Credit Rating Agency Regulations

A detailed survey of non-U.S. regulations relating to conflicts of interest involving ancillary services is beyond the scope of this report. However, described briefly below are a code of conduct published by an international organization of securities regulators, as well as certain pertinent European Union (“EU”) regulations which apply to several of the NRSROs and which are relevant to issues relating to conflicts of interest in keeping with the scope of this report.

A. IOSCO Code of Conduct

Section 939C requires that a study of the independence of NRSROs and how it affects the ratings issued by NRSROs be included in this report. In this regard, the International Organization of Securities Commissions (“IOSCO”) Code specifically addresses the issue of rating agency independence in the context of the avoidance of conflicts of interest relating to ancillary business.

IOSCO published the “Code of Conduct Fundamentals for Credit Rating Agencies” in December 2004,³⁹ which was revised in May 2008⁴⁰ (the “IOSCO Code”).⁴¹ The IOSCO Code was intended to serve as a guide to, and framework for, implementing the objectives of certain

³⁹ See Code of Conduct Fundamentals for Credit Rating Agencies, The Technical Committee of the International Organization of Securities Commissions (Dec. 2004), available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD180.pdf>.

⁴⁰ See Code of Conduct Fundamentals for Credit Rating Agencies, The Technical Committee of the International Organization of Securities Commissions (Revised May 2008), available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD271.pdf>.

⁴¹ IOSCO, established in 1983, is an international body of over 120 securities regulators, including the Commission, and 80 securities markets participants. See <http://www.iosco.org/>.

principles regarding the activities of credit rating agencies which IOSCO published in September 2003.⁴²

Section 2.5 of the IOSCO Code provides as follows:

A [credit rating agency] should separate, operationally and legally, its credit rating business and [credit rating agency] analysts from any other businesses of the [credit rating agency], including consulting businesses, that may present a conflict of interest. A [credit rating agency] should ensure that ancillary business operations which do not necessarily present conflicts of interest with the [credit rating agency's] rating business have in place procedures and mechanisms designed to minimize the likelihood that conflicts of interest will arise. A [credit rating agency] should also define what it considers, and does not consider, to be an ancillary business and why.⁴³

With the exception of EJR, the code of conduct for each NRSRO describes the extent to which it is based on, or consistent with, the IOSCO Code.⁴⁴ The specific language incorporating Section 2.5 of the IOSCO Code into the codes of conduct for the NRSROs vary among the NRSROs.

B. European Union Credit Rating Agency Regulations

The credit rating agency regulations of the EU provide that credit rating agencies “should be able to provide ancillary services where this does not create potential conflicts of interest with

⁴² See IOSCO Statement of Principles Regarding the Activities of Credit Rating Agencies, A Statement of the Technical Committee of the International Organization of Securities Commissions (25 September 2003), available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD151.pdf>.

⁴³ Code of Conduct Fundamentals for Credit Rating Agencies, The Technical Committee of the International Organization of Securities Commissions. A report prepared by The Committee of European Securities Regulators (the predecessor of the European Securities and Markets Authority or “ESMA”) dated December 2006, stated that ancillary services was one of the two areas where credit rating agencies did not comply with the IOSCO Code. See CESR’s Report to the European Commission on the compliance of credit rating agencies with the IOSCO Code, (Dec. 2006), paragraph 42, at 76, available at http://www.esma.europa.eu/pl/system/files/06_545.pdf.

⁴⁴ See Exhibit 5 to Form NRSRO for all NRSROs.

the issuing of credit ratings.”⁴⁵ The regulations define ancillary services as “services other than issue [sic] of credit ratings” that are “not part of credit rating activities; they comprise market forecasts, estimates of economic trends, pricing analysis and other general data analysis as well as related distribution services.”⁴⁶

Pursuant to such regulations, a credit rating agency must disclose in its final ratings reports any ancillary services provided for the rated entity or any related third party.⁴⁷ It must also generally disclose a list of its ancillary services and annually report revenue information including fees from non-credit rating activities, with a comprehensive description thereof.⁴⁸ Credit rating agencies are prohibited from providing consultancy or advisory services to the rated entity or a related third party regarding the corporate or legal structure, assets, liabilities or activities of that rated entity or related third party.⁴⁹

Pursuant to an EU regulation adopted in March 2012, which is currently in effect, credit rating agencies are required to provide information regarding ancillary services such as a description of resources shared by rating and ancillary services and of arrangements to prevent, disclose and mitigate conflicts of interest between the rating business and ancillary services, as well as the results of internal assessments identifying existing or potential conflicts of interest between the rating business and ancillary services.⁵⁰

⁴⁵ See Regulation (EC) No. 1060/2009 of the European Parliament and of the Council of 16 September 2009 on Credit Rating Agencies, Official Journal L. 302, November 17, 2009, at 3, available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:302:0001:0031:EN:PDF>.

⁴⁶ See Regulation (EC) No. 1060/2009 of the European Parliament and of the Council of 16 September 2009 on Credit Rating Agencies at Art. 6, Point 2 and L 302/25, Annex I, Sec. B, Point 4.

⁴⁷ See id. at Annex I, Sec. B, Point 4.

⁴⁸ See id. at Sec. E I-2 and III-7.

⁴⁹ See id. at Annex I, Sec. B, Point 4.

⁵⁰ See Commission Delegated Regulation (EU) 449/2012 of 21 March 2012 Supplementing Regulation (EC) No 1060/2009 Of The European Parliament And Of The Council With Regard To Regulatory Technical Standards On Information For Registration And Certification Of Credit Rating Agencies, Official Journal L. 140, May 30, 2012, at Article 22 and Article 26(2)(a), available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:140:0032:0052:EN:PDF>.

Part Two

VI. Overview of NRSRO Ancillary Services and Potential Conflicts of Interest Involved

A. Ancillary Services Definition Used in this Report

Solely for purposes of this report, the Staff has created a definition termed “Ancillary Services.” Although “Ancillary Services” is not defined in Section 15E or currently in the rules thereunder, such term is being used in this report to mean all products and services provided by NRSROs *other than* the issuance of credit ratings. Such term would include, without limitation, “other services, such as risk management advisory services, ancillary assistance and consulting services,” as mentioned in Section 939C.

As used in this report, “Ancillary Services” includes credit or rating evaluation services, credit or rating assessment services and indicative or impact assessment services (as further described in Section VII of this report), notwithstanding that (i) some NRSROs consider such services instead to be core ratings services and (ii) most of the NRSROs do not use the term “ancillary services” in the description of the non-ratings products and services they provide. The foregoing “Ancillary Services” definition does not reflect any position of the Staff regarding the types of products and services that are appropriately considered to constitute “Ancillary Services” and the creation of such definition should not be construed to indicate the potential for any future rulemaking or guidance in respect of such defined term.

Section VII of this report describes in greater detail the Ancillary Services provided by NRSROs, as well as the range of terms and categories used by NRSROs to describe Ancillary Services.

B. Ancillary Services Provided by NRSROs

Currently, one NRSRO's⁵¹ website indicates that it does not provide products and services in addition to credit ratings. Another NRSRO's⁵² website indicates that the NRSRO performs certain servicer evaluations, but it is unclear whether they are considered by the NRSRO to be Ancillary Services. Six of the NRSROs⁵³ provide products and services which they differentiate from credit ratings. Two of the NRSROs⁵⁴ provide Ancillary Services, but consider them to be core rating services. Some of the NRSROs provide such products and services through business lines, segments, groups or divisions within the NRSROs which are different from those providing credit ratings.⁵⁵ Other NRSROs have affiliated companies or other businesses, not part of the NRSROs, that offer products and services related to credit rating services.⁵⁶ Five of the NRSROs state in their policies that they do not provide consulting or advisory services.⁵⁷

The way in which the NRSROs define and categorize their products and services varies greatly. Only two of the NRSROs use and define the term “ancillary” to describe products and services they offer other than the issuance of credit ratings.⁵⁸ Of the NRSROs providing rating assessment services and rating evaluation services, or similarly termed services (as further described in Section VII of this report), some categorize such services as part of the core ratings

⁵¹ HR Ratings.

