Paragraph (a)(1)(iii) of proposed Rule 17g-7 would require an NRSRO to identify for each person listed in the consolidated report all outstanding credit ratings paid for by that person, which the NRSRO would need to determine in accordance with proposed paragraph (a)(3)(iii) of Rule 17g-7. Specifically, the NRSRO would need to identify by name of obligor, security, or money market instrument and, as applicable, CIK number, CUSIP, or ISIN each outstanding credit rating generated as a result of the person paying the NRSRO for the issuance or maintenance of the credit rating and attribute the outstanding credit rating to the person. For example, assume XYZ Corp. had paid the NRSRO to issue and maintain credit ratings for three different classes of debt instruments issued by XYZ Corp. and there were credit ratings outstanding for each of these classes of debt instruments as of the end of the NRSRO's fiscal year. In this case, each of these debt instruments would need to be identified by name and CUSIP number and associated with XYZ Corp. on the consolidated report.

Proposed paragraph (a)(2) of Rule 17g-7 would provide an exemption to the requirement to generate the consolidated report or to include with the publication of a credit rating the statement required by paragraph (b) of proposed Rule 17g-7 (discussed below) if, as of the end of the fiscal year, there were no credit ratings of the NRSRO outstanding that were issued or maintained as a result of a person paying the NRSRO for the issuance or maintenance of the credit rating. For example, a subscriber-paid NRSRO may be exempt from the requirements of the proposed rule if it is not paid by obligors, issuers, underwriters or investors to issue or maintain specific credit ratings. This would mean that a subscriber-paid NRSRO would not need to generate the report or make the generic statement, provided it only was paid by subscribers to access its credit ratings.

However, it would need to generate the report if it was paid, for example, by an investor to issue or maintain a credit rating on a specific debt instrument.

B. Proposed Paragraph (b) of Rule 17g-7

Proposed paragraph (b) of Rule 17g-7 would provide that an NRSRO must prominently include a statement that identifies where on its Internet Web site the consolidated report required pursuant to paragraph (a)(1) is located each time the NRSRO publishes a credit rating or credit ratings in a research report, press release, announcement, database, Internet Web site page, compendium, or any other written communication that makes the credit rating publicly available for free or a reasonable fee. Specifically, the NRSRO would need to include the following statement: "Revenue information about persons that paid the nationally statistical rating organization for the issuance or maintenance of a credit rating is available at: [insert address to Internet Web site]." The proposed statement is intended to be generic and, thereby, to minimize the burden of including it when a credit rating (or credit ratings) is published. The proposal is designed to simply alert users of credit ratings and others where they can locate the consolidated report containing information about persons who paid the NRSRO to issue or maintain a credit rating. This would allow the users of credit ratings and others accessing the consolidated report to research the persons who had paid the NRSRO for credit ratings outstanding as of the fiscal year end. The researchers could review the amount of net revenue earned by the NRSRO attributable to providing services other than credit ratings to persons who paid for specific credit ratings, the relative standing of the persons who paid for the credit ratings in terms of providing net revenue to the NRSRO, and the credit ratings that the persons paid the NRSRO to issue or maintain.

C. Conclusion

The Commission is proposing these amendments under authority to require an NRSRO to "make and disseminate such reports as the Commission, by rule, prescribes as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of [the Exchange Act]." The Commission preliminarily believes these proposed amendments are necessary and appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Exchange Act for the reasons stated above and because they are designed to provide investors and other users of credit ratings with information to assess the degree of risk that a credit rating may be compromised by the undue influence of the person that paid for the issuance or maintenance of the credit rating.

D. Request for Comment

The Commission generally requests comment on all aspects of this proposed new rule. In addition, the Commission requests comment on the following questions related to the proposal.

- Are the classifications in terms of revenue provided to the NRSRO (top 10%, top 25%, top 50%, bottom 50% or bottom 25%) proposed in new Rule 17g-7 appropriate? How uniform are the potential conflicts of interest with respect to the clients within these categories? Should there be more or less classifications? What should they be? Should the classifications be defined differently, such as on the size of the client, the total revenue, the types of other services provided to the clients?
- How would investors and other users of credit rating ratings use this

information?

- Given the potential heterogeneity among clients in a particular tier, how similar is the risk of a potential conflict of interest with regard to clients within a given tier?
- Is being in a top-tier classification likely to create an undue concern that suggests to investors that a rating is conflicted, even if it is not? To the extent a negative connotation exists when an issuer is in a top percentile, what risk, if any, exists that clients will seek out those NRSROs for which their revenue contribution is less significant? Does such behavior risk disproportionately impact smaller NRSROs? If so, how? If not, why not? What other potential behavioral changes might the disclosure induce?
- To what extent is the information in these reports already observable? Can someone look at the information on rated bonds to determine who an NRSRO's biggest clients are? Is there overlap between the biggest clients for rating services and the biggest overall clients of an NRSRO?
- Are there any potential unintended consequences of the proposed disclosures?
- Is 90 days after the end of the fiscal year sufficient time for an NRSRO to generate the information to be used for the next twelve-month period?
- Would more frequent updates of the required information provide more meaningful information to investors? Would the cost of producing more frequently updated reports greatly increase the costs to NRSRO?
- Should a newly-registered NRSRO be exempt from having to generate the consolidated report and make the generic statement until the end of its first

fiscal year as a registered NRSRO?

- Would including revenue earned by persons directly or indirectly controlling, controlled by, or under common control with, the NRSRO (i.e., affiliates) provide a more enhanced disclosure of the potential conflicts of undue influence, since the organization as a whole may care about its revenues regardless of which part of the business earned the revenues? If so, would it be useful for investors and other users of credit ratings to have this information? Would it be complicated and costly to do the calculations under proposed Rule 17g-7 if affiliates are included?
- If the term affiliate was added to the proposed disclosures, should the Commission define the term affiliate? For example, if an NRSRO controlled less than 51% of an entity, should the entity be considered an affiliate? If a natural person controlled or owned an NRSRO, should other entities the individual owns or controls be considered affiliates of the NRSRO for purposes of the proposed rule?
- How is the data to be reported currently entered and stored at NRSROs, and would such data be able to be published on an automated or nearly automated basis after a one-time systems adjustment?
- Would it be useful for investors or other users of credit ratings to require an NRSRO to calculate and disclose revenue information with respect to other persons in addition to persons that paid the NRSRO for services? For example, should the Commission attribute underwriter-paid ratings to the issuer? In addition, should the consolidated report provide for double counting

of revenues earned by the NRSRO if the Commission attributes payment to both the underwriter and issuer so that users of a credit rating could more easily evaluate whether a large percentage of the NRSRO's revenues are attributable to particular issuers or underwriters or a concentrated group of clients?

- Would it be useful to require another disclosure item in the proposed consolidated report to show the issuer or underwriter who did not pay for the service but was a party to a deal? If so, should there be a particular order of disclosing this item to highlight the frequency of this person's involvement in deals that are rated by a particular NRSRO? For example, should there be a separate disclosure item to reveal the percentage of net revenue earned by the NRSRO in which the party who did not pay for the service was involved in the deal?

Additionally, the Commission is soliciting comment from investors, market participants, and others as to whether it would be appropriate to require that specific information be reported when a credit rating action is made publicly available (i.e., more than a generic statement of where relevant information can be located). Specifically, the Commission solicits comment on the following:

- Should an NRSRO be required to include the information proposed to be included in the consolidated report about a person that paid for the issuance or maintenance of a credit rating along with the publication of the credit rating? If such a requirement were in place, would it be more beneficial to users of NRSROs of credit ratings than the requirements of proposed Rule 17g-7

discussed above? Would such a requirement have higher costs than proposed Rule 17g-7?

- Should an NRSRO be required to disclose the principal procedures and methodologies used in determining the credit rating? Should this disclosure include information about key assumptions used and the qualitative and quantitative models, if any, employed in determining the credit rating? Should the level of disclosure be sufficient so that "outside parties can understand how a rating was arrived at" by the NRSRO? What would be the benefits and costs associated with such a requirement?
- If an NRSRO should disclose information about the key assumptions used, should an NRSRO also be required to disclose the degree to which the NRSRO has analyzed how sensitive a rating is to changes in these assumptions? What would be the benefits and costs associated with such a requirement?
- Should an NRSRO be required to disclose if a rating action is being taken as a result of a change to a procedure or methodology, including a change to an applicable qualitative or quantitative model? What would be the benefits and costs associated with such a requirement?
- Should an NRSRO be required to disclose that a rating action is being taken as a result of an error identified in a procedure or methodology used to generate the credit rating? What would be the benefits and costs associated with such a requirement?

- Should an NRSRO be required to disclose information on the limitations of the credit rating, including information on the reliability, accuracy, and quality of the data relied on in determining the rating? What would be the benefits and costs associated with such a requirement?
- Would a statement on the extent to which key data inputs for the credit rating were reliable or limited, including any limits on the adequacy of historical data and limits on the availability and completeness of other relevant information be beneficial? What would be the benefits and costs associated with such a requirement?
- Should an NRSRO be required to disclose a description of relevant data about the obligor, issuer, security, or money market instrument being rated that was used and relied on for the purpose of determining the credit rating? What would be the benefits and costs associated with such a requirement?
- Should an NRSRO be required to disclose whether material nonpublic information was used in determining the credit rating? Should an NRSRO be required to disclose, in general terms, the type of confidential information used and the impact this information had on its rating action? What would be the benefits and costs associated with such a requirement?
- Is the timeframe for disclosure (the NRSRO's most recent fiscal year end) the best timeframe to evaluate whether a conflict exists and the potential extent of the conflict? For example, should the information disclosed be based on the results over a 3, 5, or 10 year period in order better capture longer term trends?

V. TECHNICAL AMENDMENTS TO FORM NRSRO INSTRUCTIONS

The Commission also is proposing to make certain technical amendments to the Instructions to Form NRSRO. The Commission is proposing to amend the title to Exhibit 6 to read "Information concerning conflicts of interest or potential conflicts of interest relating to the issuance of credit ratings by the credit rating agency," rather than the current "Identification of conflicts of interest relating to the issuance of credit ratings." The Commission is proposing this change to the title of Exhibit 6 to Form NRSRO to better reflect the additional disclosures proposed to be required, as described in Section III above. In addition, in the General Instructions[98] to the Form NRSRO Instructions, the Commission is proposing to add "Division of Trading and Markets" and "Mail Stop 7010" to the mailing address for Form NRSRO. This is designed to facilitate receipt of Form NRSRO by the Division of Trading and Markets.

Further, in the "Instructions for Annual Certifications," the Commission is prosing to clarify that the annual financial reports that an NRSRO must furnish to the Commission pursuant to Section 15E(k) of the Exchange Act and Exchange Act Rules 17g-3(a)(1) through (a)(6), as applicable, should not be furnished as part of the annual certification on Form NRSRO. The Commission also is proposing additional amendments to the instructions to state that pursuant to paragraph (b) of Rule 17g-3, the NRSRO must attach to each financial report the certification required by Rule 17g-3.[99]

There has been some confusion among some NRSROs on the requirement to provide a certification for each financial report. The annual certification is a statutory

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98 See Paragraph A.8. "Address" in the General Instructions to the Form NRSRO Instructions.

99 See 17 CFR 240.17g-3(b).

requirement set forth in Section 15E(b)(2) of the Exchange Act.[100] The Commission adopted Rule 17g-1(f) to require that an NRSRO furnish the Commission with its annual certification on Form NRSRO.[101] The annual financial reports that an NRSRO must furnish to the Commission pursuant to Section 15E(k) of the Exchange Act and Exchange Act Rules 17g-3(a)(1) through (a)(6), are separate and distinct requirements from the Form NRSRO requirements. Consequently, the Rule 17g-3 reports should be furnished separately from the Form NRSRO that is used to make the annual certification. Therefore, the Commission is proposing this amendment to clarify the distinct requirements with respect to Form NRSRO and Rule 17g-3(a)(1) through (a)(6).

The Commission also is proposing to correct certain typographical errors in the Form NRSRO. The Commission is proposing to change the phrase "withdrawal of registration" to "withdrawal from registration" in the first sentence in the "Instructions for Specific Line Items, Item 5." to the Form NRSRO Instructions.[102] In addition, in the instructions to Exhibit 8 to Form NRSRO, the Commission is proposing to delete the phrase "(See definition below)". In the instructions to Exhibit 10 to Form NRSRO, the Commission is proposing to change the word "person" to "user of credit rating services" in the first sentence. Finally, the Commission is proposing to change the paragraph heading for the section titled "Explanation of Terms" from "F." to "I." The corrected heading will read: "I. EXPLANATION OF TERMS".

The Commission generally requests comment on all aspects of these proposed amendments to Form NRSRO.

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100 15 U.S.C. 78o-7(b)(2).

101 17 CFR 240.17g-1(f).

102 See Paragraph H in the "Instructions for Specific Line Items, Item 5." to the Form NRSRO Instructions.

VI. DIFFERENTIATING STRUCTURED FINANCE CREDIT RATINGS

The Commission has adopted requirements that are designed to allow investors and other users of credit ratings to better understand the differences between structured finance products and their credit ratings and other types of debt instruments and their credit ratings. For example, the rules adopted in the February 2009 Adopting Release and in today's Companion Release include requirements for specific disclosures about the methodologies and procedures for determining credit ratings for structured finance products and the public disclosure of credit rating performance statistics and histories by class of credit rating. For instance, the February 2009 Adopting Release amended Exhibit 1 to Form NRSRO to require disclosure of performance statistics for each class of credit rating for which the NRSRO is registered with the Commission.[103] Moreover, the Commission amended the Exhibit to require that the performance statistics for the class of credit ratings specified in Section 3(a)(62)(B)(iv) of the Rating Agency Act[104] include credit ratings of any security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction.[105] This was designed to capture ratings actions for credit ratings of structured finance products that do not meet the narrower statutory definition of "issuers of asset-backed securities (as that term is defined is section 1101(c) of part 229 of title 17, Code of Federal Regulations)."[106] The amendment requires that an NRSRO registered in this class of credit ratings must generate and disclose performance statistics for this class, which includes all structured finance products. As a result, these statistics can be compared with performance statistics

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103 See February 2009 Adopting Release, 74 FR at 6457-6459.

104 15 U.S.C. 78c(a)(62)(B)(iv).

105 See February 2009 Adopting Release, 74 FR at 6457-6459.

106 Id.

for other classes of credit ratings for which the NRSRO is registered, such as corporate issuers.

Similarly, the Commission adopted amendments to paragraph (d) of Rule 17g-2, which require that an NRSRO make publicly available, on a six-month delayed basis ratings action information for a random sample of 10% of ratings documented pursuant to paragraph (a)(8) for each class of credit rating for which the NRSRO is registered and has issued 500 or more ratings paid for by the obligor being rated or by the issuer, underwriter, or sponsor of the security being rated ("issuer-paid credit ratings").[107] This requirement will allow investors and market participants to compare the rating action histories for an NRSRO's issuer-paid structured finance ratings with the histories of other classes of credit ratings where the NRSRO has 500 or more outstanding issuer-paid credit ratings. In the Companion Release being issued today, the Commission is adopting an amendment to Rule 17g-2 to require the disclosure of all outstanding credit ratings initially determined on or after June 26, 2007.[108] This will further enhance the ability of investors and other users of credit ratings to track the relative performance of structured finance credit ratings as compared with performance of other classes of credit ratings.

In the February 2009 Adopting Release, the Commission also adopted amendments to Exhibit 2 to Form NRSRO requiring specific disclosures with respect to the procedures and methodologies for determining credit ratings for structured finance products.[109] The amendments require, among other things, that an NRSRO disclose: (1) whether and, if so, how information about verification performed on assets underlying or referenced by a security or money market instrument issued by an asset pool or as part of

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107 See February 2009 Adopting Release, 74 FR at 6460-6463.

108 See Companion Release.

109 See February 2009 Adopting Release, 74 FR at 6459-6460.

any asset-backed or mortgage-backed securities transaction is relied on in determining credit ratings; and (2) whether and, if so, how assessments of the quality of originators of assets underlying or referenced by a security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction play a part in the determination of credit ratings.

All these measures will assist investors and other users of credit ratings in understanding the different characteristics and risks of structured finance products and the credit ratings for those products. The Commission, however, also continues to explore further ways to increase investor understanding of the differences between structured finance products and other types of debt instruments and the respective credit ratings for those products.

In the sections below, the Commission solicits comments on the following: (1) how the goal of the proposed Rule 17g-7 set forth in the June 2008 Proposing Release could be promoted through other measures designed to enhance investor understanding of the differences between the risk characteristics of structured finance products and other classes of debt instruments and the differences between the risk characteristics of credit ratings for structured finance products and credit ratings for other classes of credit ratings; and (2) what measures could be taken to facilitate the ability of NRSROs to determine unsolicited credit ratings for existing debt instruments issued by structured finance products. The goal of either initiative would be to provide the marketplace and investors with information that would allow them to differentiate structured finance credit ratings from credit ratings for other types of debt instruments.

A. The Use of Different Symbols for Structured Finance Products

In the June 2008 Proposing Release, the Commission proposed a new rule – Rule 17g-7 – that would have required an NRSRO to issue a report with respect to a structured finance credit rating or, alternatively, to use a distinct symbology to identify structured finance credit ratings.[110] Specifically, paragraph (a) of the Rule 17g-7 proposed in 2008 would have required an NRSRO to publish a report accompanying every credit rating it published for a security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction. The NRSRO would have been required to describe in the report the rating methodology used to determine the credit rating and how it differed from a rating for any other type of obligor or debt security, as well as how the risks associated with a security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction are different from the risks of other types of rated obligors and debt securities. Paragraph (b), however, would have permitted an NRSRO to comply with the rule by distinguishing its rating symbols for structured finance products. The Commission did not propose requiring that specific rating symbols be used to distinguish credit ratings for structured finance products, instead proposing that an NRSRO would be permitted to choose the appropriate symbol or identifier.[111]

The Commission proposed Rule 17g–7 in the June 2008 Proposing Release to address concerns that certain investors assumed the risk characteristics for structured finance products, particularly highly rated instruments, were the same as for other types

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110 As discussed above, the Commission is proposing in this release that a different proposed rule be codified as Rule 17g-7 in the CFR. The Rule 17g-7 being proposed in this Release would require an NRSRO to make publicly available a consolidated report containing information about relative percent of revenues of the NRSRO attributable to persons paying the NRSRO for the issuance or maintenance of a credit rating.

