

MEMO# 23359

March 27, 2009

ICI Comment Letter on SEC Proposed Amendments to NRSRO Rules

[23359]

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TO: SEC RULES MEMBERS No. 33-09
EQUITY MARKETS ADVISORY COMMITTEE No. 14-09
MUNICIPAL SECURITIES ADVISORY COMMITTEE No. 11-09
FIXED-INCOME ADVISORY COMMITTEE No. 9-09
MONEY MARKET FUNDS ADVISORY COMMITTEE No. 12-09
INST. MONEY MARKET FUNDS ADVISORY COMMITTEE No. 12-09 RE: ICI COMMENT LETTER
ON SEC PROPOSED AMENDMENTS TO NRSRO RULES

As we previously informed you, the Securities and Exchange Commission has re-proposed amendments to its existing rules governing the conduct of nationally recognized statistical rating organizations (“NRSROs”). [\[1\]](#) The rule amendments would (1) require the public disclosure of credit rating histories for all outstanding issuer-paid credit ratings issued by an NRSRO and (2) prohibit an NRSRO from issuing an issuer-paid rating for a structured finance product unless the information about the product is made available to other NRSROs. The Institute has prepared the attached comment letter on the proposal. The most significant aspects of the letter are summarized below.

I. Re-Proposed Rules for NRSROs

A. Credit Rating Histories

The proposal would require the public disclosure of credit rating histories for all outstanding issuer-paid credit ratings issued by an NRSRO. The letter states that credit rating histories can provide investors with useful information regarding the performance of an NRSRO’s credit rating for a particular security and information regarding the quality and accuracy of

an NRSRO's ratings as compared with other NRSROs. The letter therefore generally supports the proposed disclosure, but it questions whether the proposal, as currently structured, will provide investors with timely and sufficient information that will allow them to develop meaningful performance measurement statistics to supplement the information provided by NRSROs and to assist in their investment decisions.

1. 12-Month Delay is Too Long

The proposal would provide that a rating action need not be made publicly available until 12 months after the date of the rating action. The letter opposes the proposed 12-month time lag for making information publicly available because such a timeframe would not meet the stated goal of the proposal to make it easier for persons to analyze the actual performance and accuracy of the NRSRO's credit ratings.

The letter notes that the Institute, in its comment letter on the SEC's prior NRSRO proposal, opposed the provision that would have provided a six-month delay before requiring disclosure of rating actions, noting that such a lengthy delay would largely defeat the purpose of the proposal and make such information stale and ineffectual for users of ratings. The letter states that the 12-month delay for publication of this information under the current proposal would exacerbate these concerns. The letter therefore urges the Commission to require the public dissemination of this information in a more timely manner that would be beneficial to investors, e.g., three months after the date of the rating action.

2. The Proposal Should Apply to All Credit Ratings

The proposal would apply only to issuer-paid NRSROs in recognition of the claim by some commenters that mandated disclosure of credit rating history information would impinge upon NRSROs' revenues in a way that could prove anti-competitive. The letter recommends that the proposal be applied to all credit ratings, including those issued by subscriber-paid NRSROs. The letter states that investors should be provided with the tools to assess the value of all ratings, whether issued by issuer-paid NRSROs or subscriber-paid NRSROs.

B. Disclosure of Rating Information to Other NRSROs

The Commission's proposal would prohibit an NRSRO from issuing a rating for a structured finance product unless the information about the product provided to the NRSRO to determine the rating, and thereafter to monitor the rating, is made available to other NRSROs. The letter states that the Institute has long favored increased competition among NRSROs. The letter therefore supports facilitating the dissemination of increased information to other NRSROs to support the issuance of additional credit ratings.

1. Increase Disclosure of Information to Investors

The proposal provides that the requisite information be provided to other NRSROs only. The letter states that by proposing to limit disclosure to NRSROs only, however, the Commission reinforces the current system in which investors must rely on NRSROs for much of the data regarding a structured finance product. The letter therefore reiterates the Institute's prior recommendation that the Commission require that information made available to NRSROs also be made available to investors. The letter notes that this recommendation to disclose more information to investors is not limited to structured finance securities but also to other debt securities, particularly municipal securities.

