SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 232, 240, 249, and 249b

[Release No. 34–64514; File No. S7–18–11]

RIN 3235–AL15

Nationally Recognized Statistical Rating Organizations

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rules.

SUMMARY: In accordance with the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") and to enhance oversight, the Securities and Exchange Commission ("Commission") is proposing amendments to existing rules and new rules that would apply to credit rating agencies registered with the Commission as nationally recognized statistical rating organizations ("NRSROs"). In addition, in accordance with the Dodd-Frank Act, the Commission is proposing a new rule and form that would apply to providers of third-party due diligence services for asset-backed securities. Finally, the Commission is proposing amendments to existing rules and a new rule that would implement a requirement added by the Dodd-Frank Act that issuers and underwriters of asset-backed securities make publicly available the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter. The Commission is requesting comment on the proposed rule amendments and new rules.

DATES: Comments should be received on or before August 8, 2011.

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic Comments

- Use the Commission's Internet comment form (*http://www.sec.gov/rules.shtml*); or
- Send an e-mail to *rule-comments@sec.gov.* Please include File Number S7–18–11 on the subject line; or
- Use the Federal eRulemaking Portal (*http://www.regulations.gov*). Follow the instructions for submitting comments.

Paper Comments

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549–1090.

All submissions should refer to File Number S7–18–11. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (*http://www.sec.gov/rules.shtml*). Comments are also available for public inspection and copying in the Commission's Public Reference Room, 100 F Street NE., Washington, DC 20549. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make publicly available.

FOR FURTHER INFORMATION CONTACT: Michael A. Macchiaroli, Associate Director, at (202) 551–5525; Thomas K. McGowan, Deputy Associate Director, at (202) 551–5521; Randall W. Roy, Assistant Director, at (202) 551–5522; Raymond A. Lombardo, Branch Chief, at (202) 551–5755; Rose Russo Wells, Senior Counsel, at (202) 551–5527; Joseph I. Levinson, Special Counsel, at (202) 551–5598; or Timothy C. Fox, Special Counsel, at (202) 551–5687; Division of Trading and Markets; or, with respect to the proposals for issuers and underwriters of asset-backed securities, Eduardo A. Aleman, Special Counsel, Division of Corporation Finance at (202) 551–3430; Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549–7010.

SUPPLEMENTARY INFORMATION: The Commission, with respect to NRSROs, is proposing amendments to rules 17 CFR 232.101 ("Rule 101 of Regulation S–T"), 17 CFR 232.201 ("Rule 201 of Regulation S–T"), 17 CFR 240.17g–1 ("Rule 17g–1"), 17 CFR 240.17g–2 ("Rule 17g–2"), 17 CFR 240.17g–3 ("Rule 17g–3"), 17 CFR 240.17g–5 ("Rule 17g–5"), 17 CFR 240.17g–6 ("Rule 17g–6"), 17 CFR 240.17g–7 ("Rule 17g–7"), 17 CFR 249b.300 ("Form NRSRO"), and proposing new rules 17 CFR 240.17g–8 ("Rule 17g–8") and 17 CFR 240.17g–9 ("Rule 17g–9").

In addition, the Commission, with respect to providers of third-party due diligence services for asset-backed securities, is proposing new rules 17 CFR 240.17g–10 ("Rule 17g–10") and 17 CFR 249b.400 ("Form ABS Due Diligence-15E").

Finally, the Commission, with respect to issuers and underwriters of asset-backed securities, is proposing amendments to 17 CFR 232.314 ("Rule 314 of Regulation S–T") and 17 CFR 249.1400 ("Form ABS 15G"), and proposing new rule 17 CFR 240.15Ga–2 ("Rule 15Ga–2").

I. Background

Title IX, Subtitle C of the Dodd-Frank Act,[1] "Improvements to the Regulation of Credit Rating Agencies," among other things, establishes new self-executing requirements applicable to NRSROs, requires certain studies,[2] and requires that the Commission adopt rules applicable to NRSROs in a number of areas.[3] The NRSRO provisions in the

[1] Public Law 111–203, 124 Stat. 1376, H.R. 4173 (July 21, 2010).

[2] *See* Public Law 111–203 §§ 939, 939D–939F. On December 17, 2010, the Commission issued a request for comments to inform a required study on standardizing credit ratings terminology. *See Credit Rating Standardization Study,* Securities Exchange Act of 1934 ("Exchange Act") Release No. 34–63573 (December 17, 2010). On May 10, 2011, the Commission issued a request for comments to assist it in carrying out a required study on, among other matters, the feasibility of establishing a system in which a public or private utility or a self-regulatory organization assigns NRSROs to determine credit ratings for structured finance products. *See Solicitation of Comment to Assist in Study on Assigned Credit Ratings,* Exchange Act Release No. 64456 (May 10, 2011). The Commission also is required to conduct a study of the independence of NRSROs and how that independence affects the ratings issued by NRSROs. The Comptroller General of the United States is required to conduct a study on alternative means for compensating NRSROs in order to create incentives to provide more accurate credit ratings as well as a study on the feasibility and merits of creating an independent professional organization for rating analysts employed by NRSROs.

[3] *See* Public Law 111–203 §§ 931–939H. In addition, Title IX, Subtitle D, "Improvements to the Asset-Backed Securitization Process," contains Section 943, which provides that the Commission shall adopt rules, within 180 days, requiring an NRSRO to include in any report accompanying a credit rating of an asset-backed security a description of the representations, warranties, and enforcement mechanisms available to investors and how they differ from the representations, warranties, and enforcement mechanisms in issuances of similar securities. *See* Public Law 111–203 § 943. On January 20, 2011, the Commission adopted Rule 17g– 7 to implement Section 943. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* Securities Act of 1933 ("Securities Act") Release No. 9175 (Jan. 20, 2011), 76 FR 4489 (Jan. 26, 2011) and 17 CFR 240.17g–7. Prior to enactment of the Dodd-Frank Act and the adoption of Rule 17g–7, the Commission proposed a different rule to be codified at 17 CFR 240.17g–7. *See Proposed Rules for Nationally Recognized Statistical Rating Organizations,* Exchange Act Release No. 57967 (June 16, 2008), 73 FR 36212 (June 25, 2008). This proposed rule would have required an NRSRO to publish a report containing certain information with the publication of a credit rating for a structured finance product or, as an alternative, use ratings symbols for structured finance products that differentiate them from the credit ratings for other types of debt securities. *Id.* In November 2009, the Commission announced it was deferring consideration of action on the proposal and separately proposed a different rule to be codified at 17 CFR 240.17g–7 that would have required an NRSRO to annually disclose certain information. *See Proposed Rules for Nationally Recognized Statistical Rating Organizations* Exchange Act Release No. 61051 (Nov. 23, 2009), 74 FR 63866 (Dec. 4, 2009). Although the Commission adopted Rule 17g–7 on January 20, 2011 to implement

Dodd-Frank Act augment the Credit Rating Agency Reform Act of 2006 (the "Rating Agency Act of 2006"), which established a registration and oversight program for NRSROs through self-executing provisions added to the Exchange Act and implementing rules adopted by the Commission under the Exchange Act as amended by the Rating Agency Act of 2006.[4] Title IX, Subtitle C of the Dodd-Frank Act also provides that the Commission shall prescribe the format of a certification that providers of third-party due diligence services would need to provide to each NRSRO producing a credit rating for an asset-backed security to which the due diligence services relate.[5] Finally, Title IX, Subtitle C of the Dodd-Frank Act establishes a new requirement for issuers and underwriters of asset-backed securities to make publicly available the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter.[6]

II. The Proposed New Rules and Rule Amendments

The Commission's proposed rule amendments and proposed new rules to implement Title IX, Subtitle C of the Dodd-Frank Act are described below.[7]

A. Internal Control Structure

1. Self-Executing Requirement

Section 932(a)(2)(B) of the Dodd-Frank Act added paragraph (3) to Section 15E(c) of the Exchange Act.[8] Section 15E(c)(3)(A) requires an NRSRO to "establish, maintain, enforce, and document an effective internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings, taking into consideration such factors as the Commission may prescribe, by rule."[9] While Section 15E(c)(3)(A) provides that the Commission "may" prescribe factors an NRSRO would need to take into consideration with respect to an internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings (an "internal control structure"), the requirement that an NRSRO "establish, maintain, enforce, and document an effective internal control structure" is self-executing.[10] Consequently, an NRSRO must adhere to this self-executing provision irrespective of whether the Commission prescribes factors the NRSRO must take into consideration.[11]

The Commission preliminarily believes it would be appropriate at this time to defer prescribing factors an NRSRO must take into consideration with respect to its internal control structure. Deferring rulemaking would provide the Commission with the opportunity, through the NRSRO examination process and, as discussed below, the submission of annual reports by the NRSROs, to review how the NRSROs have complied with this self-executing requirement.[12] This review could inform any future rulemaking the Commission may initiate. Nonetheless, the Commission is requesting extensive comment below on whether it would be appropriate as part of this rulemaking to prescribe factors. Based on the comments received, the Commission may decide to prescribe by rule or identify through guidance the factors an NRSRO would need to consider with respect to its internal control structure.

Request for Comment

The Commission generally requests comment on all aspects of Section 15E(c)(3)(A) of the Exchange Act. The Commission also seeks comment on the following:

1. Should the Commission, as part of this rulemaking initiative, prescribe factors that an NRSRO would need to take into consideration when establishing, maintaining, enforcing, and documenting an effective internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings? For example, can the objectives of the self-executing requirement in Section 15E(c)(3)(A) of the Exchange Act be adequately achieved by NRSROs if the Commission does not prescribe factors?

Section 943 of the Dodd-Frank Act, the November 23, 2009 proposal remains outstanding.

[4] *See* Public Law 109–291 (2006). The Rating Agency Act of 2006, among other things, amended Section 3 of the Exchange Act to add definitions, added Section 15E to the Exchange Act to establish self-executing requirements on NRSROs and provide the Commission with the authority to implement a registration and oversight program for NRSROs, amended Section 17 of the Exchange Act to provide the Commission with recordkeeping, reporting, and examination authority over NRSROs, and amended Section 21B(a) of the Exchange Act to provide the Commission with the authority to assess penalties in administrative proceedings instituted under Section 15E of the Exchange Act. *See* Public Law 109–291 §§ 3 and 4 and 15 U.S.C. 78c, 78o–7, 78q, and 78u–2. The Commission adopted rules to implement a registration and oversight program for NRSROs in June 2007. *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* Exchange Act Release No. 55857 (June 5, 2007), 72 FR 33564 (June 18, 2007). The implementing rules were Form NRSRO, Rule 17g–1, Rule 17g–2, Rule 17g–3, Rule 17g–4, Rule 17g–5, and Rule 17g–6. The Commission has twice adopted amendments to some of these rules. *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* Exchange Act Release No. 59342 (Feb. 2, 2009), 74 FR 6456 (Feb. 9, 2009) and *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* Exchange Act Release No. 61050 (Nov. 23, 2009), 74 FR 63832 (Dec. 4, 2009). The Commission also has proposed further amendments to these rules, which remain pending. *See Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63866 (Dec. 4, 2009). In addition, as noted above, the Commission adopted Rule 17g–7 on January 20, 2011.

[5] *See* Public Law 111–203 § 932(a)(8) adding new paragraph (s)(4)(C) to Section 15E of the Exchange Act. 15 U.S.C. 78o–7(s)(4)(C).

[6] *See* Public Law 111–203 § 932(a)(8) adding new paragraph (s)(4)(A) to Section 15E of the Exchange Act. 15 U.S.C. 78o–7(s)(4)(A).

[7] As used throughout this release, the term "category" of credit rating refers to a distinct level in a rating scale represented by a unique symbol, number, or score. For example, if a rating scale consists of symbols (*e.g.,* AAA, AA, A, BBB, BB, B, CCC, CC, and C), each unique symbol would represent a category in the rating scale. Similarly, if a rating scale consists of numbers (*e.g.,* 1, 2, 3, 4, 5, 6, 7, 8, and 9), each number would represent a category in the rating scale. Each category also represents a "notch" in the rating scale. In addition, some NRSRO rating scales attach additional symbols or numbers to the symbols representing categories in order to denote gradations within a category. For example, a rating scale may indicate gradations within a category by attaching a plus or a minus or a number to a rating symbol. For example, AA+, AA, and AA− or AA1, AA2, and AA3 would be three gradations within the AA category. If a rating scale has gradations within a category, each category and gradation within a category would constitute a "notch" in the rating scale. For example, the following symbols would each represent a notch in the rating scale in descending order: AAA, AA+, AA, AA−, A+, A, A−, BBB+, BBB, BBB−, BB+, BB, BB−, CCC+, CCC, CCC−, CC, C and D. Furthermore, for the purposes of this release, changing a credit rating (*e.g.,* upgrading or downgrading the credit rating) means assigning a credit rating at a different notch in the rating scale (*e.g.,* downgrading an obligor assigned an AA rating to an AA− rating or an A+ rating). A "rating action" for the purposes of this release does not necessarily mean changing a credit rating. A rating action is taken when an NRSRO issues an expected or preliminary credit rating before it issues an initial credit rating, issues an initial credit rating, upgrades an existing credit rating, downgrades an existing credit rating (including to a default category), places an existing credit rating on credit watch or review (meaning the NRSRO is actively evaluating whether to change the credit rating), affirms (or confirms) an existing credit rating (meaning the NRSRO announces that it will not change the credit rating), or withdraws a credit rating.

[8] *See* Public Law 111–203 § 932(a)(2)(B) and 15 U.S.C. 78o–7(c)(3)(A).

[9] *Id.*

[10] *Id.*

[11] *Id.*

[12] Section 923(a)(8) of the Dodd-Frank Act struck existing Section 15E(p) of the Exchange Act, which related to the date of applicability of the Rating Agency Act of 2006 and added new Section 15E(p). *See* Public Law 111–203 § 932(a)(8). New Section 15E(p)(3) of the Exchange Act requires, among other things, the Commission staff to conduct an examination of each NRSRO at least annually. *See* 15 U.S.C. 78o–7(p)(3). The Commission staff intends to conduct such annual statutory examinations on a cycle based on the Commission's fiscal year. The staff intends to conduct the first annual statutory examination of a newly registered NRSRO in the annual cycle following its registration.

2. Alternatively, should the Commission defer rulemaking in order to review through examination and monitoring the effectiveness of the internal control structures each NRSRO establishes, maintains, enforces, and documents pursuant to Section 15E(c)(3)(A) of the Exchange Act? For example, would it be more appropriate for the Commission to evaluate through examination and the annual reports discussed below in Section II.A.3 of this release whether there is a need to prescribe factors and, if such a need is identified, incorporate in rulemaking or guidance best practices identified through examination and NRSRO reporting?

3. If appropriate to prescribe factors now, should the factors address all elements of the self-executing requirement in Section 15E(c)(3)(A) of the Exchange Act (*i.e.,* the *establishment, maintenance, enforcement,* and *documentation* of the internal control structure) or should the factors focus on the design (*i.e., establishment*) of the internal control structure or one of the other elements or a combination of some of the elements?

4. If appropriate to prescribe factors now for the *establishment* of an internal control structure, what should those factors be? For example, should the Commission prescribe any of the factors identified in the sub-paragraphs below? In analyzing these potential factors, commenters should address the potential advantages, disadvantages, benefits, and costs that could result if the Commission prescribed any of the factors, as well as the potential effectiveness of the controls and any practical issues related to implementing them.

a. Controls reasonably designed to ensure that a newly developed methodology or proposed update to an in-use methodology for determining credit ratings is subject to an appropriate review process (*e.g.,* by persons who are independent from the persons that developed the methodology or methodology update) and to management approval prior to the new or updated methodology being employed by the NRSRO to determine credit ratings; [13]

b. Controls reasonably designed to ensure that a newly developed methodology or update to an in-use methodology for determining credit ratings is disclosed to the public for consultation prior to the new or updated methodology being employed by the NRSRO to determine credit ratings, that the NRSRO makes comments received as part of the consultation publicly available, and that the NRSRO considers the comments before implementing the methodology;

c. Controls reasonably designed to ensure that in-use methodologies for determining credit ratings are periodically reviewed (*e.g.,* by persons who are independent from the persons who developed and/or use the methodology) in order to analyze whether the methodology should be updated;

d. Controls reasonably designed to ensure that market participants have an opportunity to provide comment on whether in-use methodologies for determining credit ratings should be updated, that the NRSRO makes any such comments received publicly available, and that the NRSRO considers the comments;

e. Controls reasonably designed to ensure that newly developed or updated quantitative models proposed to be incorporated into a credit rating methodology are evaluated and validated prior to being put into use;

f. Controls reasonably designed to ensure that quantitative models incorporated into in-use credit rating methodologies are periodically reviewed and back-tested;

g. Controls reasonably designed to ensure that an NRSRO engages in analysis before commencing the rating of a class of obligors, securities, or money market instruments the NRSRO has not previously rated to determine whether the NRSRO has sufficient competency, access to necessary information, and resources to rate the type of obligor, security, or money market instrument;

h. Controls reasonably designed to ensure that an NRSRO engages in analysis before commencing the rating of an "exotic" or "bespoke" type of obligor, security, or money market instrument to review the feasibility of determining a credit rating;

i. Controls reasonably designed to ensure that measures (*e.g.,* statistics) are used to evaluate the performance of credit ratings as part of the review of in-use methodologies for determining credit ratings to analyze whether the methodologies should be updated or the work of the analysts employing the methodologies should be reviewed;

j. Controls reasonably designed to ensure that, with respect to determining credit ratings, the work and conclusions of the lead credit analyst developing an initial credit rating or conducting surveillance on an existing credit rating is reviewed by other analysts, supervisors, or senior managers before a rating action is formally taken (*e.g.,* having the work reviewed through a rating committee process);

k. Controls reasonably designed to ensure that a credit analyst documents the steps taken in developing an initial credit rating or conducting surveillance on an existing credit rating with sufficient detail to permit an after-the-fact review or internal audit of the rating file to analyze whether the analyst adhered to the NRSRO's procedures and methodologies for determining credit ratings;

l. Controls reasonably designed to ensure that the NRSRO conducts periodic reviews or internal audits of rating files to analyze whether analysts adhere to the NRSRO's procedures and methodologies for determining credit ratings; or

m. Any other factors that commenters identify and explain.

5. If appropriate to prescribe factors now for the *maintenance* of an internal control structure, what should those factors be? For example, should the Commission prescribe any of the factors identified in the sub-paragraphs below? In analyzing these potential factors, commenters should address the potential advantages, disadvantages, benefits, and costs that could result if the Commission prescribed any of the factors, as well as the potential effectiveness of the controls and any practical issues related to implementing them.

a. Controls reasonably designed to ensure that the NRSRO conducts periodic reviews of whether it has devoted sufficient resources to implement and operate the documented internal control structure as designed;

b. Controls reasonably designed to ensure that the NRSRO conducts periodic reviews or ongoing monitoring to evaluate the effectiveness of the internal control structure and whether it should be updated;

c. Controls designed to ensure that any identified deficiencies in the internal control structure are assessed and addressed on a timely basis;

d. Any other factors that commenters identify and explain.

6. If appropriate to prescribe factors now for the *enforcement* of an internal

[13] Section 15E(t)(3)(A) of the Exchange Act contains a self-executing provision requiring that the board of directors of the NRSRO shall "oversee" the "establishment, maintenance, and enforcement of policies and procedures for determining credit ratings." *See* 15 U.S.C. 78o–7(t)(3)(A). At the same time, Section 15E(r) of the Exchange Act requires the Commission to adopt rules "to ensure that credit ratings are determined using procedures and methodologies, including qualitative and quantitative data and models" that are approved by the board of the NRSRO. *See* 15 U.S.C. 78o–7(r)(1)(A).

control structure, what should those factors be? For example, should the Commission prescribe any of the factors identified in the sub-paragraphs below? In analyzing these potential factors, commenters should address the potential advantages, disadvantages, benefits, and costs that could result if the Commission prescribed any of the factors, as well as the potential effectiveness of the controls and any practical issues related to implementing them.

a. Controls designed to ensure that additional training is provided or discipline taken with respect to employees who fail to adhere to requirements imposed by the internal control structure;

b. Controls designed to ensure that a process is in place for employees to report failures to adhere to the internal control structure; or

c. Any other factors that commenters identify and explain?

7. If appropriate to prescribe factors now for the *documentation* of an internal control structure, what should those factors be? For example, should there be a factor relating to the level of written detail about the internal control structure that should be documented? Are there other factors that should be considered? What potential advantages, disadvantages, benefits, and costs would result if the Commission prescribed any such factors?

8. Identify any other factors that an NRSRO should consider when establishing, maintaining, enforcing, and documenting an internal control structure. Explain the utility of any factors identified as well as the potential advantages, disadvantages, benefits, and costs that could result if the Commission prescribed any such factors.

2. Proposed Amendment to Rule 17g–2

As noted above, Section 15E(c)(3)(A) of the Exchange Act requires an NRSRO, among other things, to *document* its internal control structure.[14] Thus, the statute itself requires the NRSRO to make this record.[15] However, the statute does not prescribe how an NRSRO would need to maintain this record.[16] The Commission preliminarily believes this record should be subject to the same recordkeeping requirements applicable to other records an NRSRO is required to retain pursuant to the NRSRO recordkeeping rule—Rule 17g–2.[17] Consequently, the Commission proposes adding new paragraph (b)(12) to Rule 17g–2 to identify the internal control structure an NRSRO, among other things, must document pursuant to Section 15E(c)(3)(A) of the Exchange Act as a record that must be retained.[18] As a result, the various retention and production requirements of paragraphs (c), (d), (e), and (f) of Rule 17g–2 would apply to the documented internal control structure.[19]

Request for Comment

The Commission generally requests comment on all aspects of proposed new paragraph (b)(12) of Rule 17g–2.

3. Proposed Amendments to Rule 17g–3

Section 15E(c)(3)(B) of the Exchange Act provides that the Commission shall prescribe rules requiring an NRSRO to "submit" an annual internal controls report to the Commission, which shall contain: (1) A description of the responsibility of management in establishing and maintaining an effective internal control structure; (2) an assessment of the effectiveness of the internal control structure; and (3) the attestation of the chief executive officer ("CEO") or equivalent individual.[20] Rule 17g–3 requires an NRSRO to furnish annual reports to the Commission.[21] In particular, paragraph (a) of Rule 17g–3 requires an NRSRO to furnish five or, in some cases, six separate reports within 90 days after the end of the NRSRO's fiscal year and identifies the reports that must be furnished.[22] The first report—the NRSRO's financial statements—must be audited; the remaining reports may be unaudited.[23] Paragraph (b) of Rule 17g–3 provides that the NRSRO must attach to the reports a signed statement by a duly authorized person that the person has responsibility for the reports and, to the best knowledge of the person, the reports fairly present, in all material respects, the information contained in the reports.[24]

The Commission proposes amending paragraphs (a) and (b) of Rule 17g–3 to implement the rulemaking mandated by Section 15E(c)(3)(B) of the Exchange Act.[25] The proposed amendment would add a new paragraph (a)(7) to require an NRSRO to file an additional report—the report on the NRSRO's internal control structure—with its annual submission of reports pursuant to Rule 17g–3.[26] As discussed above in Section II.A.1 of this release, the Commission preliminarily believes it would be appropriate at this time to defer prescribing factors an NRSRO must take into consideration with respect to its internal control

[14] *See* 15 U.S.C. 78o–7(c)(3)(A).

[15] *Id.*

[16] *Id.* For example, it does not prescribe how long the document must be retained.

[17] 17 CFR 240.17g–2(c), (d), (e), and (f). Section 17(a)(1) of the Exchange Act requires an NRSRO to make and keep such records, and make and disseminate such reports, as the Commission prescribes by rule as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the Exchange Act. 15 U.S.C. 78q(a)(1). The Commission preliminarily believes it would be necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the Exchange Act to apply the record retention requirements of Rule 17g–2 to the internal control structure required pursuant to Section 15E(c)(3)(A) of the Exchange Act (15 U.S.C. 78o–7(c)(3)(A)). *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33582 (June 18, 2007) ("The Commission designed [Rule 17g–2] based on its experience with recordkeeping rules for other regulated entities. These other books and records rules have proven integral to the Commission's investor protection function because the preserved records are the primary means of monitoring compliance with applicable securities laws. Rule 17g–2 is designed to ensure that an NRSRO makes and retains records that will assist the Commission in monitoring, through its examination authority, whether an NRSRO is complying with the provisions of Section 15E of the Exchange Act and the rules thereunder.") (footnotes omitted).

[18] *See* proposed new paragraph (b)(12) of Rule 17g–2.

[19] *See* 17 CFR 240.17g–2(c), (d), (e) and (f). Paragraph (c) of Rule 17g–2 requires an NRSRO to retain the records identified in paragraphs (a) and (b) for three years after the date the record is made or received. 17 CFR 240.17g–2(c). Paragraph (d) requires, among other things, that an NRSRO maintain each record identified in paragraphs (a) and (b) in a manner that makes the original record or copy easily accessible to the principal office of the NRSRO. 17 CFR 240.17g–2(d). Paragraph (e) sets forth the requirements that apply when an NRSRO uses a third-party custodian to maintain its records. 17 CFR 240.17g–2(e). Paragraph (f) requires an NRSRO to promptly furnish the Commission with legible, complete, and current copies, and, if specifically requested, English translations, of the records identified in paragraphs (a) and (b), or any other records of the NRSRO subject to examination under Section 17(b) of the Exchange Act. *See* 17 CFR 240.17g–2(f); *see also* 15 U.S.C. 78q(b).

[20] *See* 15 U.S.C. 78o–7(c)(3)(B)(i)–(iii).

[21] *See* 17 CFR 240.17g–3.

[22] *See* 17 CFR 240.17g–3(a)(1)–(6).

[23] *Id.*

[24] *See* 17 CFR 240.17g–3(b).

[25] *See* 15 U.S.C. 78o–7(c)(3)(B)(i)–(iii). In addition, as a technical amendment, the Commission proposes to amend the title of Rule 17g–3 to replace the words "financial reports" with the words "financial and other reports." The Commission notes that the report identified in paragraph (a)(6) of Rule 17g–3, the proposed internal control report, and the compliance report discussed below in Section II.K of this release are not financial in nature. The Commission also proposes to add the word "filed" in the title of Rule 17g–3. As discussed below in Section II.M.1 of this release, the Commission is proposing amendments to Rules 17g–1 and 17g–3 to treat certain submissions of Form NRSRO and the Rule 17g–3 annual reports as being "filed" as opposed to being "furnished" to conform to amendments the Dodd-Frank Act made to Section 15E of the Exchange Act. *See* Public Law 111–203 § 932(a). Specifically, the reports identified in paragraphs (a)(1), (2), (3), (4), (5), (7) and (8) of Rule 17g–3 would be "filed" and the report identified in paragraph (a)(6) would be "furnished."

[26] *See* proposed new paragraph (a)(7) of Rule 17g–3.

structure. For similar reasons, the Commission preliminarily believes it would be appropriate at this time to implement Sections 15E(c)(3)(B)(i) and (ii) of the Exchange Act through rule text that closely mirrors the statute.[27] Consequently, proposed new paragraph (a)(7) would require that the internal control report contain: (1) a description of the responsibility of management in establishing and maintaining an effective internal control structure; and (2) an assessment by management of the effectiveness of the internal control structure.[28] As is the case with the reports currently identified in paragraphs (a)(2) through (a)(6) of Rule 17g–3, the report identified in new paragraph (a)(7) would be unaudited.[29] While the proposed rule text closely mirrors the statutory text, the Commission is requesting extensive comment below on whether it would be appropriate as part of this rulemaking to provide more explanation in terms of the standards to use in preparing the internal controls report and providing information in the report. Based on the comments received, the Commission may decide to prescribe by rule or identify through guidance such standards.

Section 15E(c)(3)(B)(iii) of the Exchange Act provides that the annual internal controls report must contain an attestation of the NRSRO's CEO, or equivalent individual.[30] Accordingly, the Commission proposes amending paragraph (b) of Rule 17g–3 to require that the NRSRO's chief executive officer, or, if the firm does not have a CEO, an individual performing similar functions, provide a signed statement that would need to be attached to the report.[31]

Request for Comment

The Commission generally requests comment on all aspects of these proposed amendments to paragraphs (a) and (b) of Rule 17g–3. The Commission also seeks comment on the following:

1. Is the requirement to provide a description of the responsibility of management in establishing and maintaining an effective internal control structure sufficiently explicit? If not, how should the Commission modify proposed paragraph (a)(7) of Rule 17g–3 to make the requirement more understandable? For example, should the Commission provide guidance on how an NRSRO must describe the responsibility of management in establishing and maintaining an effective internal control structure? If so, what should that guidance be? For example, are there existing frameworks that such guidance could be modeled on?

2. In terms of establishing an effective internal control structure, what level of NRSRO management should have primary responsibility for the design of the internal control structure and what level of management should supervise the design of the internal control structure? For example, should managers with direct responsibility for supervising the personnel who use the policies, procedures, and methodologies for determining credit ratings and the personnel who conduct compliance reviews for adherence to those policies, procedures, and methodologies design the internal control structure and a committee of the NRSRO's most senior managers supervise the design of the internal control structure? Should other management or non-management levels of the NRSRO have responsibility for either of these functions? In addition, Section 15E(t)(3)(C) of the Exchange Act provides that the board of directors of the NRSRO shall "oversee" the "effectiveness of the internal control system with respect to the policies and procedures for determining credit ratings."[32] How should this statutorily mandated board responsibility be integrated with the responsibility of the NRSRO's management to establish an effective internal control structure?

3. In terms of establishing an effective internal control structure, should the Commission define the term "internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings"? In terms of establishing an effective internal control structure, should the Commission further define the term "internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings"? If so, how should that term be further defined?[33] Provide suggested rule text and supporting analysis.

4. In terms of establishing an effective internal control structure, should the Commission prescribe a standard in terms of the design? If so, what standard would be appropriate? For example, should the internal control structure be "reasonably designed" to achieve its objectives (a standard required by Sections 15E(g) and (h) of the Exchange Act with respect to policies and procedures of an NRSRO to address, respectively, the misuse of material nonpublic information and conflicts of interest)?[34] Conversely, is the proposed requirement that the internal control structure be "effective" a sufficient standard?

5. In terms of maintaining an effective internal control structure, what level of NRSRO management should have primary responsibility for monitoring the operation of the internal control structure and the NRSRO's adherence to the internal control structure? For example, should managers with direct responsibility for supervising the personnel who use the policies, procedures, and methodologies for determining credit ratings and the personnel who conduct compliance reviews for adherence to those policies, procedures, and methodologies have day-to-day responsibility for monitoring the operation of the internal control structure and the NRSRO's adherence to the internal control structure? Should other management or non-management levels of the NRSRO have responsibility for either of these functions? For example, should the personnel responsible for monitoring the operation of the internal control structure and the NRSRO's adherence to the internal control structure generate periodic (weekly, monthly, quarterly, and/or annual) reports that are provided to the NRSRO's most senior managers and the board about the internal control structure? If so, what information should be contained in those reports? In addition, Section 15E(t)(3)(C) of the Exchange Act provides that the board of directors of the NRSRO shall "oversee" the "effectiveness of the internal control system with respect to the policies and

[27] *See* 15 U.S.C. 78o–7(c)(3)(B)(i) and (ii).

[28] *Compare* 15 U.S.C. 78o–7(c)(3)(B)(i) and (ii) with proposed new paragraphs (a)(7)(i) and (ii) of Rule 17g–3.

[29] *See* proposed new paragraph (a)(7) of Rule 17g–3.

[30] 15 U.S.C. 78o–7(c)(3)(B)(iii).

[31] *See* proposed amendments to paragraph (b) of Rule 17g–3. In particular, the Commission proposes re-organizing existing paragraph (b) of Rule 17g–3 into paragraphs (b)(1) and (b)(2). Paragraph (b)(1) would contain the current requirement that the NRSRO must attach to each of the annual reports required pursuant to paragraphs (a)(1)-(6) a signed statement by a duly authorized person associated with the NRSRO stating that the person has responsibility for the financial reports and, to the best knowledge of the person, the reports fairly present, in all material respects, the information required to be contained in the report. Paragraph (b)(2) of Rule 17g–3 would require that the report on the NRSRO's internal control structure be attested to by the NRSRO's CEO or an individual performing similar functions. *See* proposed paragraph (b)(2) of Rule 17g–3.

[32] *See* 15 U.S.C. 78o–7(t)(3)(A).

[33] The term "internal control" has been defined in other contexts. For example, the Commission has defined internal control over financial reporting. *See* 17 CFR 240.13a–15(f).

[34] *See* 15 U.S.C. 78o–7(g) and (h).

procedures for determining credit ratings." [35] How should this statutorily mandated board responsibility be integrated with the responsibility of the NRSRO's management to maintain an effective internal control structure?

6. Is the requirement to provide an assessment by management of the effectiveness of the internal control structure sufficiently explicit? If not, how should the Commission modify proposed paragraph (a)(7) of Rule 17g–3 to make the requirement more understandable? For example, given that the NRSRO needs to maintain the internal control structure (*i.e.,* keep it in operation), should the Commission clarify that the assessment should address the effectiveness of the internal control structure during the entire fiscal year covered by the report?

7. In terms of reporting management's assessment of the effectiveness of the internal control structure, should the Commission provide guidance on how an NRSRO must assess the effectiveness of the internal control structure, such as evaluative criteria or standards? If so, what should those criteria or standards be? For example, should the Commission require that management's assessment of the effectiveness of the internal control structure be based on procedures sufficient to evaluate the design of the internal control structure and test its operating effectiveness?

8. In terms of management's assessment of the effectiveness of the internal control structure, should the Commission define the conditions that preclude management from concluding that the internal control structure is effective? If so, how should an ineffective internal control structure be defined? For example, should management be precluded from concluding that the internal control structure is effective if there are one or more instances of "material weaknesses" in the internal control structure? If one or more instances of "material weaknesses" should preclude management from concluding that its internal control structure is effective, then should the Commission define "material weakness"? If so, how should the term "material weakness" be defined? If management cannot conclude that the internal control structure is effective, what corrective action or sanctions should be imposed on the NRSRO?

9. In terms of reporting management's assessment of the effectiveness of the internal control structure, should the Commission provide guidance regarding the topics to be addressed in the report? If so, what should that guidance be? For example, if the Commission prescribes factors that an NRSRO should take into consideration in establishing, maintaining, enforcing, and documenting its internal control structure, should the report specifically reference those factors? In addition, should the report identify or describe the framework management used to conduct the evaluation of the effectiveness of the internal control structure? Moreover, should the report identify deficiencies found during the assessment process? If so, should all deficiencies be identified or only those which preclude management from concluding that the internal control structure is effective? Furthermore, should the Commission require that the report disclose whether there were any significant changes in the internal control structure or other factors that could significantly affect the internal control structure subsequent to the date of the evaluation, including any corrective actions in response to any material weaknesses found during the evaluation?

10. In terms of reporting management's assessment of the effectiveness of the internal control structure, should the report identify any fraud, significant errors, or previously undisclosed conflicts of interest identified during the assessment of the effectiveness of the internal control structure that could have a material effect on the integrity of the NRSRO's procedures and methodologies for determining credit ratings? What other disclosures should the report contain?

11. Should an NRSRO be required to maintain evidential matter, including documentation, to provide reasonable support for management's assessment of the effectiveness of the internal control structure that could be used by Commission examination staff to review the adequacy of the assessment? In this regard, should the Commission identify specific objectives of an internal control structure that the evidential matter would need to support? For example, should the evidential matter provide reasonable support for an assessment that the internal control structure is designed to effectively prevent or detect failures of the NRSRO to adhere to its policies, procedures, and methodologies for determining credit ratings? If such specific objectives should be identified, describe them and identify the evidential matter that could be retained to allow the Commission examination staff to review the adequacy of the NRSRO's assessment of the effectiveness of the internal control structure in achieving the objective.

12. With respect to proposed paragraph (b)(2) of Rule 17g–3, should the Commission provide more guidance on the type of management responsibilities that would qualify an individual as one who performs functions similar to a CEO? If so, what are those types of responsibilities?

13. Should the Commission require the internal control report to be filed separately from the Rule 17g–3 annual reports (which are kept confidential to the extent permitted by law) and, instead, require the internal control report to be disclosed to the public on, for example, the Commission's Electronic Data Gathering, Analysis, and Retrieval ("EDGAR") system? What would be the benefits and costs of requiring the public disclosure of the report?

14. If it would be appropriate to make the report public, should the Commission prescribe a form for the report? If so, what information should the form require the NRSRO to provide in the disclosure? What would the form look like? Could any of the Commission's current forms serve as a model? If so, identify the forms and explain how they could be tailored to require an NRSRO to provide information about its internal control structure.

B. Conflicts of Interest Relating to Sales and Marketing

Section 932(a)(4) of the Dodd-Frank Act added new paragraph (3) to Section 15E(h) of the Exchange Act.[36] Section 15E(h)(3)(A) of the Exchange Act provides that the Commission shall issue rules to prevent the sales and marketing considerations of an NRSRO from influencing the production of credit ratings by the NRSRO.[37] Section 15E(h)(3)(B) of the Exchange Act provides that the Commission's rules must contain two additional provisions.[38] First, Section 15E(h)(3)(B)(i) requires that the Commission's rules shall provide for exceptions for small NRSROs with respect to which the Commission determines that the separation of the production of ratings and sales and marketing activities is not appropriate.[39] Second, Section 15E(h)(3)(B)(ii) requires that the Commission's rules shall provide for the suspension or revocation of the registration of an NRSRO if the Commission finds, on the record, after notice and opportunity for a hearing,

[35] *See* 15 U.S.C. 78o–7(t)(3)(A).

[36] Public Law 111–203 § 932(a)(4) and 15 U.S.C. 78o–7(h)(3).

[37] 15 U.S.C. 78o–7(h)(3)(A).

[38] 15 U.S.C. 78o–7(h)(3)(B)(i) and (ii).

[39] 15 U.S.C. 78o–7(h)(3)(B)(i).

that: (1) The NRSRO has committed a violation of a rule issued under Section 15E(h) of the Exchange Act; and (2) the violation affected a rating.[40]

The Commission proposes to implement Sections 15E(h)(3)(A), (B)(i), and (B)(ii) of the Exchange Act by amending the NRSRO conflict of interest rule—Rule 17g–5.[41] The proposals would amend the rule by: (1) identifying a new prohibited conflict in paragraph (c) of the rule; (2) adding a new paragraph (f) setting forth the finding the Commission would need to make in order to grant a small NRSRO an exemption from the prohibition; and (3) adding a new paragraph (g) setting forth the standard for suspending or revoking an NRSRO's registration for violating a rule adopted under Section 15E(h) of the Exchange Act.

1. Proposed New Prohibited Conflict

As noted above, Section 15E(h)(3)(A) of the Exchange Act provides that the Commission shall issue rules to prevent the sales and marketing considerations of an NRSRO from influencing the production of ratings by the NRSRO.[42] The Commission is proposing to implement this provision by identifying a new conflict of interest in paragraph (c) of Rule 17g–5.[43] Paragraph (c) prohibits a person within an NRSRO (as well as the NRSRO itself)[44] from having any of the conflicts of interest relating to the issuance or maintenance of a credit rating or credit rating agency identified in the paragraph under all circumstances (hereinafter the "absolute prohibitions").[45] Proposed new paragraph (c)(8) of Rule 17g–5 would identify a new absolute prohibition; namely, one in which the NRSRO issues or maintains a credit rating where a person within the NRSRO who participates in the sales or marketing of a product or service of the NRSRO or a product or service of a person associated with the NRSRO also participates in determining or monitoring the credit rating, or developing or approving procedures or methodologies used for determining the credit rating, including qualitative or quantitative models.[46]

The proposed new absolute prohibition would be designed to address situations in which, for example, individuals within the NRSRO responsible for selling its products and services could seek to influence a specific credit rating to favor an existing or prospective client or the development of a credit rating methodology to favor a class of existing or prospective clients. With regard to methodologies, the Commission notes that its staff found as part of the examination of the activities of the three largest NRSROs in rating residential mortgage-backed securities ("RMBS") and collateralized debt obligations ("CDOs") linked to subprime mortgages that it appeared "employees responsible for obtaining ratings business would notify other employees, including those responsible for criteria development, about business concerns they had related to the criteria."[47] The absolute prohibition in proposed paragraph (c)(8) of Rule 17g–5 would be designed to insulate individuals within the NRSRO responsible for the analytic function from such sales and marketing concerns and pressures.

Request for Comment

The Commission generally requests comment on all aspects of proposed new paragraph (c)(8) of Rule 17g–5. The Commission also seeks comment on the following:

1. Would the proposed amendment impact existing governance structures, reporting lines and internal organizations of NRSROs, particularly smaller NRSROs? If so, provide specific information about the nature and consequences of such impacts.

2. Are there sales and marketing activities persons that participate in determining credit ratings or developing or approving procedures or methodologies used for determining credit ratings, including qualitative or quantitative models, could participate in without undermining the goal of proposed paragraph (a)(8) of Rule 17g–5? If so, what types of activities? How could proposed new paragraph (a)(8) of Rule 17g–5 be modified to retain an absolute prohibition and at the same time not prohibit persons who participate in determining credit ratings or developing or approving procedures or methodologies used for determining credit ratings, including qualitative or quantitative models, to participate in sales and marketing activities that do not expose them to business concerns that could compromise their analytical integrity?

3. Should the Commission provide guidance on what constitutes a sales and marketing activity? If so, how should the Commission define "sales and marketing activities"? In addition, should the Commission define what it means to "participate in sales and marketing activities"? Similarly, should the Commission define what it means to "participate in developing or approving procedures and methodologies used for determining credit ratings"? If so, how should the Commission define these terms?

4. Identify other requirements applicable to NRSROs that are designed to address this conflict of interest.

2. Proposed Exemption for "Small" NRSROs

Section 15E(h)(3)(B)(i) of the Exchange Act requires that the Commission's rules under Section 15E(h)(3)(A) shall provide for exceptions for small NRSROs with respect to which the Commission determines that the separation of the production of ratings and sales and marketing activities is not appropriate.[48] To implement this provision, the Commission is proposing to amend Rule 17g–5 by adding a new paragraph (f).[49] Proposed paragraph (f) would provide a mechanism for a small NRSRO to apply in writing for an exemption from the absolute prohibition proposed in new paragraph (c)(8).[50] In particular,

[40] 15 U.S.C. 78o–7(h)(3)(B)(ii).

[41] 17 CFR 240.17g–5. The Commission adopted and subsequently amended Rule 17g–5 pursuant, in part, to authority in Section 15E(h)(2) of the Exchange Act (15 U.S.C. 78o–7(h)(2)). *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33595–33599 (June 18, 2007); *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6465–6469 (Feb. 9, 2009); *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63842–63850 (Dec. 4, 2009).

[42] 15 U.S.C. 78o–7(h)(3)(A).

[43] *See* proposed new paragraph (c)(8) of Rule 17g–5.

[44] *See* paragraph (d) of Rule 17g–5 defining "person within an NRSRO" for purposes of the rule. 17 CFR 240.17g–5(d).

[45] *See* 17 CFR 240.17g–5(c)(1)–(7). These absolute prohibitions are distinguished from the types of conflicts identified in paragraph (b) of Rule 17g–5, which are prohibited *unless* the NRSRO has taken the steps to address them set forth in paragraph (a) of Rule 17g–5. *See* 17 CFR 240.17g–5(a) and (b).

[46] *See* proposed new paragraph (c)(8) of Rule 17g–5.

[47] *See Summary Report of Issues Identified in the Commission Staff's Examination of Select Credit Rating Agencies,* Commission (July 2008), pp. 25–26.

[48] *See* 15 U.S.C. 78o–7(h)(3)(B)(i).

[49] *See* proposed new paragraph (f) of Rule 17g–5.

[50] Section 36 of the Exchange Act provides that the Commission, by rule, regulation, or order, may conditionally or unconditionally exempt any person, security, or transaction, or any class or classes of persons, securities or transactions from any provision or provisions of the Exchange Act or any rule or regulation thereunder, to the extent that such exemption is necessary or appropriate in the public interest and is consistent with the protection of investors. 17 U.S.C. 78mm. Consequently, an NRSRO could request to be exempt from the proposed sales and marketing prohibition pursuant to this more general authority in Section 36. *See id.* Nonetheless, the Commission has adopted rules providing mechanisms for registrants—such as broker-dealers—to request an exemption from specific rule requirements. *See, e.g.,* 17 CFR 240.15c3–1(b)(3); 17 CFR 240.15c3–3(k)(3); and 17 CFR 240.17a–5(m)(3). The Commission preliminarily believes proposed paragraph (f) of Rule 17g–5 should parallel such provisions.

proposed new paragraph (f) of Rule 17g–5 would provide that upon written application by an NRSRO, the Commission may exempt, either conditionally or unconditionally or on specified terms and conditions, such NRSRO from the provisions of paragraph (c)(8) of Rule 17g–5 if the Commission finds that due to the small size of the NRSRO it is not appropriate to require the separation within the NRSRO of the production of credit ratings from sales and marketing activities and such exemption is in the public interest.[51]

The Commission preliminarily believes that the absolute prohibition should apply to all NRSROs. However, the Commission notes that in some cases the small size of an NRSRO could make a complete separation of the sales and marketing function from the credit rating analytical function inappropriate. For example, the NRSRO may not have enough staff (or the resources to hire additional staff) to establish separate functions. In such a case, the Commission would entertain requests for relief. In granting such relief, the Commission may impose conditions designed to preserve as much of the separation between these two functions as possible.

Request for Comment

The Commission generally requests comment on all aspects of proposed new paragraph (f) of Rule 17g–5. The Commission also seeks comment on the following:

1. The Commission notes that Section 15E(h)(3)(A) of the Exchange Act provides that the Commission shall issue rules to prevent the sales and marketing considerations of an NRSRO from influencing the production of credit ratings by the NRSRO. Section 15E(h)(3)(B)(i) requires that the Commission's rules shall provide for exceptions for small NRSROs with respect to which the Commission determines that the *separation* of the production of ratings and sales and marketing activities is not appropriate (emphasis added). Why would the separation of the production of ratings from sales and marketing activities be appropriate for NRSROs that are not small but might not be appropriate for NRSROs that are small? For example, does the small size of an NRSRO make the conflict less likely to influence ratings? If so, why? Alternatively, could the small size of an NRSRO make the application of the absolute prohibition impractical, thus preventing a small credit rating agency from seeking registration or a small NRSRO from maintaining its registration? If so, would the adverse impact on competition outweigh the benefit of applying the absolute prohibition to a small NRSRO? If so, explain how.

2. Would the case-by-case approach proposed by the Commission appropriately implement Section 15E(h)(3)(B)(i) of the Exchange Act? If not, how should the proposal be modified? For example, should the Commission prescribe an objective self-executing exemption from the absolute prohibition in proposed paragraph (c)(8) of Rule 17g–5? For example, should the exemption be automatic for "small" NRSROs? If so, how should the Commission define a small NRSRO? For example, should the definition be based on the total assets of the NRSRO? In this regard, should the Commission adopt a rule that exempts any NRSRO that has total assets of $5 million or less from the absolute prohibition given that is how the Commission currently defines a small NRSRO for purposes of the Regulatory Flexibility Act?[52] How would such an exemption work in practice? For example, would such a rule need to provide for a transition period for an NRSRO that crosses the total asset threshold to provide time to establish the separate sales and marketing function? How long should such a transition period be? For example, should it be 90, 120, 180 or some other number of days after the required filing date of the NRSRO's audited financial statements indicating the threshold was crossed are required to be filed with the Commission?

3. What other factors should the Commission consider in analyzing whether the small size of an NRSRO makes it not appropriate to require the separation of the production of credit ratings from sales and marketing activities? Should the Commission consider the annual revenues of the NRSRO? Should the Commission consider the number of employees of the NRSRO? Would consideration of the number of employees create a disincentive to devote resources to adequately staff the NRSRO? Are there factors in addition to an NRSRO's size the Commission should consider in analyzing whether to grant an exemption under this proposal? If so, please describe any such factors.

4. If the Commission granted relief to an NRSRO, should the Commission specify conditions for obtaining the relief? If so, what should those conditions be? For example, should the conditions limit the number of credit analysts that can participate in sales and marketing activities, limit the manner in which they can participate in such activities, require additional procedures to address the conflict, and require additional procedures to document how credit analysts participate in sales and marketing activities? If any of these conditions would be appropriate, describe how they could be implemented in practice.

3. Suspending or Revoking a Registration

Section 15E(h)(3)(B)(ii) of the Exchange Act specifies that the Commission's rules under Section 15E(h) of the Exchange Act shall provide for suspension or revocation of the registration of an NRSRO if the Commission finds, on the record, after notice and opportunity for a hearing, that the NRSRO has committed a violation of "a rule issued under this subsection" and the violation of the rule affected a credit rating.[53] While Section 15E(h)(3)(A) relates only to the conflict arising from sales and marketing activities, Section 15E(h)(3)(B)(ii)—by using the term "subsection"—has a broader scope in that it refers to all rules issued under Section 15E(h) of the Exchange Act.[54] Consequently, the rule implementing Section 15E(h)(3)(B)(ii) must provide for the suspension or revocation of an NRSRO's registration for violations of any rule adopted under Section 15E(h).[55] Moreover, the Commission notes that Section 15E(h)(3)(B)(ii) does not require that the violation of the rule be "willful."[56]

Currently, the Commission can seek to suspend or revoke the registration of an NRSRO, in addition to other potential sanctions, under Section 15E(d) of the Exchange Act.[57] In particular, Section 15E(d) provides that the Commission shall, by order, censure, place limitations on the activities, functions, or operations of, suspend for a period not exceeding 12 months, or revoke the registration of an NRSRO if the Commission finds, "on the record after notice and opportunity for a hearing," that such sanction is

[51] *See* proposed new paragraph (f) of Rule 17g–5.

[52] *See* Section VII.C of this release; *see also* 5 U.S.C. 603(a), *Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR 33618 (June 18, 2007); *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6481 (Feb. 9, 2009); and *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63863 (Dec. 4, 2009).

[53] 15 U.S.C. 78o–7(h)(3)(B)(ii).

[54] *See id.*

[55] *Id.*

[56] *Id.*

[57] *See* 15 U.S.C. 78o–7(d).

"necessary for the protection of investors and in the public interest" and the NRSRO, or a person associated with the NRSRO, has engaged in one or more of six categories of conduct.[58] The first category is that the NRSRO or an associated person has: committed or omitted any act, or has been subject to an order or finding, enumerated in subparagraphs (A), (D), (E), (G), or (H) of Section 15(b)(4) of the Exchange Act; has been convicted of any offense identified in Section 15(b)(4)(B) of the Exchange Act; or has been enjoined from any action, conduct, or practice identified in Section 15(b)(4)(C) of the Exchange Act.[59] The acts enumerated in Section 15(b)(4)(D) of the Exchange Act include that the person has willfully violated any provision of the Exchange Act or the rules or regulations under the Exchange Act.[60] Therefore, the Commission has the ability, under Section 15E(d), to suspend or revoke the registration of an NRSRO for a willful violation of Rule 17g–5, but does not have the power to do so under Section 15E(d) for violations of Rule 17g–5 that are not willful.[61]

The Commission preliminarily believes a rule implementing Section 15E(h)(3)(B)(ii) of the Exchange Act should work in conjunction with Sections 15E(d) and 21C of the Exchange Act.[62] Specifically, proposed new paragraph (g) of Rule 17g–5 would provide that in a proceeding pursuant to Section 15E(d) or Section 21C of the Exchange Act, the Commission shall suspend or revoke the registration of an NRSRO if the Commission finds in such proceeding that the NRSRO has violated a rule issued under Section 15E(h) of the Exchange Act, the violation affected a rating, and that suspension or revocation is necessary for the protection of investors and in the public interest.[63] The Commission preliminarily believes this provision is appropriately placed in Rule 17g–5 given that it is the predominant rule issued under Section 15E(h) of the Exchange Act.[64]

The first two proposed findings in proposed paragraph (g) of Rule 17g–5 would mirror the text of Section 15E(h)(3)(B)(ii) of the Exchange Act.[65] The final finding—that the suspension or revocation is necessary for the protection of investors and in the public interest—is a common finding that the Commission must make to take disciplinary action against a registered person or entity.[66] It is not, however, a finding that the Commission must make in a proceeding under Section 21C.[67] Further, unlike Section 15E(d) of the Exchange Act, the Commission can take action under Section 21C for violations of the securities laws even if such violations are not willful.[68] Moreover, Section 15E(h)(3)(B)(ii) of the Exchange Act does not prescribe the maximum amount of time for which an NRSRO could be suspended, whereas Section 15E(d) provides that a suspension shall not exceed 12 months.[69] Consequently, a proceeding pursuant to paragraph (g) of Rule 17g–5 brought under Section 21C could result in a suspension that exceeds 12 months. Given that Section 21C of the Exchange Act has a lower threshold for the intent to establish a violation, and given the substantial consequences of suspending or revoking a registration, the Commission preliminarily believes that the public interest finding would be an appropriate predicate to a suspension or revocation of an NRSRO's registration under Section 21C of the Exchange Act.

Request for Comment

The Commission generally requests comment on all aspects of proposed new paragraph (g) of Rule 17g–5. The Commission also seeks comment on the following:

1. Should the Commission propose, pursuant to Section 15E(h)(3)(B)(ii) of the Exchange Act, an independent and alternative process for suspending or revoking an NRSRO's registration for a violation of a rule issued under Section 15E(h) (*i.e.,* a proceeding that is not pursuant to Sections 15E(d) and 21C of the Exchange Act)? If so, how should such a separate proceeding operate? For example, should it require the same findings proposed above or alternative or additional findings?

2. In terms of the finding that "the violation affected a rating," what type of factual predicate should support such a finding? For example, would it be appropriate to make such a finding if the Commission determined that the violation caused the NRSRO to issue a credit rating that was not based solely on its documented procedures and methodologies for determining credit ratings (*e.g.,* the Commission finds that undue influence impacted the credit rating assigned to the rated obligor, security, or money market instrument because strictly adhering to the procedures and methodologies would have resulted in the NRSRO issuing a credit rating at a lower or higher notch in the applicable rating scale)?

3. With respect to proposed new paragraph (g) of Rule 17g–5, should the proposed rule include additional or alternative findings that the Commission would need to make to revoke or suspend the registration of an NRSRO in a proceeding under Sections 15E(d) or 21C? If so, what should those findings be? For example, should the Commission need to find that the violation harmed investors or other users of credit ratings?

4. Should the Commission, as proposed, require a public interest finding in order to suspend or revoke an NRSRO's registration in a proceeding under paragraph (g) of Rule 17g–5 pursuant to Section 21C, or should the rule provide for the suspension or revocation of an NRSRO's registration solely based on a finding that a violation of a rule affected a rating?

5. With respect to proposed new paragraph (g) of Rule 17g–5, should the rule incorporate only Section 15E(d) of the Exchange Act? If so, why? Alternatively, should it incorporate only Section 21C of the Exchange Act? If so, why?

6. As noted above, there would be no limit on the amount of time for which the Commission could suspend the registration of an NRSRO in a proceeding under Section 21C of the Exchange Act and proposed paragraph (g) of Rule 17g–5. Should the Commission add such a time limit to be consistent with Section 15E(d) of the Exchange Act? Alternatively, does the

[58] 15 U.S.C. 78o–7(d).

[59] *See* 15 U.S.C. 78o–7(d)(1)(A); *see also* 15 U.S.C. 78o(b)(4)(A), (B), (C), (D), (E), (G), and (H).

[60] 15 U.S.C. 78o(b)(4)(D).

[61] *See* 15 U.S.C. 78o–7(d)(1)(A) and 15 U.S.C. 78o(b)(4)(D).

[62] 15 U.S.C. 78o–7(d) and 15 U.S.C. 78u–3.

[63] *See* proposed new paragraph (g) of Rule 17g–5; *see also* 15 U.S.C. 78o–7(d) and (h), and 78u–3. Section 21C of the Exchange Act provides the Commission with authority, among other things, to enter an order requiring, among other things, that a person cease-and-desist from continuing to violate, or future violations of, a provision of the Exchange Act or any rule or regulation thereunder. Proposed paragraph (g) of Rule 17g–5 would provide that the Commission can issue an order in a cease-and-desist proceeding suspending or revoking the registration of an NRSRO. *Id.*

[64] *See, e.g., Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33595–33599 (June 18, 2007), *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6465–6469 (Feb. 9, 2009), and *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63842–63850 (Dec. 4, 2009).

[65] *Compare* the first two findings in proposed new paragraph (g) of Rule17g–5 (that the NRSRO has violated a rule issued under Section 15E(h) of the Act; and the violation affected a rating) with Sections 15E(h)(3)(B)(ii)(I) and (II) of the Exchange Act, respectively. 15 U.S.C. 78o–7(h)(3)(B)(ii)(I) and (II).

[66] For example, the Commission must make this finding to take action under Section 15E(d) of the Exchange Act. *See* 15 U.S.C. 78o–7(d).

[67] *See* 15 U.S.C. 78u–3.

[68] *Compare* 15 U.S.C. 78o–7(d) and 15 U.S.C. 78u–3.

[69] *Compare* 15 U.S.C. 78o–7(h)(3)(B)(ii) and 15 U.S.C. 78o–7(d).

different standard provide the Commission with appropriate flexibility to seek longer suspensions?

C. "Look-Back" Review

Section 932(a)(4) of the Dodd-Frank Act amended Section 15E(h) of the Exchange Act to add a new paragraph (4).[70] The Commission is proposing to implement rulemaking required in Section 15E(h)(4)(A)(ii) of the Exchange Act through proposed paragraph (c) of new Rule 17g–8.[71] In addition, the Commission is proposing to amend Rule 17g–2 to apply that rule's record retention and production requirements to the policies and procedures required pursuant to the self-executing provisions in Section 15E(h)(4)(A) of the Exchange Act and pursuant to proposed paragraph (c) of new Rule 17g–8.[72]

1. Proposed Paragraph (c) of New Rule 17g–8

Sections 15E(h)(4)(A)(i) and (ii) of the Exchange Act require an NRSRO to establish, maintain, and enforce policies and procedures reasonably designed to ensure that, in any case in which an employee of a person subject to a credit rating of the NRSRO or the issuer, underwriter, or sponsor of a security or money market instrument subject to a credit rating of the NRSRO, was employed by the NRSRO and participated in any capacity in determining credit ratings for the person or the securities or money market instruments during the 1-year period preceding the date an action was taken with respect to the credit rating, the NRSRO shall: (1) Conduct a review to determine whether any conflicts of interest of the employee influenced the credit rating (a "look-back review"); and (2) take action to revise the rating if appropriate, *in accordance with such rules as the Commission shall prescribe.*[73] Consequently, Section 15E(h)(4)(A)(i) of the Exchange Act contains a self-executing provision requiring an NRSRO to establish, maintain, and enforce policies and procedures as described above to conduct look-back reviews, and Section 15E(h)(4)(ii) contains a provision mandating Commission rulemaking with respect to requirements for an NRSRO to revise a credit rating in certain circumstances.[74]

The Commission proposes to implement the rulemaking required in Section 15E(h)(4)(A)(ii) of the Exchange Act by proposing paragraph (c) of new Rule 17g–8.[75] Proposed paragraph (c) would require that the policies and procedures the NRSRO establishes, maintains, and enforces pursuant to Section 15E(h)(4)(A) of the Exchange Act must address instances in which a review conducted pursuant to those policies and procedures determines that a conflict of interest influenced a credit rating assigned to an obligor, security, or money market instrument by including, at a minimum, procedures that are reasonably designed to ensure the NRSRO will: (1) Immediately place the credit rating on credit watch; (2) promptly determine whether the credit rating must be revised so it no longer is influenced by a conflict of interest and is solely the product of the NRSRO's documented procedures and methodologies for determining credit ratings; and (3) promptly publish a revised credit rating, if appropriate, or affirm the credit rating if appropriate.[76]

The Commission acknowledges that Section 15E(c)(2) of the Exchange Act provides, in pertinent part, that the Commission may not regulate the substance of credit ratings or the procedures and methodologies by which an NRSRO determines credit ratings.[77] The Commission preliminarily believes that the steps described above would not regulate the procedures and methodologies by which an NRSRO determines credit ratings because the NRSRO would apply its own procedures and methodologies to determine whether the credit rating should be revised. Moreover, the placement of a credit rating on credit watch is not a determination of a credit rating (*i.e.,* it does not change the credit rating) but rather is a means of providing notice to users of the NRSRO's credit ratings that an active evaluation of the credit rating is underway. For these reasons, the Commission preliminarily believes that the approach in proposed paragraph (c) of new Rule 17g–8 appropriately avoids regulating the substance of credit ratings or the procedures and methodologies an NRSRO uses to determine credit ratings but, at the same time, requires an NRSRO to have procedures reasonably designed to ensure that it immediately provides notification and promptly address a credit rating that is influenced by a conflict of interest.[78] The Commission also preliminarily believes that the actions prescribed in proposed paragraph (c) of new Rule 17g–8 are steps a prudent NRSRO would take in the normal course when discovering a conflict of interest influenced the determination of a credit rating. Nonetheless, the Commission is soliciting comment on these issues below.

Proposed paragraph (c)(1) of new Rule 17g–8 would require the NRSRO to have procedures reasonably designed to ensure that, upon the NRSRO's discovery of the conflict, it immediately publishes a rating action placing the applicable credit ratings of the obligor, security, or money market instrument on credit watch or review.[79] When an NRSRO publishes a rating action indicating the current credit rating assigned to an obligor, security, or money market instrument (or a class of obligors, securities, or money market instruments) is on credit watch or under review, the purpose is to notify users of the NRSRO's credit ratings that the credit rating is undergoing a process of evaluation that may result in it being upgraded or downgraded.[80] The Commission preliminarily believes an NRSRO should have policies and procedures reasonably designed to ensure that the users of its credit ratings are provided immediate notice of the discovery that a conflict influenced a credit rating assigned to an obligor, security, or money market instrument.

[70] *See* Public Law 111–203 § 932(a)(4) and 15 U.S.C. 78o–7(h)(4).

[71] New Rule 17g–8 would be codified at 17 CFR 240.17g–8, if adopted. In addition, new Rule 17g–8, as proposed, would consolidate requirements that NRSROs have policies and procedures in a number of areas. As discussed below in Section II.F.1 of this release, proposed paragraph (a) of new Rule 17g–8 would require an NRSRO to establish policies and procedures with respect to credit rating methodologies. In addition, as discussed below in Section II.J.1 of this release, proposed paragraph (b) of new Rule 17g–8 would require an NRSRO to establish policies and procedures with respect to the use of credit rating symbols, numbers, and scores. And, as discussed in this section of the release, the Commission is proposing to implement rulemaking specified in Section 15E(h)(4)(A)(ii) of the Exchange Act (15 U.S.C. 78o–7(h)(4)(A)(ii)), in part, by proposing paragraph (c) of new Rule 17g–8.

[72] *See* 15 U.S.C. 78o–7(h)(4)(A), proposed paragraph (c) of new Rule 17g–8, and proposed new paragraph (a)(9) of Rule 17g–2.

[73] *See* 15 U.S.C. 78o–7(h)(4)(A)(i) and (ii) (emphasis added).

[74] *Id.*

[75] *See* proposed paragraph (c) of new Rule 17g–8 and 15 U.S.C. 78o–7(h)(4)(A)(ii).

[76] *See* proposed paragraphs (c)(1), (2) and (3) of new Rule 17g–8.

[77] 15 U.S.C. 78o–7(c)(2).

[78] The Commission also notes an NRSRO would, among other things, violate Section 15E(h)(1) of the Exchange Act and Rule 17g–5, among other rules, if it continued to assign an obligor, security, or money, market instrument a credit rating that, absent the undue influence of the conflict of interest, would be different because the NRSRO could not be deemed to have policies and procedures reasonably designed to address and manage conflicts of interest that can arise from its business under such a circumstance. *See* 15 U.S.C. 78o–7(h) and 17 CFR 17g–5.

[79] *See* proposed paragraph (c)(1) of new Rule 17g–8.

[80] For example, an NRSRO may place a credit rating on negative credit watch, which means it is evaluating whether to downgrade the credit rating, or on positive credit watch, which means it is evaluating whether to upgrade the credit rating.

The Commission also preliminarily believes an effective means of providing such notice would be to place the obligor, security, or money market instrument on credit watch.

Proposed paragraph (c)(1) of new Rule 17g–8 also would provide that the policies and procedures must be reasonably designed to ensure the NRSRO includes the information required by paragraph (a)(1)(ii)(J)(*3*)(*i*) of Rule 17g–7 with the publication of the rating action placing the credit rating of the obligor, security, or money market instrument on credit watch.[81] As discussed below in Section II.G of this release, the Commission is proposing to implement Section 15E(s) of the Exchange Act, in part, by requiring, in proposed new paragraph (a) of Rule 17g–7, that an NRSRO generate a form to be included with the publication of a credit rating.[82] Proposed paragraph (a) of Rule 17g–7, among other things, would prescribe certain qualitative and quantitative information that must be disclosed in the form.[83] The Commission is proposing that the qualitative information in the form include certain disclosures that would need to be made if the rating action results from a look-back review conducted pursuant to Section 15E(h)(4)(A)(i) of the Exchange Act and proposed paragraph (c) of new Rule 17g–8.[84] Specifically, when a credit rating is placed on credit watch, proposed new paragraph (a)(1)(ii)(J)(*3*)(*i*) of Rule 17g–7 would require the NRSRO to provide in the form published with the rating action an explanation that the reason for the action is the discovery that a credit rating assigned to the obligor, security, or money market instrument in one or more prior rating actions was influenced by a conflict of interest and the date and associated credit rating of each prior rating action the NRSRO currently has determined was influenced by the conflict.[85] This would alert users of the NRSRO's credit ratings that the credit rating assigned to the obligor, security, or money market instrument might be revised to address a conflict of interest and would identify the prior rating action or actions the NRSRO has determined were influenced by the conflict. With respect to identifying the prior rating actions, the Commission is proposing that the rule require the NRSRO to provide the date and associated credit rating of such actions the NRSRO "currently has determined" were influenced by the conflict.[86] The Commission's proposed use of the term "currently" is designed to conform to the requirement of proposed paragraph (c)(1) of Rule 17g–8 that the NRSRO have procedures designed to place the credit rating of the obligor, security, or money market instrument on credit watch *immediately* upon the discovery that a conflict influenced a prior credit rating action (*i.e.,* not wait until the NRSRO has determined whether additional credit ratings previously assigned to the obligor, security, or money market instrument also were influenced by the conflict). The Commission preliminarily believes that the best approach would be to alert users of the NRSRO's credit ratings as soon as possible after a conflict is discovered.

Proposed paragraph (c)(2) of new Rule 17g–8 would require the NRSRO to have procedures reasonably designed to ensure it promptly determines whether the current credit rating assigned to the obligor, security, or money market instrument must be revised so that it no longer is influenced by a conflict of interest and is solely a product of the documented procedures and methodologies the NRSRO uses to determine credit ratings.[87] The goal would be to ensure as quickly as possible that the credit rating assigned to the obligor, security, or money market instrument is solely a product of the NRSRO's procedures and methodologies for determining credit ratings (*i.e.,* is in no way influenced by the conflict). With respect to making this determination, the Commission preliminarily believes one approach would be to apply *de novo* the NRSRO's procedures and methodologies for determining credit ratings to the rated obligor, security, or money market instrument and revise the current credit rating if the *de novo* application produces a credit rating at a different notch on the rating scale.

The Commission does not expect an NRSRO would revise a credit rating in every circumstance in which an earlier rating action was influenced by a conflict of interest. The Commission preliminarily notes that Section 15E(h)(4)(A)(ii) of the Exchange Act provides that the NRSRO's policies and procedures shall be reasonably designed to, among other things, ensure that the NRSRO takes action to revise the credit rating "if appropriate."[88] It is possible, for example, that in the period since the NRSRO published the conflicted credit rating events unrelated to the conflict occurred that when factored into a *de novo* application of the NRSRO's procedures and methodologies for determining credit ratings would produce a credit rating at the same notch in the rating scale as the credit rating that was influenced by the conflict.[89] The Commission preliminarily believes a requirement that the NRSRO nonetheless revise the credit rating could interfere with the NRSRO's procedures and methodologies for determining credit ratings in that it would force the NRSRO to change the credit rating assigned to the obligor, security, or money market instrument to a different notch in the rating scale than would be the case if the credit rating were solely a product of the NRSRO's procedures and methodologies. Consequently, a mandatory revision requirement could, in effect, require the NRSRO to publish a credit rating that was inaccurate from the perspective of those procedures and methodologies.

Proposed paragraph (c)(3) of new Rule 17g–8 would require that the NRSRO have procedures reasonably designed to ensure it promptly publishes a revised credit rating, if appropriate, or an affirmation of the credit rating, if appropriate, based on the determination of whether the current credit rating assigned to the obligor, security, or money market instrument must be revised.[90] The Commission's intent is for the NRSRO to have procedures that are reasonably designed to notify users of the NRSRO's credit ratings as quickly as possible, whether the credit rating assigned to the obligor, security, or money market instrument will be

[81] *Id.; see also* proposed new paragraph (a)(1)(ii)(J)(*3*)(*i*) of Rule 17g–7.

[82] *See* 15 U.S.C. 78o–7(s) and proposed new paragraph (a) of Rule 17g–7.

[83] *See* proposed new paragraphs (a)(1)(ii)(A)–(N) of Rule 17g–7.

[84] *See* proposed new paragraphs (a)(1)(ii)(J)(*3*)(*i*)–(*iii*) of Rule 17g–7 and related discussion below in Section II.G.3 of the release.

[85] *See* proposed new paragraph (a)(1)(ii)(J)(*3*)(*i*) of Rule 17g–7.

[86] *Id.*

[87] *See* proposed paragraph (c)(2) of new Rule 17g–8.

[88] 15 U.S.C. 78o–7(h)(4)(A)(ii).

[89] For example, assume that nine months ago an analyst upgraded the credit rating assigned to an issuer's securities from BBB to AA. The analyst leaves the NRSRO to work for the issuer. The analyst's new employment triggers a look-back review of the rating action upgrading the credit rating from BBB to AA pursuant to Section 15E(h)(4)(A)(i) of the Exchange Act. The look-back review determines the credit rating should not have been upgraded from BBB to AA at that point in time and the analyst's action in upgrading the credit rating was influenced by the prospect of employment with the issuer. The NRSRO performs a *de novo* review of the credit rating assigned to the issuer by applying its procedures and methodologies for determining credit ratings. This review—as required by the procedures and methodologies—takes into consideration favorable financial results the issuer reported three months ago. Consequently, the process of re-rating the issuer's securities determines the current credit rating should be AA.

[90] *See* proposed paragraphs (c)(3)(i) and (ii) of new Rule 17g–8; *see also* proposed new paragraphs (a)(1)(ii)(J)(3)(ii) and (iii) of Rule 17g–7.

changed or remain the same.[91] The goal would be to promptly remove the uncertainty surrounding the credit rating to limit the potential that investors and other users of credit ratings might make investment or other credit based decisions based on incomplete information.

As with the placement of the credit rating on credit watch, proposed paragraph (c)(3) of new Rule 17g–8 would require that the NRSRO's procedures would need to be reasonably designed to ensure that information required pursuant to proposed new paragraph (a)(1)(ii)(J)(*3*)(ii) and (iii) of Rule 17g–7, respectively, is included with the publication of a revised or affirmed credit rating.[92] In the case of a revised rating, proposed new paragraph (a)(1)(ii)(J)(*3*)(*ii*) of Rule 17g–7 would require the NRSRO to provide in the form published with the rating action an explanation that the reason for the action is the discovery that a credit rating assigned to the obligor, security, or money market instrument in one or more prior rating actions was influenced by a conflict of interest, the date and associated credit rating of each prior rating action the NRSRO has determined was influenced by the conflict, and an estimate of the impact the conflict had on each such prior rating action.[93] Similarly, in the case of an affirmed rating, proposed new paragraph (a)(1)(ii)(J)(*3*)(*iii*) of Rule 17g–7 would require the NRSRO to provide an explanation of why no rating action was taken to revise the credit rating notwithstanding the conflict, the date and associated credit rating of each prior rating action the NRSRO has determined was influenced by the conflict, and an estimate of the impact the conflict had on each such prior rating action.[94]

As indicated in the proposed disclosures, the NRSRO would need to include an estimate of the impact the conflict had on each prior rating action influenced by the conflict.[95] The Commission preliminarily believes one approach an NRSRO could take to making such an estimate would be to apply *de novo* its procedures and methodologies for determining credit ratings to the rated obligor, security, or money market instrument using information and inputs as of the time period for which it was determined that the credit rating was influenced. In other words, under this approach the NRSRO would reconstruct the past rating action through a "conflict-free" application of its procedures and methodologies for determining credit ratings. The NRSRO then could compare the credit ratings and disclose the difference between the rating action that was influenced by a conflict and the reconstructed rating action.

The disclosures required by proposed new paragraphs (a)(1)(ii)(J)(*3*)(*i*), (*ii*) and (*iii*) of Rule 17g–7 would alert users of the NRSRO's credit ratings that the rating action was taken because a conflict of interest had influenced one or more credit ratings assigned to the obligor, security, or money market instrument.[96] In addition, the estimate of the impact of the conflict would provide users of the NRSRO's credit ratings with a sense of the magnitude of the variation between the credit rating influenced by the conflict and the credit rating that would have been determined had the conflict not existed. The users of the NRSRO's credit ratings could consider this information in evaluating the ability of the NRSRO to manage conflicts of interest in the production of credit ratings. Moreover, if the variation between the credit rating influenced by the conflict and the "un-conflicted" credit rating was large (*e.g.,* 2 or 3 notches in the applicable rating scale), users of the NRSRO's credit ratings could consider the potential risk of using the NRSRO's credit ratings to make investment or other credit-based decisions (particularly if the revision downgraded the credit rating to a low category in the rating scale).

Request for Comment

The Commission generally requests comment on all aspects of proposed paragraph (c) of new Rule 17g–8. The Commission also seeks comment on the following:

1. Would the requirements to have procedures reasonably designed to ensure the NRSRO takes the steps set forth in proposed paragraphs (c)(1), (2), and (3) of new Rule 17g–8 alter the procedures and methodologies an NRSRO uses to determine credit ratings? For example, would an NRSRO take materially different steps if a look-back review conducted pursuant to Section 15E(h)(4)(A) of the Exchange Act determined that a credit rating was influenced by a conflict of interest? If so, describe in detail how those steps would differ.

2. Under Section 15E(h)(4)(A)(i) of the Exchange Act, an NRSRO must, in certain circumstances, conduct a review to determine whether any conflicts of interest of an employee influenced the credit rating. Should the Commission define what it means to have a conflict of interest "influence" a credit rating? If so, how should this term be defined? For example, should a credit rating be deemed "influenced" if the NRSRO would have taken a different rating action with respect to the credit rating in the absence of the conflict?

3. How would an NRSRO determine whether this conflict influenced a credit rating? Describe the types of evidence that would support such a determination. What steps could an NRSRO take to analyze whether this conflict influenced a credit rating? Are there any practical issues with respect to making such a determination? If so, describe them.

4. Is there any reason an NRSRO should not have procedures reasonably designed to ensure it immediately publishes a rating action placing the obligor, security, or money market instrument on credit watch based on the discovery of the conflict and include with the publication of the rating action the information required by proposed new paragraph (a)(1)(ii)(J)(3)(*i*) of Rule 17g–7 as would be required by proposed paragraph (c)(1) of Rule 17g–8? If so, please explain in detail the rationale for not disclosing this information immediately in this manner. In addition, if a commenter agrees with the objective of the requirement but not the manner of disclosure, describe any alternative means of disclosure that would achieve the objective.

5. What practical issues should the Commission consider in implementing proposed paragraph (c)(1) of new Rule 17g–8? How could the proposal be modified to address any practical issues identified without undermining the objectives of the proposal?

6. Would the information required by proposed new paragraph (a)(1)(ii)(J)(*3*)(*i*) of Rule 17g–7 to be included in the form published with a rating action placing the obligor, security, or money market instrument on credit watch be useful to the users of the NRSRO's credit ratings? Is there additional or alternative information that should be provided? If so, please describe such additional or alternative information.

[91] The Commission notes that, in the case of an NRSRO that makes its rating actions available only to subscribers, former subscribers who made an investment or other credit based decision using the credit rating likely would not receive notice that the credit rating was influenced by a conflict of interest as well as any changes made to the credit rating as a result of the "look-back" review.

[92] *See* proposed paragraphs (c)(3)(i) and (ii) of new Rule 17g–8.

[93] *See* proposed new paragraph (a)(1)(ii)(J)(*3*)(*ii*) of Rule 17g–7.

[94] *See* proposed new paragraph (a)(1)(ii)(J)(*3*)(*iii*) of Rule 17g–7.

[95] *See* proposed paragraph (c)(2)(i) of new Rule 17g–8; *see also* proposed paragraph (c)(2)(ii) of Rule 17g–8.

[96] *See* proposed paragraphs (a)(1)(ii)(J)(*3*)(*i*), (*ii*) and (*iii*) of Rule 17g–7.

7. Is there any reason an NRSRO would not have procedures reasonably designed to ensure it promptly determines whether the current credit rating assigned to the obligor, security, or money market instrument must be revised so it no longer is influenced by a conflict of interest and is solely a product of the documented procedures and methodologies the NRSRO uses to determine credit ratings as would be required pursuant to proposed paragraph (c)(2) of new Rule 17g–8? If so, please explain in detail the rationale for not promptly making such a determination. In addition, are there alternative approaches to addressing conflicts of interest influencing credit ratings that the Commission should consider? If so, please identify and describe them.

8. What practical issues should the Commission consider in implementing proposed paragraph (c)(2) of new Rule 17g–8? How could the proposal be modified to address any practical issues identified without undermining the objectives of the proposal?

9. Should the Commission be more prescriptive in terms of how an NRSRO would be required to determine whether the current credit rating assigned to the obligor, security, or money market instrument must be revised so it no longer is influenced by a conflict of interest and is solely a product of the documented procedures and methodologies the NRSRO uses to determine credit ratings? If so, what actions should the Commission require be included in the NRSRO's policies and procedures? For example, should the Commission specifically require the NRSRO to apply *de novo* its policies and procedures for determining credit ratings in the ways described above?

10. Would a *de novo* application of the NRSRO's policies and procedures for determining credit ratings be sufficient to address the conflict of interest? Are there alternative or additional approaches to determining whether a credit rating influenced by a conflict of interest should be revised?

11. Is there any reason an NRSRO should not have procedures reasonably designed to ensure that it promptly publishes, as applicable, a revised credit rating or an affirmation of the current credit rating based on the determination of whether the current credit rating assigned to the obligor, security, or money market instrument must be revised and include with the rating action the information required by proposed new paragraphs (a)(1)(ii)(J)(*3*)(*ii*) or (*iii*) of Rule 17g–7, as applicable, as would be required pursuant to paragraph (c)(3) of new Rule 17g–8? If so, please explain in detail the rationale for not promptly revising or affirming the current credit rating.

12. What practical issues should the Commission consider in implementing proposed paragraph (c)(3) of new Rule 17g–8 that would require an NRSRO to have procedures reasonably designed to ensure that it promptly publishes, as appropriate, a revised credit rating or an affirmation of the current credit rating and includes with the rating action the information required by proposed new paragraphs (a)(1)(ii)(J)(*3*)(*ii*) and (*iii*) of Rule 17g–7? For example, would the requirement to estimate the impact the conflict had on the prior rating actions substantially prolong the time between placing the credit rating on credit watch and either publishing a revised credit rating or affirming the current credit rating? How could the proposal be modified to address any practical issues identified without undermining the objective of promptly addressing a credit rating influenced by a conflict of interest and at the same time providing investors and other users of credit ratings with the information about the conflict?

13. In terms of estimating the impact of a conflict on a past rating action, would a feasible approach be to apply *de novo* the procedures and methodologies for determining credit ratings to the relevant obligor, security, or money market instrument using information and inputs as of the time period in which the conflicted credit rating was determined? Would this approach result in a meaningful estimate? Are there alternative or additional steps that could be taken to estimate the impact?

14. Would the information required by proposed new paragraphs (a)(1)(ii)(J)(*3*)(*ii*) and (*iii*) of Rule 17g–7 to be included in the form published with a revised or affirmed credit rating, respectively, be useful to the users of the NRSRO's credit ratings? Is there additional or alternative information that should be provided? If so, please describe such additional or alternative information.

15. How would the proposals impact obligors and issuers subject to a credit rating determined through the "look-back" review to be influenced by the conflict of interest?

16. In the case of an NRSRO that only makes its rating actions available to subscribers, former subscribers likely would not receive the proposed notices. Does this raise a significant issue that the Commission should address? If so, describe alternatives that could be used to address this issue.

2. Proposed Amendment to Rule 17g–2

Section 15E(h)(4)(A) of the Exchange Act requires an NRSRO "to establish, maintain, and enforce policies and procedures" but does not explicitly require an NRSRO to "document" such policies and procedures.[97] Nonetheless, the Commission preliminarily believes that documenting these policies and procedures is necessary in order to carry out the statute's mandate. The Commission also preliminarily believes they should be documented because, among other reasons, it is a sound practice for any organization to document its policies and procedures to promote better understanding of them among the individuals within the organization and thereby to promote compliance with such policies and procedures. In addition, for the reasons discussed in Section II.A.2 of this release, the Commission preliminarily believes that the policies and procedures should be subject to the same recordkeeping requirements that apply to other records an NRSRO is required to retain pursuant to Rule 17g–2.[98] For these reasons, the Commission proposes adding paragraph (a)(9) to Rule 17g–2 to identify the policies and procedures an NRSRO is required to establish, maintain, and enforce pursuant to Section 15E(h)(4)(A) of the Exchange Act and paragraph (c) of Rule 17g–8 as a record an NRSRO must make and retain.[99] As a result, the policies and procedures would need to be documented in writing and be subject to the record retention and production requirements in paragraphs (c) through (f) of Rule 17g–2.[100]

Request for Comment

The Commission generally requests comment on all aspects of proposed new paragraph (a)(9) of Rule 17g–2.

D. Fines and Other Penalties

Section 932(a)(8) of the Dodd-Frank Act amended Section 15E of the Exchange Act to add new subsection (p), which contains four paragraphs: (1), (2), (3), and (4).[101] Section 15E(p)(4)(A) provides that the Commission shall establish, by rule, fines and other penalties applicable to any NRSRO that

[97] *See* 15 U.S.C. 78o–7(h)(4)(A).

[98] 17 CFR 240.17g–2.

[99] *See* proposed new paragraph (a)(9) to Rule 17g–2; *see also* Section 17(a)(1) of the Exchange Act, which requires an NRSRO to make and keep such records, and make and disseminate such reports, as the Commission prescribes by rule as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the Exchange Act. 15 U.S.C. 78q(a)(1).

[100] *See* 17 CFR 240.17g–2(c)–(f).

[101] *See* Public Law 111–203 § 932(a)(8) and 15 U.S.C. 78o–7(p)(1)–(4).

violates the requirements of Section 15E of the Exchange Act and the rules under the Exchange Act.[102]

The Exchange Act already provides a wide range of fines, penalties, and other sanctions applicable to NRSROs for violations of any section of the Exchange Act (including Section 15E) and the rules under the Exchange Act (including the rules under Section 15E).[103] For example, Section 15E(d)(1) of the Exchange Act provides that the Commission shall censure an NRSRO, place limitations on the activities, functions, or operations of an NRSRO, suspend an NRSRO for a period not exceeding 12 months, or revoke the registration of an NRSRO if, among other reasons, the NRSRO violates Section 15E of the Exchange Act or the Commission's rules thereunder.[104] In addition, Section 932(a)(3) of the Dodd-Frank Act amended Section 15E(d) to explicitly provide additional potential sanctions.[105] First, it provided the Commission with the authority to seek sanctions against persons associated with, or seeking to become associated with, an NRSRO.[106] Under these amendments, the Commission can censure such persons, place limitations on the activities or functions of such persons, suspend such persons for a period not exceeding 1 year, or bar such persons from being associated with an NRSRO.[107] Second, Section 932(a)(3) of Dodd-Frank Act amended Section 15E(d) to provide the Commission with explicit authority to temporarily suspend or permanently revoke the registration of an NRSRO in a particular class or subclass of credit ratings if the NRSRO does not have adequate financial and managerial resources to consistently produce credit ratings with integrity.[108]

Furthermore, Sections 21, 21A, 21B, 21C, and 32 of the Exchange Act provide additional means to sanction an NRSRO for violations of the provisions of the Exchange Act such as the self-executing provisions in Section 15E of the Exchange Act and the rules under the Exchange Act.[109]

The Commission preliminarily believes these provisions of the Exchange Act, as amended by the Dodd-Frank Act, provide a sufficiently broad range of means to impose fines, penalties, and other sanctions on an NRSRO for violations of Section 15E of the Exchange Act and the rules thereunder. For example, the fines, penalties, and sanctions applicable to NRSROs are similar in scope to the fines, penalties, and sanctions applicable to other registrants under the Exchange Act, such as broker-dealers. Moreover, since enactment of the Rating Agency Act of 2006, the Commission has not identified a specific need for a fine or penalty applicable to NRSROs not otherwise provided for in the Exchange Act. Consequently, the Commission preliminarily believes it would be appropriate at this time to defer establishing new fines or penalties in addition to those provided for in the Exchange Act. However, in the future, the Commission may use the authority in Section 15E(p)(4)(A) of the Exchange Act if a specific need is identified. For the foregoing reasons, to implement Section 15E(p)(4)(A) of the Exchange Act at this time, the Commission proposes to amend the instructions to Form NRSRO by adding new Instruction A.10.[110] This new instruction would provide notice to credit rating agencies applying for registration and NRSROs that an NRSRO is subject to applicable fines, penalties, and other available sanctions set forth in Sections 15E, 21, 21A, 21B, 21C, and 32 of the Exchange Act (15 U.S.C. 78o–7, 78u, 78u–1, 78u–2, 78u–3, and 78ff, respectively) for violations of the securities laws.

Request for Comment

The Commission generally requests comment on all aspects of proposed new Instruction A.10 to Form NRSRO. The Commission also seeks comment on the following:

1. Are the fines, penalties and other sanctions applicable to NRSROs in Sections 15E, 21, 21A, 21B, 21C, and 32 of the Exchange Act sufficient? If not, what additional fines and penalties should the Commission establish by rule?

E. Public Disclosure of Information About the Performance of Credit Ratings

Section 932(a)(8) of the Dodd-Frank Act amended Section 15E of the Exchange Act to add new subsection (q), which contains paragraphs (1) and (2).[111] Section 15E(q)(1) provides that the Commission shall, by rule, require each NRSRO to publicly disclose information on the initial credit ratings determined by the NRSRO for each type of obligor, security, and money market instrument, and any subsequent changes to such credit ratings, for the purpose of allowing users of credit ratings to evaluate the accuracy of ratings and compare the performance of ratings by different NRSROs.[112] Section 15E(q)(2) provides that the Commission's rules shall require, at a minimum, disclosures that:

- Are comparable among NRSROs, to allow users of credit ratings to compare the performance of credit ratings across NRSROs;[113]
- Are clear and informative for investors having a wide range of sophistication who use or might use credit ratings;[114]
- Include performance information over a range of years and for a variety of types of credit ratings, including for credit ratings withdrawn by the NRSRO;[115]
- Are published and made freely available by the NRSRO, on an easily accessible portion of its Web site, and in writing, when requested;[116]
- Are appropriate to the business model of an NRSRO;[117] and
- Require an NRSRO to include an attestation with any credit rating it issues affirming that no part of the rating was influenced by any other business activities, that the rating was based solely on the merits of the instruments being rated, and that such rating was an independent evaluation of the risks and merits of the instrument.[118]

[102] *See* 15 U.S.C. 78o–7(p)(4)(A).

[103] *See* 15 U.S.C. 78o–7(d), 15 U.S.C. 78u, 15 U.S.C. 78u–1, 15 U.S.C. 78u–2, 15 U.S.C. 78u–3 and 15 U.S.C. 78ff.

[104] *See* Section 15E(d)(1)(A)–(F) of the Exchange Act (15 U.S.C. 78o–7(d)(1)(A)–(F)), as amended by the Dodd-Frank Act.

[105] *See* Public Law 111–203 § 932(a)(3) and 15 U.S.C. 78o–7(d).

[106] 15 U.S.C. 78o–7(d)(1).

[107] *Id.*

[108] *See* Public Law 111–203 § 932(a)(3) and 15 U.S.C. 78o–7(d)(2). Prior to this amendment, the Commission already had authority to suspend or revoke the registration of an NRSRO if it failed to maintain adequate financial and managerial resources to consistently produce credit ratings with integrity. *See* Section 15E(d)(5) of the Exchange Act (15 U.S.C. 78o–7(d)(5)) before being amended by the Dodd-Frank Act, which re-designated paragraph (d)(5) of Section 15E as paragraph (d)(1)(E) (15 U.S.C. 78o–7(d)(1)(E)). Section 15E(d)(2) of the Exchange Act, however, provides explicit authority to target a suspension or registration revocation to a specific class or subclass of security. *See* 15 U.S.C. 78o–7(d)(2).

[109] *See* 15 U.S.C. 78o–7, 15 U.S.C. 78u, 15 U.S.C. 78u–1, 15 U.S.C. 78u–2, 15 U.S.C. 78u–3 and 15 U.S.C. 78ff, respectively. In fact, the Dodd-Frank Act amended Section 21B of the Exchange Act (15 U.S.C. 78u–2) to provide the Commission with the authority to assess money penalties in cease and desist proceedings under Section 21C (15 U.S.C. 78u–3). *See* Section 929P(a)(2) of the Dodd-Frank Act.

[110] *See* proposed new Instruction A.10 to Form NRSRO.

[111] *See* Public Law 111–203 § 932(a)(8) and 15 U.S.C. 78o–7(q)(1) and (2).

[112] *See* 15 U.S.C. 78o–7(q)(1).

[113] *See* 15 U.S.C. 78o–7(q)(2)(A).

[114] *See* 15 U.S.C. 78o–7(q)(2)(B).

[115] *See* 15 U.S.C. 78o–7(q)(2)(C).

[116] *See* 15 U.S.C. 78o–7(q)(2)(D).

[117] *See* 15 U.S.C. 78o–7(q)(2)(E).

[118] *See* 15 U.S.C. 78o–7(q)(2)(F). As discussed below in Section II.G.4 of this release, the

Continued

Currently, the Commission's rules require NRSROs to publish two types of information about the performance of their credit ratings: (1) Performance statistics[119] and (2) ratings histories.[120] As discussed in detail below, the Commission proposes to implement the rulemaking mandated in Section 15E(q) of the Exchange Act, in substantial part, by significantly enhancing the requirements for generating and disclosing this information by amending the instructions to Form NRSRO as they relate to Exhibit 1 and amending Rule 17g–1, Rule 17g–2, and Rule 17g–7.[121]

1. Proposed Enhancements to Disclosures of Performance Statistics

The Commission proposes to implement the rulemaking mandated in Section 15E(q) of the Exchange Act, in part, by amending Instruction H to Form NRSRO (the "instructions for Exhibit 1") and Rule 17g–1.[122]

a. Proposed Amendments to Instructions for Exhibit 1

Exhibit 1 is part of the registration application a credit rating agency seeking to be registered as an NRSRO (an "applicant") must submit to the Commission and an NRSRO must file with the Commission, keep up-to-date, and publicly disclose.[123] Section 15E(a)(1)(B)(i) of the Exchange Act requires that the registration application include performance measurement statistics over short-term, mid-term, and long-term periods (as applicable).[124] The Commission implemented this requirement, in large part, through Exhibit 1 to Form NRSRO and the instructions for Exhibit 1.[125] Section 15E(b)(1)(A) of the Exchange Act provides that the performance measurement statistics must be updated annually in an annual submission of the registration application required by Section 15E(b)(2) (the "annual certification").[126]

The instructions for Exhibit 1 require an applicant and NRSRO to provide performance measurement statistics of the credit ratings of the applicant or NRSRO, including performance measurement statistics of the credit ratings separately for each class of credit rating for which the applicant is seeking registration or the NRSRO is registered.[127] The classes of credit ratings for which an NRSRO can be registered are enumerated in the definition of "nationally recognized statistical rating organization" in Section 3(a)(62) of the Exchange Act: (1) Financial institutions, brokers, or dealers;[128] (2) insurance companies;[129] (3) corporate issuers;[130] (4) issuers of asset-backed securities (as that term is defined in Section 1101(c) of part 229 of Title 17, Code of Federal Regulations, "as in effect on the date of enactment of this paragraph");[131] and (5) issuers of government securities, municipal securities, or securities issued by a foreign government.[132] With respect to the fifth class of credit ratings, the instructions for Exhibit 1 require the NRSRO to provide performance measurement statistics for the following three subclasses (as opposed to the class

Commission preliminarily believes that the attestation requirement specified in Section 15E(q)(2)(F) should be incorporated into the rule the Commission is proposing to implement Section 15E(s) of the Exchange Act, which specifies, among other things, that the Commission adopt rules requiring an NRSRO to generate a form to be included with the publication of a credit rating. *See* 15 U.S.C. 78o–7(s) and proposed new paragraph (a)(1)(iii) of Rule 17g–7.

[119] *See* Exhibit 1 to Form NRSRO and Instruction H to Form NRSRO (as it relates to Exhibit 1). This type of disclosure shows the performance of an NRSRO's credit ratings in the aggregate through statistics. Specifically, it provides the percent of rated obligors, securities, and money market instruments in each category of credit rating in a rating scale (*e.g.,* AAA, AA, A, BBB, BB, B, CCC, CC, and C) that over a given time period were downgraded or upgraded to another credit rating category ("transition rates") and went into default ("default rates"). The goal is to provide a mechanism for users of credit ratings to compare the statistical performance of credit ratings across NRSROs.

[120] *See* 17 CFR 240.17g–2(d). This type of disclosure shows the credit rating history of a given rated obligor, security, or money market instrument. Specifically, it shows the initial credit rating and all subsequent modifications to the credit rating (such as upgrades, downgrades, and placements on watch) and the dates of such actions. The goal is to allow users of credit ratings to compare how different NRSROs rated an individual obligor, security, or money market instrument and how and when those ratings were changed over time. The disclosure of ratings histories also is designed to provide "raw data" that can be used by third parties to generate independent performance statistics such as transition and default rates.

[121] *See* proposed amendments to Instruction H to Form NRSRO (as it relates to Exhibit 1), paragraph (i) of Rule 17g–1, paragraph (d) of Rule 17g–2, and proposed new paragraph (b) of Rule 17g–7.

[122] *See* proposed amendments to the instructions for Exhibit 1 and paragraph (i) of Rule 17g–1.

[123] In particular, Section 15E(a)(1)(A) of the Exchange Act requires an applicant to furnish an application for registration to the Commission, in such form as the Commission shall require, by rule or regulation. *See* 15 U.S.C. 78o–7(a)(1)(A). Section 15E(a)(1)(B) of the Exchange Act identifies information that must be included in the application for registration. *See* 15 U.S.C. 78o–7(a)(1)(B)(i)–(x). The Commission implemented Sections 15E(a)(1)(A) and (B) of the Exchange Act by adopting Form NRSRO. *See* Form NRSRO; *see also Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33569–33582 (June 18, 2007). Section 15E(a)(3) of the Exchange Act provides that the Commission, by rule, shall require an NRSRO, upon being granted registration, to make the information and documents in its completed application for registration, or in any amendment to its application, publicly available on its Web site, or through another comparable, readily accessible means, except for certain information that is submitted on a confidential basis. *See* 15 U.S.C. 78o–7(a)(3). The Commission implemented this provision by adopting paragraph (i) of Rule 17g–1. *See* 17 CFR 240.17g–1(i); *see also Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33569 (June 18, 2007). Section 15E(b)(1) requires an NRSRO to promptly amend its application for registration if any information or document provided therein becomes materially inaccurate; however, (as discussed below) certain information does not have to be updated and other information must be updated only on an annual basis. *See* 15 U.S.C. 78o–7(b)(1); *see also* 15 U.S.C. 78o–7(b)(1) and 15 U.S.C. 78o–7(a)(1)(B)(ix). The Commission implemented this provision by adopting Form NRSRO and paragraph (e) of Rule 17g–1. *See* Form NRSRO and 17 CFR 240.17g–1(e); *see also Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33567, 33569–33582 (June 18, 2007).

[124] *See* 15 U.S.C. 78o–7(a)(1)(B)(i).

[125] *See* instructions for Exhibit 1.

[126] *See* 15 U.S.C. 78o–7(b)(1) and (2). In particular, Section 15E(b)(2) of the Exchange Act provides that not later than 90 days after the end of each calendar year, an NRSRO shall file with the Commission an amendment to its registration application, in such form as the Commission, by rule, may prescribe: (1) Certifying that the information and documents in the application for registration continue to be accurate; and (2) listing any material change that occurred to such information and documents during the previous calendar year. *See* 15 U.S.C. 78o–7(b)(2). The Commission implemented these provisions by adopting Form NRSRO and paragraph (f) of Rule 17g–1. *See* Form NRSRO and 17 CFR 240.17g–1(f); *see also Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33567, 33569–33582 (June 18, 2007).

[127] *See* instructions for Exhibit 1.

[128] *See* 15 U.S.C. 78c(a)(62)(A)(i).

[129] *See* 15 U.S.C. 78c(a)(62)(A)(ii).

[130] *See* 15 U.S.C. 78c(a)(62)(A)(iii).

[131] *See* 15 U.S.C. 78c(a)(62)(A)(iv). The instructions for Exhibit 1 broaden this class of credit rating to include a credit rating of any security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction. The intent of the instruction is to include in the class (and, therefore, in the performance statistics for the class) credit ratings for structured finance products that are outside the scope of the definition referenced in Section 3(a)(62)(A)(iv) of the Exchange Act. *See* 15 U.S.C. 78c(a)(62)(A)(iv) and *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6458 (Feb. 9, 2009). As discussed below, the Commission is proposing to continue to use a broadened definition in the proposed new instructions for Exhibit 1. Moreover, the term "structured finance product" as used throughout this release refers broadly to any security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction. *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63832, footnote 3 (Dec. 4, 2009). This broad category of financial instrument includes an "asset-backed security" as defined in Section 3(a)(77) of the Exchange Act (15 U.S.C. 78c(a)(77)) and other types of structured debt instruments such as collateralized debt obligations CDOs, including synthetic and hybrid CDOs. *Id.* The term "Exchange Act-ABS" as used throughout this release refers more narrowly to an "asset-backed security" as defined in Section 3(a)(77) of the Exchange Act. 15 U.S.C. 78c(a)(77).

[132] *See* 15 U.S.C. 78c(a)(62)(A)(v).

as a whole): sovereigns, United States public finance, and international public finance.[133]

In addition, the instructions require that the performance measurement statistics "must at a minimum show the performance of credit ratings in each class over 1-year, 3-year, and 10-year periods (as applicable) through the most recent calendar year-end, including, as applicable: historical ratings transition and default rates within each of the credit rating categories,[134] notches, grades, or rankings used by the Applicant/NRSRO as an indicator of the assessment of the creditworthiness of an obligor, security, or money market instrument in each class of credit rating."[135] Paragraph (i) of Rule 17g–1 provides, among other things, that the NRSRO must make the annual certification publicly available within 10 business days of furnishing the annual certification to the Commission.[136]

Currently, the instructions for Exhibit 1 do not prescribe the methodology an NRSRO must use to calculate and present the performance measurement statistics; nor do the instructions limit the type of information that can be disclosed in the Exhibit.[137] Consequently, NRSROs have used different techniques to produce performance measurement statistics, which has limited the ability of investors and other users of credit ratings to compare the performance of credit ratings across NRSROs.[138] In addition, several NRSROs have included substantial amounts of information in Exhibit 1 about performance measurement statistics, in addition to transition and default rates. These practices make the presentation of information in the Exhibits widely inconsistent across NRSROs.

For the foregoing reasons and to implement Section 15E(q) of the Exchange Act, the Commission is proposing significant enhancements to the requirements to disclose performance measurement statistics in Exhibit 1.[139] The enhancements would confine the disclosures in the Exhibit to transition and default rates and certain limited supplemental information. Moreover, the enhancements would standardize the production and presentation of the transition and default rates.[140] Specifically, the Commission preliminarily believes that the transition and default rates in Exhibit 1 should be produced using a "single cohort approach."[141] As explained below, under this approach, an applicant and NRSRO, on an annual basis, would be required to compute how the credit ratings assigned to obligors, securities, and money market instruments in a particular class or subclass of credit rating that were outstanding on the date 1, 3, and 10 years prior to the most recent calendar year-end performed during the respective 1-, 3-, and 10-year time period. The Commission's intent in proposing these enhancements is to make the Exhibit 1 disclosures simply presented, easy to understand, uniform in appearance, and comparable across NRSROs.[142]

To implement this proposal, the Commission is proposing to substantially revise the instructions for Exhibit 1.[143] The proposed new instructions would be divided into paragraphs (1), (2), (3), and (4), some of which would have subparagraphs.[144] The proposed new paragraphs would contain specific instructions with respect to, among other things, how required information must be presented in the Exhibit (including the order of presentation) and how transition and default rates must be produced using a single cohort approach. As with all information that must be submitted in Form NRSRO and its Exhibits, applicants *and* NRSROs would be subject to these requirements.[145]

Proposed Paragraph (1) of the Instructions for Exhibit 1. Proposed new paragraph (1) of the instructions for Exhibit 1 would require an applicant and NRSRO to provide performance measurement statistics for each class and subclass of credit ratings for which the applicant is seeking registration as an NRSRO or the NRSRO is registered.[146] Consistent with the current instructions, proposed new paragraph (1) would require an applicant and NRSRO to provide transition and default rates for 1-, 3-, and 10-year periods for each applicable class or subclass of credit rating.[147] Also consistent with the current instructions, proposed new paragraph (1) would require an applicant and NRSRO to produce and present three separate transition and default statistics for each applicable class or subclass of credit rating; namely, for 1-, 3-, and 10-year time periods through the most recently ended calendar year. In addition, as part of the enhancements, an applicant and NRSRO would need to present the transition and default rates for each time period together in tabular form using a standard format (a "Transition/Default Matrix").[148]

Proposed new paragraph (1) would identify the classes and subclasses of credit ratings for which an applicant and NRSRO would need to produce Transition/Default Matrices, as

[133] *See* instructions for Exhibit 1.

[134] The transition rate is the percentage of ratings at a given rating notch that transition to another specified rating notch over a given time period. Only ratings that were outstanding at the beginning of the time period are used in the calculation of the transition rate. Transition rates are generally used to measure the stability of the ratings. The default rate is the percentage of ratings at a given rating notch that have defaulted over a given time period. Only the ratings that were outstanding at the beginning of the time period are used in the calculation.

[135] *See* instructions for Exhibit 1.

[136] *See* 17 CFR.240.17g–1(i).

[137] When adopting Form NRSRO, the Commission explained that the instructions would not prescribe how NRSROs must calculate transition rates and default rates, noting that commenters had opposed a standard approach because NRSROs use different methodologies to determine credit ratings. *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33574 (June 18, 2007). The Commission stated that it intended to continue to consider the issue "to determine the feasibility, as well as the potential benefits and limitations, of devising measurements that would allow reliable comparisons of performance between NRSROs." *Id.* The Commission incrementally standardized the disclosure requirements in Exhibit 1 by amending the Form in 2009 to require an NRSRO to disclose transition and default rates for each class of credit rating for which it was registered and for 1-, 3-, and 10-year periods. *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations* 74 FR at 6457–6459 (Feb. 9, 2009).

[138] *See, e.g., Securities and Exchange Commission: Action Needed to Improve Rating Agency Registration Program and Performance Related Disclosures,* GAO Report 10–782 (Sept. 2010) ("GAO Report 10–782").

[139] *See* 15 U.S.C. 78o–7(q) and proposed amendments to instructions for Exhibit 1.

[140] *See* 15 U.S.C. 78o–7(q)(2)(B).

[141] *See* GAO Report 10–782, pp. 27–37 (comparing, among other things, a single cohort approach—the model for the Commission's proposal—with an average cohort approach). *See also* GAO Report 10–782, p. 25, note 38 (identifying more complex techniques for calculating credit rating performance measurement statistics).

[142] *See* Section 15E(q)(2)(A) of the Exchange Act, which provides that the disclosure of information about the performance of credit ratings should be comparable among NRSROs, to allow users of credit ratings to compare the performance of credit ratings across NRSROs. 15 U.S.C. 78o–7(q)(2)(A). *See also* Section 15E(q)(2)(B) of the Exchange Act, which provides that the disclosure of information about the performance of credit ratings should be clear and informative for investors having a wide range of sophistication who use or might use credit ratings. 15 U.S.C. 78o–7(q)(2)(B).

[143] *See* proposed amendments to instructions for Exhibit 1.

[144] *See* proposed new paragraphs (1), (2), (3), and (4) of the instructions for Exhibit 1.

[145] Form NRSRO must be used by a credit rating agency to apply for registration as an NRSRO and, once registered, an NRSRO must publicly disclose the information required in Form NRSRO and Exhibits 1 though 9. *See* 17 CFR 240.17g–1 and Instructions A.1, B, C, D, E, and F to Form NRSRO.

[146] *See* proposed new paragraph (1) of the instructions for Exhibit 1.

[147] *Compare* current instructions for Exhibit 1 with proposed new paragraph (1) of the instructions for Exhibit 1.