111 See June 2008 Proposing Release.

of similarly rated instruments, as well as concerns that some investors may not have performed adequate internal risk analysis on structured finance products before purchasing them.[112] The goal of the proposal was to spur investors to perform more rigorous internal risk analysis on such products so that they would not overly rely on NRSRO credit ratings in making investment decisions. At the time, the Commission noted that a potential ancillary benefit of the rule would be that it could cause certain investors to seek to better understand the risks of structured finance products that are not necessarily addressed in credit ratings, such as market and liquidity risk.[113]

In the June 2008 Proposing Release, the Commission expressed its preliminarily belief that requiring an NRSRO to publish a report along with each publication of a credit rating for a structured finance product likely would provide certain investors with useful information about structured finance products and spur investors to perform more rigorous internal risk analysis on structured finance products.[114] Alternatively, the Commission noted, the use of distinct symbology would alert investors that a structured finance product was being rated and, therefore, raise the question of how it differs from other types of debt instruments.[115]

The Commission generally requested comment on all aspects of the proposed new rule as well as on several specific questions.[116] A total of 40 commenters responded to this request.[117] Sixteen commenters expressed opposition to the proposed rule as a

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112 See June 2008 Proposing Release, 73 FR at 36235.

113 Id.

114 Id.

115 Id.

116 See June 2008 Proposing Release, 73 FR at 36236.

117 Letter dated June 10, 2008 from Deborah A. Cunningham and Boyce I. Greer, Co-Chairs Company, Co-Chairs, SIFMA Credit Rating Agency Task Force ("First SIFMA Symbology Letter"); letter dated June 19, 2008 from Rupert Schoder, Financial Engineer, Socit Gnrale, France ("SGF Symbology Letter"); letter dated July 14, 2008 from Robert Dobilas, President, CEO,

Realpoint LLC ("Realpoint Symbology Letter"); letter dated July 21, 2008 from Dottie Cunningham, Chief Executive Officer, Commercial Mortgage Securities Association ("CMSA Symbology Letter"); letter dated July 21, 2008 from Bruce Goldstein, SunTrust Robinson Humphrey ("STRH Symbology Letter"); letter dated July 21, 2008 from Raymond E. Petersen, President, Inland Mortgage Capital Corporation ("Inland Symbology Letter"); letter dated July 21, 2008 from Leonard W. Cotton, Vice Chairman, Centerline Capital Group ("Centerline Symbology Letter"); letter dated July 22, 2008 from Kevin Kohler, VP - Levered Finance, Capmark Investments LP ("Capmark Symbology Letter"); letter dated July 22, 2008 from Mary A. Downing, Director -Surveillance and Due Diligence, Hillenbrand Partners ("Hillenbrand Symbology Letter"); letter dated July 23, 2008 from Kent Wideman, Group Managing Director, Policy & Rating Committee and Mary Keogh, Managing Director, Policy & Regulatory Affairs, DBRS ("DBRS Symbology Letter"); letter dated July 24, 2008 from Takefumi Emori, Managing Director, Japan Credit Rating Agency, Ltd. ("JCR Symbology Letter"); letter dated July 24, 2008 from Amy Borrus, Deputy Director, Council of Institutional Investors ("Council Symbology Letter"); letter dated July 24, 2008 from Vickie A. Tillman, Executive Vice President, Standard & Poor's Ratings Services ("S&P Symbology Letter"); letter dated July 24, 2008 from Deborah A. Cunningham and Boyce I. Greer, Co-Chairs Company, Co-Chairs, SIFMA Credit Rating Agency Task Force ("Second SIFMA Symbology Letter"); letter dated July 25, 2008 from Sally Scutt, Managing Director, and Pierre de Lauzun, Chairman, Financial Markets Working Group, International Banking Federation ("IBFED Symbology Letter"); letter dated July 25, 2008 from Denise L. Nappier, Treasurer, State of Connecticut ("Nappier Symbology Letter"); letter dated July 25, 2008 from Suzanne C. Hutchinson, Mortgage Insurance Companies of America ("MICA Symbology Letter"); letter dated July 25, 2008 from Kieran P. Quinn, Chairman, Mortgage Bankers Association ("MBA Symbology Letter"); letter dated July 25, 2008 from Frank Chin, Chairman, Municipal Securities Rulemaking Board ("MSRB Symbology Letter"); letter dated July 25, 2008 from Charles D. Brown, General Counsel, Fitch Ratings ("Fitch Symbology Letter"); letter dated July 25, 2008 from Bill Lockyer, State Treasurer, California ("Lockyer Symbology Letter"); letter dated July 25, 2008 from Jeremy Reifsnyder and Richard Johns, Co-Chairs, American Securitization Forum Credit Rating Agency Task Force ("ASF Symbology Letter"); letter dated July 25, 2008 from Francisco Paez, Metropolitan Life Insurance Company ("MetLife Symbology Letter"); letter dated July 25, 2008 from Cate Long, Multiple-Markets ("Multiple-Markets Symbology Letter"); letter dated July 25, 2008 from Kurt N. Schacht, Executive Director and Linda L. Rittenhouse, Senior Policy Analyst, CFA Institute Centre for Financial Market Integrity ("CFA Institute Symbology Letter"); letter dated July 25, 2008 from Lawrence J. White, Professor of Economics, Stern School of Business, New York University ("White Symbology Letter"); letter dated July 25, 2008 from Jack Davis, Head of Fixed Income Research, Schroder Investment Management North America Inc. ("Schroders Symbology Letter"); letter dated July 25, 2008 from Karrie McMillan, General Counsel, Investment Company Institute ("ICI Symbology Letter"); letter dated July 25, 2008 from Michael Decker, Co-Chief Executive Officer and Mike Nicholas, Co-Chief Executive Officer, Regional Bond Dealers Association ("RBDA Symbology Letter"); letter dated July 25, 2008 from Richard M. Whiting, Executive Director and General Counsel, Financial Services Roundtable ("Roundtable Symbology Letter"); letter dated July 25, 2008 from James H. Gellert, Chairman and CEO and Dr. Patrick J. Caragata, Founder and Executive Vice Chairman, Rapid Ratings International Inc.("Rapid Ratings Symbology Letter"); letter dated July 25, 2008 from James A. Kaitz, President and CEO, Association for Financial Professionals ("AFP Symbology Letter"); letter dated July 25, 2008 from Gregory W. Smith, General Counsel, Colorado Public Employees' Retirement Association ("Colorado PERA Symbology Letter"); letter dated July 25, 2008 from Keith A. Styrcula, Chairman, Structured Products Association ("SPA Symbology Letter"); letter dated July 28, 2008 from Michel Madelain, Chief Operating Officer, Moody's Investors Service ("Moody's Symbology Letter"); letter dated July 28, 2008 from Keith F. Higgins, Chair, Committee on Federal Regulation of Securities and Vicki O. Tucker, Chair, Committee on Securitization and Structured Finance, American Bar Association ("ABA Business Law Committees Symbology Letter"); letter dated July 31, 2008 from Robert S. Khuzami Managing Director and General Counsel, Deutsche Bank Americas ("DBA Symbology Letter"); letter dated August 8, 2008 from Jeffrey A. Perlowitz,

whole,[118] while six commenters expressed either full or conditional support for both parts of the proposed amendment.[119] Eleven commenters argued in favor of adopting paragraph (a) alone, thereby requiring the publication of a report to accompany structured finance ratings and eliminating the paragraph (b) option of using a distinct symbology.[120] Twenty-nine commenters expressed their opposition to adopting paragraph (b).[121]

Commenters criticized the proposed amendment as burdensome[122] and as providing little, if any, benefit to investors.[123] Several commenters argued that the proposed new requirements would be confusing and, therefore, detrimental to

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Managing Director and Co-Head of Global Securitized Markets, and Myongsu Kong, Director and Counsel, Citigroup Global Markets Inc. ("Citi Symbology Letter"); letter dated August 12, 2008 from John J. Niebuhr, Managing Director, Lehman Brothers, Inc. ("Lehman Symbology Letter"); letter dated August 17, 2008 from Olivier Raingeard, Ph.D ("Raingeard Symbology Letter"); letter dated August 22, 2008 from Robert Dobilas, CEO and President, Realpoint LLC ("Realpoint Symbology Letter").

118 See Realpoint Symbology Letter; CMSA Symbology Letter; STRH Symbology Letter; Inland Symbology Letter; Centerline Symbology Letter; Capmark Symbology Letter; Hillenbrand Symbology Letter; DBRS Symbology Letter; JCR Symbology Letter; S&P Symbology Letter; Nappier Symbology Letter; MBA Symbology Letter; MetLife Symbology Letter; AFP Symbology Letter; Moody's Symbology Letter; Raingeard Symbology Letter.

119 See MICA Symbology Letter; Lockyer Symbology Letter; CFA Symbology Letter; RDBA Symbology Letter; Colorado PERA Symbology Letter; MSRB Symbology Letter.

120 See Second SIFMA Symbology Letter; IBFED Symbology Letter; ASF Symbology Letter; Schroders Symbology Letter; ICI Symbology Letter; Principal Symbology Letter; Rapid Ratings Symbology Letter; ABA Business Law Committees Symbology Letter; DBA Symbology Letter; Citi Symbology Letter; Lehman Symbology Letter.

121 See First SIFMA Letter; Realpoint Symbology Letter; CMSA Symbology Letter; STRH Symbology Letter; Inland Symbology Letter; Centerline Symbology Letter; Capmark Symbology Letter; Hillenbrand Symbology Letter; DBRS Symbology Letter; JCR Symbology Letter; S&P Symbology Letter; Second SIFMA Symbology Letter; IBFED Symbology Letter; Nappier Symbology Letter; MBA Symbology Letter; ASF Symbology Letter; Fitch Symbology Letter; MetLife Symbology Letter; Rapid Ratings Symbology Letter; Roundtable Symbology Letter; Schroders Symbology Letter; ICI Symbology Letter; Principal Symbology Letter; AFP Symbology Letter; Moody's Symbology Letter; Raingeard Symbology Letter; ABA Business Law Committees Symbology Letter; DBA Symbology Letter; Citi Symbology Letter; Lehman Symbology Letter.

122 See JCR Symbology Letter; S&P Symbology Letter; Moody's Symbology Letter; Roundtable Symbology Letter.

123 See Realpoint Symbology Letter; Schroders Symbology Letter; Raingeard Symbology Letter; MICA Symbology Letter; Roundtable Symbology Letter.

investors.[124] Others expressed concerns that the proposed amendments would stigmatize structured finance products and further weaken the market for these instruments.[125]

The Commission, like a number of commenters, is concerned that the proposal, if adopted, could have limited utility in encouraging investors to perform more rigorous internal risk analysis on such products because NRSROs likely would have opted to use a distinguishing symbology as the less costly alternative. The Commission is concerned about whether the use of a distinct symbol or identifier for structured finance ratings might not achieve the goal of the proposal: promoting independent analysis and understanding of the distinct risks of structured finance products.

Furthermore, the Commission is concerned that mandating a distinct symbology could create the inaccurate impression that the Commission believes other types of debt instruments are less risky. The Commission believes a more effective way to differentiate credit ratings for structured finance products may be by enhancing investor understanding of the distinct risk characteristics of these debt instruments and their credit ratings. For these reasons, at this time the Commission is deferring consideration of action on the proposal to issue a report or use a distinct symbology at this time. Instead, the Commission wants to study further whether there are other ways to better achieve the goals of the proposal: greater investor awareness of the unique risks of structured finance products and credit ratings for structured finance products.

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124 See CMSA Symbology Letter; STRH Symbology Letter; Inland Symbology Letter; Centerline Symbology Letter; Capmark Symbology Letter; Hillenbrand Symbology Letter; DBRS Symbology Letter; JCR Symbology Letter; ICI Symbology Letter; Principal Symbology Letter; MetLife Symbology Letter; Rapid Ratings Symbology Letter;

125 See First SIFMA Symbology Letter; Realpoint Symbology Letter; Principal Symbology Letter; MBA Symbology Letter; Lockyer Symbology Letter; ASF Symbology Letter; MetLife Symbology Letter; ABA Business Law Committees Symbology Letter; DBA Symbology Letter; Lehman Symbology Letter.

The Commission believes that some differences in the risk characteristics seem readily apparent and are fairly well understood by investors. For example, the Commission believes that an investor would understand that the continued payment of principal and interest to the holder of a structured finance debt instrument typically depends on the performance of a pool of underlying financial assets such as mortgages, business and student loans, or credit card receivables; whereas the performance of a corporate bond typically depends on the issuer's ability to generate income from business operations, and the performance of a municipal bond typically depends on the issuer's ability to collect taxes or earn revenues from services provided by a specific utility such as a sewer or water company.

However, even high-level generalizations about the differences between classes of debt instruments may not always hold true. Some structured finance issuers actively manage the composition of the pool of underlying financial assets (in contrast to a static pool) and, as a result, these products are more risk-sensitive to the discretion of the manager. For example, the performance of the structured finance issuer will depend on the judgment of the manager of the pool of underlying assets. This is similar to how the performance of corporate issuers is sensitive to the judgment of senior management and their boards. Moreover, some corporate issuers – particularly in the financial sector – are highly risk-sensitive to the performance of financial assets similar to structured finance issuers that hold or reference the same types of assets. In short, generalizations about differences that are not carefully crafted run the risk of creating more confusion or misunderstanding than clarity for investors.

For these reasons, the Commission is asking a series of questions below designed to elicit further views from market participants and others on how the risk characteristics of structured finance products and credit ratings differ from the risk characteristics of corporate, municipality, and sovereign nation debt instruments and their credit ratings.[126] Specifically, the Commission requests market participants and others to provide their views in the following four areas: (1) the differences between structured finance products and other debt instruments; (2) the differences between credit ratings for structured finance products and credit ratings for other types of debt instruments; (3) potential measures to communicate differences in structured finance products to investors; and (4) potential measures to communicate differences in structured finance credit ratings to investors.[127]

Persons making submissions are asked to provide detailed explanations of their views and analyses and cite relevant studies.

Differences between structured finance products and other debt instruments

- What do market participants and others believe are the significant differences in the risk characteristics of structured finance debt instruments as compared with debt instruments issued by corporate issuers, municipalities, and sovereign nations in terms of credit risk, market risk, interest rate risk, and liquidity risk? What do market

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126 For the purposes of this request for comment, the Commission intends the term "corporate issuer" to include any issuer that is not a structured finance issuer or a government issuer.

127 For views on some of these issues see, for example, The Role of Credit Rating Agencies in the Structured Finance Markets, May 2008, Technical Committee of the International Organization of Securities Commissioners; The Role of Ratings in Structured Finance: Issues and Implications, (CGFS 2005), January 2005, Committee on the Global Financial System, Bank of International Settlements; The Role of Credit Rating Agencies in Structured Finance, Consultation Paper, February 2008, The Committee of European Securities Regulators.

participants and others believe are the main drivers of the differences in risk characteristics?

- How do market participants and others believe the trading markets for structured finance products compare with the trading markets for debt instruments of corporate issuers, municipalities, and sovereign nations in terms of transparency and providing liquidity to investors? Do market participants and others believe differences in the trading markets for these debt instruments create differing levels of credit risk, market risk, interest rate risk, or liquidity risk for structured finance products as compared with debt instruments issued by corporate issuers companies, municipalities, and sovereign nations?
- How do market participants and others assess the relative use of leverage by structured finance issuers as compared with corporate issuers, municipalities, and sovereign nations? Do differences in the use of leverage create differing levels of credit risk, market risk, interest rate risk, or liquidity risk for structured finance products as compared with debt instruments issued by corporate issuers, municipalities, and sovereign nations? Does leverage act as a driver of differing levels of risk for structured finance products and account for the fact that certain corporate issuers also employ leverage?
- How do market participants and others assess the relative complexity of structured finance issuers as compared with corporate issuers, municipalities, and sovereign nations in terms of capital structure and

operations? For example, in assessing complexity, how do market participants and others account for the fact that a structured finance product can be comprised of a static pool of cash flow assets whereas a corporate issuer may have an array of business lines operated through hundreds of affiliates located around the globe? Do differences in complexity create differing levels of credit risk, market risk, interest rate risk, and liquidity risk for structured finance products as compared with debt instruments issued by corporate issuers, municipalities, and sovereign nations?

- How do market participants and others assess the relative sensitivity of structured finance issuers to macroeconomic factors as compared with corporate issuers, municipalities, and sovereign nations? For example, structured finance products have greater or lesser risk sensitivity to a macroeconomic stress event such as a recession than debt instruments issued by corporate issuers, municipalities, and sovereign nations?
- How do market participants and others assess the relative risks of a sector of structured finance issuers such as issuers that rely on the performance of a particular type of financial asset (e.g., residential mortgages or credit card receivables) as compared with an industry of corporate debt issuers (e.g., financial services, automakers, technology companies, or healthcare providers) or geographically concentrated municipal issuers (e.g., within a state) or sovereign debt issuers (e.g., within a region of the globe)? For example, does a structured finance sector have greater or lesser risk

sensitivity to a macroeconomic stress event such as a recession than corporate debt issuers within a specific industry or geographically concentrated municipal or sovereign issuers?

- How do market participants and others perceive the degree of idiosyncratic risk inherent in structured finance products relative to debt instruments issued by corporate issuers, municipalities, and sovereign nations? Do market participants and others believe the different ways these debt issuers generate income to meet principal and interest payments to debt holders (e.g., through underlying income generating assets for structured finance products, revenues generated through business operations for corporate issuers, and taxing authority or utility revenues for municipal and sovereign issuers) create differing levels of idiosyncratic risk?
- In assessing the relative level of idiosyncratic risk inherent in structured finance issuers as compared with debt instruments issued by corporate issuers, municipalities, and sovereign nations, what do market participants and others believe is the impact of the fact that different structured finance issuers can hold the same types of underlying cash flow generating assets (e.g., residential mortgages) and have very similar legal structures? What is the impact of the fact that corporate issuers can operate using different business models and have differing levels of management competence?
- Do market participants and others believe there are material differences between structured finance products and debt instruments issued by

corporate issuers, municipalities, and sovereign nations in terms of recovery after default? Do market participants and others believe debt holders are likely to recover more or less principal after a structured finance debt instrument defaults than after the default of a debt instrument issued by a corporate issuer, municipality, or sovereign nation?

- Do market participants and others believe there are important differences in the level of moral hazard present in structured finance products relative to debt instruments issued by corporate issuers, municipalities and sovereign nations? Could the fact that structured finance products consist of asset pools which are ultimately purchased from originators of such assets result in lower quality assets for structured finance products as compared with the assets of corporate issuers, municipalities and sovereign nations?
- To the extent that market participants and others identify differences between the risk characteristics of structured finance products and other debt instruments, do they believe the differences identified apply across all types of structured finance products or just to certain categories of products? Are generalizations about the different risk characteristics of structured finance products as compared to other debt instruments appropriate or is it more appropriate to categorize structured finance products by underlying asset type (e.g., residential mortgage, commercial mortgage, student loan, credit card receivable, lease) or structure type (e.g., asset-backed security, collateralized debt obligation (CDO), CDO-

squared or cubed, synthetic or hybrid CDO, constant proportion debt obligation, asset-backed commercial paper conduit)?