⁵² Kroll.

⁵³ A.M. Best, EJR, JCR, Moody's, Morningstar and S&P.

⁵⁴ For example, DBRS and Fitch Ratings provide impact assessments and rating assessments, respectively.

⁵⁵ A.M. Best, EJR and Morningstar.

⁵⁶ Examples are Fitch Ratings and Fitch Solutions, Moody's and Moody's Analytics, and S&P and S&P Capital IQ. For further descriptions, see Sections VII.D.i, VII.H.i. and VII.J.i, respectively, of this report.

⁵⁷ These NRSROs include A.M. Best, DBRS, Fitch Ratings, JCR and Moody's.

⁵⁸ JCR and S&P.

business and others categorize them differently, as “other services,” “ancillary services” or “other permissible services.”⁵⁹

As indicated in Sections III and V of this report, the statutory references to Ancillary Services also vary; using phrases such as services “other than the issuance of credit ratings” and “not involving the determination of credit ratings.” The variations in terminology used in the relevant statutes and by the NRSROs create difficulty in comparing revenue and other Ancillary Services information among the NRSROs and assessing the adequacy of policies and procedures which are intended to address the potential conflicts of interest involving Ancillary Services.

As mentioned in Section III.A, all but two of the NRSROs⁶⁰ disclose on Exhibit 6 of their Forms NRSRO the conflict of interest referred to in Rule 17g-5(b)(3) and, in Exhibit 7, their policies and procedures to manage such conflict of interest. Section VII of this report describes the products and services provided by each NRSRO, as well as the relevant policies and procedures disclosed publicly by the NRSROs to manage conflicts of interest relating to Ancillary Services. Section VIII of this report describes certain actions taken by NRSROs to enforce such policies, as well as relevant essential findings from the NRSRO Exam Reports.

As mentioned above, ancillary services are in some cases provided by the NRSRO, a *non-NRSRO* affiliate of the NRSRO, or in other cases, by both the NRSRO and a non-NRSRO affiliate. While this mix of delivery models reflects the state of the industry, the applicable rules under Section 15E impose requirements (for example, requirements relating to the maintenance of certain policies and procedures, management of conflicts of interest, establishment of internal supervisory controls and processing of complaints) on--and Section 15E contemplates Commission oversight and examination of--*the NRSROs themselves* including their credit rating affiliates as listed on Form NRSRO. Thus, the Staff’s ability under current Commission rules directly to obtain information regarding, and to examine, the effectiveness of policies and

⁵⁹ Such services are categorized as follows: A.M. Best – ratings services; DBRS – core services; Fitch Ratings – core services; JCR – ancillary services; Moody’s – other permissible services.

⁶⁰ HR Ratings and DBRS. In addition, EJR also discloses in such exhibits the conflict of interest described in Rule 17g-5(b)(4).

procedures could be affected by the choice of a non-NRSRO affiliate to provide such Ancillary Services.

C. Potential Conflicts of Interest Involving Ancillary Services

The independence of rating agencies and the integrity of the rating process can be compromised by potential conflicts of interest, such as those regarding Ancillary Services. Conflicts of interest involving Ancillary Services have been the subject of several reports, including a Commission report published in June 2003 entitled “Report on the Role and Function of Credit Rating Agencies in the Operation of the Securities Market” (the “2003 Report”).⁶¹

One of the matters addressed by the 2003 Report was whether rating agencies should implement procedures to manage potential conflicts of interest that arise when rating agencies develop ancillary fee-based businesses. The 2003 Report, which pre-dated the CRARA and the Dodd-Frank Act, concluded that the Commission would explore whether NRSROs should implement such procedures.⁶²

The 2003 Report expressed a concern about the impact on rating decisions by an issuer’s decision to purchase additional services offered by the rating agency.⁶³ For example, an NRSRO

⁶¹ See Report on the Role and Function of Credit Rating Agencies in the Operation of the Securities Markets, Commission staff (Jan. 2003), available at <http://www.sec.gov/news/studies/credratingreport0103.pdf>. See also, CESR’s Second Report To The European Commission On The Compliance Of Credit Rating Agencies With The IOSCO Code And The Role Of Credit Rating Agencies In Structured Finance (May 2008), at 34-35, available at http://www.esma.europa.eu/system/files/CESR_08_277.pdf. The issuance of the 2003 Report was required by the Sarbanes-Oxley Act of 2002 (“Sarbanes-Oxley”). See Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002).

⁶² In the 2007 Adopting Release, the Commission indicated that several of the rules (i.e. Rules 17g-5 and 17g-6) were being adopted partially in response to the issues raised in the 2003 Report. See 2007 Adopting Release, 72 FR at 33596-33600. Pursuant to Section 15E(h) of the CRARA, Congress gave the Commission the authority (and required the Commission) to issue final rules to prohibit, or require the management and disclosure of, any conflicts of interest relating to the issuance of credit ratings by a NRSRO, including, without limitation, conflicts of interest relating to the provision of consulting, advisory, or other services by a NRSRO to the obligor. See Section 15E(h)(2)(B).

⁶³ See Report on the Role and Function of Credit Rating Agencies in the Operation of the Securities Markets, Commission staff at 42.

might issue a more favorable than warranted credit rating to an issuer or other party in order to obtain ancillary services business from them, or an issuer that purchases a large amount of ancillary services could pressure the NRSRO to issue a more favorable than warranted rating on that issuer.

The 2003 Report stated that, “whether or not the purchase of ancillary services actually impacts the credit rating decision, issuers may be pressured into using them out of fear that their failure to do so could adversely impact their credit rating (or, conversely, with the expectation that purchasing these services could help their credit rating).”⁶⁴ The 2003 Report also mentioned that, in the case of ratings assessment services, to the extent a rating agency has already “promised” a certain rating in an issuer’s hypothetical scenario, “pressure to match the actual rating to the promised rating is likely to be forceful, even if the ultimate analysis otherwise might not have supported the rating.”⁶⁵

The 2003 Report also noted that ratings analysts also perform certain ancillary services.⁶⁶ In the case of an ancillary service for an issuer that directly relates to its rating, it could be beneficial to have the same analyst perform both services due to the analyst’s familiarity with the issuer. However, the analyst’s performance of the ancillary service could also pose a potential conflict of interest given the analyst’s proximity to the rating process and familiarity with the Ancillary Service being requested.

Another concern expressed with respect to Ancillary Services is that they could involve an NRSRO making recommendations on the structure of a security to be rated—i.e. that rating agencies engaging in pre-rating dialogues with issuers may be unable to neutrally issue a credit rating because the rating agencies have become “creators of the instruments themselves.”⁶⁷

⁶⁴ Id. at 43.

⁶⁵ Id. at 43.

⁶⁶ Id. at n.118.

⁶⁷ Andrew D. Hatchett, SOX It to ‘Em: Using Sarbanes-Oxley as a Model for Regulating Conflicts of Interest in the Credit Rating Industry, 63 Ala. L. Rev, 414 (2012).

Such concern about deal structuring was echoed in a final report issued by the Technical Committee of IOSCO in May 2008 entitled “The Role of Credit Rating Agencies in Structured Finance Markets,” as follows:

An additional concern is that [credit rating agencies] are doing more than rating structured finance securities, namely: advising issuers on how to design the trust structures. In the corporate area, [credit rating agencies] will provide a ‘private rating’ based on a pro forma credit assessment of the impact of a potential transaction (e.g. merger, asset purchase) on the company’s credit rating...The serious question that has arisen is whether the current process for rating structured finance involves advice that is, in fact, an ancillary business operation which necessarily presents a conflict of interest. Conversely, while some observers believe that the structured finance rating process does not necessarily pose an inherent conflict of interest vis-à-vis the [credit rating agency’s] business more generally, the further question is whether a [credit rating agency] has sufficient controls in place to minimize the likelihood that conflicts of interest will arise.⁶⁸

As indicated above, the potential conflicts of interest may apply to some types of Ancillary Services and not others. For example, certain of the NRSROs provide ratings or similar evaluations through their affiliates based on market indicia, which are distinct from traditional credit ratings issued by the NRSROs.⁶⁹ While the concerns expressed above may also apply to the provision of such market-implied ratings or evaluations, it is also important that the NRSROs clearly describe the differences in methodologies and procedures used for such ratings or evaluations, and traditional credit ratings, and the extent to which market-based indicia may be used (if at all) in traditional ratings criteria.