[148] *See* proposed new paragraph (1) of the instructions for Exhibit 1.

applicable. The identified classes would reference the classes of credit ratings for which an NRSRO can be registered as enumerated in the definition of NRSRO in Section 3(a)(62)(A) of the Exchange Act.[149] This would be consistent with the current instructions for Exhibit 1.[150] Moreover, also consistent with the current instructions, the class of credit ratings enumerated in Section 3(a)(62)(A)(iv) of the Exchange Act (issuers of certain asset-backed securities) would be expanded by the instructions in proposed new paragraph (1) to include a broader range of structured finance products than are within the scope of the definition of Section 3(a)(62)(A)(iv).[151]

However, to enhance the disclosure of transition and default rates in this class, the Commission is proposing to divide it into the following subclasses: RMBS;[152] commercial mortgage backed securities ("CMBS");[153] collateralized loan obligations ("CLOs");[154] CDOs;[155] issuances of asset-backed commercial paper conduits ("ABCP");[156] other asset-backed securities;[157] and other structured finance products.[158] The Commission preliminarily believes dividing the broad class of structured finance products into these subclasses would provide investors and other users of credit ratings with more useful information about the performance of an NRSRO's structured finance ratings.[159] For example, during the recent crisis, NRSROs assigned credit ratings to RMBS and CDOs that performed far differently than credit ratings of some other types of securitizations.[160] Consequently, if an applicant or NRSRO computed transition and default rates for structured finance products as a single class, the underperformance of certain subclasses could be muted by the better performance of other subclasses.

Consistent with the current instructions, proposed new paragraph (1) would divide the class of credit ratings enumerated in Section 3(a)(62)(A)(v) of the Exchange Act (issuers of government securities, municipal securities or securities issued by a foreign government) into three subclasses.[161] The subclasses would continue to be: sovereign issuers; United States public finance; and international public finance.[162]

In addition, consistent with the current instructions for an annual certification, proposed new paragraph (1) would provide that the performance measurement statistics must be updated yearly in the NRSRO's annual certification in accordance with Section 15E(b)(1)(A) and paragraph (f) of Rule 17g–1 (*i.e.,* a Form NRSRO with updated performance measurement statistics must be filed with the Commission no later than 90 days after the end of the calendar year).[163] Proposed new paragraph (1) also would remind an NRSRO that, pursuant to paragraph (i) of Rule 17g–1, the annual certification with the updated performance measurement statistics must be made publicly and freely available on an easily accessible portion of the NRSRO's corporate Internet Web site within 10 business days after the filing and that the NRSRO must make its up-to-date Exhibit 1 freely available in writing to any individual who requests a copy of the Exhibit.[164]

Proposed Paragraph (2) of the Instructions for Exhibit 1. Proposed new paragraph (2) of the instructions for Exhibit 1 would prescribe how an applicant and NRSRO must present the performance measurement statistics and other required information in the Exhibit.[165] Specifically, it would require that the Transition/Default Matrices for each applicable class and subclass of credit ratings be presented in the order that the classes and subclasses are identified in proposed paragraphs (1)(A) through (E) of Exhibit 1. In addition, the order of the Transition/Default Matrices for a given class or subclass would need to be: The 1-year matrix, the 3-year matrix, and then the 10-year matrix.

[149] *Compare* 15 U.S.C. 78c(a)(62)(A)(i)–(v) with proposed new paragraphs (1)(A)–(E) of the instructions for Exhibit 1.

[150] *Compare* current instructions for Exhibit 1 with proposed new paragraph (1).

[151] *See* 15 U.S.C. 78c(a)(62)(A)(iv); *compare* current Instructions for Exhibit 1 with proposed new paragraph (1)(D).

[152] The Commission preliminarily intends that an "RMBS" for the purposes of this disclosure requirement would mean a securitization of primarily residential mortgages. *See* proposed new paragraph (1)(D)(i) of the instructions for Exhibit 1.

[153] The Commission preliminarily intends that a "CMBS" for the purposes of this disclosure requirement would mean a securitization of primarily commercial mortgages. *See* proposed new paragraph (1)(D)(ii) of the instructions for Exhibit 1.

[154] The Commission preliminarily intends that a "CLO" for the purposes of this disclosure requirement would mean a securitization of primarily commercial loans. *See* proposed new paragraph (1)(D)(iii) of the Instructions for Exhibit 1.

[155] The Commission preliminary intends that a "CDO" for the purposes of this disclosure requirement would mean a securitization primarily of other debt instruments such as RMBS, CMBS, CLOs, CDOs, other asset-backed securities, and corporate bonds. *See* proposed new paragraph (1)(D)(iv) of the instructions for Exhibit 1.

[156] The Commission preliminarily intends that "ABCP" for the purposes of this disclosure requirement would mean short term notes issued by a structure that securitizes a variety of financial assets (*e.g.,* trade receivables, credit card receivables), which secure the notes. *See* proposed new paragraph (1)(D)(v) of the instructions for Exhibit 1.

[157] The Commission preliminarily intends that the term "other asset-backed security" for the purposes of this disclosure requirement would mean a securitization primarily of auto loans, auto leases, floor plan financings, credit card receivables, student loans, consumer loans, equipment loans, or equipment leases. *See* proposed new paragraph (1)(D)(vi) of the instructions for Exhibit 1.

[158] The Commission preliminarily intends that "other structured finance product" for the purposes of this disclosure requirement would mean a structured finance product that does not fit into any of the other subclasses of structured products. *See* proposed new paragraph (1)(D)(vii) of the instructions for Exhibit 1.

[159] *See, e.g.,* GAO Report 10–782, p. 36 (noting that NRSROs active in rating structured finance generally present performance statistics for this class by sectors (*e.g.,* RMBS, CMBS and ABS) in their voluntary disclosures). *See also,* GAO Report 10–782, p. 36 (observing that the various structured finance sectors have risk characteristics that vary significantly and, therefore, that presenting performance statistics for the class as a whole "may not be useful.").

[160] *See, e.g., A Global Cross-Asset Report Card of Ratings Performance in Times of Stress,* Standard & Poor's (June 8, 2010).

[161] *See* 15 U.S.C. 78c(a)(62)(A)(v); *compare* current instructions for Exhibit 1, *with* proposed new paragraph (1)(E).

[162] *See* proposed new paragraph (1)(E) of the instructions for Exhibit 1.

[163] *See* Instruction F to Form NRSRO and proposed new paragraph (1); *see also* 15 U.S.C. 78o–7(b)(1)(A) and 17 CFR 240.17g–1(f). While paragraph (f) of Rule 17g–1 currently requires the annual certification to be "furnished," the Commission is proposing, as discussed below in Section II.M.1 of the release, to replace the term "furnished" with the term "filed" in a number of the NRSRO rules, including Rule 17g–1.

[164] *See* proposed new paragraph (1) of the instructions for Exhibit 1. As discussed below in Section II.E.1.b of this release, the Commission is proposing to amend paragraph (i) of Rule 17g–1 (17 CFR 240.17g–1(i)) to implement Section 15E(q)(2)(D) of the Exchange Act, which provides that the Commission's rules must require that the information about the performance of credit ratings be published and made freely available on an easily accessible portion of an NRSRO's Web site, and in writing when requested. *See* 15 U.S.C. 78o–7(q)(2)(D). As discussed below, the proposed amendment to paragraph (i) of Rule 17g–1 (17 CFR 240.17g–1(i)) would require an NRSRO to publish and make freely available on an easily accessible portion of its Web site all of Form NRSRO (*i.e.,* not just Exhibit 1). However, only Exhibit 1 would need to be made freely available in writing when requested.

[165] *See* proposed new paragraph (2) of the instructions for Exhibit 1.

Proposed new paragraph (2) also would provide that if the applicant or NRSRO did not issue credit ratings in a particular class or subclass for the length of time necessary to produce a Transition/Default Matrix for a 1-, 3-, or 10-year period, it would need to explain that fact in the location where the Transition/Default Matrix would have been presented in the Exhibit.[166]

Similar to the current Instructions, proposed paragraph (2) would require an applicant and NRSRO to clearly define in Exhibit 1, after the presentation of all applicable Transition/Default Matrices, each symbol, number, or score in the rating scale used by the applicant or NRSRO to denote a credit rating category and notches within a category for each class and subclass of credit ratings in any Transition/Default Matrix presented in the Exhibit.[167] The instructions also would require the applicant or NRSRO to clearly explain the conditions under which it classifies obligors, securities, or money market instruments as being in default. As discussed below, the Commission preliminarily believes that obligors, securities, and money market instruments that the applicant or NRSRO has classified as being in default as of the period start date for a Transition/Default Matrix should be excluded from the statistics in the matrix. Also, as discussed below, the Commission is proposing a standard definition of "default" for the purpose of calculating default rates. In addition, also as discussed below, where an applicant or NRSRO has a definition of "default" that is broader than this standard definition, the instructions would require the applicant or NRSRO to supplement the standard definition with its internal definition. For these reasons, the Commission believes it would be useful for investors and other users of credit ratings to know how an NRSRO defines default.

Similar to the current instructions, proposed paragraph (2) would require that an applicant and NRSRO provide in Exhibit 1 the uniform resource locator (URL) of its corporate Internet Web site where the credit rating histories required to be disclosed pursuant to paragraph (b) of Rule 17g–7 would be located (in the case of an applicant) or are located (in the case of an NRSRO).[168]

Finally, proposed paragraph (2) would provide that Exhibit 1 must contain no performance measurement statistics or information other than as described in, and required by, the instructions for Exhibit 1; except the applicant or NRSRO would be permitted to provide, after the presentation of all required Transition/Default Matrices and other required disclosures, Internet Web site URLs where other information relating to performance measurement statistics of the applicant or NRSRO is located.[169] As noted above, some NRSROs include substantial amounts of information in Exhibit 1 about the performance of their credit ratings. The Commission preliminarily believes information in addition to the disclosures that would be required under the enhancements to Exhibit 1 may be useful to investors and other users of credit ratings. However, the Commission also preliminarily believes disclosing this related information in Exhibit 1 would make the Exhibit less easy to use in terms of locating a particular Transition/Default Matrix and comparing it with the matrices of other NRSROs. Consequently, the Commission preliminarily believes an appropriate balance would be to exclude related information from the Exhibit but permit an NRSRO to cross-reference such information by providing Internet Web site URLs at the end of the Exhibit.

Proposed Paragraph (3) of the Instructions for Exhibit 1. Proposed paragraph (3) of the Instructions for Exhibit 1 would prescribe how an applicant and NRSRO must design a Transition/Default Matrix.[170] The instructions would require an applicant and NRSRO to produce a 1-, 3-, and 10-year Transition/Default Matrix for each applicable class and subclass of credit rating that resembles, in design, the Transition/Default Matrix in Figure 1 below.[171]

FIGURE 1—CORPORATE ISSUERS—10-YEAR TRANSITION AND DEFAULT RATES

[December 31, 2000 through December 31, 2010]

Credit rating scale	Number of ratings outstanding as of 12/31/2000	AAA	AA	A	BBB	BB	B	CCC	CC	C	Default	Paid off	Withdrawn (other)
AAA	10	50%	10%	.....	.....	.....	.....	.....	.....	.....	.....	40%	.....
AA	2000	1%	39%	12%	10%	8%	5%	4%	.....	.....	1%	19%	1%
A	4000	.....	6%	34%	15%	10%	6%	4%	3%	.....	2%	18%	2%
BBB	3600	.....	2%	9%	28%	15%	10%	6%	5%	1%	4%	17%	3%
BB	1000	.....	.....	2%	4%	20%	14%	5%	.....	.....	2%	16%	37%
B	500	.....	.....	1%	3%	6%	20%	20%	15%	.....	15%	15%	5%
CCC	300	.....	.....	.....	.....	4%	6%	15%	25%	20%	20%	4%	6%

[166] For example, if an NRSRO is registered in the corporate issuer class but has been issuing credit ratings for only 7 years in that class, it could not produce a 10-year Transition/Default Matrix for the class. Instead, the NRSRO would need to provide an explanation in the location where a 10-year Transition/Default Matrix would have been located (*i.e.,* after the 3-year matrix) that it had not been issuing credit ratings in that class for a sufficient amount of time to produce a 10-year Transition/Default Matrix.

[167] *Compare* current instructions for Exhibit 1, *with* proposed new paragraph (2). As discussed in Section II.J.2 of this release, the Commission is proposing to implement Section 938(a)(2) of the Dodd-Frank Act through paragraph (b)(2) of new Rule 17g–8, which would require an NRSRO to have policies and procedures reasonably designed to clearly define the meaning of any symbol used by the NRSRO to denote a credit rating, including in Exhibit 1 to Form NRSRO. *See* Public Law 111–203 § 938(a)(2) and proposed paragraph (b)(2) of new Rule 17g–8.

[168] *Compare* current instructions for Exhibit 1, *with* proposed new paragraph (2). As discussed below in Section II.E.2 of this release, the Commission is proposing to amend Rule 17g–2 (17 CFR 240.17g–2) and Rule 17g–7 (17 CFR 240.17g–7) to enhance the credit rating history disclosure requirements currently located in Rule 17g–2. Among other things, the Commission proposes relocating the credit rating history disclosure requirements from Rule 17g–2 to proposed new paragraph (b) of Rule 17g–7. *See* proposed amendments to paragraph (d) of Rule 17g–2 and proposed new paragraph (b) of Rule 17g–7.

[169] *See* proposed new paragraph (2) of the instructions for Exhibit 1.

[170] *See* proposed new paragraph (3) of the instructions for Exhibit 1.

[171] However, as explained below, the top row and first column would be based on the rating scale used by the applicant or NRSRO for the applicable class or subclass of credit ratings. For example, in the Sample Transition/Default Matrix, there are nine categories denoted by the symbols: AAA, AA, A, BBB, BB, B, CCC, CC, and C but no notches within those categories. An NRSRO that uses notches in its ratings scale (*e.g.,* AA+, AA, and AA-) would need to include the symbol for each notch in the individual cells of the first column and top row. However, as discussed below, the applicant or NRSRO would exclude a "default" category even if it uses such a category in its rating scale (though, as explained below, there would be a column with the heading "Default" in the matrix that would depict the percent of rated obligors, securities, and money market instruments that went into default during the relevant time period based on a standard definition of "default" in the instructions for Exhibit 1 (*i.e.,* not on the definition of the applicant or NRSRO).

FIGURE 1—CORPORATE ISSUERS—10-YEAR TRANSITION AND DEFAULT RATES—Continued

[December 31, 2000 through December 31, 2010]

Credit rating scale	Number of ratings outstanding as of 12/31/2000	AAA	AA	A	BBB	BB	B	CCC	CC	C	Default	Paid off	Withdrawn (other)
CC	200						2%	8%	10%	38%	30%	2%	10%
C	160							2%	8%	10%	67%	1%	12%
Total	11,770												

A sample Transition/Default Matrix similar to Figure 1 would be depicted in proposed new paragraph (3) to provide a visual representation of how to design and present a matrix.[172] In addition to the visual depiction, proposed new paragraph (3) would contain narrative instructions on how to design a matrix. First, the narrative instructions would prescribe the headings for each required column in a Transition/Default Matrix by referring to the cells in the top row of the table (the "header row").[173] The narrative instructions would require that the first and second cells in the header row contain the headings, respectively, "Credit Rating Scale" and "Number of Ratings Outstanding as of [insert the applicable date]."[174] The applicable date would be the date 1, 3, or 10 years prior to the most recent calendar year-end depending on whether the Transition/Default Matrix was being produced for a 1-, 3-, or 10-year period. The next sequence of cells in the header row would need to contain, in order from left to right, each credit rating symbol, number, or score used to denote a category and a notch within a category in the rating scale used by the applicant or NRSRO for the applicable class or subclass of credit ratings in descending order from the highest to the lowest notch.[175] The narrative instructions would require that the applicant or NRSRO not include a "default" category in the header row even if such a category is used in the rating scale.[176] The narrative instructions would require that the cells in the last three columns in the Transition/Default Matrix contain the headings, in order from left to right, "Default", "Paid Off", and "Withdrawn (other)."[177]

Next, the narrative instructions would require that the first column have a separate cell containing each credit rating symbol, number, or score in the rating scale used by the applicant or NRSRO to denote a category and a notch within a category for the applicable class or subclass of credit ratings in descending order from the highest to the lowest notch.[178] The applicant or NRSRO would be required to populate the column with the credit rating symbols, numbers, or scores in descending order from the highest to the lowest notch. Consistent with the header row, the narrative instructions also would require that the first column not include a "default" category if the applicant or NRSRO uses such a category in its rating scale. The last cell in the first column would need to contain the term "Total."[179]

Finally, the narrative instructions would require that the Transition/Default Matrix have a title identifying the applicable class or subclass of credit ratings, the period covered (1, 3, or 10 years), and start date and end date for the period.

Proposed Paragraph (4) of the Instructions for Exhibit 1. Proposed new paragraph (4) of the instructions for Exhibit 1 would prescribe how an applicant or NRSRO would need to populate a Transition/Default Matrix with data and statistical information.[180] First, proposed new paragraph (4)(A) would prescribe how to populate the cells of the second column headed "Number of Ratings Outstanding [as the Start Date]."[181] First, the applicant or NRSRO would be required to determine a start-date cohort consisting of the obligors, securities, and money market instruments in the applicable class or subclass of credit ratings that were assigned a credit rating (other than an expected or preliminary credit rating)[182] that was outstanding as of the start date for the applicable period (*i.e.,* the date 1, 3, or 10 years prior to the most recently ended calendar year).[183] Consequently, the start-date cohort would exclude any obligor, security, or money market instrument that received an initial credit rating in the class or subclass after the start date.[184]

In addition, the proposed instructions would provide that the applicant or NRSRO must exclude from the start-date cohort any obligors, securities, or money

[172] *See* proposed new paragraph (3) of the instructions for Exhibit 1.

[173] *See* proposed new paragraph (3) of the instructions for Exhibit 1.

[174] *See, e.g.,* the 1st and 2nd columns of the Sample Transition/Default Matrix in Figure 1.

[175] *See* proposed new paragraph (3) of the instructions for Exhibit 1; *see also* the 3rd through 11th columns of the Sample Transition/Default Matrix in Figure 1.

[176] The Commission's reasoning for proposing to exclude a category of "default" from the first column is explained below.

[177] *See* proposed new paragraph (3) of the instructions for Exhibit 1; *see also* the 12th through 14th columns of the Sample Transition/Default Matrix in Figure 1.

[178] *See, e.g.,* the first column of the Sample Transition/Default Matrix in Figure 1.

[179] *See* proposed new paragraph (3) of the instructions for Exhibit 1; *see also* the first column of the Sample Transition/Default Matrix in Figure 1.

[180] *See* proposed paragraph (4) of the instructions for Exhibit 1.

[181] *See* proposed paragraph (4)(A) of the instructions for Exhibit 1; *see also* the 2nd column of the Sample Transition/Default Matrix in Figure 1.

[182] "Expected" or "preliminary" credit ratings most commonly are issued by an NRSRO with respect to a structured finance product at the time the issuer commences the offering and typically are included in pre-sale reports. Expected or preliminary credit ratings may include a range of ratings, or any other indications of a credit rating used prior to the assignment of an initial credit rating for a new issuance. As such, the Commission preliminarily believes they should be excluded from the Transition/Default Matrices since the issuance of the "initial" credit rating is the first formal expression of the NRSRO's view of the relative creditworthiness of the obligor, security, or money market instrument.

[183] For example, if the most recent year end was December 31, 2010, the NRSRO would need to determine all the obligors, securities, and money market instruments with credit ratings outstanding in the relevant class as of December 31, 2009 (for the 1-year Transition/Default Matrix), December 31, 2007 (for the 3-year Transition/Default Matrix), and December 31, 2000 (for the 10-year Transition/Default Matrix). Because some obligors, securities, and money market instruments have characteristics that could cause them to be assigned more than one class of credit rating, the Commission is seeking comment below in Section II.M.4.a of this release on which class would be the most appropriate for certain types of obligors, securities, and money market instruments. Based on the comments received in response to those questions, the Commission may decide to prescribe by rule or identify through guidance how certain types of obligors, securities, and money market instruments should be classified for the purpose of determining start-date cohorts.

[184] For example, a Transition/Default Matrix covering a 10-year period would not include obligors, securities, and money market instruments that had been rated by the NRSRO for less than 10 years. However, these obligors, securities, and money instruments may be included in the start-date cohorts for the 1- and 3-year matrices for the class or subclass.

market instruments that were classified by the applicant or NRSRO as being in default as of the period start date.[185] The Commission preliminarily believes that the Transition/Default Matrices should not include obligors, securities, and money market instruments the applicant or NRSRO has classified as in default.[186] The reason is that, if an applicant or NRSRO classifies an obligor, security, or money market instrument as in default, the applicant or NRSRO is no longer assessing the relative likelihood that the obligor, security, or money market will continue to meet its obligations to make timely payments of principal and interest as they come due (*i.e.,* not default on its obligations). Consequently, as long as the obligor, security, or money market instrument continues to be classified as in default there is no credit rating performance to measure. However, if an obligor, security, or money market instrument is upgraded from the default category because, for example, the obligor emerges from a bankruptcy proceeding, the obligor would need to be included in a Transition/Default Matrix that has a start date after the upgrade.[187]

The next step, after determining the start-date cohort, would be to determine the number of obligors, securities, and money market instruments in the start-date cohort that, as of the start date, were assigned a credit rating at each notch in the rating scale used for the class or subclass.[188] The final step would be to populate the appropriate column cells with these amounts and in the bottom cell provide the total number of obligors, securities, and money market instruments in the start-date cohort. As discussed next, determining these totals would be necessary to compute the percentages used to populate the rows of the Transition/Default Matrix. Moreover, the Commission preliminarily believes it would be useful to investors and other users of credit ratings to include these amounts in the matrix. This would inform them of the sample sizes of the obligors, securities, and money market instruments used to generate the transition and default rates for the notches entered in the matrix.[189]

Proposed new paragraph (4)(B) would focus on the horizontal axis of the Transition/Default Matrix by prescribing how an applicant and NRSRO would need to populate the rows representing sequentially in descending order the notches in the credit rating scale used for the applicable class or subclass of credit ratings.[190] The instructions would provide that each row must contain percents indicating the cumulative credit rating outcomes of the obligors, securities, and money market instruments assigned a credit rating at that notch.[191] The instructions also would provide that the percents in a row must add up to 100%.[192]

As discussed in detail below, proposed new paragraph (4)(B) would identify five potential credit rating outcomes: (1) The obligor, security, or money market instrument was assigned the same credit rating as of the period end date; (2) the obligor, security, or money market instrument was assigned a different credit rating as of the period end date; (3) the obligor, security, or money market instrument defaulted at any time during the period; (4) the obligor, security, or money market instrument paid off during the period; or (5) the applicant or NRSRO withdrew a credit rating of the obligor, security, or

[185] *See* proposed paragraph (4)(A) of the instructions for Exhibit 1. As indicated, the determination of whether an obligor, security, or money market instrument should be excluded from the start date cohort would be based on the definition of "default" used by the applicant or NRSRO. As discussed below, in determining the outcome of a credit rating assigned to an obligor, security, and money market instrument during the applicable time period covered by a Transition/Default Matrix, the applicant or NRSRO would need to use a standard definition of "default" in proposed new paragraph (4)(B)(iii) as opposed to its own definition. The Commission recognizes that the use of a standard definition of "default" to determine the outcome of a credit rating during the applicable time period could result in an obligor, security, or money market instrument being included in the start-date cohort that, as of the start date, would be classified as in "default" under the proposed definition of "default" in paragraph (4)(B)(iii). In other words, the applicant or NRSRO may not have classified the obligor, security, or money market instrument as in default as of the start date using its own narrower definition. In this case, the Commission preliminarily believes such an obligor, security, or money market instrument should be included in the start-date cohort since the applicant or NRSRO had assigned it a credit rating representing a relative assessment of the likelihood of default (rather than a classification of default) on the start date. Therefore, the performance of the applicant or NRSRO in rating that obligor, security, or money market instrument should be incorporated into the default rate.

[186] This does not mean that the obligor, security or money market instrument would never be reflected in default rates. For example, assume that as of the date 10 years prior to the most recently ended calendar year-end an obligor in the corporate issuer class was assigned a credit rating of BBB. This obligor would be included in the start-date cohort for the 10-year Transition/Default Matrix and grouped with the other obligors, securities, and/or money market instruments assigned BBB ratings. Further, assume that during the first seven years of the 10-year period, the credit rating of the obligor was downgraded from BBB to BB (in year 2), from BB to B (in year 5) and from B to CCC (in year 7). Having an outstanding credit rating of CCC in year 7, the obligor would be included in the start-date cohort for the 3-year Transition/Default Matrix and grouped with obligors, securities, and money market instruments assigned CCC ratings. Finally assume the obligor defaults in year 8. For the purposes of the 10- and 3-year Transition/Default Matrices, the obligor would need to be classified as having defaulted and included in the default rates calculated for those matrices. However, because the obligor would be in default as of the period start date for the 1-year Transition/Default Matrix, it would not be included in the start-date cohort for that matrix.

[187] *See* proposed paragraph (4)(A) of the instructions for Exhibit 1. For example, assume an obligor was classified as in default by the NRSRO as of the start date for the 10-year Transition/Default Matrix. The obligor would be excluded from the start-date cohort for the matrix. Assume further that two years later the obligor emerged from a bankruptcy proceeding after a re-structuring. At that point in time, the NRSRO upgraded the obligor from the default category by assigning it a credit rating of BBB. Assume that three years later the NRSRO upgraded the obligor's credit rating from BBB to A- and that it retained that rating for the next five years. In this case, the obligor would be included in the start-date cohorts for the 1- and 3-year Transition/Default Matrices and grouped with the obligors, securities, and money market instruments assigned A − credit ratings.

[188] *See* proposed paragraph (4)(A) of the instructions for Exhibit 1. For the class of credit ratings in the Sample Transition/Default Matrix in Figure 1, this would mean determining how many of the obligors, securities, and money market instruments in the start-date cohort were assigned a credit rating of AAA, AA, A, BBB, BB, B, CCC, CC, and C as of the start date. For example, the Sample Transition/Default Matrix in Figure 1 shows a total start-date cohort of 11,770 obligors, securities, and/or money market instruments. Within this cohort and as of the 12/31/2000 start date, 10 were rated AAA, 2000 were rated AA, 4000 were rated A, 3600 were rated BBB, 1000 were rated BB, 500 were rated B, 300 were rated CCC, 200 were rated CC, and 16 were rated C.

[189] For example, if the outcome for a notch with 10 obligors is that 5 defaulted, the default rate reflected on the Transition/Default Matrix for that notch would be 50%. Similarly, if the outcome of a notch with 5,000 obligors is that 2,500 defaulted, the default rate for that notch would be 50% as well. Investors and other users of credit ratings might conclude that 2,500 obligors going into default reflects significantly worse performance than 5 obligors. Consequently, if the sample sizes were not reflected on the matrix, investors and other users of credit ratings could draw conclusions about the comparative performance of NRSROs that are distorted by varying sample sizes.

[190] *See* proposed new paragraph (4)(B) of the instructions for Exhibit 1; *see also* the 2nd through the 10th rows of the Sample Transition/Default Matrix in Figure 1 (AAA through C).

[191] For example, in the Sample Transition/Default Matrix in Figure 1, cumulative outcomes would need to determined for: the 10 obligors, securities, and/or money market instruments in the 2nd row (AAA); the 2000 obligors, securities, and/or money market instruments in the 3rd row (AA); the 4000 obligors, securities, and/or money market instruments in the 4th row (A); the 3600 obligors, securities, and/or money market instruments in the 5th row (BBB); the 1000 obligors, securities, and/or money market instruments in the 6th row (BB); the 300 obligors, securities, and/or money market instruments in the 8th row (CCC); the 200 obligors, securities, and/or money market instruments in the 9th row (CC); and the 160 obligors, securities, and/or money market instruments in the 10th row (C).

[192] *See* proposed new paragraph (4)(B) of the instructions for Exhibit 1. For example, in the Sample Transition/Default Matrix in Figure 1, the percents in the row representing the AAA category are (from left to right): 50%, 10%, and 40%, which when added together equal 100%.

money market instrument at any time during the period for a reason other than that the obligor, security, or money market instrument defaulted or "paid off."[193] Because the percents in a row would need to add up to 100%, each obligor, security, and money market instrument reflected in the numbers contained in the 2nd column of a Transition/Default Matrix could be assigned only one credit rating outcome.[194] Proposed paragraphs (4)(B)(i) through (v) would instruct applicants and NRSROs how to compute the percents used to populate each row representing a notch in the rating scale in the Transition/Default Matrix.[195]

Proposed new paragraph (4)(B)(i) would require the applicant or NRSRO to determine the number of obligors, securities, and money market instruments assigned a credit rating at the notch represented by the row as of the period start date that were assigned a credit rating at the same notch as of the period end date.[196] The instructions would require that: (1) this number be expressed as a percent of the total number of obligors, securities, and/or money market instruments assigned a credit rating at that notch as of the period start date; and (2) the percent be entered in the column representing the same notch.[197]

An obligor, security, or money market instrument could have the same credit rating as of the period end-date because the credit rating did not change between the start date and the end date or the credit rating transitioned to one or more other notches during the relevant period but transitioned back to the start-date notch where it remained as of the period end date. Consequently, proposed new paragraph (4)(B)(i) would clarify that, to determine this amount, the applicant or NRSRO would need to use the credit rating at the notch assigned to the obligor, security, or money market instrument as of the period end date and not a credit rating at any other notch assigned to the obligor, security, or money market instrument between the period start date and the period end date.[198]

Proposed new paragraph (4)(B)(ii) would require the applicant or NRSRO to determine the number of obligors, securities, and money market instruments assigned a credit rating at the notch represented by the row as of the period start date that were assigned a credit rating at each other notch as of the period end date.[199] The instructions would require that: (1) these numbers be expressed as percents of the total number of obligors, securities, and/or money market instruments assigned a credit rating at that notch as of the period start date; and (2) the percents be entered in the columns representing each notch.[200] The instructions in the paragraph would clarify that, to determine these numbers, the applicant or NRSRO would need to use the credit rating at the notch assigned to the obligor, security, or money market instrument as of the period end-date and not a credit rating at any other notch assigned to the obligor, security, or money market instrument between the period start date and the period end date.[201]

Proposed new paragraph (4)(B)(iii) would require an applicant and NRSRO to determine the total number of obligors, securities, and money market instruments assigned a credit rating at the notch represented by the row as of the period start date that went into *Default* at any time during the applicable time period.[202] The instructions would require that: (1) This number be expressed as a percent of the total number of obligors, securities, and/or money market instruments assigned a credit rating at that notch as of the period start date; and (2) the percent to be entered in the *Default* column.[203]

As indicated, the classification of *Default* would be triggered if the obligor, security, or money market instrument went into *Default* at any time during the period.[204] This is different than the classifications in proposed paragraphs (4)(B)(i) and (ii), which are based solely on the end-date status of the obligor, security or money market instrument.[205] This period-long approach is designed to address concerns that an applicant or NRSRO might withdraw a credit rating of an obligor, security, or money market instrument that went into *Default* during the period in order to omit the obligor, security, or money market instrument from the Transition/Default

[193] *See* proposed new paragraphs (4)(B)(i)–(v) of the Instructions for Exhibit 1.

[194] *See* proposed new paragraph (4)(B) of the instructions for Exhibit 1; *see also* the 2nd column in the Sample Transition/Default Table in Figure 1.

[195] *See* proposed new paragraphs (4)(B)(i)–(v) of the instructions for Exhibit 1.

[196] *See* proposed new paragraph (4)(B)(i) of the instructions for Exhibit 1.

[197] For example, the 2nd row of the Sample Transition/Default Matrix in Figure 1 represents the AAA notch in the applicable rating scale. As reflected in the matrix, 10 obligors, securities, and/or money market instruments were assigned a credit rating of AAA as of the 12/31/2000 start date. Of these 10, 5 (or 50%) were assigned a credit rating of AAA as of the 12/31/2010 end date. Accordingly, 50% is input in the AAA column.

[198] *See* proposed new paragraph (4)(B)(i) of the instructions for Exhibit 1. For example, assume an obligor was assigned a credit rating of BBB as of the start date of a 10-year Transition/Default Matrix. Assume further that three years after the start date, the credit rating was upgraded to AA but then eight years after the start date the credit rating was downgraded to A, and nine years after the start date the credit rating was downgraded to BBB where it remained as of the period end date. For the purpose of the 10-year Transition/Default Matrix, the outcome assigned this obligor would be that it had the same credit rating as of the period end date. However, the transitions that occurred in years eight and nine would be reflected, respectively, in the 3- and 1-year Transitions/Default Matrices for the class or subclass of credit ratings. In other words, the credit rating history for this obligor would reflect volatility over the short term but stability over the long term.

[199] *See* proposed new paragraph (4)(B)(ii) of the instructions for Exhibit 1.

[200] *See* proposed new paragraph (4)(B)(ii) of the instructions for Exhibit 1. For example, the 3rd row of the Sample Transition/Default Matrix in Figure 1 represents the AA notch in the applicable rating scale. As reflected in the matrix, 2000 obligors, securities, and/or money market instruments were assigned a credit rating of AA as of the 12/31/2000 start date. Of these 2000, as of the period end date: 2 (or 1%) were assigned a credit rating of AAA; 240 (or 12%) were assigned a credit rating of A; 200 (or 10%) were assigned a credit rating of BBB; 160 (or 8%) were assigned a credit rating of BB; 100 (or 5%) were assigned a credit rating of B; and 80 (or 4%) were assigned a credit rating of CCC. Accordingly, 1% is input in the AAA column, 12% in the A column, 10% in the BBB column, 8% in the BB column, 5% in the B column, and 4% in the CCC column.

[201] *See* proposed new paragraph (4)(B)(ii) of the instructions for Exhibit 1. This instruction would mirror the instruction in proposed new paragraph (4)(B)(i). As explained above, the applicant or NRSRO would need to reflect in the transition rate for a given notch the credit ratings assigned to the obligors, securities, and money market instruments at that notch as of the period end-date (rather than transitional credit ratings assigned during the period). For example, in the Sample Transition/Default Matrix in Figure 1, there were 2000 obligors, securities and/or money market instruments assigned AA ratings as of 12/31/2000. As of 12/31/2010, 4% (or 80) of the obligors, securities, and/or money market instruments were assigned a credit rating of CCC. The path by which these obligors, securities, or money market instruments arrived at a CCC credit rating as of the period end date could have been through a series of rating actions that occurred during the 10 year period (*e.g.,* being downgraded to A, then BBB, then BB, then B, and then CCC). The transitional credit ratings of these 80 obligors, securities, and money market instruments between the AA credit rating as of 12/31/2000 and the CCC credit rating as of 12/31/2010 would not be reflected in the transition rate for the AA notch.

[202] *See* proposed new paragraph (4)(B)(iii) of the instructions for Exhibit 1. This release denotes the proposed standardized definition of the term "default" as "*Default*" to distinguish the definition and its meaning from other uses of the term "default" herein.

[203] *See* proposed new paragraph (4)(B)(iii) of the instructions for Exhibit 1. For example, the 7th row of the Sample Transition/Default Matrix in Figure 1 represents the B notch in the applicable rating scale. As reflected in the matrix, 500 obligors, securities, and/or money market instruments were assigned a credit rating of B as of the 12/31/2000 start date. Of these 500, 75 (or 15%) were classified as having gone into *Default* during period (12/31/2000–12/31/2010). Accordingly, 15% is input in the *Default* column.

[204] *See* proposed new paragraph (4)(B)(iii) of the instructions for Exhibit 1.

[205] *See* proposed new paragraphs (4)(B)(i) and (ii) of the instructions for Exhibit 1.

Matrix and, therefore, improve the default rates presented in the matrix.[206]

The Commission preliminarily believes it would be appropriate to prescribe a standard definition of *Default* in proposed new paragraph (4)(B)(iii).[207] This standard definition would need to be used by all applicants and NRSROs to determine whether an obligor, security, or money market instrument in the start-date cohort defaulted. The Commission's goal in proposing a standard definition is to make the default rates calculated and disclosed by the NRSROs more readily comparable.[208] The Commission is concerned that if applicants or NRSROs use their own definitions of "default," differences in those definitions may result in the applicants and NRSROs inconsistently classifying obligors, securities, and money market instruments as in default.[209] For example, an NRSRO that uses a narrow definition may show better (*i.e.,* lower) default rates than an NRSRO using a broader definition even though the former's credit ratings would perform no better under the broader definition. The Commission preliminarily believes that potential variances in how applicants and NRSROs may define "default" could make comparing performance across NRSROs difficult and could be a way to manipulate the data to produce more favorable results.

The Commission recognizes that a proposal to use a standard definition of default may raise concerns among the NRSROs. For example, in the past, NRSROs have argued against prescribing a standardized approach for calculating transition and default rates given the different meanings of their credit ratings and definitions of default.[210] Nonetheless, as explained above, the Commission preliminarily believes a standard definition is the preferred approach to make disclosures of default rates comparable and, therefore, useful to investors and other users of credit ratings. However, the Commission is requesting comment below on the proposed use of a standard definition, including whether there are alternatives that could achieve the Commission's goal of comparability.

Proposed new paragraph (4)(B)(iii) would prescribe two disjunctive definitions of *Default.*[211] An applicant and NRSRO would need to classify an obligor, security, or money market instrument as having gone into *Default* if the conditions in either or both of the definitions were met. The first definition would apply if the obligor failed to timely pay principal or interest due according to the terms of an obligation, or the issuer of the security or money market instrument failed to timely pay principal or interest due according to the terms of the security or money market instrument.[212] This would be the standard definition of *Default* used by the applicant or NRSRO. The goal of this proposed definition is to establish a minimum baseline for classifying an obligor, security, or money market instrument as having gone into *Default.* The Commission's intent is to avoid a situation in which applicants and NRSROs use varying definitions of default, which, as noted above, could result in some NRSROs using materially narrower definitions in order to produce more favorable default rates.[213]

The second definition would apply if the applicant or NRSRO classified the obligor, security, or money market instrument as having gone into default using its own definition of "default."[214] This proposal is designed to supplement the standard definition to address a situation where the NRSRO's definition of "default" is broader than the standard definition and, as a consequence, the NRSRO has classified an obligor, security, or money market instrument as having gone into default during the time period even though, under the standard definition, the applicant or NRSRO would not need to make a *Default* classification. The Commission preliminarily believes that the standard definition of *Default,* as proposed, is broad and would apply to most cases commonly understood as a default. Consequently, the Commission preliminarily believes a classification of default under the second definition would be rare.[215]

Finally, proposed new paragraph (4)(B)(iii) also would clarify that an obligor, security, or money market instrument that goes into in *Default* must be classified as in *Default* even if the applicant or NRSRO assigned a credit rating to the obligor, security, or money market instrument at a notch above default in its rating scale on or after the event of *Default* or withdrew the credit rating on or after the event of *Default.*[216] This proposed clarification is designed to affirm the requirement that an obligor, security, or money market instrument that goes into *Default* at any time during the period covered by the Transition/Default Matrix must be included in the default rate for the applicable category of credit rating

[206] *See* 15 U.S.C. 78o–7(q)(2)(C) (providing that the disclosures include performance information over a range of years and for a variety of types of credit ratings, including for credit ratings withdrawn by the NRSRO). The following provides an example of how withdrawals can be used to impact a default rate. In the Sample Transition/Default Matrix in Figure 1, the *Default* rate over the 10-year period for the 3600 obligors, securities, and money market instruments assigned a BBB rating as of the period start date is 4%. This means that 144 obligors, securities, or money market instruments assigned a credit rating at this notch as of the start date went into *Default* during the period (144/3600 = 4%). If the default rate was determined by the credit assigned to these 144 obligors as of the period end date, the NRSRO could withdraw, for example, 100 of these credit ratings after default. Consequently, only 44 of the obligors, securities, and/or money market instruments would be in the default category as of the period end-date and, therefore, the default rate for the BBB notch would be 1.2% instead of 4% (44/3600 = 1.2%).

[207] *See* proposed new paragraph (4)(B)(iii) of the Instructions for Exhibit 1.

[208] *See* 15 U.S.C. 78o–7(q)(2)(A) (providing that the Commission's rules shall require disclosures that are comparable among NRSROs, to allow users of credit ratings to compare the performance of credit ratings across NRSROs).

[209] *See, e.g.,* GAO Report 10–782, p. 38 ("NRSROs can differ in how they define default. Therefore, some agencies may have higher default rates than others as a result of a broader set of criteria for determining that a default has occurred.").

[210] *See, e.g.,* letter dated March 12, 2007 from Jeanne M. Dering, Executive Vice President, Moody's Investors Services and letter dated March 12, 2007 from Vickie A. Tillman, Executive Vice President, Standard & Poor's (commenting on proposals in *Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33574 (Feb. 9, 2007).

[211] *See* proposed new paragraphs (4)(B)(iii)(a) and (b) of the instructions for Exhibit 1.

[212] *See* proposed new paragraphs (4)(B)(iii)(a) of the instructions for Exhibit 1.

[213] Because this would be a standard definition, the applicant or NRSRO would need to classify the obligor, security, or money market instrument as having gone into *Default* even if the applicant or NRSRO assigned a credit rating other than default to the obligor, security, or money market instrument at the time of the event of *Default* because, for example, the applicant or NRSRO uses a narrower definition of "default."

[214] *See* proposed new paragraph (4)(B)(iii) of the instructions for Exhibit 1.

[215] The Commission recognizes that supplementing the standard definition in proposed paragraph (4)(B)(iii) with the definition used by the applicant or NRSRO could potentially import an idiosyncratic element to a given NRSRO's *Default* classifications. However, any such impact only could increase the number of obligors, securities, and money market instruments classified as having gone into *Default* (*i.e.,* an internal definition only could expand the standard definition). The Commission is not concerned if an applicant or NRSRO over-classifies (relative to other applicants or NRSROs) the number of obligors, securities, or money market instruments that went into *Default,* provided all NRSROs are using the standard definition as a baseline. Moreover, the Commission believes any such over-classifications would be *de minimis* given the broad scope of the standard definition. Furthermore, each obligor, security, and money market instrument in the start-date cohort must be assigned 1 of 5 potential outcomes. Consequently, if an applicant or NRSRO has classified an obligor, security, or money market instrument as having gone into default based on its own definition a classification of *Default* would be the most appropriate outcome among the 5 possible outcomes identified in proposed new paragraph (4)(B) of the instructions for Exhibit 1.

[216] *See* proposed new paragraph (4)(B)(iii) of the instructions for Exhibit 1.

irrespective of the post-*Default* status of the obligor, security, or money market instrument.

Proposed new paragraph (4)(B)(iv) would require an applicant and NRSRO to determine the number of obligors, securities, and money market instruments assigned a credit rating at the notch represented by the row as of the period start date that *Paid Off* at any time during the applicable time period.[217] The instructions would require that: (1) This amount be expressed as a percent of the total number of obligors, securities, and/or money market instruments assigned a credit rating at that notch as of the period start date; and (2) the percent be entered in the *Paid Off* column.[218] As with the *Default* classification, this classification would be made if the obligor, security, or money market instrument *Paid Off* at any time during the period.[219]

Proposed new paragraph (4)(B)(iv) would define *Paid Off* using two different sets of conditions: (1) One set applicable to obligors; and (2) one set applicable to securities and money market instruments.[220] The reason is that a credit rating of an "obligor" typically means a credit rating of the entity with respect to all obligations of the entity; whereas a credit rating of a "security" or "money market instrument" means a credit rating of a specific debt instrument such as a bond, note, or issuance of commercial paper.[221] Consequently, as used generally, a credit rating of an obligor does not relate to a single obligation with a term of maturity but rather to the obligor's overall ability to meet any obligations as they come due. Therefore, an obligor credit rating normally would not be classified as *Paid Off* since it does not reference a specific obligation that will mature. However, the Commission preliminarily believes it is possible that an applicant or NRSRO could determine a credit rating relating directly to an obligor's ability to meet a specific obligation with a definite term to maturity.[222] In this case, the obligor could be classified as having *Paid Off* given that the obligation to which the credit rating relates is identifiable and was extinguished during the period. At the same time, the Commission's objective is to avoid inadvertently proposing a definition that would permit an NRSRO to classify an obligor assigned a typical obligor credit rating as having *Paid Off* because it extinguished one of its obligations during the time period.[223]

For these reasons, the Commission proposes that paragraph (4)(B)(iv)(a) provide that an applicant and NRSRO may classify an obligor as having *Paid Off* only if the applicant or NRSRO assigned the obligor a credit rating with respect to a single specifically identified obligation; the obligor extinguished the obligation during the applicable time period by paying in full all outstanding principal and interest due on the obligation according to the terms of the obligation (*e.g.,* because the obligation matured, was called, or was prepaid); and the applicant or NRSRO withdrew the credit rating because the obligation was extinguished.[224] The third clause of the proposed definition (that the NRSRO withdrew the credit rating) would be designed to ensure that the credit rating, in fact, did relate to the single specifically identified obligation. If the applicant or NRSRO continued to assign a credit rating to the obligor after the obligation was extinguished, it would suggest that the credit rating related to the obligor's creditworthiness in a broader sense (*i.e.,* not with respect to the single obligation).

As for securities and money market instruments, proposed paragraph (4)(B)(iv)(b) would provide that the applicant or NRSRO may classify a security or money market instrument as having *Paid Off* only if the issuer of the security or money market instrument extinguished its obligation with respect to the security or money market instrument during the applicable time period by paying in full all outstanding principal and interest due according to the terms of the security or money market instrument (*e.g.,* because the security or money market instrument matured, was called, or was prepaid); and the applicant or NRSRO withdrew the credit rating for the security or money market instrument because the obligation was extinguished.[225] Consequently, the proposed definition would mirror the second and third elements of the definition of *Paid Off* as it relates to the credit rating of an obligor.[226]

Proposed new paragraph (4)(B)(v) would require the applicant or NRSRO to determine the number of obligors, securities, and money market instruments assigned a credit rating at the notch represented by the row as of the period start date for which the applicant or NRSRO withdrew a credit rating assigned to the obligor, security, or money market instrument at any time during the applicable time period for a reason other than *Default* or *Paid-Off*.[227] The instructions would require that: (1) This amount be expressed as a percent of the total number of obligors, securities, and/or money market instruments assigned a credit rating at that notch as of the period start date; and (2) the percent be entered in the *Withdrawn (other)* column.[228] The instructions would provide that the applicant or NRSRO must classify the obligor, security, or money market instrument as *Withdrawn (other)* even if the applicant or NRSRO assigned a credit rating to the obligor, security, or money market instrument after withdrawing the credit rating.[229]

There are legitimate reasons to withdraw a credit rating assigned to an obligor, security, or money market instrument. For example, an NRSRO might withdraw a credit rating because the rated obligor or issuer of the rated security or money market instrument stopped paying for the surveillance of the credit rating or because the NRSRO issued and was monitoring the credit rating on an unsolicited basis and no longer wanted to devote resources to

[217] *See* proposed new paragraph (4)(B)(iv) of the instructions for Exhibit 1.

[218] *Id.* For example, the 9th row of the Sample Transition/Default Matrix in Figure 1 represents the CC notch in the applicable rating scale. As reflected in the matrix, 200 obligors, securities, and/or money market instruments were assigned a credit rating of CC as of the 12/31/2000 start date. Of these 200, 4 (or 2%) were classified as having *Paid Off* during period (12/31/2000–12/31/2010). Accordingly, 2% is input in the *Paid Off* column.

[219] *See* proposed new paragraph (4)(B)(iv) of the instructions for Exhibit 1.

[220] *See* proposed new paragraphs (4)(B)(iv)(a) and (b) of the instructions for Exhibit 1.

[221] As discussed earlier, this understanding of the meaning of an "obligor" credit rating is based, in part, on the definition of "credit rating" in Section 3(a)(60) of the Exchange Act ("The term 'credit rating' means an assessment of the creditworthiness of an obligor as an entity or with respect to specific securities or money market instruments."). *See* 15 U.S.C. 78o–7(a)(60).

[222] For example, an NRSRO could issue a credit rating that relates solely to the likelihood that the obligor would meet an obligation to pay principal and interest on a specific term loan.

[223] For example, an applicant or NRSRO could seek to improve its default rates by classifying obligors as having paid off because they extinguished one obligation during the relevant period before defaulting on other obligations.

[224] *See* proposed new paragraph (4)(B)(iv)(a) of the instructions for Exhibit 1.

[225] *See* proposed new paragraph (4)(B)(iv)(b) of the instructions for Exhibit 1.

[226] *Compare* proposed new paragraphs (4)(B)(iv)(a) and (b) of the instructions for Exhibit 1.

[227] *See* proposed new paragraph (4)(B)(v) of the instructions for Exhibit 1.

[228] *Id.* For example, the 4th row of the Sample Transition/Default Matrix in Figure 1 represents the A notch in the applicable rating scale. As reflected in the matrix, 4000 obligors, securities, and/or money market instruments were assigned a credit rating of A as of the 12/31/2000 start date. Of these 4000, 80 (or 2%) were classified as having been *Withdrawn (other)* during the period (12/31/2000–12/31/2010). Accordingly, 2% is input in the *Withdrawn (other)* column.

[229] *See* proposed new paragraph (4)(B)(v) of the instructions for Exhibit 1.

monitoring it. However, the Commission also is concerned that an applicant or NRSRO could withdraw a credit rating assigned to an obligor, security, or money market instrument to make its transition or default rates appear more favorable.[230] Therefore, the Commission proposes requiring an applicant and NRSRO to disclose the percent of obligors, securities, and money market instruments for which the applicant or NRSRO withdrew the credit rating for reasons other than *Default* or *Paid Off* during the period covered by the Transition/Default Matrix.[231] Investors and other users of credit ratings could use the percents of withdrawn credit ratings to assess whether the number of withdrawals impacted the transition and default rates entered in the Transition/Default Matrix.[232] They also would be able to compare historical withdrawal percents of an NRSRO and across all NRSROs. If an NRSRO has a disproportionate number of withdrawals for one period as compared to prior periods or as compared to those of other NRSROs, investors and other users of credit ratings could consider that factor in assessing the veracity of the transition and default rates entered in the NRSRO's Transition/Default Matrix.

Request for Comment

The Commission generally requests comment on all aspects of the proposed new instructions for Exhibit 1 to Form NRSRO. The Commission also seeks comment on the following:

1. With respect to prescribing a standard method of calculating transition and default rates, would a single cohort approach (rather than an average cohort approach or some other approach)[233] be the most appropriate way to make the transition and default rates clear and informative for investors having a wide range of sophistication who use or might use credit ratings? Commenters should identify and explain any other approach they believe could be used to prescribe a standard process for calculating and presenting transition and default rates that would better achieve this goal.

2. What practical issues should the Commission consider in implementing a standard process for calculating and presenting transition and default rates? For example, would the variances in the procedures and methodologies NRSROs use to determine credit ratings raise practical issues in terms of adhering to a standard process for calculating and presenting transition and default rates? In addition, would the variances in the meanings and definitions NRSROs ascribe to the notches of credit ratings in their rating scales raise practical issues in terms of adhering to a standard process for calculating and presenting transition and default rates? How could the proposal be modified to address any practical issues identified without undermining the goal of comparability?

3. With respect to any practical issues identified in response to the solicitation of comment in question #2, would the proposed single cohort approach for calculating and presenting transition and default rates heighten or lessen the issues relative to other possible approaches such as the average cohort approach? Commenters should identify and explain any other approach they believe could be used to prescribe a standard process for calculating and presenting transition and default rates that would raise the least practical issues.

4. Would the proposals require an NRSRO to disclose proprietary information? If so, describe the type or types of proprietary information. Also, describe potential ways to address this issue.

5. Would the proposals have an impact on competition? For example, would they advantage or disadvantage a certain type of NRSRO? Could they potentially alter the behavior of NRSROs? For example, could the proposals cause certain NRSROs to stop determining a particular type of credit rating? If so, describe whether there would be any costs or negative impacts as a result and, if so, how such costs or negative impacts could be addressed.

6. How would the proposals differ from the way NRSROs currently calculate and present transition and default rates? For example, would they be more or less sophisticated than current methods? Would they be more or less burdensome than current methods? Describe the differences. Furthermore, describe the benefits of a standardized approach in terms of making the disclosure more useful to investors and other users of credit ratings.

7. Would dividing the class of credit ratings for structured finance products into the subclasses identified in proposed paragraphs (1)(D)(i) through (vii) of the instructions for Exhibit 1 provide investors and other users of credit ratings with more useful information about the performance of an NRSRO's structured finance ratings? For example, should the Commission continue to require transition and default rates for this class only as a whole? If so, explain how this would provide more useful information about the performance of an NRSRO's structured finance ratings.

8. Are the subclasses of credit ratings for structured finance products identified in proposed paragraphs (1)(D)(i) through (vii) of the instructions for Exhibit 1 the most appropriate way to stratify this class of credit ratings? For example, should the "other-ABS" subclass be divided up into subclasses based on the assets underlying the ABS (*i.e.,* auto loans, auto leases, floor plan financings, credit card receivables, student loans, consumer loans, equipment loans or equipment leases)?

[230] For example, the 5th row of the Sample Transition/Default Matrix in Figure 1 represents the BBB notch in the applicable rating scale. 3600 obligors, securities, and/or money market instruments were assigned a credit rating at this notch as of the start date. The transition rates from this notch to a lower notch are: 15% (BB), 10% (B), 6% (CCC), 5% (CC), and 1% (C). Taken together, this means that 37% (or 1332) of the obligors, securities, and money market instruments were assigned a credit rating as of the end-date that was below BBB (*i.e.,* in categories commonly referred to as "non-investment grade" or "speculative"). To lower the transition rates to "non-investment grade" categories, the credit ratings for 400 obligors, securities, or money market instruments assigned a BBB credit rating as of the start date could be withdrawn. This would reduce the transition rate to notches below BBB from 37% (1332/3600) to 26% (932/3600).

[231] *See* proposed new paragraph (4)(B)(v) of the instructions for Exhibit 1.

[232] For example, the 6th row of the Sample Transition/Default Matrix in Figure 1 represents the BB notch in the applicable rating scale. 1000 obligors, securities, and/or money market instruments were assigned a credit rating at this notch as of the start date. Of these 1000, 370 (or 37%) had their credit ratings withdrawn during the period (12/31/2000–12/31/2010). This amount is much larger than the withdrawal rates for the other notches, which range from 0% (AAA notch) to 12% (C notch). Moreover, the default rate for the BB notch (2%) is an anomaly in that it is lower than the default rate for the next highest notch BBB (4%). Normally, lower notches would be expected to have higher default rates. In addition, the AAA, AA, A, and BBB notches all have single digit default rates (ranging from 0% to 4%); whereas the notches below BBB all have double digit default rates (ranging from 15% to 67%), except for the BB notch (which, as noted, has a default rate of 2%). Furthermore, the two-notch downgrade transition rate for the BB notch is 5% (BB to CCC). This appears to be an anomaly given that the two-notch downgrade rates for the other notches are: 10% for the AA notch (AA to BBB); 10% for the A notch (A to BB); 10% for the BBB notch (BBB to B); 15% for the B notch (B to CC); 20% for the CCC notch (CCC to C); and 30% for the CC notch (CC to *Default*). An investor or other user of credit ratings reviewing this matrix could conclude that the withdrawal of credit ratings at the BB notch for reasons other than *Default* or *Paid Off* materially impacted the transition and default rates for the BB notch. The high rate of withdrawals in this instance also could be the focus of examination by the Commission staff.

[233] An average cohort approach for calculating rating transitions or default statistics consists of taking the average of several cohorts over a longer time period. For example, the one-year average transition rate would be calculated by taking the average transition rate from several one-year cohorts over a given time period.

In addition, are there other classes of structured finance products that should be identified in proposed paragraph (1)(D) of the instructions for Exhibit 1?

9. Are the descriptions of the subclasses of credit ratings for structured finance products identified in proposed paragraphs (1)(D)(i) through (vii) of the instructions for Exhibit 1 sufficiently clear to provide an applicant and NRSRO with guidance as to which credit ratings should be included in the production of the Transition/Default Matrices for each subclass? How could the descriptions be modified to make them clearer and provide better guidance?

10. Would the design and presentation of a Transition/Default Matrix prescribed in proposed paragraph (3) of the instructions for Exhibit 1 be clear and informative for investors having a wide range of sophistication who use or might use credit ratings? How could the design and presentation of the Transition/Default Matrix be modified to better achieve this goal?

11. Would the design and presentation of a Transition/Default Matrix prescribed in proposed paragraph (3) of the instructions for Exhibit 1 be an appropriate way to present transition and default rates? How could the design and presentation of the Transition/Default Matrix be modified to better accommodate these statistics?

12. Are the instructions in proposed paragraphs (1), (2), (3), and (4) of Exhibit 1 sufficiently clear in terms of requirements for producing the required Transition/Default Matrices and presenting necessary information in the Exhibit? For example, are instructions in the paragraphs sufficiently clear in terms of the requirements for populating the columns and rows of a Transition/Default Matrix? How could the instructions be modified to make them clearer and provide better guidance?

13. Should obligors, securities, and money market instruments that an applicant or NRSRO has classified as being in default as of the start date of a period covered by a Transition/Default Matrix be excluded from the start-date cohort for that matrix? If not, explain the rationale for including them.

14. Should the start-date cohorts for the Transition/Default Matrices be comprised of obligors only (*i.e.,* not include securities or money market instruments assigned credit ratings in the class or subclass)? For example, if the credit ratings of securities or money instruments issued by an obligor are simply a function of the credit rating of the obligor, would it be sufficient to include only the obligor in the start-date cohort? If so, should this be the case for all classes and subclasses of credit ratings or for certain classes and subclasses? For example, the credit ratings assigned to securities and money market instruments in the structured finance class often are based on differing levels of credit enhancement specific to each tranche of a security issued by the obligor. Consequently, in such a case, the credit rating of the security or money market instrument issued would not be a function solely or primarily of the credit rating of the obligor.

15. Commenters are referred to the questions in Section II.M.4.a of this release with respect Items 6 and 7 of Form NRSRO and how certain types of obligors, securities, and money market instruments should be classified for purposes of providing approximate amounts of credit ratings outstanding in each class of credit rating for which an applicant is seeking registration (Item 6) or an NRSRO is registered (Item 7)? In responding to those questions, commenters should consider how proposed classifications could be applied to determining the composition of start-date cohorts for the purposes of the proposed enhancements to Exhibit 1.

16. Should the default rates in the Transition/Default Matrices be determined using the proposed standard definition of *Default*? For example, would the use of a standard definition raise practical issues in light of the different meanings that NRSROs ascribe to the notches in their credit rating scales or the different definitions of "default" they utilize? How could the proposal be modified to address any practical issues identified without undermining the goal of comparability?

17. Is the proposed standard definition of *Default* sufficiently broad to apply to most, if not all, events commonly understood as constituting a default? For example, should the definition explicitly include that the obligor or issuer of the security or money market instrument is in a bankruptcy proceeding or would this be redundant in that the definition already provides that the obligor or issuer of the security has failed to timely pay interest or principal due? In addition, should the definition explicitly include events that would constitute a default due to a breach of a covenant unrelated to the failure to timely pay interest or principal due on a security or money market instrument (*e.g.,* a covenant might provide that a default by the issuer on a bank loan to a third party or a default by an affiliate of the issuer would constitute a default with respect to a rated security of the issuer)? Would it be appropriate to include such cross-default provisions as part of the definition of the *Default* in the instructions for Exhibit 1? For example, if the issuer continued to make timely payments of interest and principal to the holders of the security notwithstanding the cross-defaults, would it nonetheless be appropriate to classify the security as in *Default*? If so, how could the proposed definition be modified to make it broad enough to apply to all instances of default? Should the requirement provide for an NRSRO to be able to use its own definition if the standard definition would not be feasible given the NRSRO's procedures and methodologies for determining credit ratings? If so, should the NRSRO be required to make disclosures about why it is using its own definition? Describe the nature of such disclosures.

18. Should the proposed standard definition of *Default* be refined to distinguish between degrees of default severity? For example, should the definition distinguish between a situation where an obligor or the issuer of a security or money market instrument has failed to make a timely payment of interest or principal that potentially could be cured and the situation where the obligor or issuer of the security or money market instrument is no longer able to cure a failed payment of interest or principal or is in a bankruptcy proceeding? How could the proposed definition be modified to account for relative degrees of default severity and how should such modifications be incorporated into the proposed instructions for calculating default statistics?

19. Is the proposed standard definition of *Paid Off* sufficiently broad to apply to most, if not all, events commonly understood as constituting the extinguishment of an obligation upon which a credit rating is based? If not, how could the proposed definition be modified to make it broad enough to apply to all instances that should, for the purposes of transition and default rates, be classified as having *Paid Off*? Should the requirement provide for an NRSRO to be able to use its own definition if the standard definition would not be feasible given the NRSRO's procedures and methodologies for determining credit ratings? If so, should the NRSRO be required to make disclosures about why it is using its own definition? Describe the nature of such disclosures.

20. Would the proposed treatment for *Withdrawn (other)* credit ratings in the Transition/Default Matrices sufficiently

address the concern that an applicant or NRSRO might use withdrawals to make its transition and default rates appear more favorable? For example, should the Commission, by rule, require an NRSRO to monitor an obligor, security, or money market instrument after withdrawal in order to classify whether the obligor, security, or money market instrument went into *Default* or *Paid Off*? If so, how long should the applicant or NRSRO be required to monitor the obligor, security, or money market instrument? Alternatively, should the applicant or NRSRO be required to explain and disclose in Exhibit 1 the reason why it withdrew the credit ratings in the given class or subclass of credit ratings? If so, how much detail should the applicant or NRSRO provide in the description? Should the requirement provide for an NRSRO to be able to use its own definition if the standard definition would not be feasible given the NRSRO's procedures and methodologies for determining credit ratings? If so, should the NRSRO be required to make disclosures about why it is using its own definition? Describe the nature of such disclosures.

b. Proposed Amendments to Rule 17g–1

Section 15E(q)(2)(D) of the Exchange Act provides that the Commission's rules must require an NRSRO to make the information about the performance of credit ratings freely available and disclose it on an easily accessible portion of its Web site, and in writing when requested.[234] The Commission proposes to implement Section 15E(q)(2)(D) by amending paragraph (i) of Rule 17g–1.[235] Paragraph (i) requires an NRSRO to make its current Form NRSRO and information and documents submitted in Exhibits 1 through 9 publicly available on its Web site or through another comparable, readily accessible means within 10 business days of being granted an initial registration or a registration in an additional class of credit ratings, and within 10 business days of furnishing a Form NRSRO to update information on the Form, to provide the annual certification, and to withdraw a registration.[236] These requirements implemented Section 15E(a)(3) of the Exchange Act,[237] which provides, among other things, that the Commission shall, by rule, require an NRSRO, upon the granting of a registration, to make the information and documents submitted to the Commission in its completed application for registration, or in any amendment, publicly available on its Internet Web site, or through another comparable, readily accessible means.[238]

Although Section 15E(q)(2)(D) only addresses disclosures of information about the performance of credit ratings, the Commission is proposing to amend paragraph (i) of Rule 17g–1 to require an NRSRO to make Form NRSRO and Exhibits 1 through 9 freely available on an easily accessible portion of its corporate Internet Web site. This would avoid having separate requirements for the Exhibit 1 performance statistics and the rest of Form NRSRO and the other public Exhibits. The Commission preliminarily believes users of credit ratings would benefit if Form NRSRO and all the public Exhibits were disclosed together in the same manner. In addition, the Commission preliminarily believes applying the requirement to disclose the information on an "easily accessible" portion of the NRSRO's corporate Internet Web site would assist investors and other users of credit ratings by making it easier to locate a Form NRSRO. For example, some corporate Internet Web sites contain large amounts of information, some of which must be accessed by navigating through multiple Web pages. The Commission believes Form NRSRO and the public Exhibits should be easy for investors and other users of credit ratings to locate when they access an NRSRO's corporate Internet Web site. In this regard, the Commission preliminarily believes that a Form NRSRO would be on an "easily accessible" portion of a Web site if it could be accessed through a clearly and prominently labeled hyperlink to the Form on the home-page of the NRSRO's corporate Internet Web site.

The proposed amendment to paragraph (i) also would remove the option for an NRSRO to make its Form NRSRO publicly available "through another comparable, readily accessible means" as an alternative to Internet disclosure. The Commission preliminarily believes there is no alternative means of disclosure that makes information as "readily accessible" as (and, therefore, is comparable to) an Internet Web site. This view is supported by the fact that all NRSROs currently comply with paragraph (i) of Rule 17g–1 by making their Form NRSROs available on their corporate Internet Web sites.[239] The Commission, therefore, is proposing amending paragraph (i) to require that the disclosure of Form NRSRO and its public Exhibits be made on an NRSRO's corporate Internet Web site without exception.[240] In addition, to implement Section 15E(q)(2)(D) of the Exchange Act, the Commission is proposing to amend paragraph (i) to provide that Exhibit 1 must be made freely available in writing, when requested.

Finally, the Commission notes that throughout Form NRSRO and the Instructions to Form NRSRO there are references to the current requirement in paragraph (i) to make Form NRSRO and information and documents submitted in Exhibits 1 through 9 "publicly available on [the NRSRO's] Web site or through another comparable, readily accessible means.[241] The Commission proposes amending all these references so that they would mirror the text of the proposed amendment to paragraph (i).

Request for Comment

The Commission generally requests comment on all aspects of the proposed amendments to paragraph (i) of Rule 17g–1. The Commission also seeks comment on the following:

1. Is there any reason why the Commission should not apply the requirement to make an NRSRO's performance statistics "freely available on an easily accessible portion of its Web site" to Form NRSRO and the public Exhibits as a whole? For example, should the requirement apply only to Exhibit 1?

2. Is the Commission correct in its preliminary belief that a Form NRSRO would be on an "easily accessible" portion of a Web site if it could be accessed through a clearly and prominently labeled hyperlink to the Form on the home-page of the NRSRO's corporate Internet Web site? Are there other portions of an NRSRO's corporate Internet Web site that, provided the NRSRO placed a hyperlink to Form NRSRO on such portion of the Web site, should be deemed "easily accessible"?

3. Is there another means of making Form NRSRO publicly available besides the Internet that should be deemed "another comparable, readily accessible means"? If so, identify the means and explain the potential advantages of permitting it as a means of disclosure.

[234] *See* 15 U.S.C. 78o–7(q)(2)(D).

[235] *See* proposed amendments to paragraph (i) of Rule 17g–1.

[236] *See* 17 CFR 240.17g–1(i).

[237] 15 U.S.C. 78o–7(a)(3).

[238] *See* 15 U.S.C. 78o–7(a)(3).

[239] *See Annual Report on Nationally Recognized Statistical Rating Organizations. Commission* (Jan. 2011), pp. 18–19.

[240] *See* proposed amendments to paragraph (i) of Rule 17g–1.

[241] *See, e.g.,* references in Item 5, in the Note to Item 6.C, Item 8, and Item 9 of Form NRSRO and Instruction A.3 and Instruction H to Form NRSRO.

4. With respect to the proposed requirement that Exhibit 1 be made freely available in writing, when requested, how should an NRSRO meet such a request? For example, should an NRSRO be required to mail a written copy of Exhibit 1 to a party requesting the Exhibit? If so, would it be appropriate to permit the NRSRO to charge reasonable handling and postage fees? For example, would allowing an NRSRO to charge a reasonable handling and postage fee discourage requests that are not based on a legitimate need to obtain Exhibit 1 in paper form? In this regard, the Commission notes that Exhibit 1 currently can be immediately accessed through an NRSRO's corporate Internet Web site and, under the proposed amendments to paragraph (i) of Rule 17g–1, would need to be posted on an easily accessible portion of the NRSRO's corporate Internet Web site. Consequently, why would a person have a legitimate need to request that an NRSRO provide Exhibit 1 in paper form (which would take time to process the request and send out the Exhibit) when it could be obtained immediately through the Internet?

2. Proposed Enhancements to Rating Histories Disclosures

Paragraph (a)(8) of Rule 17g–2 requires an NRSRO to make and retain a record that, "for each outstanding credit rating, shows all rating actions and the date of such actions from the initial credit rating to the current credit rating identified by the name of the rated security or obligor and, if applicable, the CUSIP of the rated security or the Central Index Key ("CIK") number of the rated obligor." [242] An NRSRO is required to retain this record for three years pursuant to paragraph (c) of Rule 17g–2.[243]

In addition, paragraph (d) of Rule 17g–2 requires the NRSRO to publicly disclose certain of this information as well. Specifically, paragraph (d)(2) of Rule 17g–2 requires an NRSRO to "make and keep publicly available on its corporate Internet Web site in an eXtensible Business Reporting Language ("XBRL") format" the information required to be documented pursuant to paragraph (a)(8) of Rule 17g–2 for 10% of the outstanding credit ratings, selected on a random basis, in each class of credit rating for which the NRSRO is registered if the credit rating was paid for by the obligor being rated or by the issuer, underwriter, or sponsor of the security being rated ("issuer-paid" credit ratings) and the NRSRO has 500 or more such issuer-paid credit ratings outstanding in that class (the "10% Rule").[244] Paragraph (d)(2) further provides that any ratings action required to be disclosed need not be made public less than six months from the date the action is taken.[245] This six-month grace period is designed to preserve the ability of NRSROs to sell data feeds to the portfolios of their current credit ratings by making the information disclosed in the 10% Rule out-of-date.[246] Paragraph (d)(2) also requires that, if a credit rating made public pursuant to the rule is withdrawn or the rated instrument matures, the NRSRO must randomly select a new outstanding credit rating from that class of credit ratings in order to maintain the 10% disclosure threshold.[247] Finally, paragraph (d)(2) provides that in making the information available on its corporate Internet Web site, the NRSRO must use the List of XBRL Tags for NRSROs as specified on the Commission's Internet Web site.[248]

Paragraph (d)(3) of Rule 17g–2 requires an NRSRO to make publicly available on its corporate Internet Web site information required to be documented pursuant to paragraph (a)(8) of the rule for any credit rating initially determined by the NRSRO on or after June 26, 2007, the effective date of the Rating Agency Act of 2006 (the "100% Rule").[249] The 100% Rule applies to all types of credit ratings, as opposed to the 10% Rule, which is limited to issuer-paid credit ratings. However, paragraphs (d)(3)(i)(B) and (C) prescribe different grace periods for when an NRSRO must disclose a rating action depending on whether or not it was issuer-paid.[250] Specifically, paragraph (d)(3)(i)(B) provides that if the credit rating is issuer-paid, then the grace period is 12 months after the date the action is taken.[251] Similar to the 6-month grace period in the 10% Rule, this 12-month grace is designed to preserve the ability of NRSROs to sell data feeds to their portfolios of current outstanding credit ratings by making the information disclosed in the 100% Rule out-of-date.[252] For all non-issuer paid credit ratings, paragraph (d)(3)(i)(C) provides a grace period of 24 months after the date the rating action is taken. This longer grace period is designed to address the "subscriber-paid" business model in which the NRSRO makes its credit ratings available for a fee rather than for free.[253] Paragraph (d)(3)(ii) of Rule 17g–2 requires the NRSRO to disclose the ratings history information on its corporate Internet Web site in an XBRL format using the List of XBRL Tags for NRSROs as published by the Commission on its Internet Web site.[254]

The Commission is proposing amendments designed to enhance the utility of the 100% Rule.[255] Moreover, in light of the proposed amendments to the 100% Rule (discussed below) and Exhibit 1 (discussed above), the Commission is proposing to repeal the 10% Rule. The 10% Rule does not permit comparability across NRSROs

[242] 17 CFR 240.17–2(a)(8). A CIK number has ten-digits and is assigned to uniquely identify a filer using the Commission's EDGAR system.

[243] *See* 17 CFR 240.17g–2(c).

[244] 17 CFR 240.17–2(d)(2).

[245] *Id.*

[246] The fact that the disclosure involves only a random sample of 10% of the outstanding credit ratings also limits the utility of the information disclosed in terms of serving as a substitute to purchasing a data feed to the NRSRO's current portfolio of outstanding credit ratings.

[247] 17 CFR 240.17–2(d)(2).

[248] *Id.*

[249] 17 CFR 240.17–2(d)(3).

[250] 17 CFR 240.17–2(d)(3)(i)(B) and (C).

[251] 17 CFR 240.17–2(d)(3)(i)(B).

[252] *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63837–63842 (Dec. 4, 2009) (discussing the grace periods in the rule).

[253] *Id.*

[254] At the time the 10% Rule became effective (which preceded the 100% Rule), the Commission had not published the List of XBRL Tags. Consequently, the Commission issued a notice that NRSROs could use any machine readable format to publish the ratings history information required by the 10% Rule. *See Notice Regarding the Requirement to Use eXtensible Business Reporting Language Format to Make Publicly Available the Information Required Pursuant to Rule 17g–2(d) of the Exchange Act,* Exchange Act Release No. 60451 (Aug. 5, 2009). On August 27, 2010, the Commission provided notice that the List of XBRL tags required to be used for purposes of the 10% Rule and, the subsequently adopted 100% Rule, was available on the Commission's Internet Web site. *See Notice Regarding the Requirement to Use eXtensible Business Reporting Language Format to Make Publicly Available the Information Required Pursuant to Rule 17g–2(d) of the Exchange Act,* Exchange Act Release No. 62784 (Aug. 27, 2010), 75 FR 53988 (Sept. 2, 2010). Information about the List of XBRL Tags is located at the following page on the Commission's Web site: *http://www.sec.gov/spotlight/xbrl/nrsro-implementation-guide.shtml.* The publication of this notice in the **Federal Register** triggered the 60-day period after which NRSROs were required to begin using an XBRL format for purposes of the two rules. The 60-day period ended on November 1, 2010. The XBRL Tags identified by the Commission include mandatory tags with respect to the information specifically identified in paragraph (a)(8) of Rule 17g–2 (17 CFR 240.17g–2(a)(8)) (*i.e.,* the date of the rating action, the credit rating identified by the name of the rated security or obligor and, if applicable, the CUSIP of the rated security or the CIK number of the rated obligor). The XBRL Tags also identify additional information that could be tagged by the NRSRO to enhance the disclosure.

[255] *See, e.g.,* GAO Report 10–782, p. 40 ("However, we found that the data disclosed under the 10 percent sample disclosure requirement do not contain enough information to construct comparable performance statistics and are not representative of the population of credit ratings at each NRSRO and that the data disclosed under the 100 percent disclosure requirement likely present similar issues.").

because it captures only issuer-paid credit ratings in a class of credit ratings where there are 500 or more such ratings and only if two or more NRSROs randomly select the same rated obligor, issuer, or money instrument to be included in the sample.[256] Moreover, the Commission understands that the 10% Rule may not produce sufficient "raw data" to allow third parties to generate independent performance statistics.[257] The goal of the rule was to provide some information about how an NRSRO's credit ratings performed, particularly ratings assigned to obligors, securities and money market instruments that had been rated for 10 or 20 years. The Commission now preliminarily believes that, in light of the proposed enhancements to Exhibit 1 and the 100% Rule, the 10% Rule would provide minimal incremental benefit to investors and other users of credit ratings in terms of providing information about the performance of a given NRSRO's credit ratings.

With respect to the 100% Rule, the Commission is proposing its provisions be moved from Rule 17g–2 (the NRSRO recordkeeping rule) to Rule 17g–7.[258] Currently, Rule 17g–7 requires an NRSRO to disclose certain information in any report accompanying an asset-backed security.[259] In other words, the rule requires an NRSRO to publicly disclose information outside of Form NRSRO (the predominant NRSRO disclosure rule). Similarly, the 100% Rule in its current form (and as proposed) also requires (and would require) an NRSRO to disclose information outside of Form NRSRO. Finally, as discussed below in Section II.G of this release, Section 15E(s) of the Exchange Act provides that the Commission shall adopt rules to require an NRSRO to disclose further information outside of Form NRSRO.[260] The Commission is proposing to consolidate non-Form NRSRO disclosure rules by codifying them in Rule 17g–7.[261]

The proposed enhancements to the 100% Rule would be codified in new paragraph (b) of Rule 17g–7.[262] Proposed paragraph (b)(1) would require, among other things, that the NRSRO publicly disclose the ratings history information for free on an easily accessible portion of its corporate Internet Web site.[263] This would implement Section 15E(q)(2)(D) of the Exchange Act and, by using the "easily accessible portion" language, enhance the current requirement of the 100% Rule that the ratings history information be disclosed on the NRSRO's corporate Internet Web site.[264] As discussed above in Section II.E.1.b of this release, some Internet Web sites contain large amounts of information, some of which must be accessed by navigating through multiple web pages.[265] Consequently, as discussed, the Commission preliminary believes that Form NRSRO would be on an "easily accessible" portion of an Internet Web site if it could be accessed through a clearly and prominently labeled hyperlink to the Form on the homepage of the NRSRO's corporate Internet Web site. The Commission preliminarily believes that the same holds true for the disclosure of the data file or files containing the information that would be required by the enhanced 100% Rule.[266]

The next enhancement to the 100% Rule proposed by the Commission is to substantially broaden the scope of credit ratings that would be subject to the disclosure requirements. The Commission's intent is to require disclosure of information about all outstanding credit ratings in each class and subclass of credit ratings for which the NRSRO is registered but within certain prescribed time frames. As noted above, the 100% Rule currently only captures credit ratings where the NRSRO initially determined a credit rating for the obligor, security, or money market instrument on or after June 26, 2007.[267] This means that obligors, securities, and money market instruments assigned a credit rating by the NRSRO before that date are excluded entirely from the disclosure even if a rating action is taken with respect to the obligor, security, or money market instrument after that date. Consequently, if a user of the disclosures wanted to calculate a transition or default rate for a given NRSRO's credit ratings, the user could not compile a start-date cohort that included all obligors, securities, or money market instruments assigned a credit as of the start date.[268] The Commission's proposal would be designed to address this issue.[269]

In particular, the Commission is proposing that the rule no longer be limited to the disclosure of histories for credit ratings where the NRSRO initially

[256] *See, e.g.,* GAO Report 10–782, pp. 40–47.

[257] *Id.*

[258] 17 CFR 240.17g–7.

[259] *See* 17 CFR 240.17g–7, which requires an NRSRO to include in any report accompanying a credit rating with respect to an asset-backed security, as that term is defined in Section 3(a)(77) of the Exchange Act (15 U.S.C. 78c(a)(77)) a description of: the representations, warranties and enforcement mechanisms available to investors; and how they differ from the representations, warranties and enforcement mechanisms in issuances of similar securities. *Id.*

[260] *See* 15 U.S.C. 78o–7(s).

[261] *See* 15 U.S.C. 78o–7 and 15 U.S.C. 78q. The current provisions of Rule 17g–7 would be incorporated into new paragraph (a) of Rule 17g–7 as discussed below in Section II.G of this release. The Commission notes that some NRSROs may (or could in the future) have additional disclosure requirements based on their status as another type of registrant or because they are part of a company that has filing obligations under other provisions of the securities laws. The Commission does not intend to consolidate such other disclosure requirements in Rule 17g–7.

[262] *See* proposed new paragraph (b) of Rule 17g–7.

[263] *See* proposed new paragraph (b)(1) of Rule 17g–7.

[264] *See* 15 U.S.C. 78o–7(q)(2)(D); *compare* 17 CFR 240.17g–7(d)(3)(i)(A), *with* proposed new paragraph (b) of Rule 17g–7. As discussed above, Section 15E(q)(2)(D) of the Exchange Act provides that the Commission's rules shall require the information about the performance of credit ratings be published and made freely available by the NRSRO, on an easily accessible portion of its Web site, and in writing, when requested. *Id.* The Commission, however, preliminarily believes that the "in writing" requirement would not be feasible if applied to the disclosures of rating histories. First, the data file containing the disclosures would need to be constantly updated by the NRSRO as new rating actions are added. Thus, it would not remain static like the Exhibit 1 performance measurement statistics which are updated annually. Consequently, by the time a party received a written copy of the disclosure, it likely would not be up-to-date. Second, the amount of information in the data file would be substantial (particularly for NRSROs that have issued hundreds of thousands of credit ratings) and increase over time. For these reasons, the Commission preliminarily believes that converting the information in the electronic disclosure to written form and mailing it to the party making the request would be impractical and not particularly useful. In terms of utility, as discussed below, the electronic disclosure of the data would need to be made using an XBRL format. The Commission preliminarily believes this would be a much more efficient and practical medium for accessing and analyzing the information rather than obtaining it in paper form. Consequently, the Commission preliminarily believes that the benefits, if any, to requiring a written disclosure would be limited. However, the Commission is requesting comment below on this issue.

[265] *See* Section II.E.1.b of this release proposing amendments to paragraph (i) of Rule 17g–1 to implement Section 15E(q)(2)(D) of the Exchange Act. 15 U.S.C. 78o–7(q)(2)(D). Under the proposals, an NRSRO would need to make Form NRSRO and Exhibits 1 through 9 "freely available on an easily accessible portion of its website." *See* proposed amendments to paragraph (i) of Rule 17g–1.

[266] *See* 15 U.S.C. 78o–7(q)(2)(D).

[267] *See* 17 CFR 240.17g–2(d)(3)(i)(A).

[268] *See, e.g.,* GAO Report 10–782, p. 45. This issue is particularly acute when the NRSRO determines credit ratings for obligors in only one class of credit ratings. As discussed earlier, obligor credit ratings typically provide an assessment of the relative creditworthiness of the obligor as an entity for all its obligations. Thus, it is different from a credit rating for a security or money instrument that typically has a single finite obligation that will mature, be called, or be prepaid (if it does not default). An NRSRO that primarily issued obligor credit ratings in a class and initially rated them prior to June 26, 2007 would never have to include the rating histories of these obligors in the disclosure. For example, the NRSRO could be monitoring credit ratings for the same group of obligors that were initially rated 10 to 20 years ago. In this case, the NRSRO would have no ratings histories to disclose.

[269] *See, e.g.,* GAO Report 10–782, pp. 45–46.

determined a credit rating for the obligor, security, or money market instrument on or after June 26, 2007.[270] Instead, the rule, as proposed, would apply to any credit rating that was outstanding as of June 26, 2007, but the rating histories disclosed for these credit ratings would not need to include information about actions taken before June 26, 2007.[271] Moreover, in order to immediately include these credit ratings in the disclosure, the proposed rule would require the NRSRO to disclose the credit rating assigned to the obligor, security, or money market instrument and associated information as of June 26, 2007. Specifically, proposed paragraph (b)(1)(i) of Rule 17g–7 would require an NRSRO to disclose each credit rating assigned to an obligor, security, and money market instrument in every class of credit ratings for which the NRSRO is registered that was *outstanding* as of June 26, 2007 and any subsequent upgrades or downgrades of a credit rating assigned to the obligor, security, or money market instrument (including a downgrade to, or assignment of, default), any placements of a credit rating assigned to the obligor, security, or money market instrument on watch or review, any affirmation of a credit rating assigned to the obligor, security, or money market instrument, and a withdrawal of a credit rating assigned to the obligor, security, or money market instrument.[272] Consequently, an NRSRO would need to include in the XBRL file through which it makes the rating history disclosures all outstanding credit ratings as of June 26, 2007 (*i.e.,* not wait until a new rating action was taken with respect to the credit rating) and then disclose subsequent actions taken with respect to those credit ratings. In other words, the histories for this class of credit ratings would begin on June 26, 2007. This would mean that the disclosures would not contain complete histories for many credit ratings.[273] However, the disclosures would capture all outstanding credit ratings in each class of credit ratings for which the NRSRO is registered and, therefore, market participants could immediately begin computing short-term transition and default rates using start-date cohorts that include all the obligors, securities, and money market instruments assigned a credit rating in a given class.[274]

Proposed paragraph (b)(1)(ii) of Rule 17g–7 would contain the existing requirement in the 100% Rule that an NRSRO disclose rating histories for each credit rating in every class of credit ratings for which the NRSRO is registered that was initially determined on or after June 26, 2007 and any subsequent rating action taken with respect to such credit ratings.[275] Specifically, proposed paragraph (b)(1)(ii) would require the NRSRO to disclose each credit rating assigned to an obligor, security, and money market instrument in every class of credit ratings for which the NRSRO is registered that was initially determined on or after June 26, 2007, and any subsequent upgrades or downgrades of a credit rating assigned to the obligor, security, or money market instrument (including a downgrade to, or assignment of, default), any placements of a credit rating assigned to the obligor, security, or money market instrument on watch or review, any affirmation of a credit rating assigned to the obligor, security, or money market instrument, and a withdrawal of a credit rating assigned to the obligor, security, or money market instrument. Consequently, the disclosure mandated under proposed paragraph (b)(1) of Rule 17g–7 would capture all credit ratings outstanding as of June 26, 2007 (regardless of when the obligor, security, or money market instrument was initially assigned a credit rating) and the subsequent rating actions taken with respect to those credit ratings as well as all credit ratings initially determined on or after that date and the subsequent rating actions taken with respect to those credit ratings.[276]

The next enhancement to the 100% Rule proposed by the Commission is to increase the number and scope of the data fields that must be disclosed about a rating action.[277] Specifically, proposed paragraph (b)(2) of Rule 17g–7 would identify 7 categories of data that would need to be disclosed when a credit rating action is published pursuant to proposed new paragraph (b)(1) of Rule 17g–7. In addition, some of the categories would have sub-categories.[278] The goal would be to make the data more useful in terms of the amount of information provided, the ability to search and sort the information, and the ability to compare historical rating information across NRSROs.[279]

Proposed new paragraph (b)(2)(i) of Rule 17g–7 would identify the first category of data: namely, the identity of the NRSRO disclosing the rating action.[280] This may seem unnecessary as the identity of the NRSRO making the disclosure should be obvious. However, as noted above, the NRSRO would need to assign an XBRL Tag to each item of information, including the identity of the NRSRO. Including and tagging the identity of the NRSRO would assist users who download and combine data files of multiple NRSROs to sort credit ratings by a given NRSRO.

Proposed new paragraph (b)(2)(ii) of Rule 17g–7 would identify the second category of data: namely, the date of the rating action.[281] This proposed

[270] *See* proposed new paragraph (b)(1)(i) of Rule 17g–7.

[271] The Commission notes, however, that an NRSRO could voluntarily disclose more rating history information than required by the current rule or the proposed amendment to the rule.

[272] *Id.*

[273] For example, assume an obligor was initially rated in AA on June 26, 2000. Thereafter, the rating was downgraded to AA- on June 26 2003, to A on June 26, 2005, and to BBB on June 26, 2008. Under the proposed rule, the ratings history disclosure would cross the June 26, 2007 threshold with an A rating. The history for this obligor would omit the initial AA rating on June 26, 2000 and the downgrades to AA- and A on June 26, 2003 and June 26, 2005, respectively. Therefore, the first event in the rating history would be that the obligor was assigned an A rating as of June 26, 2007. The next event in the rating history would be the downgrade of the credit rating to BBB on June 26, 2008.

[274] For example, a user of the credit rating histories would be able to generate transition and default rates for a period having a start date as far back as June 26, 2007. In doing so, the user would be able to compile a start-date cohort consisting of all the obligors, securities, and money market instruments assigned an outstanding credit rating in a given class as of June 26, 2007. The user could compute transition and default rates over short-term periods (*i.e.,* 1 or 2 years) in the near term and for longer periods as time progresses and more ratings actions over a longer time horizon are added to the disclosure. In addition, the user could calculate transition or default rates using a different process than the single cohort approach proposed for the Exhibit 1 disclosures. For example, the user could begin calculating short-term transition and default rates using a rolling average in which start-date cohorts are identified each month (*e.g.,* June 26, 2007, July 26, 2007, August 26, 2007, and so on).

[275] *See* proposed new paragraph (b)(1)(ii) of Rule 17g–7.

[276] *See* proposed new paragraph (b)(1) of Rule 17g–7.

[277] *See* proposed new paragraph (b)(2) of Rule 17g–7.

[278] If adopted, the Commission would need to update the List of XBRL Tags to include some of the new data fields; whereas other of the fields are covered by existing Tags, including by some of the voluntary Tags.

[279] *See, e.g.,* GAO Report 10–782, p. 41 ("First, SEC [sic] did not specify the data fields the NRSROs were to disclose in the rule, and the data fields provided by the NRSROs were not always sufficient to identify a complete rating history for ratings in each of the seven samples. If users cannot identify the rating history for each rating in the sample, they cannot develop performance measures that track how an issuer's credit rating evolves.").

[280] *See* proposed new paragraph (b)(2)(i) of Rule 17g–7.

[281] *See* proposed new paragraph (b)(2)(ii) of Rule 17g–7. The Commission notes that many of the rating actions in an NRSRO's disclosure would share the date of June 26, 2007, which would be the first action disclosed for rating histories of credit ratings initially determined before June 26, 2007. This would result from the proposed requirement to add all credit ratings outstanding as of June 26, 2007 to the disclosure. *See* proposed new paragraph (b)(1)(i) of Rule 17g–7. As discussed below, the

requirement is in the 100% Rule as it exists today.[282] The inclusion of the date of a rating action is designed to allow investors and other users of credit ratings to review the timing of a rating action.[283] This would allow the person reviewing the credit rating histories of the NRSROs to reach conclusions about which NRSROs did the best job in determining an initial rating and, thereafter, making appropriate and timely adjustments to the credit rating.[284]

Proposed new paragraph (b)(2)(iii) of Rule 17g–7 would identify the third category of data.[285] The information in this category would need to be disclosed if the rating action is taken with respect to an obligor (*i.e.,* as opposed to a credit rating of a security or money market instrument). In this case, the NRSRO would need to disclose (if applicable): (1) the CIK number of the rated obligor; and (2) the legal name of the obligor. This proposed requirement is in the 100% Rule as it exists today.[286]

Proposed new paragraph (b)(2)(iv) of Rule 17g–7 would identify the fourth category of data.[287] The information in this category would need to be disclosed when the rating action is taken with respect to a security or money market instrument. In this case, the NRSRO would need to disclose (if applicable): (1) The CIK number of the issuer of the security or money market instrument; (2) the legal name of the issuer of the security or money market instrument; and (3) the CUSIP of the security or money market instrument.[288] The proposed requirement to include the CUSIP of security or money market instrument is in the 100% Rule as it exists today.[289] The requirements to include the name and CIK number of the issuer would be new. The Commission preliminarily believes including this information would be useful because it would allow users of the XBRL data file to sort credit ratings of securities and money market instruments by issuer.

Proposed paragraph (b)(2)(v) of Rule 17g–7 would identify the fifth category of data: namely, a classification of the type of rating action.[290] The NRSRO would be required to select 1 of 7 classifications to identify the reason for the rating action.[291] Aside from the first classification discussed below, the Commission preliminarily believes that the classifications identify all types of actions an NRSRO might take with respect to a credit rating.

The first classification would be that the rating action constitutes a disclosure of a credit rating that was outstanding as of June 26, 2007 for the purposes of proposed paragraph (b)(1)(i) of Rule 17g–7.[292] As discussed above, the Commission is proposing that the 100% rule capture all credit ratings outstanding as of June 26, 2007 by disclosing the credit rating and associated information as of that date.[293] If adopted, this would mean that thousands, if not hundreds of thousands, of ratings histories each beginning on June 26, 2007 would be disclosed. The proposed classification is designed to alert users of the disclosures that the proposed rule caused the June 26, 2007 entry in the rating history of the obligor, security, or money market instrument and not because, for example, a credit rating was initially determined for the obligor, security, or money market instrument on that date.

The second classification would be that the rating action was an initial credit rating.[294] For example, an NRSRO would select this classification if the rating action was the first credit rating determined by the NRSRO with respect to the obligor, security, or money market instrument. The third classification would be an upgrade to an existing credit rating.[295] The fourth classification would be a downgrade to an existing credit rating, which would include assigning a credit rating of default.[296] The fifth classification would be placing an existing credit rating on credit watch or review.[297] This means the NRSRO has disclosed that it is actively evaluating whether the credit rating should be changed. The sixth classification would be affirming the current credit rating assigned to the obligor, security, or money market instrument.[298] For example, an NRSRO may publish an announcement that it is affirming the current credit rating of an obligor, security, or money market instrument and, consequently, determine not to upgrade or downgrade the credit rating to a different notch in the rating scale.

The seventh classification would be the withdrawal of an existing credit rating.[299] In the case of a withdrawal, the NRSRO would be required to provide a sub-classification identifying reason for the withdrawal.[300] There would be three sub-classifications: (1) The obligor defaulted, or the security or money, market instrument went into default;[301] (2) the obligation subject to the credit rating was extinguished by payment in full of all outstanding principal and interest due on the obligation according to the terms of the obligation;[302] or (3) the credit rating was withdrawn for reasons other than those set forth in (1) and (2) above.[303]

Commission is proposing that this action (the adding of an outstanding credit rating) have a unique XBRL tag so that persons using these disclosures do not confuse the action as an initial credit rating or change to an existing credit rating (*e.g.,* an upgrade or a down grade). *See* proposed new paragraph (b)(2)(v)(A) of Rule 17g–7.

[282] *See* 17 CFR 240.17g–2(a)(8).

[283] *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63837–63838 (Dec. 4, 2009).

[284] *Id.*

[285] *See* proposed new paragraph (b)(2)(iii) of Rule 17g–7.

[286] *See* 17 CFR 240.17g–2(a)(8).

[287] *See* proposed new paragraph (b)(2)(iv) of Rule 17g–7.

[288] CUSIP stands for the Committee on Uniform Securities and Identification. A CUSIP number consists of nine characters that uniquely identify a company or issuer and the type of security.

[289] *See* 17 CFR 240.17g–2(a)(8).

[290] *See* proposed paragraph (b)(2)(v) of Rule 17g–7.

[291] The actual disclosure would need to be the type of rating action and not the credit rating resulting from the rating action. For example, if the rating action was a downgrade, the NRSRO would need to classify it as a "downgrade" and not, for example, a change of the current credit rating from the AA notch to AA- notch. This would allow users of the disclosures to sort the information by, for example, initial credit ratings, upgrades, and downgrades.

[292] *See* proposed paragraph (b)(2)(v)(A) of Rule 17g–7.

[293] *See* proposed paragraph (b)(1)(i) of Rule 17g–7.

[294] *See* proposed paragraph (b)(2)(v)(B) of Rule 17g–7. The Commission is not proposing that a rating action that results in an "expected" or "preliminary" credit rating be included in the rating history for a given obligor, security, or money market instrument. As noted above, expected or preliminary ratings most commonly are issued by an NRSRO with respect to a structured finance product at the time the issuer commences the offering and typically are included in pre-sale reports. These ratings may include a range of ratings, or any other indications of a credit rating used prior to the assignment of an initial credit rating for a new issuance. As such, the Commission preliminarily believes they should be excluded from the ratings histories since the issuance of the "initial" credit rating is the first formal expression of the NRSRO's view of the relative creditworthiness of the obligor, security, or money market instrument.

[295] *See* proposed paragraph (b)(2)(v)(C) of Rule 17g–7.

[296] *See* proposed paragraph (b)(2)(v)(D) of Rule 17g–7.

[297] *See* proposed paragraph (b)(2)(v)(E) of Rule 17g–7.

[298] *See* proposed paragraph (b)(2)(v)(F) of Rule 17g–7. Some NRSRO's also may "confirm" an existing credit rating. For the purposes of this proposed disclosure requirement, the Commission intends the term "affirmation of an existing credit rating" to include a "confirmation" of an existing credit rating.

[299] *See* proposed paragraph (b)(2)(v)(G) of Rule 17g–7.

[300] *See* proposed paragraphs (b)(2)(v)(G)(*1*), (*2*) and (*3*) of Rule 17g–7.

[301] *See* proposed paragraph (b)(2)(v)(G)(*1*) of Rule 17g–7.

[302] *See* proposed paragraphs (b)(2)(v)(G)(*2*) of Rule 17g–7.

[303] *See* proposed paragraphs (b)(2)(v)(G)(*3*) of Rule 17g–7.

These sub-classifications would parallel, in many respects, the outcomes identified in paragraphs (4)(B)(iii), (iv), and (v) of the proposed amendments to the instructions for Exhibit 1 to Form NRSRO discussed above in Section II.E.1.a of this release. However, the Commission preliminarily believes that it would not be appropriate to prescribe standard definitions of "default" and "paid-off" for the purposes of making these classifications.[304] The reason is the ratings history disclosure requirement is designed to allow investors and other users of credit ratings to compare how each NRSRO treats a commonly rated obligor, security, or money market instrument. In other words, unlike the production of performance statistics where standard definitions are necessary to promote comparability of aggregate statistics, the historical rating information should indicate on the granular level any differences between the NRSROs with respect to the rating actions they take for a commonly rated obligor, security or money, market instrument, including their differing definitions of default. This would allow investors and other users of credit ratings to review, for example, the timing of when one NRSRO downgraded an obligor to the default category as opposed to another NRSRO or group of NRSROs. Among other things, investors and other users of credit ratings could review the data to identify outliers that are either quick or slow to downgrade obligors, securities, or money market instruments to default. In addition, an NRSRO with a very narrow definition of "default" might continue to maintain a security at a notch in its rating scale above the default category; whereas other NRSROs, using broader definitions, had classified the security as having gone into default. Creating a mechanism to identify these types of variances is a goal of the enhancements to the 100% Rule. Moreover, users of the ratings history information could use the standard definition of *Default* in the proposed enhancements to the instructions for Exhibit 1 as a benchmark to compare when an NRSRO classified obligors, securities, or money markets as having gone into default.

The Commission preliminarily believes a default and the extinguishment of an obligation because it was paid in full are the most frequently occurring reasons why an NRSRO withdraws a credit rating. However, as discussed above, in Section II.E.1.a of this release, there are other reasons an NRSRO might withdraw a credit rating, including that the rated obligor or issuer of the rated security or money market instrument stopped paying for the surveillance of rating or the NRSRO decided not to devote resources to continue to perform surveillance on the rating of an obligor, security, or money market instrument on an unsolicited basis. However, as also discussed above, the withdrawal of credit ratings could be used to make performance statistics appear more favorable. Consequently, as with the Transition/Default Matrices in Exhibit 1, an NRSRO would be required to identify when a credit rating was withdrawn for reasons other than default or the extinguishment of the obligation upon which the credit rating is based. Similar to the Transition/Default Matrices, persons using the ratings history information could analyze how often an NRSRO withdraws a credit rating for "other" reasons in a class or subclass of credit ratings.

Proposed paragraph (b)(2)(vi) of Rule 17g–7 would identify the sixth category of data: Namely, a classification of the class or subclass of credit rating.[305] The classes of credit ratings would be based on the definition of "nationally recognized statistical rating organization" in Section 3(a)(62) of the Exchange Act.[306] Consequently, the first classification would be financial institutions, brokers or dealers.[307] The second classification would be insurance companies.[308] The third classification would be corporate issuers.[309]

The fourth classification would be issuers of structured finance products.[310] If the credit rating falls into this class, the proposed rule would require the NRSRO to identify a sub-classification as well.[311] The sub-classifications would be the same subclasses for structured finance credit ratings the Commission is proposing an applicant and NRSRO use for the purposes of the Transition/Default Matrices to be disclosed in Exhibit 1 to Form NRSRO:[312] RMBS;[313] CMBS;[314] CLOs;[315] CDOs;[316] ABCP;[317] other asset-backed securities;[318] and other structured finance products.[319]

The fifth classification would be issuers of government securities, municipal securities or securities issued by a foreign government.[320] If the credit rating falls into this class, the proposed rule would require the NRSRO to

[304] For the reasons discussed herein, the Commission also preliminarily believes that the NRSRO should use its definition of "default" in taking a rating action that results in a downgrade to the default category, which would need to be classified as a downgrade in the information disclosed with the rating action pursuant to proposed paragraph (b)(2)(v)(D) of Rule 17g–7.

[305] *See* proposed paragraph (b)(2)(vi) of Rule 17g–7.

[306] *See* 15 U.S.C. 78o–7(a)(62). Because some obligors, securities, and money market instruments have characteristics that could cause them to be assigned more than one class of credit rating, the Commission is seeking comment below in Section II.M.4.a of this release on which class would be the most appropriate for certain types of obligors, securities, and money market instruments. Based on the comments received in response to those requests, the Commission may decide to prescribe by rule or identify through guidance how certain types of obligors, securities, and money market instruments should be classified for the purposes proposed in new paragraph (b)(vi) of Rule 17g–7.

[307] *See* 15 U.S.C. 78o–7(a)(62)(B)(i) and proposed paragraph (b)(2)(vi)(A) of Rule 17g–7.

[308] *See* 15 U.S.C. 78o–7(a)(62)(B)(ii) and proposed paragraph (b)(2)(vi)(B) of Rule 17g–7.

[309] *See* 15 U.S.C. 78o–7(a)(62)(B)(iii) and proposed paragraph (b)(2)(vi)(C) of Rule 17g–7.

[310] *See* 15 U.S.C. 78o–7(a)(62)(B)(iv) and proposed paragraph (b)(2)(vi)(D) of Rule 17g–7. Consistent with the existing Instructions to Exhibit 1 to Form NRSRO (and the proposed amendments to those instructions) this class of credit rating would be broader than the class identified in Section 15E(a)(62)(B)(iv) of the Exchange Act.

[311] *See* proposed paragraphs (b)(2)(vi)(D)(*1*)–(*7*) of Rule 17g–7.

[312] *See* discussion in Section II.E.1.a of this release and proposed new paragraphs (1)(D)(i)–(vii) of the instructions for Exhibit 1.

[313] *See* proposed paragraph (b)(2)(vi)(D)(*1*) of Rule 17g–7. As with the proposal for Exhibit 1 to Form NRSRO, the Commission preliminarily intends that "RMBS" for the purposes of this rule means a securitization primarily of residential mortgages.

[314] *See* proposed paragraph (b)(2)(vi)(D)(*2*) of Rule 17g–7. As with the proposal for Exhibit 1 to Form NRSRO, the Commission preliminarily intends that "CMBS" for the purposes of this rule means a securitization primarily of commercial mortgages.

[315] *See* proposed paragraph (b)(2)(vi)(D)(*3*) of Rule 17g–7. As with the proposal for Exhibit 1 to Form NRSRO, the Commission preliminarily intends "CLO" for the purposes of this rule means a securitization primarily of commercial loans.

[316] *See* proposed paragraph (b)(2)(vi)(D)(*4*) of Rule 17g–7. As with the proposal for Exhibit 1 to Form NRSRO, the Commission preliminary intends "CDO" for the purposes of this rule to mean a securitization primarily of other debt instruments such as RMBS, CMBS, CLOs, CDOs, other asset backed securities, and corporate bonds.

[317] *See* proposed paragraph (b)(2)(vi)(D)(*5*) of Rule 17g–7. As with the proposal for Exhibit 1 to Form NRSRO, the Commission preliminarily intends "ABCP" for the purposes of this rule to mean short term notes issued by a structure that securitizes a variety of financial assets (*e.g.,* trade receivables or credit card receivables), which secure the notes.

[318] *See* proposed paragraph (b)(2)(vi)(D)(*6*) of Rule 17g–7. As with the proposal for Exhibit 1 to Form NRSRO, the Commission preliminarily intends that "other asset backed security" for the purposes of this rule to mean a securitization primarily of auto loans, auto leases, floor plan financings, credit card receivables, student loans, consumer loans, equipment loans or equipment leases.

[319] *See* proposed paragraph (b)(2)(vi)(D)(*7*) of Rule 17g–7. As with the proposal for Exhibit 1 to Form NRSRO, the Commission preliminarily intends that "other structured finance product" for the purposes of this rule to mean a structured finance product not identified in the other sub-classifications of structured finance products.

[320] *See* 15 U.S.C. 78o–7(a)(62)(B)(v) and proposed paragraph (b)(2)(vi)(E) of Rule 17g–7.

identify a sub-classification as well.[321] The sub-classifications would be the same for this class as are currently identified in the Instructions for Exhibit 1 to Form NRSRO: (1) Sovereign issuers;[322] (2) United States public finance;[323] or (3) International public finance.[324]

Proposed paragraph (b)(2)(vii) of Rule 17g–7 would identify the seventh category of data: Namely, the credit rating symbol, number, or score in the applicable rating scale of the NRSRO assigned to the obligor, security, or money market instrument as a result of the rating action or, if the credit rating remained unchanged as a result of the action, the credit rating symbol, number, or score in the applicable rating scale of the NRSRO assigned to the obligor, security, or money market instrument as of the date of the rating action.[325] The rating symbol, number, or score is a key component of the information that would need to be disclosed as it reflects the NRSRO's view of the relative creditworthiness of the obligor, security, or money market instrument subject to the rating as of the date the action is taken. The proposal would specify that the NRSRO, in either case, would need to include a credit rating in a default category, if applicable. Otherwise an NRSRO might exclude a default on the theory that it is not a credit rating *per se* (*i.e.,* an opinion of creditworthiness) but rather a statement of fact.

Proposed paragraph (b)(3) of Rule 17g–7 would provide that the information identified in paragraph (b)(2) of the rule (discussed above) must be disclosed in an interactive data file that uses an XBRL format and the List of XBRL Tags for NRSROs as published on the Internet Web site of the Commission.[326] This would be consistent with the current requirement of the 100% Rule.[327] As discussed above, however, the data fields that would need to have an XBRL tag would be expanded.[328]

Proposed paragraph (b)(4) of Rule 17g–7 would specify when a rating action would need to be disclosed by establishing two distinct grace periods: 12 months and 24 months.[329] In particular, a rating action would need to be disclosed: (1) Within 12 months from the date the action is taken, if the credit rating subject to the action is issuer-paid; [330] (2) or within 24 months from the date the action is taken, if the credit rating subject to the action is not issuer-paid.[331] These separate grace periods for issuer-paid and non-issuer-paid credit ratings are consistent with the current requirement of the 100% Rule.[332]

Finally, paragraph (b)(5) of Rule 17g–7 would provide that an NRSRO may cease disclosing a rating history of an obligor, security, or money market instrument no earlier than 20 years after the date a rating action with respect to the obligor, security, or money market instrument is classified as a withdrawal of the credit rating pursuant to paragraph (b)(2)(v)(G) of Rule 17g–7, provided no subsequent credit ratings are assigned to the obligor, security, or money market instrument after the withdrawal classification.[333] This proposed requirement is designed to ensure that information about credit ratings that are withdrawn for any reason would remain a part of the disclosure for a significant period of time. The Commission preliminarily believes this would address concerns that an NRSRO might withdraw a credit rating to remove its history from the disclosure requirement to, for example, make the performance of its credit ratings appear better than, in fact, is the case.