2. Impose Due Diligence Requirements for NRSROs

The proposal does nothing to assure that the information received by an NRSRO from an issuer is accurate. To address this concern, the letter recommends that NRSROs be held to basic standards of conducting due diligence on the information they review to issue ratings. It states that NRSROs should be required to have policies and procedures in place to reasonably assess the credibility of this information, and to disclose these policies and procedures to facilitate understanding of an NRSRO's actions. Further, NRSROs should provide disclosure regarding the limitations of the available information or data, any decisions they make to compensate for any missing information or data, and any risks involved with the assumptions and methodologies they use in providing a rating. The letter also reiterates the Institute's prior recommendation that NRSROs to have policies and procedures to assess the credibility of information they receive and to disclose the steps (and results of the steps) undertaken to verify information about the assets underlying a security.

C. Create a Standardized NRSRO Term Sheet

The letter states that while the amount and quality of information disclosed by NRSROs is critical to investors, presenting this information in a standardized format may be just as important. To address these concerns, the letter recommends that the Commission require that NRSROs, as a condition of rating a security, provide investors with a presale report providing a specific set of standardized information for each category of structured finance products. The letter suggests that the information to be included in the presale report could be based on a subset of information provided to an NRSRO.

II. Increase Disclosure by Issuers to Investors

The proposal acknowledges that investors and other market participants may benefit from greater disclosure of information about structured finance products but it states that the Commission believes that the more appropriate mechanism to enhance such disclosure would be to amend rules under the Securities Act. The letter recommends that the Commission amend the existing disclosure regime for issuers of those products set out in the Securities Act, particularly Regulation AB.

A. Amend the Securities Act to Require Increased Disclosure to Investors

To enhance disclosure for structured finance products, the letter recommends that the Commission amend the existing disclosure regime for issuers of those products set out in the Securities Act, particularly Regulation AB.

1. Expand the Scope of Regulation AB

The letter discusses the current disparity in disclosure requirements between “asset-backed securities” as defined under Regulation AB and instruments that fall outside that definition. It recommends that the scope of Regulation AB be expanded to include the various collateralized and pooled products that fall within the Commission’s broad definition of “structured finance product” under the NRSRO rules. Specifically, it states that there should be corresponding disclosure requirements for such products so that investors receive, at a minimum, disclosure equivalent to that required of asset-backed securities under Regulation AB. The letter therefore urges the Commission to reevaluate the line-drawing exercise that it undertook in formulating the definition of “asset-backed security” in light of market and product developments since the adoption of Regulation AB.

2. Expand the Disclosure Required Under Regulation AB

In addition to expanding the scope of Regulation AB, the letter recommends that the Commission require that additional information be disclosed pursuant to Regulation AB. Specifically, it recommends that the Commission require that additional information be disclosed pursuant to Regulation AB and that this information be standardized for each category of structured finance products and disseminated in a manner that provides sufficient specificity to be meaningful. In addition, the letter recommends that the categories of information be regularly evaluated and updated to account for newly developed structured finance products, and that the disclosure provided under Regulation AB be ongoing. It also recommends that, at the very least, the Commission provide guidance on the disclosure that issuers should provide.

B. Create an Issuer Term Sheet of Select Information Provided to NRSROs

The letter states that while the Institute believes that it would be beneficial for investors to receive much of the same information that issuers provide to NRSROs, we are cognizant of concerns that such disclosure may, among other things, create a chilling effect on information that an issuer may provide to an NRSRO. To address these issues, the letter recommends that the Commission require public disclosure of a subset of certain standardized items provided by issuers to NRSROs in the form of a term sheet or other document, similar to the “informational and computational materials” permitted under Regulation AB. This would create a two-tier disclosure regime in which issuers would provide information to NRSROs as they currently do and issuers would distribute to investors a required template of standardized information of a more summary nature.

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[Attachment](#)

endnotes

[\[1\]](#) See *Re-Proposed Rules for Nationally Recognized Statistical Rating Organizations*, SEC Release No. 34-59343 (February 2, 2009), 74 FR 6485 (February 9, 2009) ("Proposal").

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