Differences between credit ratings for structured finance products and credit ratings for other types of debt Instruments

- What are the significant differences in the risk characteristics of credit ratings for structured finance products as compared with credit ratings for debt instruments issued by corporate issuers, municipalities, and sovereign nations in terms of ratings accuracy and performance?
- Are structured finance debt instruments are inherently more difficult to rate accurately than debt instruments issued by corporate issuers, municipalities, and sovereign nations? If so, what do market participants and others believe are the factors that make structured finance products more difficult to rate?
- Does the fact that the creditworthiness of a structured finance issuer typically depends on the performance of a pool of financial assets makes these debt instruments more difficult to rate accurately than debt instruments issued by corporate issuers, municipalities, and sovereign nations?
- Do market participants and others believe that the reliance on quantitative analysis (e.g., statistical models and historical data) to determine credit ratings for structured finance products as compared with a greater reliance on qualitative analysis to determine credit ratings for debt instruments issued by corporate issuers, municipalities, and sovereign nations

increases or decreases the accuracy risk for structured finance credit ratings?

- Do market participants and others believe that the information available about structured finance issuers used to determine credit ratings as compared to the information available to be used to determine credit ratings about corporate issuers, municipalities, and sovereign nations makes it more difficult to determine accurate credit ratings for structured finance debt instruments and/or to conduct surveillance on outstanding structured finance credit ratings? If so, do market participants and others believe it is easier to determine accurate credit ratings, and monitor those ratings, for corporate issuers that are required to file periodic public reports and financial statements and provide access to management? Is the information used to determine and monitor credit ratings of corporate issuers, municipalities, or sovereign nations more forward looking (e.g., based on more on forecasts)? In addition, do market participants and others believe that the historical data used to determine and monitor structured finance credit ratings of shorter duration or otherwise less robust than the historical data used to determine and monitor credit ratings for corporate issuers, municipalities, or sovereign nations?
- Do market participants and others believe it is more difficult for investors and market observers to perform independent analysis of structured finance products than of securities issued by corporate issuers, municipalities, and sovereign nations? If so, does this impact the accuracy

of structured finance credit ratings as compared to credit ratings for corporate issuers, municipalities, and sovereign nations?

- Do market participants and others believe the conflict of being paid to determine credit ratings is more attenuated in the structured finance sector than in the corporate, municipal, and sovereign sectors? If so, why? Does this impact the accuracy of structured finance credit ratings?
- Do market participants and others believe structured finance credit ratings are more likely to have a greater number of ratings transitions (i.e., upgrades or downgrades) than credit ratings for debt instruments issued by corporate issuers, municipalities, or sovereign nations? If so, what are the factors that create this effect?
- Are structured finance credit ratings more likely to experience transitions of greater magnitude (i.e., upgrades or downgrades that span a larger number of credit rating categories (notches)) than credit ratings for debt instruments issued by corporate issuers, municipalities, or sovereign nations? If so, what are the factors that make structured finance credit ratings more prone to transitions of greater magnitude in credit rating category?
- Do market participants and others believe issuers, arrangers, sponsors, and managers of structured finance products are able to "game" rating agency methodologies resulting in credit ratings that are less accurate than ratings for other debt instruments? Do they believe the ability of issuers, arrangers, sponsors and managers to adjust the characteristics of structured

finance products, including the number and relative size of tranches and the composition of the asset pool in order to achieve particular credit ratings, result in ratings that are less accurate than ratings for debt instruments issued by corporate issuers, municipalities and sovereign nations?

- To the extent that market participants and others identify differences between the risk characteristics of structured finance credit ratings and credit ratings for other debt instruments, do differences identified apply globally to all structured finance products or just to certain categories of products? Do market participants and others believe generalizations about the different risk characteristics of credit ratings for structured finance products as compared to credit ratings for other debt instruments can be made? Is it more appropriate to categorize structured finance credit ratings by underlying asset type (e.g., residential mortgage, commercial mortgage, student loan, credit card receivable, lease) or structure type (e.g., asset-backed security, collateralized debt obligation (CDO), CDO-squared or cubed, synthetic or hybrid CDO, constant proportion debt obligation, asset-backed commercial paper conduit)?

<u>Measures to communicate differences in structured finance products to investors</u>

- To the extent that market participants and others identified significant differences in the risk characteristics of structured finance debt instruments as compared with debt instruments issued by corporate issuers, municipalities, and sovereign nations in terms of credit risk,

market risk, interest rate risk, and liquidity risk, what are their views on whether steps should be taken to better communicate these differences to investors in a manner reasonably designed to enhance investor understanding of the differences?

- Do market participants and others believe structured finance issuers should be required to disclose these general differences in the types of securities? If so, how should the disclosures be made? For example, should they be stated in offering documents and periodic reports or are there other mechanisms that could be used to convey the differences in the types of securities?
- Do market participants and others believe NRSROs should be required to disclose these differences? If so, how should the disclosures be made? For example, should the disclosures be included in a report issued at the same time a rating action is taken with respect to a structured finance product, in Form NRSRO, or through some other mechanism?
- Do market participants and others believe the disclosure documents should required to be delivered to prospective investors in investment pools that may hold structured finance products be required to include these disclosures? If so, how should these disclosures be made?

<u>Measures to communicate differences in structured finance credit ratings to investors</u>

- To the extent that market participants and others identified material differences in the risk characteristics of credit ratings for structured finance debt instruments as compared with credit ratings for debt

instruments issued by corporate issuers, municipalities, and sovereign nations in terms of ratings accuracy and performance, what are their views on measures that can be taken to communicate these differences to investors in a manner reasonably designed to enhance investor understanding of the differences?

- Do market participants and others believe structured finance issuers should be required to disclose these differences? If so, how should the disclosures be made? Should they be stated in offering documents and periodic reports, or are there other mechanisms that could be used to convey the disclosures?
- Do market participants and others believe NRSROs should be required to disclose these differences? For example, it has been suggested that NRSRO disclose the following types of information about structured finance products:[128]

    1. The diligence that is performed by or provided to the NRSRO about the underlying assets, and quality control of numerical data provided to the NRSRO;
    2. The characteristics and sensitivities of models used or relied upon by the NRSRO in assessing the likely performance of the structured finance product or the underlying assets;
    3. The extent to which the NRSRO relies on representations and warranties made by transaction participants;

[128] See e.g., June 25, 2008 Letter from Jeff Riefsnyder and Richard Johns on behalf of the American Securitization Forum to the US Securities and Exchange Commission regarding "Exchange Act Release No. 34-57967 (File No. S7-13-08)".

4. The assumptions as to future events and economic conditions that are embedded in the analytical models used by the NRSRO in arriving at a given rating;

5. Publishing "what if" scenario analyses that address the ratings implications of changes in the underlying assumptions upon which ratings are based and provide insight into ratings tolerance to changing economic or risk circumstances;

6. Providing additional information relating to default probability, loss sensitivity, severity of loss given default, short-tail and long-tail risk and similar risk metrics associated with each class of credit ratings.

- If you believe these types of disclosures and other disclosures should be made by NRSROs, how should the disclosures be made? Should the disclosures be stated in a report issued at the same time a rating action is taken with respect to a structured finance product, in Form NRSRO, or through some other mechanism?
- Do market participants and others believe the disclosure documents required to be delivered to prospective investors in investment pools that may hold structured finance products should be required to include the disclosures? If so, how should the disclosures be made?

B. Credit Ratings for Existing Structured Finance Debt Instruments

Another way to differentiate credit ratings for structured finance products from other types of debt instrument ratings is to increase the opportunity for independent

analysis of the credit worthiness of the products To this end, in the companion release, the Commission is adopting amendments to Rule 17g-5 that require NRSROs that are paid by arrangers to determine credit ratings for structured finance products to provide other NRSROs access to a password protected Internet Web site that lists each deal they have been hired to rate. A hired NRSRO also would be required to obtain representations from the arranger hiring the NRSRO that the arranger will maintain a password protected Internet Web site that contains all the information the arranger provides to the hired NRSRO to determine and monitor the credit rating and that it will make this information available to NRSROs not hired to determine and monitor the rating. As discussed in detail in the Commission's Companion Release, these requirements are designed to create a mechanism by which non-hired NRSROs will be able to access the NRSRO Internet Web sites to learn of new deals being rated and then access the arranger Internet Web sites to obtain the information provided by the arranger to the hired NRSRO during the entire initial rating process and, thereafter, for the purpose of surveillance.[129] The hired NRSRO need only provide access to its password-protected Internet Web site to a non-hired NRSRO whose certification provided to the Commission indicates that it has either (1) determined and maintained credit ratings for at least 10% of the issued securities and money market instruments for which it accessed information pursuant to Rule 17g-5(a)(3) as amended in the calendar year prior to the year covered by the certification, if it accessed such information for 10 or more issued securities or money market instruments; or (2) has not accessed information pursuant to Rule 17g-5(a)(3) as amended 10 or more times in the calendar year prior to the year covered by the certification. NRSROs also will be required to disclose in their certifications the number of deals for which they

[129] See Companion Release.

obtained information through accessing the Internet Web sites and the number of ratings they issued using that information during the most recent calendar year during which it obtained information through accessing these Internet Websites certification or that they previously had not accessed such information 10 or more times in a calendar year.

These amendments to Rule 17g-5 described above are designed to allow NRSROs not hired to rate a structured finance deal to get sufficient information to determine a credit rating for the debt instruments to be issued. Generally, the information relied on by the hired NRSROs to rate new debt issuances of structured finance issuers is non-public. This makes it difficult for other NRSROs to rate these securities and money market instruments. As a result, the products frequently are issued with ratings from only one or two NRSROs and only by NRSROs that are hired by the issuer, sponsor, or underwriter (i.e., NRSROs that may be subject to the conflict of being repeatedly paid by certain arrangers to rate these securities and money market instruments).

The rule amendments also are designed to require the disclosure of the necessary information to any NRSRO – whether hired or not – to permit non-hired NRSROs to determine credit ratings for the debt instruments to be issued. The Commission believes that absent this requirement a non-hired NRSRO would have a much more difficult time obtaining the information necessary to issue an unsolicited credit rating at the time the debt instruments were issued into the market. Without the rule amendment, in most cases, the non-hired NRSRO's prospects for determining a pre-issuance credit rating would depend on the issuer's willingness to provide the information to the NRSRO notwithstanding the fact that the issuer was paying other NRSROs to rate the to-be-issued debt instruments.

The goal is to increase the number of credit ratings extant for a given structured finance security or money market instrument and, in particular, promote the issuance of credit ratings by NRSROs that are not hired by the arranger. This is designed to provide users of credit ratings with a broader range of views on the creditworthiness of the security or money market instrument. In addition, the rule amendments are designed to make it more difficult for arrangers to exert influence over the NRSROs they hire to determine credit ratings for structured finance products. By opening up the rating process to more NRSROs, the rule amendments make it easier for the hired NRSRO to resist such pressure by increasing the likelihood that any steps taken to inappropriately favor the arranger could be exposed to the market through the credit ratings issued by other NRSROs.

As the Commission noted in the February 2009 Proposing Release, the text of paragraph (a)(3)(i) refers to transactions where the NRSRO is in the process of determining an "initial" credit rating.[130] The rule does not require the NRSRO to include on the Internet Web site information about securities or money market instruments once the NRSRO has published the initial rating and is monitoring the rating. The amendment is designed to alert other NRSROs about new deals and direct them to the Internet Web site of the arranger where information to determine initial ratings and monitor the ratings can be accessed. Consequently, upon publication of the initial rating, the NRSRO can remove the information about the security or money market instrument from the list it maintains on the Internet Web site. Similarly, if the arranger decides to terminate the

130 See February 2009 Proposing Release, 74 FR at 6493.

rating process before a hired NRSRO publishes an initial rating, the NRSRO would be permitted to remove the information from the list.[131]

The Commission is aware that there are conflicting characterizations about the ability of market participants and others, including NRSROs not hired to rate the deal, to obtain information necessary to determine and monitor a credit rating for structured finance debt instrument after issuance. The Commission understands that some of the trustees and servicers involved with the structured finance issuer provide monthly reports that allow NRSROs not hired to rate the issuer's debt instruments to determine and monitor credit ratings for those securities and money market instruments. The Commission also understands that some third-party venders aggregate the information provided by the trustees and servicers in a manner that permits independent credit analysis by NRSROs and investors. The Commission understands that some market participants argue that the trustees and servicers restrict access to the information to investors and hired NRSROs and that the third-party venders do not provide sufficient information.

The Commission believes it would be helpful to solicit comments from market participants and others as to whether measures should be taken by the Commission to enhance the ability of non-hired NRSROs to determine credit ratings for structured finance debt instruments that were issued before the compliance date of the amendments to Rule 17g-5 being adopted in the Companion Release.

For these reasons, the Commission is asking a series of questions below designed to elicit comments from market participants and others about whether currently there is sufficient information (or access to such information) to permit an NRSRO to determine

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131 See Companion Release.

unsolicited credit ratings for structured finance debt instruments issued prior to the compliance date of the amendments to Rule 17g-5 being adopted today.

Persons making submissions are asked to provide detailed explanations and analyses and cite relevant studies.

- Do market participants and others believe the ability of NRSROs to access information about structured finance debt instruments issued before the compliance date for the Rule 17a-5 amendments ("compliance date") is restricted in such a manner as to preclude or seriously discourage NRSROs from determining credit ratings if they have not been hired by the arranger? Do the issuers, trustees and servicers that control access to this information preclude a non-hired NRSRO from accessing the information or impose barriers that discourage a non-hired NRSRO from accessing it?
- Do market participants and others believe the information disclosed by structured finance issuers, trustees, and servicers or by third-party venders is insufficient to determine unsolicited credit ratings for structured finance debt instruments issued before the compliance date?
- What specific measures, if any, should be taken to secure the disclosure of information by issuers, trustees or servicers of structured finance products issued before the compliance date or the NRSROs that were hired to rate those structured finance products to enable NRSROs that were not hired to determine and monitor a credit rating where the debt instrument was issued prior the compliance date?
- Do market participants and others believe if the information provided to the hired NRSRO to determine and monitor a credit rating for a structured finance product

issued before the compliance date was made available to another NRSRO, the non-hired NRSRO would be able to determine a meaningful unsolicited credit using that information alone?

VII. GENERAL REQUEST FOR COMMENT

The Commission invites interested persons to submit written comments on any aspect of the proposed amendments, in addition to the specific requests for comments. Further, the Commission invites comment on other matters that might have an effect on the proposal contained in the release, including any competitive impact.

VIII. PAPERWORK REDUCTION ACT

Certain provisions of the proposed amendments to Rule 17g-3 and the Instructions to Exhibit 6 to Form NRSRO, as well as the new proposed Rule 17g-7 contain a "collection of information" within the meaning of the Paperwork Reduction Act of 1995 ("PRA"). The Commission is submitting the proposed amendments and the proposed new collection to the Office of Management and Budget ("OMB") for review in accordance with the PRA. An agency may not conduct or sponsor, and a person is not required to comply with, a collection of information unless it displays a currently valid control number. The titles for the collections of information are:

(1) Rule 17g-3, Annual reports to be furnished by nationally recognized statistical rating organizations (OMB Control Number 3235-0626);

(2) Rule 17g-1, Application for registration as a nationally recognized statistical rating organization; Form NRSRO and the Instructions for Form NRSRO (OMB Control Number 3235-0625); and

(3) Rule 17g-7, Reports to be made public by nationally recognized statistical rating organizations about persons that paid the nationally recognized statistical rating organization for the issuance or maintenance of a credit rating (a proposed new collection of information).

A. Collections of Information under the Proposed Rule Amendments

The Commission is proposing for comment rule amendments to prescribe additional requirements for NRSROs. The proposed amendments to Rule 17g-3 would require an NRSRO to submit an additional annual report to the Commission. The proposed amendments to Rule 17g-3 would require an NRSRO to furnish a new unaudited report describing the steps taken by the NRSRO's designated compliance officer during the fiscal year to administer the policies and procedures that are required to be established pursuant to paragraphs (g) and (h) of Section 15E of the Exchange Act (prevention of misuse of material nonpublic information and management of conflicts of interest), and to ensure compliance with the securities laws and rules and regulations thereunder.[132] The proposed amendment to Rule 17g-3 also would require that the report include a description of any compliance reviews of the activities of the NRSRO; the number of material compliance matters identified during each review of the activities of the NRSRO and a brief description of each such matter; a description of any remediation measures implemented to address material compliance matters identified during the reviews of the activities of the NRSRO; and a description of the persons within the NRSRO who were advised of the results of the reviews.[133]

In addition, proposed amendments to the Instructions to Exhibit 6 to Form NRSRO would require an applicant/NRSRO to furnish the Commission with information regarding the revenues an NRSRO receives from major clients and from services other than determining credit ratings. Finally, proposed Rule 17g-7 would require an NRSRO, on an annual basis, to make publicly available on its Internet Web site a consolidated

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132 See proposed Rule 17g-3(a)(7).

133 See proposed Rule 17g-3(a)(7)(ii). The proposed report also would be certified by the designated compliance officer. See proposed Rule 17g-3(b)(2).

report that shows certain information with respect to each person that paid the NRSRO to issue or maintain a credit rating. First, the NRSRO must include the percent of the net revenue attributable to the person earned by the NRSRO for that fiscal year for providing services and products other than credit rating services. Second, the NRSRO must include the relative standing of the person in terms of the person's contribution to the net revenue of the NRSRO for the fiscal year. Third, the NRSRO must include all outstanding credit ratings paid for by the person.[134]

B. Proposed Use of Information

The collections of information in the proposed amendments to Rule 17g-3 to add an additional unaudited report to describe the steps taken by the designated compliance officer during the fiscal year to administer certain policies and procedures and to ensure compliance with securities laws and rules and regulations would improve the integrity of the ratings process by establishing a discipline under which the NRSRO's designated compliance officer would need to report to the Commission the steps taken by the compliance officer to fulfill the officer's statutory responsibilities. The act of reporting these steps is designed to promote the active engagement of the designated compliance officer in reviewing an NRSRO's compliance with internal policies and procedures. The proposed report also could strengthen the Commission's oversight of NRSROs by highlighting possible problem areas in an NRSRO's rating processes and providing an additional tool for the Commission to monitor how the NRSRO's designated compliance officer is fulfilling the responsibilities prescribed in Section 15E(j) of the Exchange Act. In addition, with respect to the proposed amendments to Rule 17g-3, the identification of

134 See proposed Rule 17g-7.

the persons within the NRSRO advised of the results of the review could also promote the appropriate escalation of compliance issues to the management of the NRSRO.

Further, the collections of information in the proposed amendments to Exhibit 6 to the Instructions to Form NRSRO would allow users of credit ratings to more effectively evaluate the integrity of the NRSRO's credit ratings themselves and whether they believe the NRSRO is effectively managing its conflicts of interests otherwise identified in Exhibit 6. The collection of information in proposed new Rule 17g-7 would provide users of credit ratings with information about the potential conflicts of interest that arises when an NRSRO is paid to determine a credit rating for a specific obligor, security, or money market instrument.

Finally, the collections of information in the proposed amendments also are designed to further assist the Commission in effectively monitoring, through its examination function, whether an NRSRO is conducting its activities in accordance with Section 15E of the Exchange Act[135] and the rules thereunder.