Request for Comment

The Commission generally requests comment on all aspects of proposed new paragraph (b) of Rule 17g–7. The Commission also seeks comment on the following:

1. Should the 10% Rule be retained? For example, could it be enhanced to meet the requirement of Section 15E(q)(A) of the Exchange Act that disclosures be comparable among NRSROs, to allow users of credit ratings to compare the performance of credit ratings across NRSROs? If so, how could the 10% Rule be modified to better meet this requirement? Moreover, even with such modifications, would an enhanced 10% Rule provide information to investors and other users of credit ratings that would be useful to assess the performance of credit ratings across NRSROs?

2. Should the proposed rule require that the disclosure of the ratings history information under the proposed enhancements to the 100% Rule be made freely available in writing, when requested? If so, how should an NRSRO meet such a request? For example, would an NRSRO be required to mail a written copy of information in the XBRL data file to a party requesting the information? If so, would it be appropriate to permit the NRSRO to charge reasonable handling and postage fees? Would such a requirement to provide a written copy of the information in the XBRL data file be feasible? Are there other ways an NRSRO could make this disclosure freely available in writing?

3. If the rule required an NRSRO to provide a written copy of the information in the XBRL data file, when requested, under what circumstances would a party request this information in writing, given that it would be freely available on an easily accessible portion of the NRSRO's corporate Internet Web site? Moreover, why would a party request the information in written form when downloading an electronic file in an XBRL format would make accessing and analyzing the information much easier?

4. Should the rule require that an NRSRO publish quarterly, bi-annual, or annual copies of the rating histories and that these be made available when requested to implement the "in writing" provision in the statute?

5. What practical issues should the Commission consider in implementing the proposed enhancements to the 100% Rule? For example, would the variances in the procedures and methodologies NRSROs use to determine credit ratings raise practical issues in terms of classifying and disclosing the proposed required information about a credit rating action? In addition, would the variances in the meanings and definitions that NRSROs ascribe to the categories of credit ratings in their rating scales raise practical issues in terms of classifying and disclosing the proposed required information about a credit rating action? How could the proposal be modified to address any practical issues identified without undermining the goal of making the data more useful in terms of the

[321] *See* proposed paragraphs (b)(2)(vi)(E)(*1*)–(*3*) of Rule 17g–7.

[322] *See* Instructions for Exhibit 1 to Form NRSRO and proposed paragraph (b)(2)(vi)(E)(*1*) of Rule 17g–7.

[323] *See* Instructions for Exhibit 1 to Form NRSRO and proposed paragraph (b)(2)(vi)(E)(*2*) of Rule 17g–7.

[324] *See* Instructions for Exhibit 1 to Form NRSRO and proposed paragraph (b)(2)(vi)(E)(*3*) of Rule 17g–7.

[325] *See* proposed new paragraph (b)(2)(vii) of Rule 17g–7.

[326] *See* proposed new paragraph (b)(3) of Rule 17g–7.

[327] *See* 17 CFR 240.17g–2(d)(3)(ii).

[328] *See* proposed new paragraph (b)(2)(i)–(vii).

[329] *See* proposed new paragraph (b)(4) of Rule 17g–7.

[330] *See* proposed paragraph (b)(4)(i) of Rule 17g–7.

[331] *See* proposed paragraph (b)(4)(ii) of Rule 17g–7.

[332] *See* 17 CFR 240.17g–2(d)(3)(i)(B) and (C). *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63837–63842 (Dec. 4, 2009) (discussing the 100% Rule and the reasons why the Commission adopted distinct 12 and 24 month grace periods).

[333] *See* proposed paragraph (b)(5) of Rule 17g–7.

amount of information provided, the ability to search and sort the information, and the ability to compare historical rating information across NRSROs?

6. How long would it take an NRSRO to implement the proposed requirements and begin making the proposed disclosures? What steps would an NRSRO need to take to implement the proposed requirements?

7. What practical issues should the Commission consider with respect to the proposed requirement to add histories for all credit ratings outstanding as of June 26, 2007 to the disclosure? How could the proposal be modified to address any practical issues identified without undermining the rule's goal of making the data more useful in terms of the amount of information provided, the ability to search and sort the information, and the ability to compare historical rating information across NRSROs?

8. What practical issues should the Commission consider with respect to the proposed new requirement to disclose the name and CIK number of the issuer of a rated security or money market instrument? How could the proposal be modified to address any practical issues identified without undermining the goal of making the data more useful in terms of the amount of information provided, the ability to search and sort the information, and the ability to compare historical rating information across NRSROs?

9. What practical issues should the Commission consider with respect to the proposed new requirement to disclose the type of rating action? For example, are the proposed classifications a comprehensive list of the types of rating actions taken by NRSROs? If not, identify and describe any other types of rating actions. Would the disclosure of this data be useful to investors and other users of credit ratings? How could the proposal be modified to address any practical issues identified without undermining the goal of making the data more useful in terms of the amount of information provided, the ability to search and sort the information, and the ability to compare historical rating information across NRSROs?

10. With respect to the proposal to disclose the types of rating actions, are the three sub-classifications proposed for the withdrawal classification sufficient? For example, should the rule further refine the "withdrawal for other reasons" sub-classification to require disclosure of certain other reasons that a credit rating might be withdrawn such as the obligor or issuer ceased paying for the credit rating?

11. What practical issues should the Commission consider with respect to the proposed new requirement to disclose the class or subclass of the credit rating? For example, are the descriptions of the subclasses of credit ratings for structured finance products sufficiently clear to provide an NRSRO with guidance as to how such credit ratings should be classified? How could the descriptions be modified to make them clearer and provide better guidance?

12. Are the subclasses of credit ratings for structured finance products the most appropriate way to divide this class of credit ratings? For example, should the "other-ABS" subclass be separated into subclasses based on the assets underlying the ABS (*i.e.,* auto loans, auto leases, floor plan financings, credit card receivables, student loans, consumer loans, equipment loans, or equipment leases)? In addition, are there other classes of structured finance products that should be identified?

13. Commenters are referred to the questions in Section II.M.4.a of this release with respect to Items 6 and 7 of Form NRSRO and how certain types of obligors, securities, and money market instruments should be classified for purposes of providing approximate amounts of credit ratings outstanding in each class of credit rating for which an applicant is seeking registration (Item 6) or an NRSRO is registered (Item 7)? In responding to those questions, commenters should consider how proposed classifications could be applied for the purposes of proposed new paragraph (b)(2)(vi) of Rule 17g–7.

14. Is 20 years the appropriate amount of time to require that the ratings history for a withdrawn credit rating remain part of the disclosure? Should the rule require these histories be retained for a lesser period of time, such as 10 or 15 years or a greater period of time, such as 25 or 30 years? If a different time period would be more appropriate, explain the rationale for such different time period.

15. Are the existing 12 and 24 month grace periods appropriate? Should the Commission consider adopting a single grace period, rather than the existing bifurcated approach?

F. Credit Rating Methodologies

Section 932(a)(8) of the Dodd-Frank Act amends Section 15E of the Exchange Act to add new subsection (r).[334] Section 15E(r) of the Exchange Act provides that the Commission shall prescribe rules, for the protection of investors and in the public interest, with respect to the procedures and methodologies, including qualitative and quantitative data and models, used by NRSROs that require each NRSRO to ensure a number of objectives.[335] The Commission preliminarily believes it would be appropriate to implement Section 15E(r) by proposing rules requiring an NRSRO to establish, maintain, enforce, and document policies and procedures that are reasonably designed to ensure the objectives identified in that section of the statute.[336] This approach would allow an NRSRO to establish policies and procedures that can be integrated with its procedures and methodologies for determining credit ratings, which vary across NRSROs. At the same time, the proposed rule would set forth specific objectives that the policies and procedures would need to be reasonably designed to achieve both in design and operation. The Commission preliminarily believes this approach would be appropriate, particularly given that the objectives set forth in Section 15E(r) of the Exchange Act relate to the procedures and methodologies an NRSRO uses to determine credit ratings.[337]

For these reasons, the Commission is proposing to implement Section 15E(r) of the Exchange Act, in large part, through paragraph (a) of new Rule 17g–8.[338] The Commission also is proposing an amendment to Rule 17g–2 to apply the record retention and production requirements of that rule to the policies and procedures.[339]

1. Proposed Paragraph (a) of New Rule 17g–8

As noted above, proposed paragraph (a) of new Rule 17g–8 would require an NRSRO to have policies and procedures

[334] *See* Public Law 111–203 § 932(a)(8) and 15 U.S.C. 78o–7(r).

[335] *See* 15 U.S.C. 78o–7(r)(1)–(3).

[336] *See id.*

[337] *See* Section 15E(r) of the Exchange Act (15 U.S.C. 78o–7(r)); *see also* Section 15E(c)(2) of the Exchange Act (providing, in pertinent part, that the Commission may not regulate the substance of credit ratings or the procedures and methodologies by which any NRSRO determines credit ratings). 15 U.S.C. 78o–7(c)(2).

[338] *See* proposed paragraph (a) of new Rule 17g–8. As discussed above in Section II.C of this release, the Commission is proposing to implement several provisions of the Dodd-Frank Act through rules that would prescribe policies and procedures an NRSRO would need to establish, maintain, enforce, and document. The Commission is proposing that all such rule requirements be consolidated in new Rule 17g–8. *See* proposed paragraphs (a), (b), and (c) of new Rule 17g–8 and Section II.C.1 of this release discussing proposed paragraph (c) and Section II.J.1 discussing proposed paragraph (b).

[339] *See* proposed new paragraph (b)(13) of Rule 17g–2.

that are reasonably designed to achieve objectives identified in Section 15E(r) of the Exchange Act.[340] In particular, the prefatory text would require an NRSRO to establish, maintain, enforce, and document policies and procedures that are reasonably designed to ensure the objectives identified in paragraphs (a)(1), (2), (3), (4), and (5).

Proposed paragraph (a)(1) of new Rule 17g–8 would implement Section 15E(r)(1)(A) of the Exchange Act.[341] This section provides that the Commission's rules shall require an NRSRO to ensure that credit ratings are determined using procedures and methodologies, including qualitative and quantitative data and models, that are approved by the board of the NRSRO, or a body performing a function similar to that of a board.[342] The Commission preliminarily believes that the mandate set forth in the statute is explicit and, consequently, proposes rule text that would mirror the statutory text.[343] Therefore, proposed paragraph (a)(1) of new Rule 17g–8 would require an NRSRO to have policies and procedures that are reasonably designed to ensure that the procedures and methodologies, including qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are approved by its board of directors or another body performing a function similar to that of a board of directors.[344] In this regard, the Commission notes that Section 15E(t)(3)(A) of the Exchange Act contains a self-executing provision that the board of the NRSRO shall oversee the "establishment, maintenance, and enforcement of the policies and procedures for determining credit ratings."[345] Consequently, the Commission preliminarily believes that the policies and procedures proposed to be required pursuant to paragraph (a)(1) of Rule 17g–8 would need to be designed to assist the NRSRO's board in carrying out this responsibility. In addition, Section 15E(t)(5) of the Exchange Act provides that the Commission may permit an NRSRO to delegate responsibilities required in Section 15E(t) to a committee if the Commission finds that compliance with the provisions of that section present an unreasonable burden on a small NRSRO.[346] Consequently, the Commission preliminarily believes that the policies and procedures proposed to be required pursuant to paragraph (a)(1) of Rule 1717g–8 would need to be designed to assist the NRSRO's committee in carrying out the responsibility to oversee the "establishment, maintenance, and enforcement of the policies and procedures for determining credit ratings mandated by Section 15E(t)(3)(A) of the Exchange Act" if the committee (rather than the board) carries out this responsibility.[347]

Proposed paragraph (a)(2) of new Rule 17g–8 would implement Section 15E(r)(1)(B) of the Exchange Act.[348] This section provides that the Commission's rules shall require an NRSRO to ensure that credit ratings are determined using procedures and methodologies, including qualitative and quantitative data and models, that are in accordance with the policies and procedures of the NRSRO for the development and modification of credit rating procedures and methodologies.[349] The Commission preliminarily believes that the mandate set forth in the statute is explicit and, consequently, proposes rule text that would mirror the statutory text.[350] Therefore, proposed paragraph (a)(2) of new Rule 17g–8 would require an NRSRO to have policies and procedures that are reasonably designed to ensure that the procedures and methodologies, including qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are developed and modified in accordance with the policies and procedures of the NRSRO.[351]

Proposed paragraph (a)(3)(i) of new Rule 17g–8 would implement Section 15E(r)(2)(A) of the Exchange Act.[352] This section provides that the Commission's rules shall require an NRSRO to ensure that when material changes are made to credit rating procedures and methodologies (including changes to qualitative and quantitative data and models), the changes are applied consistently to all credit ratings to which the changed procedures and methodologies apply.[353] The Commission preliminarily believes that the mandate set forth in the statute is explicit and, consequently, proposes rule text that would mirror the statutory text.[354] Therefore, proposed paragraph (a)(3)(i) of new Rule 17g–8 would require an NRSRO to have policies and procedures that are reasonably designed to ensure that material changes to the procedures and methodologies, including changes to qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are applied consistently to all credit ratings to which the changed procedures or methodologies apply.[355]

Proposed paragraph (a)(3)(ii) of new Rule 17g–8 would implement Section 15E(r)(2)(B) of the Exchange Act.[356] This section provides that the Commission's rules shall require an NRSRO to ensure that when material changes are made to credit rating procedures and methodologies (including changes to qualitative and quantitative data and models), to the extent that changes are made to credit rating surveillance procedures and methodologies, the changes are applied to then-current credit ratings by the NRSRO within a reasonable time period determined by the Commission, by rule.[357] The Commission proposes that paragraph (a)(3)(ii) of new Rule 17g–8 require the NRSRO to have policies and procedures that are reasonably designed to ensure that material changes to the procedures and methodologies, including changes to qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are, to the extent that the changes are to surveillance or monitoring procedures and methodologies, applied to then-current credit ratings within a reasonable period of time taking into consideration the number of ratings impacted, the complexity of the procedures and methodologies used to determine the credit ratings, and the type of obligor, security, or money market instrument being rated.[358] This proposed rule would mirror the text of Section 15E(r)(2)(B) of the Exchange Act but add additional language to implement the rulemaking provision that the changes are applied to then-current credit ratings by the NRSRO within a "reasonable time

[340] *See* prefatory text of proposed paragraph (a) of new Rule 17g–8.

[341] *See* proposed paragraph (a)(1) of new Rule 1717g–8 and 15 U.S.C. 78o–7(r)(1)(A).

[342] *See* 15 U.S.C. 78o–7(r)(1)(A).

[343] *See* proposed paragraph (a)(1) of new Rule 17g–8.

[344] *Compare* proposed paragraph (a)(1) of new Rule 17g–8, *with* 15 U.S.C. 78og–7(r)(1)(A).

[345] *See* 15 U.S.C. 78og–7(t)(3)(A).

[346] *See* 15 U.S.C. 78og–7(t)(5).

[347] *See* 15 U.S.C. 78og–7(t)(3)(A).

[348] *See* proposed paragraph (a)(2) of new Rule 17g–8 and 15 U.S.C. 78og–7(r)(1)(B).

[349] *See* 15 U.S.C. 78o–7(r)(1)(B).

[350] *See* proposed paragraph (a)(2) of new Rule 17g–8.

[351] *Compare* proposed paragraph (a)(2) of new Rule 17g–8, *with* 15 U.S.C. 78o–7(r)(1)(B).

[352] *See* proposed paragraph (a)(3)(i) of new Rule 17g–8 and 15 U.S.C. 78o–7(r)(2)(A).

[353] *See* 15 U.S.C. 78o–7(r)(2)(A).

[354] *See* proposed paragraph (a)(3)(i) of new Rule 17g–8.

[355] *Compare* proposed paragraph (a)(3)(i) of new Rule 17g–8, *with* 15 U.S.C. 78o–7(r)(2)(A).

[356] *See* proposed paragraph (a)(3)(i) of new Rule 17g–8 and 15 U.S.C. 78o–7(r)(2)(B).

[357] 15 U.S.C. 78o–7(r)(2)(B).

[358] *See* proposed paragraph (a)(3)(ii) of new Rule 17g–8.

period determined by the Commission, by rule."[359]

In determining what time period would be reasonable, the Commission preliminarily believes that the NRSRO should be required to have policies and procedures designed to ensure that the changes are applied to existing credit ratings within a reasonable time period taking into consideration certain relevant factors; namely, the number of ratings impacted, the complexity of the procedures and methodologies used to determine the credit ratings, and the type of obligor, security, or money market instrument being rated. The Commission preliminarily believes that a prescribed time frame (*e.g.,* 1, 2, 3, 4 or more months) would not be appropriate because the reasonableness of the timeframe in which existing credit ratings are modified would depend on the facts and circumstances. If the rule mandated a time-frame that is too short, under the circumstances, the NRSRO would need to rush to meet the deadline. This could negatively impact the quality of the credit ratings determined using the changed surveillance procedures and methodologies. Moreover, prescribing a timeframe that is too long could create an inadvertent "safe harbor" allowing the NRSRO to act more slowly to apply the changed surveillance procedures and methodologies to the impacted obligors, securities, and money market instruments. Consequently, the Commission preliminarily believes that the best approach is to require the NRSRO to apply the changed surveillance procedures and methodologies to the impacted obligors, securities, and money market instruments within a reasonable amount of time given the circumstances.

Proposed paragraph (a)(4)(i) of new Rule 17g–8 would implement Sections 15E(r)(2)(C), 15E(r)(3)(B), and 15E(r)(3)(D) of the Exchange Act as they all relate to disclosing information about material changes to procedures and methodologies (including changes to qualitative and quantitative data and models) an NRSRO uses to determine credit ratings.[360] Specifically, Section 15E(r)(2)(C) provides that the Commission's rules shall require an NRSRO to ensure that when material changes are made to credit rating procedures and methodologies (including changes to qualitative and quantitative data and models), the NRSRO publicly discloses the reason for the change.[361] Section 15E(r)(3)(B) provides that the Commission's rules shall require an NRSRO to notify users of credit ratings when a material change is made to a procedure or methodology, including to a qualitative model or quantitative input.[362] Finally, Section 15E(r)(3)(D) provides that that the Commission's rules shall require an NRSRO to notify users of credit ratings when a material change is made to a procedure or methodology, including to a qualitative model or quantitative input, of the likelihood the change will result in a change in current credit ratings.[363]

Consequently, Section 15E(r)(3)(B) requires the NRSRO to notify users of a change, Section 15E(r)(2)(C) requires the NRSRO to publish the reason for a change, and Section 15E(r)(3)(D) requires the NRSRO to disclose the potential impact of the change on existing credit ratings.[364] The Commission preliminarily believes that the mandates set forth in these sections are explicit and, consequently, proposes rule text that would mirror the statutory text.[365] Moreover, because the objective of the provision is to provide disclosure to investors and users of credit ratings, the Commission preliminarily believes proposed paragraph (a)(4)(i) of Rule 17g–8 should specify that these disclosures be published on an easily accessible portion of the NRSRO's corporate Internet Web site.[366] This would be consistent with the Commission's proposed Internet disclosure requirements for Form NRSRO under paragraph (i) of Rule 17g–1 and the ratings history information under proposed new paragraph (b)(1) of Rule 17g–1. For these reasons, proposed paragraph (a)(4)(i) of new Rule 17g–8 would require the NRSRO to have policies and procedures that are reasonably designed to ensure that the NRSRO promptly publishes on an easily accessible portion of its corporate Internet Web site material changes to the procedures and methodologies, including to qualitative models or quantitative inputs, the NRSRO uses to determine credit ratings, the reason for the changes, and the likelihood the changes will result in changes to any current ratings.[367]

Proposed paragraph (a)(4)(ii) of new Rule 17g–8 would implement Sections 15E(r)(3)(C) of the Exchange Act.[368] This section provides that the Commission's rules shall require an NRSRO to notify users of credit ratings when a significant error is identified in a procedure or methodology, including a qualitative or quantitative model, that may result in credit rating actions.[369] The Commission preliminarily believes that the mandate set forth in the statute is explicit and, consequently, proposes rule text that would mirror the statutory text.[370] Moreover, as with the proposed paragraph (a)(4)(i) disclosures, the Commission preliminarily believes proposed paragraph (a)(4)(ii) of Rule 17g–8 should specify that these disclosures be published on the NRSRO's corporate Internet Web site. Therefore, proposed paragraph (a)(4)(ii) of new Rule 17g–8 would require the NRSRO to have policies and procedures that are reasonably designed to ensure the NRSRO promptly publishes on an easily accessible portion of its corporate Internet Web site significant errors identified in a procedure or methodology, including a qualitative or quantitative model, the NRSRO uses to determine credit ratings that may result in a change in current credit ratings.[371]

Proposed paragraph (a)(5) of new Rule 17g–8 would implement Section15E(r)(3)(A) of the Exchange Act.[372] This section provides that the Commission's rules shall require an NRSRO to notify users of credit ratings of the version of a procedure or methodology, including the qualitative methodology or quantitative inputs, used with respect to a particular credit rating.[373] The Commission preliminarily believes that the mandate set forth in the statute is explicit and, consequently, proposes rule text that would mirror the statutory text.[374] Therefore, proposed

[359] *Compare* proposed paragraph (a)(3)(ii) of new Rule 17g–8, *with* 15 U.S.C. 78o–7(r)(2)(B).

[360] *See* proposed paragraph (a)(4)(i) of new Rule 17g–8, 15 U.S.C. 78o–7(r)(2)(B), 15 U.S.C. 78o–7(r)(3)(B), and 15 U.S.C. 78o–7(r)(3)(D).

[361] *See* 15 U.S.C. 78o–7(r)(2)(C).

[362] *See* 15 U.S.C. 78o–7(r)(3)(B).

[363] *See* 15 U.S.C. 78o–7(r)(3)(D).

[364] 15 U.S.C. 78o–7(r)(3)(B), 15 U.S.C. 78o–7(r)(2)(C), and 15 U.S. C. 78o–7(r)(3)(D).

[365] *Compare* proposed paragraph (a)(4)(ii) of new Rule 17g–8, *with* 15 U.S.C. 78o–7(r)(3)(B), 15 U.S.C. 78o–7(r)(2)(C), and 15 U.S. C. 78o–7(r)(3)(D).

[366] As discussed above in Section II.E.1.b of this release, the Commission preliminarily believes there is no alternative means of disclosure that makes information as "readily accessible" as an Internet Web site. In addition, as discussed in that section of this release, the Commission preliminarily believes that information would be disclosed on an "easily accessible" portion of a corporate Internet Web site if it could be accessed through a clearly and prominently labeled hyperlink on the homepage of the NRSRO's corporate Internet Web site.

[367] *See* proposed paragraph (a)(4)(i) of new Rule 17g–8.

[368] *See* proposed paragraph (a)(4)(ii) of new Rule 17g–8 and 15 U.S.C. 78o–7(r)(3)(C).

[369] *See* 15 U.S.C. 78o–7(r)(3)(C).

[370] *Compare* proposed paragraph (a)(4)(ii) of new Rule 17g–8, *with* 15 U.S.C. 78o–7(r)(3)(C).

[371] *See* proposed paragraph (a)(4)(ii) of new Rule 17g–8.

[372] *See* proposed paragraph (a)(5) of new Rule 17g–8 and 15 U.S. C. 78o–7(r)(3)(A).

[373] 15 U.S.C. 78o–7(r)(3)(A).

[374] *Compare* proposed paragraph (a)(5) of new Rule 17g–8, *with* 15 U.S.C. 78o–7(r)(3)(A).

paragraph (a)(5) of new Rule 17g–8 would require the NRSRO to have policies and procedures that are reasonably designed to ensure that it discloses the version of a credit rating procedure or methodology, including the qualitative methodology or quantitative inputs, used with respect to a particular credit rating.[375]

Request for Comment

The Commission generally requests comment on all aspects of proposed paragraph (a) of new Rule 17g–8. The Commission also seeks comment on the following:

1. Are there alternatives to implementing Section 15E(r) of the Exchange Act (*i.e.,* other than requiring policies and procedures reasonably designed to achieve the objectives identified in the statute) that the Commission should consider? If so, please identify those alternatives and explain how they would better achieve the goals of Section 15E(r)?

2. Would proposed paragraph (a)(1) of new Rule 17g–8 requiring an NRSRO to have policies and procedures that are reasonably designed to achieve the objective that the procedures and methodologies, including qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are approved by its board of directors or another body performing a function similar to that of a board of directors appropriately meet the mandate identified in Section 15E(r)(1)(A) of the Exchange Act? If not, how could the proposal be modified to provide more guidance to NRSROs about how to design their policies and procedures?

3. Would proposed paragraph (a)(2) of new Rule 17g–8 requiring an NRSRO to have policies and procedures that are reasonably designed to ensure that the procedures and methodologies, including qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are developed and modified in accordance with the policies and procedures of the NRSRO appropriately meet the mandate identified in Section 15E(r)(1)(B) of the Exchange Act? If not, how should the proposal be modified to provide more guidance to NRSROs about how to design their policies and procedures? In addition, how would this proposed requirement relate to the requirement in Section 15E(c)(3)(A) of the Exchange Act requiring an NRSRO to establish, maintain, enforce, and document an effective internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings. For example, would procedures established under proposed paragraph (a)(2) of Rule 17g–8 be part of the internal control structure or would they be designed to achieve different goals?

4. Would proposed paragraph (a)(3)(i) of new Rule 17g–8 requiring an NRSRO to have policies and procedures that are reasonably designed to ensure that material changes to the procedures and methodologies, including changes to qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are applied consistently to all credit ratings to which the changed procedures or methodologies apply appropriately meet the mandate identified in Section 15E(r)(2)(A) of the Exchange Act? If not, how should the proposal be modified to provide more guidance to NRSROs about how to design their policies and procedures?

5. Would proposed paragraph (a)(3)(ii) of new Rule 17g–8 requiring an NRSRO to have policies and procedures that are reasonably designed to ensure that material changes to the procedures and methodologies, including changes to qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are, to the extent that the changes are to surveillance or monitoring procedures and methodologies, applied to then-current credit ratings within a reasonable period of time taking into consideration the number of ratings impacted, the complexity of the procedures and methodologies used to determine the credit ratings, and the type of obligor, security, or money market instrument being rated appropriately meet the mandate identified in Section 15E(r)(2)(B) of the Exchange Act? If not, how should the proposal be modified to provide more guidance to NRSROs about how to design their policies and procedures?

6. With respect to proposed paragraph (a)(3)(ii) of new Rule 17g–8, should the Commission consider prescribing specific time frames such as 1, 2, 3, 4, 5, 6 or more months to apply the new procedures and methodologies to existing credit ratings? Should the time frame depend on the methodology used to determine credit ratings (*i.e.,* quantitative as opposed to qualitative)? As another alternative, should the Commission prescribe a timeframe based on the number of outstanding credit ratings? For example, should the Commission consider requiring that the new procedures and methodologies be applied to existing credit ratings in tranches such as 10 credit ratings per week or 60 credit ratings per month or some other ratio of the period of time to the number of credit ratings? Should such a ratio depend on the methodology used to determine credit ratings (*i.e.,* quantitative as opposed to qualitative)?

7. Would proposed paragraph (a)(4)(i) of new Rule 17g–8 requiring an NRSRO to have policies and procedures that are reasonably designed to ensure that the NRSRO promptly publishes on an easily accessible portion of its corporate Internet Web site material changes to the procedures and methodologies, including to qualitative models or quantitative inputs, the NRSRO uses to determine credit ratings, the reason for the changes, and the likelihood the changes will result in changes to any current ratings appropriately meet the mandates identified in Sections 15E(r)(3)(B), 15E(r)(2)(C) and 15E(r)(3)(D) of the Exchange Act? If not, how should the proposal be modified to provide more guidance to NRSROs about how to design their policies and procedures?

8. Would proposed paragraph (a)(4)(ii) of new Rule 17g–8 requiring an NRSRO to have policies and procedures that are reasonably designed to ensure the NRSRO promptly publishes on an easily accessible portion of its corporate Internet Web site significant errors identified in a procedure or methodology, including a qualitative or quantitative model, the NRSRO uses to determine credit ratings that may result in a change in current credit ratings appropriately meet the mandates identified in Section 15E(r)(3)(C) of the Exchange Act? If not, how should the proposal be modified to provide more guidance to NRSROs about how to design their policies and procedures? For example, should the Commission define "significant error"? If so, how should the term be defined? Should the definition establish a materiality threshold? If so, how should such a threshold be prescribed? Similarly, should the Commission interpret the term "may result in a change in current credit ratings" to, for example, clarify the level of likelihood necessary to trigger the reporting requirement? For example, should there be a reasonable likelihood that the error may result in a change in current credit ratings?

9. Would proposed paragraph (a)(5) of new Rule 17g–8 requiring an NRSRO to

[375] *See* proposed paragraph (a)(5) of new Rule 17g–8. In addition, because this would be a rating-by-rating disclosure, the Commission is proposing, as discussed in Section II.G.3 of this release, that disclosure of the version of a credit rating procedure or methodology be part of the rule implementing Section 15E(s) of the Exchange Act, which specifies, among other things, that the Commission adopt rules requiring an NRSRO to generate a form to be included with the publication of a credit rating. *See* 15 U.S.C. 78o–7(s) and proposed new paragraph (a)(1)(ii)(B) of Rule 17g–7.

have policies and procedures that are reasonably designed to ensure that it discloses the version of a credit rating procedure or methodology, including the qualitative methodology or quantitative inputs, used with respect to a particular credit rating appropriately meet the mandates identified in Sections 15E(r)(3)(A) of the Exchange Act? If not, how should the proposal be modified to provide more guidance to NRSROs about how to design their policies and procedures?

2. Proposed Amendment to Rule 17g–2

For the reasons discussed in Section II.A.2 of this release, the Commission preliminarily believes that the policies and procedures that would be required pursuant to proposed paragraph (a) of new Rule 17g–8 should be subject to the record retention and production requirements of Rule 17g–2.[376] Consequently, the Commission proposes adding new paragraph (b)(13) to Rule 17g–2 to identify the policies and procedures an NRSRO is required to establish, maintain, enforce, and document pursuant to proposed paragraph (a) of new Rule 17g–8 as a record that must be retained.[377]

Request for Comment

The Commission generally requests comment on all aspects of proposed new paragraph (a)(9) of Rule 17g–2.

G. Form and Certifications To Accompany Credit Ratings

Section 932(a)(8) of the Dodd-Frank Act amended Section 15E of the Exchange Act to add new paragraph (s).[378] Sections 15E(s)(1) through (4), among other things, set forth provisions specifying Commission rulemaking with respect to disclosures an NRSRO must make with the publication of a credit rating.[379] The Commission proposes to implement these provisions by adding new paragraph (a) to Rule 17g–7.[380] As discussed in detail below, the prefatory text of proposed new paragraph (a) would require an NRSRO to publish two items when taking a rating action: (1) A form containing information about the credit rating resulting from or subject to the rating action;[381] and (2) any certification of a provider of third-party due diligence services received by the NRSRO that relates to the credit rating.[382] Proposed paragraph (a)(1) of Rule 17g–7 would contain three primary components: paragraph (a)(1)(i) prescribing the format of the form;[383] paragraph (a)(1)(ii) prescribing the content of the form;[384] and paragraph (a)(1)(iii) prescribing an attestation requirement for the form.[385] Proposed paragraph (a)(2) of Rule 17g–7 would identify the certification from a provider of third-party due diligence services as an item to be published with the rating action.[386]

1. Paragraph (a)—Prefatory Text

Section 15E(s)(1) of the Exchange Act provides that the Commission shall require, by rule, an NRSRO to prescribe a form to accompany the publication of each credit rating that discloses: (1) Information relating to the assumptions underlying the credit rating procedures and methodologies; the data that was relied on to determine the credit rating; and if applicable, how the NRSRO used servicer or remittance reports, and with what frequency, to conduct surveillance of the credit rating; and (2) information that can be used by investors and other users of credit ratings to better understand credit ratings in each class of credit rating issued by the NRSRO.[387] In addition, Section 15E(s)(2)(C) provides that the form shall be made readily available to users of credit ratings, in electronic or paper form, as the Commission may, by rule, determine.[388] Finally, Section 15E(s)(4)(D) of the Exchange Act provides that the Commission shall adopt rules requiring an NRSRO at the time it produces a credit rating, to disclose any certifications from providers of third-party due diligence services to the public in a manner that allows the public to determine the adequacy and level of due diligence services provided by the third-party.[389] The Commission proposes to implement Sections 15E(s)(1), 15E(s)(2)(C), and 15E(s)(4)(D) of the Exchange Act, in large part, through the prefatory text of proposed paragraph (a) of Rule 17g–7.[390]

The first sentence of the proposed prefatory text would provide that an NRSRO must publish the items described in paragraphs (a)(1) and (a)(2) of the proposed rule, as applicable, when taking a rating action with respect to credit rating assigned to an obligor, security, or money market instrument in a class of credit ratings for which the NRSRO is registered.[391] Proposed paragraph (a)(1) would identify the form and proposed paragraph (a)(2) would identify the certification from a provider of third-party due diligence services.[392] The Commission preliminarily intends that the requirement to publish the form and, when applicable, the certification would be triggered each time an NRSRO takes a rating action with respect to an obligor, security, or money market instrument.[393] Consequently, the second sentence of the prefatory text of paragraph (a) would define the term "rating action" to mean any of the following: the publication of an expected or preliminary credit rating assigned to an obligor, security, or

[376] 17 CFR 240.17g–2.

[377] *See* proposed new paragraph (b)(13) to Rule 17g–2; *see also* Section 17(a)(1) of the Exchange Act, which requires an NRSRO to make and keep such records, and make and disseminate such reports, as the Commission prescribes by rule as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the Exchange Act. 15 U.S.C. 78q(a)(1).

[378] *See* 15 U.S.C. 78o–7(s).

[379] *See* Public Law 111–203 § 932(a)(8) and 15 U.S.C. 78o–7(s)(1)–(4). Section 15E(s)(4) of the Exchange Act also establishes requirements for issuers and underwriters of asset-backed securities, NRSROs, and providers of third-party due diligence services with respect to third-party due diligence services relating to asset-backed securities. *See* 15 U.S.C. 78o–7(s)(4)(A)–(D). The Commission's proposals to implement additional provisions in Section 15E(s)(4) are discussed below in Section II.H of this release.

[380] *See* proposed new paragraph (a) of Rule 17g–7.

[381] *See* proposed new paragraph (a)(1) of Rule 17g–7. As discussed below, this paragraph would implement, in large part, rulemaking specified in Sections 15E(s)(1), (2), and (3) of the Exchange Act. *See* 15 U.S.C. 78o–7(s)(1), (2), and (3).

[382] *See* proposed new paragraph (a)(2) of Rule 17g–7. As discussed below, this paragraph would implement, in part, rulemaking specified in Section 15E(s)(4) of the Exchange Act. *See* 15 U.S.C. 78o–7(s)(4).

[383] *See* proposed new paragraph (a)(1)(i) of Rule 17g–7. As discussed below, this paragraph would implement, in large part, rulemaking specified in Section 15E(s)(2) of the Exchange Act. *See* 15 U.S.C. 78o–7(s)(2).

[384] See proposed new paragraph (a)(1)(ii) of Rule 17g–7. As discussed below, this paragraph would implement, in large part, rulemaking specified in Section 15E(s)(3) of the Exchange Act. *See* 15 U.S.C. 78o–7(s)(3).

[385] *See* proposed new paragraph (a)(1)(iii) of Rule 17g–7. As discussed below, this paragraph would implement, in large part, rulemaking specified in Section 15E(q)(2)(F) of the Exchange Act. *See* 15 U.S.C. 78o–7(q)(2)(F).

[386] *See* proposed paragraph (a)(2) of Rule 17g–7.

[387] *See* 15 U.S.C. 78o–7(s)(1)(A) and (B).

[388] *See* 15 U.S.C. 78o–7(s)(2)(C).

[389] *See* 15 U.S.C. 78o–7(s)(4)(D).

[390] *See* proposed new paragraph (a) of Rule 17g–7. As discussed below, the Commission proposes to implement Section 15E(s)(1)(A)(iii) of the Exchange Act—which relates to the use of servicer or remittance reports—in proposed paragraph (a)(1)(i)(G) of Rule 17g–7 because it specifies a particular item of information that would need to be disclosed in the form. *See* 15 U.S.C. 78o–7(a)(1)(i)(G).

[391] *See* proposed new paragraph (a) of Rule 17g–7.

[392] *See* proposed new paragraphs (a)(1) and (a)(2) of Rule 17g–7.

[393] In other words, the form and any certifications would need to be included when the NRSRO publishes an initial credit rating, publishes an upgrade of an existing credit rating, publishes a downgrade of an existing credit rating (including to a default category), publishes a credit rating as being on credit watch or review, publishes an affirmation of an existing credit rating, or withdraws a credit rating.

money market instrument before the publication of an initial credit rating; an initial credit rating; an upgrade or downgrade of an existing credit rating (including a downgrade to, or assignment of, default); a placement of an existing credit rating on credit watch or review; an affirmation of an existing credit rating; and a withdrawal of an existing credit rating. The inclusion of expected or preliminary credit ratings in the list of "rating actions" would incorporate the requirements in the note to current Rule 17g–7.[394] As the Commission explained when adopting Rule 17g–7, the definition of "credit rating" in the note is designed to address pre-sale reports, which are typically issued by an NRSRO with respect to an asset-backed security at the time the issuer commences the offering and typically include an expected or preliminary rating and a summary of the important features of a transaction.[395] Consequently, disclosure at the time of issuance of a pre-sale report is particularly important to investors, since such reports provide them with important information prior to the point at which they make an investment decision.[396] The Commission preliminarily believes that the importance of providing investors with timely information to enable them to make informed investment decisions applies equally to the broader range of disclosures mandated by Section 15E(s) of the Exchange Act.[397] Accordingly, the Commission is proposing that the requirement to publish the form and any certifications be triggered upon the issuance of an expected or preliminary credit rating.[398] Furthermore, as the Commission stated when adopting Rule 17g–7, the term "preliminary credit rating" includes any credit rating, any range of ratings, or any other indications of a credit rating published prior to the assignment of an initial credit rating for a new issuance.[399]

The third sentence of the proposed prefatory text would provide that the items described in the form and any applicable certifications must be published in the same medium and made available to the same persons who can receive or access the credit rating that is the result of the rating action or the subject of rating action.[400] In other words, if the NRSRO publishes its credit ratings via a press release disseminated through its corporate Internet Web site and/or through other electronic information providers, the form and any applicable certifications would need to be disseminated through the same venues. The Commission preliminarily believes one way to accomplish this disclosure would be to publish the credit rating and information in the press release on the form along with the required contents of the form (discussed below) and, if applicable, to attach any relevant certifications to the form.[401] In addition, the form and any certifications would need to be disseminated to the same persons who can receive or access the credit rating that is the result of the rating action or the subject of the rating action. Consequently, if the NRSRO publishes credit ratings for free on its corporate Internet Web site, it would need to make the form and any certifications similarly available. Alternatively, if the NRSRO operates under the subscriber-pay business model, it would need to disseminate the form and any certifications to the subscribers only.

Request for Comment

The Commission generally requests comment on all aspects of proposed prefatory text to paragraph (a) of Rule 17g–7. The Commission also seeks comment on the following:

1. What practical issues should the Commission consider in implementing the proposal that an NRSRO publish the form and the certifications every time the NRSRO takes a rating action? For example, should the certifications only be required to be included with the publication of an expected, preliminary, or initial credit rating or do they remain relevant for the term of the rated security or money market instrument and, therefore, should they continue to be published with subsequent rating actions? How could the proposal be modified to address any practical issues identified without undermining the goal of making this information available to users of the NRSRO's credit ratings?

2. What practical issues should the Commission consider in implementing the proposal that an NRSRO publish the form and the certifications in the same medium and make it available to the same persons who can receive or access the credit rating resulting from or subject to the rating action? How could the proposal be modified to address any practical issues identified without undermining the goal of making this information available to users of the NRSRO's credit ratings?

3. What practical issues should the Commission consider in implementing the proposal to apply provisions of the current note to Rule 17g–7—that the term "rating action" includes the publication of any expected or preliminary credit rating by the NRSRO—to all of the information required under Rule 17g–7 as it would be amended under these proposals? How could the proposal be modified to address any such practical issues without undermining the goal of the disclosure requirements currently contained in Rule 17g–7, that is, to make available to investors, if a credit rating is issued with respect to an asset-backed security, a description of: (1) The representations, warranties, and enforcement mechanisms available to investors; and (2) how they differ from the representations, warranties, and enforcement mechanisms in issuances of similar securities?

4. The Commission has proposed to require issuers of asset-backed securities using a registration statement on proposed Form SF–3 to file a preliminary prospectus, under proposed Rule 424(h), containing transaction-specific information at least 5 business days in advance of the first sale of securities in the offering in order to allow investors additional time to analyze the specific structure, assets, and contractual rights regarding each transaction.[402] Should the Commission

[394] *See* Note to 17 CFR 240.17g–7, which provides that for the purposes of the rule's current requirements, a "credit rating" includes any expected or preliminary credit rating issued by an NRSRO.

[395] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4503–4505 (Jan. 26, 2011).

[396] *Id.*

[397] 15 U.S.C. 78o–7(s).

[398] *See* proposed new paragraph (a) of Rule 17g–7.

[399] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4503–4505 (Jan. 26, 2011).

[400] *See* proposed new paragraph (a) of Rule 17g–7. A credit rating would be the "result" of a rating action in the case where the rating action is either the publication of an expected or preliminary credit rating assigned to an obligor, security, or money market instrument before the publication of an initial credit rating; an initial credit rating; or an upgrade or downgrade of an existing credit rating (including a downgrade to, or assignment of, default). A credit rating would be the "subject" of a rating action in the case where the rating action is either a placement of an existing credit rating on credit watch or review; an affirmation of an existing credit rating; or a withdrawal of an existing credit rating.

[401] As discussed below, the Commission is proposing that the required contents of the form include the credit rating. Consequently, if adopted, an NRSRO would be required to include the credit rating on the form regardless of whether the NRSRO also publishes the credit rating on a separate record. If the NRSRO publishes the credit rating on a separate record, the NRSRO would be required to publish the form (which would also contain the credit rating) with the separate record under proposed new paragraph (a) of Rule 17g–7.

[402] *See Asset Backed Securities,* Securities Act Release No. 9117 (Apr. 7, 2010), 75 FR 23328 (May 3, 2010).

explicitly require that the disclosures required by Rule 17g–7 be provided no later than the time of the proposed Rule 424(h) preliminary prospectus?

5. If the NRSRO publishes its credit ratings via a press release disseminated through its corporate Internet Web site and/or through other electronic information providers, would it be appropriate to permit the NRSRO to accomplish the required disclosure by publishing the credit rating and information in the press release on the form along with the required contents of the form (as discussed below) and, if applicable, attaching any relevant certifications to the form? What other methods could be used to make the required disclosures?

2. Paragraph (a)(1)(i)—Format of the Form

Proposed new paragraph (a)(1) of Rule 17g–7 would identify a form generated by the NRSRO that meets the requirements of proposed new paragraphs (a)(1)(i), (a)(1)(ii), and (a)(1)(iii) of Rule 17g–7 as the first item that must be included with a credit rating.[403] In this regard, Section 15E(s)(2) of the Exchange Act provides that the form developed by the NRSRO shall: (1) Be easy to use and helpful for users of credit ratings to understand the information contained in the report;[404] (2) require the NRSRO to provide the required quantitative content specified in Section 15E(s)(3)(B) in a manner that is directly comparable across types of securities;[405] and (3) be made readily available to users of credit ratings, in electronic or paper form, as the Commission may, by rule, determine.[406] The Commission preliminarily believes that the provisions identified in items (1) and (2) above are high-level objectives that an NRSRO should be required to achieve in developing the presentation of the form. As discussed next, Section 15E(s)(3) of the Exchange Act identifies very specific items of information that the Commission's rule shall require an NRSRO to include in the form.[407] Given the specificity in Section 15E(s)(3), the Commission preliminarily believes it would be appropriate to use the higher level objectives specified in Section 15E(s)(2) to prescribe presentation requirements for the form.[408] Consequently, the Commission is proposing rule text that would mirror the statutory text.[409] In particular, proposed new paragraph (a)(1)(i)(A) of Rule 17g–7 would provide that the form generated by the NRSRO would need to be easy to use and helpful for users of credit ratings to understand the information contained in the form.[410] For example, the Commission preliminarily believes that a form that presents the required information in complex mathematical equations would not achieve this objective.

Similarly, proposed new paragraph (a)(1)(i)(B) of Rule 17g–7 would mirror the statutory text by requiring that the content described in proposed new paragraphs (a)(1)(ii)(K), (L) and (M) of Rule 17g–7 be disclosed in a manner that is directly comparable across types of obligors, securities, and money market instruments.[411] As discussed below, Section 15E(s)(3) of the Exchange Act identifies qualitative and quantitative information that must be included in the form.[412] Section 15E(s)(2)(B) provides that the quantitative content identified in Section 15E(s)(3)(B) be directly comparable across types of securities.[413] The Commission is proposing that the quantitative content specified in Section 15E(s)(3)(B) of the Exchange Act be disclosed in the form pursuant to new paragraphs (a)(1)(ii)(K), (L), and (M) of Rule 17g–7.[414] Consequently, as proposed, new paragraph (a)(1)(i)(B) of Rule 17g–7 would implement Section 15E(s)(2)(B) by requiring an NRSRO to present this quantitative information in a manner that is directly comparable across types of obligors, securities, and money market instruments.

Request for Comment

The Commission generally requests comment on all aspects of proposed paragraph (a)(1)(ii) of proposed Rule 17g–7. The Commission also seeks comment on the following:

1. Is the objective that the form be easy to use and helpful for users of credit ratings to understand the information contained in the report sufficiently clear to provide NRSROs with guidance on how to present the information in the form in accordance with this proposed requirement? If not, how should the proposal be modified to provide better guidance? Commenters should provide specific suggested rule text and explain the rationale for it.

2. Is the objective that the content described in proposed paragraphs (a)(1)(ii)(K), (L) and (M) of Rule 17g–7 be disclosed in a manner that is directly comparable across types of obligors, securities, and money market instruments sufficiently clear to provide NRSROs with guidance on how to present this information in the form in accordance with this proposed requirement? If not, how should the proposal be modified to provide better guidance? Commenters should provide specific suggested rule text and explain the rationale for it. In addition, how would adding "obligors" and "money market instruments" to the presentation requirement expand its scope? Finally, the Commission requests commenters to provide examples of disclosures in these areas that are being made now (if such disclosures are being made) and how the disclosures might be presented under the proposed requirements.

3. Should the Commission require that the information an NRSRO must include in the form be presented in a certain order to enhance comparability? For example, should the Commission require that the information be disclosed in the order in which it is identified in proposed paragraph (a)(1)(ii) of Rule 17g–7 discussed below? Are there other means of enhancing the comparability of forms among NRSROs? For example, should the Commission require a more standardized format for the form?

3. Paragraph (a)(1)(ii)—Content of the Form

Section 15E(s)(3) of the Exchange Act provides that the Commission shall require, by rule, that the form accompanying the publication of a credit rating contain specifically

[403] *See* proposed new paragraph (a)(1) of Rule 17g–7.

[404] *See* 15 U.S.C. 78o–7(s)(2)(A).

[405] *See* 15 U.S.C. 78o–7(s)(2)(B).

[406] *See* 15 U.S.C. 78o–7(s)(2)(C). As discussed above, the Commission proposes to implement Section 15E(s)(2)(C) of the Exchange Act through the prefatory text in proposed new paragraph (a) of Rule 17g–7.

[407] *See* 15 U.S.C. 78o–7(s)(3)(A) and (B).

[408] *See* 15 U.S.C. 78o–7(s)(2) and 15 U.S.C. 78o–7(s)(3).

[409] *See* proposed new paragraphs (a)(1)(i)(A) and (B) of Rule 17g–7.

[410] *Compare* new paragraph (a)(1)(i)(A) of Rule 17g–7, *with* 15 U.S.C. 78o–7(s)(2)(A).

[411] *Compare* new paragraph (a)(1)(i)(B) of Rule 17g–7, *with* 15 U.S.C. 78o–7(s)(2)(B). *See also* 15 U.S.C. 78o–7(s)(2)(B) and 15 U.S.C. 78o–7(s)(3)(B). While the statutory text only refers to "securities," Section 3(a)(60) of the Exchange Act defines the term "credit rating" to mean an "assessment of the creditworthiness of an obligor as an entity or with respect to specific securities or money market instruments." *See* 15 U.S.C. 78c(a)(60). The Commission believes it would be appropriate to expand this presentation requirement for the form to include credit ratings of "obligors" and "money market instruments" to ensure that it applies to all types of credit ratings and to be consistent with the Commission's existing and proposed rules for NRSROs, which commonly apply to credit ratings of "obligors, securities, and money market instruments." *See, e.g.,* 17 CFR 240.17g–2 and 17 CFR 240.17g–3.

[412] *See* 15 U.S.C. 78o–7(s)(3).

[413] *See* 15 U.S.C. 78o–7(s)(3)(A) and (B).

[414] *See* proposed new paragraphs (a)(1)(ii)(K), (L), and (M) of Rule 17g–7 and 15 U.S.C. 78o–7(s)(3)(B)).

identified items of information.[415] In particular, Section 15E(s)(3)(A) identifies items of "qualitative content" and Section 15E(s)(3)(B) identifies items of "quantitative content."[416] The Commission preliminarily believes that the items of information identified in Sections 15E(s)(3)(A) and (B) are explicit and, consequently, proposes rule text that would mirror the statutory text.[417] In addition, the Commission also is proposing that certain additional information be included in the form.

Prefatory Text of Paragraph (a)(1)(ii). The prefatory text of proposed new paragraph (a)(1)(ii) of Rule 17g–7 would provide that the form generated by the NRSRO must contain information about the credit rating identified in paragraphs (a)(1)(ii)(A) through (N).[418]

Paragraph (a)(1)(ii)(A). The first item of information would be identified in proposed new paragraph (a)(1)(ii)(A) of Rule 17g–7.[419] This paragraph would implement, in part, Section 15E(s)(3)(A)(i) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose in the form the credit ratings produced by the NRSRO.[420] Specifically, paragraph (a)(1)(ii)(A) of Rule 17g–7 would require the NRSRO to include the symbol, number, or score in the rating scale used by the NRSRO to denote the credit rating categories and notches within categories assigned to the obligor, security, or money market instrument that is the subject of the rating action and the identity of the obligor, security, or money market instrument.[421] In other words, the form would need to identify the symbol, number, or score representing the notch in the applicable rating scale assigned to the obligor, security, or money market instrument, which, as proposed in the prefatory text to paragraph (a) of Rule 17g–7, would include a preliminary credit rating, an initial credit rating, an upgrade or downgrade of an existing credit rating (including a downgrade to, or assignment of, default), a placement of an existing credit rating on watch or review, an affirmation of an existing credit rating, or withdrawal of an existing credit rating.[422]

In addition, under proposed new paragraph (a)(1)(ii)(A) of Rule 17g–7, the form would need to contain the identity of the obligor, security, or money market instrument that is the subject of the rating action. The Commission preliminarily believes that the identity of the obligor would be the person's legal name and any other name the obligor uses in its business. Furthermore, the Commission preliminarily believes that the identity of the security or money market instrument would be the name of the security or money market instrument, if applicable, and a description of the security or money market instrument. For example, a bond could be identified as "senior unsecured debt issued by Company XYZ maturing in 2015." Providing the CUSIP for the security or money market instrument also could be a way to further identify it. The Commission preliminarily believes that the disclosure on the form of the identity of the obligor, security, or money market instrument must be sufficient to notify (and not confuse) users of the form as to the identity of rated obligor, security, or money market instrument. As discussed above, the Commission is proposing in new paragraph (a)(1)(i)(A) of Rule 17g–7 that the NRSRO must generate a form that is easy to use and helpful for users of credit ratings to understand the information contained in the form.[423] The Commission preliminarily believes a form that does not clearly identify the obligor, security, or money market instrument subject to the rating action would not meet this requirement.

Paragraph (a)(1)(ii)(B). The second item of information would be identified in proposed new paragraph (a)(1)(ii)(B) of Rule 17g–7.[424] This paragraph would implement, in part, Section 15E(r)(3)(A) of the Exchange Act.[425] As discussed above in Section II.F.1 of this release, Section 15E(r)(3)(A) provides that the rules adopted by the Commission must ensure an NRSRO notifies users of credit ratings of the version of a procedure or methodology, including the qualitative methodology or quantitative inputs, used with respect to a particular credit rating.[426] The Commission is proposing to implement Section 15E(r)(3)(A), in part, through paragraph (a)(5) of new Rule 17g–8.[427] Proposed paragraph (a)(5) of new Rule 17g–8 would require an NRSRO to have policies and procedures that are reasonably designed to ensure the NRSRO discloses the version of a credit rating procedure or methodology, including the qualitative methodology or quantitative inputs, used with respect to a particular credit rating.

The Commission proposes to further implement Section 15E(r)(3)(A) of the Exchange Act through proposed paragraph (a)(1)(ii)(B) of Rule 17g–7. Specifically, paragraph (a)(1)(ii)(B) would require the NRSRO to disclose on the form the version of the procedure or methodology used to determine the credit rating.[428] The Commission preliminarily believes that this disclosure could be made by identifying the name of the procedure or methodology (including any number used to denote the version), the date the procedure was implemented, and an Internet URL where further information about the procedure or methodology can be obtained.[429] The Commission preliminarily believes that proposed paragraph (a)(1)(ii)(B) of Rule 17g–7 would complement and work in conjunction with proposed paragraph (a)(5) of new Rule 17g–8.[430] Rule 17g–7 would require the disclosure and Rule 17g–8 would require the NRSRO to have policies and procedures that are reasonably designed to ensure the disclosure is made.[431]

The Commission also notes that Section 15E(s)(1)(B) of the Exchange Act provides that the Commission shall require, by rule, each NRSRO to prescribe a form to accompany the publication of a credit rating that discloses information that can be used by investors and other users of credit ratings to better understand credit ratings in each class of credit rating issued by the NRSRO.[432] The Commission preliminarily believes that disclosing the version of the procedure or methodology used to determine the credit rating would promote this goal. For example, credit rating methodologies that are predominantly quantitative rely on models to produce credit ratings. These models periodically are updated and released as newer or different versions of the

[415] *See* 15 U.S.C. 78o–7(s)(3).

[416] *See* 15 U.S.C. 78o–7(s)(3)(A) and (B).

[417] *Compare* proposed new paragraph (a)(1)(ii) of Rule 17g–7, *with* 15 U.S.C. 78o–7(s)(3).

[418] *See* proposed new paragraph (a)(1)(ii) of Rule 17g–7.

[419] *See* proposed new paragraph (a)(1)(ii)(A) of Rule 17g–7.

[420] *See* 15 U.S.C. 78o–7(s)(3)(A)(i).

[421] *Id.*

[422] *See* proposed new paragraph (a) of Rule 17g–7.

[423] *See* proposed new paragraph (a)(1)(i)(A) of Rule 17g–7.

[424] *See* proposed new paragraph (a)(1)(ii)(B) of Rule 17g–7.

[425] *See* 15 U.S.C. 78o–7(r)(3)(A).

[426] *Id.*

[427] *See* proposed paragraph (a)(5) of new Rule 17g–8.

[428] *See* proposed paragraph (a)(1)(ii)(B) of Rule 17g–7.

[429] For example, a disclosure could resemble: "RMBS Rating Methodology 3.0, implemented February 12, 2011. For further information go to [insert website address]."

[430] *See* 15 U.S.C. 78o–7(r)(3)(A), proposed new paragraph (a)(1)(ii)(B) of Rule 17g–7, and proposed paragraph (a)(5) of Rule 17g–8.

[431] *See* proposed new paragraph (a)(1)(ii)(B) of Rule 17g–7 and proposed paragraph (a)(5) of Rule 17g–8.

[432] *See* 15 U.S.C. 78o–7(s)(1)(B).

previous model. The Commission preliminarily believes disclosing the version of a model used to produce a credit rating would help investors and other users of credit ratings better understand the credit rating and how the determination of the credit rating may differ from similar products rated using an earlier version of the model.

Paragraph (a)(1)(ii)(C). The third item of information would be identified in proposed new paragraph (a)(1)(ii)(C) of Rule 17g–7.[433] This paragraph would implement Section 15E(s)(3)(A)(ii) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose in the form the main assumptions and principles used in constructing procedures and methodologies, including qualitative methodologies and quantitative inputs and assumptions about the correlation of defaults across underlying assets used in rating structured products.[434] The Commission preliminarily believes that the statutory text is explicit with respect to the information to be disclosed and, consequently proposed new paragraph (a)(1)(ii)(C) of Rule 17g–7 would mirror the statutory text.[435] In particular, proposed new paragraph (a)(1)(ii)(C) of Rule 17g–7 would require the NRSRO to disclose in the form the main assumptions and principles used in constructing the procedures and methodologies used to determine the credit rating, including qualitative methodologies and quantitative inputs and, if the credit rating is for a structured finance product, assumptions about the correlation of defaults across the underlying assets.[436]

Paragraph (a)(1)(ii)(D). The fourth item of information would be identified in proposed new paragraph (a)(1)(ii)(D) of Rule 17g–7.[437] This paragraph would implement Section 15E(s)(3)(A)(iii) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose in the form the potential limitations of the credit ratings and the types of risks excluded from the credit ratings that the NRSRO does not comment on, including liquidity, market, and other risks.[438] The Commission preliminarily believes that the statutory text is explicit with respect to the information to be disclosed and, consequently proposed new paragraph (a)(1)(ii)(D) of Rule 17g–7 would mirror the statutory text.[439] In particular, proposed new paragraph (a)(1)(ii)(D) of Rule 17g–7 would require the NRSRO to disclose in the form the potential limitations of the credit rating, including the types of risks excluded from the credit rating that the NRSRO does not comment on, including, as applicable, liquidity, market, and other risks.[440]

Paragraph (a)(1)(ii)(E). The fifth item of information would be identified in proposed new paragraph (a)(1)(ii)(E) of Rule 17g–7.[441] This paragraph would implement Section 15E(s)(3)(A)(iv) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose in the form information on the uncertainty of the credit rating, including: (1) Information on the reliability, accuracy, and quality of the data relied on in determining the credit rating; and (2) a statement relating to the extent to which data essential to the determination of the credit rating were reliable or limited, including any limits on the scope of historical data; and any limits in accessibility to certain documents or other types of information that would have better informed the credit rating.[442] The Commission preliminarily believes that the statutory text is explicit with respect to the information to be disclosed and, consequently proposed new paragraph (a)(1)(ii)(E) of Rule 17g–7 would mirror the statutory text.[443] In particular, proposed new paragraph (a)(1)(ii)(E) of Rule 17g–7 would require the NRSRO to disclose in the form information on the uncertainty of the credit rating, including: (1) Information on the reliability, accuracy, and quality of the data relied on in determining the credit rating; and (2) a statement relating to the extent to which data essential to the determination of the credit rating were reliable or limited, including: any limits on the scope of historical data; and any limits in accessibility to certain documents or other types of information that would have better informed the credit rating.[444]

Paragraph (a)(1)(ii)(F). The sixth item of information would be identified in proposed new paragraph (a)(1)(ii)(F) of Rule 17g–7.[445] This paragraph would implement Section 15E(s)(3)(A)(v) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose in the form whether and to what extent third-party due diligence services have been used by the NRSRO, a description of the information that such third-party reviewed in conducting due diligence services, and a description of the findings and conclusions of such third-party.[446] The Commission preliminarily believes that the statutory text is explicit with respect to the information to be disclosed and, consequently proposed new paragraph (a)(1)(ii)(F) of Rule 17g–7 would mirror the statutory text.[447] In particular, proposed new paragraph (a)(1)(ii)(F) of Rule 17g–7 would require the NRSRO to disclose in the form whether and to what extent third-party due diligence services were used by the NRSRO, a description of the information that such third-party reviewed in conducting due diligence services, and a description of the findings or conclusions of such third-party.[448]

The Commission notes that Section 15E(s)(4)(A) of the Exchange Act contains a requirement that the issuer or underwriter of any asset-backed security shall make publicly available the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter.[449] In addition, Section 15E(s)(4)(B) of the Exchange Act contains a self-executing requirement providing that in any case in which third-party due diligence services are employed by an NRSRO, an issuer, or an underwriter, the person providing the due diligence services shall provide to any NRSRO that produces a rating to which such services relate, written certification in a format prescribed, by rule, by the Commission.[450] Finally, as discussed above in Section II.G.1 of this release and below in Section II.G.5, the NRSRO would be required to disclose with the publication of a credit rating any certifications it receives from a provider of third-party due diligence services pursuant to Section 15E(s)(4)(B)

[433] *See* proposed new paragraph (a)(1)(ii)(C) of Rule 17g–7.

[434] *See* 15 U.S.C. 78o–7(s)(3)(A)(ii).

[435] Compare 15 U.S.C. 78o–7(s)(3)(A)(ii), *with* proposed new paragraph (a)(1)(ii)(C) of Rule 17g–7.

[436] *See* proposed new paragraph (a)(1)(ii)(C) of Rule 17g–7.

[437] *See* proposed new paragraph (a)(1)(ii)(D) of Rule 17g–7.

[438] *See* 15 U.S.C. 78o–7(s)(3)(A)(iii).

[439] Compare 15 U.S.C. 78o–7(s)(3)(A)(iii), *with* proposed new paragraph (a)(1)(ii)(D) of Rule 17g–7.

[440] *See* proposed new paragraph (a)(1)(ii)(D) of Rule 17g–7.

[441] *See* proposed new paragraph (a)(1)(ii)(E) of Rule 17g–7.

[442] *See* 15 U.S.C. 78o–7(s)(3)(A)(iv).

[443] Compare 15 U.S.C. 78o–7(s)(3)(A)(iv), *with* proposed new paragraph (a)(1)(ii)(E) of Rule 17g–7.

[444] *See* proposed new paragraph (a)(1)(ii)(E) of Rule 17g–7.

[445] *See* proposed new paragraph (a)(1)(ii)(F) of Rule 17g–7.

[446] *See* 15 U.S.C. 78o–7(s)(3)(A)(v).

[447] Compare 15 U.S.C. 78o–7(s)(3)(A)(v), *with* proposed new paragraph (a)(1)(ii)(F) of Rule 17g–7.

[448] *See* proposed new paragraph (a)(1)(ii)(F) of Rule 17g–7.

[449] *See* 15 U.S.C. 78o–7(s)(4)(A). The Commission's proposals for implementing this provision are discussed below in Section II.H.1 of this release.

[450] *See* 15 U.S.C. 78o–7(s)(4)(B). The Commission's proposals for implementing this provision are discussed below in Sections II.H.2 and II.H.3 of this release.

of the Exchange Act.[451] The Commission preliminarily believes that the disclosure that would be required pursuant to proposed paragraph (a)(1)(ii)(F) of Rule 17g–7 would need to describe how the NRSRO used the findings and conclusions of any third-party due diligence report made publicly available by an issuer or underwriter pursuant to Section 15E(s)(4)(A) of the Exchange Act.[452] Similarly, the Commission preliminarily believes that the disclosure would need to describe how the NRSRO used any certifications it receives from providers of third-party due diligence services pursuant to Section 15E(s)(4)(B) of the Exchange Act.[453]

Paragraph (a)(1)(ii)(G). The seventh item of information would be identified in proposed new paragraph (a)(1)(ii)(G) of Rule 17g–7.[454] This paragraph would implement Section 15E(s)(1)(A)(iii) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose, if applicable, how the NRSRO used servicer or remittance reports, and with what frequency, to conduct surveillance of the credit rating.[455] The Commission preliminarily believes that the statutory text is explicit with respect to the information to be disclosed and, consequently proposed new paragraph (a)(1)(ii)(G) of Rule 17g–7 would mirror the statutory text.[456] In particular, proposed new paragraph (a)(1)(ii)(G) of Rule 17g–7 would require the NRSRO to disclose in the form, if applicable, how servicer or remittance reports were used, and with what frequency, to conduct surveillance of the credit rating.[457]

Paragraph (a)(1)(ii)(H). The eighth item of information would be identified in proposed new paragraph (a)(1)(ii)(H) of Rule 17g–7.[458] This paragraph would implement Section 15E(s)(3)(A)(vi) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose in the form a description of the data about any obligor, issuer, security, or money market instrument that were relied upon for the purpose of determining the credit rating.[459] The Commission preliminarily believes that the statutory text is explicit with respect to the information to be disclosed and, consequently proposed new paragraph (a)(1)(ii)(H) of Rule 17g–7 would mirror the statutory text.[460] In particular, proposed new paragraph (a)(1)(ii)(H) of Rule 17g–7 would require the NRSRO to disclose in the form a description of the data about any obligor, issuer, security, or money market instrument that was relied upon for the purpose of determining the credit rating.[461]

Paragraph (a)(1)(ii)(I). The ninth item of information would be identified in proposed new paragraph (a)(1)(ii)(I) of Rule 17g–7.[462] This paragraph would implement Section 15E(s)(3)(A)(vii) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose in the form a statement containing an overall assessment of the quality of information available and considered in producing a rating for the obligor, security, or money market instrument, in relation to the quality of information available to the NRSRO in rating similar obligors, securities, and money market instruments.[463] The Commission preliminarily believes that the statutory text is explicit with respect to the information to be disclosed and, consequently, proposed new paragraph (a)(1)(ii)(I) of Rule 17g–7 would mirror the statutory text.[464] In particular, proposed new paragraph (a)(1)(ii)(I) of Rule 17g–7 would require the NRSRO to disclose in the form a statement containing an overall assessment of the quality of information available and considered in producing a rating for an obligor, security, or money market instrument, in relation to the quality of information available to the NRSRO in rating similar obligors, securities, or money market instruments.[465]

Paragraph (a)(1)(ii)(J). The tenth item of information would be identified in proposed new paragraph (a)(1)(ii)(J) of Rule 17g–7.[466] This paragraph would implement, in part, Section 15E(s)(3)(A)(viii) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose in the form information relating to conflicts of interest of the NRSRO.[467] The Commission preliminarily believes that the statutory text of Section 15E(s)(3)(A)(viii) is relatively general in that it does not specify the type of information about conflicts of interest that should be disclosed.[468] Accordingly, the Commission is proposing to identify three specific items of information that, at a minimum, would need to be disclosed about conflicts of interest.[469]

The first type of disclosure would be identified in proposed new paragraph (a)(1)(ii)(J)(*1*) of Rule 17g–7, which would require the NRSRO to classify the credit rating as either "solicited" or "unsolicited."[470] Proposed new paragraphs (a)(1)(ii)(*J*)(*1*)(*i*), (*ii*) and (*iii*) of Rule 17g–7 would define "solicited" and "unsolicited" credit ratings.[471] In this regard, the Commission is proposing two different sub-categories for solicited ratings: "solicited sell-side" and "solicited buy-side."[472] Proposed new paragraph (a)(1)(ii)(*J*)(*1*)(*i*) of Rule 17g–7 would define "Solicited sell-side" to mean the credit rating was paid for by the obligor being rated or the issuer, underwriter, depositor, or sponsor of the security or money market instrument being rated.[473] In other words, the "solicited sell-side" classification would be used for issuer-paid credit ratings. Proposed new paragraph (a)(1)(ii)(*J*)(*1*)(*ii*) of Rule 17g–7 would define "Solicited buy-side" to mean the credit rating was paid for by a person other than the obligor being rated or the issuer, underwriter, depositor, or sponsor of the security or money market instrument being rated. For example, a potential investor in a security may pay

[451] *See* proposed prefatory text of paragraph (a) and proposed paragraph (a)(2) of Rule 17g–7.

[452] *See* 15 U.S.C. 78o–7(s)(4)(A).

[453] *See* 15 U.S.C. 78o–7(s)(4)(B).

[454] *See* proposed new paragraph (a)(1)(ii)(G) of Rule 17g–7.

[455] *See* 15 U.S.C. 78o–7(s)(1)(A)(iii).

[456] Compare 15 U.S.C. 78o–7(s)(1)(A)(iii), *with* proposed new paragraph (a)(1)(ii)(G) of Rule 17g–7.

[457] *See* proposed new paragraph (a)(1)(ii)(G) of Rule 17g–7.

[458] *See* proposed new paragraph (a)(1)(ii)(H) of Rule 17g–7.

[459] *See* 15 U.S.C. 78o–7(s)(3)(A)(vi).

[460] *Compare* 15 U.S.C. 78o–7(s)(3)(A)(vi), *with* proposed new paragraph (a)(1)(ii)(H) of Rule 17g–7.

[461] *See* proposed new paragraph (a)(1)(ii)(H) of Rule 17g–7.

[462] *See* proposed new paragraph (a)(1)(ii)(I) of Rule 17g–7.

[463] *See* 15 U.S.C. 78o–7(s)(3)(A)(vii). The Commission notes that the end of the statutory text refers to ratings of "similar issuances." *Id.* However, the preceding text refers to rating an "obligor, security, or money market instrument." *Id.* As discussed earlier, a credit rating of an "obligor" commonly means the rating of the obligor as an entity rather than a rating of securities or money market instruments issued by the obligor. Consequently, the rating of an obligor may not relate to an "issuance" of a particular security or money market instrument. Therefore, the Commission proposes in new paragraph (a)(1)(ii)(I) of Rule 17g–7 to use the term "similar obligors, securities, or money market instruments" instead of the term "similar issuances" in the statutory text.

[464] *Compare* 15 U.S.C. 78o–7(s)(3)(A)(vii), *with* proposed new paragraph (a)(1)(ii)(I) of Rule 17g–7.

[465] *See* proposed new paragraph (a)(1)(ii)(I) of Rule 17g–7.

[466] *See* proposed new paragraph (a)(1)(ii)(I) of Rule 17g–7.

[467] *See* 15 U.S.C. 78o–7(s)(3)(A)(viii).

[468] *Id.*

[469] *See* proposed new paragraph (a)(1)(ii)(J) of Rule 17g–7.

[470] *See* proposed new paragraph (a)(1)(ii)(J)(*1*) of Rule 17g–7.

[471] *See* proposed new paragraphs (a)(1)(ii)(*J*)(*1*)(*i*), (*ii*) and (*iii*) of Rule 17g–7.

[472] *See* proposed new paragraph (a)(1)(ii)(J)(*1*)(*i*) and (*ii*) of Rule 17g–7.

[473] *See* proposed new paragraph (a)(1)(ii)(*J*)(*1*)(*i*) of Rule 17g–7.

an NRSRO to determine a credit rating for the security. The Commission preliminarily believes this distinction is relevant because, depending on the type of entity paying for the rating, the potential conflict may exert different types of undue influence on the NRSRO. For example, a sell-side purchaser of the credit rating presumably would want the highest rating possible. However, a buy-side purchaser could want a lower credit rating if the purchaser is maintaining a short position or desiring a higher interest rate.

Proposed new paragraph (a)(1)(ii)(*f*)(*1*)(*iii*) of Rule 17g–7 would define an "unsolicited" credit rating to mean a credit rating the NRSRO was not paid to determine.[474] The Commission preliminarily intends this definition to include credit ratings funded by selling subscriptions to access the credit ratings (so-called "subscriber-paid credit ratings"). However, if a subscriber paid the NRSRO to determine a credit rating for a specific obligor, security, or money market instrument, the credit rating would need to be classified as either "solicited sell-side" if the subscriber also was the obligor being rated or the issuer, underwriter, depositor, or sponsor of the security or money market instrument being rated, or "solicited buy-side" if the subscriber was not the obligor being rated or the issuer, underwriter, depositor, or sponsor of the security or money market instrument being rated. This would apply, for example, if the subscriber was an investor or potential investor in the security or money market instrument and hired the NRSRO to specifically rate the security or money market instrument. In such a case, the credit rating would need to be classified as "solicited buy-side."

The second type of conflict disclosure would be identified in proposed new paragraph (a)(1)(ii)(*f*)(*2*) of Rule 17g–7.[475] This paragraph would provide that if the credit rating is classified as either "solicited sell-side" or "solicited buy-side" the NRSRO would be required to disclose whether the NRSRO provided services other than determining credit ratings to the person that paid for the rating during the most recently ended fiscal year.[476] In other words, the NRSRO would be required to indicate whether the person who purchased the credit rating was a client with respect to other services provided by the NRSRO. The Commission preliminarily believes clients paying an NRSRO for services in addition to determining credit ratings may pose an increased risk of exerting undue influence on the NRSRO with respect to its determination of credit ratings.[477] The Commission has adopted rules that address consulting and advisory services under authority in Section 15E(h)(2)(B).[478] The Commission preliminarily believes that the proposed disclosure requirement about other services would complement these requirements.

The third type of conflict disclosure would be identified in proposed new paragraph (a)(1)(ii)(*f*)(*3*) of Rule 17g–7.[479] This paragraph would require disclosure of information about a conflict of interest influencing a credit rating action discovered as a result of a look-back review conducted pursuant to Section 15E(h)(4)(A) of the Exchange Act and proposed paragraph (c) of new Rule 17g–8.[480]

Paragraph (a)(1)(ii)(K). The eleventh item of information would be identified in proposed new paragraph (a)(1)(ii)(K) of Rule 17g–7.[481] This paragraph would implement Section 15E(s)(3)(B)(i) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose in the form an explanation or measure of the potential volatility of the credit rating, including: (1) Any factors that might lead to a change in the credit ratings; and (2) the magnitude of the change that a user can expect under different market conditions.[482] The Commission preliminarily believes that the statutory text is explicit with respect to the information to be disclosed and, consequently proposed new paragraph (a)(1)(ii)(K) of Rule 17g–7 would mirror the statutory text.[483] In particular, proposed new paragraph (a)(1)(ii)(K) of Rule 17g–7 would require the NRSRO to disclose in the form an explanation or measure of the potential volatility of the credit rating, including: (1) Any factors that might lead to a change in the credit rating; and (2) the magnitude of the change that could occur under different market conditions.[484]

Paragraph (a)(1)(ii)(L). The twelfth item of information would be identified in proposed new paragraph (a)(1)(ii)(L) of Rule 17g–7.[485] This paragraph would implement Section 15E(s)(3)(B)(ii) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose in the form information on the content of the credit rating, including: (1) The historical performance of the credit rating; and (2) the expected probability of default and the expected loss in the event of default.[486] The Commission preliminarily believes that the statutory text is explicit with respect to the information to be disclosed and, consequently proposed new paragraph (a)(1)(ii)(L) of Rule 17g–7 would mirror the statutory text.[487] In particular, proposed new paragraph (a)(1)(ii)(L) of Rule 17g–7 would require the NRSRO to disclose in the form information on the content of the rating, including: (1) If applicable, the historical performance of the rating; and (2) the expected probability of default and the expected loss in the event of default.[488]

Paragraph (a)(1)(ii)(M). The thirteenth item of information would be identified in proposed new paragraph (a)(1)(ii)(M) of Rule 17g–7.[489] This paragraph would implement Section 15E(s)(3)(B)(iii) of the Exchange Act, which provides that the Commission's rule shall require the NRSRO to disclose in the form information on the sensitivity of the credit rating to assumptions made by the NRSRO, including: (1) Five assumptions made in the ratings process that, without accounting for any other factor, would have the greatest impact on a rating if the assumptions were proven false or inaccurate; and (2) an analysis, using specific examples, of how each of the 5 assumptions identified impacts a credit rating.[490] The Commission preliminarily believes that the statutory text is explicit with respect to the information to be disclosed and, consequently proposed new paragraph (a)(1)(ii)(M) of Rule 17g–7 would mirror

[474] *See* proposed new paragraph (a)(1)(ii)(*f*)(*1*)(*iii*) of Rule 17g–7.

[475] *See* proposed new paragraph (a)(1)(ii)(*f*)(*2*) of Rule 17g–7.

[476] *Id.*

[477] In this regard, the Commission notes that Section 939H of the Dodd-Frank Act contains a sense of the Congress that the Commission should exercise rulemaking authority under Section 15E(h)(2)(B) of the Exchange Act to prevent improper conflicts of interest arising from employees of NRSROs providing services to issuers of securities that are unrelated to the issuance of credit ratings, including consulting, advisory, and other services. *See* Public Law 111–203 § 939H.

[478] *See* 17 CFR 240.17g–5(a) and (b)(3), (4) and (5) and 17 CFR 240.17g–5(c).

[479] *See* proposed new paragraph (a)(1)(ii)(*f*)(*3*) of Rule 17g–7.

[480] This information is discussed in detail above in Section II.C.1 of this release.

[481] *See* proposed new paragraph (a)(1)(ii)(K) of Rule 17g–7.

[482] *See* 15 U.S.C. 78o–7(s)(3)(B)(i).

[483] *Compare* 15 U.S.C. 78o–7(s)(3)(B)(i), *with* proposed new paragraph (a)(1)(ii)(K) of Rule 17g–7.

[484] *See* proposed new paragraph (a)(1)(ii)(K) of Rule 17g–7.

[485] *See* proposed new paragraph (a)(1)(ii)(L) of Rule 17g–7.

[486] *See* 15 U.S.C. 78o–7(s)(3)(B)(ii).

[487] *Compare* 15 U.S.C. 78o–7(s)(3)(B)(ii), *with* proposed new paragraph (a)(1)(ii)(L) of Rule 17g–7.

[488] *See* proposed new paragraph (a)(1)(ii)(L) of Rule 17g–7.

[489] *See* proposed new paragraph (a)(1)(ii)(M) of Rule 17g–7.

[490] *See* 15 U.S.C. 78o–7(s)(3)(B)(iii).

the statutory text.[491] In particular, proposed new paragraph (a)(1)(ii)(M) of Rule 17g–7 would require the NRSRO to disclose in the form information on the sensitivity of the rating to assumptions made by the NRSRO, including: (1) 5 assumptions made in the ratings process that, without accounting for any other factor, would have the greatest impact on a rating if the assumptions were proven false or inaccurate; and (2) an analysis, using specific examples, of how each of the 5 assumptions identified in the form impacts a rating.[492]

Paragraph (a)(1)(ii)(N). Finally, the fourteenth item of information would be identified in proposed new paragraph (a)(1)(ii)(N) of Rule 17g–7.[493] This paragraph would contain the current disclosure requirement in Rule 17g–7.[494] In particular, the current requirements in paragraphs (a) and (b) of Rule 17g–7 would be contained in proposed new paragraph (a)(1)(ii)(N).[495] Specifically, this paragraph would provide that if the credit rating is issued with respect to an asset-backed security, as that term is defined in Section 3(a)(77) of the Exchange Act, the NRSRO must include in the form a description of: (1) The representations, warranties, and enforcement mechanisms available to investors; and (2) how they differ from the representations, warranties, and enforcement mechanisms in issuances of similar securities.

Request for Comment

The Commission generally requests comment on all aspects of proposed paragraph (a)(1)(ii) of proposed Rule 17g–7. The Commission also seeks comment on the following:

1. With respect to proposed paragraph (a)(1)(ii)(A), should the Commission consider requiring the disclosure of information in addition to the identity of the obligor's legal name and any other name that the obligor uses in its business? Are there additional or alternative ways to identify the obligor? Also, provide examples of how this disclosure might appear on the form.

2. With respect to proposed paragraph (a)(1)(ii)(A), should the Commission consider requiring the disclosure of information in addition to the name of the security or money market instrument, if applicable, and a description of the security or money market instrument? Are there additional or alternative ways to identify the security or money market instrument? Would disclosing the CUSIP alone be sufficient to identify the security or money market instrument? If so, should the Commission consider requiring that the CUSIP be disclosed? Also, provide examples of how this disclosure might appear on the form.

3. With respect to proposed paragraph (a)(1)(ii)(B), would the disclosure of the version of the procedure or methodology used to determine the credit rating in conjunction with proposed paragraph (a)(5) of Rule 17g–8 achieve the goals of Section 15E(r)(3)(A) of the Exchange Act? If not, what alternative or additional requirements should the Commission consider? Also, provide examples of how this disclosure might appear on the form.

4. Proposed paragraph (a)(1)(ii)(C) of Rule 17g–7 would require an NRSRO to disclose in the form the main assumptions and principles used in constructing the procedures and methodologies used to determine the credit rating, including qualitative methodologies and quantitative inputs and, if the credit rating is for a structured finance product, assumptions about the correlation of defaults across the underlying assets. Is this proposed requirement sufficiently explicit with respect to the information that would need to be disclosed? If not, what additional detail should the Commission provide in terms of the information that would need to be disclosed? Also, provide examples of how this disclosure might appear on the form. In addition, would the proposal require the disclosure of proprietary information? If so, what type or types of proprietary information would be disclosed? How could this issue be addressed?

5. Proposed paragraph (a)(1)(ii)(D) of Rule 17g–7 would require the NRSRO to disclose in the form the potential limitations of the credit rating, including the types of risks excluded from the credit rating that the NRSRO does not comment on, including, as applicable, liquidity, market, and other risks. Is this proposed requirement sufficiently explicit with respect to the information that would need to be disclosed? If not, what additional detail should the Commission provide in terms of the information that would need to be disclosed? Also, provide examples of how this disclosure might appear on the form.

6. Proposed paragraph (a)(1)(ii)(E) of Rule 17g–7 require the NRSRO to disclose in the form information on the uncertainty of the credit rating, including: (1) Information on the reliability, accuracy, and quality of the data relied on in determining the credit rating; and (2) a statement relating to the extent to which data essential to the determination of the credit rating were reliable or limited, including: Any limits on the scope of historical data; and any limits in accessibility to certain documents or other types of information that would have better informed the credit rating. Is this proposed requirement sufficiently explicit with respect to the information that would need to be disclosed? If not, what additional detail should the Commission provide in terms of the information that would need to be disclosed? Also, provide examples of how this disclosure might appear on the form. In addition, would the proposal require the disclosure of proprietary information? If so, what type or types of proprietary information would be disclosed? How could this issue be addressed?

7. Proposed paragraph (a)(1)(ii)(F) of Rule 17g–7 would require the NRSRO to disclose in the form whether and to what extent third-party due diligence services were used by NRSRO organization, a description of the information that such third-party reviewed in conducting due diligence services, and a description of the findings or conclusions of such third-party? Is this proposed requirement sufficiently explicit with respect to the information that would need to be disclosed? If not, what additional detail should the Commission provide in terms of the information that would need to be disclosed? Also, provide examples of how this disclosure might appear on the form.

8. With respect to proposed paragraph (a)(1)(ii)(F) of Rule 17g–7, how should the findings and conclusions of any third-party due diligence report made publicly available by the issuer or underwriter pursuant to Section 15E(s)(4)(A) of the Exchange Act be incorporated into the disclosure if used by the NRSRO? Similarly, how should any certifications the NRSRO receives from providers of third-party due diligence services pursuant to Section 15E(s)(4)(B) of the Exchange Act be

[491] *Compare* 15 U.S.C. 78o–7(s)(3)(B)(iii), *with* proposed new paragraph (a)(1)(ii)(M) of Rule 17g–7.

[492] *See* proposed new paragraph (a)(1)(ii)(M) of Rule 17g–7.

[493] *See* proposed new paragraph (a)(1)(ii)(N) of Rule 17g–7.

[494] *See* 17 CFR 240.17g–7. As discussed above Section II.G.1 of this release, the definition of "credit rating" in the third sentence of the prefatory text to proposed new paragraph (a) of Rule 17g–7 would contain the provisions in the current Note to 17 CFR 240.17g–7, which provides that for the purposes of the rule's current requirements, a "credit rating" includes any expected or preliminary credit rating issued by an NRSRO.

[495] *Compare* 17 CFR 240.17g–7(a) and (b), *with* proposed new paragraph (a)(1)(ii)(N) of Rule 17g–7.

incorporated into the disclosure if used by the NRSRO? Also, provide examples of how this disclosure might appear on the form.

9. Proposed paragraph (a)(1)(ii)(G) of Rule 17g–7 would require the NRSRO to disclose in the form, if applicable, how servicer or remittance reports were used, and with what frequency, to conduct surveillance of the credit rating? Is this proposed requirement sufficiently explicit with respect to the information that would need to be disclosed? If not, what additional detail should the Commission provide in terms of the information that would need to be disclosed? Also, provide examples of how this disclosure might appear on the form.

10. Proposed paragraph (a)(1)(ii)(H) of Rule 17g–7 would require the NRSRO to disclose in the form a description of the data about any obligor, issuer, security, or money market instrument that was relied upon for the purpose of determining the credit rating? Is this proposed requirement sufficiently explicit with respect to the information that would need to be disclosed? If not, what additional detail should the Commission provide in terms of the information that would need to be disclosed? Also, provide examples of how this disclosure might appear on the form.

11. Proposed paragraph (a)(1)(ii)(I) of Rule 17g–7 would require the NRSRO to disclose in the form a statement containing an overall assessment of the quality of information available and considered in producing a rating for an obligor, security, or money market instrument, in relation to the quality of information available to the NRSRO in rating similar obligors, securities, or money market instruments. Is this proposed requirement sufficiently explicit with respect to the information that would need to be disclosed? If not, what additional detail should the Commission provide in terms of the information that would need to be disclosed? Also, provide examples of how this disclosure might appear on the form.

12. With respect to proposed paragraph (a)(1)(ii)(J)(*1*) of Rule 17g–7, are the proposed definitions of "solicited sell-side", "solicited buy-side", and "unsolicited" credit ratings sufficiently clear? If not, how should the definitions be augmented or altered? Also, provide examples of how this disclosure might appear on the form.

13. With respect to proposed paragraph (a)(1)(ii)(J)(*1*) of Rule 17g–7, would distinguishing between "solicited sell-side" and "solicited buy-side" credit ratings provide useful disclosure of potentially different conflicts of interest? Alternatively, should the disclosure more simply require classification of whether the credit rating was "solicited" or "unsolicited"? Also, provide examples of how this disclosure might appear on the form.

14. With respect to proposed paragraph (a)(1)(ii)(J)(*2*) of Rule 17g–7, would the proposed disclosure of whether the NRSRO provided other services to the person that paid for the credit rating during the most recently ended fiscal year provide useful disclosure of potential conflicts of interest? Also, provide examples of how this disclosure might appear on the form.

15. With respect to proposed paragraph (a)(1)(ii)(J) of Rule 17g–7, is there other information about conflicts of interest that the Commission should consider requiring to be disclosed in the form? Commenters should provide specific examples of such information and explain how it would provide useful information. Also, provide examples of how this disclosure might appear on the form.

16. Proposed paragraph (a)(1)(ii)(K) of Rule 17g–7 would require the NRSRO to disclose in the form an explanation or measure of the potential volatility of the credit rating, including: (1) Any factors that might lead to a change in the credit rating; and (2) the magnitude of the change that could occur under different market conditions. Is this proposed requirement sufficiently explicit with respect to the information that would need to be disclosed? If not, what additional detail should the Commission provide in terms of the information that would need to be disclosed? Also, provide examples of how this disclosure might appear on the form. Should the Commission provide guidance on the types of factors that should be disclosed to establish a materiality threshold? If so, describe the factors and the corresponding materiality threshold. Furthermore, should the Commission define the term "might lead to a change in the credit rating" to establish the level of probability necessary to trigger the disclosure? If so, how should the term be defined?

17. Proposed paragraph (a)(1)(ii)(L) of Rule 17g–7 would require the NRSRO to disclose in the form information on the content of the rating, including: (1) If applicable, the historical performance of the rating; and (2) the expected probability of default and the expected loss in the event of default. Is this proposed requirement sufficiently explicit with respect to the information that would need to be disclosed? If not, what additional detail should the Commission provide in terms of the information that would need to be disclosed? Also, provide examples of how this disclosure might appear on the form.

18. With respect to proposed paragraph (a)(1)(ii)(M) of Rule 17g–7 would require the NRSRO to disclose in the form information on the sensitivity of the rating to assumptions made by the NRSRO, including: (1) 5 assumptions made in the ratings process that, without accounting for any other factor, would have the greatest impact on a rating if the assumptions were proven false or inaccurate; and (2) an analysis, using specific examples, of how each of the 5 assumptions identified in the form impacts a rating? Is this proposed requirement sufficiently explicit with respect to the information that would need to be disclosed? If not, what additional detail should the Commission provide in terms of the information that would need to be disclosed? Also, provide examples of how this disclosure might appear on the form. In addition, would the proposal require the disclosure of proprietary information? If so, what type or types of proprietary information would be affected? How could this issue be addressed?

19. Is the proposal to codify the current requirements in paragraphs (a) and (b) of Rule 17g–7 in proposed paragraph (a)(1)(ii)(N) of Rule 17g–7 appropriate? For example, would this re-designation change those requirements in some manner?

4. Paragraph (a)(1)(iii)—Attestation Requirement

Section 15E(q)(2)(F) of the Exchange Act provides that the Commission's rules must require an NRSRO to include an attestation with any credit rating it issues affirming that no part of the rating was influenced by any other business activities, that the rating was based solely on the merits of the instruments being rated, and that such rating was an independent evaluation of the risks and merits of the instrument.[496] While Section 15E(q) relates to disclosure of information about the performance of credit ratings, the Commission preliminarily believes this attestation provision would more appropriately be implemented with respect to disclosures that must be made when a specific rating action is published. Consequently, the Commission proposes that it be part of the form that would be required to accompany a credit rating pursuant to

[496] *See* 15 U.S.C. 78o–7(q)(2)(F).

rulemaking under Section 15E(s) of the Exchange Act as opposed to a part of the proposed disclosures of Transition/Default Matrices in Exhibit 1 to Form NRSRO or credit rating histories that would implement Section 15E(q).[497]

Consequently, the Commission proposes to implement this attestation requirement as part of the rule requirement for an NRSRO to generate a form to accompany the publication of a credit rating.[498] In particular, under the proposal, the NRSRO would be required to attach to the form a signed statement by a person within the NRSRO stating that the person has responsibility for the credit rating and, to the best knowledge of the person: (1) No part of the credit rating was influenced by any other business activities; (2) the credit rating was based solely upon the merits of the obligor, security, or money market instrument being rated; and (3) the credit rating was an independent evaluation of the risks and merits of the obligor, security, or money market instrument.[499] Thus, the proposed requirement would mirror the statutory text in terms of the representations that would need to be made in the attestation.[500]

Request for Comment

The Commission generally requests comment on all aspects of proposed paragraph (a)(1)(iii) of proposed Rule 17g–7. The Commission also seeks comment on the following:

1. Are there alternative means of implementing Section 15E(q)(2)(F) with respect to the attestation requirement? For example, should Section 15E(q)(2)(F) be implemented in proposed provisions requiring NRSROs to disclose information about the performance of credit ratings (*i.e.,* the proposed Form NRSRO Exhibit 1 Transition/Default Matrices and/or the proposed ratings histories disclosure requirement)? If so, how would the attestation requirement be made a part of either of these other proposals?

2. What person within the NRSRO has responsibility for the credit rating and the other information that would be required to be disclosed in the form and, consequently, could make the attestation? For example, could the lead analyst, the chair of the rating committee, a senior manager, or some other person make the proposed attestation?

[497] *See* 15 U.S.C. 78o–7(s) and 15 U.S.C. 78o–7(q).

[498] *See* 15 U.S.C. 78o–7(s).

[499] *See* proposed new paragraphs (a)(1)(iii)(A)–(C) of Rule 17g–7.

[500] *Compare* proposed new paragraphs (a)(1)(iii)(A)–(C) of Rule 17g–7, *with* 15 U.S.C. 78o–7(q)(2)(F).

5. Paragraph (a)(2)—Certification of Third-Party Due Diligence Provider

Section 15E(s)(4)(B) of the Exchange Act requires a third-party providing due diligence services to an NRSRO, issuer, or underwriter with respect to an Exchange Act-ABS[501] to provide a written certification to any NRSRO that produces a credit rating to which the due diligence services relate.[502] Section 15E(s)(4)(D) of the Exchange Act provides that the Commission shall adopt a rule requiring an NRSRO that receives a certification from a provider of third-party due diligence services to disclose the certification to the public in a manner that allows the public to determine the adequacy and level of the due diligence services provided by the third-party.[503] The Commission preliminarily believes that this goal could best be achieved by requiring the NRSRO to disclose any such certifications with the publication of the NRSRO's credit rating to which the certification relates. Therefore, the Commission is proposing to add a new paragraph (a)(2) to Rule 17g–7 that, in conjunction with the proposed prefatory text of paragraph (a), would provide that the NRSRO must include with the publication of a credit rating any written certification related to the credit rating received from a provider of third-party due diligence services pursuant to Section 15E(s)(4)(B) of the Exchange Act.[504]

Request for Comment

The Commission generally requests comment on all aspects of proposed new paragraph (a)(2) of Rule 17g–7. The Commission also seeks comment on the following:

1. Would it be appropriate to require the inclusion of the certification of the provider of third-party due diligence services with the publication of the credit rating and the form containing information about the credit rating? Is there an alternative means of disclosing the certifications that would be reasonably designed to ensure they are disseminated to users of the NRSRO's credit ratings? If so, describe the method of disclosure.

[501] *See* 15 U.S.C. 78o–7(s)(4)(A)–(D). As noted earlier, the term "structured finance product" as used throughout this release refers broadly to any security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction. This broad category of financial instrument includes an "asset-backed security" as defined in Section 3(a)(77) of the Exchange Act (15 U.S.C. 78c(a)(77)) and other types of structured debt instruments such as CDOs, including synthetic and hybrid CDOs. The term "Exchange Act-ABS" as used throughout this release refers more narrowly to an "asset-backed security" as defined in Section 3(a)(77) of the Exchange Act. 15 U.S.C. 78c(a)(77).

[502] *See* 15 U.S.C. 78o–7(s)(4)(B).

[503] *See* 15 U.S.C. 78o–7(s)(4)(D).

[504] *See* proposed paragraph (a)(2) of Rule 17g–7.

H. Third-Party Due Diligence for Asset-Backed Securities

Section 932(a)(8) of the Dodd-Frank Act amended Section 15E of the Exchange Act to add new paragraph (s), which, as discussed above in Section II.G of this release, has four subparagraphs: (1), (2), (3) and (4).[505] Section 15E(s)(4), "Due diligence services for asset-backed securities," contains four provisions regarding due diligence services relating to an Exchange Act-ABS. Section 15E(s)(4)(A) requires the issuer or underwriter to make publicly available the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter.[506] Section 15E(s)(4)(B) requires that in any case in which third-party due diligence services are employed by an NRSRO, an issuer, or an underwriter, the person providing the due diligence services shall provide to any NRSRO that produces a rating to which such services relate, written certification in a format as provided in Section 15E(s)(4)(C).[507] Section 15E(s)(4)(C) of the Exchange Act provides that the Commission shall establish the appropriate format and content for the written certifications required under Section 15E(s)(4)(B), to ensure that providers of due diligence services have conducted a thorough review of data, documentation, and other relevant information necessary for an NRSRO to provide an accurate rating.[508] Finally, Section 15E(s)(4)(D) of the Exchange Act provides that the Commission shall adopt rules requiring an NRSRO, at the time at which the NRSRO produces a rating, to disclose the certification described in Section 15E(s)(4)(B) to the public in a manner that allows the public to determine the adequacy and level of due diligence services provided by a third party.[509]

As discussed below in Section II.H.1 of this release, the Commission is proposing to implement Section 15E(s)(4)(A) of the Exchange Act by proposing amendments to Rule 314 of Regulation S–T and Form ABS–15G, and proposing new Rule 15Ga–2.[510] In

[505] *See* Public Law 111–203 § 932(a)(8) and 15 U.S.C. 78o–7(s)(1)–(4).

[506] *See* 15 U.S.C. 78o–7(s)(4)(A).

[507] *See* 15 U.S.C. 78o–7(s)(4)(B).

[508] *See* 15 U.S.C. 78o–7(s)(4)(C).

[509] *See* 15 U.S.C. 78o–7(s)(4)(D).

[510] *See* proposed amendments to Rule 314 of Regulation S–T and Form ABS–15G and proposed new Rule 15Ga–2. New Rule 15Ga–2 would be codified at 17 CFR 240.15Ga–2.

addition, as discussed below in Sections II.H.2 and II.H.3 of this release, the Commission is proposing to implement Sections 15E(s)(4)(B) and (C) of the Exchange Act by proposing new Rule 17g–10 and a related form—Form ABS Due Diligence-15E.[511] As discussed above in Section II.G.5 of this release, the Commission is proposing to implement Section 15E(s)(4)(D) by proposing new paragraph (a)(2) to Rule 17g–7.[512]

Before discussing the proposals to implement Sections 15E(s)(4)(A) through (C), the Commission notes the provisions of Section 15E(s)(4) raise two fundamental questions: (1) How will a provider of third-party due diligence services know the identities of the NRSROs producing credit ratings to which its services relate (particularly NRSROs producing unsolicited credit ratings); and (2) when must the certification be provided to the NRSROs? Accordingly, the Commission is requesting comment on these questions in order to consider further guidance or rulemaking to better determine how a provider of third-party due diligence services can comply with the requirement in Section 15E(s)(4)(B) of the Exchange Act.[513]

Request for Comment

The Commission generally requests comment on all aspects of Section 15E(s)(4)(B) of the Exchange Act. The Commission also seeks comment on the following:

1. How would a provider of third-party due diligence services identify the NRSROs producing credit ratings to which the due diligence services relate? For example, would it be sufficient for the provider of third-party due diligence services to contractually require issuers and underwriters that employ it to provide these services to identify the NRSROs engaged by the issuer or underwriter to produce credit ratings for the Exchange Act-ABS and to identify any other NRSROs the issuers and underwriters have notice are producing unsolicited credit ratings for the Exchange Act-ABS? Would issuers and underwriters agree to such contractual terms or would they use a provider of third-party due diligence services that does not demand such terms? Even if issuers and underwriters agree to such contractual terms, would they know the identity of every NRSRO producing a credit rating for the Exchange Act-ABS, particularly NRSROs producing unsolicited credit ratings? Would an appropriate mechanism for providing the certifications to all NRSROs producing a credit rating for the Exchange Act-ABS be to disclose it with the information required by paragraph (a)(3) of Rule 17g–5 (which requires, among other things, the issuer or underwriter to make the information provided to an NRSRO hired to produce a credit rating for a structured finance product such as an Exchange Act-ABS available to any other NRSRO)?[514]

2. In the case where an NRSRO (as opposed to the issuer or underwriter) employs the provider of third-party due diligence services, how would the NRSRO know of any other NRSROs that are producing credit ratings to which the due diligence services relate and provide the identities of such NRSROs to the provider of the third-party due diligence services? If paragraph (a)(3) of Rule 17g–5 would be an appropriate mechanism for providing the certifications to all NRSROs producing a credit rating for the Exchange Act-ABS, could the hired NRSRO obtain a representation from the issuer or underwriter that it would make any certifications received by the NRSRO available to other NRSROs through the process by which the issuer or underwriter makes the information required by paragraph (a)(3) of Rule 17g–5 available to other NRSROs?

3. Should there be some type of centralized database where NRSROs producing credit ratings for an Exchange Act-ABS identify themselves and which would be deemed constructive notice to any provider of third-party due diligence services that is providing services related to the Exchange Act-ABS? If so, should the Commission administer this centralized database or should the issuers and underwriters, providers of third-party due diligence services, NRSROs, or users of credit ratings administer this database?

4. Should there be a centralized database where a provider of third-party due diligence services submits its certification for publication, and should submitting the certification to such a database be deemed constructive receipt by an NRSRO producing a credit rating for an Exchange Act-ABS to which the due diligence services described in the certification relate? Should this database also be the mechanism by which issuers and underwriters make publicly available, pursuant to the requirement in Section 15E(s)(4)(A) of the Exchange Act, the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter? If so, should the Commission administer this centralized database or should the issuers and underwriters, providers of third-party due diligence services, NRSROs, or users of credit ratings administer this database? For example, should the certification be furnished or filed on the Commission's EDGAR system?

5. Should there be a reasonableness test in terms of assessing whether the provider of third-party due diligence services submitted the certification to all NRSROs required to receive the certification? For example, should the provider of third-party due diligence services be required to provide the certification to all NRSROs it knows or reasonably should know are producing a credit rating for which its services relate?

6. How soon after the provider of third-party due diligence services completes its review should the certifications be provided to all NRSROs required to receive it? For example, should the certification be provided "promptly" or within 24 hours, 2 business days, 10 business days, or some other period of time?

7. Should the provider of third-party due diligence services be required to provide the certification to all required NRSROs at the same time so that no single NRSRO has the benefit of using the certification before the other NRSROs that are required to receive it? How would such a requirement be implemented and enforced in practice?

8. Should the requirement to provide the certification to all NRSROs required to receive it sunset after some period of time after the due diligence services are completed such as 30, 60, 90, 120, 150, 180 days or some longer period? For example, should the provider of third-party due diligence services be required to provide the certification to any NRSRO that produces a credit rating to which its services relate until the security matures, is called, is pre-paid, or goes into default?

9. If the provider of third-party due diligence services is hired to provide due diligence services with respect to an initial issuance of securities, would it need to provide the certification at some later time to an NRSRO that does not rate the securities initially but produces a credit rating after the securities have been outstanding for a period of time?

1. Proposed Rule 15Ga–2 and Amendments to Form ABS–15G

The Commission is re-proposing rules, with some revisions, to

[511] *See* proposed new Rule 17g–10 and Form ABS Due Diligence-15E. New Rule 17g–10 would be codified at 17 CFR 240.17g–10 and Form ABS Due Diligence 15E would be identified in the Code of Federal Regulation at 17 CFR 249b.400.

[512] *See* proposed new paragraph (a)(2) of Rule 17g–7.

[513] 15 U.S.C. 78o–7(s)(4)(B).

[514] 17 CFR 240.17g–5(a)(3).

implement Section 15E(s)(4)(A) of the Exchange Act, which requires that an issuer or underwriter of any Exchange Act-ABS make publicly available the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter.[515] The Commission previously proposed to implement Section 15E(s)(4)(A) of the Exchange Act as part of a set of rules proposed to implement Section 945 of the Dodd-Frank Act.[516] Under those proposals, an issuer of a registered Exchange Act-ABS offering would have been required to disclose the findings and conclusions of any third party engaged to perform a review obtained by the issuer, as required by Section 15E(s)(4)(A), in the prospectus.[517] In the case of unregistered Exchange Act-ABS offerings, the Commission proposed new Rule 15Ga–2.[518] This rule would have required an issuer of Exchange Act-ABS to file a new Form ABS–15G to disclose the findings and conclusions of any third-party engaged to perform a review obtained by an issuer with respect to unregistered transactions.[519] Proposed Rule 15Ga–2 also would have required an underwriter of Exchange Act-ABS to file Form ABS–15G with the same information for reports obtained by an underwriter in registered and unregistered transactions.[520] Finally, proposed Form ABS–15G would have been required to be filed with the Commission on EDGAR five business days prior to the first sale of the offering.[521]

With respect to these proposals, the Commission requested comment on, among other things, whether rules implementing Section 15E(s)(4)(A) of the Exchange Act should be part of a later rulemaking under Section 15E.[522] Some commenters stated that Section 15E(s)(4) should be read as a whole, and that it would be inappropriate to consider subsection (A) alone.[523] These commenters suggested postponing implementation of Section 15E(s)(4)(A) until the Commission implements Section 15E(s)(4)(B), (C) and (D).[524] These commenters argued that Rule 15Ga–2, as proposed, would have "construe[d] Section 15E(s)(4)(A) in a vacuum, divorced from Congress' intent to regulate NRSROs and the credit ratings process."[525] These commenters also argued that proposed Rule 15Ga–2 was inappropriately broad. One such commenter suggested that Rule 15Ga–2 be modified to apply only to any third-party due diligence report prepared for an issuer or underwriter of Exchange Act-ABS specifically for the purpose of having the issuer or underwriter share the report with an NRSRO issuing a credit rating for the securities.[526]

In January 2011, the Commission adopted rules implementing Section 7(d) of the Securities Act and, at the same time, deferred action on implementing Section 15E(s)(4)(A).[527] After considering the comment letters relating to Section 15E(s)(4)(A), the Commission is re-proposing Rule 15Ga–2 with revisions.[528] As proposed in October 2010, Rule 15Ga–2 would have required issuers and underwriters of Exchange Act-ABS to file Form ABS–15G containing, or provide prospectus disclosure with respect to, the findings and conclusions of any report of a third-party engaged for purposes of performing a review of the pool assets obtained by the issuer or underwriter.[529] As noted above, the Commission included this proposal in the context of rulemaking with respect to issuer review of assets required by Section 7(d) of the Securities Act.[530]

After reviewing the comments, the Commission now believes that Section 15E(s)(4)(A) of the Exchange Act, when considered in the context of Sections 15E(s)(4)(B), (C) and (D), should be interpreted more narrowly to relate to those provisions.[531] Therefore, as re-proposed, Rule 15Ga–2 would require an issuer or underwriter of any Exchange Act-ABS that is to be rated by an NRSRO to furnish a Form ABS–15G on the EDGAR system containing the findings and conclusions of any third-party "due diligence report" obtained by the issuer or underwriter.[532] The rule would define "due diligence report" as any report containing findings and conclusions relating to "due diligence services" as defined in proposed new Rule 17g–10 discussed below in Section II.H.2 of this release. Under the re-proposal, the disclosure would be furnished using Form ABS–15G for both registered and unregistered offerings of Exchange Act-ABS.[533] Thus, unlike the October 2010 proposal, discussed above, issuers in registered Exchange Act-ABS offerings would not be required to include the disclosure in their prospectuses.

In addition, under the Commission's re-proposal, an issuer or underwriter would not need to furnish Form ABS–15G if the issuer or underwriter obtains a representation from each NRSRO engaged to produce a credit rating for the Exchange Act-ABS that can be reasonably relied on that the NRSRO will publicly disclose the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter with the publication of the credit rating five business days prior to the first sale in the offering in an information disclosure form generated pursuant to proposed new paragraph

[515] *See* 15 U.S.C. 78o–7(s)(4)(A).