⁶⁸ The Role of Credit Rating Agencies in Structured Finance Markets, The Technical Committee of the International Organization of Securities Commissions (May 2008), available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD270.pdf>.

⁶⁹ Fitch Solutions, Moody’s Analytics and S&P Capital IQ provide such type of service. For example, Fitch Solutions uses daily credit default swap market quotes to derive implied ratings, which it views as a complement to fundamental ratings analysis, an indicator of credit quality at short-and medium-term horizons and an early warning of credit events. See http://www.fitchratings.com/web_content/product/Market_Implied_Ratings.pdf. Traditional ratings are typically based on a wider range of inputs and take a longer term perspective. See also <http://www.moodysanalytics.com/Products-and-Solutions/Credit-Research-Risk-Measurement/Quantitative-Insight/Market-Implied-Ratings.aspx>; and http://www.insightforenterprise.com/images/_slinks/ES%20Credit%20Risk%20Indicators.pdf; and Sections VII.D, VII.H and VII.J of this report for further descriptions of this service.

As described in Section III of this report, Commission rules with respect to the potential conflicts of interest involving Ancillary Services discussed above (i) require NRSROs to disclose such conflicts of interest on Form NRSRO and have and enforce written policies and procedures to address and manage such conflicts of interest (see Section III.A above); (ii) prohibit NRSROs from making recommendations to an issuer about the structure of a rated security (see Section III.B above); (iii) prohibit NRSROs from engaging in certain acts and practices involving Ancillary Services (see Section III.C above); and (iv) require the reporting of certain information concerning Ancillary Services (see Section III.D above).

The Staff's recommendations and conclusions regarding the management of conflicts of interest associated with Ancillary Services are included in Section X of this report.

VII. Description of NRSRO Ancillary Services and Policies and Procedures to Manage Potential Conflicts of Interest

Below is a general description of the types of Ancillary Services offered by NRSROs, as well as examples of the policies and procedures they have disclosed publicly pursuant to Rule 17g-5(a) (as referred to in Section III.A of this report) to manage conflicts of interest relating to such Ancillary Services. The Staff received responses from the NRSROs to requests for information relating to this Study, including descriptions of their products and services and applicable policies and procedures. For purposes of this report, the Staff considered such responses and reviewed, as of March 31, 2013 (except as otherwise expressly noted), publicly available information for all the NRSROs, as well as certain non-public information as specifically indicated, all of which is subject to change. Although some NRSROs have internal, non-public policies and procedures applicable to Ancillary Services in addition to those publicly disclosed, such internal policies and procedures are not described below.

The types of policies and procedures referred to below generally include separation of ratings and ancillary businesses, separation of analytics from commercial activities, restrictions on information sharing, specification of factors used to determine ratings, prohibitions on consulting and advisory services and prohibitions on deal structuring. Reference is made to the websites of

the various NRSROs (which are listed in footnotes at the beginning of the sections below) for a more complete description of the relevant products and services and policies and procedures.

A. A.M. Best⁷⁰

i. Products and Services

According to its website, A.M. Best's rating services include--in addition to its financial strength ratings, issuer credit ratings and debt ratings⁷¹--an interactive credit rating service,⁷² a rating assessment service⁷³ and a rating evaluation service.⁷⁴ A.M. Best states that it does not provide consulting or advisory services.⁷⁵

According to its Confidentiality, Firewall, Conflicts of Interest, and Securities Trading and Reporting Policy (the "Firewall Policy"), A.M. Best also provides communications, news and information services through different divisions ("non-ratings divisions") within the NRSRO.⁷⁶

⁷⁰ See <http://www.ambest.com/>.

⁷¹ See <http://www3.ambest.com/ratings/default.asp>.

⁷² See A.M. Best Rating Service Definitions, available at <http://www.ambest.com/ratings/definitions.html>. A.M. Best describes its interactive credit rating service as a "rating evaluation service solicited by the entity or issuer being rated" and that provides an opinion "regarding the creditworthiness of the entity, issuer or debt obligation."

⁷³ See id. A.M. Best describes its rating assessment service to be "solicited by non-rated entities" and as providing "a confidential, unpublished, unmonitored point-in-time opinion of a company's rating prospects based on a quantitative analysis of a company's financial statements and other related financial information communicated by the client to A.M. Best."

⁷⁴ See id. A.M. Best describes its rating evaluation service to be "solicited by currently rated entities" and as providing "a confidential, unpublished, unmonitored point-in-time opinion(s) of the impact of one or more hypothetical scenarios based on an interactive quantitative and qualitative analysis of the information, including financial projections and other related financial information on a company's creditworthiness, communicated by the client to A.M. Best."

⁷⁵ See A.M. Best Code of Conduct (Dec. 28, 2012), at 12, available at <http://www.ambest.com/nrsro/code.pdf>.

⁷⁶ See A.M. Best Confidentiality, Firewall, Conflicts of Interest, and Securities Trading and Reporting Policy (Dec. 28, 2012), at 6, available at http://www.ambest.com/nrsro/Confidentialityfirewallconflictsofinterestandsecuriestradingandreportpolicy_c-5.pdf.

These types of services include, but are not limited to, publications entitled “Best’s Insurance Reports” and “Best’s Directories of Recommended Insurance Attorneys and Adjusters.”⁷⁷

ii. Policies and Procedures

A.M. Best’s Firewall Policy relates to the protection of the ratings division and non-ratings divisions from any “improper influence” by one another or by any of the divisions’ clients, and restrictions on the sharing of confidential information within A.M. Best.⁷⁸ The Firewall Policy also prohibits ratings analysts from making proposals or recommendations regarding the design of structured finance products.⁷⁹ It also prohibits actions which would violate Rule 17g-6⁸⁰ as well as the provision of consulting or advisory services regarding the corporate or legal structure, assets, liabilities or activities of rated entities.⁸¹

A.M. Best also has a Code of Conduct, which relates to the quality and integrity of the rating process and the avoidance of conflicts of interest.⁸²

B. DBRS⁸³

i. Products and Services

The DBRS Core, Ancillary and Consulting Services Policy⁸⁴ (the “Services Policy”) states that DBRS does not presently provide ancillary services, which it defines as rating-related

⁷⁷ See A.M. Best Products and Services, available at <http://www.ambest.com/sales/default.asp>.

⁷⁸ See A.M. Best Confidentiality, Firewall, Conflicts of Interest, and Securities Trading and Reporting Policy at 6.

⁷⁹ Id. at 9.

⁸⁰ Id. at 20.

⁸¹ Id. at 9.

⁸² See A.M. Best Code of Conduct.

⁸³ See <http://www.dbrs.com/>.

services which may include risk management services, credit risk solutions, and indices.⁸⁵ Such policy also states that DBRS does not engage in consulting or advisory services.⁸⁶

The DBRS Services Policy states that DBRS performs a variety of core rating services and activities, including the issuance of public and private ratings, servicer and collateral manager evaluations, analytics on ratings under different stress scenarios, and subscription services.⁸⁷

ii. Policies and Procedures

In its Policies and Procedures to Address and Manage Conflicts of Interest, DBRS describes the manner in which it protects the independence of its ratings from conflicts of interest and how it manages potential conflicts of interest, including policies to ensure that ratings are influenced only by factors relevant to credit assessments.⁸⁸

DBRS also has a Code of Conduct, which relates to the quality and integrity of the rating process and avoidance of conflicts of interest.⁸⁹ The Code of Conduct prohibits analytical personnel from making proposals or recommendations regarding the design of structured finance products that DBRS rates.⁹⁰

⁸⁴ See DBRS Core, Ancillary and Consulting Services Policy, available at <http://www.dbrs.com/research/236733>.