C. Respondents

In adopting the original rules under the Rating Agency Act, as well as additional rules in February 2009, the Commission estimated that approximately 30 credit rating agencies would be registered as NRSROs.[136] The Commission believes that this estimate continues to be appropriate for identifying the number of respondents for purposes of the amendments and the proposed new rule. Since the original rules under the Rating Agency Act became effective in June 2007, ten credit rating agencies have registered

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135 15 U.S.C. 78o-7.

136 See June 2007 Adopting Release, 72 FR at 33607.

with the Commission as NRSROs.[137] The rules regarding the registration have been in effect for just over two years; consequently, the Commission expects additional entities will register.

The Commission generally requests comment on all aspects of these estimates for the number of respondents. In addition, the Commission requests specific comment on the following items related to these estimates.

- For purposes of the PRA should the Commission continue to use the estimate that 30 credit rating agencies will register as NRSROs?
- Alternatively, should the Commission raise or lower that number, given that ten credit rating agencies have registered with the Commission as NRSROs in the two years that the NRSRO registration program has been in effect? If so, what should the number be? Commenters should explain how they arrived at the estimate and identify any sources of industry information used in arriving at the estimate.

Commenters should provide specific data and analysis to support any comments they submit with respect to these estimates with respect to the number of respondents.

D. Total Annual Recordkeeping and Reporting Burden

As discussed in further detail below, the Commission estimates the total recordkeeping burden resulting from the proposed rule amendments and proposed new rule would be approximately 2,760 hours[138] on an annual basis and 4,650 hours[139] on a one-time basis.

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137 A.M. Best Company, Inc.; DBRS Ltd.; Fitch.; Japan Credit Rating Agency, Ltd.; Moody's; Rating and Investment Information, Inc.; S&P; LACE Financial Corp.; Egan-Jones Rating Company; and Realpoint LLC.

138 900 + 60 + 1,800 = 2,760.

The total annual and one-time hour burden estimates described below are averages across all types of NRSROs expected to be affected by the proposed rule amendments. The size and complexity of NRSROs range from small entities to entities that are part of complex global organizations employing thousands of credit analysts. Consequently, the burden hour estimates represent the average time across all NRSROs. The Commission further notes that, given the significant variance in size between the largest NRSROs and the smallest NRSROs, the burden estimates, as averages across all NRSROs, are skewed higher because the largest firms currently predominate in the industry.

1. Proposed Amendments to Rule 17g-3

Rule 17g-3 requires an NRSRO to furnish certain reports to the Commission on an annual basis, including audited financial statements, as well as other annual reports.[140] The Commission is proposing to amend Rule 17g-3 to require an NRSRO to furnish the Commission with an additional unaudited report containing a description of the steps taken by the designated compliance officer during the fiscal year to administer the policies and procedures that are required to be established pursuant to paragraphs (g) and (h) of Section 15E of the Exchange Act (management of conflicts of interest and prevention of the misuse of material nonpublic information); and ensure compliance with the securities laws and rules and regulations thereunder, including those promulgated by the Commission pursuant to Section 15E of the Exchange Act.[141]

Proposed new paragraph (a)(7)(ii) of Rule 17g-3 also would provide that the report must include: (1) a description of any compliance reviews of the activities of the

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139 750 + 3,900 = 4,650.

140 17 CFR 240.17g-3.

141 See proposed Rule 17g-3(a)(7)(ii).

NRSRO; (2) the number of material compliance matters identified during each review of the activities of the NRSRO and a brief description of each such matter; (3) a description of any remediation measures implemented to address material compliance matters identified during the reviews of the activities of the NRSRO; and (4) a description of the persons within the NRSRO who were advised of the results of the reviews.

The total annual burden currently approved by OMB for Rule 17g-3 is 7,000 hours.[142] The current annual hour burden estimate to prepare and file the annual reports under Rule 17g-3 is 200 hours per respondent, including the audited financial statements under Rule 17g-3(a)(1).[143] With respect to the proposed amendment, the Commission estimates, based on staff experience, that the amount of time it would take to prepare a report describing the steps taken by the designated compliance officer during the fiscal year to administer the policies and procedures that are required to be established pursuant to paragraphs (g) and (h) of Section 15E of the Exchange Act (management of conflicts of interest and prevention of the misuse of material nonpublic information); and to ensure compliance with the securities laws and rules and regulations thereunder, would be approximately 30 hours per year for a total annual hour burden of 900 hours.[144]

The Commission based this estimate, in part, on the fact that the areas covered by the proposed amendment to Rule 17g-3 overlap with the duties already required of the NRSRO's designated compliance officer pursuant to Section 15E(j) of the Exchange Act. The Commission preliminarily believes that the estimated hour burden under the

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142 See February 2009 Adopting Release, 74 FR at 6473.

143 See February 2009 Adopting Release, 74 FR at 6472. The Commission based this proposed estimate, in part, on the average number of annual hours (200 hours) divided by the number of annual reports required to be prepared under current Rule 17g-3(a)(1)-(6): 200 annual hours/6 reports = 33.33 hours (rounded to 30 hours).

144 30 hours x 30 NRSROs = 900 hours.

proposed amendment to Rule 17a-3 would include the time it would take to compile information to draft the report and the preparation and filing of the report itself. In addition, this one-time hour burden estimate also includes the time it would take to identify and describe material compliance matters, any remediation and the persons advised of the results of the reviews. Consequently, the Commission also based this estimate, in part, on the average estimated number of hours it would currently take an NRSRO to complete one annual report under current Rule 17g-3 (i.e., approximately 30 hours).[145]

Given the potentially sensitive nature of the proposed report, the Commission also preliminarily believes that an NRSRO would likely engage outside counsel to assist it in the process of drafting and reviewing the proposed report under Rule 17g-3. The Commission estimates that the time an outside attorney would spend on this work would depend on the size and complexity of the NRSRO. The Commission estimates that, on average, an outside counsel would spend approximately 20 hours assisting an NRSRO and its designated compliance officer in drafting and reviewing the proposed report on a one-time basis for an aggregate burden to the industry of 600 hours.[146] Based on industry sources, the Commission estimates that the cost of an outside counsel would be approximately $400 per hour. For these reasons, the Commission estimates that the

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145 15 U.S.C. 78o-7(j). Under this provision of the statute, an NRSRO must "designate an individual responsible for administering the policies and procedures that are required to be established pursuant to [Sections 15E(g) and (h) of the Exchange Act (15 U.S.C. 78o-7(g) and (h))], and for ensuring compliance with the securities laws and rules and regulations thereunder, including those promulgated by the Commission pursuant to [Section 15E of the Exchange Act]." Id.

146 30 NRSROs x 20 hours = 600 hours.

average one-time cost to an NRSRO would be approximately $8,000[147] and the one-time cost to the industry would be approximately $240,000.[148]

The Commission generally requests comment on all aspects of the burden estimates for the proposed amendments to Rule 17g-3. Commenters should provide specific data and analysis to support any comments they submit with respect to these burden estimates. In addition, the Commission requests specific comment on the following items related to these estimates.

- To what extent would NRSROs rely on outside counsel with respect to the preparation, drafting and review of the proposed report?

2. Amendments to Form NRSRO

The Commission is proposing to amend the Instructions to Exhibit 6 to Form NRSRO to require an applicant/NRSRO to furnish the Commission with information regarding the revenues an NRSRO receives from major clients and from services other than determining credit ratings.

As stated above, the Commission proposes amending the instructions for Exhibit 6 to augment the information about conflicts of interest disclosed in Form NRSRO. The Commission prescribed the information currently required in Exhibit 6 to implement Section 15E(a)(1)(B)(vi) of the Exchange Act, which requires that an application for registration contain information regarding any conflict of interest relating to the issuance of credit ratings by the applicant/NRSRO.[149] The proposed amendments to Form NRSRO would change the instructions for the Form to require that NRSROs provide specific disclosure of certain percentages of its revenue related to its large customers and services it

147 $400 per hour x 20 hours = $8,000.
148 $8,000 x 30 NRSROs = $240,000.
149 15 U.S.C. 78o-7(a)(1)(B)(vi).

provides, other than the issuance of credit ratings, in Exhibit 6 to the Form. The Commission preliminarily believes that an NRSRO would generate the financial information and complete the proposed new additional disclosures required by Exhibit 6 to Form NRSRO using internal records and current NRSRO personnel.

The total annual burden currently approved by OMB for Rule 17g-1 and Form NRSRO is 6,400 hours.[150] Based on staff experience, the Commission estimates that the average time necessary for an applicant or NRSRO to gather the information for the first time in order to complete the additional disclosures that would be required by the proposed amendments to Exhibit 6 to Form NRSRO would be 25 hours per NRSRO, which would be a one-time hour burden to the industry of 750 hours.[151] The Commission preliminarily believes, based on staff experience, that the average time it would take an NRSRO to complete the additional disclosures that would be required by the proposed amendments would be comparable to the current estimate of 25 hours that it would take an NRSRO to complete an amendment to a Form NRSRO.[152] The Commission preliminarily believes that these burden estimates would be comparable because, based on the staff's experience with Form NRSRO filings furnished to the Commission over the past two years, the Commission believes that time and amount of information involved in filing an amendment to part of the Form NRSRO would be similar to the time involved to update the Form NRSRO with the proposed information to Exhibit 6 to Form NRSRO.

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150 2,100 annual hours + [13,000 one-time hours annualized over the three year approval period/3] = 6,433 hours = rounded to 6,400 hours.

151 30 NRSROs x 25 hours = 750 hours. The Commission also notes that the currently approved PRA collection for Rule 17g-1 and Form NRSRO includes an estimate that an outside counsel would spend approximately 40 hours assisting a credit rating agency in the process of completing and furnishing a Form NRSRO to the Commission. June 2007 Adopting Release, 72 FR at 33608. The Commission believes that any outside counsel review of the amendments to Exhibit 6 to Form NRSRO would de minimis and therefore the current estimate remains accurate.

152 See June 2007 Adopting Release, at 72 FR 33609.

In addition, the proposed amendments to the Instructions to Exhibit 6 would provide that after registration, an NRSRO with a fiscal year end of December 31 must update the proposed additional disclosures in Exhibit 6 information as part of its annual certification. Rule 17g-1(f) requires an NRSRO to furnish the annual certification no later than 90 days after the calendar year.[153] The currently approved OMB annual hour estimate to complete the annual certification is 10 hours per NRSRO, for a total aggregate annual hour burden to the industry of 300 hours. The Commission estimates that once an NRSRO completes its first annual certification with the additional proposed disclosures required in the Instructions to Exhibit 6 to Form NRSRO that the completion of subsequent annual certifications, generally, would take less time because the additional disclosures proposed to be required would be furnished on a regular basis (albeit yearly) and, therefore, become more a matter of routine over time. Consequently, the Commission believes that the annual certifications with the proposed additional discloses would take more time to complete in the first year the rule would become effective, than it would take to complete in subsequent years.

Therefore, based on staff experience, the Commission estimates that with the additional disclosures proposed to be contained in Instructions to Exhibit 6 to Form NRSRO, the annual hour burden for each NRSRO to complete the annual certification would increase 2 hours per year, from 10 to 12 hours, for a total aggregate annual hour

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153 17 CFR 240.17g-4(f). The Commission also notes that if an NRSRO has an annual year end other than December 31st, the proposed additional instructions Exhibit 6 to Form NRSRO would require that the NRSRO file an Update of Registration no later than 90 days following the end of the NRSRO's fiscal year. The Commission believes that the annual hour burden for this proposed collection of information is encompassed within the time it would take an NRSRO to file an amendment to the Form NRSRO which has been estimated to be a 25 annual hour burden per year. The Commission estimates that an NRSRO will on average file two amendments to Form NRSRO per year.

burden of 360 hours, resulting in an increase to the estimated annual hour burden for Rule 17g-1 and Form NRSRO of 60 hours.[154]

The Commission preliminarily believes that an applicant/NRSRO would incur only limited internal costs to modify its systems to generate and disclose the proposed additional disclosures in Exhibit 6 to Form NRSRO because an applicant/NRSRO is already required to generate similar financial information in other parts of Form NRSRO and certain financial reports required under Rule 17g-3.

The Commission generally requests comment on all aspects of these proposed burden estimates for Rule 17g-1 and Form NRSRO, as proposed to be amended. Commenters should provide specific data and analysis to support any comments they submit with respect to these burden estimates.

3. Proposed Rule 17g-7

The Commission is proposing new Rule 17g-7, which would require an NRSRO, on an annual basis, to make publicly available on its Internet Web site a consolidated report that would contain certain information about the revenues earned by the NRSRO for providing products and services to any obligor, issuer, underwriter, sponsor, and subscriber that paid the NRSRO to issue or maintain the credit rating. In order to generate the report as required by proposed paragraph (a)(1) of Rule 17g-7, the NRSRO would have to perform two calculations and identify any outstanding credit ratings at the end of the fiscal year.

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[154] 12 hours x 30 NRSROs = 360 hours. The Commission also based this estimate, in part, on the time it would take an NRSRO to furnish a withdrawal of registration on Form NRSRO of 1 hour. June 2007 Proposing Release, 72 FR at 33608-33609. However, because the NRSRO would have to update information for calculations with respect to its revenues, the Commission believes it would take an NRSRO longer than 1 hour. Therefore, the Commission preliminarily believes that it would take an NRSRO approximately 2 hours each year to update the proposed information.

As proposed under new Rule 17g-7, an NRSRO would be required to perform a calculation to state the percentage of net revenue earned by the NRSRO from providing services to the entity that is derived from services other than credit ratings attributable to each person that paid the NRSRO for the issuance or maintenance of a credit rating.

The second calculation that the NRSRO would be required to perform to generate the report once a year as described in paragraph (a)(1)(i) of proposed Rule 17g-7 would require the NRSRO to derive and state the relative standing of the entity as a contributor of revenues to the NRSRO as compared to other entities that contribute revenue to the NRSRO. In particular, the NRSRO would need to identify which of the following cohorts of contributors to the annual net revenue of the NRSRO the entity is included in: top 10%, top 25%, top 50%, bottom 50%, bottom 25%. Finally, once a year an NRSRO would also be required to identify all outstanding credit ratings paid for by the person, which the NRSRO must identify by name of obligor, security, or money market instrument and, as applicable, CIK number, CUSIP, or ISIN.

The Commission also notes that paragraph (a)(2) of proposed Rule 17g-7 would exempt an NRSRO from publishing the reports if, as of the end of the fiscal year, the NRSRO had no credit ratings outstanding that the NRSRO issued or maintained as a result of a person paying the NRSRO for the issuance or maintenance of the credit ratings.[155]

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155 For purposes of this collection of information, the Commission has determined that it would preliminarily use 30 respondents in calculating the burden estimates. While some subscriber-based NRSROs would be exempt from new Rule 17g-7, the Commission has preliminarily determined to include all 30 respondents because if a subscriber-paid NRSRO was specifically requested to issue a rating, the NRSRO would no longer be exempt from Rule 17g-7. Therefore, the Commission preliminarily believes that this approach would result in an appropriate PRA estimate for new Rule 17g-7.

For purposes of the PRA, based on staff experience, the Commission estimates that it would take an NRSRO approximately 100 hours on a one-time basis to develop the calculations necessary to generate the percents required under the report under proposed Rule 17g-7; to populate the proposed report with the required data; and to develop and draft the form report. Additionally, the Commission is basing this one-time hour burden estimate on the Commission's experience with, and burden estimates for, Rules 17g-1 through 17g-6, given that the NRSRO rules have been in effect for over two years.[156] More specifically, the Commission notes that the current one-time hour burden estimates under the PRA for an NRSRO to file a Form NRSRO is 400 hours, and to file an amendment to Form NRSRO is 25 hours.[157]

The Commission preliminarily believes that the report to be required under proposed Rule 17g-7 would be more complex and comprehensive to complete than a typical amendment to Form NRSRO because the new proposed rule would require an NRSRO to calculate percents for every person that paid the NRSRO for the issuance or maintenance of a credit rating. In contrast, however, the Commission preliminarily does not believe that the one-time hour burden to comply with the new Rule 17g-7 would be as extensive and time consuming as the time necessary to complete the initial Form NRSRO. Therefore, the Commission preliminarily believes that the estimate of a one-time burden of 100 hours per respondent is conservative and reasonable given the significant variance in size between the largest NRSROs and the smallest NRSROs. Thus, based on staff experience, the Commission preliminarily estimates that the

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156 See generally, June 2007 Adopting Release.

157 June 2007 Adopting Release, 72 FR at 33609; see also February 2009 Adopting Release, 74 FR at 6,470.

aggregate initial one-time hour burden to complete the report required by proposed Rule 17g-7 would be 3,000 hours for 30 NRSROs.[158]

In addition to the one-time hour burden, proposed new Rule 17g-7 also would result in an annual hour burden for an NRSRO to generate the percents required under the proposed report and to populate the proposed report with the required data once a year. The Commission notes that an NRSRO would have already developed the equations necessary to generate the percents in order to comply with the new Rule 17g-7 in the first year. Additionally, the Commission believes that once an NRSRO complies with Rule 17g-7 in the first year, that preparation of the new annual report would become more routine. Therefore, based on staff experience, the Commission estimates that it would take an NRSRO approximately 50 hours per year to generate the percents required under the proposed report, as well as to generate the report itself.[159] Thus, the Commission preliminarily estimates that this would result in a total annual hour burden of 1,500 hours for 30 NRSROs.[160]

Proposed Rule 17g-7 also would require an NRSRO to make publicly available on its Internet Web site the report required under paragraph (a)(1).[161] The Commission estimates that it would take an NRSRO approximately 30 hours to disclose the initial information in its Web site for a total one-time burden of 900 hours,[162] and thereafter 10

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158 100 hours x 30 NRSROs = 3,000 hours.

159 The Commission based this estimate, in part, on the number of estimated hours it would take an NRSRO to file an amendment to Form NRSRO of 25 hours. The Commission, however, preliminarily believes that it would take an NRSRO substantially more time to generate the information once a year to complete the proposed report under proposed Rule 17g-7. Therefore, the Commission preliminarily estimates that the average time necessary to complete the report under proposed Rule 17g-7 would be more comparable to the time it would take an NRSRO to file 2 amendments to Form NRSRO, or 50 hours (2 x 25 hours).

160 50 hours x 30 NRSROs = 1,500 hours.