[516] *See Issuer Review of Assets in Offerings of Asset-Backed Securities,* Securities Act Release No. 9150 (Oct. 13, 2010), 75 FR 64182 (Oct. 19, 2010). In the same release in which the Commission proposed to implement Section 15E(s)(4)(A), the Commission also proposed to implement Section 7(d) of the Securities Act (15 U.S.C. 77g(d)), as added by Public Law 111–203 § 945. Section 7(d) of the Securities Act requires the Commission to adopt rules that, with respect to a registration statement for an asset-backed security, will require the issuer of the security to: (1) Perform a review of the assets underlying the asset-backed security; and (2) disclose the nature of the review. *See* 15 U.S.C. 77g(d)(1) and (2). The Commission implemented this provision by adopting new rule 17 CFR 230.193 ("Rule 193") and amendments to 17 CFR 229.1111 ("Item 1111 of Regulation AB"). *See Issuer Review of Assets in Offerings of Asset-Backed Securities,* Securities Act Release No. 9176 (Jan. 20, 2011), 76 FR 4231 (Jan. 25, 2011).

[517] *See Issuer Review of Assets in Offerings of Asset-Backed Securities,* 75 FR at 64188–64190 (Oct. 19, 2010).

[518] *Id.*

[519] *Id.*

[520] *Id.*

[521] *Id.*

[522] *Id.*

[523] *See* comment letters from American Bar Association ("ABA"); National Association of Bond Lawyers ("NABL") (responding to *Issuer Review of Asset in Offerings of Asset-Backed Securities,* 75 FR 64182 (Oct. 19, 2010)). The comment letters are available at *http://sec.gov/comments/s7–26–10/s72610.shtml.*

[524] *See* comment letters from ABA and NABL.

[525] *See* comment letters from ABA and NABL.

[526] *See* comment letter from ABA.

[527] *See Issuer Review of Assets in Offerings of Asset-Backed Securities,* 76 FR 4231 (Jan. 25, 2011). Although the Commission deferred action on implementing Section 15E(s)(4)(A), the Commission adopted, in a separate release, new Form ABS–15G to implement Section 943 of the Dodd-Frank Act. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR 4489 (Jan. 26, 2011).

[528] *See* proposed new Rule 15Ga–2. The Commission also is proposing conforming amendments to Form ABS–15G.

[529] *See Issuer Review of Assets in Offerings of Asset-Backed Securities,* 75 FR at 64188–64190 (Oct. 19, 2010).

[530] *See Issuer Review of Assets in Offerings of Asset-Backed Securities,* 76 FR 4231 (Jan. 25, 2011).

[531] *See* 15 U.S.C 78o–7(s)(4)(A) through (D), which relate to due diligence performed by third-parties with respect to Exchange Act-ABS.

[532] *See* proposed new Rule 15Ga–2 and conforming changes to Form ABS–15G. For purposes of this rule, consistent with the definition of "issuer" in proposed new Rule 17g–10, the issuer is the depositor or sponsor that participates in the issuance of Exchange Act-ABS. *See* discussion below in Section II.H.2 of this release.

[533] The Commission is proposing that the form be deemed "furnished" rather than "filed" for purposes of Section 18 of the Exchange Act (15 U.S.C. 78r) and the liabilities of that section, unless the issuer specifically states that the form be considered "filed" under the Exchange Act or incorporates it by reference into a filing under the Securities Act or the Exchange Act.

(a)(1) of Rule 17g–7.[534] As discussed above in Section II.G.3 of this release, proposed new paragraph (a)(1)(ii)(F) of Rule 17g–7 would implement Section 15E(s)(3)(A)(v) of the Exchange Act by requiring an NRSRO to disclose in the form whether and to what extent third-party due diligence services were used by the NRSRO, a description of the information that such third party reviewed in conducting due diligence services, and a description of the findings or conclusions of such third-party. In addition, as discussed below in Section II.H.3 of this release, the Commission is proposing that the certification a provider of third-party due diligence services would need to provide to an NRSRO producing a credit rating for an Exchange Act-ABS pursuant to Section 15E(s)(4)(B) and (C) include a summary of the findings and conclusions of the provider of third-party due diligence services.[535] And, as discussed above in Section II.G.5 of this release, an NRSRO would be required to include the certification with the publication of the credit rating.[536]

For these reasons, having the issuer and underwriter publicly disclose the same information an NRSRO must, when applicable, disclose pursuant to proposed new paragraphs (a)(1)(ii)(F) and (a)(2) of Rule 17g–7 with the publication of a credit rating would be redundant. Moreover, as discussed earlier, potential investors in Exchange Act-ABS may be accustomed to receiving and reviewing expected or preliminary credit ratings issued by NRSROs prior to making an investment decision and proposed new paragraph (a) of Rule 17g–7 would require the form and any certifications to be included with the issuance of such credit ratings. Therefore, the Commission believes that an effective means of disseminating this information to investors and other users of credit ratings would be to include it with the publication of the credit rating. Also, because the form would contain substantial additional information, consolidating the information in one disclosure would benefit investors and other users of credit ratings.

As noted above, the issuer or underwriter would not need to furnish Form ABS–15G if it obtained a representation from each NRSRO engaged to produce a credit rating upon which the issuer or underwriter could reasonably rely.[537] The Commission preliminarily recognizes, however, that there may be instances where, notwithstanding an issuer's or underwriter's reasonable reliance on a representation by an NRSRO engaged to produce a credit rating to publicly disclose the required information, the NRSRO fails to make such information publicly available in its information disclosure form pursuant to proposed Rule 17g–7(a)(1) five business days prior to the first sale in the offering.[538] Therefore, the Commission proposes to require that an issuer or underwriter furnish, two business days prior to the first sale in the offering, Form ABS–15G with the information required by proposed Rule 15Ga–2 if the NRSRO fails to comply with its representation to make such information publicly available in an information disclosure form generated pursuant to proposed paragraph (a)(1) of Rule 17g–7 five business days prior to the first sale in the offering. Under the proposal, issuers or underwriters would be permitted to reasonably rely on a representation by an NRSRO to meet their obligation to publicly disclose the information required to be provided in Form ABS–15G. However, they would continue to be responsible for furnishing Form ABS–15G two business days prior to the first sale in the offering if the NRSRO does not publicly disclose the information five business days prior to the first sale in the offering.

This "reasonable reliance" provision would parallel requirements in paragraph (a)(3) of Rule 17g–5 that require an NRSRO to obtain certain representations from arrangers of structured finance products that hire the NRSRO to determine a credit rating for the structured finance product.[539] When adopting this requirement the Commission stated, "The question of whether reliance was reasonable will depend on the facts and circumstances of a given situation."[540] The Commission further stated, "The factors relevant to this analysis would include, but not be limited to: (1) Ongoing or prior failures by the arranger to adhere to the representations; or (2) a pattern of conduct by the arranger where it fails to promptly correct breaches of its representations."[541] The Commission preliminarily believes that the same would hold true with respect to relying on the representations from NRSROs obtained for the purposes of proposed Rule 15Ga–2.

The Commission notes that Rule 193, adopted to implement Section 7(d) of the Securities Act, requires issuers of registered Exchange Act-ABS to perform a review of the pool assets underlying the asset-backed security.[542] This review must be designed and effected to provide reasonable assurance that the prospectus disclosure regarding the pool assets is accurate in all material respects.[543] Although third-party due diligence reports may be relevant to the review, neither Section 7(d) of the Securities Act nor Rule 193 ties the review to third-party due diligence reports.[544] Rule 193 permits, though does not require, an issuer to rely on one or more third parties to fulfill its obligation to perform the required review.[545]

The Commission recognizes Exchange Act-ABS issuers may routinely hire third-parties to conduct various types of reviews and believes that issuers may employ third parties to assist in satisfying their obligations to perform a review under Rule 193.[546] The Commission also recognizes that an issuer of Exchange Act-ABS may obtain a third-party due diligence report from a third party the issuer has engaged to assist in performing its Rule 193 review. Nonetheless, the Commission believes that the third-party due diligence reports referenced in Section 15E(s)(4) of the Exchange Act are not the same as the review required by Section 7(d) of the Securities Act and Rule 193.[547] Instead, Section 15E(s)(4) of the Exchange Act and, consequently, proposed Rule 15Ga–2 relate to a

[534] *See* 15 U.S.C. 78o–7(s)(3)(A)(v). In this context, the Commission preliminarily believes that the term "publicly disclose" means make the findings and conclusions readily available to any users of credit ratings. Consequently, an NRSRO that agreed to make the findings and conclusions available only to its subscribers or prospective investors in the Exchange Act-ABS would not satisfy this proposed requirement.

[535] *See* Item 5 of proposed new Form ABS Due Diligence-15E.

[536] *See* proposed new paragraph (a)(2) of Rule 17g–7.

[537] The issuer or underwriter would be required to provide to the Commission, upon request, information regarding the manner in which it obtained the representation. The Commission notes that in most cases the NRSROs likely would have an independent obligation to disclose the information pursuant to the proposed amendments to Rule 17g–7 and proposed new Rule 17g–10 and Form ABS Due Diligence-15E.

[538] The NRSRO's failure to disclose the certification would be a violation of proposed paragraph (a) of Rule 17g–7.

[539] *See* 17 CFR 17g–5(a)(3); *see also Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63844–63850 (Dec. 4, 2009).

[540] *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63847 (Dec. 4, 2009).

[541] *Id.*

[542] *See* 17 CFR 230.193.

[543] *Id.*

[544] *See* 15 U.S.C. 77g(d) and 17 CFR 230.193.

[545] *Id.*

[546] The Commission also notes that an issuer may rely on multiple third-parties to fulfill its Rule 193 review obligation, provided the issuer complies with the requirements of Rule 193 for each third party.

[547] *Compare* 15 U.S.C. 77g(d) and 17 CFR 230.193, *with* 15 U.S.C. 78o–7(s)(4).

particular type of report that is relevant to the determination of a credit rating by an NRSRO. By contrast, Section 7(d) of the Securities Act and Rule 193 relate to a more general concept of an issuer review of the assets underlying an Exchange Act-ABS, one aspect of which may (or may not) include a third-party due diligence report. As a result, the treatment of due diligence reports under proposed Rule 15Ga–2 is not predicated on the use of third-party due diligence services to assist with reviews under Rule 193.[548] For these reasons, the Commission also is proposing that Rule 15Ga–2 apply only with respect to Exchange-Act ABS that are to be rated by an NRSRO.[549]

As noted above, the disclosure required by proposed Rule 15Ga–2 would be required to be provided in Form ABS–15G. Unlike the first proposal, the Commission now proposes to require issuers in registered Exchange Act-ABS transactions to include the disclosure required by proposed Rule 15Ga–2 in Form ABS–15G, rather than in the prospectus. Whether the findings and conclusions of a third-party are part of the Rule 193 review and, therefore, included in the prospectus disclosure is dictated by the requirements of Rule 193 and Item 1111 of Regulation AB.[550] The Commission is not proposing to separately require that disclosure provided in connection with Rule 15Ga–2 regarding any third-party due diligence report be provided in the prospectus for a registered offering, because the information required by proposed Rule 15Ga–2 only pertains to the findings and conclusions of a third-party due diligence report relevant to the determination of a credit rating.

As stated above, Section 15E(s)(4)(A) applies to issuers and underwriters of both registered and unregistered offerings of Exchange Act-ABS. Thus, proposed Rule 15Ga–2 would apply to a municipal entity that sponsors or issues Exchange Act-ABS ("municipal Exchange Act-ABS") or an underwriter of municipal Exchange Act-ABS, if the municipal entity or underwriter of the offering obtains a third-party due-diligence report, as defined by the proposed rule, and the municipal Exchange Act-ABS is to be rated by an NRSRO. Since Section 15E(s)(4) relates to oversight of NRSROs, commenters to the first proposal noted that a significant difference between municipal Exchange Act-ABS and more typical Exchange Act-ABS is that the Municipal Securities Rulemaking Board[551] collects and publicly disseminates market information and information about municipal securities issuers and offerings on its centralized public database, the Electronic Municipal Market Access system ("EMMA").[552] Consistent with suggestions from commenters and the Commission's approach in implementing Section 943 of the Dodd-Frank Act,[553] the Commission proposes to permit municipal securitizers of Exchange Act-ABS, or underwriters in the offering, to provide the information required by Form ABS–15G on EMMA.[554] The Commission believes this would limit the cost and burden on issuers and underwriters of municipal Exchange Act-ABS subject to the new rule, as well as provide the disclosure for investors in the same location as other disclosures regarding municipal ABS. Since Section 15E(s)(4) relates to oversight of NRSROs and the ratings process, the Commission preliminarily believes it is not appropriate to exempt any particular issuers if they receive a rating for the securities.[555]

The Commission recognizes that public disclosure of information relating to an unregistered Exchange Act-ABS offering could raise concerns regarding the reliance by an issuer or underwriter on the private offering exemptions and safe harbors under the Securities Act.[556] As noted above, the Commission intends for Form ABS–15G to be used for both registered and unregistered ABS offerings. The Commission is of the view that issuers and underwriters can disclose information required by Rule 15Ga–2 without jeopardizing reliance on those exemptions and safe harbors, provided the only information made publicly available on the form is that which is required by the proposed rule, and the issuer does not otherwise use Form ABS–15G to offer or sell securities in a manner that conditions the market for offers or sales of its securities.[557]

The Commission is proposing that the disclosures—whether made by the engaged NRSROs or the issuer or underwriter—be made five business days prior to the first sale of the offering. Since the form an NRSRO would be required to include with a credit rating pursuant to proposed new paragraph (a) of Rule 17g–7 would not be required to be filed with the Commission, the Commission believes it would be consistent to permit issuers and underwriters to furnish, rather than file, Form ABS–15G. The Commission proposes that Form ABS–15G be signed by the senior officer of the depositor in charge of securitization, if the form were provided to include the findings and conclusions of a third-party hired by the

[548] The Commission does not intend for all third-parties from whom the issuer obtains a third-party due diligence report, as defined in proposed Rule 15Ga–2, to be named in the registration statement and consent to being named as an expert, in accordance with the requirements in Rule 193, solely because an issuer files Form ABS–15G. If the issuer's prospectus disclosure attributes the findings and conclusions of the Rule 193 review to the third-party from whom it obtains a third-party due diligence report, however, the third-party would be required to be named in the registration statement and consent to being named as an expert in accordance with Rule 436 under the Securities Act.

[549] *See* proposed new Rule 15Ga–2.

[550] *See* 17 CFR 230.193 and 17 CFR 229.1111.

[551] The MSRB, a self-regulatory organization subject to oversight by the Commission, regulates securities firms and banks that underwrite, trade and sell municipal securities.

[552] *See* comment letters from Minnesota Housing Finance Agency, NABL, and the National Council of State Housing Agencies (responding to proposals in *Issuer Review of Assets in Offerings of Asset-Backed Securities,* 75 FR 64182 (Oct. 19, 2010)).

[553] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR 4489 (Jan. 26, 2011).

[554] *See* proposed amendments to Rule 314 of Regulation S–T. 17 CFR 232.314. A municipal securitizer is defined as a securitizer (as that term in defined in Section 15(G)(a) of the Exchange Act (__ U.S.C. ___)) that is any State or Territory of the United States, the District of Columbia, any political subdivision of any State, Territory, or the District of Columbia, or any public instrumentality of one or more States, Territories, or the District of Columbia.

[555] As noted earlier, the Commission is soliciting comment in Section II.M.4.a of this release with respect Items 6 and 7 of Form NRSRO about how certain types of obligors, securities, and money market instruments should be classified for purposes of providing the approximate number of credit ratings outstanding in each class of credit rating for which an applicant is seeking registration (Item 6) or an NRSRO is registered (Item 7). In this regard, the Commission solicits comment on whether municipal structured finance issuers should be classified as (1) issuers of asset-backed securities identified in Section 15E(a)(62)(A)(iv) of the Exchange Act as broadened to include any rated security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction; or (2) issuers of government securities, municipal securities, or securities issued by a foreign government identified in Section 15E(a)(62)(A)(v) of the Exchange Act. The Commission is requesting comment on this matter with respect to disclosing the number of credit ratings outstanding in a particular class of credit ratings in Form NRSRO (and potentially for purposes of the proposed amendments to Exhibit 1 to Form NRSRO and the disclosure of information about the histories of credit ratings under proposed new paragraph (b) of Rule 17g–7). The Commission, in seeking comment on these matters, is not suggesting an issuer of municipal Exchange Act-ABS should be exempt from requirements in the securities laws that apply to Exchange Act-ABS because it might appropriately be classified as an issuer of government securities, municipal securities, or securities issued by a foreign government identified in Section 15E(a)(62)(A)(v) of the Exchange Act for purposes of Items 6 and 7 of Form NRSRO.

[556] *See* 15 U.S.C. 77d(2), 17 CFR 230.144A, and 17 CFR 230.501–508.

[557] Furnishing proposed Form ABS–15G would not foreclose the reliance of an issuer on the private offering exemption in the Securities Act and the safe harbor for offshore transactions from the registration provisions in Section 5. 15 U.S.C. 77e.

issuer. The Commission believes that requiring the senior officer of the depositor in charge of securitization to sign the form is consistent with other signature requirements for filings relating to Exchange Act-ABS.[558] If the form included the findings and conclusions of a third-party engaged by the underwriter, then the form would be signed by a duly authorized officer of the underwriter. The Commission believes that requiring Form ABS–15G be signed by a duly authorized officer of the underwriter would provide an incentive for the person who signs the form to review it for accuracy.

Request for Comment

The Commission generally requests comment on all aspects of proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G. The Commission also seeks comment on the following:

1. Is proposed Rule 15Ga–2 appropriate? Is the proposed definition of "third-party due diligence report" appropriate? Is there an alternative definition that would be consistent with the requirements of Section 15E(s)(4)?

2. The Commission is proposing to require disclosure regarding the findings and conclusions of third-party due diligence reports for both registered and unregistered transactions. Is there any reason Section 15E(s)(4)(A) of the Exchange Act should not apply to both registered and unregistered Exchange Act-ABS transactions? If the requirement applies to both registered and unregistered transactions, should the universe of Exchange Act-ABS offerings that would be subject to the requirement be defined, as proposed, as an offering of Exchange Act-ABS, as that term is defined in Section 3(a)(77) of the Exchange Act?

3. Proposed Rule 15Ga–2 would apply only if the Exchange Act-ABS is to be rated by a NRSRO. Is that appropriate?[559] Why or why not?

4. Should the Commission exempt any issuers, underwriters or other parties from this requirement? As proposed, Rule 15Ga–2 would apply to issuers and underwriters of Exchange Act-ABS that are exempted securities as defined in Section 3(a)(12) of the Exchange Act, including government securities and municipal securities. Should issuers or underwriters of such exempted securities be exempt from this provision?[560] Is the proposed accommodation for municipal Exchange Act-ABS appropriate?

5. Is the proposal to not require the issuer or underwriter to furnish Form ABS–15G if it obtains the necessary representations from the NRSROs engaged to produce credit ratings for the Exchange Act-ABS appropriate? For example, would investors and other users of credit ratings benefit from having issuers and underwriters *and* NRSROs disclose the findings and conclusions of the provider of third-party due diligence services? In addition, would NRSROs engaged to determine a credit rating for an Exchange Act-ABS agree to make the disclosure? Could potential concerns among NRSROs about making the disclosure be addressed by permitting them to rely on the disclosure the provider of third-party due diligence services would need to make about the findings and conclusions of the review in Item 5 of proposed new Form Due Diligence-15E discussed below in Section II.H.3 of this release?

Under proposed Rule 15Ga–2, an issuer or underwriter would not be required to furnish Form ABS–15G if it receives a representation from an NRSRO that can be reasonably relied upon that the NRSRO will publicly disclose the required information five business days prior to the first sale in the offering in an information disclosure form generated pursuant to Rule 17g–7(a)(1). Should the Commission, as proposed, also require an issuer or underwriter to furnish Form ABS–15G if the NRSRO fails to publicly disclose in an information disclosure form the required disclosure five business days prior to the first sale in the offering? If so, should the issuer or underwriter be required, as proposed, to furnish Form ABS–15G two business days prior to the first sale in the offering? Should the requirement instead be three days before? Alternatively, should the Commission require that the issuer or underwriter wait another five business days after furnishing Form ABS–15G before the first sale? If not, how long in advance of the first sale should issuers or underwriters be required to furnish Form ABS–15G? Should an issuer or underwriter not be required to furnish Form ABS–15G two business days prior to the first sale in the offering if the NRSRO fails to publicly disclose the required information five business days prior to the first sale, but does publicly disclose the information on the fourth or third business day prior to the first sale since an issuer's or underwriter's furnishing in that case would result in duplicative disclosure? If so, how could an NRSRO be properly incentivized to publicly disclose the required information five business days prior to the first sale in the offering?

6. Does the proposal to require an issuer or underwriter to furnish Form ABS–15G in the event that the NRSRO fails to fulfill its representation offset the effectiveness or benefit of the proposal to permit issuers and underwriters to reasonably rely on a representation from an NRSRO?

7. Under the proposal, the issuer or underwriter would be required to provide to the Commission, upon request, information regarding the manner in which it obtained the representation of the NRSRO engaged to produce credit ratings. Are there any other provisions that should be added to ensure compliance with the proposal not to require the issuer or underwriter to furnish Form ABS–15G if it obtains the necessary representations from the NRSRO?

8. Are there other appropriate means of making the findings and conclusions of third-party due diligence reports "publicly available" as required by Section 15E(s)(4)(A) of the Exchange Act? Is furnishing information regarding the findings and conclusions of the report of the provider of third-party due diligence services on proposed Form ABS–15G on EDGAR (except with respect to offerings of municipal Exchange Act-ABS) an appropriate way for issuers in unregistered offerings and for underwriters in registered and unregistered offerings to make this information publicly available? Should the Form ABS–15G be required to be filed instead?

9. Would the proposed requirement that Form ABS–15G be furnished five business days prior to first sale provide investors with sufficient time to review the findings and conclusions contained therein? Would it provide NRSROs with sufficient time to take the included information into account in determining a rating? If not, what would be a more appropriate deadline and why? Are five business days also appropriate in

[558] *See, e.g.,* signature requirement for Form 10–K (17 CFR 249.312). It is also consistent with the Commission's proposed signature requirements for the registration statements for offerings of asset-backed securities. *See Asset-Backed Securities,* 75 FR 23328 (May 3, 2010).

[559] For example, Fannie Mae and Freddie Mac are government sponsored enterprises ("GSEs") that purchase mortgage loans and issue or guarantee mortgage-backed securities. Mortgage-backed securities issued or guaranteed by these GSEs have been, and continue to be, exempt from registration under the Securities Act and reporting requirements under Sections 13 or 15 of the Exchange Act. These securities have not been, and are not currently, rated by credit rating agencies.

[560] Exchange Act "exempted securities" include government securities and municipal securities, as defined under the Exchange Act. For example, mortgage-backed securities issued by the Government National Mortgage Association are fully modified pass-through securities guaranteed by the full faith and credit of the United States government. *See http://www.ginniemae.gov/.*

unregistered offerings? Is there reason to require a different number of days in unregistered offerings?

10. Is the proposed signature requirement for Form ABS–15G appropriate? Is it necessary? Conversely, are there other appropriate individuals that are better suited to sign the form?

11. Should issuers of registered Exchange Act-ABS offerings be required to furnish the information required by proposed Rule 15Ga–2 on Form ABS–15G and not be required to provide the information in a prospectus that is filed with the Commission, as proposed? Why or why not?

2. Proposed New Rule 17g–10

As noted above, Section 15E(s)(4)(C) of the Exchange Act provides that the Commission shall establish the appropriate format and content for the written certifications required under Section 15E(s)(4)(B), to ensure that providers of due diligence services have conducted a thorough review of data, documentation, and other relevant information necessary for an NRSRO to provide an accurate rating for an Exchange Act-ABS.[561] The Commission preliminarily believes providers of third-party due diligence services most commonly are hired by issuers and underwriters to perform reviews of pools of mortgages that will be securitized into an RMBS; accordingly, the following discussion of proposed Rule 17g–10 and Form ABS Due Diligence–15E centers on RMBS.[562] The proposed rule and form, however, would apply to all Exchange Act-ABS. Generally, in the RMBS context, the provider of third-party due diligence services is hired by the entity (*e.g.,* the underwriter, sponsor, or depositor) purchasing the pool of mortgage loans for the purpose of securitizing them.[563] In conducting a review, the provider of third-party due diligence services analyzes a sample (for example, 25%) of the loans in the pool for one or more of the following purposes: (1) To assess the quality of the loan-by-loan data in the electronic file ("loan-tape") that aggregates the information for the pool by comparing the information on the loan tape for each loan in the sample with the information contained on the hard-copy documents in the loan file; (2) to determine whether each loan in the sample adheres to the underwriting guidelines of the loan originator; (3) to assess the validity of the appraised value of the property indicated on the loan tape that collateralizes each loan in the sample; and (4) to determine whether the originator complied with Federal, state, and local laws in making each loan in the sample. The NRSROs most active in rating RMBS have incorporated requirements for the engagement of providers of third-party due diligence services by the entities requesting such ratings (for example, the underwriter or sponsor of the RMBS) into their procedures and methodologies for determining RMBS credit ratings.[564] Moreover, the procedures and methodologies of these NRSROs prescribe the minimum scope and manner of the review of the provider of third-party due diligence services necessary to obtain a credit rating for the RMBS, including the minimum sample size of the loans to be selected from the pool.[565]

To implement the rulemaking mandated by Section 15E(s)(4)(C) of the Exchange Act, the Commission is proposing new Rule 17g–10 and related Form ABS Due Diligence–15E.[566] Proposed new Rule 17g–10 would contain three paragraphs: (a), (b) and (c).[567] Proposed paragraph (a) would provide that the written certification required pursuant to Section 15E(s)(4)(B) of the Exchange Act must be on Form ABS Due Diligence–15E.[568] In other words, a provider of third-party due diligence services would need to use Form ABS Due Diligence–15E to meet the requirement in Section 15E(s)(4)(B) of the Exchange Act.[569]

Proposed paragraph (b) of new Rule 17g–10 would provide that the written certification must be signed by an individual who is duly authorized by the person providing the third-party due diligence services to make such a certification.[570] This proposal is designed to ensure that the person executing the certification on behalf of the provider of third-party due diligence services has responsibilities that will make the person aware of the basis for the information being provided in the form. This proposed requirement parallels paragraph (b) of Rule 17g–3, which requires an NRSRO to attach to the financial reports required by that rule a signed statement by a duly authorized person associated with the NRSRO stating, among other things, that the person has responsibility for the financial reports.[571]

Proposed paragraph (c) of new Rule 17g–10 would contain four definitions to be used for the purposes of Section 15E(s)(4)(B) and Rule 17g–10.[572] Proposed paragraph (c)(1) would define the meaning of "due diligence services."[573] The Commission preliminarily believes such a definition is necessary because, while the requirements of Section 15E(s)(4)(B) are triggered, among other things, by providing due diligence services, the Dodd-Frank Act does not define the type of activities that constitute "due diligence services" in the Exchange Act-

[561] *See* 15 U.S.C. 78o–7(s)(4)(C).

[562] *See, e.g.,* Testimony of Vicki Beal, Senior Vice President, Clayton Holdings, before the Financial Crisis Inquiry Commission (Sept. 23, 2010).

[563] *Id.*

[564] *See, e.g., US RMBS Ratings Criteria,* Fitch, Inc. ("Fitch") (Dec. 3, 2009) ("In addition to Fitch's originator/issuer review and ResiLogic loan-level asset analysis of the mortgage pool, Fitch will require third-party loan-level reviews on all residential mortgage pools that Fitch is asked to rate. The reviews will be conducted by a "due diligence" company (review company) prior to Fitch providing a rating on the transaction."); *Criteria for Evaluating Independent Third-Party Loan Level Reviews for US RMBS,* Moody's Investors Service, Inc. ("Moody's") (Nov. 24, 2008) ("Moody's will not rate a transaction unless it has received a report from the third-party review firm as to the TPR scope, procedure and findings. The report must include a narrative summary of the review and an initial TPR findings report."); *Incorporating Third-Party Due Diligence Results Into The U.S. RMBS Rating Process,* Standard & Poor's Ratings Services ("S&P") (Nov. 25, 2008) ("Standard & Poor's believes that using third-party due diligence results in our rating analysis will increase transparency and strengthen the rating process. Our due diligence review ratings criteria will be effective Dec. 1, 2008, and are intended to increase our insight into the quality and validity of the information used to originate the mortgage loans pooled into securities.").

[565] For example, for established originators and loan programs, Fitch requires the randomly selected minimum sample size to be the larger of 200 loans or 10% of the pool for prime loans and the larger of 400 loans or 20% of the pool for Alt-A/subprime and all other product types. Moreover, if originators or their loan programs have had less than two years of performance history, Fitch requires that the sample size should be doubled. Moody's defines its minimum sample size through statistical techniques. Specifically, Moody's requires that the sample size must not be less than that computed using a 95% confidence level, a 5% precision level, and an assumed error rate equal to the higher of the historic error rate for the originator or a Minimum Assumed Error Rate. S&P requires a sample that is the greater of either the number of loans needed for a statistically valid sample, or a 10% random sample for subprime and 5% sample for prime. At a minimum, S&P states that the number of loans in the sample should be 200 for subprime, and 100 for prime. S&P defines a statistically valid sample as the number of loans based on a 5% one-tailed level of significance with a 2% level of precision. S&P also expects that the number of loans in the sample also will be a function of an estimate of an error rate.

[566] *See* proposed new Rule 17g–10 and new Form ABS Due Diligence–15E.

[567] *See* proposed paragraphs (a), (b) and (c) of Rule 17g–10.

[568] *See* proposed paragraph (a) of new Rule 17g–10.

[569] *See* 15 U.S.C. 78o–7(s)(4)(B) and proposed paragraph (a) of new Rule 17g–10.

[570] *See* proposed paragraph (b) of Rule 17g–10.

[571] *See* 17 CFR 240.17g–3(b).

[572] *See* proposed paragraph (c) of new Rule 17g–10 and 15 U.S.C. 78o–7(s)(4)(B).

[573] *See* proposed paragraph (c)(1) of new Rule 17g–10.

ABS context.[574] Consequently, the Commission preliminarily believes a definition would provide guidance to those entities providing due diligence services as to when the requirements of the statute and proposed new Rule 17g–10 would apply. In addition, a definition could help avoid overly broad interpretations of the meaning of "due diligence services" that cause entities not providing due diligence services to needlessly provide certifications to NRSROs.

The Commission intends the definition of "due diligence services" in the Exchange Act-ABS context to cover services provided by entities typically considered to be providers of third-party due diligence services in the securitization market and does not intend it to cover every type of person that might perform some type of diligence in the offering process. As discussed below, the Commission believes that the scope of Section 15E(s)(4)(A) is intended to address third-party due diligence reports obtained by issuers or underwriters from these specialized providers of due diligence services that are relevant to the determination of a credit rating for an Exchange Act-ABS by an NRSRO.

The Commission preliminarily believes, as discussed above, there are four categories of reviews undertaken by entities commonly understood as providers of third-party due diligence services for issuances of RMBS that NRSROs have deemed relevant for determining credit ratings for such Exchange Act-ABS.[575] Consequently, the proposed definition would identify each of the four categories. In addition, because the Commission's understanding of due diligence services largely is based on such services as applied to pools of mortgage loans, the Commission is proposing a catchall component to the proposed definition.[576] The proposed catchall would be designed to apply to due diligence services used for pools of other asset classes (*e.g.,* commercial loans, corporate loans, student loans, or credit card receivables) to the extent that providers of third-party due diligence services currently provide or in the future begin providing due diligence services with respect to other asset classes and those services, because of the different nature of the assets, do not fall into one of the four other categories.

Under the Commission's proposed definition of "due diligence services," an entity would be deemed to have provided "due diligence services" if it engaged in a review of the assets underlying an Exchange Act-ABS for the purpose of making findings with respect to any one of the five types of activities identified in proposed paragraphs (c)(1)(i) through (v) of new Rule 17g–10 (*i.e.,* the components of the proposed definition would be disjunctive).[577] The first category of "due diligence service" would be identified in proposed paragraph (c)(1)(i) of new Rule 17g–10 as a review of the assets underlying an Exchange Act-ABS for the purpose of making findings with respect to the quality or integrity of the information or data about the assets provided, directly or indirectly, by the securitizer or originator of the assets.[578] This type of review could entail comparing the data on loan-tape with the data on the hard-copy documentation in an underlying sampled loan file to verify that the loan-tape data matches and correctly represents the content of the loan file under review.[579] The provider of due diligence services would need to note any differences (exceptions) between the loan-tape data and the information in the loan file. This type of review also could entail verifying that the loan-tape contains all the information about the underlying assets the NRSRO requires for the purpose of determining a credit rating and whether that information is presented in the format required by the NRSRO.[580] For example, some NRSROs may specify items of data ("data fields") about a mortgage loan that must be included on the loan tape for an RMBS such as occupancy status, property type, loan purpose, documentation type, current FICO score of the borrower, combined original loan to value ratio, total debt-to-income ratio, and zip code of the residence.[581]

The second category of "due diligence service" would be identified in proposed paragraph (c)(1)(ii) of new Rule 17g–10 as a review of the assets underlying an Exchange Act-ABS for the purpose of making findings with respect to whether the origination of the assets conformed to stated underwriting or credit extension guidelines, standards, criteria, or other requirements.[582] This type of review could entail reviewing whether a sampled loan meets the originator's underwriting guidelines or, if not, that the originator provided a reasonable and documented exception to support the decision to make the loan.[583] This type of review also could entail how the originator verified information in a sampled loan underlying an RMBS such as the borrower's occupancy status with respect to the residence (*e.g.,* primary residence, second home, or rental property), the borrower's income, the borrower's assets, and the borrower's employment status.[584]

The third category of "due diligence service" would be identified in proposed paragraph (c)(1)(iii) of new Rule 17g–10 as a review of the assets underlying an Exchange Act-ABS for the purpose of making findings with respect to the value of collateral securing such assets.[585] This type of review could entail analyzing how the originator verified the value of the asset. For example, for an RMBS, an NRSRO might require that the review consider the quality of the appraiser of the property and the quality of the appraisal.[586] This could include reviewing whether the appraiser used a valuation model.[587] It also could require the provider of third-party due diligence services to separately use a valuation model if the reviewer believes that the original appraised value of the property is less than the value presented by the originator.[588]

The fourth category of "due diligence service" would be identified in proposed paragraph (c)(1)(iv) of new Rule 17g–10 as a review of the assets underlying an Exchange Act-ABS for the purpose of making findings with respect to whether the originator of the assets complied with Federal, state, or local laws or regulations.[589] This type of review could entail—with respect to an RMBS—analyzing legal documentation

[574] *See* 15 U.S.C. 78o–7(s)(4)(B).

[575] *See, e.g., US RMBS Ratings Criteria,* Fitch (Dec. 3, 2009), *Criteria for Evaluating Independent Third-Party Loan Level Reviews for US RMBS,* Moody's (Nov. 24, 2008), *Incorporating Third-Party Due Diligence Results Into The U.S. RMBS Rating Process,* S&P (Nov. 25, 2008).

[576] *See* proposed paragraph (c)(1)(v) of new Rule 17g–10.

[577] *See* proposed paragraphs (c)(1)(i)–(v) of new Rule 17g–10.

[578] *See* proposed paragraphs (c)(1)(i) of new Rule 17g–10.

[579] *See, e.g., US RMBS Ratings Criteria,* Fitch (Dec. 3, 2009).

[580] *Id.*

[581] *See, e.g., Incorporating Third-Party Due Diligence Results Into The U.S. RMBS Rating Process,* S&P (Nov. 25, 2008).

[582] *See* proposed paragraphs (c)(1)(ii) of new Rule 17g–10.

[583] *See, e.g., Criteria for Evaluating Independent Third-Party Loan Level Reviews for US RMBS,* Moody's (Nov. 24, 2008).

[584] *See, e.g., Incorporating Third-Party Due Diligence Results Into The U.S. RMBS Rating Process,* S&P (Nov. 25, 2008).

[585] *See* proposed paragraphs (c)(1)(iii) of new Rule 17g–10.

[586] *See, e.g., Criteria for Evaluating Independent Third-Party Loan Level Reviews for US RMBS,* Moody's (Nov. 24, 2008).

[587] *Id.*

[588] *Id.*

[589] *See* proposed paragraphs (c)(1)(iv) of new Rule 17g–10.

in a sampled loan file to verify the loan was made in conformance with, for example, with "truth-in-lending" regulations such as Regulation Z.[590]

The fifth category of "due diligence services"—the catchall—would be identified in proposed paragraph (c)(1)(v) of new Rule 17g–10 as a review of the assets underlying an Exchange Act-ABS for the purpose of making findings with respect to any other factor or characteristic of such assets that would be material to the likelihood that the issuer of the Exchange Act-ABS will pay interest and principal according to its terms and conditions.[591] The Commission preliminarily believes that findings relevant to whether the issuer of the Exchange Act-ABS will pay interest and principal according to its terms and conditions (*i.e.,* not default) would be relevant to determining a credit rating given that the statutory definition of "credit rating" is "an assessment of the creditworthiness of an obligor as an entity or with respect to specific securities or money market instruments." [592] The Commission also preliminarily believes that reviews of the assets underlying an Exchange Act-ABS that are designed to generate findings that would not be relevant to determining a credit rating would be outside the scope of proposed catchall definition and, therefore, outside the scope of Section 15E(s)(4)(B) of the Exchange Act and Rule 17g–10.[593]

Proposed paragraph (c)(2) of new Rule 17g–10 would define the term "issuer" as including a sponsor, as defined in 17 CFR 229.1011, or depositor, as defined in 17 CFR 229.1011, that participates in the issuance of an Exchange Act-ABS.[594] The Commission preliminarily believes this definition is necessary because the requirements of Section 15E(s)(4)(B) of the Exchange Act are triggered, among other things, when third-party due diligence services are employed by an "issuer." [595] The term "issuer" could be interpreted by entities subject to Section 15E(s)(4)(B) of the Exchange Act and new Rule 17g–10 as meaning the legal entity issuing the Exchange Act-ABS. However, the issuer of an Exchange Act-ABS typically is a passive entity such as a statutory trust. Consequently, a sponsor initiates an Exchange Act-ABS transaction by selling or pledging to a specially created issuing entity a group of financial assets that the sponsor either has originated itself or has purchased in the secondary market. In some instances, the transfer of assets is a two-step process: the financial assets are transferred by the sponsor first to an intermediate entity, the depositor, and then the depositor transfers the assets to the issuing entity for the particular transaction. Because the issuer is passive, the sponsor, depositor, or underwriter would be more likely to employ a provider of third-party due diligence services. Consequently, if the term "issuer" were narrowly interpreted to mean the passive entity, the objectives of Section 15E(s)(4)(B) of the Exchange Act potentially could be undermined in that the requirement to make the disclosure would not be triggered.

The Commission is proposing to define the terms "originator" and "securitizer" in proposed paragraphs (c)(3) and (c)(4), respectively, of new Rule 17g–10 because the proposed definition of "due diligence services" in proposed paragraph (c)(1) would use those terms.[596] The Commission preliminarily believes defining these terms would provide greater clarity as to the proposed meaning of "due diligence services." Moreover, Section 941 of the Dodd-Frank Act added new Section 15G of the Exchange Act.[597] Section 15G(a) contains definitions of "originator" and "securitizer" to be used for the purposes of that section.[598] Consequently, there are existing definitions the Commission can utilize for the purposes of new Rule 17g–10. For these reasons, proposed paragraph (c)(3) of new Rule 17g–10 would provide that the term "originator" has the same meaning as in Section 15G of the Exchange Act (15 U.S.C. 78o–9).[599] Similarly, proposed paragraph (c)(4) of new Rule 17g–10 would provide that the term "securitizer" has the same meaning as in Section 15G of the Exchange Act (15 U.S.C. 78o–9).[600]

Request for Comment

The Commission generally requests comment on all aspects of proposed new Rule 17g–10. The Commission also seeks comment on the following:

1. The Commission understands that "provider of third-party due diligence services" is a phrase used as a term of art in the securitization market, and the proposed rules are intended to apply to those entities that are commonly identified by that term. Would the proposed definition of "due diligence services" provide sufficient guidance to those entities providing due diligence services as to when the requirements of the self-executing provision in Section 15E(s)(4)(B) and proposed new Rule 17g–10 would apply? How could the proposal be modified to provide clearer guidance?

2. Should, as proposed, the definition of "due diligence services" apply to Exchange Act-ABS only or should it apply more broadly to structured finance products? If it should apply more broadly, what types of structured finance products that are not Exchange Act-ABS should the definition include within its scope? In addition, are providers of third-party due diligence services used with respect to these types of structured finance products? If so, explain how the results of those services are relevant to the determination of a credit rating?

3. Does the first category of "due diligence service" identified in proposed paragraph (c)(1)(i) of new Rule 17g–10 (*i.e.,* a review of the assets underlying an Exchange Act-ABS for the purpose of making findings with respect to the quality or integrity of the information or data about the assets provided, directly or indirectly, by the securitizer or originator of the assets) appropriately describe a form of due diligence service for Exchange Act-ABS that is provided to issuers or underwriters by a provider of third-party due diligence services? For example, is this component of the definition too broad or narrow? If so, how should this component of the definition be refined? Alternatively, should it be omitted from the definition as reflecting activity that is not a third-party due diligence service?

[590] *See* 12 CFR 226.1 *et seq.*

[591] *See* proposed paragraphs (c)(1)(v) of new Rule 17g–10.

[592] *See* 15 U.S.C. 78c(60).

[593] *See* 15 U.S.C. 78o–7(s)(4)(B) and proposed new Rule 17g–10.

[594] *See* proposed paragraph (c)(2) of new Rule 17g–10. The Commission interprets the term "issuer" in Section 15G(a)(3)(A) of the Exchange Act to refer to the depositor of an asset-backed security. This treatment is consistent with the Commission's historical regulatory approach to that term, including the Securities Act and the rules promulgated under the Securities Act and the Exchange Act. *See, e.g.,* 17 CFR 230.191 and 17 CFR 240.3b–19.

[595] *See* 15 U.S.C. 78o–7(s)(4)(B).

[596] *See* proposed paragraphs (c)(3) and (c)(4) of new Rule 17g–10; *see also* proposed paragraphs (c)(1)(i) and (iv) using the term "originator" and proposed paragraph (c)(1)(i) using the term "securitizer."

[597] *See* Public Law 111–203 § 941 and 15 U.S.C. 78o–9.

[598] *See* 15 U.S.C. 78o–9(a)(3) and (4).

[599] *See* proposed paragraph (c)(3) of new Rule 17g–10. Section 15G(a)(4) of the Exchange Act defines the term "originator" to mean "a person who—(A) through the extension of credit or otherwise, creates a financial asset that collateralizes and asset-backed security; and (B) sells an asset directly or indirectly to a securitizer." *See* 15 U.S.C. 78o–9(a)(4).

[600] *See* proposed paragraph (c)(4) of new Rule 17g–10. Section 15G(a)(3) of the Exchange Act defines the term "securitizer" to mean: "(A) an issuer of an asset-backed security; or (B) a person who organizes and initiates an asset-backed securities transaction by selling or transferring assets, either directly or indirectly, including through an affiliate, to the issuer." *See* 15 U.S.C. 78o–9(a)(3).

4. Does the second category of "due diligence service" identified in proposed paragraph (c)(1)(ii) of new Rule 17g–10 (*i.e.,* a review of the assets underlying Exchange Act-ABS for the purpose of making findings with respect to whether the origination of the assets conformed to underwriting or credit extension guidelines, standards, criteria or other requirements) appropriately describe a form of due diligence service for Exchange Act-ABS that is provided to issuers or underwriters by a provider of third-party due diligence services? For example, is this component of the definition too broad or narrow? If so, how should this component of the definition be refined? Alternatively, should it be omitted from the definition as reflecting activity that is not a third-party due diligence service?

5. Does the third category of "due diligence service" identified in paragraph (c)(1)(iii) of new Rule 17g–10 (*i.e.,* a review of the assets underlying an Exchange Act-ABS for the purpose of making findings with respect to the value of collateral securing such assets) appropriately describe a form of due diligence service for Exchange Act-ABS that is provided to issuers or underwriters by a provider of third-party due diligence services? For example, is this component of the definition too broad or narrow? If so, how should this component of the definition be refined? Alternatively, should it be omitted from the definition as reflecting activity that is not a third-party due diligence service?

6. Does the fourth category of "due diligence service" identified in paragraph (c)(1)(iv) of new Rule 17g–10 (*i.e.,* a review of the assets underlying an Exchange Act-ABS for the purpose of making findings with respect to whether the originator of the assets complied with Federal, state or local laws or regulations) appropriately describe a form of due diligence service for Exchange Act-ABS that is provided to issuers or underwriters by a provider of third-party due diligence services? For example, is this component of the definition too broad or narrow? If so, how should this component of the definition be refined? Alternatively, should it be omitted from the definition as reflecting activity that is not a third-party due diligence service?

7. Would the catchall component of the definition of "due diligence services" identified in proposed paragraph (c)(1)(v) of new Rule 17g–10 (*i.e.,* a review of the assets underlying an Exchange Act-ABS for the purpose of making findings with respect to any other factor or characteristic of such assets that would be material to the likelihood that the Exchange Act-ABS will pay interest and principal according to its terms and conditions) adequately capture existing or future third-party due diligence services not identified in proposed paragraphs (c)(1)(i) through (iv) of new Rule 17g–10? For example, is this component of the definition too broad or narrow? If so, how should this component of the definition be refined? Alternatively, should it be omitted from the definition?

8. Are there other types of due diligence services for Exchange Act-ABS provided to issuers or underwriters by a provider of third-party due diligence services that are not identified in the Commission's proposed definition that should be included? For example, would the proposed definitions capture third-party due diligence services provided with respect to an Exchange Act-ABS after it has been issued? If proposed definitions would not capture due diligence services provided post-issuance or any other services commonly understood as third-party due diligence services, describe such services and provide suggested rule text for how they could be incorporated into the definition. Also, provide an explanation as to how such services would be relevant to the determination of a credit rating.

9. Would the inclusion of the proposed definition of "issuer" in new Rule 17g–10 identify the types of entities that should trigger the requirements of the proposed rule? For example, is the proposed definition too broad or narrow? If so, how should the proposed definition be refined?

10. Would the inclusion of the proposed definition of "originator" in new Rule 17g–10 identify the types of entities that should trigger the requirements of the proposed rule? For example, is the proposed definition too broad or narrow? If so, how should the proposed definition be refined?

11. Would the inclusion of the proposed definition of "securitizer" in new Rule 17g–10 identify the types of entities that should trigger the requirements of the proposed rule? For example, is the proposed definition too broad or narrow? If so, how should the proposed definition be refined?

3. Proposed Form ABS Due Diligence–15E

Section 15E(s)(4)(C) of the Exchange Act specifies that the Commission shall establish the appropriate format and content for the written certifications required under Section 15E(s)(4)(B), to ensure that providers of due diligence services have conducted a thorough review of data, documentation, and other relevant information necessary for an NRSRO to provide an accurate rating.[601] The Commission is proposing to prescribe the format of the certification in Form ABS Due Diligence–15E.[602] The proposed form would contain five line items identifying information the provider of third-party due diligence services would need to set forth in the form. It also would contain a signature line with a corresponding representation.[603]

Item 1 of proposed Form ABS Due Diligence–15E would elicit the identity and address of the provider of third-party due diligence services.[604] This would notify users of the certification as to which third party conducted the review described in the certification. Item 2 of proposed Form ABS Due Diligence–15E would elicit the identity and address of the issuer, underwriter, or NRSRO that employed the provider of third party due diligence services.[605] This would notify users of the certification as to the person that employed the third-party to conduct the review described in the certification.

Item 3 of proposed Form ABS Due Diligence–15E would instruct the provider of third-party due diligence services to identify each NRSRO whose published criteria for performing due diligence the third party satisfied in performing the due diligence review.[606] As noted above, the NRSROs most active in rating RMBS have incorporated into their procedures and methodologies for determining RMBS credit ratings minimum steps a provider of third party due diligence services must take in conducting due diligence.[607] Consequently, the instructions for Item 3 would provide that if the manner and scope of the due diligence provided by the third party satisfied the criteria for due diligence published by an NRSRO, the third party should identify the NRSRO and the title and date of the published criteria in a table provided on the form.[608] The table and instructions would permit the identification of more

[601] *See* 15 U.S.C. 78o–7(s)(4)(C).

[602] *See* proposed new Rule 17 CFR 249b.400 and proposed Form ABS Due Diligence–15E.

[603] *Id.*

[604] *See* Item 1 to proposed Form ABS Due Diligence–15E.

[605] *See* Item 2 to proposed Form ABS Due Diligence–15E.

[606] *See* Item 3 to proposed Form ABS Due Diligence 15E.

[607] *See, e.g., US RMBS Ratings Criteria,* Fitch (Dec. 3, 2009) *Criteria for Evaluating Independent Third-Party Loan Level Reviews for US RMBS,* Moody's (Nov. 24, 2008) *Incorporating Third-Party Due Diligence Results Into the U.S. RMBS Rating Process,* S&P (Nov. 25, 2008).

[608] *Id.*

than one NRSRO.[609] This would allow the third party to reflect in a single form that it conducted due diligence services in a manner that satisfied the due diligence requirements of multiple NRSROs. As such, Item 3 would be designed to elicit a representation from the provider of the third-party due diligence services that it satisfied a given NRSRO's published due diligence standards.

Items 4 and 5 of proposed Form ABS Due Diligence–15E would require the provider of the third-party due diligence services to describe, respectively: (1) The scope and manner of the due diligence performed; and (2) the findings and conclusions resulting from the review. The instructions for Items 4 and 5 would require the summaries to be provided in attachments to the form, which would be considered part of the form.

As discussed above in Section II.H.1 of this release, the Commission is proposing to implement Section 15E(s)(4)(A) of the Exchange Act by requiring the issuer or underwriter of an Exchange Act-ABS to disclose the findings and conclusions of a provider of third-party due diligence services by furnishing Form ABS–15G on EDGAR pursuant to proposed Rule 15Ga–2.[610] Alternatively, the issuer or underwriter would be permitted to obtain a representation from each NRSRO engaged to determine a credit rating for the Exchange Act-ABS that the NRSRO will publicly disclose the findings and conclusions of the provider of third-party due diligence services in the form that would need to be published pursuant to proposed new paragraph (a)(1) of Rule 17g–7. In addition, as discussed above in Section II.G.3 of this release, proposed new paragraph (a)(1)(ii)(F) of Rule 17g–7 would implement Section 15E(s)(3)(A)(v) of the Exchange Act by requiring an NRSRO to disclose in the form whether and to what extent third-party due diligence services were used by the NRSRO, a description of the information that such third party reviewed in conducting due diligence services, and a description of the findings or conclusions of such third party.[611] The Commission preliminarily believes that requiring a provider of third-party due diligence services to summarize in Items 4 and 5 of Form ABS Due Diligence–15E the manner and scope of the due diligence performed and the findings and conclusions resulting from the due diligence would facilitate these other requirements.[612] For example, the NRSRO could use the summaries to make the disclosures in the form generated pursuant to proposed new paragraph (a) of Rule 17g–7. In addition, the Commission preliminarily believes that the disclosures would be useful to investors and other users of credit ratings (as noted above in Section II.G.5, an NRSRO would be required to disclose the certification with the publication of a credit rating pursuant to proposed new paragraph (a)(2) of Rule 17g–7).

To this end, the Commission proposes that Item 4 require the provider of third-party due diligence services to describe the steps taken in performing the due diligence.[613] The instructions would require the third party to provide this description regardless of whether the third party represented in Item 3 of the form that its review satisfied published criteria of an NRSRO. In other words, the third party would not be able to simply rely on a cross-reference to the NRSRO's published criteria to explain the work completed in performing the due diligence. Consequently, the instructions to Item 4 would require the third party to describe the scope and manner of the due diligence services provided in connection with the review of assets that is sufficiently detailed to provide an understanding of the steps taken in performing the review. The instructions further would require that the third party include in the description: (1) The type of assets that were reviewed; (2) the sample size of the assets reviewed; (3) how the sample size was determined and, if applicable, computed; (4) whether the quality or integrity of information or data about the assets provided, directly or indirectly, by the securitizer or originator of the assets was reviewed and, if so, how the review was conducted; (5) whether the origination of the assets conformed to, or deviated from, stated underwriting or credit extension guidelines; (6) whether the value of collateral securing such assets was reviewed and, if so, how the review was conducted; (7) whether the compliance of the originator of the assets with Federal, state and local laws and regulations was reviewed and, if so, how the review was conducted; and (8) any other type of review conducted with respect to the assets. In other words, the proposed instructions would parallel the Commission's proposed definition of "due diligence services" in paragraph (c)(1) of proposed new Rule 17g–10.[614]

As discussed above, the information required by the instructions would provide the NRSRO and investors and users of credit ratings of the NRSRO with a description of the nature of the due diligence performed along with the publication of the credit rating and the form that would be required under proposed new paragraph (a)(1) of Rule 17g–7.[615] The information also would allow the NRSRO and users of credit ratings to compare whether the provider of third-party due diligence services, based on its description, appeared to satisfy published criteria of the NRSRO if such a claim was made in Item 3. Finally, if no criteria had been published for the type of Exchange Act-ABS or no claim to satisfying criteria was made in Item 3, the description would be the sole basis of understanding the due diligence performed.

Item 5 of proposed Form ABS Due Diligence–15E would require the provider of third-party due diligence services to summarize the findings and conclusions resulting from the due diligence review.[616] Specifically, the instructions to Item 5 would require the third party to provide a summary of the findings and conclusions that resulted from the due diligence services that is sufficiently detailed to provide an understanding of the findings and conclusions that were conveyed to the person identified in Item 2 (*i.e.,* conveyed to the issuer, underwriter, or NRSRO that employed the third party to perform due diligence services). As discussed above, the reasons for proposing the requirement to provide such a summary are the same as for Item 4 of Form ABS Due Diligence–15E.

Finally, the individual executing Form ABS Due Diligence-15E on behalf of a provider of third-party due diligence services would need to make two representations.[617] First, the individual would need to represent that he or she has executed the Form on behalf of, and on the authority of, the third-party. Second, the individual would need to represent that the third-party conducted a thorough review in performing the due diligence described in Item 4 attached to the Form and that the information and statements

[609] *Id.*

[610] 15 U.S.C. 78o–7(s)(4)(A), proposed new Rule 15Ga–2, and proposed amendments to Form ABS–15G.

[611] *See* 15 U.S.C. 78o–7(s)(3)(A)(v) and proposed new paragraph (a)(1)(ii)(F) of Rule 17g–7.

[612] *See* Items 4 and 5 of proposed Form ABS Due Diligence–15E.

[613] *See* Item 4 of proposed Form ABS Due Diligence–15E.

[614] *Compare* Item 4 of proposed Form ABS Due Diligence 15E, *with* paragraph (c)(1) of proposed new Rule 17g–10.

[615] *See* proposed new paragraph (a) of Rule 17g–7.

[616] *See* Item 5 of proposed Form ABS Due Diligence 15E.

[617] *See* "Certification" of proposed Form ABS Due Diligence-15E.

contained in the Form, including Items 4 and 5 attached to the Form, which are part of the Form, are accurate in all significant respects. The Commission is proposing that this representation be made to implement the provision of Section 15E(s)(4)(C) of the Exchange Act, which provides that the Commission shall establish the appropriate format and content of the written certifications "to ensure that providers of due diligence services have conducted a *thorough review* of data, documentation, and other relevant information necessary for [an NRSRO] to provide an accurate rating (emphasis added)."[618]

Request for Comment

The Commission generally requests comment on all aspects of proposed new Form ABS Due Diligence-15E. The Commission also seeks comment on the following:

1. Would the proposed format of proposed Form ABS Due Diligence-15E appropriately achieve the objectives of Section 15E(s)(4)(C) of the Exchange Act? How could the format be modified to better achieve these objectives?

2. Should proposed Form ABS Due Diligence-15E be more prescriptive in terms of the steps a provider of third-party due diligence services would need to take in performing the review? For example, should the form specify the minimum sample size a provider of third-party due diligence services must perform on the assets underlying the Exchange Act-ABS? If so, should the sample size be the same across all asset classes and within asset classes? For example, with respect to RMBS, the scope of due diligence could be based on the type of mortgage loans (prime, Alt-A, or sub-prime), the quality of the originator of the loans, the level of documentation provided with the loans or other characteristics. Moreover, the scope of due diligence required for a CMBS could involve reviewing every pool asset (rather than a sample), since the number of underlying loans is much less than in an RMBS and, therefore, the default of one loan would have a greater impact than the default of a loan underlying an RMBS. Moreover, the scope of due diligence required by an NRSRO for an Exchange Act-ABS where the asset pool composition turns over rapidly because it contains revolving assets, such as credit card receivables or dealer floor-plan receivables, could involve different sampling techniques. How would the Commission account for these variables in prescribing minimum sample sizes or other procedures that would need to be undertaken by a provider of third-party due diligence services? What benefits and costs could result from being more prescriptive? Are there practical issues to imposing a more prescriptive approach? If so, describe these issues.

3. Would the information disclosed in Item 3 of proposed new Form ABS Due Diligence-15E identifying each NRSRO whose published criteria were satisfied by the provider of third-party due diligence services be useful to the NRSRO producing a credit rating for the Exchange Act-ABS? If not, how could the proposed instructions for Item 3 be modified to make it more useful to NRSROs? Are there practical issues to imposing a more prescriptive approach? If so, describe these issues.

4. Would the summary provided in proposed Item 4 of new Form ABS Due Diligence-15E about the scope and manner of the due diligence services provided in connection with the review of assets be useful to investors, other users of credit ratings, and NRSROs producing a credit rating for the asset-backed security? If not, how could the proposed instructions for Item 4 be modified to make it more useful? Are there practical issues to imposing a more prescriptive approach? If so, describe these issues.

5. Would the summary provided in proposed Item 5 of new Form ABS Due Diligence-15E about the findings and conclusions that resulted from the due diligence services be useful to investors, other users of credit ratings, and NRSROs producing a credit rating for the asset-backed security? If not, how could the proposed instructions for Item 5 be modified to make it more useful? Are there practical issues to imposing a more prescriptive approach? If so, describe these issues.

I. Standards of Training, Experience, and Competence

Section 936 of the Dodd-Frank Act provides that the Commission shall issue rules that are reasonably designed to ensure that any person employed by an NRSRO to perform credit ratings: (1) Meets standards of training, experience, and competence necessary to produce accurate ratings for the categories of issuers whose securities the person rates[619] and (2) is tested for knowledge of the credit rating process.[620] The Commission proposes to implement Section 936 by proposing new Rule 17g–9 and amending Rule 17g–2.[621]

1. Proposed New Rule 17g–9

The Commission proposes to implement Section 936 of the Dodd-Frank through new Rule 17g–9.[622] As proposed, new Rule 17g–9 would have three paragraphs: (a), (b) and (c).[623] Proposed paragraph (a) would contain a requirement that an NRSRO design and administer standards of training, experience, and competence.[624] Proposed paragraph (b) would identify factors an NRSRO would need to consider in designing the standards.[625] Proposed paragraph (c) would prescribe two specific requirements that would need to be incorporated into an NRSRO's standards.[626]

a. Proposed Paragraph (a)

Proposed paragraph (a) of new Rule 17g–9 would require an NRSRO to establish, maintain, enforce, and document standards of training, experience, and competence for the individuals it employs to determine credit ratings that are reasonably designed to achieve the objective that such individuals produce accurate credit ratings in the classes and subclasses of credit ratings for which the NRSRO is registered.[627] Consequently, the provision, as proposed, would require the NRSRO to design its own standards.[628] The Commission preliminarily believes this approach would be appropriate because of the varying procedures and methodologies used by NRSROs to determine credit ratings. The proposed requirement would provide flexibility to allow each NRSRO to customize the standards according to its unique procedures and methodologies for determining credit ratings and size. For example, the standards established by an NRSRO with hundreds or thousands of credit analysts that produce tens of thousands of credit ratings across a wide range of asset classes may need to be different than the standards of a small NRSRO with only a handful of credit analysts that focus on a particular class of credit ratings.

At the same time, Section 936(1) provides that the Commission's rules must be reasonably designed to ensure

[618] *See* 15 U.S.C. 78o–7(s)(4)(C).

[619] *See* Public Law 111–203 § 936(1).

[620] *See* Public Law 111–203 § 936(2).

[621] *See* proposed new Rule 17g–9 and proposed new paragraph (b)(15) of Rule 17g–2.

[622] *See* proposed new Rule 17g–9. This rule, if adopted, would be codified at 17 CFR 240.17g–9.

[623] *See* proposed paragraphs (a), (b), and (c) of new Rule 17g–9.

[624] *See* proposed paragraph (a) of new Rule 17g–9.

[625] *See* proposed paragraph (b) of new Rule 17g–9.

[626] *See* proposed paragraph (c) of new Rule 17g–9.

[627] *See* proposed paragraph (a) of new Rule 17g–9.

[628] *Id.*

that any person employed by an NRRSRO to perform credit ratings meets standards of training, experience, and competence *necessary to produce accurate ratings* for the categories of issuers whose securities the person rates.[629] Accordingly, while the Commission preliminarily believes that the rule should allow flexibility in terms of the design of the standards, the Commission also preliminarily believes that to appropriately implement Section 936(1) the rule should require that the standards have a common objective. Therefore, proposed paragraph (a) of new Rule 17g–9 would require that the standards, as established, must be reasonably designed to achieve the objective that individuals employed by the NRSRO to determine credit ratings produce accurate credit ratings in the classes of credit ratings for which the NRSRO is registered.

This approach of identifying an objective—the production of accurate ratings—and imposing a requirement that the standards be reasonably designed to achieve the objective parallels Sections 15E(g) and (h) of the Exchange Act, among other provisions in the securities laws.[630] For example, Section 15E(g) of the Exchange Act contains a self-executing requirement that each NRSRO shall establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of the business of such NRSRO, to prevent the misuse in violation of the Exchange Act, or the rules or regulations thereunder, of material, nonpublic information by such NRSRO or any person associated with such NRSRO.[631] Similarly, Section 15E(h) contains a self-executing requirement that each NRSRO shall establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of the business of such NRSRO and affiliated persons and affiliated companies thereof, to address and manage any conflicts of interest that can arise from such business.[632]

Request for Comment

The Commission generally requests comment on all aspects of proposed paragraph (a) of new Rule 17g–9. The Commission also seeks comment on the following:

1. Would the approach in paragraph (a) of new Rule 17g–9 (*i.e.,* identifying an objective for the standards and requiring the NRSRO to design its own standards to achieve that objective) appropriately implement Section 936 of the Dodd-Frank Act, particularly when taken together with the provisions of proposed paragraphs (b) and (c) of new Rule 17g–9 discussed below? If not, should the Commission specifically prescribe the requirements of the standards to establish consistent industry-wide standards? If so, would it be practical to prescribe consistent industry-wide standards applicable to each NRSRO? Commenters who believe such an approach would be feasible and appropriate should identify such a standard and provide suggested rule text.

2. Would the objective identified in proposed paragraph (a) of new Rule 17g–9 (*i.e.,* standards of training, experience, and competence that are reasonably designed to achieve the objective that such credit analysts produce accurate credit ratings) be appropriate? Would it establish an objective that could be achieved? Would it implement the goal of Section 936 of the Dodd-Frank Act? Commenters who believe that the proposed objective is not appropriate should explain why and provide suggested rule text to modify the objective.

3. Is the objective—the production of "accurate credit ratings"—assessable? For example, how should the accuracy of credit ratings be measured?

4. Would it be feasible to establish a testing program that has standardized components to review the adequacy of the standards of training, experience, and competence that an NRSRO maintains, enforces, and documents pursuant to proposed paragraph (a) of new Rule 17g–9? If so, what should the components of that testing program be? What would be the advantages and disadvantages of such a program? Are there comparable testing programs used in other contexts that would be relevant in developing such a program?

b. Proposed Paragraph (b)

While proposed paragraph (a) of new Rule 17g–9 would provide that the NRSRO must design the standards, proposed paragraph (b) would identify factors the NRSRO must consider when designing the standards.[633] The Commission intends the identified factors to provide guidance to NRSROs about the Commission's expectations for the design of the standards of training, experience, and competence. It also is intended to provide benchmarks that Commission examiners could use to evaluate whether a given NRSRO's standards are reasonably designed to meet the objective set forth in proposed paragraph (a).

Proposed paragraph (b) of new Rule 17g–9 would require the NRSRO to consider each factor in the context of the potentially varying roles of the individuals employed by the NRSRO to determine credit ratings. More specifically, the Commission preliminarily believes that the design of the standards must account for different functions and responsibilities of such individuals as well as the different procedures and methodologies they use to determine credit ratings. The Commission is not proposing that the NRSRO design a standard for each individual. Rather, the Commission preliminarily believes that the standards, particularly of a large NRSRO with hundreds or thousands of credit analysts, should account for groups of individuals who are not similarly situated, for example, in terms of years of experience, education level, responsibility, and complexity of the procedures and methodologies they use to determine credit ratings.

The first factor—identified in proposed paragraph (b)(1) of Rule 17g–9—would require the NRSRO, when establishing the standards of training, experience, and competence, to consider if the credit rating procedures and methodologies used by the individual involve qualitative analysis, the knowledge necessary to effectively evaluate and process the data relevant to the creditworthiness of the obligor being rated or the issuer of the securities or money market instruments being rated.[634] The Commission intends proposed paragraph (b)(1) to require the NRSRO to consider the fact that qualitative analysis relies, in large part, on identifying and assimilating relevant information about an obligor or issuer and making judgments on how that information impacts the creditworthiness of the obligor or the issuer.

The second factor—identified in proposed paragraph (b)(2) of Rule 17g–9—would require the NRSRO, when establishing the standards of training, experience, and competence, to consider if the credit rating procedures and methodologies used by the individual involve quantitative analysis, the technical expertise necessary to understand any models and model inputs that are a part of the procedures

[629] *See* Public Law 111–203 § 936(1).

[630] *See* 15 U.S.C. 78o–7(g) and (h).

[631] *See* 15 U.S.C. 78o–7(g).

[632] *See* 15 U.S.C. 78o–7(h).

[633] *See* proposed paragraph (b) of new Rule 17g–9.

[634] *See* proposed paragraph (b)(1) of new Rule 17g–9.

and methodologies.[635] The Commission intends proposed paragraph (b)(2) to require the NRSRO to consider the fact that quantitative analysis relies, in large part, on mathematical techniques and, consequently, credit analysts using quantitative models would need to have relevant technical expertise.

The third factor—identified in proposed paragraph (b)(3) of Rule 17g–9—would require the NRSRO, when establishing the standards of training, experience, and competence, to consider the classes and subclasses of credit ratings for which each individual participates in determining credit ratings and the factors relevant to such classes and subclasses, including the geographic location, sector, industry, regulatory and legal framework, and underlying assets, applicable to the obligors or issuers in the classes and subclasses.[636] The Commission intends proposed paragraph (b)(3) to require the NRSRO to consider the fact that different types of obligors and issuers have unique characteristics that may be relevant to the creditworthiness of the obligor or the issuer. For example, the knowledge and competence necessary to rate an operating company is different from that necessary to rate an asset-backed security or a municipal security. Moreover, there may be differences within classes of credit ratings. For example, rating an RMBS requires different knowledge than rating a CMBS, and rating a company in the oil industry requires different knowledge than rating a company in the telecommunications industry.

The fourth factor—identified in proposed paragraph (b)(4) of Rule 17g–9—would require the NRSRO to consider, when establishing the standards of training, experience, and competence, the complexity of the obligors, securities, or money market instruments being rated by the individual.[637] The Commission intends proposed paragraph (b)(4) to require the NRSRO to consider the fact that obligors and securities it rates may vary widely in terms of complexity. For example, more experience and competence may be necessary to rate a synthetic CDO as opposed to a typical RMBS or a global financial company as opposed to a community bank.

Request for Comment

The Commission generally requests comment on all aspects of proposed paragraph (b) of new Rule 17g–9. The Commission also seeks comment on the following:

1. Are there any other factors in addition to, or as an alternative to, the four factors identified in paragraphs (b)(1) through (4) an NRSRO should consider when establishing standards of training, experience, and competence? For example, should the proposed rule require an NRSRO to consider the number of initial credit ratings the individual is expected to participate in determining annually and the number of credit ratings the individual is expected to participate in monitoring annually? If so, how should these factors be taken into consideration? Identify any additional or alternative factors and provide suggested rule text.

2. Should the factor identified in proposed paragraph (b)(1) of Rule 17g–9 (*i.e.,* if the credit rating procedures and methodologies used by the individual involve qualitative analysis, the knowledge necessary to effectively evaluate and process the data relevant to the creditworthiness of the obligor being rated or the issuer of the securities or money market instruments being rated) be considered when the NRSRO designs its standards of training, experience, and competence for the individuals it employs to determine credit ratings? If not, should proposed paragraph (b)(1) be modified to provide better guidance for designing the standards? If so, how should it be modified? Alternatively, should it be omitted from the rule? If so, explain why.

3. Should the factor identified in proposed paragraph (b)(2) of Rule 17g–9 (*i.e.,* if the credit rating procedures and methodologies used by the individual involve quantitative analysis, the technical expertise necessary to understand any models and model inputs that are a part of the procedures and methodologies) be considered when the NRSRO designs its standards of training, experience, and competence for the individuals it employs to determine credit ratings? If not, should proposed paragraph (b)(2) be modified to provide better guidance for designing the standards? If so, how should it be modified? Alternatively, should it be omitted from the rule? If so, explain why.

4. Should the factor identified in proposed paragraph (b)(3) of Rule 17g–9 (*i.e.,* the classes and subclasses of credit ratings for which the individual participates in determining credit ratings and the factors relevant to such classes and subclasses, including the geographic location, sector, industry, regulatory and legal framework, and underlying assets, applicable to the obligors or issuers in the classes and subclasses) be considered when the NRSRO designs its standards of training, experience, and competence for the individuals it employs to determine credit ratings? If not, should proposed paragraph (b)(3) be modified to provide better guidance for designing the standards? If so, how should it be modified? Alternatively, should it be omitted from the rule? If so, explain why.

5. Should the factor identified in proposed paragraph (b)(4) of Rule 17g–9 (*i.e.,* the complexity of the obligors, securities, or money market instruments being rated by the individuals) be considered when the NRSRO designs its standards of training, experience, and competence for the individuals it employs to determine credit ratings? If not, should proposed paragraph (b)(4) be modified to provide better guidance for designing the standards? If so, how should it be modified? Alternatively, should it be omitted from the rule? If so, explain why.

c. Proposed Paragraph (c)

Proposed paragraph (c) of new Rule 17g–9 would prescribe two requirements that an NRSRO must incorporate into its standards of training, experience, and competence.[638] The first requirement would be prescribed in proposed paragraph (c)(1) of new Rule 17g–9.[639] This paragraph would provide that the standards of training, experience, and competence must include a requirement for periodic testing of the individuals employed by the NRSRO to determine credit ratings on their knowledge of the procedures and methodologies used by the NRSRO to determine credit ratings in the classes or subclasses of credit ratings for which the individual participates in determining credit ratings.[640] The Commission is proposing this requirement to implement Section 936(2) of the Dodd-Frank Act, which provides that the Commission shall issue rules that are reasonably designed to ensure that any person employed by an NRSRO to perform credit ratings is tested for knowledge of the credit rating process.[641] The Commission preliminarily believes that the frequency and manner of testing should be established by the NRSRO. For example, the frequency and manner of testing may depend on whether an NRSRO employs a large number of

[635] *See* proposed paragraph (b)(2) of new Rule 17g–9.

[636] *See* proposed paragraph (b)(3) of new Rule 17g–9.

[637] *See* proposed paragraph (b)(4) of new Rule 17g–9.

[638] *See* proposed paragraphs (c)(1) and (2) of new Rule 17g–9.

[639] *See* proposed paragraph (c)(1) of new Rule 17g–9.

[640] *Id.*

[641] *See* Public Law 111–203 § 936(2).

analysts with varying levels of experience to rate a wide range of obligors, securities, and money market instruments. In this case, testing may need to be more frequent, particularly with respect to more junior analysts. On the other hand, an NRSRO that employs few analysts who focus on rating a specific type of obligor, security, or money market instrument may need less frequent testing, particularly if the analysts are experienced. However, the Commission notes that the testing program—as with all aspects of the standards—would need to be reasonably designed to achieve the objective that the credit analysts produce accurate credit ratings in the classes of credit ratings for which the NRSRO is registered.[642] Consequently, an NRSRO would need to establish a training schedule that is consistent with achieving this objective.

The second requirement would be prescribed in proposed paragraph (c)(2) of new Rule 17g–9.[643] This paragraph would provide that the standards of training, experience, and competence must include a requirement that at least one individual with three years or more experience in performing credit analysis participates in the determination of a credit rating.[644] The Commission preliminarily believes three years of experience is appropriate because, among other things, being in business as a credit rating agency for three years was a minimum prerequisite to being treated as an NRSRO under the Rating Agency Act of 2006.[645] Specifically, prior to being amended by the Dodd-Frank Act, the first prong of the definition of "nationally recognized statistical rating organization," provided that the entity "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 under Section 15E."[646] Moreover, Section 15E(a)(1)(B)(ix) of the Exchange Act requires a credit rating agency applying for registration as an NRSRO to submit certifications from qualified institutional buyers ("QIBs") as specified in Section 15E(a)(1)(C) of the Exchange Act.[647] Sections 15E(a)(1)(C)(i) through (iii) of the Exchange Act provide, among other things, that the applicant must furnish certifications from a minimum of 10 QIBs, including certifications from no less than two QIBs for each category of obligor for which the applicant intends to be registered.[648] Section 15E(a)(1)(C)(iv) provides, among other things, that the certification must state that the entity meets the definition of a QIB and has used the credit ratings of the applicant for at least the three years immediately preceding the date of the certification in the subject category or categories.[649]

The Commission considered these former and current provisions of Section 15E of the Exchange Act in developing the proposed three-year requirement in paragraph (c)(2) of new Rule 17g–9. The Commission preliminarily believes that having at least one person participate in the determination of a credit rating who has at least three years experience in performing credit analysis would establish an appropriate baseline requirement that could be implemented by NRSROs without causing them to hire new staff or re-allocate staff resources. For example, in terms of participating in the credit rating, the Commission preliminarily believes an NRSRO's standard could require that at least one person with at least three years experience serve on a committee that votes to approve the credit rating or that reviews and approves a credit rating action proposed by a junior analyst. Moreover, the Commission notes that performing credit analysis is not synonymous with determining credit ratings. Many financial institutions have credit risk departments staffed by individuals who analyze the creditworthiness of existing and future counterparties and borrowers. The Commission preliminarily intends that this type of work would qualify a credit analyst to meet the three-year requirement in proposed paragraph (c)(2) of new Rule 17g–9. Consequently, if an NRSRO employed an individual who performed credit analysis for a financial institution for more than three years, that individual would qualify for purposes of the proposed "three-year" requirement.

Request for Comment

The Commission generally requests comment on all aspects of proposed paragraph (c) of new Rule 17g–9. The Commission also seeks comment on the following:

1. Would proposed paragraph (c)(1) of new Rule 17g–9 (which would provide that the standards of training, experience, and competence must include a requirement for periodic testing of the individuals employed by the NRSRO to determine credit ratings on their knowledge of the procedures and methodologies used by the NRSRO to determine credit ratings in the classes and subclasses of credit ratings for which the individual is responsible for determining credit ratings) appropriately implement Section 936(2) of the Dodd-Frank Act? If not, how should proposed paragraph (c)(1) be modified to better achieve the objective of Section 936(2)?

2. Should the Commission prescribe the frequency of the periodic testing that would be mandated under proposed paragraph (c)(1) of new Rule 17g–9? For example, should an NRSRO be required to administer testing every six months, every year, every two years?

3. Would proposed paragraph (c)(2) of new Rule 17g–9 (which would provide that the standards of training, experience, and competence must include a requirement that at least one individual with three years or more experience in performing credit analysis participates in the determination of a credit rating) be an appropriate measure in terms of implementing Section 936 of the Dodd-Frank Act? If not, how should proposed paragraph (c)(2) be modified to better achieve the objective of Section 936? For example, should the Commission establish a different minimum number of years such as 1 or 2 years experience or 4, 5, 6, 7, or some larger number of years? Alternatively, should this proposal be omitted from the rule? If so, explain why?

2. Proposed Amendment to Rule 17g–2

For the reasons discussed in Section II.A.2 of this release, the Commission preliminarily believes that the standards of training, experience, and competence an NRSRO would be required, among other things, to document pursuant to proposed paragraph (a) of new Rule 17g–9 should be subject to the recordkeeping requirements of Rule

[642] *See* proposed paragraph (a) of new Rule 17g–9.

[643] *See* proposed paragraph (c)(2) of new Rule 17g–9.

[644] *Id.*

[645] *See* Section 3(a)(61)(A) of the Exchange Act, as added by Section 3(a) of the Rating Agency Act of 2006. *See* Public Law 109–291 § 3. Section 932(b) of the Dodd-Frank Act struck subparagraph (A) of Section 3(a)(61) of the Exchange Act and re-designated paragraph (B) as paragraph (A). *See* Public Law 111–203 § 932(b). While the Dodd-Frank Act eliminated the "three-year" prong from the definition of NRSRO, the Commission does not believe this evidences a view that the credit analysts who work for a credit rating agency need not have any experience. In fact, as noted above, Section 936(1) of the Dodd-Frank Act, among other things, provides that the Commission shall issue rules that are reasonably designed to ensure that any person employed by an NRRSRO to perform credit ratings meets standards of training, *experience,* and competence necessary to produce accurate ratings for the categories of issuers whose securities the person rates. *See* Public Law 111–203 § 936(1).

[646] *Id.*

[647] *See* 15 U.S.C. 78o–7(a)(1)(B)(ix) and 15 U.S.C. 78*o*–7(a)(1)(C).

[648] *See* 15 U.S.C. 78o–7(a)(1)(C)(i)–(iii).

[649] *See* 15 U.S.C. 78o–7(a)(1)(C)(iv).

17g–2.[650] Consequently, the Commission proposes adding new paragraph (b)(15) to Rule 17g–2 to identify the standards of training, experience, and competence the NRSRO must establish, maintain, enforce, and document pursuant to proposed new Rule 17g–9 as a record that must be retained.[651] As a result, the standards would be subject to the record retention and production requirements in paragraphs (c) through (f) of Rule 17g–2.[652]

Request for Comment

The Commission generally requests comment on all aspects of proposed new paragraph (b)(15) of Rule 17g–2.

J. Universal Rating Symbols

Section 938(a) of the Dodd-Frank Act provides that the Commission shall require, by rule, each NRSRO to establish, maintain, and enforce written policies and procedures that: (1) Assess the probability that an issuer of a security or money market instrument will default, fail to make timely payments, or otherwise not make payments to investors in accordance with the terms of the security or money market instrument;[653] (2) clearly define and disclose the meaning of any symbol used by the NRSRO to denote a credit rating;[654] and (3) apply any symbol described in item (2) in a manner that is consistent for all types of securities and money market instruments for which the symbol is used.[655] Section 938(b) of the Dodd-Frank Act provides that nothing in Section 938 shall prohibit an NRSRO from using distinct sets of symbols to denote credit ratings for different types of securities or money market instruments.[656]

The Commission proposes to implement Section 938(a) of the Dodd-Frank Act by proposing paragraph (b) of new Rule 17g–8 and by amending Rule 17g–2.[657]

1. Proposed Paragraph (b) of New Rule 17g–8

The Commission preliminarily believes that Section 938(a) of the Dodd-Frank Act is explicit in prescribing the policies and procedures the Commission shall require, by rule, of each NRSRO.[658] Consequently, the Commission proposes that the rule text of proposed paragraph (b) of new Rule 17g–8 mirror the statutory text.

The prefatory text of proposed paragraph (b) of new Rule 17g–8 would provide that an NRSRO must establish, maintain, enforce, and document policies and procedures that are reasonably designed to achieve three objectives, which would be identified in paragraphs (b)(1), (2), and (3).[659] This proposed provision would mirror the prefatory text of Section 938(a) of the Dodd-Frank Act except that the proposed rule text would add the requirement that the NRSRO "document" the policies and procedures.[660] The Commission preliminarily believes it would be appropriate to add a documentation requirement because it would mean that an NRSRO would need to put its policies and procedures into writing. This requirement, coupled with the Commission's proposal discussed next to apply the record retention and production provisions of Rule 17g–2 to the policies and procedures, would be designed to make them more readily available to Commission examiners. In addition, the Commission believes it is a sound practice for any organization to document its policies and procedures to promote better understanding of them among the individuals within the organization and, therefore compliance with such policies and procedures.

Proposed paragraph (b)(1) of new Rule 17g–8 would require the NRSRO to have policies and procedures reasonably designed to assess the probability that an issuer of a security or money market instrument will default, fail to make timely payments, or otherwise not make payments to investors in accordance with the terms of the security or money market instrument.[661] This proposed provision would mirror the text of Section 938(a)(1) of the Dodd-Frank Act.[662] The Commission also notes that Section 15E(s)(3)(B)(ii) of the Exchange Act provides that the Commission's rule requiring an NRSRO to generate a form to disclose information with the publication of a credit rating requires disclosure of information on the content of the credit rating, including: (1) The historical performance of the credit rating; and (2) the expected probability of default and the expected loss in the event of default.[663] As discussed above in Section II.G.3 of this release, the Commission is proposing to implement this requirement in proposed new paragraph (a)(1)(ii)(L) of Rule 17g–7.[664] The Commission preliminarily believes proposed paragraph (b)(1) of new Rule 17g–8 would work in conjunction the requirement in proposed new paragraph (a)(1)(ii)(L) of Rule 17g–7 insomuch as the policies and procedures proposed to be required by the former would assist the NRSRO in making the disclosure proposed to be required in the latter.

Proposed paragraph (b)(2) of new Rule 17g–8 would require the NRSRO to have policies and procedures reasonably designed to clearly define each symbol, number, or score in the rating scale used by the NRSRO to denote a credit rating category and notches within a category for each class and subclass of credit ratings for which the NRSRO is registered and to include such definitions in Exhibit 1 to Form NRSRO.[665] This proposed provision would implement Section 938(a)(2) of the Dodd-Frank Act.[666] In addition, it would mirror text in the proposed revisions to the Instructions to Exhibit 1 to Form NRSRO as well as work in conjunction with the requirements in those instructions.[667] As discussed above in Section II.E.1.a of this release, the Commission is proposing to amend the Instructions for Exhibit 1. One of the proposed amendments would require the NRSRO to clearly define in Exhibit 1 the meaning of each symbol, number, or score in the rating scale used by the applicant or NRSRO to denote a credit rating category and notches within a category in any Transition/Default Matrix presented in the Exhibit.[668] Consequently, taken together, the proposals would require an NRSRO to have policies and procedures that clearly define the meaning of each

[650] 17 CFR 240.17g–2.

[651] *See* proposed new paragraph (b)(15) to Rule 17g–2; *see also* Section 17(a)(1) of the Exchange Act, which requires an NRSRO to make and keep such records, and make and disseminate such reports, as the Commission prescribes by rule as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the Exchange Act. 15 U.S.C. 78q(a)(1).

[652] *See* 17 CFR 240.17g–2.

[653] *See* Public Law 111–203 § 938(a)(1).

[654] *See* Public Law 111–203 § 938(a)(2).

[655] *See* Public Law 111–203 § 938(a)(3).

[656] *See* Public Law 111–203 § 938(b).

[657] *See* proposed paragraph (b) of Rule new 17g–8 and proposed new paragraph (b)(14) of Rule 17g–2. As discussed earlier, the Commission is proposing that rule requirements specifying policies and procedures be consolidated in new Rule 17g–8.

[658] *See* Public Law 111–203 § 936(a).

[659] *See* prefatory text of proposed paragraph (b) of new Rule 17g–8.

[660] *Compare* prefatory text of Public Law 111–203 § 938(a), *with* prefatory text of proposed paragraph (b) of new Rule 17g–8.

[661] *See* proposed paragraph (b)(1) of new Rule 17g–8.

[662] *Compare* text of Public Law 111–203 § 938(a)(1), *with* text of proposed paragraph (b)(1) of new Rule 17g–8.

[663] *See* 15 U.S.C. 78o–7(s)(3)(B)(ii).

[664] *See* proposed new paragraph (a)(1)(ii)(L) of Rule 17g–7.

[665] *See* proposed paragraph (b)(2) of new Rule 17g–8.

[666] *Compare* text of Public Law 111–203 § 938(a)(2), *with* text of proposed paragraph (b)(2) of new Rule 17g–8.

[667] *See* Instructions to Exhibit 1 to Form NRSRO.

[668] *See* proposed amendments to Instructions to Exhibit 1 to Form NRSRO.

symbol, number, or score used by the NRSRO to denote a credit rating and to disclose those meanings in Exhibit 1 where investors and other users of credit ratings can find them.

Proposed paragraph (b)(3) of new Rule 17g–8 would require the NRSRO to have policies and procedures reasonably designed to apply any symbol, number, or score defined pursuant to paragraph (b)(2) of Rule 17g–8 in a manner that is consistent for all types of obligors, securities, and money market instruments for which the symbol, number, or score is used.[669] This proposed provision would mirror the text of Section 938(a)(3) of the Dodd-Frank Act, except that the proposed rule text would add the term "obligors."[670] The Commission proposes this addition in order to apply the provisions of proposed paragraph (b)(3) of new Rule 17g–8 to credit ratings of obligors as entities in addition to credit ratings of securities and money market instruments.[671]

Request for Comment

The Commission generally requests comment on all aspects of proposed paragraph (b) of new Rule 17g–8. The Commission also seeks comment on the following:

1. Is proposed paragraph (b)(1) of new Rule 17g–8 sufficiently explicit in terms of the objective that the policies and procedures be reasonably designed to assess the probability that an issuer of a security or money market instrument will default, fail to make timely payments, or otherwise not make payments to investors in accordance with the terms of the security or money market instrument)? If not, what additional detail should the Commission provide in terms of the clarifying the objective?

2. Is proposed paragraph (b)(2) of new Rule 17g–8 sufficiently explicit in terms of the objective that the policies and procedures be reasonably designed to clearly define the meaning of each symbol, number, or score used by the NRSRO to denote a credit rating category and notches within a category in the rating scale for each class and subclass of credit ratings for which the NRSRO is registered and to include such definitions in Exhibit 1 to Form NRSRO? If not, what additional detail should the Commission provide in terms of the clarifying the objectives?

3. Is proposed paragraph (b)(3) of new Rule 17g–8 sufficiently explicit in terms of the objective that the policies and procedures be reasonably designed to apply any symbol, number, or score defined in a manner that is consistent for all types of obligors, securities, and money market instruments for which the symbol, number, or score is used? If not, what additional detail should the Commission provide in terms of the clarifying the objective?

2. Proposed Amendment to Rule 17g–2

For the reasons discussed in Section II.A.2 of this release, the Commission preliminarily believes that the policies and procedures an NRSRO would be required, among other things, to document pursuant to proposed paragraph (b) of new Rule 17g–8 should be subject to the recordkeeping requirements of Rule 17g–2.[672] Consequently, the Commission proposes adding new paragraph (b)(14) to Rule 17g–2 to identify the policies and procedures an NRSRO must establish, maintain, enforce, and document pursuant to proposed paragraph (b) of new Rule 17g–8 as a record that must be retained.[673] As a result, the policies and procedures would be subject to the record retention and production requirements in paragraphs (c) through (f) of Rule 17g–2.[674]

Request for Comment

The Commission generally requests comment on all aspects of proposed new paragraph (b)(14) of Rule 17g–2.

K. Annual Report of Designated Compliance Officer

Section 932(a)(5) of the Dodd-Frank Act amended Section 15E(j) of the Exchange Act to re-designate paragraph (j) as paragraph (j)(1) and to add new paragraphs (j)(2) through (j)(5).[675] Section 15E(j)(1) of the Exchange Act contains a self-executing provision that an NRSRO designate an individual (the "designated compliance officer") responsible for administering the policies and procedures that are required to be established pursuant to Sections 15E(g) and (h) of the Exchange Act,[676] and for compliance with the securities laws and the rules and regulations thereunder, including those promulgated by the Commission under Section 15E of the Exchange Act.[677] Sections 15E(j)(2) through (4) prescribe self-executing requirements with respect to, among other things, the activities, duties, and compensation of the designated compliance officer.[678]

Section 15E(j)(5)(A) of the Exchange Act requires the designated compliance officer to submit to the NRSRO an annual report on the compliance of the NRSRO with the securities laws and the policies and procedures of the NRSRO that includes: (1) A description of any material changes to the code of ethics and conflict of interest policies of the NRSRO; and (2) a certification that the report is accurate and complete.[679] Section 15E(j)(5)(B) of the Exchange Act provides that the NRSRO shall file the report required pursuant to Section 15E(j)(5)(A) together with the financial report that is required to be submitted to the Commission under Section 15E of the Exchange Act.[680]

Consequently, Section 15E(j)(5)(B) of the Exchange Act contains a self-executing provision requiring the NRSRO to file the annual report of the designated compliance officer "with the financial report that is required to be submitted to the Commission under this section."[681] The Commission notes that Section 15E(k) of the Exchange Act provides that each NRSRO shall, on a confidential basis, file with the Commission, at intervals determined by the Commission, such financial statements, certified (if required by the rules or regulations of the Commission) by an independent public accountant, and information concerning its financial condition, as the Commission, by rule may prescribe as necessary or appropriate in the public interest or for the protection of investors.[682] The Commission implemented Section 15E(k) by adopting Rule 17g–3.[683] Therefore, under the self-executing provisions in Section 15E(j)(5)(B) of the Exchange Act, an NRSRO must file the

[669] *See* proposed paragraph (b)(1) of new Rule 17g–8.

[670] *Compare* text of Public Law 111–203 § 938(a)(3), *with* text of proposed paragraph (b)(3) of new Rule 17g–8.

[671] *See, e.g.,* the definition of "credit rating" in Section 3(a)(60) of the Exchange Act ("The term 'credit rating' means an assessment of the creditworthiness of an obligor as an entity or with respect to specific securities or money market instruments."). 15 U.S.C. 78o–7(a)(60).

[672] 17 CFR 240.17g–2.

[673] *See* proposed new paragraph (b)(14) to Rule 17g–2; *see also* Section 17(a)(1) of the Exchange Act, which requires an NRSRO to make and keep such records, and make and disseminate such reports, as the Commission prescribes by rule as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the Exchange Act. 15 U.S.C. 78q(a)(1).

[674] *See* 17 CFR 240.17g–2.

[675] *See* Public Law 111–203 § 932(a)(5) and 15 U.S.C. 78o–7(j)(1) though (5).

[676] *See* 15 U.S.C 780–7(g) and (h).

[677] *See* 15 U.S.C. 78o–7(j)(1).

[678] *See* 15 U.S.C. 78o–7(j)(1) though (4).

[679] *See* 15 U.S.C. 78o–7(j)(5)(A).

[680] *See* 15 U.S.C. 78o–7(j)(5)(B).

[681] *Id.*

[682] The Dodd-Frank Act replaced the words "furnish to the Commission" with the words "file with the Commission" in Section 15E(k) of the Exchange Act. *See* 15 U.S.C. 78o–7(k).

[683] *See* 17 CFR 240.17g–3; *see also Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33590–33593 (June 18, 2007).

report of the designated compliance officer with the reports required to be submitted pursuant to Rule 17g–3.[684]

As discussed above in Section II.A.3 of this release, Rule 17g–3 requires an NRSRO to furnish five or, in certain cases, six separate reports not more than 90 days after the end of the NRSRO's fiscal year.[685] In order to further clarify the self-executing requirement in Section 15E(j)(5)(B) of the Exchange Act, the Commission is proposing to amend Rule 17g–3 to identify the annual report of the designated compliance officer as one of the reports that must be filed with the Commission.[686] Specifically, the Commission proposes adding a new paragraph (a)(8) to Rule 17g–3 to identify the report on the compliance of the NRSRO with the securities laws and the policies and procedures of the NRSRO required to be filed with the Commission pursuant to Section 15E(j)(5)(B) of the Exchange Act.[687] New paragraph (a)(8) would provide that the report need not be audited. Furthermore, the Commission preliminarily does not intend to prescribe how the report must be certified because Section 15E(j)(5)(A)(ii) of the Exchange Act already provides that the designated compliance officer must certify that the report is accurate and complete.[688]

Request for Comment

The Commission generally requests comment on all aspects of proposed new paragraph (a)(8) of Rule 17g–3. The Commission also seeks comment on the following:

1. Should an NRSRO be required to attach to the annual report a signed statement by a duly authorized person (*e.g.,* the designated compliance officer) stating explicitly that the person has responsibility for the reports and, to the best knowledge of the person, the reports fairly present, in all material respects, the information contained in the reports? For example, because the designated compliance officer is providing the report to the NRSRO and the NRSRO, in turn, is submitting the report to the Commission, would it be appropriate for the Commission to require an additional certification addressing the submission of the report from the NRSRO to the Commission?

L. Electronic Submission of Form NRSRO and the Rule 17g–3 Annual Reports

An NRSRO currently submits the Form NRSROs required under Rule 17g–1 and the annual reports required under Rule 17g–3 to the Commission in paper form. The Commission proposes amending Rule 17g–1, the Instructions to Form NRSRO, Rule 17g–3, and Regulation S–T to require an NRSRO to use the Commission's EDGAR system to: (1) Electronically file or furnish, as applicable, Form NRSRO and the information and documents contained in Exhibits 1 through 9 of Form NRSRO if the submission is made pursuant to paragraph (e), (f) or (g) of Rule 17g–1 (*i.e.,* an update of registration, an annual certification, or a withdrawal from registration, respectively)[689] and (2) electronically file or furnish, as applicable, the annual reports required by Rule 17g–3.[690]

Under this proposal, however, an applicant or NRSRO would continue to submit in paper format Form NRSROs pursuant to paragraphs (a), (b), (c), and (d) of Rule 17g–1 (initial applications for registration, applications to register for an additional class of credit ratings, supplements to an initial application or application to register for an additional class of credit ratings, and withdrawals of initial applications or applications to register for an additional class of credit ratings, respectively).[691] The Commission preliminarily believes that these materials are appropriately received in paper form because of the iterative nature of the NRSRO application process. For example, an applicant often will have a number of phone conferences and meetings with the Commission staff during the application process to clarify the information submitted in the application. These interactions may result in applicants informally providing additional information relating to the application and informally amending or augmenting information provided in the Form and its Exhibits. The Commission preliminarily believes paper submissions facilitate this type of iterative process.

In terms of requiring the electronic submission of Form NRSROs submitted pursuant to paragraph (e), (f), or (g) of Rule 17g–1, the Commission notes that one of the primary goals of the EDGAR system is to facilitate the rapid dissemination of financial and business information in connection with filings the Commission receives. Although paragraph (i) of Rule 17g–1 currently requires NRSROs to make the public portions of their current Form NRSROs publicly available within 10 business days after submission to the Commission, the Commission believes having all such information available immediately in one location would make the information more easily available and searchable to investors and other users of credit ratings. Further, the Commission believes submissions to the Commission are more valuable to investors and other users of credit ratings if they are available in electronic format and that adding the Form NRSRO submissions to the EDGAR database would provide a more complete picture for the public. The Commission preliminarily believes that, as a result of the proposals, the EDGAR page of the Commission's Internet Web site[692] and the NRSRO page of the Commission's Internet Web site[693] would be a comprehensive source containing most public information submitted to the Commission, as well as other information, related to NRSROs. The Commission preliminarily believes that the electronic submission of Form NRSROs would benefit investors and other users of credit ratings by

[684] *See* 15 U.S.C. 78o–7(j)(5)(B), 15 U.S.C. 78o–7(k), and 17 CFR 240.17g–3.

[685] *See* 17 CFR 240.17g–3(a)(1)–(6). As discussed above in Section II.A.3 of this release, the Commission is proposing that Rule 17g–3 be amended to add a new paragraph (a)(7) to implement Section 15E(c)(3)(B) of the Exchange Act by requiring an NRSRO to file the annual report on the NRSRO's internal control structure with the annual reports. *See* 15 U.S.C. 78o–7(c)(3)(B).

[686] *See* proposed new paragraph (a)(8) of Rule 17g–3.

[687] *Id.*

[688] *See* 15 U.S.C. 78o–7(j)(5)(A)(ii). Paragraph (b) of Rule 17g–3 provides that the NRSRO must attach to the reports required to be submitted pursuant to Rule 17g–3 a signed statement by a duly authorized person that the person has responsibility for the reports and, to the best knowledge of the person, the reports fairly present, in all material respects, the information contained in the reports. *See* 17 CFR 240.17g–3(b).

[689] *See* 17 CFR 240.17g–1(e), (f), and (g). The electronic submissions of Form NRSRO and Exhibits 1 through 9 of Form NRSRO would be made available to the public immediately upon filing.

[690] *See* 17 CFR 240.17g–3. An NRSRO is not required to make the Rule 17g–3 annual reports publicly available and the reports would not be available to the public on EDGAR. The information collected pursuant to Rule 17g–3 is, and would continue to be, kept confidential to the extent permitted by the Freedom of Information Act ("FIOA"). *See* 15 U.S.C. 552 *et seq.*

[691] Paragraph (i) of Rule 17g–1 requires an NRSRO to make Form NRSRO and information and documents submitted in Exhibits 1 through 9 publicly available within 10 business days of the Commission order granting an initial application for registration or an application to register for an additional class of credit ratings. 17 CFR 240.17g–1(i). The initial application for registration contains information and documents the NRSRO is not required to make publicly available. This includes Exhibits 10 through 13 to Form NRSRO, disclosure reporting pages to Form NRSRO, and certifications from QIBs under Section 15E(a)(1)(C) of the Exchange Act (15 U.S.C. 780–7(a)(1)(C)).

[692] *http://www.sec.gov/investor/pubs/edgarguide.htm.*

[693] *http://www.sec.gov/divisions/marketreg/ratingagency.htm.*

increasing the efficiency of retrieving and comparing NRSRO public submissions and enabling the investors and other users of credit ratings to access information more quickly. An investor or other user of credit ratings would be able to find and review a Form NRSRO on any computer with an Internet connection by accessing EDGAR data on the Commission's Internet Web site or through a third party.

In addition, while the Rule 17g–3 annual reports would not be made public through the EDGAR system, having these reports and the Form NRSROs available on EDGAR could assist the Commission in its oversight of NRSROs. For example, Commission examiners could retrieve more easily the Form NRSROs and annual reports of a specific NRSRO to prepare for an examination. Moreover, having these records submitted and stored through the EDGAR system (*i.e.,* in a centralized location) would assist the Commission from a records management perspective by establishing a more automated storage process and creating efficiencies in terms of reducing the volume of paper submissions that must be manually processed and stored.

Moreover, the Commission preliminarily believes that the electronic submission of Form NRSRO and Rule 17g–3 annual reports would benefit NRSROs. For example, NRSROs would avoid the uncertainties, delay, and expense related to the manual delivery of paper submissions. Further, NRSROs would benefit from no longer having to submit multiple paper copies of these forms and reports to the Commission.

As with other entities that make submissions through the EDGAR systems, these submissions would be subject to the provisions of Regulation S–T [694] and the EDGAR Filer Manual. Regulation S–T includes detailed rules concerning mandatory and permissive electronic EDGAR submissions. It also provides that requests for confidential treatment must be made in paper form.[695] The EDGAR Filer Manual contains detailed technical specifications concerning EDGAR submissions. The EDGAR Filer Manual also provides technical guidance concerning how to begin making submissions on EDGAR by submitting Form ID to obtain a CIK number [696] and confidential access codes and how to maintain and update company data (*e.g.,* how to change company names and contact information).[697]

One technical specification the EDGAR Filer Manual includes is the electronic "submission type" for each submission made through the EDGAR system. The Commission expects the EDGAR electronic submission types for these documents would be designed to facilitate and expedite the submission and review of these submissions. Consistent with this proposal, the Commission preliminarily intends the EDGAR Filer Manual and the EDGARLink software would provide for two EDGAR electronic submission types: one for the submission of Form NRSRO and one for the submission of the annual reports pursuant to Rule 17g–3. The Commission also preliminarily intends that Form NRSRO would become an electronic, fillable, form and that the Exhibits would be submitted with the Form.

As noted above, an NRSRO is not required to make the Rule 17g–3 annual reports public. Therefore, the Rule 17g–3 annual reports would be submitted through the EDGAR system on a confidential basis and would not be made available to the public to the extent permitted by law. The Commission anticipates that the EDGAR Filer Manual would provide guidance for choosing the correct submission type.

Amendments to Rule 17g–1. To implement the electronic submission through EDGAR of a Form NRSRO submitted to the Commission pursuant to paragraph (e), (f), or (g) of Rule 17g–1, the Commission proposes to amend each of those paragraphs to add a second sentence providing that a Form NRSRO and the information and documents in Exhibits 1 through 9, filed or furnished, as applicable, under the paragraph must be submitted electronically to the Commission in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T.[698] Furthermore, the Commission proposes amending paragraphs (a), (b), (c), and (d) of Rule 17g–1 to provide that an NRSRO should file "two paper copies" of the Form NRSROs filed pursuant to those paragraphs. This would be designed to clarify that these filings should continue to be made in paper. In addition, in the past, some NRSROs have submitted more than two paper copies of their Form NRSRO submissions. The Commission believes that the filing of two paper copies is sufficient.

Amendments to the Instructions to Form NRSRO. To further implement the electronic submission through the EDGAR system of Form NRSROs submitted to the Commission pursuant to paragraphs (e), (f), or (g) of Rule 17g–1, the Commission proposes amending Instruction A.8 to Form NRSRO to distinguish between Form NRSRO submissions under paragraph (a), (b), (c), or (d) of Rule 17g–1 (which would continue to be submitted in paper form) and submissions under paragraphs (e), (f), or (g) of Rule 17g–1 (which would be submitted electronically through the EDGAR system). Currently, Instruction A.8 simply provides the address where a Form NRSRO submitted under paragraph (a), (b), (c), (d), (e), (f), or (g) of Rule 17g–1 must be submitted (*i.e.,* the headquarters of the Commission). The Commission proposes amending Instruction 8.A to add above the address a sentence that would instruct an applicant to submit to the Commission at the address indicated below two paper copies of a Form NRSRO submitted pursuant to paragraph (a), (b), (c), or (d) of Rule 17g–1.[699] The Commission further proposes adding a sentence below the address providing that after registration, an NRSRO must submit Form NRSRO electronically to the Commission in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T, if the submission is made pursuant to paragraphs (e), (f), or (g) of Rule 17g–1.[700]

Finally, the Commission proposes amending Instruction A.9 to Form NRSRO, which currently provides that a Form NRSRO will be considered furnished to the Commission on the date the Commission receives a complete and properly executed Form NRSRO that follows all applicable instructions for the Form.[701] The Commission proposes amending the instruction to read as follows: "A Form NRSRO will be considered filed with or furnished to, as applicable, the Commission on the date the Commission receives a complete and properly executed Form NRSRO that

[694] For a comprehensive discussion of Regulation S–T and electronic filing, *see* "Electronic Filing and the EDGAR System: A Regulatory Overview," available on the Commission's Internet Web site.

[695] *See* 17 CFR 232.101.

[696] As noted earlier, a CIK number is a ten-digit number uniquely identifying the person submitting the form or report.

[697] In the case of name changes, the changes must be made via the EDGAR filing Internet Web site in advance and the new name would be reflected in the next EDGAR submission. The name on past submissions would not change.

[698] *See* proposed amendments to paragraphs (e), (f), and (g) of Rule 17g–1.

[699] *See* proposed amendments to Instruction A.8 of Form NRSRO.

[700] *Id.*

[701] *See* Instruction A.9 to Form NRSRO.

follows all applicable instructions for the Form, including the instructions in Item A.8 with respect to how a Form NRSRO must be filed with or furnished to the Commission."[702] This instruction would be designed to clarify that a Form NRSRO submitted pursuant to paragraph (e), (f), or (g) of Rule 17g–1 must be submitted electronically.

Proposed Amendments to Rule 17g–3. To implement the electronic submission through the EDGAR system of the Rule 17g–3 annual reports, the Commission proposes adding two new paragraphs to Rule 17g–3: paragraphs (d) and (e).[703] Similar to the proposed amendments to paragraphs (e), (f), and (g) of Rule 17g–1, proposed new paragraph (d) of Rule 17g–3 would provide that the reports required by the rule must be submitted electronically with the Commission in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T.[704] In addition, because the Rule 17g–3 annual reports are not required to be made public, the Commission proposes adding new paragraph (e) to Rule 17g–3.[705] Proposed new paragraph (e) would, in the first sentence, instruct an NRSRO that information submitted on a confidential basis and for which confidential treatment has been requested pursuant to applicable Commission rules will be accorded confidential treatment to the extent permitted by law.[706] Proposed new paragraph (e) of Rule 17g–3 would, in the second sentence, instruct an NRSRO that confidential treatment may be requested by marking each page "Confidential Treatment Requested" and by complying with Commission rules governing confidential treatment.[707]

Proposed Amendments to Regulation S–T. Regulation S–T requires the electronic filing of any amendments and related correspondence and supplemental information pertaining to a document that is the subject of mandated EDGAR submission.[708] The Commission proposes amending Rule 101 of Regulation S–T[709] by adding a new paragraph (a)(1)(xiv).[710] Proposed new paragraph (a)(1)(xiv) would identify the Form NRSROs and the information and documents submitted in Exhibits 1 through 9 of Form NRSRO submitted to the Commission pursuant to paragraphs (e), (f), and (g) of Rule 17g–1 and the annual reports submitted pursuant to Rule 17g–3 as submissions that must be made in electronic format.[711]

The Commission also is proposing an amendment to Rule 201 of Regulation S–T.[712] Rules 201 and 202[713] of Regulation S–T address hardship exemptions from EDGAR filing requirements, and paragraph (b) of Rule 13 of Regulation S–T[714] addresses the related issue of filing date adjustments. Under Rule 201, if an electronic filer experiences unanticipated technical difficulties that prevent the timely preparation and submission of an electronic filing, the filer may file a properly legended paper copy[715] of the filing under cover of Form TH no later than one business day after the date on which the filing was made.[716] A filer who files in paper form under the temporary hardship exemption must submit an electronic copy of the filed paper document within six business days of the filing of the paper document.[717]

In addition, an electronic filer may apply for a continuing hardship exemption under Rule 202 if it cannot file all or part of a filing without undue burden or expense.[718] The application must be made at least 10 business days before the due date of the filing. In contrast to the self-executing temporary hardship exemption process, a filer can obtain a continuing hardship exemption only by submitting a written application, upon which the Commission, or the Commission staff pursuant to delegated authority, must then act. Under paragraph (b) of Rule 13 of Regulation S–T, if an electronic filer in good faith attempts to file a document, but the filing is delayed due to technical difficulties beyond the filer's control, the filer may request that the Commission grant an adjustment of the filing date.

