

of the statute provide the Commission with authority to prohibit, or require the management and disclosure of, any potential conflict of interest relating to the issuance of credit ratings by an NRSRO.¹¹⁰ The Commission preliminarily believes the proposed amendment is necessary and appropriate in the public interest and for the protection of investors because it would address a potential practice that could impair the objectivity, and, correspondingly, the quality, of a credit rating. It has been suggested that during the process of rating structured finance products the NRSROs have recommended to arrangers how to structure a trust or complete an asset pool to receive a desired credit rating and then rated the securities issued by the trust – in effect, rating their own work.¹¹¹ This proposal would prohibit this conduct based on the Commission’s preliminary belief that it creates a conflict that cannot be effectively managed inasmuch as it would be very difficult for an NRSRO to remain objective when assessing the creditworthiness of an obligor or debt security where the NRSRO or person associated with the NRSRO made recommendations about steps the obligor or issuer of the security could take to obtain a desired credit rating.

The proposal is not intended to prohibit all interaction between the NRSRO and the obligor, issuer, underwriter, or sponsor during the rating process. The Commission preliminarily believes that the transparency of an NRSRO’s procedures and methodologies for determining credit ratings is enhanced when the NRSRO explains to obligors and issuers the bases, assumptions, and rationales behind rating decisions. For example, the Commission understands that in the structured finance area, NRSROs may

¹¹⁰ Id.

¹¹¹ See e.g., Coffee April 22, 2008 Senate Testimony, pp. 2-3.