⁸⁵ Id. at 2.

⁸⁶ Id. at 2.

⁸⁷ Id. at 1.

⁸⁸ See DBRS Policies and Procedures to Address and Manage Conflicts Of Interest, Exhibit 7 to Form NRSRO available at <http://www.dbrs.com/about/regulatoryAffairs/nrsrodisclosures>.

⁸⁹ See DBRS Code of Ethics, Exhibit 5 to Form NRSRO, available at <http://www.dbrs.com/about/regulatoryAffairs/nrsrodisclosures>.

⁹⁰ Id.

C. EJR⁹¹

i. Products and Services

EJR provides credit ratings and rating analysis reports to customers on a subscription basis.⁹² It also provides a distinct service involving proxy research, voting recommendations and voting services to a variety of institutional investors through Egan-Jones Proxy Services,⁹³ a different business line within the NRSRO.⁹⁴ Some of such investors are also ratings subscribers.⁹⁵ EJER also offers a premium service to its subscribers known as “Best Credit Ideas.”⁹⁶

ii. Policies and Procedures

In Exhibits 6 and 7 to its most recent Form NRSRO, EJER discloses several types of conflicts of interest, which include the provision of proxy research and voting services, and states in these exhibits that the proxy business line is physically and electronically separate from the ratings services.⁹⁷

EJR has a Code of Ethics and Business Conduct which prohibits the issuance or maintenance of a rating for a company “where the Firm or an associated person made recommendations to the obligor, issuer, underwriter or sponsor about the corporate or legal structure, assets, liabilities, or

⁹¹ See <http://www.egan-jones.com/>.

⁹² Id.

⁹³ See <http://www.ejproxy.com/>.

⁹⁴ See EJER Form NRSRO Exhibits 6 and 7, at 46, available at <http://www.egan-jones.com/nrsro>.

⁹⁵ Id.

⁹⁶ Id.

⁹⁷ Id. at 47.

activities of the issuer or obligor.”⁹⁸ The Code also includes, among other things, information on additional prohibited practices, conflicts of interest and confidential information.⁹⁹

D. Fitch Ratings¹⁰⁰

i. Products and Services

According to its Statement on Definition of Ancillary Businesses, Fitch Ratings provides “core” products and services including public and private ratings, credit assessments, the issuance of preliminary or indicative ratings and rating assessments.¹⁰¹ Fitch Ratings defines ancillary business as “any business other than the provision of independent analysis and rating opinions regarding a variety of risks in the financial markets.” Such statement mentions that “any ancillary business within the Fitch group of companies is provided by separate companies outside the ratings group or by separate divisions”¹⁰² and that Fitch Ratings does not provide advisory or consulting services.¹⁰³

Fitch Solutions, a non-NRSRO affiliate of Fitch Ratings and subsidiary of Fitch Group, Inc., the parent entity of Fitch Ratings, distributes Fitch Ratings research and ratings, financial data and other market-based content products.¹⁰⁴ Fitch Solutions provides market-implied ratings, which include credit default swap (“CDS”) implied ratings and equity implied ratings. For

⁹⁸ See EJR Form NRSRO, Exhibit 5, at 35, [available at http://www.egan-jones.com/nrsro](http://www.egan-jones.com/nrsro).

⁹⁹ Id.

¹⁰⁰ See <http://www.fitchratings.com/web/en/dynamic/fitch-home.jsp>.

¹⁰¹ See Fitch Ratings Statement on Definition of Ancillary Business (Aug. 2010), at 1, [available at http://www.fitchratings.com/web_content/credit_policy/statement_on_definition_of_ancillary_business.pdf](http://www.fitchratings.com/web_content/credit_policy/statement_on_definition_of_ancillary_business.pdf).

¹⁰² Id. at 1.

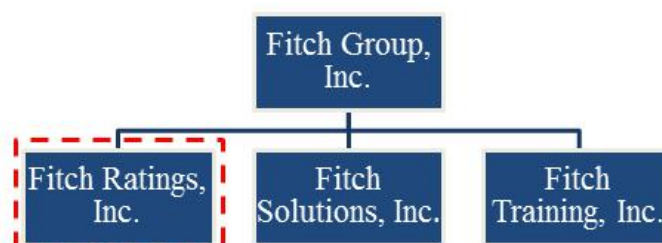
¹⁰³ Id.

¹⁰⁴ See descriptions at <http://www.fitchratings.com/jsp/corporate/ProductsAndServices.faces?context=2&detail=130>.

example, the CDS-implied rating model uses daily CDS market quotes to derive implied ratings.¹⁰⁵ Fitch Training, also a non-NRSRO affiliate of Fitch Ratings, is a training firm focused on the provision of credit and corporate finance training.¹⁰⁶

Below is an organizational chart derived from the Fitch Ratings Form NRSRO dated March 27, 2013, which illustrates the structure of Fitch Ratings, Fitch Solutions and Fitch Training:

Table 1: Fitch Group, Inc. organizational structure



Source: Fitch Ratings Form NRSRO, dated March 27, 2013 - Exhibit 4

--- Indicates registered NRSRO

ii. Policies and Procedures

Fitch Ratings has a Code of Conduct, relating to the quality and integrity of the rating process and avoidance of conflicts of interest. The Code of Conduct prohibits analysts from making proposals or recommendations regarding the design of structured finance products rated by Fitch Ratings.¹⁰⁷ The Code of Conduct also prohibits the practices described in Rule 17g-6.¹⁰⁸

¹⁰⁵ See <http://www.fitchratings.com/jsp/corporate/ProductsAndServices.faces?context=2&detail=112>.

¹⁰⁶ See descriptions at <http://www.fitchtraining.com/en/Default.aspx>. On January 23, 2013, Fitch Group acquired 7city Learning. Fitch is combining 7city with its Fitch Training unit to form Fitch 7city Learning. See http://www.fitchratings.com/creditdesk/press_releases/detail.cfm?pr_id=780601&origin=home&cm_sp=homepage-_-FeaturedContentLink-_-Learn%20More.

¹⁰⁷ See Fitch Ratings Code of Conduct (Dec. 2012), at 6, available at http://www.fitchratings.com/web_content/credit_policy/code_of_conduct.pdf.

¹⁰⁸ Id. at 8.

Fitch Ratings' Firewall Policy relates to Fitch Ratings, Fitch Solutions and Fitch Training and refers to confidentiality and the use of client information, policies and procedures so as to reduce the likelihood that any advisory, consulting or other ancillary business will influence ratings, and the separation of the ratings division from non-ratings affiliates.¹⁰⁹

Fitch Ratings also has issued a bulletin entitled "Restrictions on Advising Issuers and Others," which explains that Fitch is prohibited from providing "advice on how to achieve a desired credit rating" to issuers and others involved in the rating process.¹¹⁰

E. HR Ratings¹¹¹

i. Products and Services

From its website, HR Ratings does not appear to offer any services in addition to the issuance of credit ratings.¹¹²

ii. Policies and Procedures

HR Ratings has a Code of Conduct, which concerns quality in the provision of rating services, transparency and standards for professional conduct and prohibits employees from making recommendations or proposals concerning securities offerings for which HR Ratings

¹⁰⁹ See Fitch Ratings Firewall Policy (May 2012), at 2, available at http://www.fitchratings.com/web_content/credit_policy/firewall_policy.pdf.

¹¹⁰ See Fitch Ratings Restrictions on Advising Issuers and Others (Aug. 2010), available at http://www.fitchratings.com/web_content/credit_policy/restrictions_on_advising_issuers_and_others.pdf.

¹¹¹ See <http://www.hrratings.com/en/index>.