The Commission is proposing to make the temporary hardship exemption in Rule 201 unavailable for the submissions of Form NRSRO and the information and documents submitted in Exhibits 1 through 9 of Form NRSRO under paragraph (e), (f), or (g) of Rule 17g–1 and the annual reports required under Rule 17g–3.[719] Specifically, the Commission is proposing to amend paragraph (a) of Rule 201 of Regulation S–T to add this group of submissions to the list of submissions for which the temporary hardship exemption is unavailable.[720] An NRSRO would continue to have the ability to apply for a continuing hardship exemption under Rule 202 if it could not submit all or part of an application without undue burden or expense or for an adjustment of the due date under paragraph (b) of Rule 13 if there were technical difficulties beyond the NRSRO's control.

For the foregoing reasons, the Commission proposes amending Regulation S–T: (1) to provide for the mandatory electronic submission of Form NRSRO and the information and documents contained in Exhibits 1 through 9 of Form NRSRO pursuant to paragraphs (e), (f), or (g) of Rule 17g–1 and the annual reports pursuant to Rule 17g–3;[721] and (2) to amend paragraph (a) of Rule 201 to make the temporary hardship exemption unavailable for submissions of Form NRSROs and the information and documents contained in Exhibits 1 through 9 under paragraphs (e), (f), or (g) of Rule 17g–1 and the annual reports under Rule 17g–3.[722]

Request for Comment

The Commission generally requests comment on all aspects of these proposals to require the electronic submission of Form NRSRO under paragraphs (e), (f), and (g) of Rule 17g–1 and the annual reports under Rule 17g–3. The Commission also seeks comment on the following:

1. Should applicants be required to submit Form NRSRO electronically under paragraph (a), (b), (c), or (d) of Rule 17g–1?

2. What would be the impact of making the Form NRSROs required under paragraphs (e), (f), and (g) of Rule

[702] *See* proposed amendments to Instruction A.9 to Form NRSRO.

[703] *See* proposed new paragraphs (d) and (e) of Rule 17g–3.

[704] *See* proposed new paragraph (d) of Rule 17g–3.

[705] *See* proposed new paragraph (e) of Rule 17g–3.

[706] *See* the first sentence of proposed new paragraph (e) of Rule 17g–3.

[707] *See* the second sentence of proposed new paragraph (e) of Rule 17g–3.

[708] *See* 17 CFR 232.101(a)(1).

[709] 17 CFR 232.101(a)(1).

[710] *See* proposed paragraph (a)(1)(xiv) of Rule 101 under Regulation S–T.

[711] Related correspondence and supplemental information are not automatically disseminated publicly through the EDGAR system but are immediately available to the Commission staff.

[712] 17 CFR 232.201

[713] 17 CFR 232.202.

[714] 17 CFR 232.13(b).

[715] *See* 17 CFR 232.201(a).

[716] 17 CFR 239.65, 249.447, 269.10, and 274.404.

[717] *See* 17 CFR 232.201(b).

[718] *See* 17 CFR 232.202(a).

[719] The Commission previously has made unavailable the ability for filers to use the temporary hardship exemption for EDGAR submissions of beneficial ownership reports filed by officers, directors and principal security holders under Section 16(a) of the Exchange Act. *See* Securities Act Release No. 8230 (May 7, 2003), 68 FR 25788 (May 13, 2010).

[720] *See* proposed amendment to paragraph (a) of Rule 201 of Regulation S–T.

[721] *See* proposed new paragraph (a)(1)(xiv) to Rule 101 of Regulation S–T.

[722] *See* proposed amendment to paragraph (a) of Rule 201 of Regulation S–T.

17g–1 and the annual reports required under Rule 17g–3 mandatory electronic submissions? Are there additional burdens or costs that would result from requiring these submissions to be made electronically?

3. Are there any other difficulties and considerations unique to these proposed requirements? If so, what aspect of the proposed requirements would be burdensome? Are there other alternatives that would be less burdensome? Provide specific details and alternative approaches.

4. Should NRSROs be required to submit the financial information in Form NRSRO and the information and documents contained in Exhibits 1 through 9 and the Rule 17g–3 annual reports using the XBRL format? Should NRSROs be required to use eXtensible Markup Language (XML) for EDGAR for non-financial information? Provide detailed information on any difficulties and considerations as well as benefits concerning such requirements.

5. Should the temporary hardship exemption be available for submission of these filings?

M. Other Amendments

The Commission is proposing additional amendments to several of the NRSRO rules in response to amendments the Dodd-Frank Act made to sections of the Exchange Act that authorize or otherwise are relevant to these rules.

1. Changing "Furnish" to "File"

Section 932(a) of the Dodd-Frank Act amended Section 15E of the Exchange Act to replace the word "furnish" with the word "file" in paragraphs (b), (d), (k), and (l).[723] In addition, Section 932(a) of the Dodd-Frank Act amended paragraph (j) of Section 15E of the Exchange to, among other things, add a requirement that an NRSRO "file" a report of the designated compliance officer.[724] The Dodd-Frank Act, however, did not replace the word "furnish" with the word "file" in Section 15E(a) (which governs the submission of initial applications for registration as an NRSRO), Section 15E(e) (which governs the submission of voluntary withdrawals from registration), and Section 17(a)(1) (which provides the Commission with authority to, among other things, require NRSROs to furnish reports).[725] Consistent with the amendments to Section 15E described above, the Commission is proposing to amend Rule 17g–1 and Rule 17g–3 to treat certain of the submissions required in those rules as "filings" rather than "furnishings."[726] The Commission also is proposing to make corresponding amendments to Form NRSRO and the Instructions to Form NRSRO.

The Commission proposes amending paragraphs (a), (b), (c), and (d) of Rule 17g–1 to treat Form NRSROs submitted pursuant to those provisions as "filings" rather than "furnishings."[727] These paragraphs govern the submissions of initial applications for registration as an NRSRO. The Commission notes that the Dodd-Frank Act did not replace the word "furnish" with the word "file" in Section 15E(a) of the Exchange Act, which addresses the submission of initial applications for registration. The Commission, however, preliminarily believes that this was an inadvertent omission. For example, Section 15E(b)(1) refers to information "required to be *filed*" under Section 15E(a)(1)(B)(i) of the Exchange Act (emphasis added).[728] Similarly, Section 15E(d)(1)(B) of the Exchange Act refers to "the date on which an application for registration is *filed* with the Commission" (emphasis added).[729] In addition, the legislative history of Section 932(a) states that "[Title IX, Subtitle C, of the Dodd-Frank Act] requires all references to 'furnish' be replaced with the word 'file' in existing law."[730] For these reasons, the Commission proposes to amend paragraphs (a), (b), (c), and (d) of Rule 17g–1 to treat the submissions pursuant to those paragraphs as "filings."

The Commission proposes amending paragraphs (e) and (f) of Rule 17g–1 to treat Form NRSROs submitted pursuant to those provisions as "filings" rather than "furnishings."[731] As noted above, Section 932(a) of the Dodd-Frank Act amended Section 15E(b) of the Exchange Act to replace the word "furnish" with the word "file."[732] Section 15E(b) of the Exchange Act addresses updating Form NRSRO to keep it current and the submission of the annual certification.[733] Paragraphs (e) and (f) of Rule 17g–1 govern the submission of updated Form NRSROs and annual certifications, respectively.[734] Consequently, the Commission proposes amending these paragraphs to treat the submissions of an updated Form NRSRO and an annual certification, respectively, as "filings" rather than "furnishings."[735]

The Commission is not proposing to amend paragraph (g) of Rule 17g–1 to replace the word "furnish" with the word "file." This paragraph implemented Section 15E(e) of the Exchange Act, which addresses the submission by an NRSRO of a written notice to voluntarily withdraw a registration.[736] The Commission preliminarily believes that it is not necessary to subject a notice of withdrawal of registration to the higher standards of a "filing."

Given the proposed amendments to paragraphs (a), (b), (c), (d), (e), and (f) of Rule 17g–1, the Commission proposes amending paragraphs (h) and (i) of Rule 17g–1 to reflect that a Form NRSRO would be "filed" with the Commission under the proposed amendments to paragraphs (a), (b), (c), (d), (e), and (f) of Rule 17g–1 and "furnished" to the Commission under paragraph (g) of Rule 17g–1.

The Commission is proposing to amend paragraphs (a)(1) through (a)(5) of Rule 17g–3 to treat the reports submitted pursuant to those provisions as "filings" rather than "furnishings."[737] As noted above, Section 932(a) of the Dodd-Frank Act amended Section 15E(k) of the Exchange Act to replace the word "furnish" with the word "file."[738] Section 15E(k) of the Exchange Act provides the Commission with authority to require NRSROs to submit annual financial reports.[739] The Commission adopted paragraphs (a)(1) through (a)(5) of Rule 17g–3 under Section 15E(k).[740] Consequently, the Commission proposes amending Rule 17g–3 to treat the reports identified in paragraphs (a)(1) through (a)(5) as "filings" rather than "furnishings."[741]

[723] *See* Public Law 111–203 § 932(a) and 15 U.S.C. 78o–7(b), (d), (k), and (l).

[724] *See* Public Law 111–203 § 932(a) and 15 U.S.C. 78o–7(j)(5).

[725] *See* 15 U.S.C. 78o–7(e) and 15 U.S.C. 78q(a)(1).

[726] Among other things, an application, report, or document "filed" with the Commission pursuant to the Exchange Act or the rules thereunder is subject to the provisions of Section 18 of the Exchange Act. *See* 15 U.S.C. 78o–7r.

[727] *See* proposed amendments to paragraphs (a), (b), (c), and (d) of Rule 17g–1.

[728] *See* 15 U.S.C. 78o–7(a)(1)(B)(i).

[729] *See* 15 U.S.C. 78o–7(d)(1)(B).

[730] *See Conference Report,* H.R. 4173 (June 29, 2010), p. 872.

[731] *See* proposed amendments to paragraphs (e) and (f) of Rule 17g–1.

[732] *See* Public Law 111–203 § 932(a)(1) and 15 U.S.C. 78o–7(b).

[733] *See* 15 U.S.C. 78o–7(b)(1) and (2).

[734] *See* 17 CFR 240.17g–1(e) and (f).

[735] *See* proposed amendments to paragraphs (e) and (f) of Rule 17g–1.

[736] *See* 15 U.S.C. 78o–7(e) and 17 CFR 240.17g–1(g).

[737] *See* proposed amendments to paragraphs (a)(1) through (5) of Rule 17g–3.

[738] *See* Public Law 111–203 § 932(a)(6) and 15 U.S.C. 78o–7(k).

[739] *See* 15 U.S.C. 78o–7(k).

[740] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33590–33593 (June 18, 2007).

[741] *See* 15 U.S.C. 78o–7(k) and proposed amendments to paragraphs (a)(1)–(5) of Rule 17g–3.

In addition, the Commission proposes that the new report on internal controls discussed in Section II.A.3 of this release and the new report of the designated compliance officer discussed in Section II.K of this release be treated as "filings" rather than "furnishings."[742] Section 15E(c)(3)(B) of the Exchange Act provides, among other things, that the Commission shall prescribe rules requiring NRSROs to "submit" to the Commission an internal controls report.[743] In addition, Section 15E(j)(5)(B) of the Exchange Act, "Submission of reports to the Commission," provides that an NRSRO "shall file" the report of the designated compliance officer together with the financial report that is required to be "submitted" to the Commission under Section 15E of the Exchange Act.[744] As discussed in Section II.K of this release, the financial reports are submitted pursuant to Rule 17g–3, which was adopted under Section 15E(k).[745] Moreover, as noted above, the Section 932(a)(6) of the Dodd-Frank Act amended Section 15E(k) of the Exchange Act to replace the word "furnish" with the word "file."[746] Consequently, given the interchangeable use of the word "submit" with the word "file" in Section 15E(j)(5)(B) and the legislative history discussed above, the Commission proposes to treat the new report on internal controls as a "filing."[747] As noted above, Section 15E(j)(5)(B) of the Exchange Act explicitly provides that an NRSRO "shall file" the report of the designated compliance officer.[748] Therefore, the Commission proposes to use the term "file" in proposed new paragraph (a)(8) of Rule 17g–3.[749]

The Commission does not propose to amend paragraph (a)(6) of Rule 17g–3 to treat the report identified in that paragraph as a filing. This paragraph was adopted under Section 17(a)(1) of the Exchange Act.[750] Section 17(a)(1) of the Exchange Act provides that any report an NRSRO "is required by Commission rules under this paragraph to make and disseminate to the Commission shall be deemed furnished to the Commission."[751] As noted above, the Dodd-Frank Act did not change this provision to make the report a "filing."

The Commission is proposing to amend Form NRSRO and the Instructions to Form NRSRO to conform the Form and its Instructions to the proposed amendments discussed above.[752] Under the proposed amendments, the Commission would replace the word "furnish" with the word "file" when referring to a Form NRSRO submitted under paragraphs (a), (b), (c), (d), (e), and (f) of Rule 17g–1. In addition, in some cases, the Commission proposes using the term "submit" when referring to a Form NRSRO that may have been submitted prior to enactment of the Dodd-Frank Act when the submission would have been "furnished to" as opposed to "filed with" the Commission. The Commission intends the word "submit" as used in this context to mean the submission was either "furnished" or "filed" depending on the applicable securities laws in effect at the time of the submission.

Request for Comment

The Commission generally requests comment on all aspects of these proposals to replace the word "furnish" with the word "file" in the Commission's NRSRO rules.

2. Amended Definition of NRSRO

As discussed above in Section II.I.1.c of this release, the first prong of the definition of "nationally recognized statistical rating organization" in Section 3(a)(62) of the Exchange Act, prior to being amended by the Dodd-Frank Act, provided that the entity "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 under Section 15E."[753] Section 932(b) of the Dodd-Frank Act deleted this prong of the definition.[754] Instruction F.4 to Form NRSRO contains a definition of "NRSRO" that incorporates the Section 3(a)(62) definition as originally enacted. The Commission proposes amending this definition to conform it to the Section 3(a)(62) definition as amended by the Dodd-Frank Act.[755]

Request for Comment

The Commission generally requests comment on all aspects of this proposal to amend the definition of NRSRO in Instruction F.4 to Form NRSRO.

3. Definition of Asset-Backed Security

Several of the Commission's NRSRO rules impose requirements specific to credit ratings for structured finance products by providing that the rules apply to credit ratings with respect to "a security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed-securities transaction."[756] This language mirrors the text of Section 15E(i) of the Exchange Act, which provides the Commission with authority to prohibit an NRSRO from the practice of "lowering or threatening to lower a credit rating on, or refusing to rate, securities or money market instruments issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction, unless a portion of the assets within such pool or part of such transaction, as applicable, also is rated by the [NRSRO]."[757] As noted earlier, with respect to this language, the Commission has provided the following interpretation,

> The term "structured finance product" as used throughout this release refers broadly to any security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction. This broad category of financial instrument includes, but is not limited to, asset-backed securities such as residential mortgage-backed securities ("RMBS") and to other types of structured debt instruments such as collateralized debt obligations ("CDOs"), including synthetic and hybrid CDOs, or collateralized loan obligations ("CLOs").[758]

Section 941(a) of the Dodd-Frank Act amended Section 3 of the Exchange Act to add paragraph (a)(77), which defines the term "asset-backed security."[759] The Exchange Act definition of "asset-backed security," includes a "collateralized mortgage obligation."[760] Consequently, the Commission preliminarily believes that the current identification of structured finance products in the Commission's rules (*i.e.,* "a security or money market instrument

[742] *See* proposed new paragraphs (a)(7) and (a)(8) of Rule 17g–3.

[743] *See* 15 U.S.C. 78o–7(c)(3)(B).

[744] *See* 15 U.S.C. 78o–7(j)(5)(B).

[745] *See* 15 U.S.C. 78o–7(k) and 17 CFR 240.17g–3; *see also Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33590–33593 (June 18, 2007).

[746] *See* Public Law 111–203 § 932(a)(6) and 15 U.S.C. 78o–7(k).

[747] *See* proposed new paragraph (a)(7) of Rule 17g–3.

[748] *See* 15 U.S.C. 78o–7(j)(5)(B).

[749] *See* proposed new paragraph (a)(8) of Rule 17g–3.

[750] *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6464–65 (Feb. 9, 2009).

[751] *See* 15 U.S.C. 78o–7q(a)(1).

[752] *See* proposed amendments to Form NRSRO and the Instructions to Form NRSRO.

[753] *See* Section 3(a)(62)(A) of the Exchange Act (15 U.S.C. 78c(a)(62)(A) added by the Rating Agency Act of 2006.

[754] *See* Public Law 111–203 § 932(b).

[755] *See* proposed amendment to Instruction F.4 to Form NRSRO.

[756] *See* paragraphs (a)(2)(iii), (a)(7), and (b)(9) of Rule 17g–2; paragraph (a)(6) of Rule 17g–3; paragraphs (a)(3) and (b)(9) of Rule 17g–5; and paragraph (a)(4) of Rule 17g–6.

[757] *See* 15 U.S.C. 78o–7(i).

[758] *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63832, footnote 3 (Dec. 4, 2009).

[759] *See* Public Law 111–203 § 941(a) and 15 U.S.C. 78c(a)(77).

[760] *See* 15 U.S.C. 78c(a)(77)(A)(i).

issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction") may have redundant terms insomuch as given the new definition of "asset-backed security" in Section 3(a)(77) of the Exchange Act an "asset-backed securities transaction" would include a "mortgage-backed securities transaction."[761] Accordingly, the Commission is proposing to delete the term "or mortgage-backed" from the identification of structured finance products in these rules.[762] The term "asset-backed security[y]" as used in the proposed new NRSRO rule definition would mean an "asset-backed security" as defined in Section 3(a)(77) of the Exchange Act. The term "security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction" would include an asset-backed security as defined in Section 3(a)(77) of the Exchange Act and other structured finance products relating to asset-backed securities such as synthetic CDOs.

Request for Comment

The Commission generally requests comment on all aspects of these proposals to delete the term "or mortgage-backed" from the identification of structured finance products in the NRSRO rules. The Commission also seeks comment on the following:

1. Would the proposal to delete the term "or mortgage-backed" from the identification of structured finance products in the NRSRO rules change the requirements of these rules in any way? For example, would it exclude certain types of structured finance products that currently are within the scope of these rules by narrowing the definition? Alternatively, would it add certain types of structured finance products that currently are outside the scope of these rules by broadening the definition?

4. Other Amendments to Form NRSRO

The Commission is proposing additional amendments to the Instructions to Form NRSRO to clarify certain requirements because the instructions, as written, have created some confusion among NRSROs.

a. Clarification With Respect to Items 6 and 7

The Commission is proposing amendments to Form NRSRO and the Instructions for Form NRSRO to remove potential ambiguity as to how an applicant and NRSRO must determine the approximate number of credit ratings outstanding for the purposes of Items 6 and 7. In addition, the Commission is seeking comment on how certain types of obligors, securities, and money market instruments should be classified for the purposes of Items 6 and 7.

Item 6 requires a credit rating agency applying to be registered as an NRSRO or an NRSRO applying to be registered in a new class of credit ratings to provide, among other things, the approximate number of credit ratings it has outstanding as of the date of the application in each class of credit ratings for which it is seeking registration.[763] Item 7 requires an NRSRO submitting a Form NRSRO for the purpose of updating information in the Form, making the annual certification, or withdrawing a registration to provide, among other things, the approximate number of credit ratings it had outstanding as of the end of the most recently ended calendar year in each class of credit ratings for which it is registered.[764] As noted earlier, the classes of credit ratings for which an NRSRO can be registered are: (1) financial institutions, brokers, or dealers;[765] (2) insurance companies;[766] (3) corporate issuers;[767] (4) issuers of asset-backed securities (as that term is defined in Section 1101(c) of part 229 of Title 17, Code of Federal Regulations, as in effect on the date of enactment of this paragraph);[768] and (5) issuers of government securities, municipal securities, or securities issued by a foreign government.[769]

NRSROs have raised questions about how they should count the number of credit ratings outstanding in a given class of credit ratings for the purposes of Form NRSRO.[770] For example, in some classes, certain NRSROs count the number of issuers rated but not the number of securities or money market instruments rated.[771] Other NRSROs count the number of securities or money market instruments rated (but do include the number of rated obligors in the total).[772] Finally, some NRSROs count the number of obligors, securities, and money market instruments rated.[773]

The Commission's intent in Items 6 and 7 is to elicit the total number of obligors, securities, and money market instruments in a given class of credit ratings for which the applicant or NRSRO has assigned a credit rating that was outstanding as of the applicable date (*i.e.,* the date of the application in the case of Item 6 and the date of the most recent calendar year-end in the case of Item 7). Consequently, to make the Commission's expectations more clear, the Commission is proposing to amend the text in Items 6.A and 7.A of Form NRSRO to clarify that an applicant or NRSRO must provide the approximate number of obligors, securities, and money market instruments in each class of credit ratings for which the applicant or NRSRO has an outstanding credit rating.[774] The text in Items 6.A and 7.A currently provides that the applicant or NRSRO must provide the approximate number of credit ratings outstanding. Consequently, the amendment would clarify that the applicant or NRSRO must provide the number of "obligors, securities, and money market instruments" in the given class for which the applicant or NRSRO assigned a credit rating that was outstanding as of the applicable date.

In addition, the Commission is proposing to amend Instruction H to Form NRSRO (as it relates to Items 6.A and 7.A) in four ways. First, in conformity with the proposed amendments to the text of Items 6.A and 7.A in the Form, the Instructions would be amended to provide that the applicant or NRSRO must, for each class of credit ratings, provide in the appropriate box the approximate number of obligors, securities, and money market instruments in that class for which the applicant or NRSRO presently has a credit rating outstanding as of the date of the application (Item 6.A) or had a credit rating outstanding as of the most recently ended calendar year (Item 7.A).

Second, Instruction H would be amended to provide that the applicant or NRSRO must treat as a separately rated security or money market instrument each individually rated security and money market instrument that, for example, is assigned a distinct CUSIP or other unique identifier, has distinct credit enhancement features as compared with other securities or money market instruments of the same

[761] *See* 15 U.S.C. 78c(a)(77)(A).

[762] *See* proposed amendments to paragraphs (a)(2)(iii), (a)(7), and (b)(9) of Rule 17g–2; paragraph (a)(6) of Rule 17g–3; paragraphs (a)(3) and (b)(9) of Rule 17g–5; and paragraph (a)(4) of Rule 17g–6.

[763] *See* Item 6 of Form NRSRO and Instructions B, C, D, and H (as it relates to Item 6) to Form NRSRO.

[764] *See* Item 7 of Form NRSRO and Instructions E, F, G, and H (as it relates to Item 7) to Form NRSRO.

[765] *See* 15 U.S.C. 78c(a)(62)(A)(i).

[766] *See* 15 U.S.C. 78c(a)(62)(A)(ii).

[767] *See* 15 U.S.C. 78c(a)(62)(A)(iii).

[768] *See* 15 U.S.C. 78c(a)(62)(A)(iv).

[769] *See* 15 U.S.C. 78c(a)(62)(A)(v).

[770] *See, e.g.,* GAO Report 10–782, pp. 46–47.

[771] *Id.*

[772] *Id.*

[773] *Id.*

[774] *See* proposed amendments to the text in Items 6.A and 7.A respectively.

issuer, or has a different maturity date as compared with other securities or money market instruments of the same issuer. This proposed instruction would be designed to clarify that each security or money market instrument of an issuer must be included in the count if it is assigned a credit rating by the applicant or NRSRO. For example, if the issuer is in the structured finance class, each tranche of the structured finance product that is assigned a credit rating must be included in the count. In addition, if an issuer issues securities or money market instruments that have different maturities, the applicant or NRSRO must include each such security in the count if the NRSRO assigns a credit rating to the security or money market instrument.

Third, Instruction H would be amended to provide that the applicant or NRSRO must not include an obligor, security, or money market instrument in more than one class of credit rating. In other words, the applicant or NRSRO cannot double count an obligor, security, or money market instrument by including it in the totals for two or more classes of credit ratings. For example, some securities have characteristics that could cause an applicant or NRSRO to classify them as municipal securities or structured finance products.[775] Nonetheless, the applicant or NRSRO would need to select the most appropriate class for the security or money market instrument and include it in the count for that class. Because some obligors, securities, and money market instruments have characteristics that could cause them to be assigned more than one class, the Commission is seeking comment below on which class would be the most appropriate for these types of obligors, securities, and money market instruments. Based on the comments received, the Commission may decide to prescribe by rule or identify through guidance how certain types of obligors, securities, and money market instruments should be classified.[776]

Fourth, Instruction H would be amended to provide that the applicant or NRSRO must include in the class of credit ratings described in Section 3(a)(62)(B)(iv) of the Exchange Act (issuers of asset-backed securities) to the extent not described in Section 3(a)(62)(B)(iv), any rated security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction. As discussed above in Section II.M.3 of this release, Section 3(a)(62)(B)(iv) contains a narrower definition of "asset-backed security" than the Commission uses for the purposes of its NRSRO rules.[777] In fact, the definition is narrower than the new definition of "asset-backed security" in Section 3(a)77 of the Exchange Act.[778] The Commission expects an applicant and NRSRO to use the broader definition that captures all structured finance products when providing the number of credit ratings outstanding in this class. The proposed amendments to Instruction H to Form NRSRO would be designed to make this expectation more clear.

Request for Comment

The Commission generally requests comment on all aspects of this proposal to amend Form NRSRO Items 6.A and 7.A and Instruction H to Form NRSRO as it relates to Items 6.A and 7.A. The Commission also seeks comment on the following:

1. Would the proposed amendments to Items 6.A and 7.A and Instruction H to Form NRSRO as it relates to Items 6.A and 7.A make the Commission's expectations sufficiently clear in terms of providing the approximate number of credit ratings outstanding in each class for which an applicant is seeking registration and an NRSRO is registered? If not, how could the proposed amendments be modified to provide greater clarity?

2. How should tax-exempt housing bonds be classified for the purposes of Items 6 and 7? For example, should they be classified as: (1) Issuers of asset-backed securities identified in Section 3(a)(62)(A)(iv) of the Exchange Act as broadened to include any rated security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction; or (2) issuers of government securities, municipal securities, or securities issued by a foreign government identified in Section 3(a)(62)(A)(v) of the Exchange Act? Is there another more appropriate classification? Commenters should provide explanations for their choices.

3. How should project finance issuances be classified for the purposes of Items 6 and 7? For example, should they be classified as: (1) Corporate issuers identified in Section 3(a)(62)(A)(iii) of the Exchange Act; (2) issuers of asset-backed securities identified in Section 3(a)(62)(A)(iv) of the Exchange Act as broadened to include any rated security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction; or (3) issuers of government securities, municipal securities, or securities issued by a foreign government identified in Section 3(a)(62)(A)(v) of the Exchange Act? Is there another more appropriate classification? Commenters should provide explanations for their choices.

4. How should supra-national issuers (*e.g.,* the World Bank) be classified for the purposes of Items 6 and 7? For example, should they be classified as: (1) Financial institutions, brokers, or dealers identified in Section 3(a)(62)(A)(i) of the Exchange Act; or (2) issuers of government securities, municipal securities, or securities issued by a foreign government identified in Section 3(a)(62)(A)(v) of the Exchange Act? Is there another more appropriate classification? Commenters should provide explanations for their choices.

5. How should covered bonds be classified? For example, should they be classified as: (1) Financial institutions, brokers, or dealers identified in Section 3(a)(62)(A)(i) of the Exchange Act; or (2) issuers of asset-backed securities identified in Section 3(a)(62)(A)(iv) of the Exchange Act as broadened to include any rated security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction? Is there another more appropriate classification?

[775] For example, tax exempt housing bonds share characteristics of both municipal securities and structured finance products.

[776] As noted above in Sections II.E.1 and II.E.2 of this release, the comments also could inform Commission rulemaking or guidance with respect to the performance statistics that would need to be disclosed pursuant to the proposed enhancements to Exhibit 1 to Form NRSRO and the ratings history information that would need to be disclosed pursuant to new paragraph (b) of Rule 17g–7. The goal would be to have consistent disclosures in Items 6 and 7 of Form NRSRO, Exhibit 1 to Form NRSRO, and in the information about credit ratings histories that would be required under proposed new paragraph (b) of Rule 17g–7. The Commission notes other requirements in the securities laws may be triggered based on the type of obligor, security, or money market instrument being rated. *See, e.g.,* 17 CFR 240.17g–5(a)(3) (which applies when an NRSRO issues or maintains a credit rating for a security or money market instrument issued by an asset pool or part of any asset-backed or mortgage-backed securities transaction). The Commission, in eliciting comment, is not suggesting that an obligor, security, or money market instrument having shared characteristics of, for example, a structured finance product and a municipal security, would not be subject to these other requirements because the most appropriate classification for purposes of Items 6 and 7 of Form NRSRO, Exhibit 1 to Form NRSRO, and proposed new paragraph (b) of Rule 17g–7 would be to classify it as a type of obligor, security, or money market instrument not subject to the other requirements.

[777] *Compare* 15 U.S.C. 78c(a)(62)(B)(iv), *with:* Instructions for Exhibit 1 to Form NRSRO; paragraphs (a)(2)(iii), (a)(7), and (b)(9) of Rule 17g–2; paragraph (a)(6) of Rule 17g–3; paragraphs (a)(3) and (b)(9) of Rule 17g–5; and paragraph (a)(4) of Rule 17g–6.

[778] *Compare* 15 U.S.C. 78c(a)(62)(B)(iv), *with* 15 U.S.C. 78c(a)(77).

Commenters should provide explanations for their choices.

6. How should municipal structured finance issuers be classified? For example, should they be classified as: (1) Issuers of asset-backed securities identified in Section 3(a)(62)(A)(iv) of the Exchange Act as broadened to include any rated security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction; or (2) issuers of government securities, municipal securities, or securities issued by a foreign government identified in Section 3(a)(62)(A)(v) of the Exchange Act? Is there another more appropriate classification? Commenters should provide explanations for their choices.

7. How should for-profit health care companies (*e.g.,* hospitals, assisted living facilities, nursing homes) be treated if a municipality issues securities on behalf of the company? For example, should they be classified as: (1) Corporate issuers identified in Section 3(a)(62)(A)(iii) of the Exchange Act; or (2) issuers of government securities, municipal securities, or securities issued by a foreign government identified in Section 3(a)(62)(A)(v) of the Exchange Act? Is there another more appropriate classification? Commenters should provide explanations for their choices.

8. How should securitizations of health care receivables be classified? For example, should they be classified as: (1) Issuers of asset-backed securities identified in Section 3(a)(62)(A)(iv) of the Exchange Act as broadened to include any rated security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction; or (2) issuers of government securities, municipal securities, or securities issued by a foreign government identified in Section 3(a)(62)(A)(v) of the Exchange Act? Is there another more appropriate classification? Commenters should provide explanations for their choices.

9. How should insurance-linked securities be classified? For example, should they be classified as: (1) Insurance companies identified in Section 3(a)(62)(A)(ii) of the Exchange Act; or (2) issuers of asset-backed securities identified in Section 3(a)(62)(A)(iv) of the Exchange Act as broadened to include any rated security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction? Is there another more appropriate classification? Commenters should provide explanations for their choices.

10. Are there other types of obligors, securities, or money market instruments that share characteristics of one or more classes of credit ratings identified in Section 3(a)(62)(A) of the Exchange Act? If so, identify each such type of obligor, security, or money market instrument, provide a proposed classification, and explain the reason for the proposed classification.

b. Clarification With Respect to Exhibit 8

The Commission proposes to amend Instruction H to Form NRSRO as it relates to Exhibit 8. Exhibit 8 requires an applicant and NRSRO to provide the number of credit analysts it employs and the number of credit analyst supervisors. The Commission is proposing two amendments to the instructions for Exhibit 8. The first amendment would delete a parenthesis in the instructions that provides that the applicant or NRSRO should "see definition below" of the term "credit analyst." There is no such definition. The second amendment would clarify that the applicant or NRSRO, in providing the number of credit analysts, should include the number of credit analyst supervisors. This would be designed to ensure that the disclosures in Form NRSRO are comparable across NRSROs by avoiding the situation in which some NRSROs include credit analyst supervisors in the total number of credit analysts and some NRSROs do not include credit analyst supervisors in that amount.

Request for Comment

The Commission generally requests comment on all aspects of this proposal to amend Instruction H to Form NRSRO as it relates to Exhibit 8.

c. Clarification With Respect to Exhibits 10 through 13

As discussed above, paragraph (i) of Rule 17g–1 requires an NRSRO to make its current Form NRSRO and information and documents submitted in Exhibits 1 through 9 to Form NRSRO publicly available on its Internet Web site, or through another comparable, readily accessible means within 10 business days after the date of the Commission order granting an initial application for registration.[779] An NRSRO is not required to make Exhibits 10 through 13 of Form NRSRO publicly available or update them after registration. Instead, an NRSRO must provide similar information in the annual reports required to be filed with the Commission pursuant to Rule 17g–3.[780] An NRSRO is not required to make the annual reports public. In the past, some NRSRO have submitted the annual reports required by Rule 17g–3 in the form of Exhibits 10 through 13, on a confidential basis, as part of the annual certification. Consequently, the Commission proposes to amend Instruction H in several places to add a "Note" instructing that after registration, Exhibits 10 through 13 are not required to be made publicly available by the NRSRO pursuant to Rule 17g–1(i) and they should not be updated with the filing of the annual certification. The "Note" would further instruct that similar information must be filed with the Commission not more than 90 days after the end of each fiscal year pursuant to Rule 17g–3.[781]

Request for Comment

The Commission generally requests comment on all aspects of this proposal to amend Instruction H to Form NRSRO.

III. General Request for Comment

In responding to the specific requests for comment above, the Commission encourages interested persons to provide supporting data and analysis and, when appropriate, suggest modifications to proposed rule text. Responses that are supported by data and analysis provide great assistance to the Commission in considering the practicality and effectiveness of proposed new requirements as well as weighing the benefits and costs of proposed requirements. In addition, commenters are encouraged to identify in their responses a specific request for comment by indicating the section number of the release and question number within that section to which the response is directed (*e.g.,* Section II.E.1.a, Question #15).

The Commission also seeks comment on the proposals as a whole. In this regard, the Commission seeks comment on the following:

1. How would the proposals integrate with provisions in other Titles and Subtitles of the Dodd-Frank Act and any regulations or proposed regulations under those other Titles and Subtitles?

2. How would the proposals integrate with existing requirements applicable to NRSROs in the Exchange Act and the regulations adopted under authority in the Exchange Act?

[779] *See* 17 CFR 240.17g–1.

[780] *See* 17 CFR 240.17g–3; also *compare* Exhibits 10, 11, 12, and 13 to Form NRSRO and Instruction H of Form NRSRO (as it relates to those Exhibits), *with* paragraphs (a) through (5) of Rule 17g–3. 17 CFR 240.17g–3(a)(1)–(5).

[781] *See* "Notes" proposed to be added to Instruction H to Form NRSRO.

3. What should the implementation timeframe be for the proposed amendments and new rules? For example, should the compliance date be 60 days after publication in the **Federal Register**? Alternatively, should the compliance date be 90, 120, 150, 180, or some other number of days after publication? Should the proposed requirements have different time frames before their compliance dates are triggered? For example, would it take longer to come into compliance with certain of these proposals than others? If so, rank the requirements in terms of the length of time it would take to come into compliance with them and propose a schedule of compliance dates.

IV. Paperwork Reduction Act

Certain provisions of the proposed rule amendments and proposed new rules would contain new "collection of information" requirements within the meaning of the Paperwork Reduction Act of 1995 ("PRA").[782] The Commission has submitted the proposed rule amendments and proposed new rules 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 OMB control number.

The titles for the collections of information are:

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

(2) Rule 17g–2, Records to be made and retained by nationally recognized statistical rating organizations (OMB Control Number 3235–0628);

(3) Rule 17g–3, Annual financial reports to be furnished by nationally recognized statistical rating organizations[783] (OMB Control Number 3235–0626);

(4) Rule 17g–7, Disclosure requirements (OMB Control Number 3235–0656);

(5) Rule 17g–8, Policies and procedures (a proposed new collection of information);

(6) Rule 17g–9, Standards of training, experience, and competence for credit analysts (a proposed new collection of information);

(7) Rule 17g–10, Certification of providers of third-party due diligence services in connection with asset-backed securities; Form ABS Due Diligence-15E (a proposed new collection of information);

(8) Form ABS–15G (OMB Control Number 3235–0675);

(9) Rule 15Ga–2 (a proposed new collection of information);

(10) Regulation S–T, General Rules and Regulations for Electronic Filing (OMB Control Number 3235–0424); and

(11) Form ID (OMB Control Number 3235–0328).

The proposed amendments to Rule 17g–5 (discussed in Section II.B of this release) and Rule 17g–6 (discussed in Section II.M.3 of this release) do not contain a collection of information requirement within the meaning of the PRA.

A. Summary of Collections of Information Under the Proposed Rules and Rule Amendments

In accordance with the Dodd-Frank Act and to enhance oversight, the Commission is soliciting comment on proposed amendments to existing rules and proposed new rules that would apply to NRSROs, providers of third-party due diligence services for Exchange Act-ABS, and issuers and underwriters of Exchange Act-ABS. The following proposals contain new "collection of information" requirements within the meaning of the PRA.

1. Proposed Amendments to Rule 17g–1

The Commission is proposing to amend Rule 17g–1.[784] First, to implement rulemaking mandated in Section 15E(q)(2)(D) of the Exchange Act, the Commission is proposing to amend paragraph (i) of Rule 17g–1, which requires an NRSRO to make its current Form NRSRO and formation and documents submitted in Exhibits 1 through 9 publicly available on its Internet Web site or through another comparable, readily accessible means within 10 business days of being granted an initial registration or a registration in an additional class of credit ratings, and within 10 business days of furnishing a Form NRSRO to update information on the Form, to provide the annual certification, and to withdraw a registration.[785] The Commission's proposed amendment would require an NRSRO to make Form NRSRO and Exhibits 1 through 9 freely available on an easily accessible portion of its corporate Internet Web site.[786] The proposed amendment to paragraph (i) also would remove the option for an NRSRO to make its Form NRSRO publicly available "through another comparable, readily accessible means" as an alternative to Web site disclosure.[787] In addition, the Commission is proposing amending paragraph (i) to provide that Exhibit 1 of Form NRSRO (the performance measurement statistics) be made freely available in writing when requested.[788]

Second, the Commission is proposing to amend paragraphs (e), (f), and (g) of Rule 17g–1 to require NRSROs to use the Commission's EDGAR system to electronically submit Form NRSRO and Exhibits 1 through 9 with the Commission in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T.[789]

2. Proposed Amendments to Instructions for Exhibit 1 to Form NRSRO

The Commission is proposing to amend the instructions for Exhibit 1 to Form NRSRO.[790] The proposed amendments would be designed to implement rulemaking mandated in Section 15E(q) of the Exchange Act.[791] In particular, the amendments would confine the disclosures in the Exhibit to transition and default rates and certain limited supplemental information.[792] Moreover, the enhancements would standardize the production and presentation of the transition and default rates.[793] Specifically, the amendments would require the transition and default rates in Exhibit 1 to be produced using a "single cohort approach."[794] Under this approach, an applicant and NRSRO, on an annual basis, would be required to compute how the credit ratings assigned to obligors, securities, and money market instruments in a particular class or subclass of credit rating outstanding on the date 1, 3, and 10 years prior to the most recent calendar year-end

[782] 44 U.S.C. 3501 *et seq.;* 5 CFR 1320.11.

[783] The Commission is proposing to amend the title of Rule 17g–3 to read, "Annual financial and other reports to be filed or furnished by nationally recognized statistical rating organizations."

[784] 17 CFR 240.17g–1.

[785] *See* 15 U.S.C. 78o–7(q)(2)(D) and proposed amendments to paragraph (i) of Rule 17g–1; *see also* Section II.E.1.b of this release for a more detailed discussion of this proposal.

[786] *See* proposed amendments to paragraph (i) of Rule 17g–1.

[787] *Id.*

[788] *Id.*

[789] *See* proposed amendments to paragraphs (e), (f), and (g) of Rule 17g–1; *see also* Section II.L of this release for a more detailed discussion of these proposals.

[790] *See* Instruction H to Form NRSRO (as it relates to Exhibit 1).

[791] *See* 15 U.S.C. 78o–7(q) and proposed amendments to the instructions for Exhibit 1; *see also* Section II.E.1.a of this release for a more detailed discussion of this proposal.

[792] *See* proposed amendments to the instructions for Exhibit 1.

[793] *Id.*

[794] *Id.*

performed during respective 1, 3, and 10 year time periods.[795]

Under the amendments, the proposed new instructions would be divided into paragraphs (1), (2), (3), and (4), some of which would have subparagraphs.[796] The proposed new paragraphs would contain specific instructions with respect to, among other things, how required information should be presented in the Exhibit (including the order of presentation) and how transition and default rates should be produced using a single cohort approach.[797] As with all information that must be submitted in Form NRSRO and its Exhibits, applicants *and* NRSROs would be subject to these new requirements.[798]

3. Proposed Amendments to Rule 17g–2

The Commission proposes a number of amendments to Rule 17g–2.[799] First, the Commission proposes adding new paragraph (a)(9) to Rule 17g–2 to identify the policies and procedures an NRSRO is required to establish, maintain, and enforce pursuant to Section 15E(h)(4)(A) of the Exchange Act and paragraph (c) of Rule 17g–8 as a record that must be made and retained.[800] Second, the Commission proposes adding new paragraph (b)(12) to Rule 17g–2 to identify the internal control structure an NRSRO must establish, maintain, enforce, and document pursuant to Section 15E(c)(3)(A) of the Exchange Act as a record that must be retained.[801] Third, the Commission proposes adding new paragraph (b)(13) to Rule 17g–2 to identify the policies and procedures an NRSRO is required to establish, maintain, enforce, and document pursuant to proposed paragraph (a) of new Rule 17g–8 as a record that must be retained.[802] Fourth, the Commission proposes adding new paragraph (b)(14) to Rule 17g–2 to identify the policies and procedures an NRSRO must establish, maintain, enforce, and document pursuant to proposed paragraph (b) of new Rule 17g–8 as record that must be retained.[803] Fifth, the Commission proposes adding new paragraph (b)(15) to Rule 17g–2 to identify the standards of training, experience, and competence an NRSRO must establish, maintain, enforce, and document pursuant to proposed new Rule 17g–9 as a record that must be retained.[804]

4. Proposed Amendments to Rule 17g–3

The Commission proposes amending Rule 17g–3.[805] First, the Commission proposes amending paragraphs (a) and (b) of Rule 17g–3 to implement the rulemaking mandated by Section 15E(c)(3)(B) of the Exchange Act.[806] The proposed amendment to paragraph (a) would add a new paragraph (a)(7) to require an NRSRO to include an additional report—the report on the NRSRO's internal control structure—with its annual submission of reports pursuant to Rule 17g–3.[807] Similar to the reports currently identified in paragraphs (a)(2) through (a)(6) of Rule 17g–3, the report identified in new paragraph (a)(7) would be unaudited.[808] The proposed amendment to paragraph (b) of Rule 17g–3 would implement Section 15E(c)(3)(B)(iii) of the Exchange Act, which provides that the annual internal controls report must contain an attestation of the NRSRO's CEO, or equivalent individual.[809] Specifically, the Commission proposes amending paragraph (b) of Rule 17g–3 to require that the NRSRO's CEO or, if the firm does not have a CEO, an individual performing similar functions, provide a signed statement that would be attached to the report.[810]

Second, the Commission is proposing that all the annual reports required to be submitted to the Commission pursuant to Rule 17g–3 be submitted through the EDGAR system.[811] To implement this requirement, the Commission proposes, among other amendments, to add new paragraph (d) to Rule 17g–3. Proposed new paragraph (d) would provide that the reports required by the rule must be submitted electronically with the Commission in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T.[812]

Third, the Commission is proposing to add a new paragraph (a)(8) to Rule 17g–3 to identify the report of the NRSRO's designated compliance officer that an NRSRO is required to file with the Commission pursuant to Section 15E(j)(5)(B) of the Exchange Act as a report that must be filed with the other annual reports.[813] Section 15E(j)(5)(B) further provides that the NRSRO "shall file" this report with the financial report required to be submitted to the Commission under Section 15E of the Exchange Act (*i.e.,* the Rule 17g–3 annual reports).[814] The Commission's proposal is intended to clarify how an NRSRO must adhere to the self-executing provisions in Section 15E(j)(5)(B) of the Exchange Act. Consequently, the Commission preliminary believes this requirement would not result in a collection of information requirement under the PRA because the requirement to file the report with the other annual reports required under Rule 17g–3 derives exclusively from Section 15E(j)(5)(B) of the Exchange Act (*i.e.,* not from Commission rulemaking).[815] Moreover, the Commission is not proposing to add any additional requirements with respect to the filing other than the proposed requirement that this report and the other annual reports be submitted through the EDGAR system, which is addressed separately in this PRA.[816]

[795] *Id.*

[796] *See* proposed paragraphs (1)–(4) of the instructions for Exhibit 1.

[797] *Id.*

[798] *See, e.g.,* 17 CFR 240.17g–1; *see also* Instructions A.1, B, C, D, E, and F to Form NRSRO.

[799] 17 CFR 240.17g–2.

[800] *See* proposed new paragraph (a)(9) to Rule 17g–2(a)(9); *see also* Section II.C.2 of this release for a more detailed discussion of this proposal.

[801] *See* proposed new paragraph (b)(12) of Rule 17g–2; *see also* Section II.A.2 of this release for a more detailed discussion of this proposal.

[802] *See* proposed new paragraph (b)(13) to Rule 17g–2; *see also* Section II.F.2 of this release for a more detailed discussion of this proposal.

[803] *See* proposed new paragraph (b)(14) to Rule 17g–2; *see also* Section II.J.2 of this release for a more detailed discussion of this proposal.

[804] *See* proposed new paragraph (b)(15) to Rule 17g–2; *see also* Section II.I.2 of this release for a more detailed discussion of this proposal.

[805] 17 CFR 240.17g–3.

[806] *See* 15 U.S.C. 78o–7(c)(3)(B) and proposed new paragraphs (a)(7) and (b)(2) of Rule 17g–3; *see also* Section II.A.3 of this release for a for a more detailed discussion of this proposal.

[807] *See* proposed new paragraph (a)(7) of Rule 17g–3.

[808] *See* 17 CFR 240.17g–3(a)(2)–(6).

[809] 15 U.S.C. 78o–7(c)(3)(B)(iii).

[810] *See* proposed new paragraph (b)(2) of Rule 17g–3.

[811] *See* proposed new paragraph (d) of Rule 17g–3; *see also* Section II.L of this release for a more detailed discussion of this proposal.

[812] *See* proposed new paragraph (d) of Rule 17g–3.

[813] *See* proposed new paragraph (a)(8) of Rule 17g–3; *see also* Section II.K of this release for a more detailed discussion of this proposal.

[814] *See* 15 U.S.C. 78o–7(j)(5)(B). Section 15E(k) of the Exchange Act provides that each NRSRO shall, on a confidential basis, file with the Commission, at intervals determined by the Commission, such financial statements, certified (if required by the rules or regulations of the Commission) by an independent public accountant, and information concerning its financial condition, as the Commission, by rule may prescribe as necessary or appropriate in the public interest or for the protection of investors. *See* 15 U.S.C. 78o–7(k). The Commission implemented Section 15E(k) by adopting Rule 17g–3. *See* 17 CFR 240.17g–3; *see also Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33590–33593 (June 18, 2007).

[815] *See* 15 U.S.C. 78o–7(j)(5)(B).

[816] *Compare* 15 U.S.C. 78o–7(j)(5)(B), *with* proposed new paragraph (a)(8) of Rule 17g–3.

5. Proposed Amendments to Rule 17g–7

The Commission proposes to amend Rule 17g–7.[817] First, the Commission is proposing to add new paragraphs (a)(1) and (2) to Rule 17g–7 to implement rulemaking mandated in Sections 15E(s)(1), (2), (3), and (4)(D) of the Exchange Act.[818] Proposed new paragraphs (a)(1) and (2) of Rule 17g–2 would require, respectively, an NRSRO when taking a rating action to publish a form containing information about the credit rating resulting from or subject to the rating action; and any certification of a provider third-party due diligence services received by the NRSRO that relates to the credit rating.[819] Proposed paragraph (a)(1) of Rule 17g–7 would contain three primary components: paragraph (a)(1)(i) prescribing the format of the form;[820] paragraph (a)(1)(ii) prescribing the content of the form;[821] and paragraph (a)(1)(iii) prescribing an attestation requirement for the form.[822] Proposed paragraph (a)(2) of Rule 17g–7 would identify a certification from a provider of third-party due diligence services as an item that must be published with a rating action.[823]

Second, the Commission is proposing to add new paragraph (b) to Rule 17g–7. This proposed amendment would implement rulemaking mandated in Section 15E(q) of the Exchange Act by: (1) Re-codifying in paragraph (b) of Rule 17g–7 requirements currently contained in paragraph (d)(3) of Rule 17g–2; and (2) substantially enhancing those requirements.[824] More specifically, paragraph (d)(3) of Rule 17g–2 requires an NRSRO to, among other things, make publicly available on its corporate Internet Web site in an XBRL format the information required to be documented pursuant to paragraph (a)(8) of the rule with respect to any credit rating initially determined by the NRSRO on or after June 26, 2007, the effective date of the Rating Agency Act of 2006.[825]

These requirements would be enhanced in four ways. The first enhancement would make the disclosure easier for investors and other users of credit ratings to locate. Specifically, new proposed paragraph (b)(1) of Rule 17g–7 would require the NRSRO, among other things, to publicly disclose the ratings history information for free on an *easily accessible portion* of its corporate Internet Web site.[826]

The second enhancement would broaden the scope of credit ratings subject to the disclosure requirements. Specifically, proposed new paragraph (b)(1)(i) of Rule 17g–7 would require an NRSRO to disclose each credit rating assigned to an obligor, security, and money market instrument in every class of credit ratings for which the NRSRO is registered that was *outstanding* as of June 26, 2007 and any subsequent upgrades or downgrades of a credit rating assigned to the obligor, security, or money market instrument (including a downgrade to, or assignment of, default), any placements of a credit rating assigned to the obligor, security, or money market instrument on watch or review, any affirmation of a credit rating assigned to the obligor, security, or money market instrument, and a withdrawal of a credit rating assigned to the obligor, security, or money market instrument.[827] With respect to credit ratings initially determined on or after June 26, 2007, the amendments would clarify that the disclosure of the rating history information would be triggered when an NRSRO publishes any expected or preliminary credit rating assigned to an obligor, security, or money market instrument before the publication of an initial credit rating, and any subsequent upgrades or downgrades of a credit rating assigned to the obligor, security, or money market instrument (including a downgrade to, or assignment of, default), any placements of a credit rating assigned to the obligor, security, or money market instrument on watch or review, any affirmation of a credit rating assigned to the obligor, security, or money market instrument, and a withdrawal of a credit rating assigned to the obligor, security, or money market instrument.[828]

The third enhancement would increase the scope of information that must be disclosed about a rating action. Specifically, proposed paragraph (b)(2) of Rule 17g–7 would identify 7 categories of data that would need to be disclosed when a credit rating action is published pursuant to proposed new paragraph (b)(1) of Rule 17g–7.[829] The fourth enhancement would be to require that a rating history not be removed from the disclosure until 20 years after the NRSRO withdraws the credit rating assigned to the obligor, security, or money market instrument.[830]

6. Proposed New Rule 17g–8

The Commission is proposing new Rule 17g–8 that would have paragraphs (a), (b), and (c) (each paragraph would have sub-paragraphs). Proposed paragraph (a) of new Rule 17g–8 would implement rulemaking mandated in Section 15E(r) of the Exchange Act by requiring an NRSRO to have policies and procedures with respect to the procedures and methodologies the NRSRO uses to determine credit ratings.[831] In particular, proposed paragraph (a)(1) would require the NRSRO to have policies and procedures that are reasonably designed to ensure that the procedures and methodologies, including qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are approved by its board of directors or, if the NRSRO does not have a board of directors, a body performing a function similar to that of a board of directors.[832] Proposed paragraph (a)(2) would require an NRSRO to have policies and procedures that are reasonably designed to ensure that the procedures and methodologies, including qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are developed and modified in accordance with the policies and procedures of the NRSRO.[833] Proposed paragraph (a)(3)(i) would require an NRSRO to have policies and procedures that are reasonably designed to ensure that material changes to the procedures and

[817] 17 CFR 240.17g–7.

[818] *See* 15 U.S.C. 78o–7(s)(1), (2), (3), and (4)(D) and proposed new paragraph (a) of Rule 17g–7; *see also* Sections II.G.1 through G.5 of this release for a more detailed discussion of this proposal.

[819] *See* proposed new paragraphs (a)(1) and (2) of Rule 17g–7.

[820] *See* Section II.G.2 of this release for a detailed discussion of this proposal.

[821] *See* Section II.G.3 of this release for a detailed discussion of this proposal.

[822] *See* Section II.G.4 of this release for a detailed discussion of this proposal.

[823] *See* Section II.G.5 of this release for a detailed discussion of this proposal.

[824] *See* 15 U.S.C. 78o–7(q) and proposed new paragraph (b) of Rule 17g–7; *see also* Section II.E.2 of this release for a more detailed discussion of this proposal.

[825] 17 CFR 240.17–2(d)(3)(i)(A). Paragraph (a)(8) of Rule 17g–2 requires an NRSRO to make and retain a record that, "for each outstanding credit rating, shows all rating actions and the date of such actions from the initial credit rating to the current credit rating identified by the name of the rated security or obligor and, if applicable, the CUSIP of the rated security or the Central Index Key ("CIK") number of the rated obligor." 17 CFR 240.17–2(a)(8).

[826] *See* proposed new paragraph (b)(1) of Rule 17g–7.

[827] *See* proposed new paragraph (b)(1)(i) of Rule 17g–7.

[828] *See* proposed new paragraph (b)(1)(ii) of Rule 17g–7.

[829] *See* proposed new paragraph (b)(2) of Rule 17g–7.

[830] *See* proposed new paragraph (b)(5) of Rule 17g–7.

[831] *See* 15 U.S.C. 78o–7(r) and proposed new paragraph (a) of Rule 17g–8; *see also* Section II.F.1 of this release for a more detailed discussion of this proposal.

[832] *See* proposed paragraph (a)(1) of new Rule 17g–8.

[833] *See* proposed paragraph (a)(2) of new Rule 17g–8.

methodologies, including changes to qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are applied consistently to all credit ratings to which the changed procedures or methodologies apply.[834] Proposed paragraph (a)(3)(ii) would require the NRSRO to have policies and procedures that are reasonably designed to ensure that material changes to the procedures and methodologies, including changes to qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are, to the extent that the changes are to surveillance or monitoring procedures and methodologies, applied to then-current credit ratings within a reasonable period of time taking into consideration the number of ratings impacted, the complexity of the procedures and methodologies used to determine the credit ratings, and the type of obligor, security, or money market instrument being rated.[835] Proposed paragraph (a)(4)(i) would require the NRSRO to have policies and procedures that are reasonably designed to ensure that the NRSRO promptly publishes on an easily accessible portion of its corporate Internet Web site material changes to the procedures and methodologies, including to qualitative models or quantitative inputs, the NRSRO uses to determine credit ratings, the reason for the changes, and the likelihood the changes will result in changes to any current ratings.[836] Proposed paragraph (a)(4)(ii) would require the NRSRO to have policies and procedures that are reasonably designed to ensure the NRSRO promptly publishes on an easily accessible portion of its corporate Internet Web site significant errors identified in a procedure or methodology, including a qualitative or quantitative model, the NRSRO uses to determine credit ratings that may result in a change in current credit ratings.[837] Finally, proposed paragraph (a)(5) would require the NRSRO to have policies and procedures that are reasonably designed to ensure that it discloses the version of a credit rating procedure or methodology, including the qualitative methodology or quantitative inputs, used with respect to a particular credit rating.[838]

Proposed paragraph (b) of new Rule 17g–8 would implement rulemaking mandated in Section 938(a) of the Dodd-Frank Act by requiring an NRSRO to have policies and procedures with respect to the symbols, numbers, or scores it uses to denote credit ratings.[839] In particular, proposed paragraph (b)(1) of new Rule 17g–8 would require the NRSRO to have policies and procedures reasonably designed to assess the probability that an issuer of a security or money market instrument will default, fail to make timely payments, or otherwise not make payments to investors in accordance with the terms of the security or money market instrument.[840] Proposed paragraph (b)(2) of new Rule 17g–8 would require the NRSRO to have policies and procedures reasonably designed to clearly define the meaning of each symbol, number, or score in the rating scale used by the NRSRO to denote a credit rating category and notches within a category for each class and subclass of credit ratings for which the NRSRO is registered and to include such definitions in Exhibit 1 to Form NRSRO.[841] Proposed paragraph (b)(3) of new Rule 17g–8 would require the NRSRO to have policies and procedures reasonably designed to apply any symbol, number, or score defined pursuant to paragraph (b)(2) of new Rule 17g–8 in a manner that is consistent for all types of obligors, securities and money market instruments for which the symbol, number, or score is used.[842]

Proposed paragraph (c) of new Rule 17g–8 would implement rulemaking mandated in Section 15E(h)(4)(A)(ii) of the Exchange Act by requiring the NRSRO to include certain policies and procedures in the policies and procedures the NRSRO is required to establish, maintain, and enforce pursuant to Section 15E(h)(4)(A) of the Exchange Act.[843] Specifically, proposed paragraph (c) would require the NRSRO to have policies and procedures to address instances in which a look-back review determines that a conflict of interest influenced a credit rating assigned to an obligor, security, or money market instrument by including, at a minimum, procedures that are reasonably designed to ensure that the NRSRO will: (1) Immediately place the credit rating on credit watch and disclose certain information about the reason for the rating action; (2) promptly evaluate whether the credit rating must be revised to conform it to the NRSRO's documented procedures and methodologies for determining credit ratings (*i.e.,* remove the influence of the conflict); and (3) promptly publish a revised credit rating, if appropriate, or affirm the credit rating, if appropriate, and, in either case, disclose certain information about the reason for the rating action.[844]

7. Proposed New Rule 17g–9

The Commission is proposing new Rule 17g–9.[845] This proposed rule would implement rulemaking mandated in Section 936 of the Dodd-Frank Act by requiring an NRSRO to establish, maintain, enforce, and document standards of training, experience, and competence for the individuals it employs to determine credit ratings.[846] Proposed paragraph (a) of new Rule 17g–9 would require an NRSRO to establish, maintain, enforce, and document standards of training, experience, and competence for the individuals it employs to determine credit ratings that are reasonably designed to achieve the objective that such individuals produce accurate credit ratings in the classes and subclasses of credit ratings for which the NRSRO is registered.[847] Proposed paragraph (b) would identify four factors the NRSRO must consider when designing the standards.[848] Proposed paragraph (c) would prescribe two requirements an NRSRO must incorporate into its standards of training, experience, and competence.[849]

8. Proposed New Rule 17g–10 and Form ABS Due Diligence–15E

The Commission is proposing new Rule 17g–10 and new Form ABS Due

[834] *See* proposed paragraph (a)(3)(i) of new Rule 17g–8.

[835] *See* proposed paragraph (a)(3)(ii) of new Rule 17g–8.

[836] *See* proposed paragraph (a)(4)(i) of new Rule 17g–8.

[837] *See* proposed paragraph (a)(4)(ii) of new Rule 17g–8.

[838] *See* proposed paragraph (a)(5) of new Rule 17g–8.

[839] *See* Public Law 111–203 § 938(a) and proposed paragraph (b) of new Rule 17g–8; *see also* Section II.J.1 of this release for a more detailed discussion of this proposal.

[840] *See* proposed paragraph (b)(1) of new Rule 17g–8.

[841] *See* proposed paragraph (b)(2) of new Rule 17g–8.

[842] *See* proposed paragraph (b)(1) of new Rule 17g–8.

[843] *See* 15 U.S.C. 78o–7(h)(4)(A)(ii) and proposed new paragraph (c) of Rule 17g–8; *see also* Section II.C.1 of this release for a more detailed discussion of this proposal.

[844] *See* proposed paragraphs (c)(1), (2) and (3) of new Rule 17g–8.

[845] Proposed new Rule 17g–9 would be codified at 17 CFR 240.17g–9, if adopted.

[846] *See* Public Law 111–203 § 936 and proposed new Rule 17g–9; *see also* Section II.I.1 of this release for a more detailed discussion of this proposal.

[847] *See* proposed paragraph (a) of new Rule 17g–9; *see also* Section II.I.1.a of this release for a more detailed discussion of this proposal.

[848] *See* proposed paragraphs (b)(1)–(4) of new Rule 17g–9; *see also* Section II.I.1.b of this release for a more detailed discussion of this proposal.

[849] *See* proposed paragraphs (c)(1) and (2) of new Rule 17g–9; *see also* Section II.I.1.c of this release for a more detailed discussion of this proposal.

Diligence–15E.[850] The new rule and form would implement rulemaking mandated in Sections 15E(s)(4)(B) and (C) of the Exchange Act.[851] Proposed new Rule 17g–10 would contain three paragraphs: (a), (b) and (c).[852] Proposed paragraph (a) would provide that the written certifications of providers of third-party due diligence services required pursuant to Section 15E(s)(4)(B) of the Exchange Act must be made on Form ABS Due Diligence–15E.[853] Proposed paragraph (b) of new Rule 17g–10 would provide that the written certification must be signed by an individual who is duly authorized by the person providing the third-party due diligence services to make such a certification.[854] Proposed paragraph (c) of new Rule 17g–10 would contain four definitions to be used for the purposes of Section 15E(s)(4)(B) and Rule 17g–10; namely, a definition of "due diligence services,"[855] "issuer,"[856] "originator,"[857] and "securitizer."[858]

Proposed Form ABS Due Diligence–15E would contain five line items identifying information the provider of third-party due diligence services would need to provide in the form.[859] It also would contain a signature line with a corresponding representation.[860] Item 1 would elicit the identity and address of the provider of third-party due diligence services.[861] Item 2 would elicit the identity and address of the issuer, underwriter, or NRSRO that employed the provider of third-party due diligence services.[862] Item 3 would instruct the provider of third-party due diligence services to identify each NRSRO whose published criteria for performing due diligence the provider of third-party due diligence services satisfied in performing the due diligence review.[863] Item 4 would require the provider of third-party due diligence services to describe the scope and manner of the due diligence performed.[864] Item 5 would require the provider of third-party due diligence services to describe the findings and conclusions resulting from the review.[865]

9. Rule 15Ga–2 and Form ABS–15G

The Commission is proposing new Rule 15Ga–2 and amendments to Form ABS–15G.[866] The new rule and amended form would implement Section 15E(s)(4)(A) of the Exchange Act.[867] Proposed new Rule 15Ga–2 would require an issuer or underwriter of any Exchange Act-ABS that is to be rated by an NRSRO to furnish a Form ABS–15G on the EDGAR system containing the findings and conclusions of any third-party "due diligence report" obtained by the issuer or underwriter. The rule would define "due diligence report" as any report containing findings and conclusions relating to "due diligence services" as defined in proposed new Rule 17g–10.[868] Under the proposal, the disclosure would be furnished using Form ABS–15G for both registered and unregistered offerings of Exchange Act-ABS. In addition, under the Commission's proposal, an issuer or underwriter would not need to furnish Form ABS–15G if the issuer or underwriter obtains a representation from each NRSRO engaged to produce a credit rating for the Exchange Act-ABS that can be reasonably relied on that the NRSRO will publicly disclose the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter with the publication of the credit rating five business days prior to the first sale in the offering in an information disclosure form generated pursuant to proposed new paragraph (a)(1) of Rule 17g–7.[869]

10. Proposed Amendments to Regulation S–T

The Commission is proposing that certain Form NRSRO submissions and all Rule 17g–3 annual report submissions be submitted to the Commission using the EDGAR system.[870] In order to implement this requirement, the Commission is proposing amendments to Rule 101 of Regulation S–T to require Form NRSROs and Exhibits 1 through 9 submitted pursuant to paragraphs (e), (f), and (g) of Rule 17g–1 and the annual reports submitted pursuant Rule 17g–3 be submitted through the EDGAR system.[871] The Commission also is proposing to amend Rule 201 of Regulation S–T, which governs temporary hardship exemptions from electronic filing, to make this exemption unavailable for NRSRO filings.[872]

The Commission also is proposing amendments to Rule 314 of Regulation S–T to permit municipal securitizers of Exchange Act-ABS, or underwriters in the offering of municipal Exchange Act-ABS, to provide the information required by Form ABS–15G on EMMA, the Municipal Securities Rulemaking Board's centralized public database.[873]

11. Form ID

NRSROs would need to file a Form ID with the Commission in order to gain access to the Commission's EDGAR system to make electronic filings with the Commission.[874]

The Commission preliminarily believes that the issuers and underwriters of Exchange Act-ABS that would need to furnish Form ABS–15G to the Commission through the EDGAR system pursuant to proposed new Rule 15Ga-2 already have access to the EDGAR system because, for example, they need such access for the purpose of Rule 15Ga-1.

B. Proposed Use of Information

1. Proposed Amendments to Rule 17g–1

The Commission proposes amending paragraph (i) of Rule 17g–1 to require

[850] Proposed new Rule 17g–10 would be codified at 17 CFR 240.17g–10 and proposed new Form ABS Due Diligence–15E would be identified at 17 CFR 249b.400.

[851] *See* 15 U.S.C. 78o–7(s)(4)(B) and (C), proposed new Rule 17g–10, and proposed new Form ABS Due Diligence–15E; *see also* Section II.H of this release for a more detailed discussion of this proposal.

[852] *See* proposed paragraphs (a), (b) and (c) of Rule 17g–10; *see also* Section II.H.2 of this release for a more detailed discussion of this proposal.

[853] *See* proposed paragraph (a) of new Rule 17g–10.

[854] *See* proposed paragraph (b) of Rule 17g–10.

[855] *See* proposed paragraph (c)(1) of new Rule 17g–10.

[856] *See* proposed paragraph (c)(2) of new Rule 17g–10.

[857] *See* proposed paragraph (c)(3) of new Rule 17g–10.

[858] *See* proposed paragraph (c)(4) of new Rule 17g–10.

[859] *See* proposed new Form ABS Due Diligence–15E; *see also* Section II.H.3 of this release for a more detailed discussion of this proposal.

[860] *See* proposed new Form ABS Due Diligence–15E.

[861] *See* Item 1 to proposed Form ABS Due Diligence–15E.

[862] *See* Item 2 to proposed Form ABS Due Diligence–15E.

[863] *See* Item 3 to proposed Form ABS Due Diligence–15E.

[864] *See* Item 4 to proposed Form ABS Due Diligence–15E.

[865] *See* Item 5 to proposed Form ABS Due Diligence–15E.

[866] *See* proposed new Rule 15Ga–2 and proposed amendments to Form ABS–15G.

[867] *See* 15 U.S.C. 78o–7(s)(4)(A), proposed new Rule 15Ga–2, and proposed amendments to Form ABS–15G; *see also* Section II.H.1 of this release for a more detailed discussion of this proposal.

[868] *See* proposed paragraph (c)(1) of new Rule 17g–10.

[869] *See* proposed new paragraph (a)(1) of Rule 17g–7.

[870] *See* proposed amendment of Rule 101 of Regulation S–T (17 CFR 231.101); *see also* Section II.L of this release for a more detailed discussion of this proposal.

[871] *See* proposed new paragraph (a)(xiv) of Rule 101 of Regulation S–T.

[872] *See* proposed amendment to paragraph (a) of Rule 201 of Regulation S–T (17 CFR 231.201); *see also* Section II.L of this release for a more detailed discussion of this proposal.

[873] *See* proposed amendments to Rule 314 of Regulation S–T (17 CFR 231.314); *see also* Section II.H.1 of this release for a more detailed discussion of this proposal.

[874] *See* Section II.L of this release for a more detailed discussion of these proposals.

that an NRSRO make Form NRSRO and Exhibits 1 through 9 freely available on an easily accessible portion of its corporate Internet Web site.[875] The proposed amendment to paragraph (i) also would remove the option for an NRSRO to make its Form NRSRO publicly available "through another comparable, readily accessible means" as an alternative to Internet disclosure. In addition, the Commission is proposing amending paragraph (i) to provide that Exhibit 1 of Form NRSRO (the performance measurement statistics) be made freely available in writing when requested. Second, the Commission is proposing to amend paragraphs (e), (f), and (g) of Rule 17g–1 to require that NRSROs use the Commission's EDGAR system to electronically file or submit Form NRSRO with the Commission pursuant to these paragraphs in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T.[876]

The proposed requirements that an NRSRO make Form NRSRO and Exhibits 1 through 9 freely available on an easily accessible portion of its corporate Internet Web site and file the Form through the EDGAR system are designed to make this information more readily accessible to investors and other users of credit ratings. As the Commission stated when adopting Form NRSRO, the Form will provide users of credit ratings with information that will assist them in comparing NRSROs and understanding how a given NRSRO conducts its business activities.[877] In addition, the filing of the Form NRSROs on the EDGAR system would allow Commission examiners to more easily retrieve the submissions of a specific NRSRO to prepare for an examination. Furthermore, having the Forms filed and stored through the EDGAR system (*i.e.,* in a centralized location), would assist the Commission from a records management perspective by establishing a more automated storage process and creating efficiencies in terms of reducing the volume of paper filings that must be manually processed and stored.

2. Proposed Amendments to Instructions for Exhibit 1 to Form NRSRO

The Commission is proposing to amend the instructions for Exhibit 1 to Form NRSRO.[878] The amendments would confine the disclosures in the Exhibit to transition and default rates and certain limited supplemental information.[879] Moreover, the amendments would standardize the production and presentation of the transition and default rates. As the Commission stated when adopting Form NRSRO, the information provided in Exhibit 1 is an important indicator of the performance of an NRSRO in terms of its ability to assess the creditworthiness of issuers and obligors and, consequently, will be useful to users of credit ratings in evaluating an NRSRO.[880] In addition, Commission staff would use the enhanced performance statistics provided in an applicant's initial application for registration and in an NRSRO's Form NRSRO to, among other things, assess whether the applicant or NRSRO has adequate financial and managerial resources to consistently produce credit ratings with integrity.[881] For example, statistics indicating the applicant or NRSRO is performing poorly in determining credit ratings could be an indication the applicant or NRSRO fails to maintain adequate financial and managerial resources to consistently produce credit ratings with integrity in a particular class or subclass of credit ratings. Finally, the disclosure of the enhanced performance statistics in an applicant's initial application would allow the Commission staff to verify that the applicant, if granted registration, would publicly disclose the information in accordance with the proposed amendments to the Instructions for Exhibit 1.[882]

3. Proposed Amendments to Rule 17g–2

The Commission proposes adding paragraph (a)(9) to Rule 17g–2 to identify the policies and procedures an NRSRO is required to establish, maintain, and enforce pursuant to Section 15E(h)(4)(A) of the Exchange Act and proposed paragraph (c) of new Rule 17g–8 as a record that must be made and retained.[883] In addition, the Commission is proposing to add the following new paragraphs to Rule 17g–2 to identify additional records that must be retained: (1) Paragraph (b)(12) would identify the internal control structure an NRSRO must establish, maintain, enforce, and document pursuant to Section 15E(c)(3)(A);[884] (2) paragraph (b)(13) would identify the policies and procedures an NRSRO is required to establish, maintain, enforce, and document pursuant to proposed paragraph (a) of new Rule 17g–8;[885] (3) paragraph (b)(14) would identify the policies and procedures an NRSRO must establish, maintain, enforce, and document pursuant to proposed paragraph (b) of new Rule 17g–8;[886] and (4) paragraph (b)(15) would identify the standards of training, experience, and competence an NRSRO must establish, maintain, enforce, and document pursuant to proposed new Rule 17g–9.[887]

The proposed requirement that a record of the policies and procedures identified in proposed new paragraph (a)(9) of Rule 17g–2 be made (*i.e.,* documented) would promote better

[875] *See* proposed amendments to paragraph (i) of Rule 17g–1; *see also* Section II.E.1.b of this release for a more detailed discussion of this proposal.

[876] *See* proposed amendments to paragraphs (e), (f), and (g) of Rule 17g–1; *see also* Section II.L of this release for a more detailed discussion of these proposals.

[877] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR 33569–335670 (June 18, 2007).

[878] *See* Instruction H to Form NRSRO (as it relates to Exhibit 1).

[879] *See* proposed amendments to the instructions for Exhibit 1 to Form NRSRO (17 CFR 249b.300); *see also* Section II. E.1.a of this release for a more detailed discussion of this proposal.

[880] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33574 (June 18, 2007); *see also Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6474 (Feb. 9, 2009) ("The amendments to the instructions to Exhibit 1 to Form NRSRO will require NRSROs to provide more detailed performance statistics and, thereby, make it easier for users of credit ratings to compare the performance of the NRSROs.").

[881] *See, e.g.,* 15 U.S.C. 78o–7(a)(2)(C) (setting forth grounds to deny an initial application) and 15 U.S.C. 78o–7(d)(1)(E) and (d)(2) (setting forth grounds to sanction an NRSRO, including revoking the NRSRO's registration); *see also Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33612 (June 18, 2007) ("Form NRSRO requires that a credit rating agency provide information required under Section 15E(a)(1)(B) of the Exchange Act and certain additional information. The additional information will assist the Commission in making the assessment regarding financial and managerial resources required under Section 15E(a)(2)(C)(2)(ii)(I) of the Exchange Act.").

[882] As indicated above, paragraph (i) requires an NRSRO to make Form NRSRO and Exhibits 1 through 9 publicly available within 10 business days of being granted an initial registration. *See* 17 CFR 240.17g–1(i). In addition, the public disclosure of Form NRSRO and Exhibits 1 through 9 could be accelerated if the Commission adopts the proposal that this information be filed through the EDGAR system upon registration.

[883] *See* proposed new paragraph (a)(9) to Rule 17g–2(a)(9); *see also* Section II.C.2 of this release for a more detailed discussion of this proposal.

[884] *See* proposed new paragraph (b)(12) of Rule 17g–2; *see also* Section II.A.2 of this release for a more detailed discussion of this proposal.

[885] *See* proposed new paragraph (b)(13) to Rule 17g–2; *see also* Section II.F.2 of this release for a more detailed discussion of this proposal.

[886] *See* proposed new paragraph (b)(14) to Rule 17g–2; *see also* Section II.J.2 of this release for a more detailed discussion of this proposal.

[887] *See* proposed new paragraph (b)(15) to Rule 17g–2; *see also* Section II.I.2 of this release for a more detailed discussion of this proposal.

understanding of them among the individuals within the organization and, therefore, promote compliance with such policies and procedures. The requirement that the policies and procedures identified in proposed new paragraphs (a)(9), (b)(12), (b)(13), (b)(14), and (b)(15) be retained would subject these records to the various retention and production requirements of paragraphs (c), (d), (e), and (f) of Rule 17g–2.[888] The Commission staff would use these records to review whether an NRSRO was complying with the provisions of the securities laws requiring the NRSRO to establish, maintain, enforce, and document these policies, procedures, and standards.[889]

4. Proposed Amendments to Rule 17g–3

The Commission proposes amending paragraphs (a) and (b) of Rule 17g–3 to implement the rulemaking mandated by Section 15E(c)(3)(B) of the Exchange Act.[890] The proposed amendment to paragraph (a) would add a new paragraph (a)(7) to require an NRSRO to include an additional report—a report on the NRSRO's internal control structure—with its annual submission of reports pursuant to Rule 17g–3. The proposed amendment to paragraph (b) of Rule 17g–3 would require that the NRSRO's CEO or, if the firm does not have a CEO, an individual performing similar functions, provide a signed statement that would be attached to the report. The Commission staff would use this report along with the other Rule 17g–3 annual reports to monitor the NRSRO's compliance with applicable securities laws.[891] For example, Section 15E(c)(3)(A) of the Exchange Act requires an NRSRO to "establish, maintain, enforce, and document an effective internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings."[892] Among other things, the annual report that an NRSRO would file pursuant to proposed new paragraph (a)(7) of Rule 17g–3 would require the NRSRO to provide an assessment by management of the effectiveness of the internal control structure. Consequently, Commission staff could use the report as a starting point to assess whether the NRSRO is complying with Section 15E(c)(3)(A) of the Exchange Act.[893]

The Commission also is proposing that all the annual reports required to be submitted to the Commission pursuant to Rule 17g–3 be submitted through the EDGAR system.[894] The submission of the annual reports through the EDGAR system would allow Commission examiners to more easily retrieve the reports of a specific NRSRO to prepare for an examination. Moreover, having these reports submitted and stored through the EDGAR system (*i.e.,* in a centralized location), would assist the Commission from a records management perspective by establishing a more automated storage process and creating efficiencies in terms of reducing the volume of paper submissions that must be manually processed and stored.

5. Proposed Amendments to Rule 17g–7

The Commission proposes to amend Rule 17g–7.[895] First, the Commission is proposing to add new paragraphs (a)(1) and (2) to Rule 17g–7 to implement rulemaking mandated in Sections 15E(s)(1), (2), (3), and (4)(D) of the Exchange Act.[896] Proposed new paragraphs (a)(1) and (2) of Rule 17g–2 would require, respectively, an NRSRO when taking a rating action to publish a form containing information about the credit rating resulting from or subject to the rating action; and any certification of a provider of third-party due diligence services received by the NRSRO that relates to the credit rating.[897] As stated in Section 15E(s)(1)(B) of the Exchange Act, the purpose of the disclosures required in the form would be to provide information that can be used by investors and other users of credit ratings to better understand credit ratings in each class of credit rating issued by the NRSRO.[898] Furthermore, as stated in Section 15E(s)(4)(D) of the Exchange Act, the purpose of the disclosure of the certification would be to allow the public to determine the adequacy and level of due diligence services provided by a third-party.[899]

Second, the Commission is proposing to add new paragraph (b) to Rule 17g–7.[900] The proposed amendments would: (1) Re-codify in paragraph (b) of Rule 17g–7 requirements currently contained in paragraph (d)(3) of Rule 17g–2; and (2) substantially enhance those requirements. Under the current and proposed enhanced requirements, an NRSRO is (and would be) required to disclose certain historical information about its credit ratings. As the Commission stated when adopting the current disclosure requirement, the "intent of the rule is to facilitate comparisons of credit rating accuracy across all NRSROs—including direct comparisons of different NRSROs' treatment of the same obligor or instrument—in order to enhance NRSRO accountability, transparency, and competition."[901] The proposals also

[888] *See* 17 CFR 240.17g–2(c), (d), (e) and (f). Paragraph (c) of Rule 17g–2 requires an NRSRO to retain the records identified in paragraphs (a) and (b) for three years after the date the record is made or received. 17 CFR 240.17g–2(c). Paragraph (d) requires, among other things, that an NRSRO maintain each record required to be retained pursuant to paragraphs (a) and (b) in a manner that makes the original record or copy easily accessible to the principal office of the NRSRO. 17 CFR 240.17g–2(d). Paragraph (e) sets forth the requirements that apply when an NRSRO uses a third-party custodian to maintain its records. 17 CFR 240.17g–2(e). Paragraph (f) requires an NRSRO to promptly furnish the Commission with legible, complete, and current copies, and, if specifically requested, English translations, of those records of the NRSRO required to be retained pursuant to paragraphs (a) and (b), or any other records of the NRSRO subject to examination under Section 17(b) of the Exchange Act. *See* 17 CFR 240.17g–2(f); *see also* 15 U.S.C. 78q(b).

[889] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33582 (June 18, 2007) ("The Commission designed [Rule 17g–2] based on its experience with recordkeeping rules for other regulated entities. These other books and records rules have proven integral to the Commission's investor protection function because the preserved records are the primary means of monitoring compliance with applicable securities laws. Rule 17g–2 is designed to ensure that an NRSRO makes and retains records that will assist the Commission in monitoring, through its examination authority, whether an NRSRO is complying with the provisions of Section 15E of the Exchange Act and the rules thereunder.") (footnotes omitted).

[890] *See* proposed new paragraphs (a)(7) and (b)(2) of Rule 17g–3; *see also* Section II.A.3 of this release for a for a more detailed discussion of this proposal.

[891] *See, e.g., Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33612–33613 (June 18, 2007) ("[Rule 17g–3] will aid the Commission in monitoring whether the initiation of a proceeding under Section 15E(d) of the Exchange Act will be appropriate because the NRSRO 'fails to maintain adequate financial and managerial resources to consistently produce credit ratings with integrity. In addition, the financial reports also will assist the Commission in monitoring potential conflicts of interest of a financial nature arising from the operation of an NRSRO.") (footnotes omitted); *see also Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6465 (Feb. 9, 2009) ("[The amendment to Rule 17g–3] will assist the Commission in its examination function of NRSROs.").

[892] 15 U.S.C. 78o–7(c)(3)(A).

[893] *Id.*

[894] *See* proposed new paragraph (d) of Rule 17g–3; *see also* Section II.L of this release for a more detailed discussion of this proposal.

[895] 17 CFR 240.17g–7.

[896] *See* 15 U.S.C. 78o–7(s)(1), (2), (3), and (4)(D) and proposed new paragraph (a) of Rule 17g–7; *see also* Sections II.G.1 through G.5 of this release for a more detailed discussion of this proposal.

[897] *See* proposed new paragraphs (a)(1) and (2) of Rule 17g–7.

[898] *See* 15 U.S.C. 78o–7(s)(1)(B).

[899] *See* 15 U.S.C. 78o–7(s)(4)(D).

[900] *See* proposed new paragraph (b) of Rule 17g–7; *see also* Section II.E.2 of this release for a more detailed discussion of this proposal.

[901] *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR

are designed to provide persons with the "raw data" necessary to generate statistical information about the performance of each NRSRO's credit ratings.[902] Finally, the proposals are designed to implement provisions of Section 15E(q)(2) of the Exchange Act, which provides, among other things, that the Commission's rules shall require NRSROs to disclose information about the performance of credit ratings that is comparable among NRSROs, to allow users of credit ratings to compare the performance of credit ratings across NRSROs.[903]

6. Proposed New Rule 17g–8

The Commission is proposing new Rule 17g–8 that would have paragraphs (a), (b), and (c) (each paragraph would have sub-paragraphs). Paragraph (a) of new Rule 17g–8 would implement Section 15E(r) of the Exchange Act by requiring an NRSRO to have policies and procedures with respect to the procedures and methodologies the NRSRO uses to determine credit ratings.[904] These policies and procedures would be used by the NRSRO to achieve the objectives identified in Section 15E(r) of the Exchange Act,[905] namely, that the NRSRO:

- determines credit ratings using procedures and methodologies, including qualitative and quantitative data and models, that are approved by the board of the NRSRO, or a body performing a function similar to that of a board;[906]
- determines credit ratings using procedures and methodologies, including qualitative and quantitative data and models, that are in accordance with the policies and procedures of the NRSRO for the development and modification of credit rating procedures and methodologies;[907]
- when material changes are made to credit rating procedures and methodologies (including changes to qualitative and quantitative data and models), applies the changes consistently to all credit ratings to which the changed procedures and methodologies apply;[908]
- when material changes are made to credit rating procedures and methodologies (including changes to qualitative and quantitative data and models), to the extent that changes are made to credit rating surveillance procedures and methodologies, applies the changes to then-current credit ratings within a reasonable time period determined by the Commission, by rule;[909]
- when material changes are made to credit rating procedures and methodologies (including changes to qualitative and quantitative data and models), the NRSRO publicly discloses the reason for the change;[910]
- notifies users of credit ratings of the version of a procedure or methodology, including the qualitative methodology or quantitative inputs, used with respect to a particular credit rating.[911]
- notifies users of credit ratings when a material change is made to a procedure or methodology, including to a qualitative model or quantitative input;)[912]
- notifies users of credit ratings when a significant error is identified in a procedure or methodology, including a qualitative or quantitative model, that may result in credit rating actions;[913] and
- notifies users of credit ratings when a material change is made to a procedure or methodology, including to a qualitative model or quantitative input, of the likelihood the change will result in a change in current credit ratings.[914]

Proposed paragraph (b) of new Rule 17g–8 would implement Section 938(a) of the Dodd-Frank Act by requiring an NRSRO to have policies and procedures with respect to the symbols, numbers, or scores it uses to denote credit ratings.[915] These policies and procedures would be used by the NRSRO to achieve the objectives mandated in Sections 938(a)(1) through (3) of the Dodd-Frank Act.[916] Namely, that the NRSRO establishes, maintains, and enforces written policies and procedures to: (1) Assess the probability that an issuer of a security or money market instrument will default, fail to make timely payments, or otherwise not make payments to investors in accordance with the terms of the security or money market instrument;[917] (2) clearly define and disclose the meaning of any symbol used by the NRSRO to denote a credit rating;[918] and (3) apply any symbol described in item (2) in a manner that is consistent for all types of securities and money market instruments for which the symbol is used.[919]

Proposed paragraph (c) of new Rule 17g–8 would implement Section 15E(h)(4)(A)(ii) of the Exchange Act by requiring the NRSRO to include certain policies and procedures in the policies and procedures the NRSRO is required to establish, maintain, and enforce under Section 15E(h)(4)(A) of the Exchange Act.[920] These policies and procedures would be used by the NRSRO: (1) To achieve the objective specified in Section 15E(h)(4)(A)(ii) of the Exchange Act to revise a credit rating, if appropriate, when a look-back review determines the credit rating was influenced by the conflict of interest of the credit analyst seeking employment with the person subject to the credit rating or the issuer, underwriter, or sponsor of a security or money market instrument subject to the credit rating;[921] and (2) to make the disclosures that would be required in proposed new paragraph (a)(1)(ii)(J)(*3*) of Rule 17g–7.[922]

at 63838 (Dec. 4, 2009) ("Ratings history information for outstanding credit ratings is the most direct means of comparing the performance of two or more NRSROs. It allows an investor or other user of credit ratings to compare how all NRSROs that maintain a credit rating for a particular obligor or instrument initially rated that obligor or instrument and, thereafter, how and when they adjusted their credit rating over time."). The Commission notes that under the proposals the disclosures would not contain complete histories for many credit ratings because the NRSRO would not need to include information about rating actions taken before June 26, 2007. However, the Commission believes that the disclosures would still be used to compare how different NRSROs rated a particular obligor, security, or money market instrument beginning as of June 26, 2007 and from that date forward.

[902] *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63837–63838 (Dec. 4, 2009) ("The raw data to be provided by NRSROs pursuant to the new ratings history disclosure requirements…will enable market participants to develop performance measurement statistics that would supplement those required to be published by NRSROs themselves in Exhibit 1, tapping into the expertise of credit market observers and participants in order to create better and more useful means to compare the credit ratings performance of NRSROs.").

[903] *See* 15 U.S.C. 78o–7(q)(2).

[904] *See* 15 U.S.C. 78o–7(r) and proposed new paragraph (a) of Rule 17g–8; *see also* Section II.F.1 of this release for a more detailed discussion of this proposal.

[905] *See* 15 U.S.C. 78o–7(r)(1)–(3).

[906] *See* 15 U.S.C. 78o–7(r)(1)(A).

[907] *See* 15 U.S.C. 78o–7(r)(1)(B).

[908] *See* 15 U.S.C. 78o–7(r)(2)(A).

[909] 15 U.S.C. 78o–7(r)(2)(B).

[910] *See* 15 U.S.C. 78o–7(r)(2)(C).

[911] 15 U.S.C. 78o–7(r)(3)(A).

[912] *See* 15 U.S.C. 78o–7(r)(3)(B).

[913] *See* 15 U.S.C. 78o–7(r)(3)(C).

[914] *See* 15 U.S.C. 78o–7(r)(3)(D).

[915] *See* Public Law 111–203 § 938(a) and proposed paragraph (b) of new Rule 17g–8; *see also* Section II.J.1 of this release for a more detailed discussion of this proposal.

[916] *See* Public Law 111–203 §§ 938(a)(1)–(3).

[917] *See* Public Law 111–203 § 938(a)(1).

[918] *See* Public Law 111–203 § 938(a)(2).

[919] *See* Public Law 111–203 § 938(a)(3).

[920] *See* 15 U.S.C. 78o–7(h)(4)(A)(ii) and proposed new paragraph (c) of Rule 17g–8; *see also* Section II.C.1 of this release for a more detailed discussion of this proposal.

[921] *See* 15 U.S.C. 78o–7(h)(4)(A)(ii).

[922] *See* proposed paragraph (a)(1)(ii)(J)(*3*) of Rule 17g–7.

7. Proposed New Rule 17g–9

The Commission is proposing new Rule 17g–9.[923] This rule would implement Section 936 of the Dodd-Frank Act by requiring an NRSRO to establish, maintain, enforce, and document standards of training, experience, and competence for the individuals it employs to determine credit ratings.[924] These standards would be used by the NRSRO to achieve the objectives specified in Sections 936(1) and (2) of the Dodd-Frank Act that any person employed by the NRSRO to perform credit ratings produces accurate ratings for the categories of issuers whose securities the person rates and is tested for knowledge of the credit rating process.[925]

8. Proposed New Rule 17g–10 and Form ABS Due Diligence–15E

The Commission is proposing new Rule 17g–10 and new Form ABS Due Diligence–15E.[926] Proposed new Rule 17g–10 would implement rulemaking mandated in Sections 15E(s)(4)(B) and (C) of the Exchange Act by requiring that the written certification a provider of third-party due diligence services must provide to an NRSRO be made on Form ABS Due Diligence-15E.[927] Proposed new Rule 17g–10 and proposed new Form ABS Due Diligence-15E would be designed to achieve the objective stated in Section 15E(s)(4)(B) of the Exchange Act; namely, that the provider of third-party due diligence services conducts a thorough review of data, documentation, and other relevant information necessary for an NRSRO to provide an accurate credit rating.[928] They also would be designed—in combination with the disclosure requirement in proposed new paragraph (a)(2) of Rule 17g–7—to achieve the objective stated in Section 15E(s)(4)(D) of the Exchange Act; namely, to allow the public to determine the adequacy and level of due diligence services provided by a third party.[929]

9. Rule 15Ga–2 and Form ABS–15G

The Commission is proposing new Rule 15Ga–2 and amendments to Form ABS–15G.[930] The new rule and amended form would implement Section 15E(s)(4)(A) of the Exchange Act.[931] Proposed new Rule 15Ga–2 would require an issuer or underwriter of any Exchange Act-ABS that is to be rated by an NRSRO to furnish a Form ABS–15G on the EDGAR system containing the findings and conclusions of any third-party "due diligence report" obtained by the issuer or underwriter. Under the proposal, the disclosure would be furnished using Form ABS–15G for both registered and unregistered offerings of Exchange Act-ABS. In addition, under the Commission's proposal, an issuer or underwriter would not need to furnish Form ABS–15G if the issuer or underwriter obtains a representation from each NRSRO engaged to produce a credit rating for the Exchange Act-ABS that can be reasonably relied on that the NRSRO will publicly disclose the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter with the publication of the credit rating five business days prior to the first sale in the offering in an information disclosure form generated pursuant to proposed new paragraph (a)(1) of Rule 17g–7.

The information proposed to be disclosed under these requirements would be used by investors and other users of credit ratings to determine the adequacy and level of due diligence services provided by a third party. In addition, if no disclosure is made, investors and other users of credit ratings would be put on notice that the issuer or underwriter did not employ a provider of third-party due diligence services in connection with the offering of an Exchange Act-ABS.

10. Proposed Amendments to Regulation S–T

As noted above, the Commission is proposing that certain Form NRSRO submissions and all Rule 17g–3 annual report submissions be made through the EDGAR system. In order to implement this requirement, the Commission is proposing amendments to Rule 101 of Regulation S–T to require that the EDGAR system be used to submit Form NRSRO pursuant to paragraphs (e), (f), and (g) of Rule 17g–1 and the annual reports pursuant Rule 17g–3.[932] The Commission also is proposing to amend Rule 201 of Regulation S–T, which governs temporary hardship exemptions from electronic filings, to make this exemption unavailable for NRSRO submissions.[933]

These proposed requirements would implement the proposals that NRSROs use the EDGAR system to submit Form NRSROs pursuant to paragraphs (e), (f), and (g) of Rule 17g–1 and the annual reports pursuant to Rule 17g–3. With respect to the Form NRSROs, the proposal is designed to make the information contained in the Form more readily accessible to investors and other users of credit ratings. As the Commission stated when adopting Form NRSRO, the Form will provide users of credit ratings with information that will assist them in comparing NRSROs and understanding how a given NRSRO conducts its business activities.[934] In addition, the filing of the Form NRSROs and annual reports on the EDGAR system would allow Commission examiners to more easily retrieve the Forms of a specific NRSRO to prepare for an examination. Moreover, having the Forms and annual reports filed and stored through the EDGAR system (*i.e.,* in a centralized location), would assist the Commission from a records management perspective by establishing a more automated storage process and creating efficiencies in terms of reducing the volume of paper filings that must be manually processed and stored.

The Commission also is proposing amendments to Rule 314 of Regulation S–T that would permit municipal securitizers of Exchange Act-ABS, or underwriters in the offering of municipal Exchange Act-ABS, to provide the information required by Form ABS–15G on EMMA, the Municipal Securities Rulemaking Board's centralized public database.[935] This would allow investors and other market participants to access the information required in Form ABS–15G

[923] Proposed new Rule 17g–9 would be codified at 17 CFR 240.17g–9, if adopted.

[924] *See* Public Law 111–203 § 936 and proposed new Rule 17g–9; *see also* Section II.I.1 of this release for a more detailed discussion of this proposal.

[925] Public Law 111–203 §§ 936(1) and (2).

[926] Proposed new Rule 17g–10 would be codified at 17 CFR 240.17g–10 and proposed new Form ABS Due Diligence–15E would be identified at 17 CFR 249b.400.

[927] *See* 15 U.S.C. 78o–7(s)(4)(B) and (C), proposed new Rule 17g–10, and proposed new Form ABS Due Diligence-15E; *see also* Sections II.H of this release for a more detailed discussion of this proposal.

[928] *See* 15 U.S.C. 78o–7(s)(4)(B).

[929] *See* 15 U.S.C. 78o–7(s)(4)(D); *see also* Sections II.G.5 of this release for a more detailed discussion of proposed new paragraph (a)(2) of Rule 17g–7.

[930] *See* proposed new Rule 15Ga–2 and proposed amendments to Form ABS–15G.

[931] *See* 15 U.S.C. 78o–7(s)(4)(A); *see also* Section II.H.1 of this release for a more detailed discussion of this proposal.

[932] *See* proposed amendment of Rule 101 of Regulation S–T (17 CFR 231.101); *see also* Section II.L of this release for a more detailed discussion of this proposal.

[933] *See* proposed amendment of Rule 201 of Regulation S–T (17 CFR 231.201); *see also* Section II.L of this release for a more detailed discussion of this proposal.

[934] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR 33569–335670 (June 18, 2007).

[935] *See* proposed amendments to Rule 314 of Regulation S–T (17 CFR 231.314); *see also* Section II.H.1 of this release for a more detailed discussion of this proposal.

along with other information on EMMA about the municipal Exchange Act-ABS.

11. Form ID

NRSROs would need to file a Form ID with the Commission in order to gain access to the Commission's EDGAR system to electronically submit Form NRSROs submitted pursuant to paragraphs (e), (f), and (g) of Rule 17g–1 and the annual reports submitted pursuant to Rule 17g–3 through the EDGAR system with the Commission.[936] The use of this information is addressed in Sections IV.D.1, IV.D.4 and IV.A.10 of this release.

C. Respondents

In adopting the first rules under the Rating Agency Act of 2006, the Commission estimated that approximately 30 credit rating agencies ultimately would be registered as NRSROs.[937] Since that time, 10 credit rating agencies have registered with the Commission as NRSROs.[938] This number has remained constant for several years. Consequently, while the Commission expects several more credit rating agencies may become registered as NRSROs over the next few years, the Commission preliminarily believes that the actual number of NRSROs should be used for purposes of the PRA.

The Commission notes the current industry-wide annual burden estimates for the NRSRO Rules are based on 30 respondents. Consequently, these estimates would need to be adjusted to reflect the Commission's use of the actual number of NRSROs (*i.e.,* 10 respondents). In this regard, the current OMB approved industry-wide annual hour burdens are: 6,400 hours for Rule 17g–1 and Form NRSRO; 12,000 hours for Rule 17g–2; 7,900 hours for Rule 17g–3; and 96,948 hours for Rule 17g–7. Adjusting for 10 respondents, these industry-wide annual hour burdens would be: 2,133 hours for Rule 17g–1 and Form NRSRO;[939] 4,000 hours for Rule 17g–2;[940] 2,633 hours for Rule 17g–3;[941] and 92,948 hours for Rule 17g–7.[942] For the purposes of the PRA discussion below and the economic analysis in Section V of this release, the Commission uses the adjusted current industry-wide annual hour burdens above (the "adjusted industry-wide annual hour burdens"). For example, when discussing how a proposed amendment would increase an industry-wide annual hour burden, the Commission adds the increased hour burden to the applicable rule's adjusted current industry-wide annual hour burden.

The Commission preliminarily believes there are approximately 10 firms that provide, or would begin providing, third-party "due diligence services" to issuers and underwriters of Exchange Act-ABS as the term "due diligence services" would be defined in paragraph (a) of proposed new Rule 17g–10.[943] As discussed in Section II.H.2 of this release, the Commission preliminarily believes that the firms providing third-party "due diligence services" as that term would be defined in proposed new Rule 17g–10 concentrate mostly on providing such services for RMBS. Consequently, given the low issuance rate for RMBS, the number of active firms may be small but it could grow if issuance volume increases.

The Commission preliminarily believes there are 270 unique securitizers that would be subject to the proposed requirements in new Rule 15Ga–2 and the amendments to Form ABS–15G.[944] This estimate is based on the Commission's estimate of the number of securitizers that would be subject to requirements in Rule 15Ga–1 and Form ABS–15G.[945]

Request for Comment

The Commission generally requests comment on all aspects of these estimates of the number of respondents. In addition, the Commission requests specific comments on the following:

1. Is it reasonable for the Commission to use the actual number of NRSROs for purposes of the PRA? Alternatively, should the Commission either use, for purposes of the PRA, the estimate of 30 NRSROs it has used in the past or develop and use a new estimate of the expected eventual number of NRSROs? Explain any choices made with respect to the number of NRSROs that should be used for the purposes of the PRA, including any data and analysis supporting the choice.

2. Identify any sources of industry information that could be used to estimate the number of NRSROs that may become registered with the Commission over the next few years for purposes of the PRA.

[936] *See* Section II.L of this release for a more detailed discussion of these proposals.

[937] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33607 (June 18, 2007).

[938] A.M. Best Company, Inc., DBRS Ltd., Egan-Jones Rating Company, Fitch, Inc., Japan Credit Rating Agency, Ltd., Kroll Bond Rating Agency, Inc. (formerly LACE Financial Corp.), Moody's Investors Service, Inc., Rating and Investment Information, Inc., Realpoint LLC, and Standard & Poor's Ratings Services.

[939] The current OMB approved total industry-wide annual hour burden for Rule 17g–1 and Form NRSRO of 6,400 hours is based on 30 respondents preparing and filing Form NRSROs. *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33607–33609 (June 18, 2007); *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6470 (Feb. 9, 2009), and *Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63889–63890 (Dec. 4, 2009). Consequently, the adjusted current industry-wide annual hour burden for Rule 17g–1 and Form NRSRO would be 2,133 hours (6,400 hours/30 NRSROs = 213 hours; 10 NRSROs × 213 hours = 2,133 hours).

[940] The current OMB approved total industry-wide annual hour burden for Rule 17g–2 of 12,000 hours is based on 30 respondents making and retaining the required records identified in paragraphs (a) and (b) of Rule 17g–2 and making the required disclosures in paragraphs (d)(2) and (d)(3) (except the hour burden resulting from paragraph (d)(2) of Rule 17g–2 was allocated across 7 NRSROs; however, the impact on the per firm total of allocating to 7 as opposed to 10 firms is minimal). *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33609–33610 (June 18, 2007); *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6473 (Feb. 9, 2009), and *Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63888–63889 (Dec. 4, 2009). Consequently, the adjusted current industry-wide annual hour burden for Rule 17g–2 would be 4,000 hours (12,000 hours/30 NRSROs = 400 hours; 10 NRSROs × 400 hours = 4,000 hours).

[941] The current OMB approved total industry-wide annual hour burden for Rule 17g–3 of 7,900 hours is based on 30 respondents preparing and filing the annual reports. *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33610 (June 18, 2007); *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6473 (Feb. 9, 2009), and *Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63888–63889 (Dec. 4, 2009). Consequently, the adjusted current industry-wide annual hour burden for Rule 17g–3 would be 2,633 hours (7,900 hours/30 NRSROs = 263 hours; 10 NRSROs × 263 hours = 2,633 hours).

[942] Of the 96,948 hours in the current OMB approved total industry-wide annual hour burden for Rule 17g–7, 90,948 hours are based on the number of Exchange Act-ABS transactions per year for which the disclosure requirement in the rule would apply (*i.e.,* not based on the number of respondents). *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4508 (Jan. 26, 2011). However, 6,000 hours in that total are based on the number of respondents. *Id.* Consequently, the adjusted current industry-wide annual hour burden for Rule 17g–7 would be 92,948 hours (6,000 hours/30 NRSROs = 200 hours; 10 NRSROs × 200 hours = 2,000 hours; 90,948 hours + 2,000 hours = 92,948 hours).

[943] *See, e.g.,* Testimony of Vicki Beal, Senior Vice President, Clayton Holdings, before the Financial Crisis Inquiry Commission (Sept. 23, 2010).

[944] *See* proposed new Rule 15Ga–2 and the amendments to Form ABS–15G; *see also* Section II.H.1 of this release for a more detailed discussion of this proposal.

[945] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4506–4507 (Jan. 26, 2011)

3. Is the estimate that 10 firms will be operate as third-party "due diligence service" providers over the next few years reasonable? Alternatively, should the Commission use some other number? Explain any choices made with respect to the number of third-party "due diligence service" providers that should be used for the purposes of the PRA, including any data and analysis supporting the choice.

4. Identify any sources of industry information that could be used to estimate the number of third-party "due diligence service" providers for purposes of the PRA.

D. Total Initial and Annual Recordkeeping and Reporting Burdens

Unless otherwise noted, the one-time and annual hour burden estimates per NRSRO described below are averages across all types of NRSROs that would be subject to the proposed amendments and new rules. The NRSROs vary, in terms of size and complexity, from small entities that employ less than 20 credit analysts to complex global organizations that employ over a thousand credit analysts.[946] Given the 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 dominate in terms of size and the volume of credit rating issuance.[947]

As discussed below, with respect to some burden estimates, the Commission preliminarily believes it would be reasonable to use the approximate number of credit ratings outstanding or the number of credit analysts employed based on the most recently submitted annual certifications of the NRSROs.[948] These data are presented in Figure 2 and Figure 3 below, respectively.

FIGURE 2—OUTSTANDING CREDIT RATINGS REPORTED BY NRSROS ON FORM NRSRO BY RATINGS CLASS

NRSRO	Financial institutions	Insurance companies	Corporate issuers	Asset-backed securities	Government, municipal & sovereign	Total ratings
A.M. Best	3	5,364	2,246	54	0	7,667
DBRS	16,630	120	5,350	8,430	12,400	42,930
EJR	82	45	853	14	13	1,007
Fitch	72,311	4,599	12,613	69,515	352,697	511,735
JCR	156	31	518	64	53	822
Kroll	17,263	60	1,000	0	61	18,384
Moody's	76,801	5,455	31,008	106,337	862,240	1,081,841
R&I	100	30	543	186	123	982
Realpoint	0	0	0	8,856	0	8,856
S&P	52,500	8,600	41,400	124,600	1,004,500	1,231,600
Total	235,846	24,304	95,531	318,056	2,232,087	2,905,824
HHI	2,599	2,601	3,145	3,145	3,767	3,495
HHI Inverse	3.85	3.84	3.18	3.18	2.65	2.86

FIGURE 3—CREDIT ANALYSTS EMPLOYED REPORTED BY NRSROS ON FORM NRSRO

NRSRO	Credit analysts	Credit analyst supervisors
A.M. Best	134	42
DBRS	67	20
EJR	5	3
Fitch	1,035	345
JCR	61	27
Kroll	7	4
Moody's	1,096	143
R&I	81	6
Realpoint	15	7

FIGURE 3—CREDIT ANALYSTS EMPLOYED REPORTED BY NRSROS ON FORM NRSRO—Continued

NRSRO	Credit analysts	Credit analyst supervisors
S&P	1,019	223
Total	3,520	820

1. Proposed Amendments to Rule 17g–1

The Commission is proposing several amendments to Rule 17g–1. As discussed below, the Commission preliminarily estimates that these proposals would result in additional one-time and annual hour burdens for NRSROs.

The Commission proposes amending paragraph (i) of Rule 17g–1 to require that an NRSRO make Form NRSRO and Exhibits 1 through 9 freely available on an easily accessible portion of its corporate Internet Web site.[949] The proposed amendment would remove the option for an NRSRO to make the Form publicly available "through another comparable, readily accessible means" as an alternative to Internet Web site disclosure. The Commission preliminarily estimates that there would be a minimal one-time hour burden attributable to requiring that an NRSRO make Form NRSRO and Exhibits 1 through 9 freely available on an easily

[946] *See, e.g., Annual Report on Nationally Recognized Statistical Rating Organizations. Commission* (Jan. 2011), pp. 4–9.