161 See proposed Rule 17g-7(a)(1).

162 30 hours x 30 NRSROs = 900 hours.

hours per year to disclose updated information for a total annual burden of 300 hours.[163] This one-time hour burden is estimated in part based on the current one-time and annual burden hours for an NRSRO to publicly disclose its Form NRSRO. [164] Accordingly, the Commission estimates that implementation of proposed new Rule 17g-7 would result in a total one-time hour burden of 3,900[165] hours and a total annual hour burden of 1,800 hours.[166]

The Commission also believes that an NRSRO may need to purchase and/or modify its software and operating systems in order to generate and publish the information proposed to be required in the report in proposed new Rule 17g-7. The Commission estimates that the cost of any software incurred in connection with its systems modifications would vary based on the size and complexity of the NRSRO. The Commission estimates that some NRSROs would not need such software because they may already have such systems in place to generate the proposed report, or given their small size, other NRSROs may find the purchase of additional software unnecessary. The Commission preliminarily believes that an NRSRO would be able to generate and compile the information for the reports using the NRSRO's own personnel. Therefore, based on staff experience, the Commission estimates that the average cost of software across all NRSROs would be approximately $4,000 per firm, with an aggregate one-time cost to the industry of $120,000.[167]

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163 30 NRSROs x 10 hours = 300 hours.

164 June 2007 Adopting Release, 71 FR at 33609.

165 3,000 hours + 900 hours = 3,900 total hours for one-time burden.

166 1,500 hours + 300 hours = 1,800 total annual hours.

167 $4,000 x 30 NRSROs = $120,000. As a means of comparison, the Commission notes that the average cost of recordkeeping software across all NRSROs under Rule 17g-2 is estimated to be $1,800 per respondent. See February 2009 Adopting Release, 74 FR, at 6472. The Commission preliminarily believes that the one-time cost of purchasing software in order to comply with

The Commission generally requests comment on all aspects of these burden estimates for proposed Rule 17g-7. In addition, the Commission requests specific comment on the following items related to these burden estimates:

- Would there be additional systems costs or other costs involved in developing this collection of information?
- Given that paragraph (a)(2) of proposed Rule 17g-7 would exempt an NRSRO from publishing the reports if, as of the end of the fiscal year, the NRSRO had no credit ratings outstanding that the NRSRO issued or maintained as a result of a person paying the NRSRO for the issuance or maintenance of the credit ratings, should the Commission revise the number of respondents for this proposed new collection of information? If so, what should the number be?

Commenters should provide specific data and analysis to support any comments they submit with respect to these estimates.

E. Collection of Information Is Mandatory

The collection of information obligations imposed by the proposed rule amendments and the proposed new rule would be mandatory for credit rating agencies that are registered with the Commission as NRSROs. Such registration is voluntary.[168]

F. Confidentiality

The information collected under the proposed amendments to Rule 17g-3 would be generated from the internal records of the NRSRO and would be furnished to the

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proposed new Rule 17g-7 would be greater than $1,800 because the proposed rule would require the publication of two new reports not previously required by any rule.

168 See Section 15E of the Exchange Act (15 U.S.C. 78o-7).

Commission on a confidential basis, to the extent permitted by law.[169] The proposed disclosures that would be required under Exhibit 6 to Form NRSRO and proposed Rule 17g-7 would be public.

G. Record Retention Period

The records required under the proposed amendments to Rules 17g-3 and 17g-7, as well as Exhibit 6 to Form NRSRO would need to be retained by the NRSRO for at least three years.[170]

H. Request for Comment

The Commission requests pursuant to 44 U.S.C. 3306(c)(2)(B) comment on the proposed collections of information in order to: (1) evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information would have practical utility; (2) evaluate the accuracy of the Commission's estimates of the burden of the proposed collections of information; (3) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; (4) evaluate whether there are ways to minimize the burden of the collection of information on those who respond, including through the use of automated collection techniques or other forms of information technology; and (5) evaluate whether the proposed rule amendments would have any effects on any other collection of information not previously identified in this section.

Persons who desire to submit comments on the collection of information requirements should direct their comments to the OMB, Attention: Desk Officer for the

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169 15 U.S.C. 78o-7(k). An NRSRO can request that the Commission keep this information confidential. See Section 24 of the Exchange Act (15 U.S.C. 78x), 17 CFR 240.24b-2, 17 CFR 200.80 and 17 CFR 200.83.

170 17 CFR 240.17g-2(c).

Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, DC 20503, and should also send a copy of their comments to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090, and refer to File No. S7-28-09. OMB is required to make a decision concerning the collections of information between 30 and 60 days after publication of this document in the Federal Register; therefore, comments to OMB are best assured of having full effect if OMB receives them within 30 days of this publication. Requests for the materials submitted to OMB by the Commission with regard to these collections of information should be in writing, refer to File No. S7-28-09, and be submitted to the Securities and Exchange Commission, Records Management Office, 100 F Street, NE, Washington, DC 20549.

IX. COSTS AND BENEFITS OF THE PROPOSED RULES

The Commission is sensitive to the costs and benefits that result from its rules. The Commission has identified certain costs and benefits of the proposed rule amendments and proposed new rule and requests comment on all aspects of this cost-benefit analysis, including identification and assessment of any costs and benefits not discussed in the analysis.[171] The Commission seeks comment and data on the value of

[171] For the purposes of this cost/benefit analysis, the Commission is using salary data from the Securities Industry and Financial Markets Association ("SIFMA") Report on Management and Professional Earnings in the Securities Industry 2008, which provides base salary and bonus information for middle-management and professional positions within the securities industry. The Commission believes that the salaries for these securities industry positions would be comparable to the salaries of similar positions in the credit rating industry. The salary costs derived from the report and referenced in this cost benefit section are modified to account for an 1800-hour work year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead. The Commission used comparable estimates in adopting final rules implementing the Rating Agency Act in 2007 and additional rules in 2009, requested comments on such estimates, and received no comments in response to these requests. See June 2007 Adopting Release, note 576, and February 2009 Adopting Release, note 179. Hereinafter, references to data derived from the report as modified in the manner described above will be cited as "SIFMA 2008 Report as Modified."

the benefits identified. The Commission also seeks comments on the accuracy of its cost estimates in each section of this cost-benefit analysis, and requests those commenters to provide data, including identification of statistics relied on by commenters to reach conclusions on cost estimates. Finally, the Commission seeks estimates and views regarding these costs and benefits for particular types of market participants, as well as any other costs or benefits that may result from these proposed rule amendments and the new proposed rule.

A. Benefits

The purposes of the Rating Agency Act, as stated in the accompanying Senate Report, are to improve ratings quality for the protection of investors and in the public interest by fostering accountability, transparency, and competition in the credit rating industry.[172] As the Senate Report states, the Rating Agency Act establishes "fundamental reform and improvement of the designation process" with the goal that "eliminating the artificial barrier to entry will enhance competition and provide investors with more choices, higher quality ratings, and lower costs."[173]

The Commission is proposing to amend Rule 17g-3 to require an NRSRO to furnish the Commission with an additional unaudited report containing a description of the steps taken by the designated compliance officer during the fiscal year to administer the policies and procedures that are required to be established pursuant to paragraphs (g) and (h) of Section 15E of the Exchange Act (management of conflicts of interest and prevention of the misuse of material nonpublic information); and ensure compliance with

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172 See Senate Report," p. 2.

173 Id, p. 7.

the securities laws and rules and regulations thereunder, including those promulgated by the Commission pursuant to Section 15E of the Exchange Act.

The Commission's staff understands that the designated compliance officer of some NRSROs may, in some cases, not be fulfilling the compliance officer's statutorily mandated duties, as prescribed by Section 15E(j) of the Exchange Act.[174] Further, during examinations in 2008 of three of the largest NRSRO's, Commission staff also identified issues with respect to each NRSROs policies and procedures and improvements that could be made.[175] In light of these concerns and the importance of an effective NRSRO compliance program, the Commission is proposing to amend Rule 17g-3 by adding paragraph (a)(7), which would require an NRSRO to furnish to the Commission an additional unaudited annual report.

The amendments to proposed new paragraph (a)(7) of Rule 17g-3 would also provide that the report must include: (1) a description of any compliance reviews of the activities of the NRSRO; (2) the number of material compliance matters identified during each review of the activities of the NRSRO and a brief description of each such finding; (3) a description of any remediation measures implemented to address material compliance matters identified during the reviews of the activities of the NRSRO; and (4) a description of the persons within the NRSRO who were advised of the results of the reviews.[176]

The Commission believes that the proposed amendment to Rule 17g-3 would further address concerns about the integrity of the ratings process by establishing a

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174 15 U.S.C. 78o-7(j).

175 See generally, Summary Report of Issues Identified in the Commission Staff's Examinations of Select Credit Rating Agencies (July 8, 2008). The report is available on the Commission's Internet Web site, located at http://www.sec.gov/news/studies/2008/craexamination070808.pdf.

176 See proposed Rule 17g-3(a)(7)(ii).

discipline under which the NRSRO's designated compliance officer would need to report to the Commission the steps taken by the compliance officer to fulfill the officer's responsibilities as set forth in Section 15E(j) of the Exchange Act. The act of reporting these steps is designed to promote the active engagement of the designated compliance officer in reviewing an NRSRO's compliance with internal policies and procedures. The reports also could strengthen the Commission's oversight of NRSROs by highlighting possible problem areas in an NRSRO's rating processes and providing an additional tool for the Commission to monitor how the NRSRO's designated compliance officer is fulfilling the responsibilities prescribed in Section 15E of the Exchange Act. For example, if an NRSRO reports an unusual level of significant compliance exceptions in a particular area, the Commission examination staff could focus their next review of the NRSRO in that particular area. Alternatively, if a report indicates no problems, but a subsequent staff examination reveals significant compliance exceptions, this could be brought to the attention of the NRSRO's management to be used to assess whether the designated compliance officer is adequately fulfilling the officer's statutory duties.

As stated above, the proposed amendment to Rule 17g-3 also would set forth specific items to be included in the proposed new report under Rule 17g-3(a)(7). The first item the Commission is proposing be included in the report is a description of any compliance reviews of the activities of the NRSRO.[177] The Commission intends that the designated compliance officer would describe all such reviews conducted during the most recently ended fiscal year. This would provide the Commission with an understanding of the scope of the designated compliance officer's reviews of the NRSRO's activities. The second item the Commission is proposing be included in the report is the number of

[177] See proposed Rule 17g-3(a)(7)(ii)(A).

material compliance matters identified during each review of the activities of the NRSRO and a brief description of each such finding. The Commission preliminarily intends a "material compliance matter" to be the discovery that the NRSRO or a person within the NRSRO had violated the securities laws[178] or the rules thereunder or the policies, procedures, or methodologies established, maintained and enforced by the NRSRO to, for example, determine credit ratings, prevent the misuse of material non-public information, manage conflicts of interest, and comply with the Commission's NRSRO rules.[179] The proposed requirement to report a material compliance matter would be designed to alert the Commission to matters identified by the designated compliance officer that could raise questions about the integrity of the NRSRO's activities and operations. It also could assist the Commission's oversight of NRSROs to the extent a reported material compliance matter is one that could arise in other NRSROs because, for example, it relates to a new type of debt instrument that is being rated by more than one NRSRO or involves interactions with an issuer that hired several NRSROs to rate its securities.

The third item the Commission is proposing be included in the report is a description of any remediation measures implemented to address material compliance matters identified during the reviews of the activities of the NRSRO.[180] The reporting of these measures could assist the Commission in evaluating the risk of such re-occurrences. It also could provide the Commission with potential "best practices" for mitigating the risk of future material compliance matters, which could assist the Commission in its overall supervision of NRSROs. Finally, the fourth item the Commission is proposing be included in the report is a description of the persons within the NRSRO who were

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178 The term "securities laws" is defined in Section 3(a)(47) of the Exchange Act

179 See e.g., 17 CFR 270.38a-1(e)(2); see also supra note 37.

180 See proposed Rule 17g-3(a)(7)(ii)(C).

advised of the results of the reviews. The information with respect to those persons who were advised of the results of reviews is designed to provide the Commission with an understanding of how the NRSRO responds to material compliance matters and the role and structure of the compliance program within the NRSRO. For example, it would indicate whether the compliance officer reported the matters to the NRSRO's board or senior management or only to the business unit that underwent the compliance review. This is designed to promote the appropriate escalation of compliance issues to the management of the NRSRO. The Commission also believes that this proposed information would be a useful tool for examiners to improve the focus of examination resources of a particular NRSRO on practices related to material compliance matters reported and the possible selection of NRSROs for examination.

In summary, as stated above, the amendments to Rule 17g-3 related to the new unaudited annual report related to the NRSRO's compliance function could serve to improve the NRSRO's compliance function. This improved compliance function, in turn, could improve the integrity of NRSROs' ratings processes.

The Commission also believes that the proposed new report would facilitate improvements to an NRSRO's compliance program in light of the concerns that the designated compliance officer of some NRSROs may, in some cases, not be fulfilling the compliances officer's statutorily mandated duties as prescribed in Section 15E(j) of the Exchange Act. The proposed rule amendments also would further enhance the Commission's oversight of NRSROs by providing the Commission staff an additional resource with which to evaluate the performance of the designated compliance officers in carrying out their statutory responsibilities prescribed in Section 15E(j) of the Exchange

Act. In addition to improving the quality of credit ratings, increased oversight of NRSROs could increase the accountability of an NRSRO to its subscribers, investors, and other persons who rely on the credibility and objectivity of a credit rating in making an investment decision.

Finally, the Commission believes that the proposed amendments to Rule 17g-3 would complement the Commission's examination program for NRSROs, and that the proposed amendments would enhance the Commission's ability to protect investors. The requirement to furnish the Commission with an annual report related to an NRSRO's compliance program would serve to help facilitate the examination staff's efforts to conduct each NRSRO examination in an organized and efficient manner and thus to allocate resources to maximize investor protection. The Commission notes that the proposed report would be one of numerous factors the Commission's exam staff may use to determine the focus of a particular exam.

The proposed amendments to the Instructions to Exhibit 6 to Form NRSRO would require an applicant/NRSRO to furnish the Commission with information regarding the revenues an NRSRO receives from major clients and from services other than determining credit ratings. The proposed new information is designed to assist users of NRSRO credit ratings in assessing the potential magnitude of the conflicts of interest inherent in a given NRSRO's business operations. In particular, by disclosing information about revenues received from major clients and other services, users of credit ratings would have access to more information about conflicts of interest that may exist when the NRSRO is being paid to determine credit ratings and is offering other services to persons who pay for ratings. The Commission believes these enhanced disclosures

would allow users of credit ratings to more effectively assess the conflicts of interest affecting an NRSRO. Although the disclosures an NRSRO provides on the Form NRSRO, including the proposed additional disclosures to Exhibit 6 to Form NRSRO cannot substitute for an investor's due diligence in evaluating a credit rating and the integrity of an NRSRO, the Commission believes the proposed amendment to Exhibit 6 to Form NRSRO would aid investors by providing additional publicly accessible information about an NRSRO.

The first proposed new disclosure in Exhibit 6 would require that an applicant/NRSRO disclose the percentage of total net revenue attributable the 20 largest users of credit rating services of the applicant/NRSRO. The Commission preliminarily believes this disclosure would assist investors and other users of credit ratings by providing them with an understanding of the degree to which revenues earned by the NRSRO come from a concentrated base of customers. This could be useful in understanding the conflicts inherent in the NRSRO's business given that an increase in concentration would result in an increase in the potential risk that the customers could use their contribution to the NRSRO's revenues to influence the objectivity of its credit ratings. Making the degree of this concentration transparent would allow investors and market participants to take this potential risk into account when considering the accuracy and reliability of the NRSRO's credit ratings. This, in turn, could improve the integrity of NRSROs. Increased confidence in the integrity of NRSROs and the credit ratings they issue could promote participation in the securities markets. In addition, the Commission believes that the proposed disclosures would allow investors and market participants to more effectively compare the concentrations across all NRSROs.

The second proposed new disclosure would require the applicant/NRSRO to disclose the percentage of total revenue attributable to other services and products of the applicant/NRSRO. The Commission preliminarily believes this information would be useful to investors and other users of credit ratings because it would provide scale to the amount of revenues an NRSRO earns from providing services other than credit ratings. An NRSRO that obtains substantial revenues from other services may be inclined to favor a client that purchases those other services when determining credit ratings solicited by the client. Consequently, creating greater transparency about the revenues generated from other services could assist investors and other users of credit ratings in assessing the potential risks to the NRSRO's objectivity.

Proposed Rule 17g-7 would require an NRSRO to make publicly available on its Internet Web site a consolidated report, which would need to be updated annually, containing information about the revenues earned by the NRSRO as a result of providing services and products to persons that paid the NRSRO to issue or maintain a credit rating. The Commission preliminarily believes that proposed Rule 17g-7 would provide users of credit ratings with information about the potential risk that arises when an NRSRO is paid to determine a credit rating for a specific obligor, security, or money market instrument - the risk that the revenue generated from the person paying the NRSRO to determine a credit rating could influence the NRSRO's objectivity if the NRSRO feels the need to curry favor from that person with a corresponding negative impact on the quality and accuracy of the credit rating. Simply put, it could cause the credit rating agency to determine a higher than warranted credit rating, which, as a result, does not accurately reflect the NRSRO's true view of the level of credit risk inherent in the

obligor, security, or money market instrument. Providing users of credit ratings with the information on revenue generated from other services provided to the person paying the NRSRO for the issuance or maintenance of the credit rating and on the relative standing of the entity as a contributor of revenue to the NRSRO would enable them to better assess the degree that a particular rating may be subject to this risk.

In addition, proposed Rule 17g-7 could have the benefit of helping to mitigate the potential ability an obligor, issuer, underwriter, sponsor, and subscriber as a large consumer of the services and products of the NRSRO from using its status to exert undue influence on the NRSRO. Specifically, by making the potential conflict more transparent to the marketplace, users of credit ratings, market participants, and others could assess how credit ratings solicited by large revenue providers are handled by the NRSRO, particularly with respect to NRSROs that make their ratings publicly available for free.

As stated above, the Commission also believes that the reports that would be required to be published by proposed Rule 17g-7 would create greater transparency about the revenues generated from other services and could assist investors and other users of credit ratings in assessing the potential risks to the NRSRO's objectivity by providing investors and other users of credit ratings with information to assess the degree of risk that a credit rating may be compromised by the undue influence of the person that paid for the issuance or maintenance of the credit rating. The Commission generally requests comment on all aspects of the proposed new rule. In addition, the Commission requests specific comment on the following items related to these benefits.

- Are there metrics available to quantify these benefits and any other benefits the commenter may identify, including the identification of sources of empirical data that could be used for such metrics?
- With respect to Rule 17g-7, to what use do users of credit ratings anticipate putting the proposed disclosures? To what extent, if any, might these disclosures create misimpressions as to the existence of potential conflicts? Are the proposed disclosures in proposed Rule 17g-7 granular enough to be of value to users of credit ratings?

Commenters should provide specific data and analysis to support any comments they submit with respect to the benefits discussed above and any other benefits identified by the commenters.

B. Costs

The Commission recognizes that there are potential costs that would result if the Commission adopts the proposed rule amendments to Rule 17g-3,[181] Exhibit 6 to Form NRSRO and proposed new Rule 17g-7. The Commission preliminarily believes that potential costs incurred by an NRSRO to comply with the proposed rule amendments to a given NRSRO would depend on its size and the complexity of its business activities. The size and complexity of NRSROs vary significantly. Therefore, the cost could vary significantly across NRSROs. The Commission is providing estimates of the average cost per NRSRO taking into consideration the variance in size and complexity of NRSROs. Any costs incurred would also vary depending on which classes of credit ratings an NRSRO issues and how many outstanding ratings it has in each class. For these reasons, the cost estimates represent the average cost across all NRSROs.