¹¹² Due to its registration as an NRSRO in November 2012, HR Ratings is currently undergoing its first Staff examination pursuant to Section 15E(p)(3) of the Exchange Act.

provides its rating services.¹¹³ The Code also provides for certain disclosure if HR Ratings were to receive income for services other than the provision of credit ratings.¹¹⁴

F. JCR¹¹⁵

i. Products and Services

JCR provides a variety of ancillary services including credit assessment services, servicer ratings and private credit assessments.¹¹⁶ JCR defines ancillary business as any business other than the credit rating business that is related to a credit rating action.¹¹⁷

ii. Policies and Procedures

JCR has a Code of Conduct which relates to the quality and integrity of the credit rating process and avoidance of conflicts of interest and includes procedures and mechanisms, with respect to ancillary business, to identify, eliminate, manage or minimize matters that may unfairly affect the assignment or the provision of credit ratings.¹¹⁸ JCR's Code prohibits the provision of consulting services regarding the organizational structure or the structure of the main assets and liabilities of rated companies and securities.¹¹⁹

¹¹³ See HR Ratings Code of Conduct (May 2012), at 30, available at <http://www.hrratings.com/pdf/lista/FormNRSRO.pdf>.

¹¹⁴ Id. at 17.

¹¹⁵ See <http://www.jcr.co.jp/english/>.

¹¹⁶ See <http://www.jcr.co.jp/english/ancillary/index.html?PHPSESSID=9e7d0ebfb5f4fe21e48db623e9c50fbf>.

¹¹⁷ See JCR Code of Conduct (Dec. 2012), at 12, available at http://www.jcr.co.jp/english/criterion/pdf/coce_e20120326.pdf.

¹¹⁸ Id. at 4.

¹¹⁹ Id. at 3.

JCR also has a Basic Compliance Policy regarding measures to ensure that actual or potential conflicts of interest “will not have an adverse impact on the interest of investors”.¹²⁰ JCR’s Conflicts of Interest Management Policy requires a separation of its ratings division from its departments and divisions that manage sales and ancillary business revenues, and contains certain measures designed to prevent conflicts of interest associated with its ancillary business.¹²¹

G. Kroll¹²²

i. Products and Services

Kroll “assigns credit ratings to issuers and their obligations and, through its Subscription Rating Service (SRS), financial strength ratings to financial institutions, corporations and sovereigns.”¹²³ Kroll also provides commercial mortgage-backed securities servicer evaluations, which are reviews of all entities that service commercial mortgage-backed securities transactions that Kroll rates or is likely to rate in the future.¹²⁴

ii. Policies and Procedures

Kroll has a Code of Conduct, which relates to the quality and integrity of the ratings process and avoidance of conflicts of interest, and prohibits analysts from making proposals or recommendations regarding the design of structured finance products that the company rates.¹²⁵

¹²⁰ See JCR Basic Compliance Policy, at 23, available at http://www.jcr.co.jp/english/nrsro/pdf/Update_20130131.pdf.

¹²¹ See JCR Conflicts of Interest Management Policy, at 31-32, available at http://www.jcr.co.jp/english/nrsro/pdf/Update_20130131.pdf.

¹²² See <https://www.krollbondratings.com/>.

¹²³ <https://www.krollbondratings.com/ratings/scales>.

¹²⁴ See <https://www.krollbondratings.com/products/cmbs-servicer-evaluations>.

¹²⁵ See Kroll Code of Conduct (Oct. 2012), at 6, available at https://www.krollbondratings.com/show_report/83.

The Code of Conduct also provides for certain disclosures if the company receives compensation from a rated entity unrelated to its ratings service.¹²⁶

H. Moody's¹²⁷

i. Products and Services

Moody's Policy for Ancillary and Other Permissible Services states that Moody's provides "Other Permissible Services" but does not currently offer "Ancillary Services"¹²⁸ (such "Ancillary Services" appear to be provided by Moody's Analytics, which is described below). "Other Permissible Services," which are described in such policy as being distinct from the credit rating services offered by Moody's¹²⁹ include bond fund ratings, credit estimates, indicative assessment services¹³⁰ and rating assessment services,¹³¹ as defined in a description of Moody's rating symbols and definitions.¹³² Such policy also states that Moody's does not provide consulting services or advisory services regarding the corporate or legal structure, assets, liabilities or activities of a rated entity.¹³³

¹²⁶ Id. at 8.

¹²⁷ See <http://www.moodys.com/Pages/atc.aspx>.

¹²⁸ Moody's defines ancillary services as those products and services that are not Credit Rating Services, and which are market forecasts, estimates of economic trends, pricing analysis, or other general data analysis, as well as related distribution services. See Moody's Policy for Ancillary and Other Permissible Services (Aug. 2012), at 2, available at http://www.moodys.com/sites/products/ProductAttachments/Compliance/9-9-2011/SP13347_Policy%20for%20Ancillary%20and%20Other%20Permissible%20Services.pdf.

¹²⁹ See Moody's Rating Symbols and Definitions (Feb. 2013), available at http://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

¹³⁰ See id. Indicative assessment services are defined as "[a] confidential, unpublished, unmonitored, point-in-time opinion of the potential Credit Rating(s) of, and based solely on, one or more hypothetical scenario(s) communicated to Moody's in writing by an applicant in relation to an entity/issuer that does not currently have a public Credit Rating from MIS."

¹³¹ See id. Rating assessment services are defined as "[a] confidential, unpublished, unmonitored, point-in-time opinion of the potential impact on the Credit Rating(s) of one or more hypothetical Scenario(s) communicated to MIS in writing by a Rated Entity."

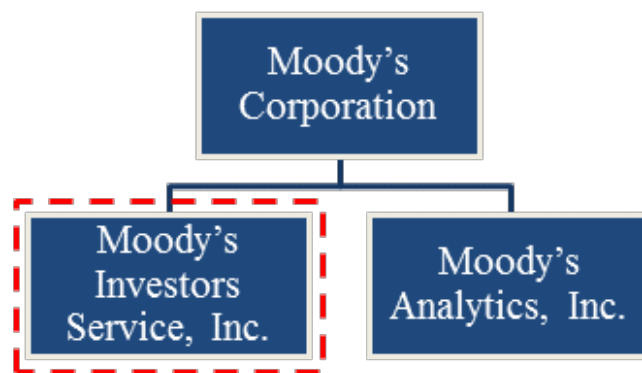
¹³² See id. for a complete list of other services identified in the policy as permissible services.

¹³³ See Moody's Policy for Ancillary and Other Permissible Services at 1.

Moody’s Analytics, which is a subsidiary of Moody’s Corporation, the parent entity of Moody’s, and therefore is not part of the NRSRO, performs non-rating commercial activities¹³⁴ including market-implied ratings, financial institutions research and performance data services.¹³⁵ According to the website of Moody’s Analytics, a market-implied rating “translates prices from the [CDS], bond, loan and equity markets into standard [Moody’s] ratings language,”¹³⁶ and Moody's ratings analysts use market-implied ratings to identify material and systematic gaps between Moody’s ratings and the ratings implied by market data.¹³⁷

Below is an organizational chart derived from the Moody’s Form NRSRO dated March 29, 2013, which illustrates the structure of Moody’s and Moody’s Analytics:

Table 2: Moody’s Corporation organizational structure



Source: Moody’s Form NRSRO, dated March 29, 2013 - Exhibit 4

--- Indicates registered NRSRO

¹³⁴ See Moody’s Corporation 10-K for the year ended December 31, 2012, available at <http://www.sec.gov/cgi-bin/browse-edgar?action=getcompany&CIK=0001059556&type=10-k&dateb=&owner=include&count=40>.

¹³⁵ See <http://www.moodyanalytics.com/products-and-solutions/az-product-list.aspx#F>.

¹³⁶ See http://www.moodyanalytics.com/~/_/media/Brochures/Credit-Research-Risk-Measurement/Quantative-Insight/MIR/MIR-Brochure.ashx.