[947] Based on data collected from the NRSROs in their Form NRSROs and Rule 17g-3 annual reports, the Commission has used the Herfindahl-Hirschmann Index (HHI) to analyze market concentration among the 10 NRSROs. *Id.* HHI is calculated by squaring the market share of each firm competing in the market and then summing the resulting number. *Id.* The HHI is measured on a scale of 0 to 10,000 and approaches zero when a market consists of a large number of firms of relatively equal size. The HHI increases both as the number of firms in the market decreases and as the disparity in size between those firms increases. *Id.* According to the U.S. Department of Justice, markets in which the HHI is between 1,000 and 1,800 points are considered to be moderately concentrated, and those in which the HHI is in excess of 1,800 points are considered to be concentrated. *Id.* The Commission has calculated an HHI number using the number credit ratings outstanding per NRSRO and that number is 3,495, which is equivalent to there being approximately 2.86 equally sized firms. *Id.* The HHI using earnings reported by NRSROs in the Rule 17g-3 annual reports is 3,926, which the equivalent of 2.55 equally sized firms. *Id.* The inverse of the HHI ("HHI Inverse") is a measure of the number of equally sized firms which would constitute a comparable level of concentration for a given HHI and is calculated by dividing 10,000 by the HHI. *Id.*

[948] *See, Annual Report on Nationally Recognized Statistical Rating Organizations. Commission* (Jan. 2011), pp. 4–9.

[949] *See* proposed amendments to paragraph (i) of Rule 17g–1; *see also* Section II.E.1.b of this release for a more detailed discussion of this proposal.

accessible portion of its corporate Internet Web site and removing the option for an NRSRO to make its Form NRSRO and Exhibits 1 through 9 available through another comparable, readily accessible means. Currently, all NRSROs make Form NRSRO and Exhibits 1 through 9 available on their corporate Internet Web sites.[950] However, as noted earlier, the Commission preliminarily believes that a Form NRSRO and Exhibits 1 through 9 would be "easily accessible" if they could be accessed through a clearly and prominently labeled hyperlink on the home page of the NRSRO's corporate Internet Web site. All NRSROs would need to make changes to their corporate Internet Web sites to place clearly and prominently labeled hyperlinks on the Web sites to Form NRSRO and Exhibits 1 through 9. Based on staff experience, the Commission preliminarily estimates that re-configuring a corporate Internet Web site for this purpose would take an average of approximately 5 hours. For these reasons, the Commission preliminarily estimates that the proposed requirement would result in an average one-time hour burden to each NRSRO of approximately 5 hours, resulting in an average one-time industry-wide hour burden of approximately 50 hours.[951] The Commission preliminarily estimates that NRSROs would prepare these responses internally using their own corporate Internet Web site administrators. The Commission preliminarily does not believe the proposed requirement would result in an increase in the industry-wide annual hour burden attributable to Rule 17g–1 and Form NRSRO.

The Commission also is proposing to amend paragraph (i) of Rule 17g–1 to require that Exhibit 1 be made freely available in writing when requested. This would implement rulemaking mandated in Section 15E(q)(2)(D) of the Exchange Act.[952] With respect to making Exhibit 1 freely available in writing, the Commission notes that, under the proposed amendments to paragraph (i) of Rule 17g–1, Form NRSRO and Exhibits 1 through 9 would need to be made freely available on an easily accessible portion of the NRSRO's corporate Internet Web site. Moreover, as noted above, NRSROs currently comply with paragraph (i) of Rule 17g–1 by making their Form NRSROs and Exhibits 1 through 9 available on their corporate Internet Web sites. Consequently, an individual with access to the Internet and a printer can (and would be able to) obtain Exhibit 1 immediately through the Internet and could print the Exhibit if the individual wanted to have it in paper form. Therefore, the Commission preliminarily estimates that the instances in which an individual would request an NRSRO to provide a written copy of Exhibit 1 would be rare, given that the individual would need to wait for the request to be processed by the NRSRO and the Exhibit to arrive by mail as opposed to accessing it immediately via the Internet. Nonetheless, the Commission preliminarily estimates that some number of individuals may request an NRSRO to provide Exhibit 1 in writing.

The Commission preliminarily estimates that the proposed requirement would result in a one-time hour burden to each NRSRO as they would need to establish procedures and protocols for receiving and processing these requests. Based on staff experience, the Commission preliminarily estimates that each NRSRO would spend an average of approximately 48 hours establishing such procedures and protocols, resulting in an average industry-wide one-time hour burden of approximately 480 hours.[953]

In terms of annual hour burden, the Commission notes it is difficult to quantify the number of requests an NRSRO would receive each year. However, the Commission preliminarily estimates each NRSRO would on average receive approximately 200 requests per year and would spend an average of 20 minutes processing each request. The estimate of 200 requests is intended to serve as a "placeholder" for PRA purposes and the Commission will revise this estimate based on information provided by NRSROs and other commenters. For these reasons, the Commission estimates that the average annual hour burden to each NRSRO would be approximately 67 hours,[954] resulting in a total industry-wide annual hour burden of approximately 670 hours.[955] The Commission preliminarily estimates that NRSROs would prepare these responses internally.

The Commission also is proposing to amend paragraphs (e), (f), and (g) of Rule 17g–1 to require that an NRSRO use the Commission's EDGAR system to electronically submit Form NRSRO and Exhibits 1 through 9 with the Commission pursuant to these paragraphs in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T.[956] NRSROs currently submit these documents to the Commission in paper form.

The Commission preliminarily estimates that each NRSRO would spend an average of approximately 5 hours becoming familiar with the EDGAR filing system and completing and submitting Form ID, which is necessary to access the system. As discussed below, the Commission preliminarily estimates that the one-time hour burden for each NRSRO to complete Form ID would be 15 minutes.[957] In addition, as discussed above and below, the Commission is proposing that the Rule 17g–3 annual report also be submitted using the EDGAR system.[958] The Commission's preliminary estimate of 5 hours to become familiar with the EDGAR system would include developing an understanding of how to use the system for both submitting Form NRSROs and submitting the Rule 17g–3 annual reports. Consequently, for purposes of the PRA and the Economic Analysis in Section V of this release, the Commission is allocating this one-time hour burden and corresponding cost solely to Rule 17g–1. In addition, because the hour burden of 15 minutes for Form ID is addressed below, the Commission estimates that each NRSRO would spend an average of 4.75 hours becoming familiar with how to use the EDGAR system, resulting in an industry-wide one-time hour burden of approximately 47.5 hours.[959]

The Commission does not believe changing the method of submitting Form NRSRO and Exhibits 1 through 9 from a paper submission to an electronic submission would increase the current annual hour burden for Rule 17g–1. In particular, the Commission believes that both the amount of time it currently takes an NRSRO to send these materials, once compiled, to the Commission's headquarters by mail, messenger, or hand-delivery by a representative of the NRSRO and the time it would take to submit them electronically through the EDGAR system are *de minimus.*

[950] *See, e.g., Annual Report on Nationally Recognized Statistical Rating Organizations. Commission* (Jan. 2011), pp. 18–19.

[951] 10 NRSROs × 5 hours = 50 hours.

[952] *See* 15 U.S.C. 78o–7(q)(2)(D).

[953] 10 NRSROs × 48 hours = 480 hours.

[954] 200 requests × 20 minutes per request = 67 hours per year.

[955] 10 NRSROs × 67 hours per year = 670 hours per year.

[956] *See* proposed amendments to paragraphs (e), (f), and (g) of Rule 17g–1; *see also* Section II.L of this release for a more detailed discussion of these proposals.

[957] *See* Section IV.D.11 of this release.

[958] *See* proposed amendments to Regulation S–T and Rule 17g–3; *see also* Section II.L of this release for a more detailed discussion of this proposal.

[959] 10 NRSROs × 4.75 hours = 47.5 hours.

For the foregoing reasons, the Commission estimates that the total industry-wide one-time hour burden resulting from the proposed amendments to Rule 17g–1 would be approximately 577.5 hours [960] and the total industry-wide annual burden would be approximately 670 hours.[961]

2. Proposed Amendments to Form NRSRO Instructions

The Commission is proposing to amend the instructions for Exhibit 1 to Form NRSRO.[962] The amendments would confine the disclosures in the Exhibit to transition and default rates and certain limited supplemental information.[963] Moreover, the amendments would standardize the production and presentation of the transition and default statistics. As discussed below, the Commission preliminarily estimates that these proposals would result in additional one-time and annual hour burdens for NRSROs.

The Commission notes that an NRSRO currently is required to provide transition and default rates in Exhibit 1 for each class of credit rating for which it is registered and for 1, 3, and 10-year periods. The Commission preliminarily estimates that an NRSRO would use the internal information technology systems and expertise and other resources it currently devotes to processing the information necessary to monitor credit ratings and calculate transition and default statistics in order to program a system to comply with the proposed amendments to the Instructions for Exhibit 1. At the same time, the Commission notes that, under the proposed amendments, NRSROs would be required to adhere to specific requirements that may not be the same as their current methods for calculating and presenting transition and default rates. Consequently, the Commission preliminarily estimates that the proposed amendments requiring standardized Transition/Default Matrices would result in a one-time hour burden to program existing systems to create the Transition/Default Matrices that would be required under the proposed amendments and an increase in the annual hour burden to comply with the proposed instructions to Exhibit 1.

As noted above, the size and complexity of the NRSROs varies greatly. The magnitude of this variance is reflected in the number of credit ratings each NRSRO has outstanding.[964] For example, two NRSROs have over 1,000,000 credit ratings outstanding in the classes of credit ratings for which they are registered; others have fewer than 1,000 such ratings.[965] The hour burden associated with calculating and presenting these performance statistics would depend in large part on the number of obligors, securities, and money market instruments assigned credit ratings by the NRSRO.[966] Consequently, the one-time and annual burdens per NRSRO would vary widely.

In order to account for this variance, the Commission preliminarily believes that the one-time and annual hour burden estimates should be based on the number of credit ratings outstanding. Based on the annual certifications submitted by the NRSROs for the 2009 calendar year-end, there were approximately 2,905,824 credit ratings outstanding across all 10 NRSROs.[967] The Commission preliminarily estimates that the one-time industry-wide hour burden to establish systems to process the relevant information necessary to calculate the Transition/Default Matrices and make the necessary calculations would be approximately 3 seconds per outstanding credit rating, which would result in a one-time industry-wide hour burden of approximately 2,420 hours.[968] Moreover, because of the wide variance in the number of credit ratings outstanding among the NRSROs, the Commission preliminarily estimates that this one-time hour burden of 2,420 hours would be allocated to the 10 NRSROs based on the number of credit ratings each has outstanding (although larger NRSROs may realize economies of scale). For example, the two largest NRSROs had just over 1,000,000 credit ratings outstanding, the next largest had approximately 500,000 credit ratings outstanding, and the remaining 7 NRSROs had amounts ranging from 42,930 credit ratings outstanding to 982 credit ratings outstanding.[969]

The Commission preliminarily believes that the annual hour burden to comply with the proposed amendments to the Instructions for Exhibit 1 would be less than the one-time hour burden since the NRSROs would have established systems to process the necessary information to produce the required Transition/Default Matrices. Consequently, the Commission preliminarily estimates that the annual hour burden to each NRSRO to calculate the Transition/Default Matrices would be approximately 1.5 seconds per outstanding credit rating, resulting in an industry-wide annual hour burden of approximately 1,210 hours.[970] Moreover, although larger NRSROs may realize economies of scale, the Commission preliminarily estimates that the industry-wide annual hour burden of 1,210 hours would be allocated to each NRSRO based on the number of credit ratings the firm had outstanding.[971]

For the foregoing reasons, the Commission estimates that the total industry-wide one-time hour burden resulting from the proposed amendments to the instructions for Exhibit 1 to Form NRSRO would be approximately 2,420 hours and the total industry-wide annual burden would be approximately 1,210 hours.[972]

[960] 480 hours + 50 + 47.5 hours = 577.5 hours.

[961] This estimate would increase the adjusted industry-wide annual hour burden for Rule 17g–1 and Form NRSRO from 2,133 hours to 2,803 hours (2,133 hours + 670 hours = 2,803 hours).

[962] *See* Instruction H to Form NRSRO (as it relates to Exhibit 1).

[963] *See* proposed amendments to the instructions for Exhibit 1 to Form NRSRO (17 CFR 249b.300); *see also* Section II.E.1.a of this release for a more detailed discussion of this proposal.

[964] *See* Figure 2 in Section IV.D of this release.

[965] *Id.*

[966] For example, as discussed in more detail in Section II.E.1.a of this release, the applicant or NRSRO, in producing a Transition/Default Matrix, would need to determine a start-date cohort consisting of the obligors, securities, and money market instruments in the applicable class or subclass of credit ratings that were assigned a credit rating that was outstanding as of the start date for the applicable period (*i.e.,* the date 1, 3, or 10 years prior to the most recently ended calendar year). The applicant or NRSRO also would need to group the obligors, securities, and money market instruments in the start-date cohort based on the credit rating assigned to them as of the start date and determine the outcome for each such obligor, security, and money market instrument in the group during, or as of the end of, the relevant period. This exercise would be more time-consuming for an NRSRO that has over 1,000,000 credit ratings outstanding than for an NRSRO that has fewer than 10,000 credit ratings outstanding (2 NRSROs have over 1,000,000 credit ratings outstanding and 5 NRSROs have fewer than 10,000 credit ratings outstanding). *See* Figure 2 in Section IV.D of this Release.

[967] *Id.*

[968] 2,905,824 credit ratings × 3 seconds = 2,421.52 hours (rounded to 2,420 hours).

[969] *See* Figure 2 in Section IV.D of this release.

[970] 2,905,824 credit ratings × 1.5 seconds = 1,210.76 hours (rounded to 1,210 hours).

[971] *See* Figure 2 in Section IV.D of this release.

[972] These estimates would increase the adjusted industry-wide annual hour burden for Rule 17g–1 and Form NRSRO from 2,133 hours to 3,343 hours (2,133 hours + 1,210 hours = 3,343 hours). Combined with the industry-wide annual burden hour increase of 670 hours resulting from the proposed amendments to Rule 17g–1 discussed above in Section IV.D.2 of this release, the total increase to the adjusted industry-wide annual hour burden for Rule 17g–1 and Form NRSRO would be from 2,133 hours to 4,013 hours (2,133+670 hours + 1,210 hours = 4,013 hours). The Commission notes that the adjusted industry-wide annual hour burden for all of Rule 17g–1 and Form NRSRO (which includes providing the transition and default rates required in Exhibit 1 under the existing instructions) is 2,133 hours. Consequently, the Commission preliminarily believes these estimates of the incremental burden that would

3. Proposed Amendments to Rule 17g–2

The Commission proposes adding paragraph (a)(9) to Rule 17g–2 to identify the policies and procedures an NRSRO is required to establish, maintain, and enforce pursuant to Section 15E(h)(4)(A) of the Exchange Act and proposed paragraph (c) of Rule 17g–8 as a record that must be made and retained.[973] In addition, the Commission is proposing to add the following new paragraphs to Rule 17g–2 to identify records that must be retained: (1) paragraph (b)(12) would identify the internal control structure an NRSRO must establish, maintain, enforce, and document pursuant to Section 15E(c)(3)(A);[974] (2) paragraph (b)(13) would identify the policies and procedures an NRSRO is required to establish, maintain, enforce, and document pursuant to proposed paragraph (a) of new Rule 17g–8;[975] (3) paragraph (b)(14) would identify the policies and procedures an NRSRO must establish, maintain, enforce, and document pursuant to proposed paragraph (b) of new Rule 17g–8;[976] and (4) paragraph (b)(15) would identify the standards of training, experience, and competence for credit analysts an NRSRO must establish, maintain, enforce, and document pursuant to proposed new Rule 17g–9.[977] As discussed below, the Commission preliminarily estimates that these proposals would result in additional one-time and annual hour burdens for NRSROs.

The Commission is providing preliminary estimates below in Section IV.D.5 of this release of the one-time and annual hour burdens that would result from establishing, maintaining, enforcing, and *documenting* the policies and procedures required by Section 15E(h)(4)(A) of the Exchange Act and proposed paragraph (c) of Rule 17g–8. Because the requirement to *document* these procedures would be the same as the requirement in proposed paragraph (a)(9) of Rule 17g–2 to *make* this record, the PRA burdens associated with that aspect of the making of the record are addressed below in Section IV.D.5 of this release.

Consequently, for the purposes of Rule 17g–2, the Commission is providing preliminary estimates of the one-time and annual hour burdens resulting from the requirement to *retain* the records that would be identified in new paragraphs (a)(9), (b)(12), (b)(13), (b)(14), and (b)(15) of Rule 17g–2. The Commission preliminarily estimates that the one-time hour burden would result from the NRSRO needing to update its record retention policies and procedures to incorporate these new records that would need to be retained. Based on staff experience, the Commission preliminarily estimates that each NRSRO would spend an average of approximately 20 hours updating its record retention policies and procedures, resulting in an industry-wide one-time hour burden of approximately 200 hours.[978]

In terms of annual hour burden, the Commission notes that the adjusted industry-wide annual hour burden attributable to Rule 17g–2 is 4,000 hours, resulting in an average annual burden of 400 hours per NRSRO.[979] This burden amount is attributable to 8 different types of records that must be made and retained by the NRSRO, 11 types of records that must be retained if made or received, and to the disclosure requirements in paragraphs (d)(2) and (d)(3) of Rule 17g–2.[980] The Commission preliminarily believes that most of the hour burden is attributable to making the records identified in paragraph (a) of the Rule 17g–2 and making the disclosures required in paragraph (d) of Rule 17g–2 as this work is substantially more labor intensive than retaining a record. Consequently, the Commission preliminarily estimates that the burden associated with retaining the 5 new records that would be identified in new paragraphs (a)(9), (b)(12), (b)(13), (b)(14), and (b)(15) of Rule 17g–2 would be minimal because NRSROs already should have well-established procedures with respect to the records they must make and retain pursuant to Rule 17g–2. In addition, the Commission does not expect the new records would change frequently given that they would be the NRSRO's internal control structure required pursuant to Section 15E(c)(3)(A) of the Exchange Act,[981] various types of policies and procedures, and the standards of training, experience, and competence for credit analysts an NRSRO must establish, maintain, enforce, and document pursuant to proposed new Rule 17g–9. Accordingly, once the original record is retained, the need to expend resources to retain updated versions of the original record would be infrequent. Therefore, the Commission preliminarily estimates that it would take approximately one hour per record each year to retain updated versions of these records. For these reasons, the Commission preliminarily estimates that the annual hour burden for each NRSRO attributable to these proposals would be approximately 5 hours,[982] resulting in an industry-wide annual hour burden of approximately 50 hours.[983]

The Commission is proposing to repeal paragraph (d)(2) of Rule 17g–2 and re-codify and enhance the requirements in paragraph (d)(3) of Rule 17g–2 in proposed new paragraph (b) of Rule 17g–7.[984] The Commission preliminarily estimates that the repeal and re-codification would result in *de minimis* one-time hour burdens to each NRSRO.[985] The one-time and annual hour burden resulting from the proposed enhancements to the requirements currently codified in paragraph (d)(3) are discussed below in Section V.D.4 of this release, which addresses the one-time and annual hour burdens resulting from the proposed amendments to Rule 17g–7.

For the foregoing reasons, the Commission estimates that the total industry-wide one-time hour burden resulting from the proposed amendments to Rule 17g–2 would be approximately 200 hours and the total industry-wide annual hour burden would be approximately 50 hours.[986]

result from the proposed amendments to the Instructions for Exhibit 1 are conservatively large.

[973] *See* proposed new paragraph (a)(9) to Rule 17g–2(a)(9); *see also* Section II.C.2 of this release for a more detailed discussion of this proposal.

[974] *See* proposed new paragraph (b)(12) of Rule 17g–2; *see also* Section II.A.2 of this release for a more detailed discussion of this proposal.

[975] *See* proposed new paragraph (b)(13) to Rule 17g–2; *see also* Section II.F.2 of this release for a more detailed discussion of this proposal.

[976] *See* proposed new paragraph (b)(14) to Rule 17g–2; *see also* Section II.J.2 of this release for a more detailed discussion of this proposal.

[977] *See* proposed new paragraph (b)(15) to Rule 17g–2; *see also* Section II.I.2 of this release for a more detailed discussion of this proposal.

[978] 10 NRSROs × 20 hours = 200 hours.

[979] 4,000 hours/10 NRSROs = 400 hours.

[980] *See* 17 CFR 240.17g–2(a), (b), (d)(2), and (d)(3).

[981] *See* 15 U.S.C. 78o–7(c)(3)(A).

[982] 5 records × 1 hour = 5 hours.

[983] 10 NRSROs × 5 hours = 50 hours.

[984] *See* proposed amendments to paragraphs (d)(2) and (3) of Rule 17g–2 and proposed new paragraph (b) of Rule 17g–7; *see also* Section II.E.2 of this release for a more detailed discussion of this proposal.

[985] For example, each NRSRO likely would remove the disclosures required pursuant to paragraph (d)(2) Rule 17g–2 from its corporate Internet Web sites (though such a removal would not be mandatory).

[986] The adjusted industry-wide annual hour burden for Rule 17g–2 is 4,000 hours. The elimination of the requirements in paragraph (d)(2) of Rule 17g–7 would subtract 70 hours from that amount. *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6472 (Feb. 9, 2009). In addition, the re-codification of paragraph (d)(3) of Rule 17g–2 in proposed new paragraph (b) of Rule 17g–7 would subtract an additional 450 hours from the adjusted industry-wide annual hour burden for Rule 17g–2. *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR

Continued

4. Proposed Amendments to Rule 17g–3

The Commission proposes amending paragraphs (a) and (b) of Rule 17g–3 to implement the rulemaking mandated by Section 15E(c)(3)(B) of the Exchange Act.[987] As discussed below, the Commission preliminarily estimates that these proposals would result in additional one-time and annual hour burdens for NRSROs.

The proposed amendment to paragraph (a) would add a new paragraph (a)(7) to require an NRSRO to include an additional report—a report on the NRSRO's internal control structure—with its annual submission of reports pursuant to Rule 17g–3. The proposed amendment to paragraph (b) of Rule 17g–3 would require the NRSRO's CEO or, if the firm does not have a CEO, an individual performing similar functions, to provide a signed statement that would be attached to the report. The Commission preliminarily estimates that the proposed amendments would result in one-time and annual hour burdens.

The Commission notes that NRSROs already should have developed processes and protocols to prepare the annual reports required by Rule 17g–3. Consequently, the Commission preliminarily estimates that the internal hour burden associated with the first submission of the report would not be materially different than the hour burden associated with submitting subsequent reports, although the time required to prepare subsequent reports could decrease incrementally over time as the NRSRO gains experience with the requirement. The Commission, however, preliminarily estimates that an NRSRO likely would engage outside counsel to analyze the requirements for the report and assist in drafting and reviewing the first report, given that it must be signed by the NRSRO's CEO or an individual performing a similar function. The time an outside attorney would spend on this work would depend on the size and complexity of the NRSRO. The Commission preliminarily estimates that an attorney would spend an average of approximately 100 hours assisting an NRSRO and its CEO or other qualified individual in drafting and reviewing the first report, resulting in an industry-wide external one-time hour burden of approximately 1,000 hours.[988] Based on industry sources, the Commission estimates that the cost of an outside counsel would be approximately $400 per hour.[989] For these reasons, the Commission estimates that the average one-time cost to an NRSRO would be approximately $40,000,[990] resulting in an industry-wide one-time cost of approximately $400,000.[991]

The Commission preliminarily estimates, based on staff experience, that each NRSRO would spend on average approximately 150 hours preparing the internal control report to be included with the other annual reports filed with the Commission, resulting in an industry-wide annual burden of approximately 1,500 hours.[992]

In addition, the Commission preliminarily estimates that an NRSRO likely would continue to engage outside counsel to assist in preparing the report. As noted above, the time an outside attorney would spend on this work would depend on the size and complexity of the NRSRO. In addition, the Commission preliminarily estimates that the time an outside attorney would spend assisting in the preparation of subsequent reports would be less than the time spent on preparing the first report since the counsel's work would not need to include an initial analysis of the new requirements. Consequently, the Commission estimates that an attorney would spend an average of approximately 50 hours assisting an NRSRO and its CEO or other qualified individual in drafting and reviewing the report, resulting in an industry-wide annual hour burden of approximately 500 hours.[993] As stated above, 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 annual cost to an NRSRO to comply with this requirement would be approximately $20,000,[994] resulting in an industry-wide annual cost of approximately $200,000.[995]

The amendments also would require that the Rule 17g–3 annual reports be submitted electronically on the Commission's EDGAR system.[996] As discussed in Section IV.D.1 of this release, the Commission preliminarily estimates each NRSRO would spend 5 hours becoming familiar with how to use the EDGAR system and to complete Form ID for the purposes of submitting Form NRSRO (and Exhibits 1 through 9) and the Rule 17g–3 annual reports. For the purposes of this PRA and the Economic Analysis section below, the Commission is allocating that time to Rule 17g–1 and Form ID.

In addition, the Commission does not believe that changing the method of submitting the annual reports from a paper submission to an electronic submission would increase the current hour burden for Rule 17g–3. For example, the Commission does not believe the amount of time it currently takes an NRSRO to gather these materials and send them to the Commission's headquarters by mail, messenger, or hand-delivery would be less than the time it would take to submit them electronically through the EDGAR system.

For the foregoing reasons, the Commission preliminarily estimates that the proposed amendments to Rule 17g–3 would result in a total industry-wide one-time cost of approximately $400,000, a total industry-wide annual hour burden of approximately 1,500 hours, and a total industry-wide annual cost of approximately $200,000.[997]

5. Proposed New Rule 17g–7

The Commission is proposing to add new paragraphs (a) and (b) to Rule 17g–7, which would contain substantial new requirements.[998] As discussed below, the Commission preliminarily estimates that these proposals would result in additional one-time and annual hour burdens for NRSROs.

The Commission is proposing to add new paragraphs (a)(1) and (2) to Rule 17g–7 to implement rulemaking

at 63853 (Dec. 4, 2009). Consequently, after these subtractions, the adjusted industry-wide annual hour burden for Rule 17g–2 would be 3,480 hours (4,000 hours − 70 hours − 450 hours = 3,480 hours). The proposed amendments to add paragraphs (a)(9), (b)(12), (b)(13), (b)(14), and (b)(15) to Rule 17g–2 would, as discussed above, add approximately 50 hours to the adjusted industry-wide annual hour burden resulting in a total adjusted industry-wide annual hour burden of 3,530 hours (3,480 hours + 50 hours = 3,530 hours).

[987] *See* proposed new paragraphs (a)(7) and (b)(2) of Rule 17g–3; *see also* Section II.A.3 of this release for a for a more detailed discussion of this proposal.

[988] 10 NRSROs × 20 hours = 200 hours.

[989] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011) (providing an estimate of $400 an hour to engage outside professionals) and *Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63889 (Dec. 4, 2009) (providing an estimate of $400 per hour to engage an outside attorney).

[990] 100 hours × $400 = $40,000. *See also, Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63889 (Dec. 4, 2009) (providing an estimate of $400 per hour to engage an attorney).

[991] 10 NRSROs × $40,000 = $400,000.

[992] 10 NRSROs × 150 hours = 1,500 hours.

[993] 10 NRSROs × 20 hours = 200 hours.

[994] 50 hours × $400 = $20,000. *See also, Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63889 (Dec. 4, 2009) (providing an estimate of $400 per hour to engage an attorney).

[995] 10 NRSROs × $20,000 = $200,000.

[996] *See* proposed new paragraph (d) of Rule 17g–3; *see also* Section II.L of this release for a more detailed discussion of this proposal.

[997] This estimate would increase the adjusted industry-wide annual hour burden for Rule 17g–3 from 2,633 hours to 4,133 hours.

[998] 17 CFR 240.17g–7.

mandated in Sections 15E(s)(1), (2), (3), and (4)(D) of the Exchange Act.[999] Proposed new paragraphs (a)(1) and (2) of Rule 17g–2 would require, respectively, an NRSRO, when taking a rating action, to publish a form containing information about the credit rating resulting from, or subject to, the rating action and any certification of a provider of third-party due diligence services received by the NRSRO relating to the credit rating.[1000]

The Commission preliminarily believes that much of the information required to be disclosed in the form could be standardized based on the class and subclass of credit rating. For example, an NRSRO could develop a set of standardized disclosures for structured finance products based on whether the credit rating was issued for an RMBS, CMBS, CDO, CLO, ABCP, or other type of structured finance product. Similarly, for corporate issuers, the NRSRO could develop a set of standardized disclosures depending on factors such as the industry sector and geographic location of the rated issuer. In addition, the Commission believes that much of the information, particularly as it relates to the specific obligor, security, or money market instrument that is subject to the rating action, already would be generated or collected through the credit rating process. Finally, the Commission notes that globally active NRSROs are subject to similar requirements.[1001]

Consequently, the Commission estimates that the proposal would result in a one-time hour burden to develop the standardized disclosures and to create systems, protocols, and procedures for populating the form with information generated and collected during the rating process. In addition, the NRSRO would need to develop procedures designed to ensure that all the information required to be included in the form is input into the form prior to the publication of the credit rating, that any certifications received from a provider of third-party due diligence services are attached to the form, and that the form and certifications are published with the credit rating.

The Commission preliminarily estimates that the one-time hour burden to develop these standardized disclosures would vary considerably among NRSROs based on the number of credit ratings they issue and monitor and the number of classes and subclasses of credit ratings for which they issue and monitor credit ratings. Specifically, the larger NRSROs that issue and monitor a high volume of credit ratings across multiple classes and subclasses of credit ratings would bear a significantly greater burden than smaller NRSROs that may need to develop standardized disclosures for far fewer classes and subclasses of credit ratings. The Commission estimates that an NRSRO would spend an average of approximately 5,000 hours to develop the standardized disclosures and create the systems, protocols, and procedures for populating the form with information generated and collected during the rating process.[1002] However, the Commission preliminarily estimates that this amount is heavily skewed upward by the number of credit ratings issued, as well as the breadth of the classes and subclasses rated, by the three largest NRSROs as compared to the seven smaller NRSROs. Given the 5,000 hours per NRSRO preliminary estimate, the Commission preliminarily estimates that the proposal would result in a one-time industry wide hour burden of approximately 50,000 hours.[1003] In addition, the Commission preliminarily allocates 75% of these burden hours (37,500 hours) to internal burden and the remaining 25% (12,500 hours) to external burden to hire outside professionals to assist in setting up the process to generate the forms and publish them with applicable credit ratings.[1004] The Commission preliminarily estimates $400 per hour for retaining outside professionals such as attorneys and information technology consultants, resulting in an industry-wide one-time cost of approximately $5,000,000.[1005]

With respect to the annual hour burden, the Commission preliminarily estimates that the estimate should be divided into two components. The first component would constitute the amount of time an NRSRO would spend to update its standardized disclosures. The Commission preliminarily estimates an NRSRO would spend substantially less time updating the disclosures than the one-time estimate of approximately 5,000 hours per NRSRO to initially establish the standardized disclosures and the systems, protocols, and processes to generate the forms. Consequently, the Commission preliminarily estimates that each NRSRO would spend an average of approximately 500 hours per year updating the standardized disclosures, resulting in an annual industry-wide hour burden of approximately 5,000 hours. The Commission preliminarily estimates that the update process would be handled by the NRSROs internally.

The second component would constitute the amount of time an NRSRO would spend generating and publishing each form and attaching applicable certifications to the form. The Commission preliminarily believes that this estimate should be based on the number of rating actions taken per year by the NRSROs because the requirement to generate and publish the form and attach the certifications would be triggered upon the taking of a rating action. Based on information submitted to the Commission by NRSROs pursuant to paragraph (a)(6) of Rule 17g–3, the Commission preliminarily estimates that NRSROs took approximately 2,000,000 credit rating actions in 2009, consisting of upgrades, downgrades, placements on credit watch, and withdrawals of credit ratings.[1006]

The Commission notes this figure does not include the following rating actions: Expected or preliminary credit ratings, initial credit ratings, and affirmations of existing credit ratings.[1007] Based on staff experience,

[999] *See* 15 U.S.C. 78o–7(s)(1), (2), (3), and (4)(D) and proposed new paragraph (a) of Rule 17g–7; *see also* Sections II.G.1 through G.5 of this release for a more detailed discussion of this proposal.

[1000] *See* proposed new paragraphs (a)(1) and (2) of Rule 17g–7.

[1001] *See, e.g.,* Regulation no. 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies, Article 8.2 and Annex 1, Section D.

[1002] This estimate is based on the Commission's estimate for the amount of time it would take a securitizer to set-up a system to make the disclosures required by Form ABS–15G. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011). The Commission significantly increases the estimate for Form ABS–15G because the form required pursuant to Rule 17g–7 would contain substantially more qualitative information for which the NRSRO would need to develop standardized disclosures.

[1003] 10 NRSROs × 5,000 hours = 50,000 hours.

[1004] 50,000 hours × 0.75 = 37,500 hours; 50,000 hours × 0.25 = 12,500 hours. This allocation is based on the Commission's allocation of the industry-wide hour burden for the amount of time it would take a securitizer to set-up a system to make the disclosures required by Form ABS–15G. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011).

[1005] 12,500 hours × $400 = $5,000,000. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011) (providing an estimate of $400 an hour engage outside professionals) and *Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63889 (Dec. 4, 2009) (providing an estimate of $400 per hour to engage an outside attorney).

[1006] *See* 17 CFR 240.17g–7(a)(6).

[1007] As discussed in more detail in Section II.G.1 of this release, the Commission is proposing that the requirement to publish the form and any

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the Commission preliminarily believes expected or preliminary credit ratings are published primarily (but not exclusively) with respect to new issuances of structured finance products. In the PRA for the adoption of Rule 17g–7, the Commission estimated that there would be an average of approximately 2,067 Exchange Act-ABS offerings per year.[1008] The Commission, based on staff experience, believes expected or preliminary credit ratings are used in other types of offerings as well and, therefore, is increasing that estimate by 100% or to 4,134 preliminary or expected credit ratings per year.[1009]

In terms of estimating the number initial credit ratings, the Commission notes that there were approximately 2,905,824 credit ratings outstanding across all 10 NRSROs as of the 2009 calendar year-end.[1010] Based on staff experience, the Commission estimates that the average maturity of rated securities and money market instruments is approximately 7 years. Consequently, assuming 2,905,824 is the approximate average number of credit ratings outstanding at any given time, the Commission preliminarily estimates that approximately 415,117 initial credit rating are issued per year.[1011]

Finally, with respect to affirmations of existing credit ratings, the Commission preliminarily believes that NRSROs generally affirm existing credit ratings at least once a year. Consequently, the Commission preliminarily estimates that the number of affirmations would be the total number of credit ratings outstanding (2,905,824), less the number of credit ratings subject to other types of rating actions, excluding expected or preliminary ratings (2,000,000), and less the number of credit ratings assigned to securities or money market instruments that are paid off in full during the year (415,117). Consequently, the Commission preliminarily estimates that the number of affirmations per year is approximately 490,707.[1012]

Based on these estimates, the Commission preliminarily estimates that the 10 NRSROs take approximately 2,909,958 credit rating actions per year.[1013] The Commission preliminarily estimates that the time it would take to generate a form by populating it with the required disclosures and to publish the form with the credit rating would be approximately 15 minutes on average, resulting in an industry-wide annual hour burden of approximately 727,490 hours.[1014] Moreover, although larger NRSROs may realize economies of scale, the Commission preliminarily estimates that the annual burden would be allocated to the 10 NRSROs based on the number of credit ratings they have outstanding.[1015]

The Commission also is proposing to add new paragraph (b) to Rule 17g–7. The proposed amendments would: (1) Re-codify in paragraph (b) of Rule 17g–7 requirements currently contained in paragraph (d)(3) of Rule 17g–2; and (2) substantially enhance those requirements.[1016] The Commission notes that NRSROs currently are required to provide ratings history information for each credit rating initially determined on or after June 26, 2007. The Commission preliminarily estimates that NRSROs could use the internal information technology systems and expertise and other resources they currently devote to complying with this requirement to implement the proposed enhancements. At the same time, the Commission notes that, under the proposed amendments, NRSROs would be required to add substantially more ratings histories to the disclosures and provide more information about each rating action in the ratings history for a given obligor, security, or money market instrument. Consequently, the Commission preliminarily estimates that the proposed amendments would result in a one-time hour burden to program existing systems and initially add the ratings histories for all outstanding credit ratings as of June 26, 2007, and an incremental increase in the annual hour burden to comply with the enhanced requirements.

When adopting paragraph (d)(3) of Rule 17g–2, the Commission estimated that the average one-time hour burden per NRSRO would be approximately 45 hours.[1017] Based on that estimate, the Commission estimates that the proposed amendments to this disclosure requirement would result in an average one-time hour burden for each NRSRO of approximately 135 hours, resulting in an industry-wide one-time hour burden of approximately 1,350 hours.[1018] In addition, when adopting paragraph (d)(3) of Rule 17g–2, the Commission estimated the average annual burden per NRSRO would be approximately 15 hours.[1019] Based on that estimate, the Commission preliminarily estimates that the proposed enhancements would require each NRSRO to spend an average of 45 hours per year making the disclosures, resulting in an industry-wide annual hour burden of approximately 450 hours.[1020]

For the foregoing reasons, the Commission estimates that the proposed amendments to Rule 17g–7 would result in a total industry-wide one-time hour burden of approximately 51,350 hours,[1021] a total industry-wide one-time cost of approximately $5,000,000,[1022] and a total industry-wide annual hour burden of approximately 732,940 hours.[1023]

certifications would be triggered when an NRSRO takes the following rating actions: Publication of an expected or preliminary credit rating assigned to an obligor, security, or money market instrument before the publication of an initial credit rating; an initial credit rating; an upgrade or downgrade of an existing credit rating (including a downgrade to, or assignment of, default); a placement of an existing credit rating on credit watch or review; an affirmation of an existing credit rating; and a withdrawal of an existing credit rating.

[1008] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4508 (Jan. 26, 2011).

[1009] 2,067 offerings × 2 = 4,134 offerings.

[1010] *See* Figure 2 in Section IV.D of this Release.

[1011] 2,905,824 credit ratings/7 = 415,117 credit ratings. In other words, the Commission estimates that issuers pay off in full all outstanding principal and interest outstanding with respect to approximately 415,117 rated securities or money market instruments and, consequently, the credit ratings for these securities and money market instruments are withdrawn. Those withdrawn credit ratings, in turn, are replaced by 415,117 initial (or new) credit ratings. The Commission notes that outstanding credit ratings assigned to securities and money market instruments are withdrawn for other reasons, including the security or money market instrument went into default. In addition, the Commission notes that a percent of the outstanding credit ratings are assigned to obligors as entities and, therefore, these credit ratings would not be withdrawn because an obligation was extinguished. However, they might be withdrawn for other reasons, including the obligor went into default. Nonetheless, the Commission preliminarily believes these estimates are reasonable approximations of the number of initial credit ratings determined per year.

[1012] [2,905,824 outstanding credit ratings] − [2,000,000 credit ratings that are upgraded, downgraded, placed on watch, or withdrawn] − [415,117 rated securities and money market instruments that pay off in full] = 490,707 affirmations.

[1013] [2,000,000 credit rating actions constituting upgrades, downgrades, placements on credit watch, and withdrawals] + [4,134 preliminary or expected credit ratings] + [415,117 initial credit ratings] + [490,707 affirmations of existing credit ratings] = 2,909,958 rating actions per year.

[1014] 2,909,958 rating actions × .25 hours = 727,489.5 hours (rounded to 727,490 hours).

[1015] *See* Figure 2 in Section IV.D of this release.

[1016] *See* proposed new paragraph (b) of Rule 17g–7; *see also* Section II.E.2 of this release for a more detailed discussion of this proposal.

[1017] *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63853 (Dec. 4, 2009).

[1018] 10 NRSRO × 135 hours = 1,350 hours.

[1019] *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63853 (Dec. 4, 2009).

[1020] 10 NRSRO × 45 hours = 450 hours.

[1021] 50,000 hours + 1,350 hours = 51,350 hours.

[1022] 12,500 hours × $400 = $5,000,000.

[1023] 727,490 hours + 5,000 hours + 450 hours = 732,940 hours. This estimate would increase the adjusted industry-wide annual hour burden for Rule 17g–7 from 92,948 hours to 820,888 hours (732,940 hours + 92,948 = 825,888 hours). In addition, the annual hour burden per NRSRO resulting from the existing requirements in

6. Proposed New Rule 17g–8

The Commission is proposing new Rule 17g–8, which would have three paragraphs (a), (b), and (c).[1024] As discussed below, the Commission preliminarily estimates that these proposals would result in additional one-time and annual hour burdens for NRSROs.

Proposed paragraph (a) of new Rule 17g–8 would implement Section 15E(r) of the Exchange Act by requiring an NRSRO to have policies and procedures with respect to the procedures and methodologies the NRSRO uses to determine credit ratings.[1025] The Commission preliminarily estimates that the proposed requirement in paragraph (a) of new Rule 17g–8 would result in one-time and annual hour burdens for NRSROs. In this regard, the Commission notes that Section 15E(g)(1) of the Exchange Act requires an NRSRO to establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of the business of the NRSRO, to prevent the misuse of material, nonpublic information by the NRSRO or any person associated with the NRSRO.[1026] The Commission supplemented this statutory requirement by adopting Rule 17g–4, which provides that the policies and procedures under Section 15E(g) of the Exchange Act must include policies and procedures reasonably designed to prevent: (1) The inappropriate dissemination within and outside the NRSRO of material nonpublic information obtained in connection with the performance of credit rating services; (2) a person within the NRSRO from purchasing, selling, or otherwise benefiting from any transaction in securities or money market instruments when the person is aware of material nonpublic information obtained in connection with the performance of credit rating services that affects the securities or money market instruments; and (3) the inappropriate dissemination within and outside the NRSRO of a pending credit rating action before issuing the credit rating on the Internet or through another readily accessible means.[1027]

When adopting Rule 17g–4, the Commission assumed NRSROs already had procedures in place to address the specific misuses of material nonpublic information identified in Rule 17g–4.[1028] Nonetheless, the Commission expected that some NRSROs might need to modify their procedures to comply with the rule.[1029] Based on staff experience, the Commission estimated that it would take approximately 50 hours for an NRSRO to establish procedures in conformance with the rule.[1030] Given the specificity of paragraph (a) proposed Rule 17g–8 as well as the fact that unlike the policies and procedures required under Rule 17g–4, the policies and procedures that would be required under paragraph (a) of proposed Rule 17g–8 would not be supplementing policies and procedures that are required under a separate self-executing statutory provision (*i.e.,* the requirement would be based solely on the Commission's rule), the Commission preliminarily believes that paragraph (a) of proposed Rule 17g–8 would result in a greater hour burden for an NRSRO. For these reasons, the Commission preliminarily estimates that an NRSRO would spend an average of approximately 200 hours establishing the policies and procedures, resulting in an industry-wide one-time hour burden of approximately 2,000 hours.[1031] In addition, the Commission preliminarily estimates an NRSRO would spend an average of approximately 50 hours per year reviewing the policies and procedures and updating them (if necessary), resulting in an industry-wide annual hour burden of approximately 500 hours.[1032]

Proposed paragraph (b) of new Rule 17g–8 would implement Section 938(a) of the Dodd-Frank Act by requiring an NRSRO to have policies and procedures with respect to the symbols, numbers, or scores it uses to denote credit ratings.[1033] These policies and procedures would be used by the NRSRO to achieve the objectives specified in Sections 938(a)(1) through (3) of the Dodd-Frank Act.[1034] For the reasons stated above with respect to proposed paragraph (a) of new Rule 17g–8, the Commission estimates that an NRSRO would spend an average of approximately 200 hours establishing the policies and procedures, resulting in an industry-wide one-time hour burden of approximately 2,000 hours.[1035] In addition, the Commission preliminarily estimates an NRSRO would spend an average of approximately 50 hours per year reviewing the policies and procedures and updating them (if necessary), resulting in an industry-wide annual hour burden of approximately 500 hours.[1036]

Proposed paragraph (c) of new Rule 17g–8 would implement Section 15E(h)(4)(A)(ii) of the Exchange Act by requiring the NRSRO to establish, maintain, and enforce certain policies and procedures pursuant to Section 15E(h)(4)(A) of the Exchange Act.[1037] The Commission preliminarily believes that the hour burdens resulting from this proposal would be closer to the one-time hour burden estimate for Rule 17g–4 because these policies and procedures would supplement policies and procedures that are required under a separate self-executing statutory provision. However, the Commission also believes there would be new policies and procedures and, therefore, as with the proposed requirements in paragraphs (a) and (b) of new Rule 17g–8, the NRSRO would need to establish new policies and procedures. For these reasons, the Commission preliminarily estimates an NRSRO would spend an average of approximately 100 hours establishing the policies and procedures, resulting in an industry-wide one-time hour burden of approximately 1,000 hours.[1038] In addition, the Commission preliminarily estimates an NRSRO would spend an average of approximately 25 hours per year reviewing the policies and procedures and updating them (if necessary), resulting in an average industry-wide annual hour burden of approximately 250 hours.[1039]

For the foregoing reasons, the Commission estimates that the total industry-wide one-time hour burden to the NRSROs resulting from the proposed amendments to Rule 17g–8

paragraph (d)(3) of Rule 17g–2 is 15 hours, which would result in an adjusted industry-wide annual hour burden of 150 hours (10 NRSROs × 15 hours = 150 hours). This amount would need to be transferred to the industry-wide annual hour burden for Rule 17g–7 resulting in a total industry-wide annual hour burden of 826,038 hours (825,888 hours + 150 hours = 826,038 hours).

[1024] New Rule 17g–8, if adopted, would be codified at 17 CFR 240.17g–8.

[1025] *See* 15 U.S.C. 78o–7(r) and proposed new paragraph (a) of Rule 17g–8; *see also* Section II.F.1 of this release for a more detailed discussion of this proposal.

[1026] *See* 15 U.S.C. 78o–7(g).

[1027] *See* 17 CFR 240.17g–4; *see also Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33593–33595 (June 18, 2007).

[1028] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33610–33611 (June 18, 2007).

[1029] *Id.*

[1030] *Id.*

[1031] 10 NRSROs × 200 hours = 2,000 hours.

[1032] 10 NRSROs × 50 hours = 500 hours.

[1033] *See* Public Law 111–203 § 938(a) and proposed paragraph (b) of new Rule 17g–8; *see also* Section II.J.1 of this release for a more detailed discussion of this proposal.

[1034] *See* Public Law 111–203 §§ 938(a)(1)–(3).

[1035] 10 NRSROs × 200 hours = 2,000 hours.

[1036] 10 NRSROs × 50 hours = 500 hours.

[1037] *See* 15 U.S.C. 78o–7(h)(4)(A)(ii) and proposed new paragraph (c) of Rule 17g–8; *see also* Section II.C.1 of this release for a more detailed discussion of this proposal.

[1038] 10 NRSROs × 100 hours = 1,000 hours.

[1039] 10 NRSROs × 25 hours = 250 hours.

would be approximately 5,000 hours[1040] and the total industry-wide annual hour burden would be approximately 1,250 hours.[1041]

7. Proposed New Rule 17g–9

The Commission is proposing new Rule 17g–9.[1042] This rule would implement Section 936 of the Dodd-Frank Act by requiring an NRSRO to establish, maintain, enforce, and document standards of training, experience, and competence for the individuals it employs to determine credit ratings.[1043] As discussed below, the Commission preliminarily estimates that these proposals would result in additional one-time and annual hour burdens for NRSROs.

In this regard, the Commission preliminarily believes that several of the NRSROs already have implemented standards of training, experience, and competence for the individuals they employ to determine credit ratings. For example, Section 1.4 of the *Code of Conduct Fundamentals for Credit Rating Agencies* of the International Organization of Securities Commissions ("IOSCO Code") provides that credit rating agencies "should use people who, individually or collectively (particularly where rating committees are used) have appropriate knowledge and experience in developing a rating opinion for the type of credit being applied."[1044] A number of NRSROs disclose that they have implemented the IOSCO Code.[1045] In addition, some NRSROs disclose in the Exhibits to their Form NRSROs that they have standards of training, experience, competence, continuing education, and testing programs for their credit analysts.[1046]

As noted above, the size and complexity of the NRSROs varies greatly. The magnitude of this variance is reflected in the number of credit analysts and credit analyst supervisors each NRSRO employs (hereinafter collectively referred to as "credit analysts") as shown in Figure 3 above.[1047] For example, three NRSROs employed over 1,000 credit analysts as of calendar year-end 2009 and three NRSROs employed fewer than 30 credit analysts.

The Commission preliminarily estimates that the degree of the one-time and annual hour burdens resulting from proposed new Rule 17g–9 would depend on the number of credit analysts an NRSRO employs as well as the range and complexity of the obligors, securities, and money market instruments it rates. Consequently, the one-time and annual hour burdens per NRSRO would vary widely.

In order to account for this variance, the Commission preliminarily believes that the one-time and annual hour burden estimates should be based on the number of credit rating analysts employed by the NRSROs. Based on the 2009 annual certifications, the Commission estimates that the NRSROs currently employ approximately 3,520 credit analysts.[1048] In addition, as noted above, the Commission preliminarily believes some of the NRSROs have established standards of training, experience, and competence for their credit analysts. Consequently, for purposes of this estimate, the Commission preliminarily believes these firms would be required to augment or modify existing standards to comply with the proposed rule as opposed to developing a set of completely new standards. For these reasons, the Commission preliminarily estimates that the one-time burden to establish the standards required pursuant to proposed new Rule 17g–9 would be approximately 5 hours per credit analyst, resulting in an industry-wide one-time hour burden of approximately 17,600 hours.[1049] In addition, the Commission preliminarily allocates 75% of these burden hours (13,200 hours) to internal burden and the remaining 25% (4,400 hours) to external burden to hire outside professionals to assist in setting up training programs.[1050] The Commission preliminarily estimates $400 per hour for external costs for retaining outside consultants, resulting in an industry-wide cost of approximately $1,760,000.[1051] Although larger NRSROs may realize economies of scale, the Commission preliminarily estimates that the industry-wide annual hour burden of 17,600 hours, including the external burden costs, would be allocated to each NRSRO based on the number of credit analysts the firm employs.[1052]

The Commission believes that the annual hour burden to comply with proposed new Rule 17g–9 would be less than the one-time hour burden since NRSROs would have established the standards of training, experience, and competence for the individuals they employ to determine credit ratings. The annual hour burden would arise from reviewing and updating the standards. Consequently, the Commission preliminarily estimates that the annual industry-wide hour burden to update the standards would be approximately 1 hour per credit analyst employed, resulting in an industry-wide annual hour burden of approximately 3,520 hours across all NRSROs.[1053] In addition, the Commission preliminarily allocates 75% of these burden hours (2,640 hours) to internal burden and the remaining 25% (880 hours) to external burden to hire outside professionals to assist in reviewing and updating training programs.[1054] The Commission preliminarily estimates $400 per hour for external costs for retaining outside consultants, resulting in an industry-wide cost of $352,000.[1055] Finally,

[1040] 2,000 hours + 2,000 + 1,000 hours = 5,000 hours.

[1041] 500 hours + 500 hours + 250 hours = 1,250 hours.

[1042] Proposed new Rule 17g–9 would be codified at 17 CFR 240.17g–9, if adopted.

[1043] *See* Public Law 111–203 § 936 and proposed new Rule 17g–9; *see also* Section II.I.1 of this release for a more detailed discussion of this proposal.

[1044] *Code of Conduct Fundamentals for Credit Rating Agencies,* Technical Committee of IOSCO (May 2008).

[1045] The following NRSROs, for example, reported in Exhibit 5 to Form NRSRO that they comply with the IOSCO Code: A.M. Best Company, Inc., DBRS Ltd., Kroll Bond Rating Agency, Inc., Moody's Investors Service, Inc., Rating and Investment Information, Inc., Realpoint LLC, and Standard & Poor's Ratings Services.

[1046] For example, Fitch, Inc., Moody's Investors Service, Inc., and Standard & Poor's Ratings Services reported in Exhibit 8 to Form NRSRO that they had standards of experience and competence for their credit analysts, and Moody's Investors Service, Inc. reported in Exhibit 5 to Form NRSRO that its analysts were required to complete 20 hours of coursework annually.

[1047] These figures are based on the annual certifications on Form NRSRO submitted to the Commission and publicly disclosed by the NRSROs for the calendar year-end 2009. *See Annual Report on Nationally Recognized Statistical Rating Organizations,* Commission (Jan. 2011), p. 5.

[1048] NRSROs reported that they have a total of 3,520 credit analysts and 820 credit analyst supervisors. *See* Figure 3. As discussed above in Section II.M.4.b of this release, some NRSROs included credit analyst supervisors in the number of credit analysts they reported; whereas others may not have included the supervisors. Based on staff experience, the Commission preliminarily believes that the majority of NRSROs included credit analyst supervisors in the number of reported credit analysts. Consequently, for the purposes of the PRA, the Commission is using a total of 3,520 credit analysts across the 10 NRSROs.

[1049] 3,520 credit analysts × 5 hours = 17,600 hours.

[1050] 17,600 hours × 0.75 = 13,200 hours; 17,600 hours × 0.25 = 4,400 hours.

[1051] 4,400 hours × $400 = $1,760,000. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011) (providing an estimate of $400 an hour to engage outside professionals) and *Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63889 (Dec. 4, 2009) (providing an estimate of $400 per hour to engage an outside attorney).

[1052] *See* Figure 3.

[1053] 3,520 credit analysts × 1 hour = 3,520 hours.

[1054] 3,520 hours × 0.75 = 2,640 hours; 3,520 hours × 0.25 = 880 hours.

[1055] 880 hours × $400 = $352,000. *See Disclosure for Asset-Backed Securities Required by Section 943*

although larger NRSROs may realize economies of scale, the Commission estimates that the industry-wide annual hour burden of 3,520 hours, including the external costs, would be allocated to each NRSRO based on the number of credit analysts the firm employs.[1056]

For the foregoing reasons, the Commission estimates that proposed new Rule 17g–9 would result in a total industry-wide one-time hour burden of approximately 17,600 hours,[1057] a total industry-wide one-time cost of approximately $1,760,000, a total industry-wide annual hour burden of approximately 3,520 hours, and a total industry-wide annual external cost of approximately $352,000.

8. Proposed New Rule 17g–10 and Form ABS Due Diligence-15E

The Commission is proposing new Rule 17g–10 and new Form ABS Due Diligence-15E.[1058] Proposed new Rule 17g–10 would implement rulemaking mandated in Sections 15E(s)(4)(B) and (C) of the Exchange Act by requiring that the written certification a provider of third-party due diligence services must provide to an NRSRO be made on Form ABS Due Diligence-15E.[1059] As discussed below, the Commission preliminarily estimates that these proposals would result in additional one-time and annual hour burdens for providers of third-party due diligence services.

In terms of one-time hour burdens, the Commission preliminarily estimates that providers of third-party due diligence services would need to develop processes and protocols to provide the required information in new Form ABS Due Diligence-15E and submit the certifications to NRSROs. The Commission preliminarily estimates that providers of third-party due diligence services would spend an average of approximately 300 hours per firm developing these processes and protocols, resulting in a one-time industry-wide hour burden of 3,000 hours.[1060] In addition, the Commission preliminarily allocates 75% of these burden hours (2,250 hours) to internal burden and the remaining 25% (750 hours) to external burden to hire outside attorneys to provide legal advice on the requirements of new Rule 17g–10 and Form ABS Due Diligence-15E.[1061] The Commission preliminarily estimates $400 per hour for external costs for retaining outside consultants, resulting in an industry-wide one-time cost of $300,000.[1062]

With respect to the annual burden, the Commission preliminarily believes that the estimate should be based on the number of issuances per year of Exchange Act-ABS because the requirement to produce the certification and provide it to NRSROs would be triggered when an issuer, underwriter, or NRSRO hires a provider of third-party due diligence services for transactions.[1063] In the PRA for the adoption of Rule 17g–7, the Commission estimated, on average, there would be approximately 2,067 Exchange Act-ABS offerings per year.[1064] In addition, the Commission preliminarily estimates that a provider of third-party due diligence services would spend approximately 30 minutes completing and submitting Form ABS Due Diligence-15E. The Commission bases this preliminary estimate on the fact that the first three Items in the form require basic information and the fourth Item (the due diligence performed) and the fifth Item (the findings and conclusions of the review) could be drawn directly from the due diligence reports the Commission expects that providers of third-party due diligence services generate with respect to their performance of due diligence services. Therefore, the Commission preliminarily estimates that the industry-wide annual hour burden resulting from proposed new Rule 17g–10 and Form ABS Due Diligence-15E would be approximately 1,034 hours.[1065]

For the foregoing reasons, the Commission estimates proposed new Rule 17g–8 would result in a total industry-wide one-time burden of approximately 3,000 hours, a total industry-wide one-time cost of approximately $300,000, and a total industry-wide annual hour burden of approximately 1,034 hours.

9. Rule 15Ga–2 and Form ABS–15G

The Commission is proposing new Rule 15Ga–2 and amendments to Form ABS–15G.[1066] The new rule and amended form would implement Section 15E(s)(4)(A) of the Exchange Act.[1067] As discussed below, the Commission preliminarily estimates that these proposals would result in additional one-time and annual hour burdens for issuers and underwriters of the Exchange Act-ABS.

Proposed new Rule 15Ga–2 would require an issuer or underwriter of any Exchange Act-ABS that is to be rated by an NRSRO to furnish a Form ABS–15G on the EDGAR system containing the findings and conclusions of any third-party "due diligence report" obtained by the issuer or underwriter. Under the proposal, the disclosure would be furnished using Form ABS–15G for both registered and unregistered offerings of Exchange Act-ABS. In addition, under the Commission's proposal, an issuer or underwriter would not need to furnish Form ABS–15G if the issuer or underwriter obtains a representation

of the Dodd-Frank Wall Street Reform and Consumer Protection Act, 76 FR at 4507–4506 (Jan. 26, 2011) (providing an estimate of $400 an hour to engage outside professionals) and *Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63889 (Dec. 4, 2009) (providing an estimate of $400 per hour to engage an outside attorney).

[1056] *See* Figure 3.

[1057] 2,000 hours + 2,000 + 1,000 hours = 5,000 hours.

[1058] Proposed new Rule 17g–10 would be codified at 17 CFR 240.17g–10 and proposed new Form ABS Due Diligence-15E would be identified at 17 CFR 249b.400.

[1059] *See* 15 U.S.C. 78o–7(s)(4)(B) and (C), proposed new Rule 17g–10, and proposed new Form ABS Due Diligence-15E; *see also* Sections II.H of this release for a more detailed discussion of this proposal.

[1060] 10 Providers of third-party due diligence services × 300 hours = 3,000 hours. This estimate is based on the Commission's estimate for the amount of time it would take a securitizer to set up a system to make the disclosures required by Form ABS–15G. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011). The Commission, however, has reduced the hour estimate of 850 hours used for Form ABS–15G by approximately two-thirds because information required to be provided in proposed new Form ABS Due Diligence-15E is substantially less detailed and complex than the information required in Form ABS–15G.

[1061] 3,000 hours × 0.75 = 2,250 hours; 3,000 hours × 0.25 = 750 hours.

[1062] 750 hours × $400 = $300,000. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011) (providing an estimate of $400 an hour to engage outside professionals) and *Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63889 (Dec. 4, 2009) (providing an estimate of $400 per hour to engage an outside attorney).

[1063] *See* 15 U.S.C. 78o–7(s)(4)(B) and (C), and proposed new Rule 17g–10.

[1064] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4508 (Jan. 26, 2011). The Commission notes that issuers, underwriters, and NRSROs may not use providers of third-party due diligence services with respect to every issuance of Exchange Act-ABS. For example, as discussed in Section II.H of this release, the Commission preliminarily believes that providers of third-party due diligence services are used primarily for RMBS transactions. However, the Commission's estimate uses the total number of estimated Exchange Act-ABS offerings (as opposed to a lesser amount based on an estimate of RMBS offerings) because the use of providers of third-party due diligence services may migrate to other types of Exchange Act-ABS. This also makes the Commission's estimates more conservative.

[1065] 2,067 Exchange Act-ABS offerings × 30 minutes = 1,034 hours.

[1066] *See* proposed new Rule 15Ga–2 and proposed amendments to Form ABS–15G.

[1067] *See* 15 U.S.C. 78o–7(s)(4)(A); *see also* Section II.H.1 of this release for a more detailed discussion of this proposal.

from each NRSRO engaged to produce a credit rating for the Exchange Act-ABS that can be reasonably relied on that the NRSRO will publicly disclose the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter with the publication of the credit rating five business days prior to the first sale in the offering in an information disclosure form generated pursuant to proposed new paragraph (a)(1) of Rule 17g–7.

The Commission preliminarily believes that this proposal would result in a one-time hour burden to issuers and underwriters in offerings of registered and unregistered Exchange Act-ABS in connection with developing processes and protocols to provide the required information to comply with new Rule 15Ga–2, including modifying their existing Form ABS–15G processes and protocols to accommodate the requirements of Rule 15Ga–2. In the adopting release for Form ABS–15G, the Commission estimated that 270 unique securitizers would be required to file the form.[1068] The Commission preliminarily estimates that each securitizer would require approximately 100 hours to develop processes and protocols to comply with new Rule 15Ga–2 and to modify their existing Form ABS–15G processes and protocols to provide for the disclosure of the information required pursuant to Rule 15Ga–2, resulting in an industry-wide total of 27,000 hours.[1069] The Commission believes that this work would be done internally by issuers and underwriters.

The PRA burden assigned to Form ABS–15G reflects the cost of preparing and furnishing the form on EDGAR. As noted above, the proposed amendment to Form ABS–15G would require that it be furnished by issuers and underwriters in offerings of registered and unregistered Exchange Act-ABS. Consequently, the Commission preliminarily believes that the estimate of the annual hour burden for furnishing Form ABS–15G should be based on an estimate of the number of Exchange Act-ABS offerings per year. As noted above, in the PRA for the adoption of Rule 17g–7, the Commission estimated, on average, there would be approximately 2,067 Exchange Act-ABS offerings per year.[1070] In addition, the Commission preliminarily estimates that an issuer or underwriter would spend approximately one hour completing and submitting Form ABS–15G for purposes of meeting the requirement in Rule 15Ga–2. The Commission bases this preliminary estimate on the fact that Form ABS–15G would elicit much less information when used solely for the purpose of complying with proposed new Rule 15Ga–2. In addition, the information required in the form could be drawn directly from the due diligence reports the Commission expects providers of third-party due diligence services generate with respect to their performance of due diligence services. Therefore, the Commission preliminarily estimates that the industry-wide annual hour burden resulting from proposed new Rule 15Ga–2 and the amendments to Form ABS–15G would be approximately 2,067 hours.[1071] In addition, the Commission preliminarily believes that this work would be done internally by issuers and underwriters of Exchange Act-ABS.

To avoid duplicative disclosure, however, the Commission notes that an issuer or underwriter would not need to furnish Form ABS–15G if the issuer or underwriter obtains a representation from each NRSRO engaged to produce a credit rating for the Exchange Act-ABS that can be reasonably relied on that the NRSRO will publicly disclose the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter with the publication of the credit rating five business days prior to the first sale in the offering in an information disclosure form generated pursuant to proposed new paragraph (a)(1) of Rule 17g–7. The Commission anticipates that issuers and underwriters subject to this proposed requirement likely will seek to obtain such representations from the NRSROs engaged to produce credit ratings for Exchange Act-ABS. Consequently, the PRA burden for issuers and underwriters may be reduced substantially. However, to be conservative, the Commission preliminarily allocates the PRA burden for complying with proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G to the issuers and underwriters.

In addition, the Commission also is proposing to permit issuers of municipal Exchange Act-ABS, or underwriters in such offerings, to provide the information required by Form ABS–15G on EMMA. The Commission believes this would limit the PRA burden on issuers and underwriters of municipal Exchange Act-ABS subject to the proposed rule, as well as provide the disclosure for investors in the same location as other disclosures regarding municipal Exchange Act-ABS.

For the foregoing reasons, the Commission preliminarily estimates that proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G would result in a total industry-wide one-time hour burden of approximately 27,000 hours and a total industry-wide annual hour burden of approximately 2,067 hours.

10. Proposed Amendments to Regulation S–T

The Commission is proposing that certain Form NRSRO submissions and all Rule 17g–3 annual report submissions be submitted to the Commission using the EDGAR system. In order to implement this requirement, the Commission is proposing amendments to Rule 101 of Regulation S–T to require the electronic submission using the EDGAR system of Form NRSRO pursuant to paragraphs (e), (f), and (g) of Rule 17g–1 and the annual reports pursuant to Rule 17g–3.[1072] The Commission also is proposing to amend Rule 201 of Regulation S–T, which governs temporary hardship exemptions from electronic filing, to make this exemption unavailable for NRSRO submissions.[1073]

[1068] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4506 (Jan. 26, 2011).

[1069] 270 unique securitizers × 100 hours = 27,000 hours. This estimate is based on the Commission's estimate for the amount of time it would take a securitizer to set up a system to make the disclosures required by Form ABS–15G as originally adopted by the Commission. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011). The Commission, however, believes that the hour burden for amending existing Form ABS–15G processes and protocols will be significantly lower than the estimate of 850 hours used to initially develop those processes and protocols.

[1070] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4508 (Jan. 26, 2011). As noted above, issuers, underwriters, and NRSROs may not use providers of third-party due diligence services with respect to every issuance of Exchange Act-ABS. For example, as discussed in Section II.H of this release, the Commission preliminarily believes that providers of third-party due diligence services are used primarily for RMBS transactions. However, the Commission's estimate uses the total number of estimated Exchange Act-ABS offerings (as opposed to a lesser amount based on an estimate of RMBS offerings) because the use of providers of third-party due diligence services may migrate to other types of Exchange Act-ABS. This also makes the Commission's estimates more conservative.

[1071] 2,067 Exchange Act-ABS transactions × 1 hour = 2,067 hours.

[1072] *See* proposed amendment of Rule 101 of Regulation S–T (17 CFR 231.101); *see also* Section II.L of this release for a more detailed discussion of this proposal.

[1073] *See* proposed amendment of Rule 201 of Regulation S–T (17 CFR 231.201); *see also* Section II.L of this release for a more detailed discussion of this proposal.

The Commission is proposing new Rule 15Ga–2, which would require an issuer or underwriter of any Exchange Act-ABS that is to be rated by an NRSRO to furnish a Form ABS–15G on the EDGAR system containing the findings and conclusions of any third-party "due diligence report" obtained by the issuer or underwriter.[1074]

OMB requires the Commission to assign a burden of one hour to Regulation S–T and to indicate that the Regulation has one respondent so that the automated OMB system will be able to handle approval of the Regulation. OMB has already approved a burden of one hour for one respondent to the Regulation.

11. Form ID

The Commission expects that NRSROs would need to file a Form ID with the Commission in order to gain access to the EDGAR system. Form ID is used to request the assignment of access codes to make submissions on EDGAR. The current OMB approved hour burden for Form ID is 15 minutes per respondent.[1075] Thus, the Commission estimates that the total one-time hour burden resulting from filing Form ID would be approximately 2.5 hours.[1076]

The Commission preliminarily believes that the issuers and underwriters of Exchange Act-ABS that would need to furnish Form ABS–15G to the Commission through the EDGAR system pursuant to proposed new Rule 15Ga–2 already have access to the EDGAR system because, for example, they need such access for the purpose of Rule 15Ga–1.

12. Total Paperwork Burdens

Based on the foregoing, the Commission estimates that the total recordkeeping burden for NRSRO respondents resulting from the proposed rule amendments and proposed new rules would be approximately 77,150 industry-wide one-time hours, $7,160,000 industry-wide external one-time costs, 741,140 industry-wide annual hours, and $552,000 industry-wide external annual costs.

Based on the foregoing, the Commission estimates that the total recordkeeping burden for respondents that are providers of third-party due diligence services resulting from the rule amendments and proposed new rules would be approximately 3,000 industry-wide one-time hours, $300,000 industry-wide external one-time costs, and 1,034 industry-wide annual hours.

Based on the foregoing, the Commission estimates that the total recordkeeping burden for issuer and underwriter respondents resulting from the rule amendments and proposed new rules would be approximately 27,000 industry-wide one-time hours and 2,067 industry-wide annual hours.

E. Collection of Information Is Mandatory

The collections of information pursuant to the proposed amendments and new rules are mandatory, as applicable, for NRSROs, providers of third-party due diligence services, and issuers and underwriters.

F. Confidentiality

Other than information for which an NRSRO, provider of third-party due diligence services, or issuer or underwriter requests confidential treatment, or as may otherwise be kept confidential by the Commission, and which may be withheld from the public in accordance with the provisions of FOIA, the collection of information requirements resulting from the proposed amendments and new rules would not be confidential and would be publicly available.[1077]

G. Retention Period of Recordkeeping Requirements

All records an NRSRO is required to retain under Rule 17g–3 (including records that would need to be made or received by an NRSRO under the proposed amendments and new rules) must be retained for three years after the record is made or retained.[1078]

The Dodd-Frank Act did not establish record retention requirements for providers of third-party due diligence services.

The records issuers and underwriters are required to make and furnish to the Commission pursuant to the requirements in proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G would be mandatory. Responses to the information collections will not be kept confidential and there is no mandatory retention period for the collections of information.

H. Request for Comment

Pursuant to 44 U.S.C. 3505(c)(2)(B), the Commission solicits comment to:

1. Evaluate whether the proposed collection of information requirements are necessary for the performance of the functions of the Commission, including whether the information shall have practical utility;

2. Evaluate the accuracy of the Commission's estimates of the burden of the proposed collection of information requirements;

3. Determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and

4. Minimize the burden of the collection of information requirements on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

Persons wishing to submit comments on the collection of information requirements should direct them to the following persons: (1) Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, OMB, Room 3208, New Executive Office Building, Washington, DC 20503; and (2) Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE., Washington, DC 20549–1090 with reference to File No. S7–18–11. OMB is required to make a decision concerning the collection of information between 30 and 60 days after publication, so a comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication. The Commission has submitted the proposed collection of information to OMB for approval. Requests for the materials submitted to OMB by the Commission with regard to this collection of information should be in writing, refer to File No. S7–18–11, and be submitted to the Securities and Exchange Commission, Office of Investor Education and Advocacy, Station Place, 100 F Street, NE., Washington, DC 20549–0213.

V. Economic Analysis

The Commission is sensitive to the costs imposed by its rules. To the extent possible, the discussion below focuses on the benefits and costs of the decisions made by the Commission to fulfill the mandates of the Dodd-Frank Act within its permitted discretion, rather than the benefits and costs of the mandates of the Dodd-Frank Act itself. However, as discussed below, to the extent that the Commission exercises discretion in implementing the provisions of the Dodd-Frank Act, the benefits and costs arising from the Commission's exercise of its discretion and the benefits and costs arising directly from the requirements of the Dodd-Frank Act are not entirely separable. Accordingly, where the

[1074] *See* proposed new Rule 15Ga–2 and proposed amendments to Form ABS–15G; *see also* Section II.H.1 of this release for a more detailed discussion of this proposal.

[1075] *See* Form ID (OMB Number 3235–0328).

[1076] 10 NRSROs × 15 minutes = 150 minutes; 150 minutes/60 minutes = 2.5 hours.

[1077] *See* 15 U.S.C. 552 *et seq.*

[1078] *See* 17 CFR 240.17g–2(a), (b), and (c).

Commission believes that it has exercised some discretion in implementing the Dodd-Frank Act, hour burden estimates and dollar cost estimates in the above PRA analysis are included in full below, even where a portion—in most cases, the significantly greater portion—of the anticipated costs are attributable to the rulemaking mandates of the Dodd-Frank Act and not the exercise of the Commission's discretion in how to implement those requirements.[1079] Where the Commission believes, however, that it has not exercised discretion in implementing the rulemaking mandates of the Dodd-Frank Act and that any anticipated benefits and costs are *entirely* attributable to those mandates, those anticipated benefits and costs are not addressed in the discussion below. Finally, as used below, the term "incremental costs" refers to costs attributable to the exercise of the Commission's rulemaking discretion that are in addition to costs attributable to the rulemaking mandates of the Dodd-Frank Act.

In addition, the Commission notes that Section 3(f) of the Exchange Act requires the Commission, whenever it engages in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action would promote efficiency, competition, and capital formation.[1080] Furthermore, Section 23(a)(2) of the Exchange Act requires the Commission, when issuing rules under the Exchange Act, to consider the impact such rules would have on competition.[1081] 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.[1082] The Commission's analysis under these requirements as applied to the proposed amendments to existing rules and proposed new rules is included below in the discussions of the benefits and the costs of the proposals where appropriate. In this regard, the Commission's analysis focuses on the discretionary component of the Commission's proposals and the incremental costs resulting from that discretion.

Unless otherwise noted, the total one-time and annual cost estimates per NRSRO for PRA purposes as used in this section are averages across all types of NRSROs that would be subject to the proposed amendments and new rules. The NRSROs vary, in terms of size and complexity, from small entities that employ less than 20 credit analysts to complex global organizations that employ over a thousand credit analysts.[1083] Given the variance in size between the largest NRSROs and the smallest NRSROs, the cost estimates, as averages across all NRSROs, are skewed higher because the largest firms currently dominate in terms of size and the volume of credit rating activities.[1084]

The Commission's estimates of the benefits and costs of the proposals, as well as the anticipated effects on efficiency, competition and capital formation, are described below. The Commission recognizes that there may be benefits and costs resulting from the proposals that are not required to be described or otherwise identified below. The Commission generally requests that commenters identify and describe any such benefits and costs.

A. Internal Control Structure

Section 932(a)(2)(B) of the Dodd-Frank Act added paragraph (3) to Section 15E(c) of the Exchange Act.[1085] Section 15E(c)(3)(A) requires an NRSRO to "establish, maintain, enforce, and document an effective internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings, taking into consideration such factors as the Commission may prescribe by rule."[1086] Section 15E(c)(3)(B) of the Exchange Act provides that the Commission shall prescribe rules requiring an NRSRO to submit an annual internal controls report to the Commission, which shall contain: (1) A description of the responsibility of management in establishing and maintaining an effective internal control structure; (2) an assessment of the effectiveness of the internal control structure; and (3) the attestation of the CEO or equivalent individual.[1087] The Commission proposes to implement this rulemaking by: (1) Adding a new paragraph (b)(12) to Rule 17g–2;[1088] and (2) amending paragraphs (a) and (b) of Rule 17g–3.[1089]

Proposed new paragraph (b)(12) of Rule 17g–2 would identify the internal control structure an NRSRO, among other things, must document pursuant to Section 15E(c)(3)(A) of the Exchange Act as a record that must be retained.[1090] As a result, the various retention and production requirements of paragraphs (c), (d), (e), and (f) of Rule 17g–2 in its current form would apply to the documented internal control structure.[1091]

Proposed new paragraph (a)(7) of Rule 17g–3 would require an NRSRO to include with the other reports required under that rule a report regarding the NRSRO's internal control structure established pursuant to Section 15E(c)(3)(A) of the Exchange Act.[1092] The proposed amendment would mirror the text of Section 15E(c)(3)(B) of the Exchange Act by requiring that the report contain: (1) A description of the responsibility of management in establishing and maintaining an effective internal control structure; and (2) an assessment by management of the effectiveness of the internal control structure.[1093] The Commission's proposed amendment to paragraph (b) of Rule 17g–3 would require that the NRSRO's CEO, or, if the firm does not have a CEO, an individual performing similar functions, provide a signed statement that would need to be attached to the report.[1094] The CEO or other individual would need to state, among other things, that the report fairly presents, in all material respects, a description of the responsibility of management in establishing and

[1079] For purposes of this economic analysis, the Commission's salary figures are from SIFMA's Management & Professional Earnings in the Securities Industry 2010, modified by Commission staff to account for an 1800-hour work year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead.

[1080] *See* 15 U.S.C. 78c(f).

[1081] *See* 15 U.S.C. 78w(a)(2).

[1082] *See id.*

[1083] *See, e.g., Annual Report on Nationally Recognized Statistical Rating Organizations. Commission* (January 2011), pp. 4–9.

[1084] As discussed above in Section IV.D of this release, based on data collected from the NRSROs in their Form NRSROs and Rule 17g–3 annual reports, the Commission has calculated an HHI number using the number credit ratings outstanding per NRSRO and that number is 3,495, which is equivalent to there being approximately 2.86 equally sized firms. The HHI using earnings reported by NRSROs in the Rule 17g–3 annual reports is 3,926, which the equivalent of 2.55 equally sized firms.

[1085] *See* Public Law 111–203 § 932(a)(2)(B) and 15 U.S.C. 78o–7(c)(3)(A); *see also* Section II.A.1 of this release for a more detailed discussion of this provision.

[1086] *Id.*

[1087] *See* 15 U.S.C. 78o–7(c)(3)(B)(i)–(iii).

[1088] *See* proposed new paragraph (b)(12) to Rule 17g–2; *see also* Section II.A.2 of this release for a more detailed discussion of this proposal.

[1089] *See* proposed new paragraphs (a)(7) and of Rule 17g–3; *see also* Section II.A.3 of this release for a for a more detailed discussion of these proposals.

[1090] *See* proposed new paragraph (b)(12) of Rule 17g–2.

[1091] *See* 17 CFR 240.17g–2(c), (d), (e) and (f).

[1092] *See* proposed new paragraph (a)(7) of Rule 17g–3.

[1093] *Compare* 15 U.S.C. 78o–7(c)(3)(B)(i) and (ii) and proposed new paragraphs (a)(7)(i) and (ii) of Rule 17g–3.

[1094] *See* proposed amendments to paragraph (b) of Rule 17g–3.

maintaining an effective internal control structure and an assessment of the effectiveness of the internal control structure.

1. Benefits

Section 15E(c)(3)(A) of the Exchange Act requires an NRSRO to establish, maintain, enforce, and document an effective internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings.[1095] The Commission proposes to further implement this provision by applying the record retention and production requirements of Rule 17g–2 to the documented internal control structure by adding new paragraph (b)(12).[1096] Recordkeeping rules such as Rule 17g–2 have proven integral to the Commission's investor protection function because the preserved records are the primary means of monitoring compliance with applicable securities laws.[1097] Rule 17g–2 is designed to ensure that an NRSRO makes and retains records that will assist the Commission in monitoring, through its examination authority, whether an NRSRO is complying with applicable securities laws, including the provisions of Section 15E of the Exchange Act and the rules thereunder.[1098] The proposed amendment to Rule 17g–2 is designed to assist the Commission in monitoring an NRSRO's compliance with the requirement in Section 15E(c)(3)(A) of the Exchange Act to establish, maintain, enforce, and document an effective internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings.

The Commission preliminarily believes that implementing the internal control structure reporting requirement through an amendment to Rule 17g–3 would facilitate the Commission's oversight of NRSROs. First, it would assist the Commission in monitoring an NRSRO's compliance with the requirement in Section 15E(c)(3)(A) of the Exchange Act to establish, maintain, enforce, and document an effective internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings. Second, it would specify the format, manner, and timeframe in which the report must be submitted to the Commission, thereby facilitating the Commission's processing of the report. Furthermore, the Commission preliminarily believes that proposed amendments to Rules 17g–2 and 17g–3 would provide an efficient process for NRSROs by allowing them to file the internal control report with the other annual reports required under Rule 17g–3.

2. Costs

The Commission preliminarily estimates that, although the costs resulting from the proposed amendment to Rule 17g–2, discussed below, would largely be attributable to the Commission's discretionary rulemaking, those incremental costs would be minimal. An NRSRO already should have recordkeeping and control systems in place to comply with the existing requirements in Rule 17g–2 to make and retain or to retain documents listed in the rule.

The Commission preliminarily estimates that the Commission's exercise of rulemaking discretion with respect to the amendments to Rule 17g–3 would also impose minimal incremental costs. The Commission preliminarily estimates that the costs resulting from the proposed amendments to Rule 17g–3 would largely be attributable to the rulemaking mandated by the Dodd-Frank Act.[1099]

An NRSRO already should have control systems in place to comply with the existing requirements of Rule 17g–3. Consequently, the Commission preliminarily estimates that the internal hour burden associated with the first filing of the internal control report would not be materially different than the hour burden associated with filing subsequent reports (though the time spent on subsequent reports may decrease incrementally over time as the NRSRO gains experience with the requirement). The Commission, however, preliminarily believes that an NRSRO likely would engage outside counsel to analyze the requirements for the report and assist in drafting and reviewing the first report, given that it must be signed by the NRSRO's CEO or an individual performing a similar function. The time an outside attorney would spend on this work would depend on the size and complexity of the NRSRO.

In addition, as discussed above in Section IV.D.4 of this release with respect to the PRA, the Commission preliminarily believes an NRSRO likely would continue to engage outside counsel to assist in the process of preparing the report on an annual basis and that the time an outside attorney would spend on this work would depend on the size and complexity of the NRSRO but in all cases be less than time spent on the first report.

In sum, limiting the analysis to the elements of the proposals over which the Commission exercised discretion, the Commission acknowledges that the proposals would entail some compliance burdens for NRSROs. Some of the compliance effects are estimated for the industry in Sections Section IV.D.3 and Section IV.D.4 as $600,000 for the use of outside counsel and 1,550 internal burden hours for creating and retaining documents and complying with management's assessment of the internal control structure. However, the Commission preliminarily believes these compliance effects would result largely from the rulemaking mandated by the Dodd-Frank Act rather than the Commission's exercise of discretion.

The Commission preliminarily believes that the incremental cost resulting from the proposed amendments would not impact competition or impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with proposed new paragraph (b)(12) of Rule 17g–2 and proposed new paragraphs (a)(7) and (b)(2) of Rule 17g–3.

B. Conflicts of Interest Relating to Sales and Marketing

Section 932(a)(4) of the Dodd-Frank Act added new paragraph (3) to Section 15E(h) of the Exchange Act.[1100] Section 15E(h)(3)(A) of the Exchange Act provides that the Commission shall issue rules to prevent the sales and marketing considerations of an NRSRO from influencing the production of credit ratings by the NRSRO.[1101] The Commission is proposing to implement this provision by identifying a new conflict of interest in paragraph (c) of Rule 17g–5.[1102] The existing requirements in paragraph (c) prohibit a person within an NRSRO (which

[1095] *See* 15 U.S.C. 78o–7(c)(3)(A).

[1096] *See* 17 CFR 240.17g–2(c), (d), (e) and (f).

[1097] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33582 (June 18, 2007).

[1098] *Id.*

[1099] *Compare* 15 U.S.C. 78o–7(c)(3)(B)(i) and (ii) with proposed new paragraphs (a)(7)(i), (a)(7)(ii), and (b)(2) of Rule 17g–3.

[1100] Public Law 111–203 § 932(a)(4) and 15 U.S.C. 78o–7(h)(3).

[1101] 15 U.S.C. 78o–7(h)(3)(A).

[1102] *See* proposed new paragraph (c)(8) of Rule 17g–5; *see also* Section II.B.1 of this release for a more detailed discussion of this proposal.

includes the NRSRO)[1103] from having any of the conflicts of interest identified in the paragraph under all circumstances.[1104] Proposed new paragraph (c)(8) of Rule 17g–5 would identify a new absolute prohibition: an NRSRO issuing or maintaining a credit rating where a person within the NRSRO who participates in the sales or marketing of a product or service of the NRSRO or a product or service of a person associated with the NRSRO also participates in determining or monitoring the credit rating or developing or approving procedures or methodologies used for determining the credit rating, including qualitative or quantitative models.[1105]

Section 15E(h)(3)(B) of the Exchange Act provides that the Commission's rules must contain two additional provisions.[1106] First, Section 15E(h)(3)(B)(i) requires that the Commission's rules shall provide for exceptions for small NRSROs with respect to which the Commission determines that the separation of the production of ratings and sales and marketing activities is not appropriate.[1107] To implement this provision, the Commission is proposing to amend Rule 17g–5 by adding a new paragraph (f).[1108] Proposed paragraph (f) would provide a mechanism for a small NRSRO to apply in writing for an exemption from the absolute prohibition proposed in new paragraph (c)(8). In particular, proposed new paragraph (f) of Rule 17g–5 would provide that upon written application by an NRSRO, the Commission may exempt, either conditionally or unconditionally or on specified terms and conditions, such NRSRO from the provisions of paragraph (c)(8) of Rule 17g–5 if the Commission finds that due to the small size of the NRSRO it is not appropriate to require the separation within the NRSRO of the production of credit ratings from sales and marketing activities and such exemption is in the public interest.[1109]

Second, Section 15E(h)(3)(B)(ii) requires that the Commission's rules shall provide for the suspension or revocation of the registration of an NRSRO if the Commission finds, on the record, after notice and opportunity for a hearing, that the NRSRO has committed a violation of a rule issued under Section 15E(h) of the Exchange Act; and (2) the violation affected a rating.[1110] The Commission proposes to implement this provision by adding new paragraph (g) of Rule 17g–5.[1111] This paragraph would provide that in a proceeding pursuant to Section 15E(d) or Section 21C of the Exchange Act, the Commission shall suspend or revoke the registration of an NRSRO if the Commission finds in such proceeding that the NRSRO has violated a rule issued under Section 15E(h) of the Exchange Act, the violation affected a rating, and that suspension or revocation is necessary for the protection of investors and in the public interest.

1. Benefits

The Commission preliminarily believes that the proposed new absolute prohibition in proposed paragraph (c)(8) of Rule 17g–5 would provide benefits to investors by mitigating the potential that undue influences based on sales and marketing considerations could impact the objectivity of the NRSRO's credit rating process.[1112] As discussed above in Section II.B.1 of this release, Commission staff found as part of its 2007–2008 examination of the activities of the three largest NRSROs in rating asset-backed securities linked to subprime mortgages that it appeared that marketing personnel discussed with other employees, including those responsible for credit rating criteria development, business concerns they had related to those criteria.[1113] The rule proposal would be designed to insulate individuals within the NRSRO responsible for determining credit ratings from such pressures. In addition, the bright line on prohibited behavior is likely to allow the company to effectively comply with the proposed rules. The Commission believes that this could benefit investors by increasing the integrity of credit ratings and the procedures and methodologies used to determine credit ratings.

With respect to the proposal for the suspension or revocation of the registration of an NRSRO after a violation of a rule, the Commission preliminarily believes that it would provide the Commission with more flexibility in determining appropriate sanctions for violations of the securities laws. This could act as a deterrent against violations by NRSROs and could motivate them to strengthen their internal controls to manage conflicts of interest.

The Commission preliminarily believes that codifying these requirements mandated by the Dodd-Frank Act in Rule 17g–5 may promote efficiency. NRSROs should already have developed a system of controls to comply with the existing requirements relating to conflicts of interest that are codified in Rule 17g–5. In addition, the Commission believes proposed paragraph (g) may promote efficiency by incorporating existing processes for sanctioning NRSROs (*i.e.,* those provided for Sections 15E(d) or Section 21C of the Exchange Act).

2. Costs

The Commission preliminarily estimates that the Commission's exercise of rulemaking discretion with respect to the proposed amendments to Rule 17g–5 would impose minimal incremental costs. However, the Commission preliminarily estimates that the costs discussed below resulting from the proposed amendments to Rule 17g–5 would be attributable largely to the rulemaking mandated by Dodd-Frank Act.[1114]

The Commission notes that, when it adopted three new absolutely prohibited conflicts by amending paragraph (c) of Rule 17g–5 in 2009, the Commission provided estimates of one-time and annual compliance costs for NRSROs resulting from the amendments.[1115] Moreover, one of those amendments resulted in an absolute prohibition that is similar to the Commission's proposed new absolute prohibition in that it prohibits an NRSRO from issuing or maintaining a credit rating where the fee paid for the rating was negotiated, discussed, or arranged by a person within the NRSRO who has responsibility for participating in determining credit ratings or for

[1103] *See* paragraph (d) of Rule 17g–5 defining "person within an NRSRO" for purposes of the rule. 17 CFR 240.17g–5(d).

[1104] *See* 17 CFR 240.17g–5(c)(1)–(7).

[1105] *See* proposed new paragraph (c)(8) of Rule 17g–5.

[1106] 15 U.S.C. 78o–7(h)(3)(B)(i) and (ii).

[1107] 15 U.S.C. 78o–7(h)(3)(B)(i).

[1108] *See* proposed new paragraph (f) of Rule 17g–5; *see also* Section II.B.2 of this release for a more detailed discussion of this proposal.

[1109] *See* proposed new paragraph (f) of Rule 17g–5.

[1110] 15 U.S.C. 78o–7(h)(3)(B)(ii).

[1111] *See* proposed new paragraph (g) of Rule 17g–5; *see also* Section II.B.3 of this release for a more detailed discussion of this proposal.

[1112] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33598–33599, 33613 (June 18, 2007) (discussing objectives and benefits of paragraph (c) of Rule 17g–5 when it was adopted); *see also Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6465–6469, 6474–6475 (February 9, 2009) (discussing objectives and benefits of paragraph (c) of Rule 17g–5 when it was amended).

[1113] *See Summary Report of Issues Identified in the Commission Staff's Examination of Select Credit Rating Agencies,* Commission (July 2008), pp. 25–26.

[1114] *Compare* 15 U.S.C. 78o–7(h)(3)(A), (B)(i), and (B)(ii) with proposed new paragraphs (c)(8), (f), and (g) of Rule 17g–5.

[1115] *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6479 (February 9, 2009).

developing or approving procedures or methodologies used for determining credit ratings, including qualitative and quantitative models.[1116] With respect to the 2009 amendments, the Commission estimated that the costs to the three largest NRSROs as a result of the three new prohibited conflicts would be approximately $5,442,100 per firm in one-time costs and $1,563,800 per firm in annual costs.[1117] In addition, the Commission estimated that the costs to the seven smaller NRSROs would be approximately $47,600 per firm in one-time costs and $13,760 per firm in annual costs.[1118] The Commission preliminarily believes that the compliance cost for the new absolute prohibition proposed in this release would be proportionally less than the estimates provided above for the three 2009 prohibitions. The Commission also preliminarily believes that granting an exemption from the proposed new absolute prohibition for a small NRSRO that applied in writing for such exemption could reduce potential costs for a smaller NRSRO for which the complete separation of sales and marketing activities from the analytical function would not be appropriate.

The Commission therefore preliminarily believes any incremental cost resulting from the amendments would not impact competition or impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with proposed new paragraphs (c)(8), (f), and (g) of Rule 17g–5.

C. "Look-Back" Review

Section 932(a)(4) of the Dodd-Frank Act amended Section 15E(h) of the Exchange Act to add a new paragraph (4).[1119] The Commission is proposing to implement the rulemaking required in Section 15E(h)(4)(A)(ii) of the Exchange Act through proposed paragraph (c) of new Rule 17g–8.[1120] Proposed paragraph (c) would require that the policies and procedures the NRSRO establishes, maintains, and enforces pursuant to Section 15E(h)(4)(A) of the Exchange Act must address instances in which a review conducted pursuant to those policies and procedures determines that a conflict of interest influenced a credit rating assigned to an obligor, security, or money market instrument by including, at a minimum, procedures that are reasonably designed to ensure the NRSRO will: (1) Immediately place the credit rating on credit watch; (2) promptly determine whether the credit rating must be revised so it no longer is influenced by a conflict of interest and is solely the product of the NRSRO's documented procedures and methodologies for determining credit ratings; and (3) promptly publish a revised credit rating, if appropriate, or affirm the credit rating if appropriate.[1121]

In addition, the Commission proposes adding paragraph (a)(9) to Rule 17g–2 to identify the policies and procedures an NRSRO is required to establish, maintain, and enforce pursuant to Section 15E(h)(4)(A) of the Exchange Act and proposed paragraph (c) of new Rule 17g–8 as a record an NRSRO must make and retain.[1122] As a result, the policies and procedures would need to be documented in writing and subject to the record retention and production requirements in paragraphs (c) through (f) of Rule 17g–2.[1123]

1. Benefits

The Commission preliminarily believes that the proposed look-back review provisions would provide three primary benefits. First, they would implement the rulemaking mandate in a way that would require an NRSRO to notify users of its credit ratings that a prior rating action was subject to a conflict and to review whether the credit rating should be revised. This would help ensure as quickly as possible that the credit rating assigned to the obligor, security, or money market instrument is solely a product of the NRSRO's procedures and methodologies for determining credit ratings. In addition, by prescribing the steps an NRSRO must take to remove the uncertainty surrounding the credit rating, the rule proposal could limit the potential that investors and other users of credit ratings might make investment or other credit based decisions based on incomplete, biased or inaccurate information.

Second, the Commission preliminarily believes that the proposal could operate within the existing framework of an NRSRO's policies and procedures for taking rating actions and procedures and methodologies for determining credit ratings. Placing a rated obligor, security, or money market instrument on credit watch and subsequently affirming or revising (*i.e.,* upgrading or downgrading the rating) are among the rating actions NRSRO's commonly take with respect to their credit ratings. In addition, in terms of revising the conflicted credit rating, the proposal would rely on an NRSRO's policies and procedures for determining credit ratings and not require revisions that are contrary to those policies and procedures. The Commission preliminarily believes that the approach in proposed paragraph (c) of new Rule 17g–8 appropriately avoids regulating the substance of credit ratings or the procedures and methodologies an NRSRO uses to determine credit ratings but, at the same time, requires an NRSRO to have procedures reasonably designed to ensure that it promptly addresses a credit rating that is subject to a conflict of interest.[1124]

Third, the Commission preliminarily believes that having these policies and procedures in writing would promote better understanding of them among the individuals within the NRSRO and, therefore, promote compliance with the policies and procedures. In addition, the record retention requirements would facilitate Commission oversight of NRSROs. In this regard, recordkeeping rules such as Rule 17g–2 have proven

[1116] *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6479 (February 9, 2009) and 17 CFR 240.17g–5(c)(6).

[1117] *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6479 (February 9, 2009).

[1118] *Id.*

[1119] *See* Public Law 111–203 § 932(a)(4) and 15 U.S.C. 78o–7(h)(4).

[1120] *See* proposed paragraph (c) of new Rule 17g–8; *see also* Section II.C.1 of this release for a more detailed discussion of this proposal. Sections 15E(h)(4)(A)(i) and (ii) of the Exchange Act require an NRSRO to establish, maintain, and enforce policies and procedures reasonably designed to ensure that, in any case in which an employee of a person subject to a credit rating of the NRSRO or the issuer, underwriter, or sponsor of a security or money market instrument subject to a credit rating of the NRSRO, was employed by the NRSRO and participated in any capacity in determining credit ratings for the person or the securities or money market instruments during the 1-year period preceding the date an action was taken with respect to the credit rating, the NRSRO shall: (1) Conduct a review to determine whether any conflicts of interest of the employee influenced the credit rating; and (2) take action to revise the rating if appropriate, in accordance with such rules as the Commission shall prescribe. *See* 15 U.S.C. 78o–7(h)(4)(A)(i) and (ii).

[1121] *See* proposed paragraphs (c)(1), (2) and (3) of new Rule 17g–8.

[1122] *See* proposed new paragraph (a)(9) to Rule 17g–2; *see also* Section II.C.2 of this release for a more detailed discussion of this proposal.

[1123] *See* 17 CFR 240.17g–2(c)–(f).

[1124] The Commission also notes an NRSRO would violate Section 15E(h) of the Exchange Act (15 U.S.C. 78o–7(h)) and Rule 17g–5, among other rules, if it continued to assign an obligor, security, or money, market instrument a credit rating that, absent the undue influence of the conflict of interest, would be different because the NRSRO could not be deemed to have policies and procedures reasonably designed to address and manage conflicts of interest that can arise from its business under such a circumstance. *See* 15 U.S.C. 78o–7(h) and 17 CFR 17g–5.

integral to the Commission's investor protection function because the preserved records are the primary means of monitoring compliance with applicable securities laws.[1125]

The Commission preliminarily believes that the proposed implementation of Section 15E(h)(4)(A)(ii) of the Exchange Act as mandated by the Dodd-Frank Act may promote efficiency. As noted above, the proposal would be designed to work within the existing processes NRSROs have for taking rating actions and would not interfere with their procedures and methodologies for determining credit ratings.

2. Costs

The Commission preliminarily estimates that the Commission's exercise of rulemaking discretion with respect to proposed paragraph (c) of new Rule 17g–8 would impose minimal incremental costs. The Commission preliminarily estimates that the costs resulting from proposed paragraph (c) of new Rule 17g–8 would be attributable largely to the rulemaking mandated by Dodd-Frank Act.[1126] As discussed above in Section IV.D.6, the Commission preliminarily estimates that for PRA purposes, the average annual cost to each NRSRO would be approximately $7,000, resulting in an industry-wide annual cost of approximately $70,000.[1127]

The Commission preliminarily estimates that the costs resulting from the proposed amendment to Rule 17g–2 discussed below largely would be attributable to the Commission's discretionary rulemaking. As discussed above in Section IV.D.3 of this release with respect to the PRA, the Commission preliminary believes applying the recordkeeping requirements of Rule 17g–2 to five new types of records would result in one-time and annual hour burdens for NRSROs in connection with updating their record retention policies and procedures to account for and retain these new records. Also, as discussed above in Section IV.D.3 of this release with respect to the PRA, based on staff experience, the Commission preliminarily estimates that the additional one-time hour burden for each NRSRO to update its record retention policies and procedures to account for the new records that would need to be retained under proposed new paragraphs (a)(9), (b)(12), (b)(13), (b)(14), and (b)(15) of Rule 17g–2 would be 20 hours. Based on that estimate, the Commission preliminary believes that the one-time hour burden resulting from proposed new paragraph (a)(9) of Rule 17g–2 would be approximately 4 hours per NRSRO, resulting in an industry-wide hour burden of approximately 40 hours.[1128] As discussed above in Section IV.D.3 of this release with respect to the PRA, the Commission preliminarily estimates it would take an average of approximately one hour each year for an NRSRO to retain updated versions of the internal control structure, resulting in an annual industry-wide hour burden of 10 hours.[1129]

The Commission believes that in addition to the compliance costs calculated above for PRA purposes, there could be other potential economic effects resulting from the proposed release that are hard to quantify. For example, former subscribers, who bought on the basis of the original rating but who no longer subscribe to the rating service, would not be notified when a rating has been revised.

For the foregoing reasons, the Commission preliminarily believes any incremental cost resulting from the amendments would not impact competition or impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with proposed paragraph (c) of new Rule 17g–8 and proposed new paragraph (a)(9) of Rule 17g–2.

D. Fines and Other Penalties

Section 932(a)(8) of the Dodd-Frank Act amended Section 15E of the Exchange Act to add new subsection (p), which contains four paragraphs: (1), (2), (3), and (4).[1130] Section 15E(p)(4)(A) provides that the Commission shall establish, by rule, fines and other penalties applicable to any NRSRO that violates the requirements of Section 15E of the Exchange Act and the rules under the Exchange Act.[1131] The Commission proposes to amend the instructions to Form NRSRO by adding new Instruction A.10.[1132] This new instruction would provide notice to credit rating agencies applying for registration and NRSROs that an NRSRO is subject to the fine and penalty provisions, and other available sanctions contained in Sections 15E, 21, 21A, 21B, 21C, and 32 of the Exchange Act for violations of the securities laws.[1133]

1. Benefits

The Commission preliminarily believes this amendment to Form NRSRO would benefit credit rating agencies applying for registration as NRSROs and NRSROs because it would notify them of the potential consequences of violating provisions of the Exchange Act and Commission rules. The Commission also believes that this notification could potentially cause the NRSROs to enhance their compliance and compliance procedures, which would benefit investors and other users of credit ratings. In addition, the Commission believes implementing the rule in this manner would create efficiencies by relying on existing authority to seek fines, penalties, and other available sanctions contained in Sections 15E, 21, 21A, 21B, 21C, and 32 of the Exchange Act for violations of the securities laws.[1134]

2. Costs

The Commission preliminarily estimates that the proposed amendment to the instructions to Form NRSRO would not result in additional regulatory obligations for NRSROs. Consequently, the Commission preliminarily believes it would not impact competition or impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

Request for Comment

The Commission requests comment on all aspects of the benefits and costs associated with the proposal to amend the instructions to Form NRSRO by adding new Instruction A.10.

E. Proposed Enhancements to Disclosures of Performance Statistics

Section 932(a)(8) of the Dodd-Frank Act amended Section 15E of the Exchange Act to add new subsection (q), which contains paragraphs (1) and (2).[1135] Section 15E(q)(1) provides that

[1125] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33582 (June 18, 2007).

[1126] *Compare* 15 U.S.C. 78o–7(h)(4)(A) with proposed paragraph (c) of new Rule 17g–8.

[1128] 20 hours/5 new required records = 4 hours; 10 NRSROs × 4 hours = 40 hours.

[1129] 10 NRSROs × 1 hour = 10 hours.

[1130] *See* Public Law 111–203 § 932(a)(8) and 15 U.S.C. 78o–7(p)(1)–(4).

[1131] *See* 15 U.S.C. 78o–7(p)(4)(A).

[1132] *See* proposed new Instruction A.10 to Form NRSRO; *see also* Section II.D of this release for a more detailed discussion of this proposal.

[1133] *See* 15 U.S.C. 78o–7, 15 U.S.C. 78u, 15 U.S.C. 78u–1, 15 U.S.C. 78u–2, 15 U.S.C. 78u–3 and 15 U.S.C. 78ff, respectively.

[1134] *Id.*

[1135] *See* Public Law 111–203 § 932(a)(8) and 15 U.S.C. 78o–7(q)(1) and (2).

the Commission shall, by rule, require each NRSRO to publicly disclose information on the initial credit ratings determined by the NRSRO for each type of obligor, security, and money market instrument, and any subsequent changes to such credit ratings, for the purpose of allowing users of credit ratings to evaluate the accuracy of ratings and compare the performance of ratings by different NRSROs.[1136] Section 15E(q)(2) provides that the Commission's rules shall require, at a minimum, disclosures that, among other things: (1) Are comparable among NRSROs, to allow users of credit ratings to compare the performance of credit ratings across NRSROs;[1137] (2) are clear and informative for investors having a wide range of sophistication who use or might use credit ratings;[1138] (3) include performance information over a range of years and for a variety of types of credit ratings, including for credit ratings withdrawn by the NRSRO;[1139] and (4) are appropriate to the business model of an NRSRO.[1140]

The Commission proposes to implement the rulemaking mandated in Section 15E(q) of the Exchange Act, in part, by significantly enhancing the requirements applicable to NRSROs with respect to generating and disclosing performance statistics in Exhibit 1 of Form NRSRO.[1141] Among other things, the amendments would confine the disclosures in the Exhibit to transition and default rates and certain limited supplemental information.[1142] Moreover, the amendments would standardize the production and presentation of the transition and default rates.[1143] Specifically, the amendments would require the transition and default rates in Exhibit 1 to be produced using a "single cohort approach."[1144] Under this approach, an applicant and NRSRO, on an annual basis, would be required to compute how the credit ratings assigned to obligors, securities, and money market instruments in a particular class or subclass of credit rating outstanding on the date 1, 3, and 10 years prior to the most recent calendar year-end performed during those respective 1, 3, and 10-year time periods.[1145]

Under the amendments, the proposed new instructions would be divided into paragraphs (1), (2), (3), and (4), some of which would have subparagraphs.[1146] The proposed new paragraphs would contain specific instructions with respect to, among other things, how required information should be presented in the Exhibit (including the order of presentation) and how transition and default rates should be produced using a single cohort approach.[1147] As with all information that must be submitted in Form NRSRO and its Exhibits, applicants *and* NRSROs would be subject to these new requirements.[1148]

The Commission also is proposing implementing Section 15E(q)(2)(D) of the Exchange Act, which requires that the Commission's rules must require NRSROs to make its performance statistics freely available and disclose them on an easily accessible portion of its Web site, and in writing when requested, by amending paragraph (i) of Rule 17g–1.[1149] The amendment would require an NRSRO to make Form NRSRO and Exhibits 1 through 9 "freely available on an easily accessible portion of its Web site." The proposed amendment to paragraph (i) also would remove the option for an NRSRO to make its Form NRSRO publicly available "through another comparable, readily accessible means" as an alternative to Web site disclosure.

1. Benefits

Section 15E(q)(1) of the Exchange Act provides that the Commission shall, by rule, require each NRSRO to publicly disclose information on the initial credit ratings determined by the NRSRO for each type of obligor, security, and money market instrument, and any subsequent changes to such credit ratings, for the purpose of allowing users of credit ratings to evaluate the accuracy of ratings and compare the performance of ratings by different NRSROs.[1150] The Commission is proposing to implement this rulemaking mandate, in part, through amendments to the instructions for Exhibit 1 to Form NRSRO. The amendments would be designed to meet the goal in Section 15E(q)(1) that the information disclosed by NRSROs allows users of credit ratings to evaluate the accuracy of credit ratings and compare the performance of credit ratings by different NRSROs. In this regard, the amendments are designed to make disclosures simply presented, easy to understand, uniform in appearance, and comparable across NRSROs.[1151]

As the Commission stated when originally adopting Form NRSRO, the information provided in Exhibit 1 is an important indicator of the performance of an NRSRO in terms of its ability to assess the creditworthiness of issuers and obligors and, consequently, will be useful to users of credit ratings in evaluating an NRSRO.[1152] The performance statistics required to be disclosed in Exhibit 1 of Form NRSRO were designed to allow users of the credit ratings to compare the credit ratings quality of different NRSROs and, thereby, make it easier for users of credit ratings to compare the ratings performance of the NRSROs. The performance statistics also were designed to allow an NRSRO to demonstrate that it has a superior ratings methodology or competence and, thereby, attract clients. In doing so, the Commission believed, the performance statistics would therefore enhance competition in the credit ratings industry.[1153] The proposed amendments to the instructions to Exhibit 1 of Form NRSRO are designed to improve the utility of the required performance statistics disclosure to investors and other users of credit ratings and facilitate comparisons between

[1136] *See* 15 U.S.C. 78o–7(q)(1).

[1137] *See* 15 U.S.C. 78o–7(q)(2)(A).