[181] See proposed Rule 17g-3(a)(7).

1. Proposed Amendments to Rule 17g-3

Rule 17g-3 requires an NRSRO to furnish audited annual financial statements to the Commission, including certain specified schedules.[182] The Commission is proposing to amend Rule 17g-3 to require an NRSRO to furnish the Commission with an additional unaudited report containing a description of the steps taken by the designated compliance officer during the fiscal year to administer the policies and procedures that are required to be established pursuant to paragraphs (g) and (h) of Section 15E of the Exchange Act; and ensure compliance with the securities laws and rules and regulations thereunder, including those promulgated by the Commission pursuant to Section 15E of the Exchange Act. The proposed amendments to Rule 17g-3 also would provide that the report must include: (1) a description of any compliance reviews of the activities of the NRSRO; (2) the number of material compliance matters identified during each review of the activities of the NRSRO and a brief description of each such matter; (3) a description of any remediation measures implemented to address material compliance matters identified during the reviews of the activities of the NRSRO; and (4) a description of the persons within the NRSRO who were advised of the results of the reviews.[183]

The Commission believes that the costs to NRSROs to comply with the proposed amendment to Rule 17g-3 would vary depending on the size and complexity of the NRSRO, as well as the size of its compliance programs. Larger NRSROs with comprehensive compliance programs may already periodically review portions of their compliance programs. These larger NRSROs may incur a cost associated with transforming their periodic reviews into more systematic reviews and developing the

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182 17 CFR 240.17g-3.

183 See proposed Rule 17g-3(a)(7)(ii).

report to be required under Rule 17g-3. While smaller NRSROs all have designated compliance officers, the Commission preliminarily believes, based on issues brought to the staff's attention, that some NRSROs may have less robust compliance programs than others. The Commission believes, however, that the information to be included in the proposed report under the amendments to Rule 17g-3 for smaller NRSROs would be less extensive, because smaller NRSRO's may have less complex organizational structures, fewer employees and fewer sources of revenue than larger NRSROs which may be part of a complex global organization with thousands of employees. Therefore, it may be less costly than for larger NRSROs.

Further, the Commission notes that the proposed report would explicitly require the NRSRO to describe the steps taken by the designated compliance officer during the fiscal year to administer the policies and procedures that are required to be established pursuant to paragraphs (g) and (h) of Section 15E of the Exchange Act; and ensure compliance with the securities laws and rules and regulations thereunder. Since these are statutorily mandated responsibilities of the designated compliance officer under Section 15E(j) of the Exchange Act, the Commission notes that certain costs are already being incurred by the NRSRO and therefore are not direct costs of the proposed amendments to Rule 17g-3. The Commission has preliminarily quantified certain costs with respect to the amendments to Rule 17g-3 which are discussed in detail below.

As discussed with respect to the PRA, the Commission preliminarily believes that the estimated hour burden under the proposed amendments to Rule 17a-3 would include the time it would take to compile information to draft the report and the preparation and filing of the report itself. In addition, this one-time hour burden estimate also includes

the time it would take to identify and describe material compliance matters, any remediation and the persons advised of the results of the reviews. Consequently, the Commission also based this estimate, in part, on the average estimated number of hours it would currently take an NRSRO to complete one annual report under current Rule 17g-3 (i.e., approximately 30 hours).[184] Consequently, as discussed above with respect to the PRA, the Commission estimates that the average amount of time across all NRSROs to prepare the additional report proposed to be required under the rule would be approximately 900 hours[185] at a total aggregate annual cost to the industry of $232,200.[186]

Given the potentially sensitive nature of the proposed report, the Commission also preliminarily believes that an NRSRO would likely engage outside counsel to assist it in the process of drafting and reviewing the proposed report under Rule 17g-3 on a one-time basis. The Commission estimates that the time an outside attorney would spend on this work would depend on the size and complexity of the NRSRO. Therefore, the Commission estimates that, on average, an outside counsel would spend approximately 20 hours assisting an NRSRO and its designated compliance officer in drafting and reviewing the proposed report on a one-time basis for an aggregate burden to the industry of 600 hours.[187] Based on industry sources, the Commission estimates that the cost of an outside counsel would be approximately $400 per hour. For these reasons, the Commission estimates that the average one-time cost to an NRSRO would be

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184 15 U.S.C. 78o-7(j). Under this provision of the statute, an NRSRO must "designate an individual responsible for administering the policies and procedures that are required to be established pursuant to [Sections 15E(g) and (h) of the Exchange Act (15 U.S.C. 78o-7(g) and (h))], and for ensuring compliance with the securities laws and rules and regulations thereunder, including those promulgated by the Commission pursuant to [Section 15E of the Exchange Act]." Id.

185 30 hours x 30 NRSROs = 900 hours.

186 $7,740 x 30 NRSROs = $232,200.

187 30 NRSROs x 20 hours = 600 hours.

approximately $8,000[188] and the one-time cost to the industry would be approximately $240,000.[189]

The Commission generally requests comment on all aspects of these cost estimates for the proposed amendments to Rule 17g-3. In addition, the Commission requests specific comment on the following items related to these cost estimates:

- Would an NRSRO incur any additional costs to employ an outside counsel on an annual basis to review the proposed 17g-3 report, rather than just on a one-time basis?
- Would the cost incurred by an NRSRO be less than those estimated because the designated compliance officer is already performing many of the responsibilities required to be described in the proposed report, as well as drafting compliance reports?
- What other costs are NRSROs likely to incur?
- Are the proposals likely to impose costs on other market participants, including persons who use credit ratings to make investment decisions or for regulatory purposes, and persons who purchase services and products from NRSROs?

Commenters should provide specific data and analysis to support any comments they submit with respect to the costs discussed above and any other costs identified by commenters.

2. Proposed Amendments to Form NRSRO

The proposed amendments to the Instructions to Exhibit 6 of Form NRSRO would require an applicant/NRSRO to furnish the Commission with information

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188 $400 per hour x 20 hours = $8,000.

189 $8,000 x 30 NRSROs = $240,000.

regarding the revenues an NRSRO receives from major clients and from products and services other than determining credit ratings. In particular, the additional disclosures to Exhibit 6 would require an applicant/NRSRO to provide the following disclosures, as applicable:

- The percentage of the applicant/NRSRO's net revenue attributable to the 20 largest users of credit rating services of the applicant/NRSRO; and
- The percentage of the applicant/NRSRO's revenue attributable to services and products other than credit rating services of the applicant/NRSRO.

The Commission believes that the costs to NRSROs to comply with the proposed amendment to Exhibit 6 to Form NRSRO would vary depending on the size and complexity of the NRSRO. Larger NRSROs may have more customers and complex revenue streams, while smaller NRSROs may be less complex in terms of sources of revenue or numbers of customers. Consequently, as discussed above with respect to the PRA, the Commission estimates that the average time necessary for an applicant or NRSRO to gather the information on a one-time basis in order to complete the additional disclosures proposed to be required by the amendments to Exhibit 6 to Form NRSRO would be one-time hour burden to the industry of 750 hours.[190] For these reasons, the Commission estimates that the average one-time cost to an NRSRO would be $6,520[191] and the total aggregate one-time cost to the industry would be $195,600.[192]

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190 30 NRSROs x 25 hours = 750 hours.

191 The Commission estimates that these responsibilities would be split between a Financial Reporting Manager (10 hours) and a Compliance Manager (15 hours). The SIA Management Report 2008 indicates that the average hourly cost for a Financial Reporting Manager is $265 and for a Compliance Manager is $258. Therefore, the average one-time cost would be $6,520 [(10 hours x $265 per hour) + (15 hours x $258 per hour)].

192 $6,520 x 30 NRSROs = $195,600.

In addition, with respect to the PRA, the Commission estimated that the average annual burden to complete an annual certification under Rule 17g-1(f) would increase 60 hours for all NRSROs.[193] For these reasons, the Commission estimates that the average annual cost with respect to the proposed amendment to an NRSRO would be $516[194] and the total aggregate annual cost to the industry would be $15,480.[195]

The Commission also notes that included in the current estimated costs for the Form NRSRO are the costs related to the engagement of outside counsel to assist in the process of completing and submitting a Form NRSRO.[196] In the June 2007 Proposing Release, the Commission estimated that the amount of time an outside attorney will spend on this work will depend on the size and complexity of the NRSRO. Therefore, the Commission estimated that, on average, an outside counsel will spend approximately 40 hours assisting an NRSRO in preparing its application for registration. The Commission further estimated that the average hourly cost for an outside counsel will be approximately $400 per hour. For these reasons, the Commission estimated that the average one-time cost to an NRSRO will be $16,000 and the one-time cost to the industry will be $480,000.[197] With respect to the proposed amendments to Exhibit 6 to Form NRSRO, the Commission estimates that the cost to outside counsel to review a Form NRSRO containing the additional disclosures to Exhibit 6 to Form NRSRO would

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193 2 hours x 30 NRSROs = 60 hours.

194 The Commission estimates that these responsibilities would be performed by a Compliance Manager. The SIA Management Report 2008 indicates that the average hourly cost a Compliance Manager is $258. Therefore, the average annual cost to an NRSRO would be $516 (2 hours x $258).

195 $516 x 30 NRSROs = $15,480.

196 June 2007 Adopting Release, 72 FR at 33614.

197 Id.

already be included within the original cost estimate for Rule 17g-1 and Form NRSRO[198] or that such costs would be de minimis.[199]

As discussed above with respect to the PRA, the Commission preliminarily believes that an applicant/NRSRO would incur only limited internal costs to modify its systems to generate and disclose the proposed additional disclosures in Exhibit 6 to Form NRSRO because an applicant/NRSRO is already required to generate similar financial information in other parts of Form NRSRO and certain financial reports required under Rule 17g-3.

The Commission generally requests comment on all aspects of these cost estimates for the proposed amendment to Form NRSRO. In addition, the Commission requests specific comment on the following items related to these cost estimates:

- Whether the proposals would impose costs on other market participants, including persons who use credit ratings to make investment decisions or for regulatory purposes, and persons who purchase services and products from NRSROs?
- Would the one-time cost to engage an outside counsel to assist in the preparation of the Form NRSRO increase as a result of the amendments to Exhibit 6 to Form NRSRO?
- Would the proposed disclosures in Exhibit 6 to Form NRSRO have any effect on the willingness of persons to pay for ratings as well as other credit rating services? What are the risks that investors and other users of credit ratings would be

198 Id.

199 The Commission believes that the review of the additional disclosures would overlap with the review of similar financial information already required to be disclosed in Exhibits 10 and 12 in Form NRSRO.

confused as to the significance of the revenue-based conflicts of interest being disclosed as a result of the proposed amendments to Exhibit 6 to Form NRSRO? Commenters should provide specific data and analysis to support any comments they submit with respect to the costs discussed above and any other costs identified by commenters.

3. Proposed Rule 17g-7

Proposed Rule 17g-7 would require an NRSRO to make publicly available on its Internet Web site a consolidated report containing information about the revenues earned by the NRSRO as a result of providing services and products to persons that paid the NRSRO to issue or maintain a credit rating. This report would need to be updated annually. As discussed above with respect to PRA, the Commission estimates that it would take an NRSRO approximately 100 hours to develop the calculations necessary to generate the percents required by the report under proposed Rule 17g-7; to populate the proposed report with the required data; and to develop and draft the form report. The Commission estimates that the proposed new Rule 17g-7 would impose a total one-time hour burden of 3,000 hours for 30 NRSROs to prepare the report. The Commission estimates that the average one-time cost to an NRSRO would be $23,500[200] and the total aggregate one-time cost for all NRSROs would be $705,000.[201]

As discussed above with respect to the PRA, the Commission also estimates that after the first year it would take NRSRO 50 hours per year to generate the percents

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200 The Commission estimates an NRSRO would have a Senior Accountant and a Senior Programmer working together to generate the initial calculations and report and that the two senior officers would divide the estimated 100 hours equally. The SIFMA 2008 Report as Modified indicates that the average hourly cost for a Senior Accountant is $178 and that the average hourly cost for a Senior Programmer is $292. Therefore, the average one-time cost to an NRSRO would be $23,500 (50 hours x $178) + (50 hours x $292).

201 30 NRSROs x $23,500 = $705,000.

required under the proposed report and to populate the proposed report with the required data once a year. Therefore, the Commission estimates that the average annual cost to an NRSRO would be $3,150[202] and the total aggregate annual cost to the industry would be $94,500 to generate the proposed report once a year.[203]

Proposed Rule 17g-7 would also require an NRSRO to make publicly available on its Internet Web site the report required under paragraph (a)(1). As discussed with respect to the PRA, the Commission estimates that it would take an NRSRO approximately 30 hours to disclose the initial information in its Web site for a total one-time burden of 900 hours, and thereafter 10 hours per year to disclose updated information for an annual hour burden of 300 hours. The Commission estimates that an NRSRO would incur an average one-time cost of $8,760 and an average annual cost of $2,920.[204] The total one-time cost to the industry would be approximately $262,800[205] and the total aggregate annual cost to the industry would be approximately $87,600.[206]

Finally, the Commission also believes that an NRSRO may need to purchase and/or modify its software and operating systems in order to generate and publish the information required in the proposed reports in proposed Rule 17g-7. As discussed in the PRA, the Commission estimates that the cost of any software would vary based on the size and complexity of the NRSRO. The Commission estimates that some NRSROs

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202 The Commission estimates that after the equations and initial report has been developed that an NRSRO would have a Compliance Clerk perform the necessary tasks to generate the annual report. The SIFMA 2008 Office Salaries Report as Modified indicates that the average hourly cost for a Compliance Clerk is $63. Therefore, the average yearly cost to an NRSRO would be $3,150 (50 hours x $63).

203 $3,150 x 30 NRSROs = $94,500.

204 The Commission estimates that an NRSRO will have a Senior Programmer perform this work. The SIFMA 2008 Report as Modified indicates that a Senior Programmer is $292. Therefore the average one-time cost will be $8,760 (30 hours x $292) and the average annual cost will be $2,920 (10 hours x $292).

205 $8,760 x 30 NRSROs = $262,800.

206 $2,920 x 30 NRSROs = $87,600.

would not need such software. Therefore, the Commission estimates that the average cost of software across all NRSROs would be approximately $120,000.[207]

The Commission generally requests comment on all aspects of these cost estimates for the proposed Rule 17g-7. In addition, the Commission requests specific comment on the following items related to these cost estimates:

- Would these proposals impose costs on other market participants, including persons who use credit ratings to make investment decisions or for regulatory purposes, and persons who purchase services and products from NRSROs?
- Would the proposed disclosures in new Rule 17g-7 have any effect on the willingness of persons to pay for ratings and other credit rating services? What are the risks that investors and other users of credit ratings would be confused as to the significance of the information being disclosed as a result new Rule 17g-7?
- Would there be costs in addition to those identified above, such as costs arising from systems changes and restructuring business practices to account for the new reporting requirement?
- To what extent, if any, might issuers shift to larger NRSROs in which their revenue contribution would contribute a lower percentage to the NRSROs overall revenue to avoid being in a particular tier?

Commenters should provide specific data and analysis to support any comments they submit with respect to the costs discussed above and any other costs identified by commenters.

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[207] $4,000 x 30 NRSROs = $120,000.

X. CONSIDERATION OF BURDEN ON COMPETITION AND PROMOTION OF EFFICIENCY, COMPETITION, AND CAPITAL FORMATION

Under Section 3(f) of the Exchange Act,[208] the Commission shall, when engaging in rulemaking that requires the Commission to consider or determine whether an action is necessary or appropriate in the public interest, consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation. Section 23(a)(2) of the Exchange Act[209] requires the Commission to consider the anticompetitive effects of any rules the Commission adopts under the Exchange Act. Section 23(a)(2) prohibits the Commission from adopting any rule that would impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act. As discussed below, the Commission's preliminary view is that the proposed rule amendments may promote efficiency, competition, and capital formation.

The Commission generally requests comment on all aspects of this analysis of the burden on competition and promotion of efficiency, competition, and capital formation. Commenters should provide specific data and analysis to support their views.

A. Rule 17g-3

The proposed amendment to Rule 17g-3[210] would require an NRSRO to furnish the Commission with an additional unaudited report containing a description of the steps taken by the designated compliance officer during the fiscal year to administer the policies and procedures that are required to be established pursuant to paragraphs (g) and (h) of Section 15E of the Exchange Act; and ensure compliance with the securities laws

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208 15 U.S.C. 78c(f).

209 15 U.S.C. 78w(a)(2).

210 See proposed Rule 17g-3(a)(7).

and rules and regulations thereunder, including those promulgated by the Commission pursuant to Section 15E of the Exchange Act.[211]

The amendments to Rule 17g-3 also would provide that the proposed report must include: (1) a description of any compliance reviews of the activities of the NRSRO; (2) the number of material compliance matters identified during each review of the activities of the NRSRO and a brief description of each such matter; (3) a description of any remediation measures implemented to address material compliance matters identified during the reviews of the activities of the NRSRO; and (4) a description of the persons within the NRSRO who were advised of the results of the reviews. As stated above, the proposed new report would be unaudited, consistent with the other unaudited reports currently required under Rule 17g-3.[212]

The Commission believes that the proposed amendments to Rule 17g-3 could indirectly increase efficiency in a number of ways. The proposed amendments to Rule 17g-3 may improve the efficiency of the credit ratings process by establishing a more structured discipline under which the NRSRO's designated compliance officer would need to report to the Commission the steps taken to fulfill the officer's statutory responsibilities. The act of reporting these steps is designed to promote the active engagement of the designated compliance officer in reviewing an NRSRO's compliance with the securities laws and its own internal policies and procedures.

The Commission also believes that improved compliance as a result of the proposed rule amendments may increase efficiency in the credit ratings process by

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211 See proposed Rule 17g-3(a)(7).

212 17 CFR 240.17g-3(a)(2)-(6). Under Rule 17g-3, the only required audited report is the NRSRO's financial statements as of its most recent fiscal year. 17 CFR 240.17g-3(a)(1).

focusing the NRSRO's designated compliance officer in fulfilling his or her responsibilities prescribed under Section 15E(j) of the Exchange Act, as well as by facilitating an NRSRO's early intervention to decrease the severity of compliance violations which may occur. Because the compliance officer would be required to report these steps, the proposed amendments may foster improved compliance overall. This may, in turn, promote greater efficiencies in the credit rating process.

The Commission further believes that these proposed amendments could promote more efficient allocation of capital by investors to the extent that the quality of credit ratings is improved.