¹³⁷ See <http://www.moody.com/sites/products/ProductAttachments/MIRFrequentlyAskedQuestions.pdf>.

ii. Policies and Procedures

Moody's Code of Professional Conduct relates to the quality and integrity of the rating process and the avoidance and management of conflicts of interest. It includes provisions regarding the separation of its ratings services from other businesses that may present a conflict of interest and refers to procedures and mechanisms regarding conflicts of interest associated with ancillary services and other permissible services.¹³⁸ The Code also provides for certain disclosures if Moody's receives compensation unrelated to its ratings service.¹³⁹

Moody's also has a policy which pertains to the physical, legal and operational separation of Moody's from Moody's Analytics and the sharing of confidential information.¹⁴⁰

Moody's Policy Banning Recommendations Associated with Credit Ratings prohibits the issuance or maintenance of a credit rating where any Moody's Corporation¹⁴¹ employee made recommendations to the rated entity or its agent about the corporate or legal structure, assets, liabilities or activities of the rated entity, on how to achieve a better rating.¹⁴²

¹³⁸ See Moody's Code of Professional Conduct (June 2011), at 10, available at http://www.moody.com/uploadpage/Mco%20Documents/Documents_professional_conduct.pdf.

¹³⁹ Id.

¹⁴⁰ See Moody's MIS-MA Separation Policy (Sept. 2011), at 1, available at http://www.moody.com/sites/products/ProductAttachments/Compliance/9-9-2011/SP13372_MIS%20-%20MA%20Separation%20Policy_Sept_06_2011%20Final.pdf.

¹⁴¹ Moody's Corporation refers to Moody's Corporation and all its subsidiaries.

¹⁴² See Moody's Policy Banning Recommendations Associated with Credit Ratings (Sept. 2011), at 1, available at <http://www.moody.com/sites/products/ProductAttachments/nrsro/SP13375.pdf>.

I. Morningstar¹⁴³

i. Products and Services

In addition to providing credit ratings for residential mortgage-backed securities and commercial mortgage-backed securities,¹⁴⁴ Morningstar also offers, through two different business groups within the NRSRO, (a) operational risk assessment services to institutional investors which analyze the operational risks associated with transaction participants,¹⁴⁵ and (b) research/advisory services, which includes Private Client Services, and includes products and services such as portfolio analysis, a commercial mortgage backed securities due diligence workstation and synthetic benchmarking.¹⁴⁶

ii. Policies and Procedures

Morningstar's Code of Conduct relates to the quality and integrity of the rating process and the avoidance of conflicts of interest, and refers to policies and procedures for managing conflicts of interest between Morningstar's credit rating business and its other businesses.¹⁴⁷

Morningstar's Confidential Information and Analytic Firewalls Policy pertains to the protection of confidential information and the prevention of improper exchange of such

¹⁴³ See <https://ratingagency.morningstar.com/RPLogin.aspx>.

¹⁴⁴ See Morningstar Exhibit 2 to Form NRSRO, available at <https://ratingagency.morningstar.com/PublicDocs/Exhibit%202.pdf>.

¹⁴⁵ See <https://ratingagency.morningstar.com/RPLogin.aspx>.

¹⁴⁶ See Morningstar's Confidential Information and Analytic Firewalls Policy, Exhibit 3 Form NRSRO, at 139, available at <https://ratingagency.morningstar.com/PublicDocs/NRSRO%20Application.pdf>. Synthetic benchmarking is a "service where the performance of a pool of residential mortgages, such as the collateral of a securitization or whole loan portfolio, is compared to similar loans in the Morningstar RMBS database." See <https://ratingagency.morningstar.com/PublicDocs/RMBS%20Services%20Brochure.pdf>.

¹⁴⁷ See Morningstar's Code of Conduct, Exhibit 5 Form NRSRO, at 159, available at <https://ratingagency.morningstar.com/PublicDocs/NRSRO%20Application.pdf>.

information. The policy also relates to the participation by rating analysts in consulting or advisory services.¹⁴⁸

Morningstar's Code of Ethics states that Morningstar is prohibited from issuing a rating where Morningstar made recommendations about the corporate or legal structure, assets, liabilities or activities of an obligor or security.¹⁴⁹

J. S&P¹⁵⁰

i. Products and Services

According to its Ancillary and Other Services Policy,¹⁵¹ in addition to its products and services related to the issuance of credit ratings, S&P provides and sells "Ancillary Services" and "Other Services." S&P's Glossary of Terms also refers to services entitled "Credit Assessments" and "Credit Estimates"¹⁵² and its website refers to "Ratings Evaluation Services."¹⁵³ As part of

¹⁴⁸ See Morningstar's Confidential Information and Analytic Firewalls Policy, at 144.

¹⁴⁹ See Morningstar's Code of Ethics, Form NRSRO Exhibit 7, at 173, available at <https://ratingagency.morningstar.com/PublicDocs/NRSRO%20Application.pdf>.

¹⁵⁰ See <http://www.standardandpoors.com/home/en/us>.

¹⁵¹ See S&P's Ancillary and Other Services Policy (Sept. 2011), at 1, available at <http://www.standardandpoors.com/ratings/form-nrsro/en/us>. As defined in S&P's Glossary of Terms, "ancillary service" is defined as a "product or service that Rating Services provides or sells that is not a Credit Rating or Credit Rating Activity and is either a market forecast, an estimate of economic trends, a pricing analysis, other general data analysis, or distribution services related to a Credit Rating, a market forecast, an estimate of economic trends, a pricing analysis, or general data analysis."

¹⁵² See S&P's Glossary of Terms (Jan. 2013) available at <http://www.standardandpoors.com/ratings/form-nrsro/en/us> and S&P's Ratings Definitions (June 2012), available at <http://www.standardandpoors.com/ratings/form-nrsro/en/us>. As defined in Rating Definitions, a Credit Estimate is "an indication, provided to a third party, of the likely Standard & Poor's issue or issuer credit rating on an unrated obligation or obligor" and a Credit Assessment is "an indicator of Standard & Poor's opinion of creditworthiness."

¹⁵³ "Ratings Evaluation Services" are described as "an analytical tool for corporations that are considering strategic or financial initiatives that could impact its [sic] creditworthiness. More specifically, this service allows corporations to assess the potential ratings impact of different types of debt." See <http://www.standardandpoors.com/ratings/corporates/en/us/>.

its EU regulatory disclosures, S&P considers “Credit Assessments” and “Credit Estimates,” as performed by certain of its European business operations, to be part of “Other Services,” for purposes of the applicable European regulations.¹⁵⁴

S&P Capital IQ, which is not part of the registered NRSRO, and is described as a separate segment of The McGraw-Hill Companies,¹⁵⁵ provides a variety of financial and analytical products to a variety of clients.¹⁵⁶ Examples of products and services offered by S&P Capital IQ include market derived ratings analytics, CreditModel, and Global Credit Portal.¹⁵⁷ S&P Capital IQ also provides Market Derived Signals (MDS) that are derived from a statistical model that evaluates credit default swaps.¹⁵⁸

¹⁵⁴ See S&P’s Product Descriptions available at <http://www.standardandpoors.com/ratings/european-union-regulatory-disclosures/en/eu>.

¹⁵⁵ See Exhibit 4 of S&P’s Form NRSRO, available at <http://www.standardandpoors.com/ratings/form-nrsro/en/us>. Such Exhibit describes S&P as a business unit within Standard & Poor’s Financial Services LLC, a company wholly-owned by The McGraw-Hill Companies, Inc. (“McGraw-Hill”). McGraw-Hill completed the sale of its McGraw-Hill Education business on March 22, 2013. McGraw-Hill was subsequently renamed McGraw Hill Financial, Inc. on May 1, 2013. See McGraw Hill Financial, Inc. 10-Q for the quarter ended June 30, 2013 available at <http://www.sec.gov/Archives/edgar/data/64040/000006404013000015/mhp-2013630xq2.htm> and McGraw Hill Financial, Inc. Form 8-K available at <http://www.sec.gov/Archives/edgar/data/64040/000119312513200788/d529200d8k.htm>.