[1138] *See* 15 U.S.C. 78o–7(q)(2)(B).

[1139] *See* 15 U.S.C. 78o–7(q)(2)(C).

[1140] *See* 15 U.S.C. 78o–7(q)(2)(E).

[1141] *See* proposed amendments to Instruction H to Form NRSRO (as it relates to Exhibit 1); *see also* Section II.E.1.a of this release for a more detailed discussion of this proposal.

[1142] *See* proposed amendments to the instructions for Exhibit 1.

[1143] *Id.*

[1144] *Id.*

[1145] *Id.*

[1146] *See* proposed paragraphs (1)–(4) of the instructions for Exhibit 1.

[1147] *Id.*

[1148] *See, e.g.,* 17 CFR 240.17g–1; *see also* Instructions A.1, B, C, D, E, and F to Form NRSRO.

[1149] A detailed discussion of this proposal is at Section II.E.1.b of this release.

[1150] 15 U.S.C. 78o–7(q)(1).

[1151] *See* Section 15E(q)(2)(A) of the Exchange Act, which provides that the disclosure of information about the performance of credit ratings should be comparable among NRSROs, to allow users of credit ratings to compare the performance of credit ratings across NRSROs. 15 U.S.C. 78o–7(q)(2)(A). *See also* Section 15E(q)(2)(B) of the Exchange Act, which provides that the disclosure of information about the performance of credit ratings should be clear and informative for investors having a wide range of sophistication who use or might use credit ratings. 15 U.S.C. 78o–7(q)(2)(B).

[1152] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33574 (June 18, 2007); *see also Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6474 (Feb. 9, 2009) ("The amendments to the instructions to Exhibit 1 to Form NRSRO will require NRSROs to provide more detailed performance statistics and, thereby, make it easier for users of credit ratings to compare the performance of the NRSROs. In addition, these amendments will make it easier for an NRSRO to demonstrate that it has a superior ratings methodology or competence and, thereby, attract clients.").

[1153] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33612 (June 18, 2007); *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6474 (Feb. 9, 2009).

NRSROs, thereby amplifying this positive effect on competition.

In addition, the proposed amendments could improve the Commission's ability to carry out its oversight function for NRSRO which, in turn, would benefit investors. For example, the enhanced utility of the performance statistics provided in an applicant's initial application for registration and in an NRSRO's Form NRSRO could aid the Commission in, among other things, assessing whether the applicant or NRSRO has adequate financial and managerial resources to consistently produce credit ratings with integrity.[1154] Furthermore, the disclosure of the enhanced performance statistics in an applicant's initial application would allow the Commission staff to verify that the applicant, if granted registration, would publicly disclose the information in accordance with the proposed amendments to the Instructions for Exhibit 1.[1155]

In addition, the Commission preliminarily believes that applying the requirement to disclose Form NRSRO and Exhibits 1 through 9 on an "easily accessible" portion of the NRSRO's Web site would assist investors and other users of credit ratings by making it easier to locate a Form NRSRO. The Commission also believes that amending paragraph (i) to provide that Exhibit 1 be made freely available in writing when requested[1156] would benefit those investors who do not have access to the Internet.

The Commission preliminarily believes that enhancing the existing requirements in Exhibit 1 to Form NRSRO is an efficient means of implementing the rulemaking mandated through Section 15E(q) of the Exchange Act. An NRSRO already should have in place information technology systems to meet the existing requirements of the instructions for Exhibit 1 to Form NRSRO, which it could adjust to comply with the proposed new disclosure requirements.

2. Costs

The Commission preliminarily estimates that the Commission's exercise of rulemaking discretion in proposing amendments to the instructions for Exhibit 1 of Form NRSRO would impose incremental costs. The Commission preliminarily estimates, however, that the costs discussed below would be attributable largely to the rulemaking mandated by the Dodd-Frank Act[1157] and that the incremental costs would be minimal.

An NRSRO should already have in place information technology systems to meet the existing requirements of the instructions to Exhibit 1 of Form NRSRO, which it could adjust to comply with the proposed new disclosure requirements. NRSROs are already subject to substantial performance statistic disclosure requirements, including the requirement to provide transition and default rates in Exhibit 1 for each class of credit rating for which they are registered and for 1, 3, and 10-year periods. The Commission preliminarily believes that NRSROs could use the internal information technology systems and expertise and other resources they currently devote to processing the information necessary to monitor credit ratings and calculate transitions and default statistics in order to program a system to comply with the proposed amendments to the Instructions for Exhibit 1.

At the same time, the Commission notes that under the proposed amendments, NRSROs would be required to adhere to specific requirements that may not follow their traditional practices for calculating and presenting transitions and default rates. Consequently, the Commission preliminarily estimates that the proposed amendments requiring standardized Transition/Default Matrices would result in one-time costs to program existing systems to create the Transition/Default Matrices that would be required under the proposed amendments and annual costs to comply with the requirement to update the transition and default rates in Exhibit 1.

As discussed above in Section IV.D.2, the Commission preliminarily believes that the one-time and annual hour burden estimates for implementing these changes should be based on the number of credit ratings outstanding. Based on the annual certifications submitted by the NRSROs for the 2009 calendar year-end, there were approximately 2,905,824 credit ratings outstanding across all 10 NRSROs.[1158] The Commission preliminarily estimates that the one-time industry-wide burden to establish systems to process the relevant information necessary to calculate the Transition/Default Matrices and make the necessary calculations would be an average of approximately 3 seconds per outstanding credit rating, resulting in a one-time industry-wide hour burden of approximately 2,420 hours.[1159]

The Commission preliminarily believes that the annual hours burden to comply with the proposed amendments to the Instructions for Exhibit 1 would be less than the one-time burden since the NRSROs would have established systems to process the necessary information to produce the required Transition/Default Matrices. As discussed above in Section IV.D.2 of this release with respect to the PRA, the Commission preliminarily estimates that the annual industry-wide hour burden to calculate the Transition/Default Matrices would be an average of approximately 1.5 seconds per outstanding credit rating, resulting in an industry-wide annual hour burden of approximately 1,210 hours.[1160]

As discussed above in Section IV.D.1 of this release with respect to the PRA, the Commission preliminarily estimates that there would be a minimal one-time hour burden attributable to requiring that an NRSRO make Form NRSRO and Exhibits 1 through 9 freely available on an easily accessible portion of its corporate Internet Web site and removing the option for an NRSRO to make its Form NRSRO and Exhibits 1 through 9 available through another comparable, readily accessible means. Currently, all NRSROs make Form NRSRO and Exhibits 1 through 9 available on their corporate Internet Web sites.[1161] However, the Commission preliminarily believes that

[1154] *See, e.g.,* 15 U.S.C. 78o–7(a)(2)(C) (setting forth grounds to deny an initial application) and 15 U.S.C. 78o–7(d)(1)(E) and (d)(2) (setting forth grounds to sanction an NRSRO, including revoking the NRSRO's registration); *see also Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33612 (June 18, 2007) ("Form NRSRO requires that a credit rating agency provide information required under Section 15E(a)(1)(B) of the Exchange Act and certain additional information. The additional information will assist the Commission in making the assessment regarding financial and managerial resources required under Section 15E(a)(2)(C)(2)(ii)(I) of the Exchange Act.").

[1155] As indicated above, paragraph (i) requires an NRSRO to make Form NRSRO and Exhibits 1 through 9 publicly available within 10 business days of being granted an initial registration. *See* 17 CFR 240.17g–1(i). In addition, the public disclosure of Form NRSRO and Exhibits 1 through 9 could be accelerated if the Commission adopts the proposal that this information be filed through the EDGAR system upon registration.

[1156] *See* proposed amendments to paragraph (i) of Rule 17g–1.

[1157] *Compare* 15 U.S.C. 78o–7(q) with the proposed amendments to the instructions for Exhibit 1 to Form NRSRO; *see also* GAO Report 10–782, pp. 27–40 (indicating the current requirements for disclosing performance statistics in Exhibit 1 to Form NRSRO may not achieve the objectives of 15 U.S.C. 78o–7(q)).

[1158] *Id.*

[1159] 2,905,824 credit ratings × 3 seconds = 2,421.52 hours (rounded to 2,420 hours).

[1160] 2,905,824 credit ratings × 1.5 seconds = 1,210.76 hours (rounded to 1,210 hours).

[1161] *See, e.g., Annual Report on Nationally Recognized Statistical Rating Organizations. Commission* (Jan. 2011), pp. 18–19.

a Form NRSRO and Exhibits 1 through 9 would be "easily accessible" if they could be accessed through a clearly and prominently labeled hyperlink on the home page of the NRSRO's corporate Internet Web site. Consequently, NRSROs may need to make changes to their corporate Internet Web sites to disclose the information on an "easily accessible" portion of the Web site. The Commission preliminarily estimates re-configuring a corporate Internet Web site for this purpose would take an NRSRO an average of approximately 5 hours. For these reasons, the Commission preliminarily estimates that the proposed requirement would result in an average one-time hour burden of 5 hours per NRSRO, resulting in a one-time industry-wide hour burden of 50 hours.[1162]

Also as discussed in Section IV.D.1 with respect to the PRA, the Commission expects that the proposed requirement that an NRSRO provide a written copy of Exhibit 1 on request would result in a one-time hour burden for each NRSRO to establish procedures and protocols for receiving and processing these requests. The Commission preliminarily estimates that each NRSRO would spend an average of approximately 48 hours establishing such procedures and protocols, resulting in an industry-wide one-time hour burden of approximately 480 hours.[1163]

Also as discussed in Section IV.D.1 with respect to the PRA, the Commission preliminarily estimates that an NRSRO would receive an average of 200 requests per year to provide Exhibit 1 in writing and that it would take an average of 20 minutes to respond to each request. Therefore, the Commission preliminarily estimates that the average annual hour burden to each NRSRO would be approximately 67 hours, resulting in an annual industry-wide burden of approximately 670 hours. [1164]

In addition, the Commission preliminarily estimates that the incremental cost resulting from implementing the rulemaking mandated by Section 15E(q) of the Exchange Act in this manner would be minimal and, as noted above, the proposal would have substantial benefits. Consequently, the Commission preliminarily believes any incremental cost resulting from the amendments would not impact competition or impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

Request for Comment

The Commission requests comment on all aspects of the benefits and costs associated with the proposals to amend the Instructions to Exhibit 1 of Form NRSRO and paragraph (i) of Rule 17g–1.

F. Proposed Enhancements to Rating Histories Disclosures

As discussed above, Section 932(a)(8) of the Dodd-Frank Act amended Section 15E of the Exchange Act to add new subsection (q), which contains paragraphs (1) and (2).[1165] In addition to the proposed amendments to the Instructions for Exhibit 1 discussed in the preceding section, the Commission proposes to further implement the rulemaking mandated in Section 15E(q) of the Exchange Act, in part, by adding new paragraph (b) to Rule 17g–7.[1166] This proposed amendment would implement rulemaking mandated in Section 15E(q) of the Exchange Act by: (1) Re-codifying in paragraph (b) of Rule 17g–7 requirements currently contained in paragraph (d)(3) of Rule 17g–2; and (2) substantially enhancing those requirements.[1167] More specifically, paragraph (d)(3) of Rule 17g–2 requires an NRSRO to, among other things, make publicly available on its corporate Internet Web site in an XBRL format the information required to be documented pursuant to paragraph (a)(8) of the rule with respect to any credit rating initially determined by the NRSRO on or after June 26, 2007, the effective date of the Rating Agency Act of 2006.[1168]

These requirements would be enhanced in four ways. The first enhancement would make the disclosure easier for investors and other users of credit ratings to locate. Specifically, new proposed paragraph (b)(1) of Rule 17g–7 would require the NRSRO, among other things, to publicly disclose the ratings history information for free on an *easily accessible portion* of its corporate Internet Web site.[1169]

The second enhancement would broaden the scope of credit ratings subject to the disclosure requirements. Specifically, proposed new paragraph (b)(1)(i) of Rule 17g–7 would require an NRSRO to disclose each credit rating assigned to an obligor, security, and money market instrument in every class of credit ratings for which the NRSRO is registered that was *outstanding* as of June 26, 2007 and any subsequent upgrades or downgrades of a credit rating assigned to the obligor, security, or money market instrument (including a downgrade to, or assignment of, default), any placements of a credit rating assigned to the obligor, security, or money market instrument on watch or review, any affirmation of a credit rating assigned to the obligor, security, or money market instrument, and a withdrawal of a credit rating assigned to the obligor, security, or money market instrument.[1170] With respect to credit ratings initially determined on or after June 26, 2007, the amendments would clarify that the disclosure of the rating history information would be triggered when an NRSRO publishes an initial credit rating, and any subsequent upgrades or downgrades of a credit rating assigned to the obligor, security, or money market instrument (including a downgrade to, or assignment of, default), any placements of a credit rating assigned to the obligor, security, or money market instrument on watch or review, any affirmation of a credit rating assigned to the obligor, security, or money market instrument, and a withdrawal of a credit rating assigned to the obligor, security, or money market instrument.[1171]

The third enhancement would increase the scope of information that must be disclosed about a rating action. Specifically, proposed paragraph (b)(2) of Rule 17g–7 would identify 7 categories of data that would need to be disclosed when a credit rating action is published pursuant to proposed new paragraph (b)(1) of Rule 17g–7.[1172] The fourth enhancement, contained in proposed new paragraph (b)(5) to Rule 17g–7, would be to require that a rating history not be removed from the disclosure until 20 years after the NRSRO withdraws the credit rating

[1162] 10 NRSROs × 5 hours = 50 hours.

[1163] 10 NRSROs × 48 hours = 480 hours.

[1164] 200 requests × ⅓ hours = 67 hours per NRSRO; 10 NRSROs × 67 hours = 670 hours.

[1165] *See* Public Law 111–203 § 932(a)(8) and 15 U.S.C. 78o–7(q)(1) and (2). *See* Section

[1166] *See* proposed new paragraph (b) of Rule 17g–7; *see also* Section II.E.2 of this release for a more detailed discussion of this proposal.

[1167] *See* 15 U.S.C. 78o–7(q) and proposed new paragraph (b) of Rule 17g–7; *see also* Section II.E.2 of this release for a more detailed discussion of this proposal.

[1168] 17 CFR 240.17–2(d)(3)(i)(A). Paragraph (a)(8) of Rule 17g–2 requires an NRSRO to make and retain a record that, "for each outstanding credit rating, shows all rating actions and the date of such actions from the initial credit rating to the current credit rating identified by the name of the rated security or obligor and, if applicable, the CUSIP of the rated security or the Central Index Key ("CIK") number of the rated obligor." 17 CFR 240.17–2(a)(8).

[1169] *See* proposed new paragraph (b)(1) of Rule 17g–7.

[1170] *See* proposed new paragraph (b)(1)(i) of Rule 17g–7.

[1171] *See* proposed new paragraph (b)(1)(ii) of Rule 17g–7.

[1172] *See* proposed new paragraph (b)(2) of Rule 17g–7.

assigned to the obligor, security, or money market instrument.[1173]

1. Benefits

Section 15E(q)(1) of the Exchange Act provides that the Commission shall, by rule, require each NRSRO to publicly disclose information on the initial credit ratings determined by the NRSRO for each type of obligor, security, and money market instrument, and any subsequent changes to such credit ratings, for the purpose of allowing users of credit ratings to evaluate the accuracy of ratings and compare the performance of ratings by different NRSROs.[1174] The Commission is proposing to implement this rulemaking mandate, in part, through proposed new paragraph (b) of Rule 17g–7. The amendments would be designed to meet the goal in Section 15E(q)(1) that the information disclosed by NRSROs allows users of credit ratings to evaluate the accuracy of credit ratings and compare the performance of credit ratings by different NRSROs.

As the Commission stated when adopting the current ratings history disclosure requirement, the "intent of the rule is to facilitate comparisons of credit rating accuracy across all NRSROs—including direct comparisons of different NRSROs' treatment of the same obligor or instrument—in order to enhance NRSRO accountability, transparency, and competition." [1175] The proposals also are designed to provide persons with the "raw data" necessary to generate statistical information about the performance of each NRSRO's credit ratings.[1176] Finally, the proposals also are designed to implement provisions of Section 15E(q)(2) of the Exchange Act, which provides, among other things, that the Commission's rules shall require NRSROs to disclose information about the performance of credit ratings that is comparable among NRSROs, to allow users of credit ratings to compare the performance of credit ratings across NRSROs.[1177]

The Commission preliminarily believes that implementing the rulemaking mandated through Section 15E(q) of the Exchange Act through proposed new paragraph (b) of Rule 17g–7 would promote an efficient process for NRSROs. An NRSRO already should have in place information technology systems to meet the existing requirements of paragraph (d)(3) of Rule 17g–2, which it could adjust to comply with the proposed new disclosure requirements.

2. Costs

The Commission preliminarily estimates that the Commission's exercise of rulemaking discretion in proposing new paragraph (b) of Rule 17g–7 would impose incremental costs. However, the Commission preliminarily estimates that the costs discussed below resulting from the proposed new paragraph would be attributable largely to the rulemaking mandated by Dodd-Frank Act [1178] and that the incremental costs would be minimal.

The Commission preliminarily believes that requiring an NRSRO to make ratings histories available on an "easily accessible" portion of its Web site would result in the same burden as re-configuring a corporate Internet Web site for the purpose of making Form NRSRO and Exhibits 1 through 9 "easily accessible." The Commission, therefore, preliminarily believes that the hour burden estimates discussed above in Section V.F.2 of this release with respect to the PRA would be appropriate for estimating the costs resulting from this requirement. Consequently, the Commission preliminarily estimates that requiring an NRSRO to make ratings histories available on an "easily accessible" portion of its corporate Internet Web site would take each NRSRO an average of approximately 5 hours, resulting in a one-time industry-wide hour burden of 50 hours.[1179]

Pursuant to paragraph (d)(3) of Rule 17g–2, NRSROs currently are required to provide ratings history information for each credit rating initially determined on or after June 26, 2007. Proposed new paragraph (b) of Rule 17g–7 would incorporate the requirements currently contained in paragraph (d)(3) of Rule 17g–2 with substantial enhancements that would require NRSROs to add more ratings histories to their disclosures and provide more information about each rating action in the ratings history for each given obligor, security, or money market instrument.[1180] The Commission preliminarily estimates that NRSROs would meet the requirements of new paragraph (b) of Rule 17g–7 by adapting the internal information technology systems and expertise and other resources they currently devote to complying with paragraph (d)(3) of Rule 17g–2, which would result in one-time costs to NRSROs. Consequently, the Commission preliminarily estimates that the proposed amendments would result in one-time costs to reprogram existing systems as well as to add the required information for all credit ratings outstanding as of (as opposed to initially determined on or after) June 26, 2007. As discussed in section IV.D.5 of this release with respect to the PRA, the Commission preliminarily estimates that the proposed enhancements to the current disclosure requirements would result in an average one-time hour burden to each NRSRO of approximately 135 hours, resulting in an industry-wide one-time hour burden of approximately 1,350 hours.[1181] The Commission preliminarily believes that NRSROs would implement the required changes internally.

In addition, as discussed in section IV.D.5 of this release with respect to the PRA, the Commission preliminarily estimates that the proposed enhanced disclosure requirements would result in an average annual hour burden per NRSRO of approximately 45 hours, resulting in an industry-wide annual hour burden of approximately 450 hours.[1182]

Finally, the Commission preliminarily believes any incremental cost resulting from the amendments would not impact competition or impose a burden on

[1173] *See* proposed new paragraph (b)(5) of Rule 17g–7.

[1174] 15 U.S.C. 78o–7(q)(1).

[1175] *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63838 (Dec. 4, 2009) ("Ratings history information for outstanding credit ratings is the most direct means of comparing the performance of two or more NRSROs. It allows an investor or other user of credit ratings to compare how all NRSROs that maintain a credit rating for a particular obligor or instrument initially rated that obligor or instrument and, thereafter, how and when they adjusted their credit rating over time."). The Commission notes that under the proposals the disclosures would not contain complete histories for many credit ratings because the NRSRO would not need to include information about rating actions taken before June 26, 2007. However, the Commission believes that the disclosures would still be used to compare how different NRSROs rated a particular obligor, security, or money market instrument beginning as of June 26, 2007 and from that date forward.

[1176] *See Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63837–63838 (Dec. 4, 2009) ("The raw data to be provided by NRSROs pursuant to the new ratings history disclosure requirements * * * will enable market participants to develop performance measurement statistics that would supplement those required to be published by NRSROs themselves in Exhibit 1, tapping into the expertise of credit market observers and participants in order to create better and more useful means to compare the credit ratings performance of NRSROs.").

[1177] *See* 15 U.S.C. 78o–7(q)(2).

[1178] *Compare* 15 U.S.C. 78o–7(q) with proposed new paragraph (b) of Rule 17g–7; *see also* GAO Report 10–782, pp. 40–46 (indicating the current requirements of paragraph (d)(3) of Rule 17g–2 may not achieve the objectives of 15 U.S.C. 78o–7(q)).

[1179] 10 NRSROs × 5 hours = 50 hours.

[1180] *See* proposed new paragraph (b) of Rule 17g–7; *see also* Section II.E.2 of this release for a more detailed discussion of this proposal.

[1181] 10 NRSRO × 135 hours = 1,350 hours.

[1182] 10 NRSRO × 45 hours = 450 hours.

competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

Request for Comment

The Commission requests comment on all aspects of the benefits and costs associated with proposed new paragraph (b) of Rule 17g–7.

G. Credit Rating Methodologies

Section 932(a)(8) of the Dodd-Frank Act amends Section 15E of the Exchange Act to add new subsection (r).[1183] Section 15E(r) of the Exchange Act provides that the Commission shall prescribe rules, for the protection of investors and in the public interest, with respect to the procedures and methodologies, including qualitative and quantitative data and models, used by NRSROs that require each NRSRO to ensure a number of objectives.[1184] The Commission is proposing to implement Section 15E(r) of the Exchange Act through paragraph (a) of proposed new Rule 17g–8.[1185]

In particular, proposed paragraph (a)(1) would require the NRSRO to have policies and procedures that are reasonably designed to ensure that the procedures and methodologies, including qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are approved by its board of directors or, if the NRSRO does not have a board of directors, another body performing a function similar to that of a board of directors.[1186] Proposed paragraph (a)(2) would require an NRSRO to have policies and procedures that are reasonably designed to ensure that the procedures and methodologies, including qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are developed and modified in accordance with the policies and procedures of the NRSRO.[1187] Proposed paragraph (a)(3)(i) would require an NRSRO to have policies and procedures that are reasonably designed to ensure that material changes to the procedures and methodologies, including changes to qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are applied consistently to all credit ratings to which the changed procedures or methodologies apply.[1188] Proposed paragraph (a)(3)(ii) would require the NRSRO to have policies and procedures that are reasonably designed to ensure that material changes to the procedures and methodologies, including changes to qualitative and quantitative data and models, the NRSRO uses to determine credit ratings, to the extent that the changes are to surveillance or monitoring procedures and methodologies, are applied to then-current credit ratings within a reasonable period of time taking into consideration the number of ratings impacted, the complexity of the procedures and methodologies used to determine the credit ratings, and the type of obligor, security, or money market instrument being rated.[1189] Proposed paragraph (a)(4)(i) would require the NRSRO to have policies and procedures that are reasonably designed to ensure that the NRSRO promptly publishes on an easily accessible portion of its corporate Internet Web site material changes to the procedures and methodologies, including to qualitative models or quantitative inputs, the NRSRO uses to determine credit ratings, the reason for the changes, and the likelihood the changes will result in changes to any current ratings.[1190] Proposed paragraph (a)(4)(ii) would require the NRSRO to have policies and procedures that are reasonably designed to ensure the NRSRO promptly publishes on its corporate Internet Web site significant errors identified in a procedure or methodology, including a qualitative or quantitative model, the NRSRO uses to determine credit ratings that may result in a change in current credit ratings.[1191] Finally, proposed paragraph (a)(5) would require the NRSRO to have policies and procedures that are reasonably designed to ensure that it discloses the version of a credit rating procedure or methodology, including the qualitative methodology or quantitative inputs, used with respect to a particular credit rating.[1192]

The Commission also is proposing that the policies and procedures required pursuant to proposed paragraph (a) of new Rule 17g–8 be subject to the record retention and production requirements of Rule 17g–2.[1193] Consequently, the Commission proposes adding new paragraph (b)(13) to Rule 17g–2 to identify the policies and procedures an NRSRO is required to establish, maintain, enforce, and document pursuant to proposed paragraph (a) of new Rule 17g–8 as a record that must be retained.[1194]

1. Benefits

The Commission is proposing to implement Sections 15E(r) of the Exchange Act through paragraph (a) of proposed new Rule 17g–8. The Commission preliminarily believes that the proposals would provide several primary benefits for investors and other users of credit ratings. First, having the NRSRO's board of directors or a body performing a function similar to a board approve the NRSRO's procedures and methodologies for determining credit ratings could promote the quality and consistency of the procedures and methodologies.[1195] In addition, taking steps to ensure that such procedures and methodologies are developed and modified pursuant to the NRSRO's policies and procedures also could promote the quality and consistency of the procedures and methodologies.[1196]

Furthermore, taking steps to ensure that material changes to the procedures and methodologies, including changes to qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are applied consistently to all credit ratings to which the changed procedures or methodologies apply could promote consistent and timely application of such changes, which could benefit investors and other users of credit ratings.[1197] Similarly, the consistent and timely application of changes to procedures and methodologies for determining credit ratings could be promoted by an NRSRO taking steps to ensure that material changes to the procedures and methodologies, including changes to qualitative and quantitative data and models, the NRSRO uses to determine credit ratings are, to the extent that the changes are to surveillance or monitoring procedures and methodologies, applied to then-current credit ratings within a reasonable period of time taking into consideration the number of ratings impacted, the

[1183] *See* Public Law 111–203 § 932(a)(8) and 15 U.S.C. 78o–7(r).

[1184] *See* 15 U.S.C. 78o–7(r)(1)–(3).

[1185] *See* proposed paragraph (a) of new Rule 17g–8; *see also* Section II.F.1 of this release for a more detailed discussion of this proposal.

[1186] *See* proposed paragraph (a)(1) of new Rule 17g–8.

[1187] *See* proposed paragraph (a)(2) of new Rule 17g–8.

[1188] *See* proposed paragraph (a)(3)(i) of new Rule 17g–8.

[1189] *See* proposed paragraph (a)(3)(ii) of new Rule 17g–8.

[1190] *See* proposed paragraph (a)(4)(i) of new Rule 17g–8.

[1191] *See* proposed paragraph (a)(4)(ii) of new Rule 17g–8.

[1192] *See* proposed paragraph (a)(5) of new Rule 17g–8.

[1193] 17 CFR 240.17g–2.

[1194] *See* proposed new paragraph (b)(13) to Rule 17g–2; *see also* Section II.F.2 of this release for a more detailed discussion of this proposal.

[1195] *See* proposed paragraph (a)(1) of new Rule 17g–8.

[1196] *See* proposed paragraph (a)(2) of new Rule 17g–8.

[1197] *See* proposed paragraph (a)(3)(i) of new Rule 17g–8.

complexity of the procedures and methodologies used to determine the credit ratings, and the type of obligor, security, or money market instrument being rated.[1198]

In addition, the Commission preliminarily believes the proposal would benefit investors and other users of credit ratings by improving the transparency of an NRSRO's procedures and methodologies for determining credit ratings. Specifically, investors and other users of credit ratings would benefit from the transparency arising from requiring that an NRSRO promptly publishes on an easily accessible portion of its corporate Internet Web site material changes to the procedures and methodologies, including to qualitative models or quantitative inputs, the reason for the changes, and the likelihood the changes will result in changes to any current ratings as well as significant errors identified in a procedure or methodology, including a qualitative or quantitative model.[1199] Finally, transparency also would be promoted by requiring that an NRSRO disclose the version of a credit rating procedure or methodology, including the qualitative methodology or quantitative inputs, used with respect to a particular credit rating.[1200]

The Commission preliminarily believes that an additional benefit of the proposal is that implementing Section 15E(r) of the Exchange Act by requiring the NRSRO to have policies and procedures designed to achieve the objectives set forth in that section would provide the NRSRO with flexibility to integrate the required policies and procedure with its procedures and methodologies for determining credit ratings. In other words, the proposal would rely on the NRSRO's policies and procedures for determining credit ratings and not require revisions that are contrary to those policies and procedures. The Commission preliminarily believes this approach appropriately avoids regulating the substance of credit ratings or the procedures and methodologies an NRSRO uses to determine credit ratings but, at the same time, requires an NRSRO to have procedures reasonably designed to achieve the objectives set forth in Section 15E(r) of the Exchange Act.

The Commission preliminarily believes this proposed implementation of Section 15E(r) of the Exchange Act would promote an efficient process for NRSROs to comply with the requirements. As noted above, the proposal would be designed to provide the NRSRO with flexibility to integrate the required policies and procedure with its procedures and methodologies for determining credit ratings.

The Commission proposes to further implement Section 15E(r) of the Exchange Act by adding new paragraph (b)(13) to Rule 17g–2 to apply the record retention and production requirements of Rule 17g–2 to the policies and procedures required pursuant to paragraph (a) of proposed new Rule 17g–8.[1201] The record retention requirements would promote efficiency by facilitating Commission oversight of NRSROs. In this regard, recordkeeping rules such as Rule 17g–2 have proven integral to the Commission's investor protection function because the preserved records are the primary means of monitoring compliance with applicable securities laws.[1202] Rule 17g–2 is designed to ensure that an NRSRO makes and retains records that will assist the Commission in monitoring, through its examination authority, whether an NRSRO is complying with the provisions of Section 15E of the Exchange Act and the rules thereunder.[1203] The proposed amendment to Rule 17g–2 is designed to assist the Commission in monitoring an NRSRO's compliance with paragraph (a) of proposed new Rule 17g–8.

2. Costs

The Commission preliminarily estimates that the Commission's exercise of rulemaking discretion in proposed paragraph (a) of new Rule 17g–8 would impose incremental costs. However, the Commission preliminarily estimates that the costs discussed below resulting from proposed paragraph (a) of new Rule 17g–8 would be attributable largely to the rulemaking mandated by Dodd-Frank Act [1204] and that the incremental costs would be minimal.

As discussed in Section IV.D.6 of this release with respect to the PRA, the Commission preliminarily estimates that an NRSRO would spend an average of approximately 200 hours establishing the policies and procedures that would be required under paragraph (a) of proposed new Rule 17g–8, resulting in an industry-wide one-time hour burden of approximately 2,000 hours.[1205] In addition, as discussed in Section IV.D.6 of this release with respect to the PRA, the Commission preliminarily estimates an NRSRO would spend an average of approximately 50 hours annually reviewing and updating the policies and procedures required under proposed paragraph (a) of Rule 17g–8, resulting in an annual industry-wide hour burden of approximately 500 hours.[1206]

As noted above, the Commission preliminarily estimates that the costs resulting from proposed new paragraph (b)(13) of new Rule 17g–2 largely would be attributable to the Commission's discretionary rulemaking. As discussed above in Section IV.D.3 of this release with respect to the PRA, the Commission preliminary believes applying the recordkeeping requirements of Rule 17g–2 to five new types of records would result in one-time and annual hour burdens for NRSROs in connection with updating their record retention policies and procedures to account for and retain these new records. As discussed above in Section IV.D.3 of this release with respect to the PRA, based on staff experience, the Commission preliminarily estimates that the additional one-time hour burden for each NRSRO to update its record retention policies and procedures to account for the new records that would need to be retained under proposed new paragraphs (a)(9), (b)(12), (b)(13), (b)(14), and (b)(15) of Rule 17g–2 would be 20 hours. Based on that estimate, the Commission preliminary believes that the average one-time hour burden resulting from proposed new paragraph (b)(13) to Rule 17g–2 would be approximately 4 hours per NRSRO, resulting an industry-wide one-time hour burden of approximately 40 hours.[1207] As discussed above in Section IV.D.3 of this release with respect to the PRA, the Commission preliminarily estimates it would take an average of approximately one hour each year for an NRSRO to retain updated versions of the information required pursuant to paragraph (a) of new Rule 17g–8 resulting in an annual industry-wide burden of 10 hours.[1208]

For the foregoing reasons, Commission preliminarily believes any incremental cost resulting from the amendments would not impact competition or impose a burden on

[1198] *See* proposed paragraph (a)(3)(ii) of new Rule 17g–8.

[1199] *See* proposed paragraph (a)(4) of new Rule 17g–8.

[1200] *See* proposed paragraph (a)(5) of new Rule 17g–8.

[1201] *See* 17 CFR 240.17g–2(a), (c), (d), (e) and (f).

[1202] *See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR at 33582 (June 18, 2007).

[1203] *Id.*

[1204] *Compare* 15 U.S.C. 78o–7(r)(1)–(3), *with* proposed paragraph (a) of new Rule 17g–8.

[1205] 10 NRSROs × 200 hours = 2,000 hours.

[1206] 10 NRSROs × 50 hours = 500 hours.

[1207] 20 hours/5 new required records = 4 hours; 10 NRSROs × 4 hours = 40 hours.

[1208] 10 NRSROs × 1 hour = 10 hours.

competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with proposed new paragraph (a)(8) of Rule 17g–8 and proposed new paragraph (b)(13) of Rule 17g–2.

H. Form and Certification to Accompany Credit Ratings

Section 932(a)(8) of the Dodd-Frank Act amended Section 15E of the Exchange Act to add new paragraph (s).[1209] Sections 15E(s)(1) through (4), among other things, set forth provisions specifying Commission rulemaking with respect to disclosures an NRSRO must make with the publication of a credit rating.[1210] The Commission proposes to implement these provisions by adding new paragraph (a) to Rule 17g–7.[1211] As discussed in detail below, the prefatory text of proposed new paragraph (a) would require an NRSRO to publish two items when taking a rating action: (1) A form containing information about the credit rating resulting from or subject to the rating action; [1212] and (2) any certification of a provider of third-party due diligence services received by the NRSRO that relates to the credit rating.[1213] Proposed paragraph (a)(1) of Rule 17g–7 would contain three primary components: Paragraph (a)(1)(i) prescribing the format of the form; [1214] paragraph (a)(1)(ii) prescribing the content of the form; [1215] and paragraph (a)(1)(iii) prescribing an attestation requirement for the form.[1216] Proposed paragraph (a)(2) of Rule 17g–7 would identify the certification from a provider of third-party due diligence services as an item to be published with the rating action.[1217]

1. Benefits

The Commission preliminarily believes that the proposed implementation of the rulemaking mandated by Sections 15E(s)(1), (2), (3), and (4)(D) through disclosure requirements in proposed new paragraph (a) of Rule 17g–7 could be used by investors and other users of credit ratings to better understand credit ratings in each class of credit rating issued by the NRSRO and to determine the adequacy and level of due diligence services provided by a third party with respect to an issuance of Exchange Act-ABS.[1218] As the Commission has noted previously, the NRSRO credit ratings of structured finance products such as Exchange Act-ABS played a role in the recent credit crisis.[1219] The proposed information to be disclosed in the form, including information about the limitations of credit ratings and information regarding the due diligence performed on Exchange Act-ABS, could promote more prudent use of credit ratings by investors and other users of credit ratings, and discourage undue reliance by investors and other users of credit ratings in making investment and other credit based decisions.

The Commission preliminarily believes that the proposed implementation of Section 15E(s) of the Exchange Act as mandated by the Dodd-Frank Act may promote efficiency. As noted above, the proposal would be designed to enable investors and other users of credit ratings to better understand the credit ratings and, thereby, promote more prudent use of credit ratings in terms of not unduly relying on credit ratings in making investment and other credit based decisions.

2. Costs

The Commission preliminarily estimates that the Commission's exercise of rulemaking discretion in proposed new paragraph (a) of Rule 17g–7 would impose incremental costs. However, the Commission preliminarily estimates that the costs discussed below resulting from the proposed new paragraph (a) of Rule 17g–7 would be attributable largely to the rulemaking mandated by Dodd-Frank Act and that the incremental costs would be minimal.[1220]

The Commission preliminarily estimates that proposed new paragraph (a) to Rule 17g–7 would result in a one-time cost to develop the standardized disclosures and establish systems, protocols, and procedures for generating the new information as well as protocols, procedures, and systems designed to ensure that all the information required to be included in the form is input into a form prior to the publication of the credit rating, that any certifications received from a provider of third-party due diligence services are attached to the form, and that the form and certifications are published with the credit rating.

As discussed in above in Section IV.D.5 of this release with respect to the PRA, the Commission preliminarily estimates that the one-time hour burden to develop the required disclosures and establish systems, protocols, and procedures would be approximately 5,000 hours, resulting in a one-time industry-wide hour burden of approximately 50,000 hours.[1221] In addition, the Commission preliminarily allocates 75% of these burden hours (37,500 hours) to internal burden and the remaining 25% (12,500 hours) to external burden to hire outside professionals to assist in setting up the process to generate the forms and publish them with applicable credit ratings.[1222] The Commission

[1209] *See* 15 U.S.C. 78o–7(s).

[1210] *See* 15 U.S.C. 78o–7(s)(1)–(4).

[1211] *See* proposed new paragraph (a) of Rule 17g–7. *See also* Sections II.G.1 through G.5 of this release for a more detailed discussion of this proposal.

[1212] *See* proposed new paragraph (a)(1) of Rule 17g–7. This paragraph would implement, in large part, rulemaking specified in Sections 15E(s)(1), (2), and (3) of the Exchange Act. *See* 15 U.S.C. 78o–7(s)(1), (2), and (3).

[1213] *See* proposed new paragraph (a)(2) of Rule 17g–7. This paragraph would implement, in part, rulemaking specified in Section 15E(s)(4) of the Exchange Act. *See* 15 U.S.C. 78o–7(s)(4).

[1214] *See* proposed new paragraph (a)(1)(i) of Rule 17g–7. This paragraph would implement, in large part, rulemaking specified in Section 15E(s)(2) of the Exchange Act. *See* 15 U.S.C. 78o–7(s)(2).

[1215] *See* proposed new paragraph (a)(1)(ii) of Rule 17g–7. This paragraph would implement, in large part, rulemaking specified in Section 15E(s)(3) of the Exchange Act. *See* 15 U.S.C. 78o–7(s)(3). It would also incorporate the existing text of Rule 17g–7 as adopted by the Commission on January 20, 2011 to implement Section 943 of the Dodd-Frank Act. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* Securities Act of 1933 ("Securities Act") Release No. 9175 (Jan. 20, 2011), 76 FR 4489 (Jan. 26, 2011) and 17 CFR 240.17g–7.

[1216] *See* proposed new paragraph (a)(1)(iii) of Rule 17g–7. This paragraph would implement, in large part, rulemaking specified in Section 15E(q)(2)(F) of the Exchange Act. *See* 15 U.S.C. 78o–7(q)(2)(F). Section 15E(q)(2)(F) of the Exchange Act requires that the Commission's rules require an NRSRO to include an attestation with any credit rating it issues affirming that no part of the rating was influenced by any other business activities, that the rating was based solely on the merits of the instruments being rated, and that such rating was an independent evaluation of the risks and merits of the instrument. *See* 15 U.S.C. 78o–7(q)(2)(F). Proposed paragraph (a)(1)(iii) of Rule 17g–7 would require the NRSRO to attach to the form a signed statement by a person within the NRSRO who has responsibility for the credit rating affirming that: (1) No part of the credit rating was influenced by any other business activities; (2) the credit rating was based solely upon the merits of the instruments being rated; and (3) the credit rating was an independent evaluation of the risks and merits of the instrument. Thus, the proposed requirement would mirror the statutory text in terms of the representations that would need to be made in the attestation. *Compare* proposed new paragraphs (a)(1)(iii)(A) through (C) of Rule 17g–7, *with* 15 U.S.C. 78o–7(q)(2)(F).

[1217] *See* proposed paragraph (a)(2) of Rule 17g–7.

[1218] *See* 15 U.S.C. 78o–7(s)(1)(B).

[1219] *See Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 73 FR 36212 (June 25, 2008).

[1220] *Compare* 15 U.S.C. 78o–7(s)(1), (2), (3) and (4)(D) with proposed new paragraph (a) of Rule 17g–7.

[1221] 10 NRSROs × 5,000 hours = 50,000 hours.

[1222] 50,000 hours × 0.75 = 37,500 hours; 50,000 hours × 0.25 = 12,500 hours. This allocation is

Continued

preliminarily estimates $273 per hour for internal costs [1223] and $400 per hour for external costs for retaining outside professionals such as attorneys and information technology consultants,[1224] resulting in an industry-wide one-time cost of approximately $15,237,500.[1225]

With respect to the annual costs, the Commission preliminarily believes that the estimate should be broken into two components. The first component would constitute the cost to an NRSRO to update its standardized disclosures. As discussed in above in Section IV.D.5 of this release with respect to the PRA, the Commission preliminarily believes an NRSRO would spend substantially less time updating the disclosures than the one-time estimate of approximately 5,000 hours per NRSRO to initially develop the standardized disclosures and establish the systems, protocols, and procedures to generate the forms. Consequently, the Commission preliminarily estimates that each NRSRO would spend an average of approximately 500 hours per year updating the standardized disclosures, resulting in an annual industry-wide burden of approximately 5,000 hours. The Commission preliminarily believes that the update process would be handled by the NRSROs internally.

The second component would constitute the amount of time an NRSRO would spend generating and publishing each form and attaching to the form applicable certifications. The Commission preliminarily believes this estimate should be based on the number of rating actions taken per year by the NRSROs because the requirement to generate and publish the form and attach the certifications would be triggered upon the taking of a rating action. As discussed above in Section IV.D.5 of this release with respect to the PRA, the Commission preliminarily estimates that the 10 NRSROs take approximately 2,909,958 credit rating actions per year.[1226] The Commission preliminarily estimates that the time it would take to generate a form by populating it with the required disclosures (most of which would have been pre-established) and to publish the form and any applicable certifications with the credit rating would be 15 minutes, resulting in an industry-wide annual hour burden of approximately 727,490.[1227] Moreover, although larger NRSROs may realize economies of scale, the Commission preliminarily believes that the annual hour burden would be allocated to the 10 NRSROs based on the number of credit ratings they have outstanding.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with proposed new paragraph (a) of Rule 17g–7.

I. Rule 15GA–2 and Form ABS–15G

The Commission is proposing new Rule 15Ga–2 and amendments to Form ABS–15G.[1228] The new rule and amended form would implement Section 15E(s)(4)(A) of the Exchange Act.[1229] Proposed new Rule 15Ga–2 would require an issuer or underwriter of any Exchange Act-ABS that is to be rated by an NRSRO to furnish a Form ABS–15G on the EDGAR system containing the findings and conclusions of any third-party "due diligence report" obtained by the issuer or underwriter. Under the proposal, the disclosure would be furnished using Form ABS–15G for both registered and unregistered offerings of Exchange Act-ABS. In addition, under the Commission's proposal, an issuer or underwriter would not need to furnish Form ABS–15G if the issuer or underwriter obtains a representation from each NRSRO engaged to produce a credit rating for the Exchange Act-ABS that can be reasonably relied on that the NRSRO will publicly disclose the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter with the publication of the credit rating five business days prior to the first sale in the offering in an information disclosure form generated pursuant to proposed new paragraph (a)(1) of Rule 17g–7.

1. Benefits

The proposed rulemaking would provide a standardized format for an issuer or underwriter to make the disclosures required by Section 15E(s)(4)(A). In addition, the Commission proposes to permit an issuer or underwriter to rely on an NRSRO to make the required disclosure. This would avoid duplicate disclosures. The Commission preliminarily believes these proposals would give effect to the objective in Section 15E(s)(4)(A) of the Exchange Act that there be public disclosure of the findings and conclusions of a provider of third-party due diligence services. In addition to directly using the summaries of due diligence findings contained in the disclosure to evaluate the Exchange Act-ABS, investors and other users of credit ratings could benefit by being able to review that disclosure to determine the adequacy and the level of due diligence services provided by a third party. The required increased transparency regarding the due diligence process could promote greater rigor and discipline in that process, to the benefit of investors. In addition, if no disclosure is made, investors and other users of credit ratings would be put on notice that the issuer or underwriter did not employ a provider of third-party due diligence services in connection with the offering of an Exchange Act-ABS.

The Commission also is proposing amendments to Rule 314 of Regulation S–T that would permit municipal securitizers of Exchange Act-ABS, or underwriters in the offering of municipal Exchange Act-ABS, to provide the information required by Form ABS–15G on EMMA, the Municipal Securities Rulemaking Board's centralized public database.[1230] The Commission preliminarily believes that the use of this pre-existing database would promote an efficient process for municipal securitizers of Exchange Act-ABS or underwriters in the offering of municipal Exchange Act-ABS, who would use it to file the required information, as well as for investors and other market participants, who would

based on the Commission's allocation of the industry-wide hour burden for the amount of time it would take a securitizer to set-up a system to make the disclosures required by Form ABS–15G. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011).

[1223] The $273 per hour figure is based on the salary for compliance managers from SIFMA's Management & Professional Earnings in the Securities Industry 2010, modified by Commission staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead.

[1224] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011) (providing an estimate of $400 an hour engage outside professionals) and *Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63889 (Dec. 4, 2009) (providing an estimate of $400 per hour to engage an outside attorney).

[1225] 37,500 hours × $273 = $10,237,500; 12,500 hours × $400 = $5,000,000; $10,237,500 + $5,000,000 = $15,237,500.

[1226] [2,000,000 credit rating actions constituting upgrades, downgrades, placements on credit watch, and withdrawals] + [4,134 preliminary or expected credit ratings] + [415,117 initial credit ratings] + [490,707 affirmations of existing credit ratings] = 2,909,958 rating actions per year. *See* Section IV.D.5 of this release for an extensive discussion and explanation of these numbers.

[1227] 2,909,958 rating actions × .25 hours = 727,489.5 hours (rounded to 727,490 hours).

[1228] *See* proposed new Rule 15Ga–2 and proposed amendments to Form ABS–15G.

[1229] *See* 15 U.S.C. 78o–7(s)(4)(A); *see also* Section II.H.1 of this release for a more detailed discussion of this proposal.

[1230] *See* proposed amendments to Rule 314 of Regulation S–T (17 CFR 231.314); *see also* Section II.H.1 of this release for a more detailed discussion of this proposal.

use it to access that information. The Commission preliminarily believes that the proposed implementation of Section 15E(s)(4)(A) of the Exchange Act would promote an efficient process for issuers and underwriters by requiring an issuer or underwriter to use a standardized form to make the disclosure. It also would permit an issuer or underwriter to rely on an NRSRO to make the disclosures, thereby eliminating duplicate disclosure requirements.

2. Costs

The Commission preliminarily estimates that the costs arising from proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G would be attributable largely to the requirements set forth in Section 15E(s)(4)(A) of the Exchange Act.[1231] Specifically, the Commission believes that the costs to issuers and underwriters arising from preparing a summary of the findings and conclusions of any third-party due diligence report they obtained would be directly attributable to the Dodd-Frank Act, while the incremental costs associated with placing such summaries into Form ABS–15G and furnishing the form on EDGAR (or EMMA, as appropriate) would be attributable to the Commission's rulemaking. As noted above, however, the Commission's rulemaking would provide issuers and underwriters with guidelines as to how they can meet the requirements of Section 15E(s)(4)(A) of the Exchange Act, which the Commission believes would eliminate costs that could potentially arise from uncertainty as to how those requirements could be fulfilled.

As discussed above in Section IV.D.9 of this release with respect to the PRA, the Commission preliminarily estimates that proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G would result in one-time and annual costs for issuers and underwriters in offerings of registered and unregistered Exchange Act-ABS.[1232] The Commission preliminarily estimates that issuers and underwriters would incur a one-time cost in connection with developing processes and protocols to provide the required information to comply with new Rule 15Ga–2, including modifying their existing Form ABS–15G processes and protocols to accommodate the requirements of Rule 15Ga–2. In the adopting release for Form ABS–15G, the Commission estimated that 270 unique securitizers would be required to file the form.[1233] The Commission preliminarily estimates that each securitizer would spend an average of approximately 100 hours to develop processes and protocols to comply with new Rule 15Ga–2 and to modify their existing Form ABS–15G processes and protocols to provide for the disclosure of the information required pursuant to Rule 15Ga–2, resulting in an industry-wide one-time hour burden of approximately 27,000 hours.[1234] The Commission further believes that this work would be done internally.

As discussed above in Section IV.D.9 of this release with respect to the PRA, the Commission has preliminarily based its estimate of the annual hour burden for preparing and furnishing Form ABS–15G on an estimate of the total number of Exchange Act-ABS offerings per year. In the adopting release for Rule 17g–7, the Commission estimated that there would be an average of approximately 2,067 Exchange Act-ABS offerings per year.[1235] The Commission preliminarily estimates that an issuer or underwriter would spend an average of approximately one hour completing and submitting each Form ABS–15G for purpose of meeting the requirement in Rule 15Ga–2. The Commission bases this preliminary estimate on the fact that the information that would be required to be included in Form ABS–15G pursuant to proposed new Rule 15Ga–2 could be drawn directly from the due diligence reports the Commission expects providers of third-party due diligence services to generate with respect to their performance of due diligence services. Therefore, the Commission preliminarily estimates that the industry-wide annual hour burden resulting from proposed new Rule 15Ga–2 and the amendments to Form ABS–15G would be approximately 2,067 hours.[1236] The Commission believes that this work would be done internally.

The Commission preliminarily believes any incremental cost resulting from the amendments would not impact competition or impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G.

J. Third-Party Due Diligence for Asset-Backed Securities

Section 932(a)(8) of the Dodd-Frank Act amended Section 15E of the Exchange Act to add new paragraph (s)(4).[1237] The Commission is proposing new Rule 17g–10 and new Form ABS Due Diligence-15E to implement rulemaking mandated in Sections 15E(s)(4)(B) and (C) of the Exchange Act.[1238] Proposed new Rule 17g–10 would contain three paragraphs: (a), (b)

[1231] *Compare* 15 U.S.C. 78o–7(s)(4)(A), *with* proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G.

[1232] As discussed above in Section IV.D.9, although issuers and underwriters likely will seek to obtain representations from NRSROs engaged to produce a credit rating for Exchange Act-ABS that the NRSRO will publicly disclose the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter with the publication of the credit rating five business days prior to the first sale in the offering in an information disclosure form generated pursuant to proposed new paragraph (a)(1) of Rule 17g–7, thus removing the need for the issuer or underwriter to do so. Consequently, the PRA burden for issuers and underwriters may be reduced substantially. However, to be conservative, the Commission preliminarily allocates the PRA burden for complying with proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G to the issuers and underwriters. The Commission also is proposing to permit issuers of municipal Exchange Act-ABS, or underwriters in such offerings, to provide the information required by Form ABS–15G on EMMA, which would also limit the PRA burden on issuers and underwriters of municipal Exchange Act-ABS subject to the proposed rule.

[1233] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4506 (Jan. 26, 2011).

[1234] 270 unique securitizers × 100 hours = 27,000 hours. This estimate is based on the Commission's estimate for the amount of time it would take a securitizer to set up a system to make the disclosures required by Form ABS–15G as originally adopted by the Commission. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011). The Commission, however, believes that the hour burden for amending existing Form ABS–15G processes and protocols will be significantly lower than the estimate of 850 hours used to initially develop those processes and protocols.

[1235] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4508 (Jan. 26, 2011). As noted above, issuers, underwriters, and NRSROs may not use providers of third-party due diligence services with respect to every issuance of Exchange Act-ABS. For example, as discussed in Section II.H of this release, the Commission preliminarily believes that providers of third-party due diligence services are used primarily for RMBS transactions. However, the Commission's estimate uses the total number of estimated Exchange Act-ABS offerings (as opposed to a lesser amount based on an estimate of RMBS offerings) because the use of providers of third-party due diligence services may migrate to other types of Exchange Act-ABS. This also makes the Commission's estimates more conservative.

[1236] 2,067 Exchange Act-ABS transactions × 1 hour = 2,067 hours.

[1237] *See* Public Law 111–203 § 932(a)(8) and 15 U.S.C. 78o–7(s)(4).

[1238] *See* proposed new Rule 17g–10, and proposed new Form ABS Due Diligence-15E; *see also* Sections II.H.2 and II.H.3 of this release for a more detailed discussion of this proposal.

and (c).[1239] Proposed paragraph (a) would provide that the written certification of a provider of third-party due diligence services required pursuant to Section 15E(s)(4)(B) of the Exchange Act must be made on Form ABS Due Diligence-15E.[1240] Proposed paragraph (b) of new Rule 17g–10 would provide that the written certification must be signed by an individual who is duly authorized by the person providing the third-party due diligence services to make such a certification.[1241] Proposed paragraph (c) of new Rule 17g–10 would contain four definitions to be used for the purposes of Section 15E(s)(4)(B) and Rule 17g–10; namely, a definition of "due diligence services,"[1242] "issuer,"[1243] "originator,"[1244] and "securitizer."[1245]

Proposed Form ABS Due Diligence-15E would contain five line items identifying information the provider of third-party due diligence services would need to provide in the form.[1246] It also would contain a signature line with a corresponding representation.[1247] Item 1 would elicit the identity and address of the provider of third-party due diligence services.[1248] Item 2 would elicit the identity and address of the issuer, underwriter, or NRSRO that employed the provider of third-party due diligence services.[1249] Item 3 would instruct the provider of third-party due diligence services to identify each NRSRO whose published criteria for performing due diligence the provider of third-party due diligence services satisfied in performing the due diligence review.[1250] Item 4 would require the provider of third-party due diligence services to describe the scope and manner of the due diligence performed.[1251] Item 5 would require the provider of third-party due diligence services to describe the findings and conclusions resulting from the review.[1252]

1. Benefits

The proposed rulemaking would be designed to promote a thorough review by the provider of third-party due diligence services of data, documentation, and other relevant information necessary for an NRSRO to provide an accurate credit rating.[1253] The Commission also preliminarily believes that, in combination with the proposed requirement in proposed new paragraph (a)(2) of Rule 17g–7 that the NRSRO disclose the certifications, the proposed rulemaking would allow the public to determine the adequacy and level of due diligence services provided by a third party.

The Commission preliminarily believes that the proposed implementation of Section 15E(s)(4)(C) of the Exchange Act as mandated by the Dodd-Frank Act would promote an efficient process for NRSROs by establishing a standardized format for the certification and providing clarity through the definition of "due diligence services" as to when the requirement was triggered.

2. Costs

The Commission preliminarily estimates that the Commission's exercise of rulemaking discretion with respect to proposed new Rule 17g–10 and new Form ABS Due Diligence-15E would impose incremental costs. However, the Commission preliminarily estimates that the costs discussed below resulting from proposed new Rule 17g–10 and new Form ABS Due Diligence-15E would be attributable largely to the rulemaking mandated by Dodd-Frank Act[1254] and that the incremental costs would be minimal.

As discussed above in Section IV.D.8 of this release with respect to the PRA, the Commission preliminarily estimates that the proposed new rule and form would result in one-time hour burdens for providers of third-party due diligence services to develop processes and protocols to provide the required information in new Form ABS Due Diligence-15E and submit the certifications to NRSROs. The Commission preliminarily estimates that there are approximately 10 firms that provide, or would begin providing, third-party "due diligence services" to issuers and underwriters of Exchange Act-ABS as the term "due diligence services" would be defined in paragraph (a) of proposed new Rule 17g–10. The Commission preliminarily estimates that each of these providers of third-party due diligence services would spend approximately 300 hours to develop these processes and protocols, resulting in a one-time industry-wide burden of 3,000 hours.[1255] In addition, the Commission preliminarily allocates 75% of these burden hours (2,250 hours) to internal burden and the remaining 25% (750 hours) to external burden to hire outside attorneys to provide legal advice on the requirements of new Rule 17g–10 and Form ABS Due Diligence-15E.[1256] The Commission, therefore, preliminarily estimates that the average one-time cost to each provider third-party due diligence services would be $91,425, resulting in an industry-wide one-time cost of $914,250.[1257]

With respect to the annual cost, the Commission preliminarily believes that the estimate should be based on the number of issuances per year of Exchange Act-ABS, since the requirement to produce the certification and provide it to NRSROs would be triggered when an issuer, underwriter, or NRSRO hires a provider of third-party due diligence services with respect to such transactions.[1258] In the adopting release for Rule 17g–7, the

[1239] *See* proposed paragraphs (a), (b) and (c) of Rule 17g–10 *see also* Sections II.H.2 of this release for a more detailed discussion of this proposal.

[1240] *See* proposed paragraph (a) of new Rule 17g–10.

[1241] *See* proposed paragraph (b) of Rule 17g–10.

[1242] *See* proposed paragraph (c)(1) of new Rule 17g–10.

[1243] *See* proposed paragraph (c)(2) of new Rule 17g–10.

[1244] *See* proposed paragraph (c)(3) of new Rule 17g–10.

[1245] *See* proposed paragraph (c)(4) of new Rule 17g–10.

[1246] *See* proposed new Form ABS Due Diligence-15E; *see also* Section II.H.3 of this release for a more detailed discussion of this proposal.

[1247] *See* proposed new Form ABS Due Diligence-15E.

[1248] *See* Item 1 to proposed Form ABS Due Diligence-15E.

[1249] *See* Item 2 to proposed Form ABS Due Diligence-15E.

[1250] *See* Item 3 to proposed Form ABS Due Diligence 15E.

[1251] *See* Item 4 to proposed Form ABS Due Diligence 15E.

[1252] *See* Item 5 to proposed Form ABS Due Diligence 15E.

[1253] *See* 15 U.S.C. 78o–7(s)(4)(B).

[1254] *Compare* 15 U.S.C. 78o–7(s)(4)(B) and (C), *with* proposed new Rule 17g–10 and proposed new Form ABS Due Diligence-15E.

[1255] 10 Providers of third-party due diligence services × 300 hours = 3,000 hours. This estimate is based on the Commission's estimate for the amount of time it would take a securitizer to set up a system to make the disclosures required by Form ABS–15G as originally adopted by the Commission. *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011). The Commission, however, reduces the hour estimate of 850 hours originally used for Form ABS–15G by approximately two-thirds because information required to provided in proposed new Form ABS Due Diligence-15E is substantially less detailed and complex than the information required in Form ABS–15G as initially adopted by the Commission.

[1256] 3,000 hours × 0.75 = 2,250 hours; 3,000 hours × 0.25 = 750 hours.

[1257] 2,250 hours × $273 = $614,250; 750 hours × $400 = $300,000; $614,250 + $300,000 = $914,250; $914,250/10 providers of third-party due diligence services = $91,250. The $273 per hour figure is based on the rate for compliance managers from SIFMA's Management & Professional Earnings in the Securities Industry 2010, modified by Commission staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead. The $400 figure is based on the Commission's estimate of $400 per hour to engage an outside attorney. *See Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63889 (Dec. 4, 2009).

[1258] *See* 15 U.S.C. 78o–7(s)(4)(B) and (C), and proposed new Rule 17g–10.

Commission estimated there would be an average of approximately 2,067 Exchange Act-ABS offerings per year.[1259] In addition, the Commission preliminarily estimates that a provider of third-party due diligence services would spend approximately 30 minutes completing and submitting Form ABS Due Diligence-15E. The Commission bases this preliminary estimate on the fact that first three Items in the form require basic information and the fourth Item (the due diligence performed) and the fifth Item (the findings and conclusions of the review) could be drawn directly from the due diligence reports the Commission expects providers of third-party due diligence services generate with respect to their performance of due diligence services. Therefore, the Commission preliminarily estimates that the industry-wide annual hour burden resulting from proposed new Rule 17g–10 and Form ABS Due Diligence-15E would be approximately 1,034 hours.[1260] The Commission believes that completing and submitting Form ABS Due Diligence-15E would be done internally.

The Commission preliminarily believes any incremental cost resulting from the amendments would not impact competition or impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with proposed new Rule 17g–10 and new Form ABS Due Diligence-15E.

K. Standards of Training, Experience, and Competence

Section 936 of the Dodd-Frank Act provides that the Commission shall issue rules that are reasonably designed to ensure that any person employed by an NRSRO to perform credit ratings: (1) Meets standards of training, experience, and competence necessary to produce accurate ratings for the categories of issuers whose securities the person rates;[1261] and (2) is tested for knowledge of the credit rating process.[1262] The Commission proposes to implement Section 936 by proposing new Rule 17g–9 and amending Rule 17g–2.[1263]

Proposed paragraph (a) of new Rule 17g–9 would require an NRSRO to establish, maintain, enforce, and document standards of training, experience, and competence for the individuals it employs to determine credit ratings that are reasonably designed to achieve the objective that such individuals produce accurate credit ratings in the classes and subclasses of credit ratings for which the NRSRO is registered.[1264]

Proposed paragraph (b) would identify factors the NRSRO must consider when designing the standards.[1265] Specifically, the NRSRO would need to consider:

- If the credit rating procedures and methodologies used by the individual involve qualitative analysis, the knowledge necessary to effectively evaluate and process the data relevant to the creditworthiness of the obligor being rated or the issuer of the securities or money market instruments being rated;
- If the credit rating procedures and methodologies used by the individual involve quantitative analysis, the technical expertise necessary to understand any models and model inputs that are a part of the procedures and methodologies;
- The classes and subclasses of credit ratings for which the individual participates in determining credit ratings and the factors relevant to such classes and subclasses, including the geographic location, sector, industry, regulatory and legal framework, and underlying assets, applicable to the obligors or issuers in the classes and subclasses; and
- The complexity of the obligors, securities, or money market instruments being rated by the individuals.

Proposed paragraph (c) of new Rule 17g–9 would prescribe two requirements that an NRSRO must incorporate into its standards of training, experience, and competence.[1266] Proposed paragraph (c)(1) of new Rule 17g–9 would provide that the standards of training, experience, and competence must include a requirement for periodic testing of the individuals employed by the NRSRO to determine credit ratings on their knowledge of the procedures and methodologies used by the NRSRO to determine credit ratings in the classes or subclasses of credit ratings for which the individual is responsible for determining credit ratings.[1267] Proposed paragraph (c)(2) of new Rule 17g–9 would provide that the standards of training, experience, and competence must include a requirement that at least one individual with three years or more experience in performing credit analysis participates in the determination of a credit rating.[1268]

In addition, the Commission proposes adding new paragraph (b)(15) to Rule 17g–2 to identify the standards of training, experience, and competence the NRSRO must establish, maintain, enforce, and document pursuant to proposed new Rule 17g–9 as a record that must be retained.[1269] As a result, the procedures would be subject to the record retention and production requirements in paragraphs (c) through (f) of Rule 17g–2.[1270]

1. Benefits

The Commission is proposing to implement rulemaking mandated by Section 936 of the Dodd-Frank Act through proposed new Rule 17g–9. The proposed rule would be designed to achieve the objectives in Section 936 that any person employed by an NRSRO to perform credit ratings: (1) Meets standards of training, experience, and competence necessary to produce accurate ratings for the categories of issuers whose securities the person rates;[1271] and (2) is tested for knowledge of the credit rating process.[1272] The Commission preliminarily believes that the proposed new rule could promote the integrity of the ratings process to the benefit of

[1259] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4508 (Jan. 26, 2011). The Commission notes that issuers, underwriters, and NRSROs may not use providers of third-party due diligence services with respect to every issuance of Exchange Act-ABS. For example, as discussed in Section II.H of this release, the Commission preliminarily believes that providers of third-party due diligence services are used primarily for RMBS transactions. However, the Commission's estimate uses the total number of estimated Exchange Act-ABS offerings (as opposed to a lesser amount based on an estimate of RMBS offerings) because the use of providers of third-party due diligence services may migrate to other types of Exchange Act-ABS. This also makes the Commission's estimates more conservative.

[1260] 2,067 Exchange Act-ABS offerings × 30 minutes = 1,034 hours.

[1261] *See* Public Law 111–203 § 936(1).

[1262] *See* Public Law 111–203 § 936(2).

[1263] *See* proposed new Rule 17g–9 and proposed new paragraph (b)(15) of Rule 17g–2.

[1264] *See* proposed paragraph (a) of new Rule 17g–9; *see also* Section II.I.1.a of this release for a more detailed discussion of this proposal.

[1265] *See* proposed paragraph (b) of new Rule 17g–9; *see also* Section II.I.1.b of this release for a more detailed discussion of this proposal.

[1266] *See* proposed paragraphs (c)(1) and (2) of new Rule 17g–9; *see also* Section II.I.1.c of this release for a more detailed discussion of this proposal.

[1267] *See* proposed paragraph (c)(1) of new Rule 17g–9.

[1268] *See* proposed paragraph (c)(2) of new Rule 17g–9.

[1269] *See* proposed new paragraph (b)(15) to Rule 17g–2.

[1270] *See* 17 CFR 240.17g–2; *see also* Section II.I.2 of this release for a more detailed discussion of this proposal.

[1271] *See* Public Law 111–203 § 936(1).

[1272] *See* Public Law 111–203 § 936(2).

investors and other users of credit ratings.

Paragraph (a) of proposed new Rule 17g–9 would require the NRSRO to design its own standards but provide that they must be reasonably designed to achieve the common objective that individuals employed by the NRSRO to determine credit ratings produce accurate credit ratings in the classes of credit ratings for which the NRSRO is registered. This could benefit NRSROs by providing flexibility to allow each NRSRO to customize the standards according to its unique procedures and methodologies for determining credit ratings and its size.

Paragraph (b) of proposed new Rule 17g–9 would identify factors the NRSRO must consider when designing the standards.[1273] This would provide guidance to NRSROs about the Commission's expectations for the design of the standards of training, experience, and competence. It also could serve an investor protection function by providing benchmarks that Commission examiners could use to evaluate whether a given NRSRO's standards are reasonably designed to meet the objective that individuals employed by the NRSRO to determine credit ratings produce accurate credit ratings in the classes of credit ratings for which the NRSRO is registered.

Paragraph (c)(1) of proposed new Rule 17g–9 would provide that the standards of training, experience, and competence must include a requirement for periodic testing of the individuals employed by the NRSRO to determine credit ratings on their knowledge of the procedures and methodologies used by the NRSRO to determine credit ratings in the classes or subclasses of credit ratings for which the individual participates in determining credit ratings.[1274] The rule could benefit NRSROs by allowing each NRSRO to establish the frequency and manner of testing its analysts. These considerations may depend on the number of analysts the NRSRO employs, the complexity of the products that are being rated, and the varying levels of experience of the analysts.

Paragraph (c)(2) of proposed new Rule 17g–9 would provide that the standards of training, experience, and competence must include a requirement that at least one individual with three years or more experience in performing credit analysis participates in the determination of a credit rating.[1275] This would establish a minimum requirement that someone with experience performing credit analysis is involved in determining the credit rating.

2. Costs

The Commission preliminarily estimates that the Commission's exercise of rulemaking discretion with respect to proposed new Rule 17g–9 would impose incremental costs. However, the Commission preliminarily estimates that the costs discussed below resulting from proposed new Rule 17g–9 would be attributable largely to the rulemaking mandated by Dodd-Frank Act and that the incremental costs would be minimal.[1276]

As discussed above in Section IV.D.7 of this release with respect to the PRA, the Commission preliminary estimates that an NRSRO would incur one-time and annual hour burdens as a result of proposed new Rule 17g–9. Also, the Commission preliminarily estimates that the degree of the one-time and annual hour burdens resulting from proposed Rule 17g–9 would depend on the number of credit analysts an NRSRO employs as well as the range and complexity of the obligors, securities, and money market instruments it rates. Thus, hour burdens in the PRA and the costs estimated below are based on the number of credit rating analysts employed by the NRSROs.

As discussed above in Section IV.D.7 of this release with respect to the PRA, the Commission preliminarily estimates that the one-time hour burden to establish the standards that would be required under proposed new Rule 17g–9 would be approximately 5 hours per credit analyst. Based on the 2009 annual certifications, the Commission estimates that the NRSROs currently employ approximately 3,520 credit analysts,[1277] resulting in an industry-wide one-time hour burden of 17,600 hours.[1278] In addition, the Commission estimates that 75% of the burden hours (13,200 hours) would be internal and the remaining 25% (4,400 hours) would be external to hire outside professionals to assist in setting up training programs.[1279] Consequently, the Commission preliminarily estimates that the industry-wide one-time internal cost would be approximately $3,603,000.[1280] With respect to the external costs associated with the proposal, the Commission preliminarily estimates that outside professionals would charge approximately $400 per hour.[1281] Consequently, the Commission preliminarily estimates that the industry-wide external cost would be approximately $1,760,000.[1282] The Commission, therefore, preliminarily estimates that the total industry-wide one-time cost of proposed Rule 17g–9 would be approximately $5,363,000.[1283] The Commission preliminarily estimates that this cost would be allocated to the 10 NRSROs based on the number of credit analysts each employs.

As discussed above in Section IV.D.7 of this release with respect to the PRA, the Commission believes that the annual cost to comply with proposed new Rule 17g–9 would be less than the one-time cost since NRSROs already would have established the standards of training, experience, and competence for the individuals they employ to determine credit ratings and, therefore, only would need to update them. The Commission preliminarily estimates that reviewing and updating the standards as appropriate would take approximately 1 hour per credit analyst, resulting in an annual industry-wide hour burden of approximately 3,520 hours.[1284] The Commission estimates that approximately 75% of these burden hours (2,640 hours) would be internal and the remaining 25% (880 hours) would be external to hire outside professionals to assist in updating the training programs. Consequently, the Commission preliminarily estimates that the industry-wide annual internal costs would be approximately $720,720.[1285] With respect to the external costs, the Commission preliminarily estimates that outside

[1273] *See* proposed paragraph (b) of new Rule 17g–9.

[1274] *Id.*

[1275] *Id.*

[1276] *Compare* Public Law 111–203 § 936 with proposed new Rule 17g–9.

[1277] *See* Figure 3.

[1278] 3,520 credit analysts × 5 hours = 17,600 hours.

[1279] 17,600 hours × 0.75 = 13,200 hours; 17,600 hours × 0.25 = 4,400 hours.

[1280] 13,200 hours × $273 = $3,603,600. The $273 per hour figure is based on the rate for compliance managers from SIFMA's Management & Professional Earnings in the Securities Industry 2010, modified by Commission staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead.

[1281] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011) (providing an estimate of $400 an hour engage outside professionals) and *Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63889 (Dec. 4, 2009) (providing an estimate of $400 per hour to engage an outside attorney).

[1282] 4,400 hours × $400 = $1,760,000.

[1283] $1,760,000 + $3,603,000 = $5,363,000.

[1284] 3,520 credit analysts × 1 hour = 3,520 hours.

[1285] 2,640 hours × $273 = $720,720. The $273 per hour figure is based on the rate for compliance managers from SIFMA's Management & Professional Earnings in the Securities Industry 2010, modified by Commission staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead.

professionals would charge approximately $400 per hour.[1286] Consequently, the Commission preliminarily estimates that the annual industry-wide external costs would be approximately $352,000.[1287] The Commission, therefore, preliminarily estimates that the total industry-wide annual cost would be approximately $1,072,720.[1288] The Commission preliminarily estimates that this cost would be allocated to the 10 NRSROs based on the number of credit analysts each employs.

The Commission acknowledges that the three-year analyst experience requirement proposed in paragraph (c)(2) of proposed new Rule 17g–9 could impose a barrier to entry to becoming an NRSRO. It is possible that this requirement, as well as the increased training standards in general, could increase labor costs for NRSROs by increasing the competition for credit analysts with the requisite amount of experience. The Commission further understands that the effects could likely be more pronounced with existing smaller NRSROs, as well as with new NRSRO entrants, as these smaller firms would presumably be less able to bear the costs. This could, in turn, decrease competition amongst NRSROs. The Commission requests comment on this potential effect of the proposed rulemaking.

The Commission preliminarily estimates that, although the costs resulting from proposed new paragraph (b)(15) of new Rule 17g–2 would be attributable to the Commission's discretionary rulemaking, those incremental costs would be minimal. As discussed above in Section IV.D.3 of this release with respect to the PRA, the Commission preliminary believes that applying the recordkeeping requirements of Rule 17g–2 to five new types of records would result in one-time and annual hour burdens for NRSROs in connection with updating their record retention policies and procedures to retain these new records. As discussed above in Section IV.D.3 of this release with respect to the PRA, based on staff experience, the Commission preliminarily estimates that the additional one-time hour burden for each NRSRO to update its record retention policies and procedures for the new records that would need to be retained under proposed new paragraphs (a)(9), (b)(12), (b)(13), (b)(14), and (b)(15) of Rule 17g–2 would be 20 hours. Based on that estimate, the Commission preliminary believes that the average one-time hour burden attributable to proposed new paragraph (b)(15) of Rule 17g–2 would be approximately 4 hours per NRSRO, resulting in an industry-wide hour burden of approximately 40 hours.[1289] As discussed above in Section IV.D.3 of this release with respect to the PRA, the Commission preliminarily estimates it would take an average of approximately one hour each year for an NRSRO to retain updated versions of the information required pursuant to proposed new paragraph (b)(15) of Rule 17g–2, resulting in an industry-wide hour burden of 10 hours.[1290]

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with proposed new Rule 17g–9 and new paragraph (b)(15) of Rule 17g–2.

L. Universal Rating Symbols

Section 938(a) of the Dodd-Frank Act provides that the Commission shall require, by rule, each NRSRO to establish, maintain, and enforce written policies and procedures that: (1) Assess the probability that an issuer of a security or money market instrument will default, fail to make timely payments, or otherwise not make payments to investors in accordance with the terms of the security or money market instrument;[1291] (2) clearly define and disclose the meaning of any symbol used by the NRSRO to denote a credit rating;[1292] and (3) apply any symbol described in item (2) in a manner that is consistent for all types of securities and money market instruments for which the symbol is used.[1293]

The Commission proposes to implement this rulemaking mandate through paragraph (b) of proposed new Rule 17g–8. In particular, paragraph (b)(1) of proposed new Rule 17g–8 would require the NRSRO to have policies and procedures reasonably designed to assess the probability that an issuer of a security or money market instrument will default, fail to make timely payments, or otherwise not make payments to investors in accordance with the terms of the security or money market instrument.[1294] Paragraph (b)(2) of proposed new Rule 17g–8 would require the NRSRO to have policies and procedures reasonably designed to clearly define the meaning of each symbol, number, or score in the rating scale used by the NRSRO to denote a credit rating category and notches within a category for each class and subclass of credit ratings for which the NRSRO is registered and to include such definitions in Exhibit 1 to Form NRSRO.[1295] Paragraph (b)(3) of proposed new Rule 17g–8 would require the NRSRO to have policies and procedures reasonably designed to apply any symbol, number, or score defined pursuant to paragraph (b)(2) of new Rule 17g–8 in a manner that is consistent for all types of obligors, securities, and money market instruments for which the symbol, number, or score is used.[1296]

The Commission also is proposing that the policies and procedures required pursuant to proposed paragraph (b) of new Rule 17g–8 be subject to the record retention and production requirements of Rule 17g–2.[1297] Consequently, the Commission proposes adding new paragraph (b)(14) to Rule 17g–2 to identify the policies and procedures an NRSRO is required to establish, maintain, enforce, and document pursuant to proposed paragraph (b) of new Rule 17g–8 as a record that must be retained.[1298]

1. Benefits

The proposal could facilitate investor understanding of credit ratings by promoting a consistent application of rating methodologies to particular credit ratings, at least within a class of credit ratings. In addition, the proposed requirement for NRSROs to disclose the meaning of credit rating symbols, numbers, and scores could benefit investors and other users of credit ratings by promoting a better understanding of credit rating terminology and allowing them to better compare the various ratings issued by a single NRSRO.

[1286] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* 76 FR at 4507–4506 (Jan. 26, 2011) (providing an estimate of $400 an hour engage outside professionals) and *Proposed Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR 63889 (Dec. 4, 2009) (providing an estimate of $400 per hour to engage an outside attorney).

[1287] 880 hours × $400 = $352,000.

[1288] $720,720 + $352,000 = $1,072,072.

[1289] 20 hours/5 new required records = 4 hours; 10 NRSROs × 4 hours = 40 hours.

[1290] 10 NRSROs × 1 hour = 10 hours.

[1291] *See* Public Law 111–203 § 938(a)(1).

[1292] *See* Public Law 111–203 § 938(a)(2).

[1293] *See* Public Law 111–203 § 938(a)(3).

[1294] *See* proposed paragraph (b)(1) of new Rule 17g–8.

[1295] *See* proposed paragraph (b)(2) of new Rule 17g–8.

[1296] *See* proposed paragraph (b)(1) of new Rule 17g–8.

[1297] 17 CFR 240.17g–2.

[1298] *See* proposed new paragraph (b)(13) to Rule 17g–2; *see also* Section II.F.2 of this release for a more detailed discussion of this proposal.

2. Costs

The Commission preliminarily estimates that the Commission's exercise of rulemaking discretion with respect to proposed paragraph (b) of new Rule 17g–8 would impose incremental costs. However, the Commission preliminarily estimates that the costs discussed below resulting from proposed paragraph (b) of new Rule 17g–8 would be attributable largely to the rulemaking mandated by Dodd-Frank Act [1299] and that the incremental costs would be minimal.

As discussed in above in Section IV.D.6 with respect to the PRA, the Commission preliminarily estimates each NRSRO would spend an average of approximately 200 hours establishing the policies and procedures that would be required under paragraph (b) of proposed new Rule 17g–8, resulting in an industry-wide one-time hour burden of 2,000 hours.[1300] In addition, as discussed in above in Section IV.D.6 with respect to the PRA, the Commission preliminarily estimates an NRSRO would spend an average of approximately 50 hours annually reviewing and updating those policies and procedures, resulting in an industry-wide annual burden of 500 hours.[1301]

The Commission preliminarily estimates that, although the costs resulting from proposed new paragraph (b)(14) of new Rule 17g–2 would be attributable to the Commission's discretionary rulemaking, those incremental costs would be minimal. As discussed above in Section IV.D.3 of this release with respect to the PRA, the Commission preliminary believes applying the recordkeeping requirements of Rule 17g–2 to five new types of records would result in one-time and annual hour burdens for NRSROs in connection with updating their record retention policies and procedures to account for and retain these new records. As discussed above in Section IV.D.3 of this release with respect to the PRA, based on staff experience, the Commission preliminarily estimates that the additional one-time hour burden for each NRSRO to update its record retention policies and procedures to account for the new records that would need to be retained under proposed new paragraphs (a)(9), (b)(12), (b)(13), (b)(14), and (b)(15) of Rule 17g–2 would be 20 hours. Based on that estimate, the Commission preliminary believes that the average one-time hour burden attributable to proposed new paragraph (b)(14) of Rule 17g–2 would be approximately 4 hours per NRSRO, resulting in an industry-wide hour burden of approximately 40 hours.[1302]

As discussed above in Section IV.D.3 of this release with respect to the PRA, the Commission preliminarily estimates it would take an average of approximately one hour each year for an NRSRO to retain updated versions of the information required pursuant to proposed new paragraph (b)(14) of Rule 17g–2, resulting in an industry-wide hour burden of 10 hours.[1303]

The Commission preliminarily believes any incremental cost resulting from the amendments would not impact competition or impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with proposed paragraph (b) of new Rule 17g–8.

M. Annual Report of Designated Compliance Officer

Section 932(a)(5) of the Dodd-Frank Act amended Section 15E(j) of the Exchange Act to re-designate paragraph (j) as paragraph (j)(1) and to add new paragraphs (j)(2) through (j)(5).[1304] Section 15E(j)(1) of the Exchange Act contains a self-executing provision that an NRSRO 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,[1305] and for compliance with the securities laws and the rules and regulations thereunder, including those promulgated by the Commission under Section 15E of the Exchange Act.[1306] Section 15E(j)(5)(A) of the Exchange Act requires the designated compliance officer to submit to the NRSRO an annual report on the compliance of the NRSRO with the securities laws and the policies and procedures of the NRSRO that includes: (1) A description of any material changes to the code of ethics and conflict of interest policies of the NRSRO; and (2) a certification that the report is accurate and complete.[1307] Section 15E(j)(5)(B) of the Exchange Act provides that the NRSRO shall file the report required pursuant to Section 15E(j)(5)(A) together with the financial report that is required to be submitted to the Commission under Section 15E of the Exchange Act.[1308]

As discussed above in Section II.A.3 of this release, Rule 17g–3 requires an NRSRO to submit five or, in certain cases, six separate reports not more than 90 days after the end of the NRSRO's fiscal year and identifies the reports to be submitted to the Commission.[1309] In order to further clarify the self-executing requirement in Section 15E(j)(5)(B) of the Exchange Act, the Commission is proposing to amend Rule 17g–3 to identify the annual report of the designated compliance officer as one of the reports that must be submitted to the Commission.[1310] Specifically, the Commission proposes adding a new paragraph (a)(8) to Rule 17g–3 to identify the report on the compliance of the NRSRO with the securities laws and the policies and procedures of the NRSRO required pursuant to Section 15E(j)(5)(B) of the Exchange Act.[1311] The Commission preliminarily estimates that the costs and benefits of this proposal are entirely attributable to the mandates of the Dodd-Frank Act, and are not a result of decisions made by the Commission to fulfill the mandates of the Dodd-Frank Act within its permitted discretion. Proposed new paragraph (a)(8) to Rule 17g–3 is intended only to clarify how an NRSRO must adhere to the self-executing provisions in Section 15E(j)(5)(B) of the Exchange Act and would result in no additional costs. Moreover, the Commission is not proposing to add any additional requirements with respect to the filing other than the proposed requirement that this report and the other annual reports be filed through the EDGAR system, which is addressed separately below.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with proposed new paragraph (a)(8) to Rule 17g–3.

[1299] *Compare* Public Law 111–203 § 938, *with* proposed new Rule 17g–9.

[1300] 10 NRSROs × 200 hours = 2000 hours.

[1301] 10 NRSROs × 50 hours = 500 hours.

[1302] 20 hours/5 new required records = 4 hours; 10 NRSROs × 4 hours = 40 hours.

[1303] 10 NRSROs × 1 hour = 10 hours.

[1304] *See* 15 U.S.C. 78o–7(j)(1) through (5).

[1305] *See* 15 U.S.C 780–7(g) and (h).

[1306] *See* 15 U.S.C. 78o–7(j)(1).

[1307] *See* 15 U.S.C. 78o–7(j)(5)(A).

[1308] *See* 15 U.S.C. 78o–7(j)(5)(B).

[1309] *See* 17 CFR 240.17g–3(a)(1)–(6). As discussed above in Section II.A.3 of this release, the Commission is proposing that Rule 17g–3 be amended to add a new paragraph (a)(7) to implement Section 15E(c)(3)(B) of the Exchange Act by requiring an NRSRO to file the annual internal controls report. *See* 15 U.S.C. 78o–7(c)(3)(B).

[1310] *See* proposed new paragraph (a)(8) of Rule 17g–3.

[1311] *Id.*

N. Electronic Submission of Form NRSRO and the Rule 17g–3 Annual Reports

The Commission is proposing that certain Form NRSRO submissions and all Rule 17g–3 annual report submissions be submitted to the Commission using the EDGAR system. In order to implement this requirement, the Commission is proposing amendments to Rule 101 of Regulation S–T to require the electronic submission using the EDGAR system of Form NRSRO pursuant to paragraphs (e), (f), and (g) of Rule 17g–1 and the annual reports pursuant Rule 17g–3.[1312] The Commission also is proposing to amend Rule 201 of Regulation S–T, which governs temporary hardship exemptions from electronic filing, to make this exemption unavailable for NRSRO submissions.[1313]

1. Benefits

One of the primary goals of the EDGAR system since its inception is to facilitate the rapid dissemination of financial and business information in connection with filings the Commission receives. Although paragraph (i) of Rule 17g–1 currently requires NRSROs to make the public portions of their current Form NRSROs publicly available within 10 business days after submission to the Commission, the Commission believes that having all such information available immediately upon submission in one location would make the information more easily available and searchable to investors and other users of credit ratings. Further, the Commission believes that submissions made to the Commission are more valuable to investors and other users of credit ratings if they are available in electronic form and that adding the Form NRSRO submissions to the EDGAR database would provide a more complete picture for the public. The Commission preliminarily estimates that, as a result of the proposals, the EDGAR page of the Commission's Web site,[1314] in conjunction with the NRSRO page of the Commission's Web site,[1315] would be a comprehensive source from which to find most public information submitted to the Commission, as well as other information, related to NRSROs. The Commission preliminarily believes that the electronic submission of Form NRSRO would benefit investors and other users of credit ratings by increasing the efficiency of retrieving and comparing NRSRO public submissions and enabling the investors and other users of credit ratings to access information more quickly.

In addition, while the Rule 17g–3 annual reports would not be made public on EDGAR, having them submitted on EDGAR would assist the Commission in its oversight of NRSROs. For example, Commission examiners could easily retrieve the annual reports of a specific NRSRO to prepare for an examination. Moreover, having these records submitted and stored through EDGAR in a centralized location would assist the Commission from a records management perspective by establishing a more automated storage process and creating efficiencies in terms of reducing the volume of paper submissions that must be manually processed and stored.

Moreover, the Commission preliminarily believes that the electronic submission of the Form NRSROs and the Rule 17g–3 annual reports would benefit NRSROs. For example, NRSROs would avoid the uncertainties, delay, and expense related to the manual delivery of paper submissions. Further, NRSROs would benefit from no longer having to submit multiple paper copies of these submissions to the Commission.

The Commission preliminarily believes that the proposed requirement that Form NRSROs and Exhibits 1 through 9 and the Rule 17g–3 annual reports be submitted through the EDGAR system would promote efficiency. As noted above, the proposal would provide a central location for an investor or other user of credit ratings to access the Forms and Exhibits. It also would assist the Commission staff in storing and accessing these records in furtherance of the Commission's NRSRO oversight function. Furthermore, it would provide NRSROs with a more efficient way to submit these forms and reports to the Commission.

2. Costs

The Commission preliminarily estimates that, although the Commission's exercise of rulemaking discretion with respect to the proposed amendments to Rules 101 and 201 of Regulation S–T, Rule 17g–1, and Rule 17g–3 would impose incremental costs, those incremental costs would be minimal.

As discussed in Section IV.D.1 of this release with respect to the PRA, the Commission preliminarily estimates that each NRSRO would spend an average of approximately 5 hours becoming familiar with the EDGAR filing system and completing and submitting Form ID.[1316] The Commission preliminarily estimates that the annual cost attributable to submitting the Form NRSROs and Rule 17g–3 annual reports through the EDGAR system would be no greater than the annual costs attributable to submitting them in paper form.

The Commission preliminarily believes any incremental cost resulting from the amendments would not impact competition or impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with the proposed amendments to Rules 101 and 201 of Regulation S–T, Rule 17g–1, and Rule 17g–3.

O. Other Amendments

The Commission is proposing additional amendments to several of the NRSRO rules in response to amendments the Dodd-Frank Act made to sections of the Exchange Act that authorize or otherwise are relevant to these rules. The Commission preliminarily estimates that these proposals would not result in any one-time or annual incremental costs to NRSROs. Furthermore, the Commission preliminarily believes these proposals would benefit NRSROs and Commission staff be making terms in Commission rules applicable to NRSROs consistent with terms in Section 15E of the Exchange. This could promote greater clarity as to the requirements in the rules and remove potential ambiguity caused by inconsistent terms.

The Commission preliminarily believes that the proposals would promote efficiency. As noted above, the proposals would be designed to promote greater clarity as to the requirements in the rules and remove potential

[1312] *See* proposed amendment of Rule 101 of Regulation S–T (17 CFR 231.101); *see also* Section II.L of this release for a more detailed discussion of this proposal.

[1313] *See* proposed amendment of Rule 201 of Regulation S–T (17 CFR 231.201); *see also* Section II.L of this release for a more detailed discussion of this proposal.

[1314] *http://www.sec.gov/investor/pubs/edgarguide.htm.*

[1315] *http://www.sec.gov/divisions/marketreg/ratingagency.htm.*

[1316] An NRSRO would need to complete Form ID in order to be eligible to submit documents using the EDGAR system. However, completing Form ID is a simple process. The Commission has noted in the past that the burden associated with Form ID is 15 minutes. *See* Securities Exchange Act Release No. 57280 (Feb. 6, 2008), 73 FR 10592, 10610 (Feb. 27, 2008). Thus, the Commission preliminarily estimates that the one-time hour burden per NRSRO associated with the filing of Form ID would be 15 minutes, resulting in an industry-wide burden of 1.5 hours.

ambiguity caused by inconsistent terms. In addition, as discussed above, the Commission preliminarily estimates that the proposals would not result in any one-time or annual incremental costs to NRSROs and would have substantial benefits. Consequently, the Commission preliminarily believes that the proposals would not impact competition or impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

1. Changing "Furnish" To "File"

In accordance with the Dodd-Frank Act, the Commission is proposing amending certain provisions of Rule 17g–1 and Rule 17g–3 to replace the word "furnish" with the word "file".[1317] The Commission also is proposing to make conforming amendments to Form NRSRO and the instructions for Form NRSRO.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with these proposed amendments, including whether they would result in one-time or annual incremental costs to NRSROs.

2. Amended Definition of "NRSRO"

The definition of "nationally recognized statistical rating organization" in Section 3(a)(62) of the Exchange Act, prior to being amended by the Dodd-Frank Act, included a condition in Section 3(a)(62)(A) that the entity "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 under Section 15E".[1318] Section 932(b) of the Dodd-Frank Act struck subparagraph (A) of Section 3(a)(62).[1319] Form NRSRO contains a definition of "NRSRO" that tracks Section 3(a)(62) as originally enacted. The Commission proposes amending this definition to conform it to Section 3(a)(62) as amended by the Dodd-Frank Act.[1320] The Commission does not believe these proposals would result in any incremental costs to NRSROs.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with these proposed amendments, including whether they would result in one-time or annual incremental costs to NRSROs.

3. Definition of Asset-Backed Security

Section 941(a) of the Dodd-Frank Act amended Section 3 of the Exchange Act to add Section 3(a)(77), which defines "asset-backed security."[1321] In response, the Commission is proposing that certain language in Exchange Act Rules 17g–2(a)(2)(iii); 17g–2(a)(7); 17g–5(a)(3); 17g–5(b)(9); 17g–6(a)(4); and Form NRSRO be amended to reflect this new definition.[1322] The Commission preliminarily estimates that these proposals would result in no incremental costs to NRSROs.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with these proposed amendments, including whether they would result in one-time or annual incremental costs to NRSROs.

4. Other Amendments to Form NRSRO

The Commission is proposing a number of additional amendments to the Instructions to Form NRSRO to clarify certain requirements because the instructions, as written, have created some confusion among NRSROs. The Commission preliminarily estimates that these proposals would not result in any one-time or annual incremental costs to NRSROs as they would clarify existing requirements (not create new requirements). Furthermore, the Commission preliminarily believes these proposals would benefit NRSROs and Commission staff by addressing parts of the instructions that have led to inconsistent interpretations among the NRSROs as to the requirements.

The Commission preliminarily believes that the proposals would promote efficiency. As noted above, the proposals would be designed to promote greater clarity as to the requirements in the instructions. In addition, as discussed above, the Commission preliminarily estimates that the proposals would not result in any one-time or annual incremental costs to NRSROs and would have substantial benefits. Consequently, the Commission preliminarily believes that the proposals would not impact competition or impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

a. Clarification With Respect to Items 6 and 7

The Commission is proposing amendments to Form NRSRO and the Instructions for Form NRSRO to remove potential ambiguity as to how an applicant and NRSRO must determine the approximate number of credit ratings outstanding for the purposes of Items 6 and 7. In particular, the Commission is proposing to amend the text in Items 6.A and 7.A of Form NRSRO to clarify that an applicant or NRSRO must provide the approximate number of obligors, securities, and money market instruments in each class of credit ratings for which the applicant or NRSRO has an outstanding credit rating.[1323]

In addition, the Commission is proposing to amend Instruction H to Form NRSRO (as it relates to Items 6.A and 7.A) in four ways. First, in conformity with the proposed amendments to the text of Items 6.A and 7.A in the Form, the Instructions would be amended to provide that the applicant or NRSRO must, for each class of credit ratings, provide in the appropriate box the approximate number of obligors, securities, and money market instruments in that class for which the applicant or NRSRO presently has a credit rating outstanding as of the date of the application (Item 6.A) or had a credit rating outstanding as of the end of the most recently ended calendar year (Item 7.A).

Second, Instruction H would be amended to provide that the applicant or NRSRO must treat as a separately rated security or money market instrument each individually rated security and money market instrument that, for example, is assigned a distinct CUSIP or other unique identifier, has distinct credit enhancement features as compared with other securities or money market instruments of the same issuer, or has a different maturity date as compared with other securities or money market instruments of the same issuer. This proposed instruction would be designed to clarify that each security or money market instrument of an issuer must be included in the count if it is assigned a credit rating by the applicant or NRSRO.

Third, Instruction H would be amended to provide that the applicant or NRSRO must not include an obligor,

[1317] *See* Section II.M.1 of this release.

[1318] *See* Section 3(a)(62)(A) of the Exchange Act (15 U.S.C. 78c(a)(62)(A)) added by the Rating Agency Act of 2006.

[1319] The Dodd-Frank Act did not, however, amend Section 15E(a)(1)(C), which requires that the certifications from qualified institutional buyers that are required to be submitted with an application for registration as an NRSRO under Section 15E(a)(1)(B), include a representation that the qualified institutional buyer "has used the credit ratings of the applicant for at least the 3 years immediately preceding the date of the certification in the subject category or categories of obligors."

[1320] *See* Section II.M.2 of this release.

[1321] 15 U.S.C. 78c(a)(77).

[1322] *See* Section II.M.3 of this release.

[1323] *See* proposed amendments to the text in Items 6.A and 7.A respectively.

security, or money market instrument in more than one class of credit rating. In other words, the applicant or NRSRO cannot double count an obligor, security, or money market instrument by including it in total credit ratings outstanding for two or more classes. Fourth, Instruction H would be amended to provide that the applicant or NRSRO must include in the class of credit ratings described in Section 3(a)(62)(B)(iv) of the Exchange Act (issuers of asset-backed securities) to the extent not described in Section 3(a)(62)(B)(iv), any rated security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction. As discussed above in Section II.M.3 of this release, Section 3(a)(62)(B)(iv) contains a narrower definition of "asset-backed security" than the Commission uses for the purposes of its NRSRO rules.[1324]

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with these proposed amendments, including whether they would result in one-time or annual incremental costs to NRSROs.

b. Clarification With Respect to Exhibit 8

The Commission proposes to amend Instruction H to Form NRSRO as it relates to Exhibit 8. Exhibit 8 requires an applicant and NRSRO to provide the number of credit analysts it employs and the number of credit analyst supervisors. The Commission is proposing two amendments to the instructions for Exhibit 8. The first amendment would delete a parenthesis in the instructions that provides that the applicant or NRSRO should "see definition below" of the term "credit analyst." There is no such definition. The second amendment would clarify that the applicant or NRSRO, in providing the number of credit analysts, should include the number of credit analyst supervisors. This would be designed to ensure that the disclosures in Form NRSRO are comparable across NRSROs by avoiding the situation in which some NRSROs include credit analyst supervisors in the total number of credit analysts and some NRSROs do not include credit analyst supervisors in that amount.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with these proposed amendments, including whether they would result in one-time or annual incremental costs to NRSROs.

c. Clarification With Respect to Exhibits 10 through 13

The Commission proposes to amend Instruction H in several places to add a "Note" instructing that after registration, Exhibits 10 through 13 are not required to be made publicly available by the NRSRO pursuant to Rule 17g–1(i) and they should not be updated with the filing of the annual certification. The "Note" further would instruct that similar information is required in the annual reports that must be filed with the Commission not more than 90 days after the end of each fiscal year under Rule 17g–3.[1325]

The Commission preliminarily believes that none of these proposed clarifications entail any changes to the existing requirements of the Commission's rules, but instead merely explain more clearly what those rules already require. Therefore, Commission does not attribute any costs or benefits to these clarifications.

Request for Comment

The Commission requests comment on all aspects of the costs and benefits associated with these proposed amendments, including whether they would result in one-time or annual incremental costs to NRSROs.

VI. Consideration of Impact on the Economy

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, or "SBREFA," [1326] the Commission must advise OMB as to whether the proposed regulation constitutes a "major" rule. Under SBREFA, a rule is considered "major" where, if adopted, it results or is likely to result in: (1) An annual effect on the economy of $100 million or more (either in the form of an increase or a decrease); (2) a major increase in costs or prices for consumers or individual industries; or (3) 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 amendments to existing rules and proposed new rules on the economy on an annual basis, on the costs or prices for consumers or individual industries, and on competition, investment or innovation. Commenters are requested to provide empirical data and other factual support for their view to the extent possible.

VII. Initial Regulatory Flexibility Analysis

The Commission has prepared this Initial Regulatory Flexibility Analysis (IRFA) in accordance with Section 603(a) of the Regulatory Flexibility Act (RFA).[1327] This IRFA relates to the Commission's proposed new requirements for NRSROs that would result from the amendments to Rule 101 of Regulation S–T, Rule 201 of Regulation S–T, Rule 17g–1, Rule 17g–2, Rule 17g–3, Rule 17g–5, Rule 17g–6, Rule 17g–7, and Form NRSRO, and proposed new Rule 17g–8 and new Rule 17g–9. In addition, the IRFA relates to the Commission's proposed new requirements for providers of third-party due diligence services that would result from new Rule 17g–10 and new Form ABS Due Diligence–15E. Finally, this IRFA relates to the Commission's proposed new requirements for issuers and underwriters of Exchange Act-ABS that would result from the amendments to Rule 314 of Regulation S–T and Form ABS–15G, and new Rule 15Ga–2.

A. Reasons and Objectives

Section II of this release describes the reasons and objectives of the proposed amendments to existing rules and proposed new rules. In addition, Section IV.B of this release describes the intended use of the collection of information requirements that would result from the proposed amendments to existing rules and proposed new rules. Moreover, as described in Section II of this release, these proposed amendments and proposed new rules would implement rulemaking mandated in Title IX, Subtitle C of the Dodd-Frank Act.[1328] In Section 931 of Title IX, Subtitle C of the Dodd-Frank Act, Congress made the following findings:

- Because of the systemic importance of credit ratings and the reliance placed on credit ratings by individual and institutional investors and financial regulators, the activities and performances of credit rating agencies, including NRSROs, are matters of national public interest, as credit rating agencies are central to capital formation, investor confidence, and the efficient

[1324] *Compare* 15 U.S.C. 78c(a)(62)(B)(iv) with: Instructions for Exhibit 1 to Form NRSRO; paragraphs (a)(2)(iii), (a)(7), and (b)(9) of Rule 17g–2; paragraph (a)(6) of Rule 17g–3; paragraphs (a)(3) and (b)(9) of Rule 17g–5; and paragraph (a)(4) of Rule 17g–6.

[1325] *See* "Notes" proposed to be added to Instruction H to Form NRSRO.

[1326] Public Law 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).

[1327] *See* 5 U.S.C. 603(a).

[1328] *See* Public Law 111–203 §§ 931–939H.

performance of the United States economy.[1329]

• Credit rating agencies, including NRSROs, play a critical "gatekeeper" role in the debt market that is functionally similar to that of securities analysts, who evaluate the quality of securities in the equity market, and auditors, who review the financial statements of firms. Such role justifies a similar level of public oversight and accountability.[1330]

• Because credit rating agencies perform evaluative and analytical services on behalf of clients, much as other financial "gatekeepers" do, the activities of credit rating agencies are fundamentally commercial in character and should be subject to the same standards of liability and oversight as apply to auditors, securities analysts, and investment bankers.[1331]

• In certain activities, particularly in advising arrangers of structured financial products on potential ratings of such products, credit rating agencies face conflicts of interest that need to be carefully monitored and that therefore should be addressed explicitly in legislation in order to give clearer authority to the Securities and Exchange Commission.[1332]

• In the recent financial crisis, the ratings on structured financial products have proven to be inaccurate. This inaccuracy contributed significantly to the mismanagement of risks by financial institutions and investors, which in turn adversely impacted the health of the economy in the United States and around the world. Such inaccuracy necessitates increased accountability on the part of credit rating agencies.[1333]

B. Legal Basis

The Commission's proposed amendments to existing rules and proposed new rules are made pursuant to the Exchange Act,[1334] particularly Sections 15E, 17(a) and 36 of the Exchange Act,[1335] and Sections 936 and 938(a) of the Dodd-Frank Act.[1336]

C. Small Entities Subject to the Rule

1. NRSROs and Providers of Third-Party Due Diligence Services

Under section 601(3) of the RFA, the term "small business" is defined as having "the same meaning as the term 'small business concern' under Section 3 of the Small Business Act, unless an agency, after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition(s) in the **Federal Register**."[1337] The Commission's rules do not define "small business" or "small organization" with respect to NRSROs. However, paragraph (a) of Rule 0–10 provides that for purposes of the RFA, 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."[1338] The Commission has stated in the past that an NRSRO with total assets of $5 million or less would qualify as a "small" entity for purposes of the RFA.[1339] The Commission continues to believe this threshold of total assets of $5 million or less would qualify an NRSRO as "small" for purposes of the RFA. In addition, the Commission preliminarily believes this would be an appropriate threshold for determining whether a provider of third-party due diligence services is "small" for purposes of the RFA.

Currently, there are 10 NRSROs and, based on their most recently filed annual reports pursuant to Rule 17g–3, one NRSRO is a small entity under the above definition. For purposes of the PRA, the Commission preliminarily estimates that there will be 10 providers of third-party due diligence services subject to the proposed new requirements.[1340] Of these 10 respondents, the Commission estimates that all 10 would be "small" entities.

2. Issuers and Underwriters

The proposing release for Form ABS–15G certified that the form would not have a significant economic impact on a substantial number of small entities.[1341] As discussed above in Section V.I.2 of this release, the Commission believes that the costs to the issuers and underwriters subject to proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G would be less than those arising from the adoption of Form ABS–15G. The Commission, therefore, certifies pursuant to 5 U.S.C. 605(b) that proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G contained in this release, if adopted, would not have a significant economic impact on a substantial number of small entities. The proposals relate to disclosure requirements for Exchange Act-ABS. As noted above, Rule 0–10(a)[1342] defines an issuer, other than an investment company, to be a "small business" or "small organization" if it had total assets of $5 million or less on the last day of its most recent fiscal year. The Commission's data indicates that only one sponsor could meet the definition of a small broker-dealer for purposes of the Regulatory Flexibility Act.[1343] Accordingly, the Commission does not believe that proposed new Rule 15Ga–2 and the proposed amendments to Form ABS–15G, if adopted, would have a significant economic impact on a substantial number of small entities.

D. Reporting, Recordkeeping, and Other Compliance Requirements

The proposed amendments and proposed new rules would impose certain reporting, recordkeeping, and other compliance requirements on small NRSROs and small providers of third-party due diligence services. Preliminary estimates of the costs attributable to these proposals are discussed in detail in Section V of this release. As discussed in Section V of this release, the Commission preliminarily estimates that the costs are largely attributable to rulemaking mandates in the Dodd-Frank Act and not to the exercise of Commission discretionary rulemaking.

The Commission is providing summary information below about the preliminary cost estimates in Section V of this release to estimate the impact the proposals would have on the one small NRSRO and the 10 small providers of third-party due diligence services. In some cases, the Commission preliminarily believes it is appropriate to estimate the one-time and annual costs per small NRSRO using average costs across all NRSROs that would be subject to the proposed amendments and new rules. The NRSROs vary, in terms of size and complexity, from

[1329] Public Law 111–203 § 931(1).

[1330] Public Law 111–203 § 931(2).

[1331] Public Law 111–203 § 931(3).

[1332] Public Law 111–203 § 931(4).

[1333] Public Law 111–203 § 931(5).

[1334] 15 U.S.C. 78a *et seq.*

[1335] 15 U.S.C. 78o–7, 78q and 78mm.

[1336] Public Law 111–203 §§ 936 and 938(a).

[1337] 5 U.S.C. 601(3).

[1338] 17 CFR 240.0–10(a).

[1339] *See e.g., Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations,* 72 FR 33618 (June 18, 2007); *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 6481 (Feb. 9, 2009); and *Amendments to Rules for Nationally Recognized Statistical Rating Organizations,* 74 FR at 63863 (Dec. 4, 2009).

[1340] *See* Section VI.C of this release.

[1341] *See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act,* Securities Act Release No. 9148 (Oct. 4, 2010), 75 FR 62718 at 62734 (Oct. 13, 2010).

[1342] 17 CFR 240.0–10(a).