Additionally, the Commission believes that the proposed report could promote efficient allocation of Commission resources and time by facilitating the Commission's examination staff efforts to conduct each exam of an NRSRO in an organized and efficient manner. These efficiencies will help the Commission to better allocate its own resources to maximize investor protection.[213]

The Commission believes that the proposed amendments to Rule 17g-3 could promote participation in the securities markets, and, thereby, promote capital formation and competition among NRSROs by increasing confidence in the integrity of NRSROs and the credit ratings they issue. Consequently, the Commission also does not believe that the proposed amendments to Rule 17g-3 would be a burden on competition.

The proposed amendments to Rule 17g-3 could improve the integrity of the ratings process by establishing a discipline under which the NRSRO's designated

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[213] The Commission also notes that other areas of the Commissions rules and regulations also require an annual report by a chief compliance officer with respect to investment companies and investment advisers. See generally, Rule 38a-1, 17 CFR 270.38a-1, and Rule 206(4)-7, 17 CFR 275.206(4)-7.

compliance officer would need to report to the Commission the steps taken by the compliance officer to fulfill the officer's statutory responsibilities. The act of reporting these steps is designed to promote the active engagement of the designated compliance officer in reviewing an NRSRO's compliance with internal policies and procedures. The proposed report also could strengthen the Commission's oversight of NRSROs by highlighting possible problem areas in an NRSRO's rating processes and providing an additional tool for the Commission to monitor how the NRSRO's designated compliance officer is fulfilling the responsibilities prescribed in Section 15E of the Exchange Act. For example, if an NRSRO reports an unusual level of significant compliance exceptions in a particular area, the Commission examination staff could focus their next review of the NRSRO in that particular area. Alternatively, if a report indicates no problems, but a subsequent staff examination reveals significant compliance exceptions, this could be brought to the attention of the NRSRO's management to be used to assess whether the designated compliance officer is adequately fulfilling the officer's statutory duties. Furthermore, the identification of the persons within the NRSRO advised of the results of the review and remediation measures implemented could also promote the appropriate escalation of compliance issues to the management of the NRSRO.

Thus, enhancing the Commission's oversight and improving compliance of the NRSROs could help in restoring confidence in credit ratings issued by NRSROs which, in turn, could promote capital formation.

B. Amendments to Form NRSRO

The proposed amendments to the Instructions to Exhibit 6 to Form NRSRO are designed to provide more information to users of credit ratings with respect to an

NRSRO's conflicts of interest. The Commission is proposing to require an applicant/NRSRO to furnish the Commission with information regarding the revenues an NRSRO receives from major clients and from services other than determining credit ratings. In particular, the additional disclosures to Exhibit 6 to Form NRSRO would require an applicant/NRSRO to provide the following disclosures, as applicable:

- The percentage of the applicant/NRSRO's net revenue attributable to the 20 largest users of credit rating services of the applicant/NRSRO; and
- The percentage of the applicant/NRSRO's revenue attributable to services and products other than credit rating services of the applicant/NRSRO.

By assisting investors and other users of credit ratings in assessing the potential magnitude of the conflicts of interest inherent in a given NRSRO's business operations, the proposed additional disclosures to Exhibit 6 to Form NRSRO may promote more efficient investment analyses and decisions by these investors and users.

The proposed additional disclosures are designed to provide the marketplace with additional information for comparing NRSROs and, therefore, provide users of credit ratings with more useful metrics with which to compare these NRSROs. In particular, by disclosing information about revenues received from major clients and for other services, users of credit ratings would be given more information about the potential dimensions of the conflict of being paid to determine credit ratings and offering other services to persons who pay for ratings. Increased disclosure of these conflicts would make the incentives of the NRSROs more transparent to the marketplace and, thereby, highlight those firms that may have fewer or less significant conflicts of interest. These proposed disclosures would allow investors and other users of credit ratings to compare

concentrations of revenue across all NRSROs, thus promoting efficiency for investors and other users of credit ratings in evaluating NRSROs and a particular credit rating in making an investment decision.

The Commission further believes that these proposed amendments could promote more efficient allocation of capital by investors to the extent that the quality of credit ratings is improved.

These proposed disclosures are also designed to increase competition and promote capital formation by restoring confidence in the NRSROs credit ratings, which are an integral part of the capital formation process.

By proposing to provide more information about an NRSRO's conflicts of interest, investors and users of credit ratings will be better able to evaluate the integrity of an NRSRO and the credit ratings that it issues. This enhanced information, in turn, may promote greater competition among NRSROs for the business of those users and investors. Consequently, the Commission does not believe that the proposed disclosures would be a burden on competition among NRSROs.

Moreover, because users of credit ratings would have greater confidence in the integrity of the NRSROs as well as the credit ratings that they issue, such increased confidence could promote investor participation in the securities markets, and, thereby, promote capital formation.

C. Rule 17g-7

The Commission also is proposing to adopt a new rule – Rule 17g-7 – which would require an NRSRO to make publicly available on its Internet Web site a consolidated report containing information about the revenues earned by the NRSRO as a

result of providing services and products to persons that paid the NRSRO to issue or maintain a credit rating. This report would need to be updated annually. Specifically, proposed Rule 17g-7 would require the NRSRO to include in the report: (1) the percent of the net revenue attributable to the person that paid the NRSRO that were earned by the NRSRO during the most recently ended fiscal year from providing services and products other than credit rating services to the person; (2) the relative standing of the person in terms of the person's contribution to the NRSRO's net revenue as compared with other persons that contributed to the NRSRO's net revenues; and (3) the identity of all outstanding credit ratings issued by the NRSRO and paid for by the person.

The Commission preliminarily believes that proposed Rule 17g-7 would provide users of credit ratings with information about the potential risk that arises when an NRSRO is paid to determine a credit rating for a specific obligor, security, or money market instrument. Namely, the risk that the revenue generated from the person soliciting the NRSRO to determine a credit rating could influence the NRSRO's objectivity in an effort to favor with that person with a corresponding negative impact on the quality and accuracy of the credit rating.

By assisting investors and other users of credit ratings in analyzing the nature and degree of potential conflicts, proposed Rule 17g-7 may promote more efficient investment analyses and decisions by these investors and users.

The proposed additional disclosures are designed to provide the marketplace with additional information for comparing NRSROs and, therefore, provide users of credit ratings with more useful metrics with which to compare these NRSROs. The Commission believes that the enhanced disclosure requirements of proposed Rule 17g-7

may enable investors and other users of credit ratings to better assess when and to what degree a NRSRO's objectivity may be compromised. Increased disclosures also will make the incentives of the NRSROs more transparent to the marketplace. Based on this information, investors and users of credit ratings issued by an NRSRO may make more informed investment decisions when considering credit ratings, which could promote efficiency.

The Commission further believes that these proposed amendments could promote more efficient allocation of capital by investors to the extent that the quality of credit ratings is improved.

These proposed disclosures, like the proposed additional disclosures to Form NRSRO, are designed to increase competition and promote capital formation by restoring confidence in the credit ratings. By providing more information about the nature and extent of potential revenue-based conflicts, investors and users of credit ratings will be better able to evaluate the integrity of an NRSRO and the credit ratings that it issues and assess whether its objectivity may be compromised. This enhanced information, in turn, may promote greater competition among NRSROs for the business of those users and investors.

A risk, however, exists with respect to proposed Rule 17g-7 that competition may be negatively impacted to the extent that issuers shift to larger NRSROs in which their revenue contribution will likely make up a smaller percentage of revenue to avoid any potential "stigma" associated with being perceived as a large client of an NRSRO.

Moreover, because users of credit ratings would have greater confidence in the integrity of the NRSROs as well as the credit ratings that they issue, such increased

confidence could promote investor participation in the securities markets, and, thereby, promote capital formation.

XI. CONSIDERATION OF IMPACT ON THE ECONOMY

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, or "SBREFA,"[214] the Commission must advise OMB whether a proposed regulation constitutes a major rule. Under SBREFA, a rule is "major" if it has resulted in, or is likely to result in:

- an annual effect on the economy of $100 million or more;
- a major increase in costs or prices for consumers or individual industries; or
- a significant adverse effect on competition, investment, or innovation.

If a rule is "major," its effectiveness will generally be delayed for 60 days pending Congressional review. The Commission requests comment on the potential impact of the proposed rule amendments on the economy on an annual basis. Commenters are requested to provide empirical data and other factual support for their view to the extent possible.

XII. INITIAL REGULATORY FLEXIBILITY ANALYSIS

The Commission has prepared the following Initial Regulatory Flexibility Analysis ("IRFA"), in accordance with the provisions of the Regulatory Flexibility Act,[215] regarding the proposed rule amendments to Rule 17g-3 and Form NRSRO under the Exchange Act and proposed new Rule 17g-7.

A. Reasons for the Proposed Action

The proposed amendments and proposed new rule would prescribe additional

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214 Pub. L. No. 104-121, Title II, 110 Stat. 857 (1996) (codified in various sections of 5 U.S.C., 15 U.S.C. and as a note to 5 U.S.C. 601).

215 5 U.S.C. 603.

requirements for NRSROs to address concerns raised about the role of credit rating agencies in the recent credit market turmoil. The proposed amendments and proposed new rule would enhance and strengthen the rules the Commission to implement specific provisions of the Rating Agency Act.[216] The Rating Agency Act defines the term "nationally recognized statistical rating organization" as a credit rating agency registered with the Commission, provides authority for the Commission to implement registration, recordkeeping, financial reporting, and oversight rules with respect to registered credit rating agencies.

As discussed in detail above, the proposed amendments seek to further the substantive goals of the Commission's current oversight program for NRSROs, including, increasing transparency and disclosure, diminishing conflicts, and strengthening oversight more generally.[217]

The Commission believes that the proposed amendments to Rule 17g-3 would improve the integrity of the ratings process by establishing a discipline under which the NRSRO's designated compliance officer would need to report to the Commission the steps taken by the compliance officer to fulfill the officer's statutory responsibilities.[218] The act of reporting these steps is designed to promote the active engagement of the designated compliance officer in reviewing an NRSRO's compliance with internal policies and procedures. The proposed report also could strengthen the Commission's oversight of NRSROs by highlighting possible problem areas in an NRSRO's rating

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216 Pub. L. No. 109-291 (2006); see also Exchange Act Release No. 55857 (June 5, 2007), 72 FR 33564, 33609 (June 18, 2007).

217 See Report of the Senate Committee on Banking, Housing, and Urban Affairs to Accompany S. 3850, Credit Rating Agency Reform Act of 2006, S. Report No. 109-326, 109th Cong., 2d Sess. (Sept. 6, 2006) ("Senate Report"), p. 2.

218 See proposed Rule 17g-3(a)(7) and (b)(2).

processes and providing an additional tool for the Commission to monitor how the NRSRO's designated compliance officer is fulfilling the responsibilities prescribed in Section 15E of the Exchange Act. Furthermore, the identification of the persons within the NRSRO advised of the results of the review and remediation measures implemented could also promote the appropriate escalation of compliance issues to the management of the NRSRO.

The Commission believes that the proposed amendments to Exhibit 6 to the Instructions to Form NRSRO would allow users of credit ratings to more effectively evaluate the integrity of the NRSRO's credit ratings themselves and whether they believe the NRSRO is effectively managing its conflicts of interests otherwise identified in Exhibit 6. Finally, the purpose of proposed new Rule 17g-7 is to provide users of credit ratings with information about the potential risk that arises when an NRSRO is paid to determine a credit rating for a specific obligor, security, or money market instrument.

B. Objectives

The objectives of the Rating Agency Act are "to improve ratings quality for the protection of investors and in the public interest by fostering accountability, transparency, and competition in the credit rating industry."[219] The proposed amendments and proposed new rule are designed to further enhance these objectives and assist the Commission in monitoring whether an NRSRO complies with the provisions of the Rating Agency Act and rules thereunder, fulfilling the Commission's statutory mandate to adopt rules to implement the NRSRO regulatory program, and provide information regarding NRSROs to the public and to users of credit ratings.

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[219] See Senate Report, supra note 217.

The objective of the proposed amendment to Rule 17g-3 is to improve the integrity of the ratings process and enhance accountability by requiring the designated compliance officer to annually report on actions taken to fulfill the officer's statutory responsibilities. The requirement to provide the Commission with such a report would, the Commission believes, help establish or reinforce a discipline and rigor in the compliance officer's performance of his or her duties. It also is designed to strengthen the Commission's oversight of NRSROs by highlighting possible problem areas in an NRSRO's rating processes and providing an additional tool for the Commission to determine whether the NRSRO's designated compliance officer is fulfilling the responsibilities prescribed in Section 15E of the Exchange Act.[220] In addition, this information is designed to assist the Commission staff in its examination of NRSROs. Furthermore, the identification of the persons within the NRSRO advised of the results of the review and remediation measures implemented could also promote the appropriate escalation of compliance issues to the management of the NRSRO.

The proposed amendments to the Exhibit 6 Instructions to Form NRSRO that would require additional disclosures are designed to increase transparency by allowing users of credit ratings to more effectively evaluate the integrity of an NRSRO's credit ratings and analyze whether the NRSRO is effectively managing its conflicts of interests.

Finally, proposed new Rule 17g-7 is designed to increase transparency as well as enhance disclosures with respect to an NRSRO's management of its conflicts of interest by providing users of credit ratings with information about the potential risk of undue influence that arises when an NRSRO is paid to determine a credit rating for a specific obligor, security, or money market instrument.

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[220] 15 U.S.C. 78o-7(j).

C. Legal Basis

Pursuant to the Exchange Act[221] and, particularly, Sections 15E and 17(a) of the Exchange Act, the Commission is proposing amendments to Rule 17g-3 and Exhibit 6 to Form NRSRO, as well as proposing new Rule 17g-7.[222]

D. Small Entities Subject to the Rule

Paragraph (a) of Rule 0-10 provides that for purposes of the Regulatory Flexibility Act, a small entity "[w]hen used with reference to an 'issuer' or a 'person' other than an investment company" means "an 'issuer' or 'person' that, on the last day of its most recent fiscal year, had total assets of $5 million or less."[223] The Commission believes that an NRSRO with total assets of $5 million or less would qualify as a "small" entity for purposes of the Regulatory Flexibility Act. Currently, there are two NRSROs that are classified as "small" entities for purposes of the Regulatory Flexibility Act.[224]

E. Reporting, Recordkeeping, and Other Compliance Requirements

The proposal would amend Rule 17g-3 to require an NRSRO to furnish the Commission with an additional unaudited annual report containing a description of the steps taken by the designated compliance officer during the fiscal year to administer the policies and procedures that are required to be established pursuant to paragraphs (g) and (h) of Section 15E of the Exchange Act; and ensure compliance with the securities laws

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221 15 U.S.C. 78a et seq.

222 15 U.S.C. 78o-7.

223 17 CFR 240.0-10(a).

224 See 17 CFR 240.0-10(a). Two of the 10 credit rating agencies currently registered as NRSROs would be considered "small" entities for purposes of the Regulatory Flexibility Act. The Commission previously sought comment on the number of small entities that may be effected by other proposed rule amendments to the Commission's NRSRO rules. The Commission received no comments in response to those requests. See generally, February 2009 Adopting Release, at 74 FR 6481.

and rules and regulations thereunder, including those promulgated by the Commission pursuant to Section 15E of the Exchange Act.[225]

The amendments to proposed new paragraph (a)(7) of Rule 17g-3 would also provide that the report must include: (1) a description of any compliance reviews of the activities of the NRSRO; (2) the number of material compliance matters identified during each review of the activities of the NRSRO and a brief description of each such matter; (3) a description of any remediation measures implemented to address material compliance matters identified during the reviews of the activities of the NRSRO; and (4) a description of the persons within the NRSRO who were advised of the results of the reviews.[226]

The Commission believes that the costs to NRSROs to comply with the proposed amendment to Rule 17g-3 would vary depending on the size and complexity of the NRSRO, as well as the size of its compliance programs. Larger NRSROs with comprehensive compliance programs may already periodically review portions of their compliance programs. These larger NRSROs may incur a cost associated with transforming their periodic reviews into a more systematic review and developing a form of report. While smaller NRSROs all have designated compliance officers, the Commission preliminarily believes, based on issues brought to the staff's attention, that some NRSROs may have less robust compliance programs than others NRSRO's. The Commission believes that the information to be included in the proposed report for smaller NRSROs would be less extensive, because smaller NRSRO's may have less complex organizational structures, fewer employees and fewer sources of revenue than

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225 See proposed Rule 17g-3(a)(7).

226 See proposed Rule 17g-3(a)(7)(ii).

larger NRSROs which may be part of a complex global organization with thousands of employees. Therefore, it may be less costly than for larger NRSROs. Finally, the proposed new report under Rule 17g-3 would need to be retained by NRSROs for three years under Rule 17g-2.

The Commission is proposing to amend the Instructions to Exhibit 6 to Form NRSRO to require an applicant/NRSRO to furnish the Commission with information regarding the revenues an NRSRO receives from major clients and from services other than determining credit ratings. In particular, the amendments to Exhibit 6 would require an applicant/NRSRO to provide the following disclosures, as applicable:

- The percentage of the applicant/NRSRO's net revenue attributable to the 20 largest users of credit rating services of the applicant/NRSRO; and
- The percentage of the applicant/NRSRO's revenue attributable to services and products other than credit rating services of the applicant/NRSRO.

In order to comply with the proposed amendments to Exhibit 6 to Form NRSRO, an applicant/NRSRO would need to compile the information in order to complete the additional disclosures. The Commission believes that the burdens imposed by the proposed rule amendments would vary based on the size and complexity of each applicant/NRSRO. The Commission believes that the potential impact of the amendments to Exhibit 6 to Form NRSRO on small NRSROs should not be significant because these entities would have fewer clients and less revenue and therefore lower costs to produce the additional disclosures under the amendments to Exhibit 6 to Form NRSRO.

The Commission is also proposing new Rule 17g-7, which would require an NRSRO to make publicly available on its Internet Web site a consolidated report containing information about the revenues earned by the NRSRO as a result of providing services and products to persons that paid the NRSRO to issue or maintain a credit rating. This report would need to be updated annually. In order to comply with new Rule 17g-7, each NRSRO would need to develop the calculations necessary to generate the percents required under the report; to populate the proposed report with the required data; and to develop and draft the form report. The Commission believes that the burdens imposed by new Rule 17g-7 would vary based on the size and complexity of each applicant/NRSRO. The Commission believes that the potential impact of the proposed Rule 17g-7 on small NRSROs should not be significant because these entities would have fewer clients and less revenue and therefore lower costs to produce the consolidated report required by proposed new Rule 17g-7. The consolidated report would need to be retained for three years in accordance with Rule 17g-2.

F. Duplicative, Overlapping, or Conflicting Federal Rules

The Commission believes that there are no federal rules that duplicate, overlap, or conflict with the proposed rule amendments and the proposed new rule.

G. Significant Alternatives

Pursuant to Section 3(a) of the Regulatory Flexibility Act,[227] the Commission must consider certain types of alternatives, including: (1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance and reporting requirements under the rule for small entities; (3) the use of

[227] 5 U.S.C. 603(c).

performance rather than design standards; and (4) an exemption from coverage of the rule, or any part of the rule, for small entities.