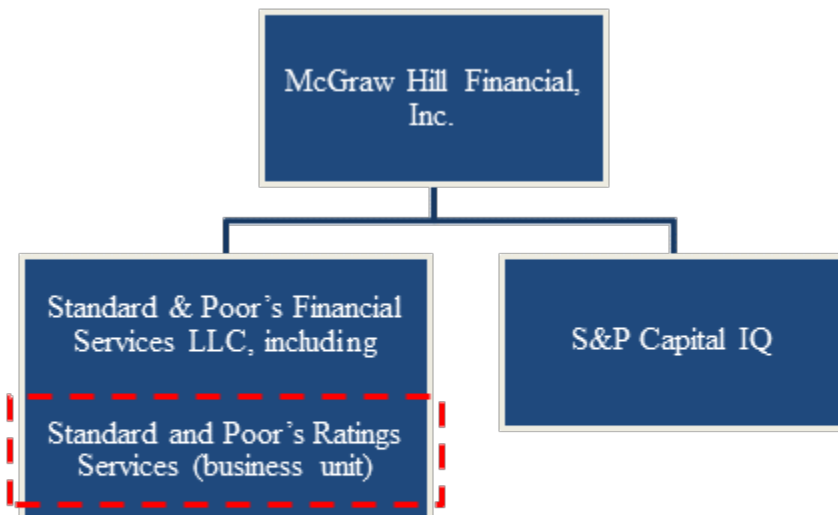
¹⁵⁶ See <https://www.capitaliq.com/home.aspx>.

¹⁵⁷ See <http://www.standardandpoors.com/products-services/main/en/us>.

¹⁵⁸ See http://www.insightforenterprise.com/images/_slicks/ES%20Credit%20Risk%20Indicators.pdf.

Below is an organizational chart derived from the S&P's Form NRSRO dated March 27, 2013, which illustrates the structure of S&P Ratings and S&P Capital IQ:¹⁵⁹

Table 3: McGraw Hill Financial, Inc. organizational structure



Source: S&P Form NRSRO, dated March 27, 2013 - Exhibit 4 and McGraw Financial, Inc. Form 8-K available at <http://www.sec.gov/Archives/edgar/data/64040/000119312513200788/d529200d8k.htm>

- - - - - Indicates registered NRSRO

ii. Policies and Procedures

S&P has a Code of Conduct relating to the quality and integrity of the rating process and the avoidance of conflicts of interest.¹⁶⁰ S&P also has an Ancillary and Other Services Policy relating to the prevention of confusion between its credit rating activities and its ancillary services or other services, and the implementation of appropriate measures to manage actual or potential conflicts of interest.¹⁶¹

¹⁵⁹ See *supra* text accompanying note 155.

¹⁶⁰ See S&P's Code of Conduct (June 2012), available at <http://www.standardandpoors.com/ratings/form-nrsro/en/us>.

¹⁶¹ See S&P's Ancillary and Other Services Policy at 1.

S&P's Roles and Responsibilities Policy refers to prohibitions on rating analysts and employees in commercial activities participating in each other's activities,¹⁶² and its Confidentiality, Conflicts and Firewall Policy relates to the sharing of confidential information and prohibitions against employees engaging in certain practices involving an issuer's purchase of any other service or product of S&P or [The] McGraw-Hill [Companies].¹⁶³ S&P's Policy Against Structuring Transactions prevents employees from structuring transactions and making recommendations to an issuer related to any security it may rate for that issuer.¹⁶⁴

VIII. NRSRO Enforcement of Policies and Procedures; NRSRO Exam Report Findings

A. NRSRO Enforcement of Policies and Procedures

Some of the NRSROs reported that they take certain of the actions below in order to self-enforce the policies and procedures with respect to Ancillary Services, which are described in Section VII of this report. The information was provided to the Staff by the NRSROs specifically in connection with the Study.

- (a) Internal audits to check for compliance with, and the effectiveness of, policies and procedures;
- (b) Employee training with respect to the applicable policies and procedures;
- (c) Maintenance of a "firewall log" to track collaboration between ratings and non-ratings employees;
- (d) Reviews of employee emails;
- (e) Random interviews with employees to verify compliance with policies and procedures;

¹⁶² See S&P's Roles & Responsibilities Policy (May 2012), at 1, available at <http://www.standardandpoors.com/ratings/form-nrsro/en/us>.

¹⁶³ See S&P's Confidentiality, Conflicts and Firewall Policy (Jan 2012), at 2, available at <http://www.standardandpoors.com/ratings/form-nrsro/en/us>.

¹⁶⁴ See S&P's Policy Against Structuring Transactions (Sept. 2010), at 1, available at <http://www.standardandpoors.com/ratings/form-nrsro/en/us>.

- (f) Employee confirmations at rating committee meetings that conflicts of interest did not influence rating decisions; and
- (g) Maintenance of a list to track clients with ancillary service business in excess of a certain amount, which is consulted before credit rating activity may be accepted.

B. NRSRO Exam Report Findings

Based on examinations performed to date, essential findings related to the conflict of interest concerning Ancillary Services were included in both the 2011 NRSRO Exam Report and 2012 NRSRO Exam Report.¹⁶⁵

In the 2011 NRSRO Exam Report, the Staff found that two of the smaller NRSROs appeared to have weak policies and procedures to disclose and manage conflicts of interest associated with certain ancillary businesses. The Staff recommended that each such NRSRO fully disclose and implement policies and procedures to manage such conflicts.

According to the 2011 NRSRO Exam Report, one of such NRSROs failed to disclose and implement policies and procedures to manage conflicts of interest associated with an ancillary service. The NRSRO considered such service to be a core rating service rather than an ancillary service, and as a result, did not disclose or establish policies and procedures to manage the relevant conflict of interest as required by Rule 17g-5(a). The NRSRO subsequently adopted policies and procedures in response to the examination finding. The other NRSRO was determined by the Staff to have weak policies and procedures to manage conflicts of interest associated with an ancillary service because it was unclear how the ratings business was kept separate from the ancillary service business due to the physical proximity of employees from both businesses. The NRSRO has not yet appropriately addressed this issue and the Staff is handling this issue through the examination process.

¹⁶⁵ See supra notes 9 and 11.

Additionally, in the 2011 NRSRO Exam Report, the Staff found that one of the smaller NRSROs appeared to have weak barriers between its ratings analysts and employees of a business unit providing an ancillary service posing a potential conflict of interest. At such NRSRO, ratings analysts shared office space with employees of the ancillary business unit providing investment advice. The Staff considered the potential conflicts between the interests of investment advice clients and ratings analytics to be significant and that the potential for the inappropriate dissemination of material nonpublic information among the ratings analysts and investment advice employees was significantly increased due to the sharing of office space. The Staff recommended that the NRSRO implement stronger barriers between such lines of business, including physical separation of the employees.

In the 2012 NRSRO Exam Report, the Staff found that one of the smaller NRSROs appeared to have insufficient policies and procedures to manage conflicts of interest associated with an ancillary service and recommended that the NRSRO enhance and adhere to its policies, procedures, and internal controls to effectively manage such conflict of interest and adequately disclose it in Exhibit 7 of Form NRSRO. In such case, the Staff noted that certain entities are customers of both the ratings and ancillary service businesses but that improvements were needed in the NRSRO's recordkeeping of the clients in the ancillary service business, maintenance of physical separation of the relevant employees, adherence to policies and procedures and creation of effective policies and procedures to manage the conflict of interest. The Staff is examining the NRSRO's response to this finding in the NRSRO's 2013 examination and will include any further essential findings in an NRSRO Exam Report.

IX. Comparable Conflicts of Interest

The 2003 Report compared the conflicts of interest relating to NRSROs' provision of ancillary services to the conflicts of interest addressed by Sarbanes-Oxley (i.e., involving accounting firms offering non-audit services and research analysts seeking additional business

for their investment banking firms through their recommendations).¹⁶⁶ Sarbanes-Oxley was enacted in part to address the risks to auditor independence which resulted from accounting firms providing certain non-audit services to their public company audit clients. Sarbanes-Oxley prohibited accounting firms from providing a specified list of non-audit services to their public audit clients.¹⁶⁷

Sarbanes-Oxley also addressed the conflicts of interest that arose when securities analysts recommended securities in research reports and public appearances in order for their firms to obtain additional investment banking business. Section 501 of Sarbanes-Oxley requires, among other things, the establishment of structural and institutional safeguards within registered brokers or dealers to assure that securities analysts are separated from review, pressure or oversight by employees whose involvement in investment banking activities might potentially bias the analysts' judgment or supervision.¹⁶⁸

Similarly, the Commission's Global Analyst Research Settlement of 2003 originally required certain investment firms, among other actions, to separate research from investment banking activities, including by physical separation, separate reporting lines, separate legal and compliance staffs and separate budgeting processes.¹⁶⁹

¹⁶⁶ See Report on the Role and Function of Credit Rating Agencies in the Operation of the Securities Markets, Commission staff.