The Commission considered whether it is necessary or appropriate to establish different compliance or reporting requirements or timetables; or clarify, consolidate, or simplify compliance and reporting requirements under the rule for small entities. Because the proposed rule amendments are designed to improve the overall quality of ratings and enhance the Commission's oversight, the Commission preliminarily believes that small entities should be covered by the rule. The Commission also preliminarily believes that the proposed rule amendments and proposed new rule are flexible and simple enough to allow small NRSROs to comply without the need for the establishment of differing compliance or reporting requirements for small entities.

H. Request for Comments

The Commission encourages written comments on matters discussed in this IRFA. In particular, the Commission seeks comment on the number of small entities that would be affected by the proposed rule amendments and the proposed new rule, and whether the effect on small entities would be economically significant. Commenters are asked to describe the nature of any effect and to provide empirical data to support their views.

XIII. STATUTORY AUTHORITY

The Commission is proposing amendments to Rule 17g–3 and the Instructions to Form NRSRO and new Rule 17g-7, pursuant to the authority conferred by the Exchange Act, including Sections 15E and 17(a).[228]

Text of Proposed Rules

[228] 15 U.S.C. 78o–7 and 78q.

List of Subjects in 17 CFR Parts 240 and 249b

Brokers, Reporting and recordkeeping requirements, Securities.

In accordance with the foregoing, the Commission hereby proposes that Title 17, Chapter II of the Code of Federal Regulation be amended as follows.

PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

1. The authority citation for part 240 continues to read, in part, as follows:

Authority: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z-2, 77z-3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78d, 78e, 78f, 78g, 78i, 78j, 78j-1, 78k, 78k-1, 78l, 78m, 78n, 78o, 78p, 78q, 78s, 78u-5, 78w, 78x, 78ll, 78mm, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4, 80b-11, and 7201 et. seq.; and 18 U.S.C. 1350, unless otherwise noted.

2. Section 240.17g–3 is amended by:

a. Adding a new paragraph (a)(7); and

b. Revising paragraph (b).

The additions and revisions read as follows:

(a) * * *

(7)(i) An unaudited report containing a description of the steps taken by the designated compliance officer during the fiscal year to:

(A) Administer the policies and procedures that are required to be established pursuant to paragraphs (g) and (h) of Section 15E of the Exchange Act (15 U.S.C. 78o-7(g) and (h)); and

(B) Ensure compliance with the securities laws and rules and regulations thereunder, including those promulgated by the Commission pursuant to Section 15E of the Exchange Act.

(ii) The report required pursuant to paragraph (a)(7)(i) of this section must include:

(A) A description of any compliance reviews of the activities of the nationally recognized statistical rating organization;

(B) The number of material compliance matters identified during each review of the activities of the nationally recognized statistical rating organization and a brief description of each such matter;

(C) A description of any remediation measures implemented to address material compliance matters identified during the reviews of the activities of the nationally recognized statistical rating organization; and

(D) A description of the persons within the nationally recognized statistical rating organization who were advised of the results of the reviews.

* * * * *

(b) The nationally recognized statistical rating organization must:

(1) Attach to the financial reports furnished pursuant to paragraphs (a)(1) through (a)(6) of this section a signed statement by a duly authorized person associated with the nationally recognized statistical rating organization stating that the person has responsibility for the financial reports and, to the best knowledge of the person, the financial reports fairly present, in all material respects, the financial condition, results of

operations, cash flows, revenues, analyst compensation, and credit rating actions of the nationally recognized statistical rating organization for the period presented; and

(2) Attach to the report furnished pursuant to paragraph (a)(7) of this section a signed statement by the designated compliance officer of the nationally recognized statistical rating organization stating that the person has responsibility for the report and, to the best knowledge of the designated compliance officer, the report fairly presents, in all material respects, steps taken by the designated compliance officer for the period presented.

* * * * *

3. Section 240.17g-7 is added to read as follows:

§ 240.17g-7 Reports to be made public by nationally recognized statistical rating organizations about persons that paid the nationally recognized statistical rating organization for the issuance or maintenance of a credit rating.

(a)(1) A nationally recognized statistical rating organization must annually, not later than 90 calendar days after the end of its fiscal year (as indicated on its current Form NRSRO), make publicly available on its Internet Web site a consolidated report that shows, with respect to each person that paid the nationally recognized statistical rating organization to issue or maintain a credit rating that was outstanding as of the end of the fiscal year, the following information:

(i) the percent of the net revenue attributable to the person earned by the nationally recognized statistical rating organization for that fiscal year from providing services and products other than credit rating services to the person, which the nationally recognized statistical rating organization must calculate in accordance with paragraph (a)(3)(i) of this section;

(ii) the relative standing of the person in terms of the person's contribution to the net revenue of the nationally recognized statistical rating organization for the fiscal year, which the nationally recognized statistical rating organization must determine in accordance with paragraph (a)(3)(ii) of this section; and

(iii) all outstanding credit ratings paid for by the person, which the nationally recognized statistical rating organization must determine in accordance with paragraph (a)(3)(iii) of this section.

(2) A nationally recognized statistical rating organization is not required to make publicly available on its Internet Web site the report required by paragraph (a)(1) of this section or include with the publication of a credit rating the statement required by paragraph (b) of this section if, as of the end of the fiscal year, there are no credit ratings outstanding that the nationally recognized statistical rating organization issued or maintained as a result of a person paying the nationally recognized statistical rating organization for the issuance or maintenance of such credit ratings.

(3)(i) The nationally recognized statistical rating organization must calculate the percent of the net revenue attributable to the person earned by the nationally recognized statistical rating organization for the fiscal year from providing services and products other than credit rating services to the person as follows:

(A) Calculate the net revenue attributable to the person earned by the nationally recognized statistical rating organization for the fiscal year from providing services and products other than credit rating services to the person;

(B) Calculate the net revenue attributable to the person earned by the nationally recognized statistical rating organization for the fiscal year from providing all services and products, including credit rating services, to the person; and

(C) Divide the amount calculated pursuant to paragraph (a)(3)(i)(A) of this section by the amount calculated pursuant to paragraph (a)(3)(i)(B) of this section and convert that quotient to a percent.

(ii) The nationally recognized statistical rating organization must determine the relative standing of the person in terms of the person's contribution to the net revenue of the nationally recognized statistical rating organization for the fiscal year as follows:

(A) For each person from whom the nationally recognized statistical rating organization earned net revenue during the fiscal year, calculate the net revenue attributable to the person earned by the nationally recognized statistical rating organization for the fiscal year from providing all services and products, including credit rating services, to the person;

(B) Make a list that sorts the persons subject to the calculation in paragraph (a)(3)(ii)(A) of this section in order from largest to smallest in terms of the amount of net revenue attributable to the person, as determined pursuant to that paragraph; and

(C) Divide the list generated pursuant to paragraph (a)(3)(ii)(B) of this section into the following categories: top 10%, top 25%, top 50%, bottom 50%, and bottom 25% and determine which category contains the person.

(iii) Identify by name of obligor, security, or money market instrument and, as applicable, CIK number, CUSIP, or ISIN each outstanding credit rating generated as a result of the person paying the nationally recognized statistical rating organization for the

issuance or maintenance of the credit rating and attribute the outstanding credit rating to the person.

(b) A nationally recognized statistical rating organization must prominently include the following statement indicating where on its Internet Web site the consolidated report required pursuant to paragraph (a)(1) of this section is located each time the nationally recognized statistical rating organization publishes a credit rating or credit ratings in a research report, press release, announcement, database, Internet Web site page, compendium, or any other written communication that makes the credit rating publicly available for free or a reasonable fee: "revenue information about persons that paid the nationally statistical rating organization for the issuance or maintenance of a credit rating is available at: [insert address to Internet Web site]."

(c) For purposes of this section:

(1) The term credit rating services means any of the following: rating an obligor (regardless of whether the obligor or any other person paid for the credit rating); rating an issuer's securities or money market instruments (regardless of whether the issuer, underwriter, or any other person paid for the credit rating); and providing credit ratings, credit ratings data, or credit ratings analysis to a subscriber.

(2) The term net revenue means revenue earned for any type of service or product provided to a person, regardless of whether related to credit rating services, and net of any rebates and allowances paid or owed to the person.

PART 249b—FURTHER FORMS, SECURITIES EXCHANGE ACT OF 1934

4. The authority citation for part 249b continues to read in part as follows:

Authority: 15 U.S.C. 78a et seq., unless otherwise noted;

* * * * *

5. Form NRSRO (referenced in § 249b.300) is amended by revising Exhibit 6 in Item 9 to read as follows:

Note: The text of Form NRSRO does not and this amendment will not appear in the Code of Federal Regulations.

Form NRSRO

* * * * *

9. Exhibits * * *

* * * * *

Exhibit 6. Information concerning conflicts of interest or potential conflicts of interest relating to the issuance of credit ratings by the credit rating agency.

☐ Exhibit 6 is attached to and made a part of this Form NRSRO.

* * * * *

6. Amend Form NRSRO Instructions (referenced in § 249b.300) by:

a. Revising Instruction A.8.;

b. Adding a Note to the end of Instruction F;

c. Removing the words “withdrawal of registration” and adding in their place the words “withdrawal from registration” in the first sentence of Instruction H, Item 5;

d. Revising Exhibit 6 in Instruction H, Item 9;

e. Removing the words “(See definition below)” from the first sentence of Exhibit 8 in Instruction H, Item 9;

f. Removing the word “person” and adding in its place the words “user of credit rating services” in the first sentence in Exhibit 10, Instruction H, Item 9, and removing

the fifth sentence in Exhibit 10, Instruction H, Item 9, which includes the definitions of "net revenue" and "credit rating services";

g. Redesignating Instruction F as Instruction I; and

h. Revising newly redesignated Instruction I.

The revisions and addition read as follows:

Note: The text of Form NRSRO does not and this amendment will not appear in the Code of Federal Regulations.

FORM NRSRO INSTRUCTIONS

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A. GENERAL INSTRUCTIONS.

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8. ADDRESS - The mailing address for Form NRSRO is:

Division of Trading and Markets

U.S. Securities and Exchange Commission

100 F Street, NE

Washington, DC 20549-7010

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F. INSTRUCTIONS FOR ANNUAL CERTIFICATIONS

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Note to Instruction F: The annual financial reports that an NRSRO must furnish to the Commission pursuant to Section 15E(k) of the Exchange Act and Exchange Act Rules 17g-3(a)(1) through (a)(6), as applicable, should not be furnished as part of the Annual Certification on Form NRSRO. If the fiscal year end of the NRSRO is December 31, however, the financial reports may be furnished in the

same mailing as the Annual Certification. In accordance with Exchange Act Rule 17g-3(b), the NRSRO must attach to each report the certification required by the Rule.

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H. INSTRUCTIONS FOR SPECIFIC LINE ITEMS

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Item 9. Exhibits. *** * ***

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Exhibit 6. Provide in this Exhibit information concerning conflicts of interest or potential conflicts of interest relating to the issuance of credit ratings by the Applicant/NRSRO.

Part A. Identify the types of conflicts of interest relating to the issuance of credit ratings by the Applicant/NRSRO that are material to the Applicant/NRSRO. First, identify the conflicts described in the list below that apply to the Applicant/NRSRO. The Applicant/NRSRO may use the descriptions below to identify an applicable conflict of interest and is not required to provide any further details. Second, briefly describe any other type of conflict of interest relating to the issuance of credit ratings by the Applicant/NRSRO that is not covered in the descriptions below that is material to the Applicant/NRSRO (for example, one the Applicant/NRSRO has established specific policies and procedures to address):

- The Applicant/NRSRO is paid by issuers or underwriters to determine credit ratings with respect to securities or money market instruments they issue or underwrite.

- The Applicant/NRSRO is paid by obligors to determine credit ratings of the obligors.
- The Applicant/NRSRO is paid for services in addition to determining credit ratings by issuers, underwriters, or obligors that have paid the Applicant/NRSRO to determine a credit rating.
- The Applicant/NRSRO is paid by persons for subscriptions to receive or access the credit ratings of the Applicant/NRSRO and/or for other services offered by the Applicant/NRSRO where such persons may use the credit ratings of the Applicant/NRSRO to comply with, and obtain benefits or relief under, statutes and regulations using the term "nationally recognized statistical rating organization."
- The Applicant/NRSRO is paid by persons for subscriptions to receive or access the credit ratings of the Applicant/NRSRO and/or for other services offered by the Applicant/NRSRO where such persons also may own investments or have entered into transactions that could be favorably or adversely impacted by a credit rating issued by the Applicant/NRSRO.
- The Applicant/NRSRO allows persons within the Applicant/NRSRO to:
    - Directly own securities or money market instruments of, or have other direct ownership interests in, obligors or issuers subject to a credit rating determined by the Applicant/NRSRO.
    - Have business relationships that are more than arms length ordinary course business relationships with obligors or issuers subject to a credit rating determined by the Applicant/NRSRO.

- A person associated with the Applicant/NRSRO is a broker or dealer engaged in the business of underwriting securities or money market instruments (identify the person).
- The Applicant/NRSRO has any other material conflict of interest that arises from the issuances of credit ratings (briefly describe).

Part B. Provide the following information concerning revenues of the Applicant/NRSRO. An Applicant must provide this information for the fiscal year ending immediately before the date of the Applicant's initial application to the Commission. An NRSRO with a fiscal year end of December 31 must provide this information as part of its Annual Certification. Otherwise, an NRSRO must provide this information with an Update of Registration not later than 90 days after the end of each fiscal year.

(1) Provide the percentage of total net revenue attributable to the 20 largest users of credit rating services of the Applicant/NRSRO by dividing:

- The total amount of net revenue earned by the Applicant/NRSRO attributable to the 20 largest users of credit rating services of the Applicant/NRSRO; by
- The total amount of the four classifications of revenue of the Applicant as reported in Exhibit 12 to Form NRSRO or the NRSRO as reported in the financial report furnished to the Commission under Exchange Act Rule 17g-3(a)(4).

Note to Part B(1) of Exhibit 6: The 20 largest users of credit rating services includes issuers, subscribers, obligors, and underwriters, and

may not be the same as the list of 20 largest issuers and subscribers identified by the Applicant in Exhibit 10 to Form NRSRO or by the NRSRO in the financial report furnished to the Commission under Exchange Act Rule 17g-3(a)(5).

(2) Provide the percentage of total net revenue attributable to other services and products of the Applicant/NRSRO by dividing:

- The total amount of revenue earned by the Applicant/NRSRO for "all other services and products" of the Applicant as reported in Exhibit 12 to Form NRSRO or of the NRSRO as reported in the financial report furnished to the Commission under Exchange Act Rule 17g-3(a)(4); by
- The total amount of the four classifications of revenue of the Applicant as reported in Exhibit 12 to Form NRSRO or of the NRSRO as reported in the financial report furnished to the Commission under Exchange Act Rule 17g-3(a)(4).

* * * * *

Exhibit 10. Provide in this Exhibit a list of the largest users of credit rating services of the Applicant by the amount of net revenue earned by the Applicant attributable to the user of credit rating services during the fiscal year ending immediately before the date of the initial application. First, determine and list the 20 largest issuers and subscribers in terms of net revenue. Next, add to the list any obligor or underwriter that, in terms of net revenue during the fiscal year, equaled or exceeded the 20th largest issuer or subscriber. In making the list, rank the

persons in terms of net revenue from largest to smallest and include the net revenue amount for each person.

An NRSRO is not required to make this Exhibit publicly available on its Web site, or through another comparable, readily accessible means pursuant to Exchange Act Rule 17g-1(i). An NRSRO may request that the Commission keep this Exhibit confidential by marking each page "Confidential Treatment" and complying with Commission rules governing confidential treatment (See 17 CFR 200.80 and 17 CFR 200.83). The Commission will keep the information and documents in the Exhibit confidential upon request to the extent permitted by law.

* * * * *

I. EXPLANATION OF TERMS.

1. COMMISSION - The U. S. Securities and Exchange Commission.
2. CREDIT RATING [Section 3(a)(60) of the Exchange Act] - An assessment of the creditworthiness of an obligor as an entity or with respect to specific securities or money market instruments.
3. CREDIT RATING AGENCY [Section 3(a)(61) of the Exchange Act] - Any person:
    - engaged in the business of issuing credit ratings on the Internet or through another readily accessible means, for free or for a reasonable fee, but does not include a commercial credit reporting company;
    - employing either a quantitative or qualitative model, or both to determine credit ratings; and

- receiving fees from either issuers, investors, other market participants, or a combination thereof.

4. CREDIT RATING SERVICES - Any of the following services:
    - rating an obligor (regardless of whether the obligor or any other person paid for the credit rating);
    - rating an issuer's securities or money market instruments (regardless of whether the issuer, underwriter, or any other person paid for the credit rating); and
    - providing credit ratings, credit ratings data, or credit ratings analysis to a subscriber.
5. NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATION [Section 3(a)(62) of the Exchange Act] - A credit rating agency that:
    - has been in business as a credit rating agency for at least the 3 consecutive years immediately preceding the date of its application for registration as an NRSRO;
    - issues credit ratings certified by qualified institutional buyers in accordance with Section 15(a)(1)(B)(ix) of the Exchange Act with respect to:
        - financial institutions, brokers, or dealers;
        - insurance companies;
        - corporate issuers;
        - issuers of asset-backed securities;

- issuers of government securities, municipal securities, or securities issued by a foreign government; or
- a combination of one or more of the above; and

- is registered as an NRSRO.

6. NET REVENUE - revenue earned by the Applicant/NRSRO for any type of service or product provided to a person, regardless of whether related to credit rating services, and net of any rebates and allowances the Applicant/NRSRO paid or owes to the person.

7. PERSON - An individual, partnership, corporation, trust, company, limited liability company, or other organization (including a separately identifiable department or division).

8. PERSON WITHIN AN APPLICANT/NRSRO – The person furnishing Form NRSRO identified in Item 1, any credit rating affiliates identified in Item 3, and any partner, officer, director, branch manager, or employee of the person or the credit rating affiliates (or any person occupying a similar status or performing similar functions).

9. SEPARATELY IDENTIFIABLE DEPARTMENT OR DIVISION - A unit of a corporation or company:

- that is under the direct supervision of an officer or officers designated by the board of directors of the corporation as responsible for the day-to-day conduct of the corporation's credit rating activities for one or more affiliates, including the supervision of all employees engaged in the performance of such activities; and

- for which all of the records relating to its credit rating activities are separately created or maintained in or extractable from such unit's own facilities or the facilities of the corporation, and such records are so maintained or otherwise accessible as to permit independent examination and enforcement by the Commission of the Exchange Act and rules and regulations promulgated thereunder.

10. QUALIFIED INSTITUTIONAL BUYER [Section 3(a)(64) of the Exchange Act] - An entity listed in 17 CFR 230.144A(a) that is not affiliated with the credit rating agency.

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By the Commission.

Elizabeth M. Murphy
Secretary

Dated: November 23, 2009