¹⁶⁷ Section 201 of Sarbanes Oxley – Services Outside the Scope of Practice of Auditors. 15 U.S.C. 78j-1 (2006) (banning non-audit services such as bookkeeping, designing financial information systems, actuarial services, internal audit outsourcing services and management functions or human resources).

¹⁶⁸ Section 501 of Sarbanes-Oxley.

¹⁶⁹ See SEC Fact Sheet on Global Analyst Research Settlements available at <http://www.sec.gov/news/speech/factsheet.htm>. On March 15, 2010, Judge William H. Pauley III of the U.S. District Court for the Southern District of New York approved various modifications to the final judgments entered against the firms covered by such settlements; however, of the activities mentioned above, the requirements for physical separation of research analysts and investment banking, and separate budgeting processes, remained in place. See SEC v. Bear, Stearns & Co., No. 03 Civ. 2937 (WHP), slip op. at Addendum A § I.3 (S.D.N.Y. Mar. 15, 2010).

Academic commentary is mixed on whether the NRSROs' provision of Ancillary Services poses the same potential for conflicts of interest as the pre-Sarbanes-Oxley accounting firms' provision of consulting services. One commenter concludes that ancillary services provided by credit rating agencies are a "nonissue" because they contribute to an "insignificant fraction" of the credit rating agencies' total revenue,¹⁷⁰ "fees from the average credit rating client constitute only a small fraction of each [credit rating agency's] total revenue"¹⁷¹ and the rating agencies have "firewalls and self-regulations in place to prevent any conflicts of interest from negatively impacting the integrity of their rating processes."¹⁷² However, another commenter disagrees, arguing that the percentage of revenue contributed by any single rating client, as a "metric for independence," does not address whether the audit team [or credit analyst] is actually independent,¹⁷³ and observing that Enron accounted for only one percent of its auditor's total revenues.¹⁷⁴

According to information reported by the NRSROs to the Commission for purposes of the Dodd-Frank Independence Study, for the fiscal year ended in 2011, it appears that: (i) four NRSROs did not have any revenue attributable to products and services in addition to NRSRO ratings; (ii) two NRSROs had less than 10% of total NRSRO revenues that were attributable to products and services in addition to NRSRO ratings; and (iii) four NRSROs had between approximately 10% and 28% of total revenues that were attributable to products and services in addition to NRSRO ratings. In addition, for NRSROs which have reported revenue annually

¹⁷⁰ See Nicole Neuman, A Sarbanes-Oxley for Credit Rating Agencies? A Comparison of the Roles Auditors' and Credit Rating Agencies' Conflicts of Interests Played in Recent Financial Crises, 12 U. Pa. J. Bus. L. 921 (2010). For this conclusion, the author relies on the 2003 Report. In the 2003 Report, ancillary services were described as representing a "very small percentage" of total NRSRO revenues, with the rating agencies noting that ancillary services are an "insignificant" aspect of their businesses, so that potential conflicts of interest are "immaterial." See 2003 Report, at 43.

¹⁷¹ Id. at 942.

¹⁷² Id. at 922.

¹⁷³ Hatchett at 420, n. 95. In making this argument, Hatchett quotes an article in the Villanova Law Review which discusses the independence of the audit team. Hatchett includes the bracketed reference to "credit analyst" in order to analogize between rating analysts and auditors.

¹⁷⁴ Id. at 420.

since 2007 (which is the first year such information was required to be reported to the Commission) under Rule 17g-3(a)(3)(iv),¹⁷⁵ such revenues have for the most part either declined or remained steady. The reported information referred to above reflects the categorizations of products and services used by the NRSROs which, as indicated in Section VI.B of this report, differ among the NRSROs and may be less inclusive than the definition of Ancillary Services used in this report.

X. Conclusions and Recommendations

The essential findings (which are limited in number) in the NRSRO Exam Reports relating to certain NRSROs' management of conflicts of interest involving Ancillary Services do not suggest that NRSROs generally have been unable to manage such conflicts of interest through their existing policies and procedures. Accordingly, at this time, the Staff does not believe that it is warranted to recommend to the Commission changes to the rules on an NRSRO's providing Ancillary Services to issuers for which it also provides a rating.¹⁷⁶

Notwithstanding the foregoing, the Staff will continue to consider and monitor the potential conflicts of interest posed by the provision of Ancillary Services to issuers. According to information reported to the Commission for purposes of the Dodd-Frank Independence Study, four of the NRSROs had 2011 fiscal year revenues attributable to products and services in addition to NRSRO ratings (based on the NRSROs' own classification of such products and services) ranging between approximately 10% and 28% of total revenue. As suggested in Section IX of this report,¹⁷⁷ conflicts of interest may exist even for clients representing a small percentage of total NRSRO revenues. Also, a particular client might be very important to the business conducted by a specific office of, or a business line within, an NRSRO even if it

¹⁷⁵ See the last paragraph of Section III.D.i of this report. Rule 17g-3(a)(3)(iv) requires reporting of "all other services and products" besides credit ratings determinations and certain other items.

¹⁷⁶ If any such changes to the rules are to be recommended in the future, the Staff believes that they should address the provision of Ancillary Services by non-NRSRO affiliates.

¹⁷⁷ Hatchett at 420.

represents a small percentage of the NRSRO's overall revenues. Finally, it is possible that Ancillary Services may experience future growth, even though revenues reported by NRSROs under Rule 17g-3(a)(3)(iv)¹⁷⁸ appear to have either declined or remained steady over the past six years.

Regardless of how they categorize Ancillary Services and report the associated revenue¹⁷⁹, NRSROs must manage conflicts of interest involving Ancillary Services in accordance with the applicable regulatory requirements, including those in Section 15E(h) and Rule 17g-5(a) of the Exchange Act. The Commission's examination function is a vital tool to assess how well the NRSROs are complying with such requirements, as well as providing an opportunity to observe whether actual conflicts of interest exist.

Through the NRSRO examination process, essential findings are communicated to the NRSROs and the Staff monitors NRSRO responsiveness to suggested remedial actions. Potential violations of U.S. securities laws discovered in NRSRO examinations have been and may in the future be referred for potential enforcement action. In addition, essential findings are communicated to the public through the NRSRO Exam Reports.

In order to assess whether to recommend to the Commission in the future changes to the rules on the provision of Ancillary Services by NRSROs to rated entities, the Staff will: (a) continue to monitor the revenue information received from NRSROs regarding Ancillary Services, (b) conduct the required annual examinations of each of the NRSROs to review their management of conflicts of interest (including those associated with Ancillary Services) and (c) specifically examine whether NRSROs may have deviated from rating procedures or methodologies in performing ratings of issuers that provide non-ratings revenue to the NRSRO or its affiliates.

¹⁷⁸ See the last paragraph of Section IX of this report.

¹⁷⁹ As indicated in Sections VI.B and IX of this report, the differing definitions and categories used by NRSROs to describe Ancillary Services may result in either over- or under-inclusiveness by NRSROs in reporting revenue information regarding such services and make it difficult to compare such information among the NRSROs. The revenue information reported under Rule 17g-3(a)(3)(iv) does not include revenues of non-NRSRO affiliates which provide similar services (although such information may be available in the public securities filings of certain NRSROs), or indicate the extent to which rating services customers also purchase Ancillary Services or similar services from non-NRSRO affiliates.

The Staff will continue to report, in its NRSRO Exam Reports, these and other findings and recommendations made to the NRSROs with respect to such matters, and will consider whether to make additional recommendations concerning the management of conflicts of interest involving Ancillary Services if the Staff deems appropriate based on examination results.