[1343] This is based on data from Asset-Backed Alert.

small entities that employ less than 20 credit analysts to complex global organizations that employ over a thousand credit analysts.[1344] Given the variance in size between the largest NRSROs and the smallest NRSROs, the average costs are skewed higher because the largest firms currently dominate in terms of size and the volume of credit rating activities.[1345] In other cases, as described below, the Commission preliminarily believes it is appropriate to estimate the one-time and annual costs per small NRSRO based on the number of credit ratings outstanding or the number of credit analysts employed by the seven smaller NRSROs.[1346] In a cost estimate based on the number of credit ratings outstanding, the Commission preliminarily proposes to use the number of credit ratings outstanding of the 7 smaller NRSROs.[1347] In a cost estimate based on the number of credit analysts, the Commission preliminarily proposes to use the number of credit analysts employed by the 7 smaller NRSROs.[1348]

As discussed above in Section V.A.2 of this release, the Commission preliminarily estimates that the proposed amendments to Rule 17g–3 would result in one-time and annual costs to NRSROs.[1349] In particular, the Commission preliminarily estimates that the proposal would result in an average one-time cost to each NRSRO of approximately $40,000 and an average annual cost to each NRSRO of approximately $60,950.[1350]

As discussed above in Section V.B.2 of this release, the Commission preliminarily estimates that the proposed amendments to Rule 17g–5 would result in one-time and annual costs to each NRSRO.[1351] Moreover, the Commission provides separate preliminary cost estimates for the three larger NRSROs and the seven smaller NRSROs. In particular, the Commission preliminarily estimates that the proposal would result in an average one-time cost to each of the seven smaller NRSROs of approximately $15,867 and an average annual cost to each of the seven smaller NRSROs of approximately $4,587.[1352]

As discussed above in Section V.C.2 of this release, the Commission preliminarily estimates proposed paragraph (c) to new Rule 17g–8 would result in one-time and annual costs to each NRSRO.[1353] In particular, the Commission preliminarily estimates that the proposal would result in an average one-time cost to each NRSRO of approximately $27,300 and an average annual cost to each NRSRO of approximately $6,825.[1354]

As discussed above in Section V.E.2 of this release, the Commission preliminarily estimates that the proposed amendments to the instructions to Exhibit 1 of Form NRSRO would result in one-time and annual costs to each NRSRO.[1355] Based on the total number of ratings outstanding across all 10 NRSROs, the Commission preliminarily estimates an industry-wide one-time cost of approximately $735,680 and an industry-wide annual cost of approximately $367,840.[1356] Moreover, because of the wide variance in the number of credit ratings outstanding among the NRSROs, the Commission preliminarily believes that it is appropriate to allocate these costs to NRSROs based on the number of credit ratings each has outstanding (although larger NRSROs may realize economies of scale). Consequently, the Commission preliminarily estimates that the proposal would result in an average one-time cost to the small NRSRO of approximately $2,913 and an average annual cost to the small NRSRO of approximately $1,457.[1357]

As discussed above in Section V.E.2 of this release, the Commission preliminarily estimates that the proposed amendments to Rule 17g–1 would result in one-time and annual costs to each NRSRO.[1358] First, the Commission preliminarily estimates that the proposal to require an NRSRO to it make its Form NRSRO and Exhibits 1 through 9 freely available on an "easily accessible" portion of its corporate Internet Web site would result in an average one-time cost to each NRSRO of approximately $1,125.[1359] Second, the Commission preliminarily estimates that the proposal to require an NRSRO to provide, when requested, a written copy of Exhibit 1 would result in an average one-time cost to each NRSRO of approximately $13,104 and an average annual cost to each NRSRO of approximately $18,291.[1360]

As discussed above in Section V.F.2 of this release, the Commission preliminarily estimates that proposed new paragraph (b) of Rule 17g–7 would result in one-time and annual costs to each NRSRO.[1361] First, the Commission preliminarily estimates that the proposal to make the ratings histories available on an "easily accessible" portion of the NRSRO's corporate Internet Web site would result in an average one-time cost to each NRSRO of approximately $1,125.[1362] Second, the Commission preliminarily estimates that the proposed enhancements to the current ratings history disclosure requirements would result in an average one-time cost to each NRSRO of approximately $30,375 and an average

[1344] *See, e.g., Annual Report on Nationally Recognized Statistical Rating Organizations. Commission* (Jan. 2011), pp. 4–9.

[1345] As discussed above in Section IV.D of this release, based on data collected from the NRSROs in their Form NRSROs and Rule 17g–3 annual reports, the Commission has calculated an HHI number using the number credit ratings outstanding per NRSRO and that number is 3,495, which is equivalent to there being approximately 2.86 equally sized firms. The HHI using earnings reported by NRSROs in the Rule 17g–3 annual reports is 3,926, which the equivalent of 2.55 equally sized firms.

[1346] The seven smaller NRSROs are: A.M. Best Company, Inc., DBRS Ltd., Egan-Jones Rating Company, Japan Credit Rating Agency, Ltd., Kroll Bond Rating Agency, Inc. (formerly LACE Financial Corp.), Rating and Investment Information, Inc., and Realpoint LLC. *See* Figures 2 and 3. The small NRSRO is one these NRSROs.

[1347] 80,648 (total credit ratings outstanding for the seven smaller NRSROs)/2,905,825 (total credit ratings outstanding for all ten NRSROs)/7 (the number of smaller NRSROs) = 0.00396. *See* Figure 2.

[1348] 370 (the total number of credit analysts employed by the seven smaller NRSROs)/3,520 (the total number of credit analysts employed by all ten NRSROs)/7 (the number of smaller NRSROs) = .01502. *See* Figure 3.

[1349] *See* proposed new paragraph (a)(7) and proposed amendments to paragraph (b) of Rule 17g–3; *see also* Section II.A.1 of this release for a more detailed discussion of these provisions.

[1350] *See* Section V.A.2 of this release for a more detailed discussion of the basis for these cost estimates.

[1351] *See* proposed new paragraph (c)(8) of Rule 17g–5; *see also* Section II.B.1 of this release for a more detailed discussion of this proposal.

[1352] *See* Section V.B.2 of this release for a more detailed discussion of the basis for these cost estimates.

[1353] *See* proposed paragraph (c) of new Rule 17g–8; *see also* Section II.C.1 of this release for a more detailed discussion of this proposal.

[1354] *See* Section V.C.2 of this release for a more detailed discussion of the basis for these cost estimates.

[1355] *See* proposed amendments to Instruction H to Form NRSRO (as it relates to Exhibit 1); *see also* Section II.E.1.a of this release for a more detailed discussion of this proposal.

[1356] *See* Section V.E.2 of this release for a more detailed discussion of the basis for these cost estimates.

[1357] $735,680 × .00396 = $2,913.29, rounded to $2,913; $367,840 × .00396 = $1,456.65, rounded to $1,457.

[1358] *See* proposed amendments to paragraph (i) of Rule 17g–1; *see also* Section II.E.1.b of this release for a more detailed discussion of this proposal.

[1359] *See* Section V.E.2 of this release for a more detailed discussion of the basis for this cost estimate.

[1360] *Id.*

[1361] *See* proposed new paragraph (b) of Rule 17g–7; *see also* Section II.E.2 of this release for a more detailed discussion of this proposal.

[1362] *See* Section V.F.2 of this release for a more detailed discussion of the basis for this cost estimate.

annual cost to each NRSRO of approximately $10,125.[1363]

As discussed above in Section V.G.2 of this release, the Commission preliminarily estimates that paragraph (a) of proposed new Rule 17g–8 would result in one-time and annual costs to each NRSRO.[1364] In particular, the Commission preliminarily estimates that the proposal would result in an average one-time cost to each NRSRO of approximately $54,600 and an average annual cost to each NRSRO of approximately $13,650.[1365]

As discussed above in Section V.H.2 of this release, the Commission preliminarily estimates that proposed new paragraph (a) of Rule 17g–7 would result in one-time and annual costs to each NRSRO.[1366] Based on the total number of ratings outstanding across all 10 NRSROs, the Commission preliminarily estimates an industry-wide one-time cost of approximately $15,237,500 and an industry-wide annual cost of approximately $115,580,930.[1367] Moreover, the Commission preliminarily estimates that the one-time and annual costs would vary considerably among NRSROs based on the number of credit ratings they issue and monitor and the number of classes and subclasses of credit ratings for which they issue and monitor credit ratings. Consequently, the Commission preliminarily estimates that the proposal would result in an average one-time cost to the small NRSRO of approximately $60,340 and an average annual cost to the small NRSRO of approximately $457,700.[1368]

As discussed above in Section V.K.2 of this release, the Commission preliminarily estimates that proposed new Rule 17g–9 would result in one-time and annual costs to each NRSRO.[1369] Based on the total number of credit rating analysts employed by the 10 NRSROs, the Commission preliminarily estimates an industry-wide one-time cost of approximately $5,363,000 and an industry-wide annual cost of approximately $1,072,720.[1370] Moreover, the Commission preliminarily estimates that these costs would be allocated to the 10 NRSROs based on the number of credit analysts each employs. Consequently, the Commission preliminarily estimates that the proposal would result in an average one-time cost to the small NRSRO of approximately $80,552 and an average annual cost to the small NRSRO of approximately $16,112.[1371]

As discussed above in Section V.L.2 of this release, the Commission preliminarily estimates that paragraph (b) of proposed new Rule 17g–8 would result in one-time and annual costs to each NRSRO.[1372] In particular, the Commission preliminarily estimates that the proposal would result in an average one-time cost to each NRSRO of approximately $54,600 and an average annual cost to each NRSRO of approximately $13,650.[1373]

As discussed above in Section V.N.2 of this release, the Commission preliminarily estimates that proposed requirement to file certain Form NRSROs (and Exhibits 1 through 9) and the Rule 17g–3 annual reports with the Commission through the EDGAR system would result in one-time costs to each NRSRO.[1374] In particular, the Commission preliminarily estimates that the proposal would result in an average one-time cost to each NRSRO of approximately $1,365.[1375]

As discussed above in Sections V.A.2, V.C.2, V.G.2, V.K.2, and V.L.2 of this release, the Commission has proposed applying the recordkeeping requirements of Rule 17g–2 to five new types of records.[1376] The Commission preliminarily estimates that these proposals would result in one-time and annual costs to each NRSRO. In particular, the Commission preliminarily estimates an average one-time cost to each NRSRO of approximately $5,460 and an average annual cost to each NRSRO of approximately $1,365.[1377]

Finally, as discussed in Section V.J.2 of this release, the Commission preliminarily estimates that proposed new Rule 17g×10 and proposed new Form ABS Due Diligence-15E would result in one-time and annual costs to providers of third-party due diligence services.[1378] In particular, the Commission estimates an average one-time cost to each provider of third-party due diligence services of approximately $91,425.[1379] In addition, the Commission preliminarily estimates that the annual cost resulting from these proposals would be based on the number of Exchange Act-ABS transactions issued per year. Consequently, the Commission preliminarily estimates that the industry-wide annual cost would be approximately $282,282.[1380] For this reason, the Commission preliminarily estimates that the average annual cost to each provider of third-party due diligence services would be approximately $28,228.[1381]

As noted above, the Commission preliminarily estimates that these costs largely are attributable to rulemaking mandates in the Dodd-Frank Act. The Commission also notes that the Dodd-Frank Act explicitly provides that the Commission's rulemaking make exceptions for small NRSROs in one instance.[1382] The Commission preliminary believes that the exercise of the Commission's discretionary rulemaking would not disproportionately affect small entities. The Commission preliminarily believes that the exercise of discretionary rulemaking strikes an appropriate balance between minimizing the burden on small entities and meeting the rulemaking mandates in the Dodd-Frank Act.

[1363] *See* Section V.F.2 of this release for a more detailed discussion of the basis for these cost estimates.

[1364] *See* paragraph (a) of new Rule 17g–8; *see also* Section II.F.1 of this release for a more detailed discussion of this proposal.

[1365] *See* Section V.G.2 of this release for a more detailed discussion of the basis for these cost estimates.

[1366] *See* proposed new paragraph (a) of Rule 17g–7 *see also* Sections II.G.1 through G.5 of this release for a more detailed discussion of this proposal.

[1367] *See* Section V.H.2 of this release for a more detailed discussion of the basis for these cost estimates.

[1368] $15,237,500 × .00396 = $60,340.50, rounded to $60,340; $115,580,930 × .00396 = $457,700.48, rounded to $457,700.

[1369] *See* proposed new Rule 17g–9; *see also* Section II.I.1 of this release for a more detailed discussion of this proposal.

[1370] *See* Section V.K.2 of this release for a more detailed discussion of the basis for these cost estimates.

[1371] $5,363,000 x .01502 = $80,552.26, rounded to $80,552; $1,072,720 x .01502 = $16,112.25, rounded to $16,112..

[1372] *See* paragraph (b) of proposed new Rule 17g–8; *see also* Section II.J.1 of this release for a more detailed discussion of this proposal.

[1373] *See* Section V.L.2 of this release for a more detailed discussion of the basis for these cost estimates.

[1374] *See* proposed amendments to Regulation S–T, Rule 17g–1, and Rule 17g–3; *see also* Section II.L of this release for a more detailed discussion of this proposal.

[1375] *See* Section V.N.2 of this release for a more detailed discussion of the basis for this cost estimate.

[1376] *See* proposed new paragraphs (a)(9), (b)(12), (b)(13), (b)(14), and (b)(15) of Rule 17g–2; *see also* Sections II.A.2, II.C.2, II.F.2, II.I.2, and II.J.2 of this release, respectively, for a more detailed discussion of these proposals.

[1377] $1,092 × 5 = $5,460; $273 × 5 = $1,365. *See* Sections V.A.2, V.C.2, V.G.2, V.K.2, and V.L.2 of this release for a more detailed discussion of the basis for these cost estimates.

[1378] *See* proposed new Rule 17g–10 and proposed new Form ABS Due Diligence-15E; *see also* Sections II.H.2 and II.H.3 of this release, respectively, for a more detailed discussion of these proposals.

[1379] *See* Section V.J.2 of this release for a more detailed discussion of the basis for this cost estimate.

[1380] *Id.*

[1381] $282,282/10 small providers of third-party due diligence services = $28,228.20 (rounded to $28,228).

[1382] *See* Public Law 111–203 § 932(a)(4) and 15 U.S.C. 78o–7(h)(3)(B)(i).

E. Duplicative, Overlapping, or Conflicting Federal Rules

The Commission believes that there are no Federal rules that duplicate, overlap, or conflict with the proposed rules.

F. Significant Alternatives

Pursuant to Section 3(a) of the RFA,[1383] the Commission must consider certain types of alternatives, including: (1) The establishment of differing compliance or recording 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 proposed rules for small entities; (3) the use of performance rather than design standards; and (4) an exemption from coverage of the proposed rules, or any part of the proposed rules, for small entities.

The Commission preliminarily believes that the exercise of discretionary rulemaking with respect to the proposed amendments to existing rules and proposed new rules strike the appropriate balance between minimizing the burden on entities and allowing the Commission to meet its mandate under the Dodd-Frank Act. The Commission notes the Dodd-Frank Act explicitly mandated the Commission provide for exceptions for small NRSROs with respect to only one rulemaking and the Commission has proposed a rule amendment to implement this provision.[1384] Consequently, the Commission does not believe it is necessary or appropriate to establish different compliance or reporting requirements or timetables; clarify, consolidate, or simplify compliance and reporting requirements under the proposed amendments to existing rules and proposed new rules for small entities; or summarily exempt small entities from coverage of the rule, or any part of the rule. The Commission believes that it is inconsistent with the goals of the Dodd-Frank Act to use performance standards rather than design standards. Further, the Commission believes that it would be inconsistent with the purposes of the Dodd-Frank Act to exempt small entities from compliance with the proposed rules.

G. Request for Comment

The Commission generally requests comment on the certification and all aspects of its analysis in the IRFA. In addition, the Commission also seeks comment on the following:

1. Would the number of small entities that would be subject to the proposed requirements have any effects that have not been discussed?

2. Describe the nature of any effects on small entities subject to proposed requirements and provide empirical data to support the nature and extent of such effects.

3. Describe the compliance burdens and how they would affect small entities.

VIII. Statutory Authority

The Commission is proposing amendments to §§ 232.101, 232.201, 232.314, 240.17g–1, 240.17g–2, 240.17g–3, 240.17g–5, 240.17g–6, 240.17g–7, Form NRSRO, and Form ABS–15G and is proposing to adopt §§ 240.15Ga–2, 240.17g–8, 240.17g–9, 240.17g–10, and Form ABS Due Diligence-15E pursuant to the authority conferred by the Exchange Act, including Sections 15E, 17(a) and 36 (15 U.S.C. 78o–7, 78q, and 78mm), and pursuant to authority in Sections 936, 938, and 943 of the Dodd-Frank Act (Pub. L. 111–203 §§ 936, 938, and 943).

List of Subjects in 17 CFR Parts 232, 240, 249, and 249b

Brokers, Reporting and recordkeeping requirements, Securities.

Text of Proposed Rules

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

PART 232—REGULATION S–T—GENERAL RULES AND REGULATIONS FOR ELECTRONIC FILINGS

1. The authority citation for part 232 continues to read, in part, as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s(a), 77z–3, 77sss(a), 78c(b), 78*l,* 78m, 78n, 78o(d), 78w(a), 78*ll,* 80a–6(c), 80a–8, 80a–29, 80a–30, 80a–37, and 7201 *et seq.;* and 18 U.S.C. 1350.

* * * * *

2. Section 232.101 is amended by adding paragraph (a)(1)(xiv) to read as follows:

§ 232.101 Mandated electronic submissions and exceptions.

(a) * * *

(1) * * *

(xiv) Form NRSRO (§ 249b.300 of this chapter), and the information and documents in Exhibits 1 through 9 of Form NRSRO, filed with or furnished, as applicable, to the Commission pursuant to § 240.17g–1(e), (f), and (g) of this chapter and the annual reports filed with or furnished to, as applicable, the Commission pursuant to § 240.17g–3 of this chapter.

* * * * *

3. Section 232.201 is amended by revising paragraph (a) introductory text to read as follows:

§ 232.201 Temporary hardship exemption.

(a) If an electronic filer experiences unanticipated technical difficulties preventing the timely preparation and submission of an electronic filing other than a Form 3 (§ 249.103 of this chapter), a Form 4 (§ 249.104 of this chapter), a Form 5 (§ 249.105 of this chapter), a Form ID (§§ 239.63, 249.446, 269.7, and 274.402 of this chapter), a Form TA–1 (§ 249.100 of this chapter), a Form TA–2 (§ 249.102 of this chapter), a Form TA–W (§ 249.101 of this chapter), a Form D (§ 239.500 of this chapter), an application for an order under any section of the Investment Company Act (15 U.S.C. 80a–1 *et seq.*), an Interactive Data File (§ 232.11 of this chapter), or a Form NRSRO (§ 249b.300 of this chapter), and the information and documents in Exhibits 1 through 9 of Form NRSRO, filed with or furnished to, as applicable, the Commission pursuant to § 240.17g–1(e), (f), or (g) of this chapter, or the annual reports filed with or furnished to, as applicable, the Commission pursuant to § 240.17g–3 of this chapter, the electronic filer may file the subject filing, under cover of Form TH (§§ 239.65, 249.447, 269.10, and 274.404 of this chapter), in paper format no later than one business day after the date on which the filing was to be made.

* * * * *

4. Section 232.314 is amended by:

a. In the introductory text adding the phrase "or in response to Rule 15Ga–2 (§ 240.15Ga–2 of this chapter)" after the phrase "The information required in response to Rule 15Ga-1 (§ 240.15Ga–1 of this chapter)";

b. In paragraph (a), removing the words "Securities Exchange Act of 1934" and in their place inserting the word "Act"; and

c. In paragraph (b):

i. Adding the words "or Rule 15Ga–2" after the phrase "The information required by Rule 15Ga–1"; and

ii. Removing the words "Web site" and in their place inserting the word "website".

[1383] 5 U.S.C. 603(c).

[1384] *See* 15 U.S.C. 78o–7(h)(3)(B)(i) and proposed new paragraph (f) of Rule 17g–5; *see also* Section II.B.2 of this release for a more detailed discussion of this proposal.

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

5. The authority citation for part 240 is amended by adding sectional authorities for §§ 240.15Ga–2, 240.17g–8, and 240.17g–9 to read 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, 78*l,* 78m, 78n, 78n–1, 78o, 78o–4, 78p, 78q, 78s, 78u–5, 78w, 78x, 78*ll,* 78mm, 80a–20, 80a–23, 80a–29, 80a–37, 80b–3, 80b–4, 80b–11, and 7201 *et. seq.;* 18 U.S.C. 1350; and 12 U.S.C. 5221(e)(3) unless otherwise noted.

* * * * *

Section 240.15Ga–2 is also issued under sec. 943, Public Law 111–203, 124 Stat. 1376.

* * * * *

Section 240.17g–8 is also issued under sec. 938, Public Law 111–203, 124 Stat. 1376.

* * * * *

Section 240.17g–9 is also issued under sec. 936, Public Law 111–203, 124 Stat. 1376.

* * * * *

6. Section 240.15Ga–2 is added to read as follows:

§ 240.15Ga–2 Findings and conclusions of third-party due diligence reports.

(a) The issuer or underwriter of an offering of any asset-backed security (as that term is defined in Section 3(a)(77) of the Act (15 U.S.C. 78c(a)(77)) shall furnish Form ABS–15G (§ 249.1400 of this chapter) if the security is to be rated by a nationally recognized statistical rating organization, containing the findings and conclusions of any third-party due diligence report obtained by the issuer or underwriter five business days prior to the first sale in the offering; however, if the issuer or underwriter receives a representation from a nationally recognized statistical rating organization that can be reasonably relied upon that the disclosure required by this paragraph will be publicly disclosed by the nationally recognized statistical rating organization five business days prior to the first sale in the offering in an information disclosure form generated pursuant to Rule 17g–7(a)(1) (§ 240.17g–7(a)(1) of this chapter) and included with the credit rating, the issuer or underwriter would not be required to furnish Form ABS–15G five days prior to the first sale in the offering.

(b) If the issuer or underwriter receives a representation pursuant to paragraph (a) of this section, but the nationally recognized statistical rating organization has not fulfilled its representation to publicly disclose the disclosure five business days prior to the first sale in the offering, the issuer or underwriter shall furnish Form ABS–15G two business days prior to the first sale in the offering.

(c) For purposes of paragraph (a) of this section, "third-party due diligence report" means any report containing findings and conclusions of any "due diligence services" as defined in Rule 17g–10(c)(1) (§ 240.17g–10(c)(1) of this chapter) performed by a third party.

Instruction to paragraph (a) of this section: The issuer or underwriter shall provide to the Commission, upon request, information regarding the manner in which the representation by the nationally recognized statistical rating organization was obtained and relied upon for purposes of this paragraph.

7. Section 240.17g–1 is amended by:

a. In paragraphs (a), (b), and (c) removing the phase "furnish the Commission with" wherever it appears and adding in its place the phrase "file with the Commission two paper copies of";

b. In paragraph (d), adding the phrase "two paper copies of" after the phrase "the applicant must furnish the Commission with"; and

c. Revising paragraphs (e), (f), (g), (h), and (i).

The revisions read as follows:

§ 240.17g–1 Application for registration as a nationally recognized statistical rating organization.

* * * * *

(e) *Update of registration.* A nationally recognized statistical rating organization amending materially inaccurate information in its application for registration pursuant to section 15E(b)(1) of the Act (15 U.S.C. 78o–7(b)(1)) must promptly file with the Commission an update of its registration on Form NRSRO that follows all applicable instructions for the Form. A Form NRSRO and the information and documents in Exhibits 1 through 9 of Form NRSRO filed under this paragraph must be filed electronically with the Commission in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T.

(f) *Annual certification.* A nationally recognized statistical rating organization amending its application for registration pursuant to section 15E(b)(2) of the Act (15 U.S.C. 78o–7(b)(2)) must file with the Commission an annual certification on Form NRSRO that follows all applicable instructions for the Form not later than 90 days after the end of each calendar year. A Form NRSRO and the information and documents in Exhibits 1 through 9 of Form NRSRO filed under this paragraph must be filed electronically with the Commission in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T.

(g) *Withdrawal from registration.* A nationally recognized statistical rating organization withdrawing from registration pursuant to section 15E(e)(1) of the Act (15 U.S.C. 78o–7(e)(1)) must furnish the Commission with a notice of withdrawal from registration on Form NRSRO that follows all applicable instructions for the Form. The withdrawal from registration will become effective 45 calendar days after the notice is furnished to the Commission upon such terms and conditions as the Commission may establish as necessary in the public interest or for the protection of investors. A Form NRSRO furnished under this paragraph must be furnished electronically with the Commission in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T.

(h) *Filing or furnishing Form NRSRO.* A Form NRSRO filed or furnished, as applicable, under any paragraph of this section will be considered filed with or furnished to, as applicable, the Commission on the date the Commission receives a complete and properly executed Form NRSRO that follows all applicable instructions for the Form. Information filed or furnished, as applicable, on a confidential basis and for which confidential treatment has been requested pursuant to applicable Commission rules will be accorded confidential treatment to the extent permitted by law.

(i) *Public availability of Form NRSRO.* A nationally recognized statistical rating organization must make its current Form NRSRO and information and documents in Exhibits 1 through 9 to Form NRSRO publicly and freely available on an easily accessible portion of its corporate Internet Web site within 10 business days after the date of the Commission order granting an initial application for registration as a nationally recognized statistical rating organization or an application to register for an additional class of credit ratings and within 10 business days after filing with or furnishing to, as applicable, the Commission a Form NRSRO under paragraphs (e), (f), or (g) of this section. In addition, a nationally recognized statistical rating organization must make its up-to-date Exhibit 1 to Form NRSRO freely available in writing to any individual who requests a copy of the Exhibit.

8. Section 240.17g–2 is amended by:

a. In paragraphs (a)(2)(iii) and (a)(7) introductory text, removing the words "or mortgage-backed";

b. Adding paragraph (a)(9);

c. Revising paragraph (b)(1);

d. In paragraph (b)(9), removing the words "or mortgage-backed";

e. Revising paragraph (b)(11);

f. Adding paragraphs (b)(12) through (15);

g. Re-designating paragraph (d)(1) as paragraph (d); and

h. Removing paragraphs (d)(2) and (d)(3);

The additions and revisions read as follows:

§ 240.17g–2 Records to be made and retained by nationally recognized statistical rating organizations.

(a) * * *

(9) A record documenting the policies and procedures the nationally recognized statistical rating organization is required to establish, maintain, and enforce pursuant to Section 15E(h)(4)(A) of the Act (15 U.S.C. 78o–7(h)(4)(A)) and § 240.17g–8(c) of this chapter.

* * * * *

(b) * * *

(1) Significant records (for example, bank statements, invoices, and trial balances) underlying the information included in the annual financial reports the nationally recognized statistical rating organization files with or furnishes to, as applicable, the Commission pursuant to § 240.17g–3 of this chapter.

* * * * *

(11) Form NRSROs (including Exhibits and accompanying information and documents) the nationally recognized statistical rating organization files with or furnishes to, as applicable, the Commission.

(12) The internal control structure the nationally recognized statistical rating organization is required to establish, maintain, enforce, and document pursuant to Section 15E(c)(3)(A) of the Act (15 U.S.C. 78o–7(c)(3)(A)).

(13) The policies and procedures the nationally recognized statistical rating organization is required to establish, maintain, enforce, and document pursuant to § 240.17g–8(a) of this chapter.

(14) The policies and procedures the nationally recognized statistical rating organization is required to establish, maintain, enforce, and document pursuant to § 240.17g–8(b) of this chapter.

(15) The standards of training, experience, and competence for credit analysts the nationally recognized statistical rating organization is required to establish, maintain, enforce, and document pursuant to § 240.17g–9 of this chapter.

* * * * *

9. Section 240.17g–3 is amended by:

a. Revising the heading;

b. Revising the introductory text of paragraph (a);

c. In paragraph (a)(1) introductory text, removing the first word "Audited" and adding in its place the phrase "File with the Commission a financial report, as of the end of the fiscal year, containing audited";

d. In paragraph (a)(2) introductory text, removing the first word "If" and adding in its place the phrase "File with the Commission a financial report, as of the end of the fiscal year, containing, if";

e. In the Note to paragraph (a)(2), removing the word "furnished" and adding in its place the word "filed";

f. In the introductory texts to paragraphs (a)(3), (4), and (5), removing the first word "An" and adding in its place the phrase "File with the Commission an unaudited financial report, as of the end of the fiscal year,";

g. In paragraph (a)(6) introductory text, removing the first word "An" and adding in its place the phrase "Furnish the Commission with an unaudited report, as of the end of the fiscal year,";

h. In the Note to paragraph (a)(6), removing the words "or mortgage-backed";

i. Adding paragraphs (a)(7) and (8);

j. Revising paragraph (b);

k. Adding paragraphs (d) and (e).

The additions and revisions read as follows:

§ 240.17g–3 Annual financial and other reports to be filed or furnished by nationally recognized statistical rating organizations.

(a) A nationally recognized statistical rating organization must annually, not more than 90 calendar days after the end of its fiscal year (as indicated on its current Form NRSRO):

* * * * *

(7) File with the Commission an unaudited report, as of the end of the fiscal year, concerning the internal control structure the nationally recognized statistical rating organization is required to establish, maintain, enforce, and document pursuant to Section 15E(c)(3)(A) of the Act (15 U.S.C. 78o–7(c)(3)(A)) that contains:

(i) A description of the responsibility of management in establishing and maintaining an effective internal control structure; and

(ii) An assessment by management of the effectiveness of the internal control structure.

(8) File with the Commission an unaudited annual report on the compliance of the nationally recognized statistical rating organization with the securities laws and the policies and procedures of the nationally recognized statistical rating organization pursuant to Section 15E(j)(5)(B) of the Act (15 U.S.C. 78o–7(j)(5)(B)).

(b) The nationally recognized statistical rating organization must:

(1) Attach to the reports filed or furnished, as applicable, pursuant to paragraphs (a)(1) through (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 reports and, to the best knowledge of the person, the 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 filed pursuant to paragraph (a)(7) of this section a signed statement by the chief executive officer of the nationally recognized statistical rating organization or, if the nationally recognized statistical rating organization does not have a chief executive officer, an individual performing similar functions, stating that the chief executive officer or individual has responsibility for the report and, to the best knowledge of the chief executive officer or other individual, the report fairly presents, in all material respects, a description of the responsibility of management in establishing and maintaining an effective internal control structure and an assessment of the effectiveness of the internal control structure.

* * * * *

(d) Electronic Filing. The reports must be filed with or furnished to, as applicable, the Commission electronically in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T.

(e) Confidential Treatment. Information in a report filed or furnished, as applicable, on a confidential basis and for which confidential treatment has been requested pursuant to applicable Commission rules will be accorded confidential treatment to the extent permitted by law. Confidential treatment may be requested by marking each page "Confidential Treatment Requested" and by complying with Commission rules governing confidential treatment.

10. Section 240.17g–5 is amended by:

a. In paragraph (a)(3) introductory text, removing the words "or mortgaged-backed";

b. In paragraphs (a)(3)(i), (a)(3)(ii) introductory text, (a)(3)(iii)(A), (a)(3)(iii)(B) introductory text, (a)(3)(iii)(C), and (a)(3)(iii)(D), removing the words "Web site" and adding in their place the word "Web site";

c. In paragraph (b)(9), removing the words "or mortgaged-backed";

d. In paragraph (c)(6), removing the word "or" at the end of the paragraph after the semicolon;

e. In paragraph (c)(7), removing the period and adding "; or" at the end of the paragraph;

f. Adding paragraph (c)(8);

g. In paragraph (e), removing the words "Web site" and adding in their place the word "website" and removing the words "Web sites" and adding in their place the word "websites" wherever it occurs; and

h. Adding paragraphs (f) and (g).

The additions read as follows:

§ 240.17g–5 Conflicts of interest.

* * * * *

(c) * * *

(8) The nationally recognized statistical rating organization issues or maintains a credit rating where a person within the nationally recognized statistical rating organization who participates in sales or marketing of a product or service of the nationally recognized statistical rating organization or a product or service of a person associated with the nationally recognized statistical rating organization also participates in determining or monitoring the credit rating, or developing or approving procedures or methodologies used for determining the credit rating, including qualitative or quantitative models.

* * * * *

(f) Upon written application by a nationally recognized statistical rating organization, the Commission may exempt, either conditionally or unconditionally or on specified terms and conditions, such nationally recognized statistical rating organization from the provisions of paragraph (c)(8) of this section if the Commission finds that due to the small size of the nationally recognized statistical rating organization it is not appropriate to require the separation within the nationally recognized statistical rating organization of the production of credit ratings from sales and marketing activities and such exemption is in the public interest.

(g) In a proceeding pursuant to Section 15E(d) of the Act (15 U.S.C. 78o–7(d)) or Section 21C of the Act (15 U.S.C. 78u–3), the Commission shall suspend or revoke the registration of a nationally recognized statistical rating organization if the Commission finds in such proceeding that the nationally recognized statistical rating organization has violated a rule issued under Section 15E(h) of the Act (15 U.S.C. 78o–7(h)), that the violation affected a rating, and that suspension or revocation is necessary for the protection of investors and in the public interest.

§ 240.17g–6 [Amended]

11. Section 240.17g–6 is amended in paragraph (a)(4) by removing the words "or mortgage-backed".

12. Section 240.17g–7 is revised to read as follows:

§ 240.17g–7 Disclosure requirements.

(a) *Disclosures to be made when taking a rating action.* A nationally recognized statistical rating organization must publish the items described in paragraphs (a)(1) and (2) of this section, as applicable, when taking a rating action with respect to a credit rating assigned to an obligor, security, or money market instrument in a class of credit ratings for which the nationally recognized statistical rating organization is registered. For purposes of this section, the term "rating action" means any of the following: the publication of an expected or preliminary credit rating assigned to an obligor, security, or money market instrument before the publication of an initial credit rating; an initial credit rating; an upgrade or downgrade of an existing credit rating (including a downgrade to, or assignment of, default); a placement of an existing credit rating on credit watch or review; an affirmation of an existing credit rating; and a withdrawal of an existing credit rating. The items described in paragraphs (a)(1) and (a)(2) of this section must be published in the same medium and made available to the same persons who can receive or access the credit rating that is the result of the rating action or that is the subject of the rating action.

(1) *Information disclosure form.* A form generated by the nationally recognized statistical rating organization that meets the requirements of paragraphs (a)(1)(i), (ii), and (iii) of this section.

(i) *Format.* The form generated by the nationally recognized statistical rating organization must be in a format that:

(A) Is easy to use and helpful for users of credit ratings to understand the information contained in the form; and

(B) Provides the content described in paragraphs (a)(1)(ii)(K), (L), and (M) of this section in a manner that is directly comparable across types of obligors, securities, and money market instruments.

(ii) *Content.* The form generated by the nationally recognized statistical rating organization must contain the following information about the credit rating:

(A) The symbol, number, or score in the rating scale used by the nationally recognized statistical rating organization to denote credit rating categories and notches within categories assigned to the obligor, security, or money market instrument that is the subject of the credit rating and the identity of the obligor, security, or money market instrument;

(B) The version of the procedure or methodology used to determine the credit rating;

(C) The main assumptions and principles used in constructing the procedures and methodologies used to determine the credit rating, including qualitative methodologies and quantitative inputs and, if the credit rating is for a structured finance product, assumptions about the correlation of defaults across the underlying assets;

(D) The potential limitations of the credit rating, including the types of risks excluded from the credit rating that the nationally recognized statistical rating organization does not comment on, including, as applicable, liquidity, market, and other risks;

(E) Information on the uncertainty of the credit rating, including:

(*1*) Information on the reliability, accuracy, and quality of the data relied on in determining the credit rating; and

(*2*) A statement relating to the extent to which data essential to the determination of the credit rating were reliable or limited, including:

(*i*) Any limits on the scope of historical data; and

(*ii*) Any limits on accessibility to certain documents or other types of information that would have better informed the credit rating;

(F) Whether and to what extent third-party due diligence services were used by the nationally recognized statistical rating organization, a description of the information that such third party reviewed in conducting due diligence services, and a description of the findings or conclusions of such third party;

(G) If applicable, how servicer or remittance reports were used, and with what frequency, to conduct surveillance of the credit rating;

(H) A description of the data about any obligor, issuer, security, or money market instrument that were relied upon

for the purpose of determining the credit rating;

(I) A statement containing an overall assessment of the quality of information available and considered in determining the credit rating for the obligor, security, or money market instrument, in relation to the quality of information available to the nationally recognized statistical rating organization in rating similar obligors, securities, or money market instruments;

(J) Information relating to conflicts of interest of the nationally recognized statistical rating organization, which must include:

(*1*) A classification of the credit rating as either:

(*i*) "Solicited sell-side," meaning the credit rating was paid for by the obligor being rated or the issuer, underwriter, depositor, or sponsor of the security or money market instrument being rated;

(*ii*) "Solicited buy-side," meaning the credit rating was paid for by a person other than the obligor being rated or the issuer, underwriter, depositor, or sponsor of the security or money market instrument being rated; or

(*iii*) "Unsolicited," meaning the nationally recognized statistical rating organization was not paid to determine the credit rating;

(*2*) If the credit rating is classified as either "solicited sell-side" or "solicited buy-side" under paragraph (a)(1)(ii)(J)(*1*) of this section, disclosure of whether the nationally recognized statistical rating organization provided services other than determining credit ratings to the person that paid for the rating during the most recently ended fiscal year; and

(*3*) If the rating action results from a review conducted pursuant to Section 15E(h)(4)(A) of the Act (15 U.S.C. 78o–7(h)(4)(A)) and § 240.17g–8(c) of this chapter, provide the following information (as applicable):

(*i*) If the rating action is a placement of the credit rating on credit watch pursuant to § 240.17g–8(c)(1) of this chapter, an explanation that the reason for the action is the discovery that a credit rating assigned to the obligor, security, or money market instrument in one or more prior rating actions was influenced by a conflict of interest and the date and associated credit rating of each prior rating action that the nationally recognized statistical rating organization currently has determined was influenced by the conflict;

(*ii*) If the rating action is a revision of the credit rating pursuant to § 240.17g–8(c)(3)(i) of this chapter, an explanation that the reason for the action is the discovery that a credit rating assigned to the obligor, security, or money market instrument in one or more prior rating actions was influenced by a conflict of interest, the date and associated credit rating of each prior rating action the nationally recognized statistical rating organization has determined was influenced by the conflict, and an estimate of the impact the conflict had on each such prior rating action;

(*iii*) If the rating action is an affirmation of the credit rating pursuant to § 240.17g–8(c)(3)(ii) of this chapter, an explanation of why no rating action was taken to revise the credit rating notwithstanding the conflict, the date and associated credit rating of each prior rating action the nationally recognized statistical rating organization has determined was influenced by the conflict, and an estimate of the impact the conflict had on each such prior rating action.

(K) An explanation or measure of the potential volatility of the credit rating, including:

(*1*) Any factors that might lead to a change in the credit rating; and

(*2*) The magnitude of the change that could occur under different market conditions;

(L) Information on the content of the credit rating, including:

(*1*) If applicable, the historical performance of the credit rating; and

(*2*) The expected probability of default and the expected loss in the event of default;

(M) Information on the sensitivity of the credit rating to assumptions made by the nationally recognized statistical rating organization, including:

(*1*) Five assumptions made in the ratings process that, without accounting for any other factor, would have the greatest impact on a rating if the assumptions were proven false or inaccurate; and

(*2*) An analysis, using specific examples, of how each of the five assumptions identified in paragraph (a)(1)(ii)(M)(*1*) of this section impacts a rating;

(N) If the credit rating is issued with respect to an asset-backed security, as defined in Section 3(a)(77) of the Act (15 U.S.C. 78c(a)(77)), a description of:

(*1*) The representations, warranties, and enforcement mechanisms available to investors; and

(*2*) How they differ from the representations, warranties, and enforcement mechanisms in issuances of similar securities.

(iii) *Attestation.* The nationally recognized statistical rating organization must attach to the form a signed statement by a person within the nationally recognized statistical rating organization stating that the person has responsibility for the rating action and, to the best knowledge of the person:

(A) No part of the credit rating was influenced by any other business activities;

(B) The credit rating was based solely upon the merits of the obligor, security, or money market instrument being rated; and

(C) The credit rating was an independent evaluation of the risks and merits of the obligor, security, or money market instrument.

(2) *Third-party due diligence certification.* Any written certification related to the credit rating received by the nationally recognized statistical rating organization from a provider of third-party due diligence services pursuant to Section 15E(s)(4)(B) of the Act (15 U.S.C. 78o–7(s)(4)(B)).

(b) *Disclosure of credit rating histories.* (1) *Credit ratings subject to the disclosure requirement.* A nationally recognized statistical rating organization must publicly disclose for free on an easily accessible portion of its corporate Internet Web site:

(i) Each credit rating assigned to an obligor, security, and money market instrument in every class of credit ratings for which the nationally recognized statistical rating organization is registered that was outstanding as of June 26, 2007, and any subsequent upgrades or downgrades of a credit rating assigned to the obligor, security, or money market instrument (including a downgrade to, or assignment of, default), any placements of a credit rating assigned to the obligor, security, or money market instrument on credit watch or review, any affirmation of a credit rating assigned to the obligor, security, or money market instrument, and a withdrawal of a credit rating assigned to the obligor, security, or money market instrument; and

(ii) Each credit rating assigned to an obligor, security, and money market instrument in every class of credit ratings for which the nationally recognized statistical rating organization is registered that was initially determined on or after June 26, 2007 and any subsequent upgrades or downgrades of a credit rating assigned to the obligor, security, or money market instrument (including a downgrade to, or assignment of, default), any placements of a credit rating assigned to the obligor, security, or money market instrument on credit watch or review, any affirmation of a credit rating assigned to the obligor, security, or money market instrument, and a withdrawal of a credit rating assigned to the obligor, security, or money market instrument.

(2) *Information.* A nationally recognized statistical rating organization must include, at a minimum, the following information with each credit rating disclosed pursuant to paragraph (b)(1) of this section:

(i) The identity of the nationally recognized statistical rating organization disclosing the rating action;

(ii) The date of the rating action;

(iii) If the rating action is taken with respect to a credit rating of an obligor as an entity, the following identifying information about the obligor, as applicable:

(A) The Central Index Key (CIK) number of the rated obligor; and

(B) The legal name of the obligor.

(iv) If the rating action is taken with respect to a credit rating of a security or money market instrument, as applicable:

(A) The Central Index Key (CIK) number of the issuer of the security or money market instrument;

(B) The legal name of the issuer of the security or money market instrument; and

(C) The CUSIP of the security or money market instrument;

(v) A classification of the rating action as either:

(A) A disclosure of a credit rating that was outstanding as of June 26, 2007, for the purposes of paragraph (b)(1)(i) of this section;

(B) An initial credit rating;

(C) An upgrade of an existing credit rating;

(D) A downgrade of an existing credit rating, which would include classifying the obligor, security, or money market instrument as in default, if applicable;

(E) A placement of an existing credit rating on credit watch or review;

(F) An affirmation of an existing credit rating; or

(G) A withdrawal of an existing credit rating and, if the classification is withdrawal, the nationally recognized statistical rating organization also must classify the reason for the withdrawal as either:

(*1*) The obligor defaulted, or the security or money market instrument went into default;

(*2*) The obligation subject to the credit rating was extinguished by payment in full of all outstanding principal and interest due on the obligation according to the terms of the obligation; or

(*3*) The credit rating was withdrawn for reasons other than those set forth in paragraph (b)(2)(v)(G)(*1*) or (*2*) of this section; and

(vi) The classification of the class or subclass that applies to the credit rating as either:

(A) Financial institutions, brokers, or dealers;

(B) Insurance companies;

(C) Corporate issuers; or

(D) Issuers of structured finance products in one of the following subclasses:

(*1*) Residential mortgage backed securities ("RMBS") (for purposes of this subclass, RMBS means a securitization primarily of residential mortgages);

(*2*) Commercial mortgage backed securities ("CMBS") (for purposes of this subclass, CMBS means a securitization primarily of commercial mortgages);

(*3*) Collateralized loan obligations ("CLOs") (for purposes of this subclass, a CLO means a securitization primarily of commercial loans);

(*4*) Collateralized debt obligations ("CDOs) (for purposes of this subclass, a CDO means a securitization primarily of other debt instruments such as RMBS, CMBS, CLOs, CDOs, other asset backed securities, and corporate bonds);

(*5*) Asset-backed commercial paper conduits ("ABCP") (for purposes of this subclass, ABCP means short term notes issued by a structure that securitizes a variety of financial assets, such as trade receivables or credit card receivables, which secure the notes);

(*6*) Other asset-backed securities ("other ABS") (for purposes of this subclass, other ABS means a securitization primarily of auto loans, auto leases, floor plans, credit card receivables, student loans, consumer loans, or equipment leases); or

(*7*) Other structured finance products ("other SFPs") (for purposes of this subclass, other SFPs means any structured finance product not identified in paragraphs (b)(2)(iv)(D)(1) through (6)) of this section; or

(E) Issuers of government securities, municipal securities, or securities issued by a foreign government in one of the following subclasses:

(*1*) Sovereign issuers;

(*2*) United States public finance; or

(*3*) International public finance; and

(vii) The credit rating symbol, number, or score in the applicable rating scale of the nationally recognized statistical rating organization assigned to the obligor, security, or money market instrument as a result of the rating action or, if the credit rating remained unchanged as a result of the rating action, the credit rating symbol, number, or score in the applicable rating scale of the nationally recognized statistical rating organization assigned to the obligor, security, or money market instrument as of the date of the rating action (in either case, include a credit rating in a default category, if applicable).

(3) *Format.* The information identified in paragraph (b)(2) of this section must be disclosed in an interactive data file that uses an XBRL (eXtensible Business Reporting Language) format and the List of XBRL Tags for NRSROs as published on the Internet Web site of the Commission.

(4) *Timing.* The nationally recognized statistical rating organization must disclose the information required in paragraph (b)(2) of this section:

(i) Within twelve months from the date the rating action is taken, if the credit rating subject to the action was paid for by the obligor being rated or by the issuer, underwriter, depositor, or sponsor of the security being rated; or

(ii) Within twenty-four months from the date the rating action is taken, if the credit rating subject to the action is not a credit rating described in paragraph (b)(4)(i) of this section.

(5) *Removal of a credit rating history.* The nationally recognized statistical rating organization may cease disclosing a rating history of an obligor, security, or money market instrument no earlier than 20 years after the date a rating action with respect to the obligor, security, or money market instrument is classified as a withdrawal of the credit rating pursuant to paragraph (b)(2)(v)(G) of this section, provided that no subsequent credit ratings are assigned to the obligor, security, or money market instrument after the withdrawal classification.

13. Section 240.17g–8 is added to read as follows:

§ 240.17g–8 Policies and procedures.

(a) *Policies and procedures with respect to the procedures and methodologies used to determine credit ratings.* A nationally recognized statistical rating organization must establish, maintain, enforce, and document policies and procedures reasonably designed to ensure:

(1) That the procedures and methodologies, including qualitative and quantitative data and models, the nationally recognized statistical rating organization uses to determine credit ratings are approved by its board of directors or a body performing a function similar to that of a board of directors.

(2) That the procedures and methodologies, including qualitative and quantitative data and models, the nationally recognized statistical rating organization uses to determine credit ratings are developed and modified in accordance with the policies and procedures of the nationally recognized statistical rating organization.

(3) That material changes to the procedures and methodologies, including changes to qualitative and

quantitative data and models, the nationally recognized statistical rating organization uses to determine credit ratings are:

(i) Applied consistently to all credit ratings to which the changed procedures or methodologies apply; and

(ii) To the extent that the changes are to surveillance or monitoring procedures and methodologies, applied to then-current credit ratings within a reasonable period of time, taking into consideration the number of ratings impacted, the complexity of the procedures and methodologies used to determine the credit ratings, and the type of obligor, security, or money market instrument being rated.

(4) That the nationally recognized statistical rating organization promptly publishes on an easily accessible portion of its corporate Internet Web site:

(i) Material changes to the procedures and methodologies, including to qualitative models or quantitative inputs, the nationally recognized statistical rating organization uses to determine credit ratings, the reason for the changes, and the likelihood the changes will result in changes to any current ratings; and

(ii) Significant errors identified in a procedure or methodology, including a qualitative or quantitative model, the nationally recognized statistical rating organization uses to determine credit ratings that may result in a change in current credit ratings.

(5) That the nationally recognized statistical rating organization discloses the version of a credit rating procedure or methodology, including the qualitative methodology or quantitative inputs, used with respect to a particular credit rating.

(b) *Policies and procedures with respect to credit rating symbols, numbers, or scores.* A nationally recognized statistical rating organization must establish, maintain, enforce, and document policies and procedures that are reasonably designed to:

(1) Assess the probability that an issuer of a security or money market instrument will default, fail to make timely payments, or otherwise not make payments to investors in accordance with the terms of the security or money market instrument.

(2) Clearly define each symbol, number, or score in the rating scale used by the nationally recognized statistical rating organization to denote a credit rating category and notches within a category for each class and subclass of credit ratings for which the nationally recognized statistical rating organization is registered and to include such definitions in Exhibit 1 to Form NRSRO (§ 240b.300 of this chapter).

(3) Apply any symbol, number, or score defined pursuant to paragraph (b)(2) of this section in a manner that is consistent for all types of obligors, securities, and money market instruments for which the symbol, number, or score is used.

(c) *Policies and procedures with respect to look-back reviews.* The policies and procedures a nationally recognized statistical rating organization is required to establish, maintain, and enforce pursuant to Section 15E(h)(4)(A) of the Act (15 U.S.C. 78o–7(h)(4)(A)) must address instances in which a review conducted pursuant to those policies and procedures determines that a conflict of interest influenced a credit rating assigned to an obligor, security, or money market instrument by including, at a minimum, procedures that are reasonably designed to ensure that the nationally recognized statistical rating organization will:

(1) Immediately publish a rating action placing the applicable credit ratings of the obligor, security, or money market instrument on credit watch or review based on the discovery of the conflict and include with the publication of the rating action the information required by § 240.17g–7(a)(1)(ii)(J)(*3*)(*i*) of this chapter;

(2) Promptly determine whether the current credit rating assigned to the obligor, security, or money market instrument must be revised so that it no longer is influenced by a conflict of interest and is solely a product of the documented procedures and methodologies the nationally recognized statistical rating organization uses to determine credit ratings; and

(3) Promptly publish, based on the determination of whether the current credit rating assigned to the obligor, security, or money market instrument must be revised (as applicable):

(i) A revised credit rating, if appropriate, and include with the publication of the revised credit rating the information required by § 240.17g–7(a)(1)(ii)(J)(*3*)(*ii*) of this chapter; or

(ii) An affirmation of the credit rating, if appropriate, and include with the publication of the affirmation the information required by § 240.17g–7(a)(1)(ii)(J)(*3*)(*iii*) of this chapter.

14. Section 240.17g–9 is added to read as follows:

§ 240.17g–9 Standards of training, experience, and competence for credit analysts.

(a) A nationally recognized statistical rating organization must establish, maintain, enforce, and document standards of training, experience, and competence for the individuals it employs to determine credit ratings that are reasonably designed to achieve the objective that such individuals produce accurate credit ratings in the classes and subclasses of credit ratings for which the nationally recognized statistical rating organization is registered.

(b) The nationally recognized statistical rating organization must consider the following when establishing the standards required under paragraph (a) of this section:

(1) If the credit rating procedures and methodologies used by the individual involve qualitative analysis, the knowledge necessary to effectively evaluate and process the data relevant to the creditworthiness of the obligor being rated or the issuer of the securities or money market instruments being rated;

(2) If the credit rating procedures and methodologies used by the individual involve quantitative analysis, the technical expertise necessary to understand any models and model inputs that are a part of the procedures and methodologies;

(3) The classes and subclasses of credit ratings for which the individual participates in determining credit ratings and the factors relevant to such classes and subclasses, including the geographic location, sector, industry, regulatory and legal framework, and underlying assets, applicable to the obligors or issuers in the classes and subclasses; and

(4) The complexity of the obligors, securities, or money market instruments being rated by the individual.

(c) The nationally recognized statistical rating organization must include the following in the standards required under paragraph (a) of this section:

(1) A requirement for periodic testing of the individuals employed by the nationally recognized statistical rating organization to determine credit ratings on their knowledge of the procedures and methodologies used by the nationally recognized statistical rating organization to determine credit ratings in the classes and subclasses of credit ratings for which the individual participates in determining credit ratings; and

(2) A requirement that at least one individual with three years or more experience in performing credit analysis participates in the determination of a credit rating.

15. Section 240.17g–10 is added to read as follows:

§ 240.17g–10 Certification of providers of third-party due diligence services in connection with asset-backed securities.

(a) The written certification that a person employed to provide third-party due diligence services is required to provide to a nationally recognized statistical rating organization pursuant to Section 15E(s)(4)(B) of the Act (15 U.S.C. 78o–7(s)(4)(B)) must be on Form ABS Due Diligence–15E (§ 240b.400 of this chapter).

(b) The written certification must be signed by an individual who is duly authorized by the person providing the third-party due diligence services to make such a certification.

(c) For the purposes of Section 15E(s)(4)(B) of the Act (15 U.S.C. 78o–7(s)(4)(B)) and this section:

(1) The term *due diligence services* means a review of the assets underlying an asset-backed security, as defined in Section 3(a)(77) of the Act (15 U.S.C. 78c(a)(77)) for the purpose of making findings with respect to:

(i) The quality or integrity of the information or data about the assets provided, directly or indirectly, by the securitizer or originator of the assets;

(ii) Whether the origination of the assets conformed to, or deviated from, stated underwriting or credit extension guidelines, standards, criteria, or other requirements;

(iii) The value of collateral securing such assets;

(iv) Whether the originator of the assets complied with Federal, state, or local laws or regulations; or

(v) Any other factor or characteristic of such assets that would be material to the likelihood that the issuer of the asset-backed security will pay interest and principal according to its terms and conditions.

(2) The term *issuer* includes a sponsor, as defined in § 229.1011 of this chapter, or depositor, as defined in § 229.1011 of this chapter, that participates in the issuance of an asset-backed security, as defined in Section 3(a)(77) of the Act (15 U.S.C. 78c(a)(77)).

(3) The term *originator* has the same meaning as in Section 15G of the Act (15 U.S.C. 78o–9).

(4) The term *securitizer* has the same meaning as in Section 15G of the Act (15 U.S.C. 78o–9).

PART 249—FORMS, SECURITIES EXCHANGE ACT OF 1934

16. The authority citation for Part 249 continues to read as follows:

Authority: 15 U.S.C. 78a *et seq.* and 7201 *et seq.;* and 18 U.S.C. 1350, unless otherwise noted.

Subpart O—Forms for Securitizers of Asset-Backed Securities

17. Section 249.1400 and Form ABS–15G (referenced in § 249.1400) to Part 249 are revised to read as follows:

§ 249.1400 Form ABS–15G, Asset-backed securitizer report pursuant to Section 15G of the Securities Exchange Act of 1934.

This form shall be used for reports of information required by Rule 15Ga–1 (§ 240.15Ga–1 of this chapter) and Rule 15Ga–2 (§ 240.15Ga–2 of this chapter).

Note: The text of Form ABS–15G does not, and this amendment will not, appear in the Code of Federal Regulations.

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM ABS–15G

ASSET–BACKED SECURITIZER REPORT PURSUANT TO SECTION 15G OF THE SECURITIES EXCHANGE ACT OF 1934

Check the appropriate box to indicate the filing obligation which this form is intended to satisfy:

__ Rule 15Ga–1 under the Exchange Act (17 CFR 240.15Ga–1) for the reporting period _____ to _____

__ Rule 15Ga–2 under the Exchange Act (17 CFR 240.15Ga–2)

Date of Report (Date of earliest event reported)_____

Commission File Number of securitizer: _____

Central Index Key Number of securitizer: _____

_____

Name and telephone number, including area code, of the person to contact in connection with this filing

Indicate by check mark whether the securitizer has no activity to report for the initial period pursuant to Rule 15Ga–1(c)(1) [ ]

Indicate by check mark whether the securitizer has no activity to report for the quarterly period pursuant to Rule 15Ga–1(c)(2)(i) [ ]

Indicate by check mark whether the securitizer has no activity to report for the annual period pursuant to Rule 15Ga–1(c)(2)(ii) [ ]

____ For forms furnished pursuant to Rule 15Ga–2 under the Exchange Act (17 CFR 240.15Ga–2), also provide the following information:

Commission File Number of depositor: _____

Central Index Key Number of depositor: _____

_____

(Exact name of issuing entity as specified in its charter)

Central Index Key Number of issuing entity (if applicable): _____

Commission File Number of issuing entity (if applicable): _____

Commission File Number of underwriter (if applicable): _____

Central Index Key Number of underwriter (if applicable): _____

GENERAL INSTRUCTIONS

A. Rule as to Use of Form ABS–15G.

This form shall be used to comply with the requirements of Rule 15Ga–1 (17 CFR 240.15Ga–1) and Rule 15Ga–2 (17 CFR 240.15Ga–2) under the Exchange Act.

B. Events to be Reported and Time for Filing of Reports.

Forms filed under Rule 15Ga–1. In accordance with Rule 15Ga–1, file the information required by Part I in accordance with Item 1.01, Item 1.02, or Item 1.03, as applicable. If the filing deadline for the information occurs on a Saturday, Sunday, or holiday on which the Commission is not open for business, then the filing deadline shall be the first business day thereafter.

Forms filed under Rule 15Ga–2. In accordance with Rule 15Ga–2, furnish the information required by Part II no later than five business days prior to the first sale of securities in the offering.

C. Preparation of Report

This form is not to be used as a blank form to be filled in, but only as a guide in the preparation of the report on paper meeting the requirements of Rule 12b–12 (17 CFR 240.12b–12). The report shall contain the number and caption of the applicable item, but the text of such item may be omitted, provided the answers thereto are prepared in the manner specified in Rule 12b–13 (17 CFR 240.12b–13). All items that are not required to be answered in a particular report may be omitted and no reference thereto need be made in the report. All instructions should also be omitted.

D. Signature and Filing of Report

1. *Forms filed under Rule 15Ga–1.* Any form filed for the purpose of meeting the requirements in Rule 15Ga–1 must be signed by the senior officer in charge of securitization of the securitizer.

2. *Forms filed under Rule 15Ga–2.* Any form filed for the purpose of meeting the requirements in Rule 15Ga–2 must be signed by the senior officer in charge of securitization of the depositor if information required by Item 2.01 is required to be provided and must be signed by a duly authorized officer of

the underwriter if information required by Item 2.02 is required to be provided.

3. *Copies of report.* If paper filing is permitted, three complete copies of the report shall be filed with the Commission.

INFORMATION TO BE INCLUDED IN THE REPORT

PART I: REPRESENTATION AND WARRANTY INFORMATION

Item 1.01 Initial Filing of Rule 15Ga–1 Representations and Warranties Disclosure

Provide the disclosures required by Rule 15Ga–1 (17 CFR 240.15Ga–1) according to the filing requirements of Rule 15Ga–1(c)(1).

Item 1.02 Periodic Filing of Rule 15Ga–1 Representations and Warranties Disclosure

Provide the disclosures required by Rule 15Ga–1 (17 CFR 240.15Ga–1) according to the filing requirements of Rule 15Ga–1(c)(2).

Item 1.03 Notice of Termination of Duty to File Reports under Rule 15Ga–1

If a securitizer terminates its reporting obligation pursuant to Rule 15Ga–1(c)(3), provide the date of the last payment on the last asset-backed security outstanding that was issued by or issued by an affiliate of the securitizer.

PART II: FINDINGS AND CONCLUSIONS OF THIRD–PARTY DUE DILIGENCE REPORTS

Item 2.01 Findings and Conclusions of a Third Party Due Diligence Report Obtained by the Issuer

Provide the disclosures required by Rule 15Ga–2 (17 CFR 240.15Ga–2) for any third-party due diligence report obtained by the issuer.

Item 2.02 Findings and Conclusions of a Third-Party Due Diligence Report Obtained by the Underwriter

Provide the disclosures required by Rule 15Ga–2 (17 CFR 240.15Ga–2) for any third party engaged by the underwriter.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the reporting entity has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

_____ (Securitizer or Underwriter)

Date _____

_____(Signature)*

*Print name and title of the signing officer under his signature.

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

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

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

* * * * *

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

19. Form NRSRO (referenced in § 249b.300) is revised to read as follows:

Form NRSRO

APPLICATION FOR REGISTRATION AS A NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATION (NRSRO)

Persons who respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB control number.

SEC 1541 (4–09)

BILLING CODE 8011–01–P

APPLICATION FOR REGISTRATION AS A NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATION (NRSRO)

☐ INITIAL APPLICATION

☐ APPLICATION TO ADD CLASS OF CREDIT RATINGS

☐ APPLICATION SUPPLEMENT
Items and/or Exhibits Supplemented:

_____

☐ ANNUAL CERTIFICATION

☐ UPDATE OF REGISTRATION
Items and/or Exhibits Amended:

_____

☐ WITHDRAWAL FROM REGISTRATION

Important: Refer to Form NRSRO Instructions for General Instructions, Item-by-Item Instructions, an Explanation of Terms, and the Disclosure Reporting Page (NRSRO). "You" and "your" mean the person filing or furnishing, as applicable, this Form NRSRO and any credit rating affiliate identified in Item 3.

1. **A.** Your full name:

_____

B. (i) Name under which your credit rating business is primarily conducted, if different from Item 1A:

_____

(ii) Any other name under which your credit rating business is conducted and where it is used (other than the name of a credit rating affiliate identified in Item 3):

_____

C. Address of your principal office (do not use a P.O. Box):

_____
(Number and Street) (City) (State/Country) (Zip/Postal Code)

D. Mailing address, if different:

_____
(Number and Street) (City) (State/Country) (Zip/Postal Code)

E. Contact person (See Instructions):

_____
(Name and Title)

_____
(Number and Street) (City) (State/Country) (Zip/Postal Code)

CERTIFICATION:

The undersigned has executed this Form NRSRO on behalf of, and on the authority of, the Applicant/NRSRO. The undersigned, on behalf of the Applicant/NRSRO, represents that the information and statements contained in this Form, including Exhibits and attachments, all of which are part of this Form, are accurate in all significant respects. If

this is an ANNUAL CERTIFICATION, the undersigned, on behalf of the NRSRO, represents that the NRSRO's application on Form NRSRO, as amended, is accurate in all significant respects.

_____
(Date) (Name of the Applicant/NRSRO)

By:

_____
(Signature) (Print Name and Title)

2. **A**. Your legal status:

☐ Corporation ☐ Limited Liability Company ☐ Partnership ☐ Other (specify) _____

B. Month and day of your fiscal year end: _____

C. Place and date of your formation (i.e., state or country where you were incorporated, where your partnership agreement was filed, or where you otherwise were formed):

State/Country of formation: _____ Date of formation: _____

3. Your credit rating affiliates (See Instructions):

_____
(Name) (Address)

_____
(Name) (Address)

_____
(Name) (Address)

_____
(Name) (Address)

_____
(Name) (Address)

4. The designated compliance officer of the Applicant/NRSRO (See Instructions):

_____
(Name and Title)

_____
(Number and Street) (City) (State/Country) (Postal Code)

5. Describe in detail how this Form NRSRO and Exhibits 1 through 9 to this Form NRSRO will be made publicly and freely available on an easily accessible portion of the corporate Internet website of the Applicant/NRSRO (See Instructions):

_____

_____

_____

6. COMPLETE ITEM 6 ONLY IF THIS IS AN INITIAL APPLICATION, APPLICATION SUPPLEMENT, OR APPLICATION TO ADD A CLASS OF CREDIT RATINGS.

A. Indicate below the classes of credit ratings for which the Applicant/NRSRO is applying to be registered. For each class, indicate the approximate number of obligors, securities, and money market instruments in that class as of the date of this application for which the Applicant/NRSRO has an outstanding credit rating and the

approximate date the Applicant/NRSRO began issuing credit ratings as a "credit rating agency" in that class on a continuous basis through the present (See Instructions):

Class of credit ratings	Applying for registration	Approximate number currently outstanding	Approximate date issuance commenced
financial institutions as that term is defined in section 3(a)(46) of the Exchange Act (15 U.S.C. 78c(a)(46)), brokers as that term is defined in section 3(a)(4) of the Exchange Act (15 U.S.C. 78c(a)(4)), and dealers as that term is defined in section 3(a)(5) of the Exchange Act (15 U.S.C. 78c(a)(5))	☐		
insurance companies as that term is defined in section 3(a)(19) of the Exchange Act (15 U.S.C. 78c(a)(19))	☐		
corporate issuers	☐		
issuers of asset-backed securities as that term is defined in 17 CFR 229.1101(c)	☐		
issuers of government securities as that term is defined in section 3(a)(42) of the Exchange Act (15 U.S.C. 78c(a)(42)), municipal securities as that term is defined in section 3(a)(29) of the Exchange Act (15 U.S.C. 78c(a)(29)), and foreign government securities	☐		

B. Briefly describe how the Applicant/NRSRO makes the credit ratings in the classes indicated in Item 6A readily accessible for free or for a reasonable fee (See Instructions):

_____

_____

_____

C. Check the applicable box and attach certifications from qualified institutional buyers, if required (See Instructions):

☐ The Applicant/NRSRO is attaching _____ certifications from qualified institutional buyers to this application. Each is marked "Certification from Qualified Institutional Buyer."

☐ The Applicant/NRSRO is exempt from the requirement to file certifications from qualified institutional buyers pursuant to section 15E(a)(1)(D) of the Exchange Act.

Note: You are not required to make a Certification from a Qualified Institutional Buyer filed with this Form NRSRO publicly available on your corporate Internet website pursuant to Exchange Act Rule 17g-1(i). You may request that the Commission keep these certifications confidential by marking each page "Confidential Treatment" and complying with Commission rules governing confidential treatment. The Commission will keep the certifications confidential upon request to the extent permitted by law.

7. DO NOT COMPLETE ITEM 7 IF THIS IS AN INITIAL APPLICATION.

A. Indicate below the classes of credit ratings for which the NRSRO is currently registered. For each class, indicate the approximate number of obligors, securities, and money market instruments in that class for which the NRSRO had an outstanding credit rating as of the most recent calendar year end and the approximate date the NRSRO began issuing credit ratings as a "credit rating agency" in that class on a continuous basis through the present (See Instructions):

Class of credit rating	Currently registered	Approximate number outstanding as of the most recent calendar year end	Approximate date issuance commenced
financial institutions as that term is defined in section 3(a)(46) of the Exchange Act (15 U.S.C. 78c(a)(46)), brokers as that term is defined in section 3(a)(4) of the Exchange Act (15 U.S.C. 78c(a)(4)), and dealers as that term is defined in section 3(a)(5) of the Exchange Act (15 U.S.C. 78c(a)(5))	☐		
insurance companies as that term is defined in section 3(a)(19) of the Exchange Act (15 U.S.C. 78c(a)(19))	☐		
corporate issuers	☐		
issuers of asset-backed securities as that term is defined in 17 CFR 229.1101(c)	☐		
issuers of government securities as that term is defined in section 3(a)(42) of the Act (15 U.S.C. 78c(a)(42)), municipal securities as that term is defined in section 3(a)(29) of the Exchange Act (15 U.S.C. 78c(a)(29)), and foreign government securities	☐		

B. Briefly describe how the NRSRO makes the credit ratings in the classes indicated in Item 7A readily accessible for free or for a reasonable fee (See Instructions):

_____

_____

_____

8. Answer each question. Provide information that relates to a "Yes" answer on a Disclosure Reporting Page (NRSRO) and submit the Disclosure Reporting Page with this Form NRSRO (See Instructions). You are not required to make any disclosure reporting pages submitted with this Form publicly available on your corporate Internet website pursuant to Exchange Act Rule 17g-1(i). You may request that the Commission keep any disclosure reporting pages confidential by marking each page "Confidential Treatment" and complying with Commission rules governing confidential treatment. The Commission will keep the disclosure reporting pages confidential upon request to the extent permitted by law.	
	YES NO

A. Has the Applicant/NRSRO or any person within the Applicant/NRSRO committed or omitted any act, or been subject to an order or finding, enumerated in subparagraphs (A), (D), (E), (G), or (H) of section 15(b)(4) of the Securities Exchange Act of 1934, been convicted of any offense specified in section 15(b)(4)(B) of the Securities Exchange Act of 1934, or been enjoined from any action, conduct, or practice specified in section 15(b)(4)(C) of the Securities Exchange Act of 1934 in the ten years preceding the date of the initial application of the Applicant/NRSRO for registration as an NRSRO or at any time thereafter?	☐	☐
B. Has the Applicant/NRSRO or any person within the Applicant/NRSRO been convicted of any crime that is punishable by imprisonment for 1 or more years, and that is not described in section 15(b)(4) of the Securities Exchange Act of 1934, or been convicted of a substantially equivalent crime by a foreign court of competent jurisdiction in the ten years preceding the date of the initial application of the Applicant/NRSRO for registration as an NRSRO or at any time thereafter?	☐	☐
C. Is any person within the Applicant/NRSRO subject to any order of the Commission barring or suspending the right of the person to be associated with an NRSRO?	☐	☐

9. Exhibits (See Instructions).

Exhibit 1. Credit ratings performance measurement statistics. ☐ Exhibit 1 is attached and made a part of this Form NRSRO.
Exhibit 2. A description of the procedures and methodologies used in determining credit ratings. ☐ Exhibit 2 is attached and made a part of Form NRSRO.
Exhibit 3. Policies or procedures adopted and implemented to prevent the misuse of material, nonpublic information. ☐ Exhibit 3 is attached and made a part of this Form NRSRO.
Exhibit 4. Organizational structure. ☐ Exhibit 4 is attached to and made a part of this Form NRSRO.
Exhibit 5. The code of ethics or a statement of the reasons why a code of ethics is not in effect. ☐ Exhibit 5 is attached to and made a part of this Form NRSRO.
Exhibit 6. Identification of conflicts of interests relating to the issuance of credit ratings. ☐ Exhibit 6 is attached to and made a part of this Form NRSRO.
Exhibit 7. Policies and procedures to address and manage conflicts of interest. ☐ Exhibit 7 is attached to and made a part of this Form NRSRO.
Exhibit 8. Certain information regarding the credit rating agency's credit analysts and credit analyst supervisors. ☐ Exhibit 8 is attached to and made a part of this Form NRSRO.

Exhibit 9. Certain information regarding the credit rating agency's designated compliance officer.

☐ Exhibit 9 is attached to and made a part of this Form NRSRO.

Exhibit 10. A list of the largest users of credit rating services by the amount of net revenue earned from the user during the fiscal year ending immediately before the date of the initial application.

☐ Exhibit 10 is attached to and made a part of this Form NRSRO.

Note: You are not required to make this Exhibit publicly available on your corporate Internet website pursuant to Exchange Act Rule 17g-1(i). You may request that the Commission keep this Exhibit confidential by marking each page "Confidential Treatment" and complying with Commission rules governing confidential treatment. The Commission will keep the information and documents in the Exhibit confidential upon request to the extent permitted by law.

Exhibit 11. Audited financial statements for each of the three fiscal or calendar years ending immediately before the date of the initial application.

☐ Exhibit 11 is attached to and made a part of this Form NRSRO.

Note: You are not required to make this Exhibit publicly available on your corporate Internet website pursuant to Exchange Act Rule 17g-1(i). You may request that the Commission keep this Exhibit confidential by marking each page "Confidential Treatment" and complying with Commission rules governing confidential treatment. The Commission will keep the information and documents in the Exhibit confidential upon request to the extent permitted by law.

Exhibit 12. Information regarding revenues for the fiscal or calendar year ending immediately before the date of the initial application.

☐ Exhibit 12 is attached to and made a part of this Form NRSRO.

Note: You are not required to make this Exhibit publicly available on your corporate Internet website pursuant to Exchange Act Rule 17g-1(i). You may request that the Commission keep this Exhibit confidential by marking each page "Confidential Treatment" and complying with Commission rules governing confidential treatment. The Commission will keep the information and documents in the Exhibit confidential upon request to the extent permitted by law.

Exhibit 13. The total and median annual compensation of credit analysts.

☐ Exhibit 13 is attached and made a part of this Form NRSRO.

Note: You are not required to make this Exhibit publicly available on your corporate Internet website pursuant to Exchange Act Rule 17g-1(i). You may request that the Commission keep this Exhibit confidential by marking each page "Confidential Treatment" and complying with Commission rules governing confidential treatment. The Commission will keep the information and documents in the Exhibit confidential upon request to the extent permitted by law.

BILLING CODE 8011–01–C

FORM NRSRO INSTRUCTIONS

A. GENERAL INSTRUCTIONS.

1. Form NRSRO is the Application for Registration as a Nationally Recognized Statistical Rating Organization ("NRSRO") under Section 15E of the Securities Exchange Act of 1934 ("Exchange Act") and Exchange Act Rule 17g–1. Exchange Act Rule 17g–1 requires an Applicant/NRSRO to use Form NRSRO to:

- File an initial application to be registered as an NRSRO with the U.S. Securities and Exchange Commission ("Commission");
- File an application to register for an additional class of credit ratings with the Commission;
- File an application supplement with the Commission;
- File an update of registration pursuant to Section 15E(b)(1) of the Exchange Act with the Commission;
- File an annual certification pursuant to Section 15E(b)(2) of the Exchange Act with the Commission; and
- Furnish a withdrawal of registration pursuant to Section 15E(e) of the Exchange Act to the Commission.

2. Exchange Act Rule 17g–1(c) requires that an Applicant/NRSRO

promptly file with the Commission a written notice if information filed with the Commission in an initial application for registration or in an application to register for an additional class of credit ratings is found to be or becomes materially inaccurate before the Commission has granted or denied the application. The notice must identify the information found to be materially inaccurate. The Applicant/NRSRO must also promptly file with the Commission accurate and complete information as an application supplement on Form NRSRO.

3. Pursuant to Exchange Act Rule 17g–1(i), an NRSRO must make its current Form NRSRO and information and documents filed in Exhibits 1 through 9 to Form NRSRO publicly and freely available on an easily accessible portion of its corporate Internet website within 10 business days after the date of the Commission Order granting an initial application for registration as an NRSRO or an application to register for an additional class of credit ratings and within 10 business days after filing with or furnishing to, as applicable, the Commission an update of registration, annual certification, or withdrawal from registration on Form NRSRO. The certifications from qualified institutional buyers, disclosure reporting pages, and Exhibits 10 through 13 are not required to be made publicly available by the NRSRO pursuant to Rule 17g–1(i). An Applicant/NRSRO may request that the Commission keep confidential the certifications from qualified institutional buyers, the disclosure reporting pages, and the information and documents in Exhibits 10–13 filed with the Commission. An Applicant/NRSRO seeking confidential treatment for these submissions should mark each page "Confidential Treatment" and comply with Commission rules governing confidential treatment (*See* 17 CFR 200.80 and 17 CFR 200.83). The Commission will keep this information confidential to the extent permitted by law.

4. Section 15E(a)(2) of the Exchange Act prescribes time periods and requirements for the Commission to grant or deny an initial application for registration as an NRSRO. These time periods also apply to an application to register for an additional class of credit ratings.

5. Type or clearly print all information. Use only the current version of Form NRSRO or a reproduction of it.

6. Section 15E of the Exchange Act (15 U.S.C. 78o–7) authorizes the Commission to collect the Information on Form NRSRO from an Applicant/NRSRO. The principal purposes of Form NRSRO are to determine whether an Applicant should be granted registration as an NRSRO, whether an NRSRO should be granted registration in an additional class of credit ratings, whether an NRSRO continues to meet the criteria for registration as an NRSRO, for an NRSRO to withdraw from registration, and to provide information about an NRSRO to users of credit ratings. Intentional misstatements or omissions may constitute federal criminal violations under 18 U.S.C. 1001.

The information collection is in accordance with the clearance requirements of Section 3507 of the Paperwork Reduction Act of 1995 (44 U.S.C. 3507). The Commission may not conduct or sponsor, and you are not required to respond to, a collection of information unless it displays a valid Office of Management and Budget (OMB) control number. The time required to complete and file or furnish, as applicable, this form, will vary depending on individual circumstances. The estimated average time to complete an initial application is displayed on the facing page of this Form. Send comments regarding this burden estimate or suggestions for reducing the burden to Chief Information Officer, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549 or *PRA Mailbox@sec.gov*.

7. Under Exchange Act Rule 17g–2(b)(10), an NRSRO must retain copies of all Form NRSROs (including Exhibits, accompanying information, and documents) filed with or furnished to, as applicable, the Commission. Exchange Act Rule 17g–2(c) requires that these records be retained for three years after the date the record is made.

8. An Applicant must file with the Commission at the address indicated below two paper copies of an initial application for registration as an NRSRO under Exchange Act Rule 17g–1(a), an application to register for an additional class of credit ratings under Exchange Act Rule 17g–1(b), a supplement to an initial application or application to register for an additional class of credit ratings under Exchange Act Rule 17g–1(c), or a withdrawal of an initial application or an application to register for an additional class of credit ratings under Exchange Act Rule 17g–1(d).

ADDRESS—The mailing address for Form NRSRO is: U.S. Securities and Exchange Commission, 100 F Street, NE. Washington, DC 20549.

After registration, an NRSRO must file with or furnish to, as applicable, the Commission electronically in the format required by the EDGAR Filer Manual, as defined in Rule 11 of Regulation S–T, an update of registration under Exchange Act Rule 17g–1(e), an annual certification under Exchange Act Rule 17g–1(f), or a withdrawal from registration under Exchange Act Rule 17g–1(g).

9. A Form NRSRO will be considered filed with or furnished to, as applicable, the Commission on the date the Commission receives a complete and properly executed Form NRSRO that follows all applicable instructions for the Form, including the instructions in Item A.8 with respect to how a Form NRSRO must be filed with or furnished to the Commission.

10. An NRSRO is subject to applicable fines, penalties, and other available sanctions set forth in Sections 15E, 21, 21A, 21B, 21C, and 32 of the Exchange Act (15 U.S.C. 78o–7, 78u, 78u–1, 78u–2, 78u–3, and 78ff, respectively) for violations of the securities laws.

B. INSTRUCTIONS FOR AN INITIAL APPLICATION

An Applicant applying to be registered with the Commission as an NRSRO must file with the Commission an initial application on Form NRSRO. To complete an initial application:

- Check the "INITIAL APPLICATION" box at the top of Form NRSRO.
- Complete Items 1, 2, 3, 4, 5, 6, and 8. (See Instructions below for each Item). Enter "None" or "N/A" where appropriate.
- Unless exempt from the requirement, attach certifications from qualified institutional buyers, marked "Certification from Qualified Institutional Buyer" (See Instructions below for Item 6C).
- Attach Exhibits 1 through 13 (See Instructions below for each Exhibit).
- Execute the Form.

The Applicant must promptly file with the Commission a written notice if information submitted to the Commission in an initial application is found to be or becomes materially inaccurate prior to the date of a Commission order granting or denying the application. The notice must identify the information found to be materially inaccurate. The Applicant also must promptly file with the Commission an application supplement on Form NRSRO (*See* instructions below for an application supplement).

C. INSTRUCTIONS FOR AN APPLICATION TO ADD A CLASS OF CREDIT RATINGS

An NRSRO applying to register for an additional class of credit ratings must file with the Commission an application on Form NRSRO. To complete an application to register for an additional class of credit ratings:

- Check the "APPLICATION TO ADD CLASS OF CREDIT RATINGS" box at the top of Form NRSRO.
- Complete Items 1, 2, 3, 4, 5, 6, 7, and 8 on the Form following all applicable instructions for each Item (See Instructions below for each Item). If any information in an Item on a previously submitted Form NRSRO is materially inaccurate, update that information. Enter "None" or "N/A" where appropriate. Complete each Item even if the Item is not being updated.
- Unless exempt from the requirement, attach certifications from qualified institutional buyers for the additional class of credit ratings marked "Certification from Qualified Institutional Buyer" (See Instructions below for Item 6C).
- If any information in an Exhibit previously submitted is materially inaccurate, update that information.
- Execute the Form.

The Applicant must promptly file with the Commission a written notice if information submitted to the Commission in an application to add a class of credit ratings is found to be or becomes materially inaccurate prior to the date of a Commission order granting or denying the application. The notice must identify the information found to be materially inaccurate. The Applicant also must promptly file with the Commission an application supplement on Form NRSRO (See instructions below for an application supplement).

D. INSTRUCTIONS FOR AN APPLICATION SUPPLEMENT

An Applicant must file an application supplement with the Commission on Form NRSRO if information submitted to the Commission in a pending initial application for registration as an NRSRO or a pending application to register for an additional class of credit ratings is found to be or becomes materially inaccurate. To complete an application supplement:

- Check the "APPLICATION SUPPLEMENT" box at the top of Form NRSRO.
- Indicate on the line provided under the box the Item(s) or Exhibit(s) being supplemented.
- Complete Items 1, 2, 3, 4, 5 and 8 on the Form following all applicable instructions for each Item (See Instructions below for each Item). If supplementing an initial application, also complete Item 6. If supplementing an application for registration in an additional class of credit ratings, also complete Items 6 and 7. If any information in an Item on a previously submitted Form NRSRO is materially inaccurate, update that information. Enter "None" or "N/A" where appropriate. Complete each Item even if the Item is not being updated.
- If a certification from a qualified institutional buyer is being updated or a new certification is being added, attach the updated or new certification.
- If an Exhibit is being updated, attach the updated Exhibit.
- Execute the Form.

E. INSTRUCTIONS FOR AN UPDATE OF REGISTRATION

After registration is granted, Section 15E(b)(1) of the Exchange Act requires that an NRSRO must *promptly* amend its application for registration if information or documents provided in a previously submitted Form NRSRO become *materially inaccurate.* This requirement does not apply to Item 7 and Exhibit 1, which only are required to be updated annually with the annual certification. It also does not apply to Exhibits 10–13 and the certifications from qualified institutional buyers, which are not required to be updated on Form NRSRO after registration. An NRSRO amending its application for registration must file with the Commission an update of its registration on Form NRSRO. To complete an update of registration:

- Check the "UPDATE OF REGISTRATION" box at the top of Form NRSRO.
- Indicate on the line provided under the box the Item(s) or Exhibit(s) being updated.
- Complete Items 1, 2, 3, 4, 5, 7, and 8 on the Form following all applicable instructions for each Item (See Instructions below for each Item). If any information in an Item on a previously submitted Form NRSRO is materially inaccurate, update that information. Enter "None" or "N/A" where appropriate. Complete each Item even if the Item is not being updated.
- If an Exhibit is being updated, attach the updated Exhibit.
- Execute the Form.

F. INSTRUCTIONS FOR ANNUAL CERTIFICATIONS

After registration is granted, Section 15E(b)(2) of the Exchange Act requires that an NRSRO file with the Commission an annual certification not later than 90 days after the end of each calendar year. The annual certification must be filed with the Commission on Form NRSRO and must include an update of the information in Item 7 and the credit rating transition and default rates submitted in Exhibit 1, a certification that the information and documents on or with Form NRSRO continue to be accurate (use the certification on the Form), and a list of material changes to the application for registration that occurred during the previous calendar year. To complete an annual certification:

- Check the "ANNUAL CERTIFICATION" box at the top of Form NRSRO.
- Complete Items 1, 2, 3, 4, 5, 7, and 8 on the Form following all applicable instructions for each Item (See Instructions below for each Item). If any information in an Item on the previously submitted Form NRSRO is materially inaccurate, update that information. Enter "None" or "N/A" where appropriate. Complete each Item even if the Item is not being updated.
- If any information in a non-confidential Exhibit previously submitted is materially inaccurate, update that information. (Note: After registration, Exhibits 10 through 13 are not required to be made publicly available by the NRSRO pursuant to Exchange Act Rule 17g–1(i) and they should not be updated with the filing of the annual certification. Instead, similar information must be filed with the Commission not more than 90 days after the end of each fiscal year under Exchange Act Rule 17g–3.).
- Attach a list of all material changes made to the information or documents in the application for registration of the NRSRO that occurred during the previous calendar year.
- Execute the Form.

G. INSTRUCTIONS FOR A WITHDRAWAL FROM REGISTRATION

Section 15E(e)(1) of the Exchange Act provides that an NRSRO may voluntarily withdraw its registration with the Commission. Under Exchange Act Rule, 17g–1(g), to withdraw from registration, an NRSRO must furnish the Commission with a notice of withdrawal from registration on Form NRSRO. The withdrawal from registration will become effective 45 calendar days after the withdrawal from registration is furnished to the Commission upon such terms and conditions as the Commission may establish as necessary in the public interest or for the protection of

investors. To complete a withdrawal from registration:

- Check the "WITHDRAWAL FROM REGISTRATION" box at the top of Form NRSRO.
- Complete Items 1, 2, 3, 4, 5, 7, and 8 on the Form following all applicable instructions for each Item (See Instructions below for each Item). If any information on a previously submitted Form NRSRO is materially inaccurate, update that information. Enter "None" or "N/A" where appropriate. Complete each Item even if the Item is not being updated.
- Execute the Form.

H. INSTRUCTIONS FOR SPECIFIC LINE ITEMS

Item 1A. Provide the name of the person (*e.g.,* XYZ Corporation) that is filing or furnishing, as applicable, the Form NRSRO. This means the name of the person that is applying for registration as an NRSRO or is registered as an NRSRO and not the name of the individual that is executing the Form.

Item 1E. The individual listed as the contact person must be authorized to receive all communications and papers from the Commission and must be responsible for their dissemination within the Applicant/NRSRO.

Certification. The certification must be executed by the Chief Executive Officer or the President of the person that is filing or furnishing, as applicable, the Form NRSRO or an individual with similar responsibilities.

Item 3. Identify credit rating affiliates that issue credit ratings on behalf of the person filing or furnishing, as applicable, the Form NRSRO in one or more of the classes of credit ratings identified in Item 6 or Item 7. A "credit rating affiliate" is a separate legal entity or a separately identifiable department or division thereof that determines credit ratings that are credit ratings of the person filing or furnishing, as applicable, the Form NRSRO. The information in Items 4–8 and all the Exhibits must incorporate information about the credit ratings, methodologies, procedures, policies, financial condition, results of operations, personnel, and organizational structure of each credit rating affiliate identified in Item 3, as applicable. Any credit rating determined by a credit rating affiliate identified in Item 3 will be treated as a credit rating issued by the person filing or furnishing, as applicable, the Form NRSRO for purposes of Section 15E of the Exchange Act and the Commission's rules thereunder. The terms "Applicant" and "NRSRO" as used on Form NRSRO and the Instructions for the Form mean the person filing or furnishing, as applicable, the Form NRSRO and any credit rating affiliate identified in Item 3.

Item 4. Section 15E(j)(1) of the Exchange Act requires an NRSRO to designate a compliance officer responsible for administering the policies and procedures of the NRSRO established pursuant to Sections 15E(g) and (h) of the Exchange Act (respectively, to prevent the misuse of material nonpublic information and address and manage conflicts of interest) and for ensuring compliance with applicable securities laws, rules, and regulations.

Item 5. Section 15E(a)(3) of the Exchange Act and Exchange Act Rule 17g–1(i) require an NRSRO to make Form NRSRO and Exhibits 1–9 to Form NRSRO filed with the Commission publicly and freely available on an easily accessible portion of the NRSRO's corporate Internet Web site within 10 business days after the date of the Commission order granting an initial application for registration as an NRSRO or an application to register for an additional class of credit ratings and within 10 business days after filing with or furnishing to, as applicable, the Commission an amendment, annual certification, or withdrawal from registration on Form NRSRO. The certifications from qualified institutional investors, Disclosure Reporting Pages, and Exhibits 10 through 13 are not required to be made publicly available on the NRSRO's corporate Internet Web site. Describe how the current Form NRSRO and Exhibits 1–9 will be made publicly and freely available on an easily accessible portion of the NRSRO's corporate Internet Web site by providing the Internet address and link to the Form and Exhibits.

Item 6. Complete Item 6 only if filing an initial application for registration, an application to be registered in an additional class of credit ratings, or an application supplement.

Item 6A. Pursuant to Section 15E(a)(1)(B)(vii) of the Exchange Act, an Applicant applying for registration as an NRSRO must disclose in the application the classes of credit ratings for which the Applicant/NRSRO is applying to be registered. Indicate these classes by checking the appropriate box or boxes. For each class of credit ratings, provide in the appropriate box the approximate number of obligors, securities, and money market instruments in that class for which the Applicant/NRSRO presently has a credit rating outstanding as of the date of the application. In determining this amount, the Applicant/NRSRO must treat as a separately rated security or money market instrument each individually rated security and money market instrument that, for example, is assigned a distinct CUSIP or other unique identifier, has distinct credit enhancement features as compared with other securities or money market instruments of the same issuer, or has a different maturity date as compared with other securities or money market instruments of the same issuer. The Applicant/NRSRO must not include an obligor, security, or money market instrument in more than one class of credit rating. An Applicant/NRSRO must include in the class of credit ratings described in Section 3(a)(62)(B)(iv) of the Exchange Act (issuers of asset-backed securities) to the extent not described in Section 3(a)(62)(B)(iv), any rated security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction. For each class of credit ratings, also provide in the appropriate box the approximate date the Applicant/NRSRO began issuing and making readily accessible credit ratings in the class on a continuous basis through the present as a "credit rating agency," as that term is defined in Section 3(a)(61) of the Exchange Act. If there was a period when the Applicant/NRSRO stopped issuing credit ratings in a particular class or stopped operating as a credit rating agency, provide the approximate date the Applicant/NRSRO resumed issuing and making readily accessible credit ratings in that class as a credit rating agency. Refer to the definition of "credit rating agency" in the instructions below (also at 15 U.S.C. 78c(a)(61)) to determine when the Applicant/NRSRO began operating as a "credit rating agency."

Item 6B. To meet the definition of "credit rating agency" pursuant to Section 3(a)(61)(A) of the Exchange Act, the Applicant must, among other things, issue "credit ratings on the Internet or through another readily accessible means, for free or for a reasonable fee." Briefly describe how the Applicant/NRSRO makes the credit ratings in the classes indicated in Item 6A readily accessible for free or for a reasonable fee. If a person must pay a fee to obtain a credit rating made readily accessible by the Applicant/NRSRO, provide a fee schedule or describe the price(s) charged.

Item 6C. If the Applicant/NRSRO is required to file qualified institutional buyer certifications under Section 15E(a)(1)(C) of the Exchange Act file a minimum of 10 certifications from qualified institutional buyers, none of which is affiliated with the Applicant/

NRSRO. Each certification may address more than one class of credit ratings. To be registered as an NRSRO for a class of credit ratings identified in Item 6A under "Applying for Registration," the Applicant/NRSRO must file at least two certifications that address the class of credit ratings. If this is an application of an NRSRO to be registered in one or more additional classes of credit ratings, file at least two certifications that address each additional class of credit ratings.

The required certifications must be signed by a person duly authorized by the certifying entity, must be notarized, must be marked "Certification from Qualified Institutional Buyer," and must be in substantially the following form:

"I, [Executing official], am authorized by [Certifying entity] to execute this certification on behalf of [Certifying entity]. I certify that all actions by stockholders, directors, general partners, and other bodies necessary to authorize me to execute this certification have been taken and that [Certifying entity]:

(i) Meets the definition of a 'qualified institutional buyer' as set forth in section 3(a)(64) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(64)) pursuant to the following subsection(s) of 17 CFR 230.144A(a)(1) [insert applicable citations];

(ii) Has seriously considered the credit ratings of [the Applicant/NRSRO] in the course of making some of its investment decisions for at least the three years immediately preceding the date of this certification, in the following classes of credit ratings: [Insert applicable classes of credit ratings]; and

(iii) Has not received compensation either directly or indirectly from [the Applicant/NRSRO] for executing this certification.

[*Signature*]

Print Name and Title

You are not required to make a Certification from a Qualified Institutional Buyer filed with this Form NRSRO publicly available on your corporate Internet Web site pursuant to Exchange Act Rule 17g–1(i). You may request that the Commission keep these certifications 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 certifications confidential upon request to the extent permitted by law.

Item 7. An Applicant filing Form NRSRO to apply for registration as an NRSRO should not complete Item 7. An NRSRO filing or furnishing, as applicable, Form NRSRO for any other reason must complete Item 7. The information in Item 7 must be updated on an annual basis with the filing of the annual certification.

Item 7A. Indicate the classes of credit ratings for which the NRSRO is currently registered by checking the appropriate box or boxes. For each class of credit ratings, provide in the appropriate box the approximate number of obligors, securities, and money market instruments in that class for which the NRSRO had a credit rating outstanding as of the end of the most recently ended calendar year. In determining this amount, NRSRO must treat as a separately rated security or money market instrument each individually rated security and money market instrument that, for example, is assigned a distinct CUSIP or other unique identifier, has distinct credit enhancement features as compared with other securities or money market instruments of the same issuer, or has a different maturity date as compared with other securities or money market instruments of the same issuer. The NRSRO must not include an obligor, security, or money market instrument in more than one class of credit rating. An NRSRO must include in the class of credit ratings described in Section 3(a)(62)(B)(iv) of the Exchange Act (issuers of asset-backed securities) to the extent not described in Section 3(a)(62)(B)(iv), any rated security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction. For each class of credit ratings, also provide in the appropriate box the approximate date the NRSRO began issuing and making readily accessible credit ratings in the class on a continuous basis through the present as a "credit rating agency," as that term is defined in Section 3(a)(61) of the Exchange Act. If there was a period when the NRSRO stopped issuing credit ratings in a particular class or stopped operating as a credit rating agency, provide the approximate date the NRSRO resumed issuing and making readily accessible credit ratings in that class as a credit rating agency. Refer to the definition of "credit rating agency" in the instructions below (also at 15 U.S.C. 78c(a)(61)) to determine when the NRSRO began operating as a "credit rating agency."

Item 7B. Briefly describe how the NRSRO makes the credit ratings in the classes indicated in Item 7A readily accessible for free or for a reasonable fee. If a person must pay a fee to obtain a credit rating made readily accessible by the NRSRO, provide a fee schedule or describe the price(s) charged.

Item 8. Answer each question by checking the appropriate box. Refer to the definition of "person within an Applicant/NRSRO" set forth below to determine the persons to which the questions apply. Information that relates to an affirmative answer must be provided on a Disclosure Reporting Page (NRSRO) and filed with Form NRSRO. Submit a separate Disclosure Reporting Page (NRSRO) for each person that: (a) has committed or omitted any act, or has been subject to an order or finding, enumerated in subparagraphs (A), (D), (E), (G), or (H) of section 15(b)(4) of the Securities Exchange Act of 1934, has been convicted of any offense specified in section 15(b)(4)(B) of the Securities Exchange Act of 1934, or has been enjoined from any action, conduct, or practice specified in section 15(b)(4)(C) of the Securities Exchange Act of 1934; (b) has been convicted of any crime that is punishable by imprisonment for 1 or more years, and that is not described in section 15(b)(4) of the Securities Exchange Act of 1934, or has been convicted of a substantially equivalent crime by a foreign court of competent jurisdiction; or (c) is subject to any order of the Commission barring or suspending the right of the person to be associated with an NRSRO. The Disclosure Reporting Page (NRSRO) is attached to these instructions. Note: The definition of "person within an Applicant/NRSRO" is narrower than the definition of "person associated with a nationally recognized statistical rating organization" in Section 3(a)(63) of the Exchange Act. You are not required to make any disclosure reporting pages submitted with this Form NRSRO publicly available on your corporate Internet Web site pursuant to Exchange Act Rule 17g–1(i). You may request that the Commission keep any disclosure reporting pages confidential by marking each page "Confidential Treatment" and complying with Commission rules governing confidential treatment. The Commission will keep the disclosure reporting pages confidential upon request to the extent permitted by law.

Item 9. Exhibits. Section 15E(a)(1)(B) of the Exchange Act requires a credit rating agency's application for registration as an NRSRO to contain certain specific information and documents and, pursuant to Section 15E(a)(1)(B)(x), any other information and documents concerning the applicant and any person associated with the applicant that the Commission requires as necessary or appropriate in the public interest or for the protection of investors. If any information or

document required to be included with any Exhibit is maintained in a language other than English, file a copy of the original document and a version of the document translated into English. Attach a certification by an authorized person that the translated version is a true, accurate, and complete English translation of the information or document. Attach the Exhibits to Form NRSRO in numerical order. Bind each Exhibit separately, and mark each Exhibit or bound volume of the Exhibit with the appropriate Exhibit number. The information in the Exhibits must be sufficiently detailed to allow for verification. The information and documents in Exhibits 1 through 9 must be made publicly and freely available on an easily accessible portion of the NRSRO's corporate Internet Web site pursuant to Exchange Act Rule 17g–1(i). The information and documents in Exhibits 10 through 13 are not required to be made publicly available on the NRSRO's corporate Internet Web site pursuant to Exchange Act Rule 17g–1(i). An NRSRO may request that the Commission keep these Exhibits confidential by marking each page of them "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 these Exhibits confidential upon request to the extent permitted by law. (Note: After registration, Exhibits 10 through 13 are not required to be made publicly available by the NRSRO pursuant to Exchange Act Rule 17g–1(i) and they should not be updated with the filing of the annual certification. Instead, similar information must be filed with the Commission not more than 90 days after the end of each fiscal year pursuant to Exchange Act Rule 17g–3.).

Exhibit 1. (1) An Applicant/NRSRO must provide in this Exhibit performance measurement statistics consisting of transition and default rates for each class and subclass of credit ratings (listed below) for which it is seeking registration as an NRSRO or for which it is registered as an NRSRO. For each applicable class and subclass of credit ratings, an Applicant/NRSRO must provide transition and default rates for 1-, 3-, and 10-year time periods through the most recent calendar year end. The transition and default rates for each time period must be presented together in tabular form ("Transition/Default Matrix"). The Transition/Default Matrices must be presented on a calendar year basis even if the Applicant/NRSRO has a fiscal year end other than December 31. Exhibit 1 must be updated annually with the filing of the NRSRO's Annual Certification pursuant to Exchange Act Rule 17g–1(f). Pursuant to Exchange Act Rule 17g–1(i), an NRSRO must make the Annual Certification publicly and freely available on an easily accessible portion of the NRSRO's corporate Internet Web site within 10 business days after the filing and must make its up-to-date Exhibit 1 freely available in writing to any individual who requests a copy of the Exhibit. The classes and subclasses of credit ratings for which an Applicant/NRSRO must provide Transition/Default Matrices are (as applicable):

(A) The class of credit ratings described in Section 3(a)(62)(B)(i) of the Exchange Act (financial institutions, brokers, or dealers).

(B) The class of credit ratings described in Section 3(a)(62)(B)(ii) of the Exchange Act (insurance companies);

(C) The class of credit ratings described in Section 3(a)(62)(B)(iii) of the Exchange Act (corporate issuers);

(D) The following subclasses of credit ratings described in Section 3(a)(62)(B)(iv) of the Exchange Act (issuers of asset-backed securities) and, to the extent not described in Section 3(a)(62)(B)(iv), any security or money market instrument issued by an asset pool or as part of any asset-backed securities transaction:

(i) Residential mortgage backed securities ("RMBS") (for the purposes of Exhibit 1, RMBS means a securitization primarily of residential mortgages);

(ii) Commercial mortgage backed securities ("CMBS") (for the purposes of Exhibit 1, CMBS means a securitization primarily of commercial mortgages);

(iii) Collateralized loan obligations ("CLOs") (for the purposes of Exhibit 1, a CLO means a securitization primarily of commercial loans);

(iv) Collateralized debt obligations ("CDOs") (for the purposes of Exhibit 1, a CDO means a securitization primarily of other debt instruments such as RMBS, CMBS, CLOs, CDOs, other asset backed securities, and corporate bonds);

(v) Asset-backed commercial paper ("ABCP") (for the purposes of Exhibit 1, ABCP means short term notes issued by a structure that securitizes a variety of financial assets (e.g., trade receivables or credit card receivables), which secure the notes);

(vi) Other asset-backed securities ("other ABS") (for the purposes of Exhibit 1, other ABS means a securitization primarily of auto loans, auto leases, floor plan financings, credit card receivables, student loans, consumer loans, or equipment leases); and

(vii) Other structured finance products ("other SFPs") (for the purposes of Exhibit 1, other SFPs means any structured finance product not identified in subparagraphs (i) through (vi) above—the Applicant/NRSRO must provide a description of the products in this subclass); and

(E) The following subclasses of credit ratings described in Section 3(a)(62)(B)(v) of the Exchange Act (issuers of government securities, municipal securities, or securities issued by a foreign government):

(i) Sovereign issuers;

(ii) United States public finance; and

(iii) International public finance.

(2) The Transition/Default Matrices for applicable classes and subclasses of credit ratings must be presented in the same order that the classes and subclasses of credit ratings are identified in paragraphs (1)(A) through (E) above. For a given class or subclass, Transition/Default Matrices must be presented in the following order: 1-year matrix, 3-year matrix and then 10-year matrix. If the Applicant/NRSRO has not been determining credit ratings in the applicable class or subclass for the length of time necessary to produce a 1-, 3-, and/or 10-year Transition/Default Matrix, it must explain that fact in the location where the Transition/Default Matrix would have been presented in the Exhibit. The Applicant/NRSRO must clearly define, after the presentation of all applicable Transition/Default Matrices, each symbol, number, or score in the rating scale used by the Applicant/NRSRO to denote a credit rating category and notches within a category for each class and subclass of credit ratings in any Transition/Default Matrix presented in the Exhibit. In, addition the Applicant/NRSRO must clearly explain the conditions under which it classifies obligors, securities, or money market instruments as being in default. Next, the Applicant/NRSRO must provide the uniform resource locator (URL) of its corporate Internet Web site where the credit rating histories required to be disclosed pursuant to 17 CFR 17g–7(b) will be located (in the case of an Applicant) or are located (in the case of an NRSRO). Exhibit 1 must contain no performance measurement statistics or information other than as described in, and required by, these Instructions for Exhibit 1; except that the Applicant/NRSRO may provide after the presentation of all required Transition/Default Matrices and other disclosures the Internet Web site URLs where other information relating to performance

measurement statistics of the Applicant/NRSRO is located.

(3) The Transition/Default Matrices must be presented using the format of the sample matrix ("Sample Matrix") below. The top row of a Transition/Default Matrix (the "header row") must contain column headings. The first and second cells in the header row must contain the headings, respectively: "Credit Rating Scale" and "Number of Ratings Outstanding as of [insert applicable date]." The applicable date is the date 1, 3, or 10 years prior to the most recent calendar year end depending on whether the Transition/Default Matrix is for a 1-, 3-, or 10-year period. The next sequence of cells in the header row must contain, from left to right, each symbol, number, or score in the rating scale used by the Applicant/NRSRO to denote a credit rating category and notches within a category for the applicable class or subclass of credit ratings in descending order from the highest to the lowest notch. The Applicant/NRSRO must not include a "default" category if its rating scale has such a category. The next headings must be in the following order, from left to right, "Default" (see explanation below), "Paid Off" (see explanation below), and "Withdrawn (other)" (see explanation below). The first column of a Transition/Default Matrix must have a separate cell containing each symbol, number, or score in the rating scale used by the Applicant/NRSRO to denote a credit rating category and notches within a category for the applicable class or subclass of credit ratings in descending order from the highest to the lowest notch. The Applicant/NRSRO must not include a "default" category in the column if its rating scale has such a category. The last cell of the first column must contain the word "Total." Finally, the Transition/Default Matrix must have a title identifying the applicable class or subclass of credit ratings, the period covered, and the start date and end date of the period.

The Transition/Default Matrix must resemble the Sample Matrix below except that the number of credit rating symbols depicted in the cells of the first column and header row of a matrix will depend on the number of notches in the applicable rating scale of the Applicant/NRSRO (excluding a "default" category).

CORPORATE ISSUERS—10-YEAR TRANSITION AND DEFAULT RATES
[December 31, 2000 through December 31, 2010]

Credit rating scale	Number of ratings outstanding as of 12/31/2000	AAA	AA	A	BBB	BB	B	CCC	CC	C	Default	Paid off	Withdrawn (other)
AAA	10	50%	10%	.....	.....	;	.....	.....	.....	.....	.....	40%	.....
AA	2,000	1%	39%	12%	10%	8%	5%	4%	.....	.....	1%	19%	1%
A	4,000	.....	6%	34%	15%	10%	6%	4%	3%	.....	2%	18%	2%
BBB	3,600	.....	2%	9%	28%	15%	10%	6%	5%	1%	4%	17%	3%
BB	1,000	.....	.....	2%	4%	20%	14%	5%	.....	.....	2%	16%	37%
B	500	.....	.....	1%	3%	6%	20%	20%	15%	.....	15%	15%	5%
CCC	300	.....	.....	.....	.....	4%	6%	15%	25%	20%	20%	4%	6%
CC	200	.....	.....	.....	.....	.....	2%	8%	10%	38%	30%	2%	10%
C	160	.....	.....	.....	.....	.....	.....	2%	8%	10%	67%	1%	12%
Total	11,770	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....

(4) An Applicant/NRSRO must populate the cells in the columns and rows of a Transition/Default Matrix in the following manner:

(A) *Second Column Showing Number of Ratings Outstanding as of the Period Start Date.* To populate the cells of this column, the Applicant/NRSRO must determine the number of obligors, securities, and money market instruments in the applicable class or subclass of credit ratings that were assigned an outstanding credit rating as of the period start date (cumulatively, the "start-date cohort"). In determining the start-date cohort, the Applicant/NRSRO must exclude any obligors, securities, or money market instruments that the NRSRO classified as in default as of the start date. Next, the Applicant/NRSRO must determine the number of obligors, securities, and money market instruments in the start-date cohort assigned a credit rating (other than an expected or preliminary credit rating) as of the start date in each notch represented in the "Credit Rating Scale" column. The Applicant/NRSRO must populate the cells of this column with the number of obligors, securities, and/or money market instruments assigned a credit rating in each notch and in the bottom cell the total number of credit ratings in the start-date cohort.

(B) *Rows Representing Credit Rating Notches.* Each row representing a credit rating notch must contain percents indicating the credit rating outcomes of all the obligors, securities, and/or money market instruments assigned a credit rating at that notch as of the period start date. The percents in a row must add up to 100%. To compute the percents for each row representing a notch in the rating scale in the Transition/Default Matrix:

(i) The Applicant/NRSRO must determine the number of obligors, securities, and money market instruments assigned a credit rating at that notch as of the period start-date that were assigned a credit rating at the same notch as of the period end date. This number must be expressed as a percent of the total number of obligors, securities, and/or money market instruments assigned a credit rating at that notch as of the period start date and the percent must be entered in the column representing the same notch. To determine this percent, the Applicant/NRSRO must use the credit rating at the notch assigned to the obligor, security, or money market instrument as of the period end date and not a credit rating at any other notch assigned to the obligor, security, or money market instrument between the period start date and the period end date.

(ii) The Applicant/NRSRO must determine the number of obligors, securities, and money market instruments assigned a credit rating at that notch as of the period start date that were assigned a credit rating at each other notch as of the period end date. These numbers must be expressed as percents of the total number of obligors, securities, and/or money market instruments assigned a credit rating at that notch as of the period start date and the percents must be entered in the columns representing each different notch. To determine these percents, the Applicant/NRSRO must use the credit rating at the notch assigned to the obligor, security, or money market instrument as of the period end date and not a credit rating at any other notch assigned to the obligor, security, or money market instrument between the period start date and the period end date.

(iii) The Applicant/NRSRO must determine the number of obligors, securities, and money market

instruments assigned a credit rating at that notch as of the period start date that went into *Default* (see explanation below) at any time during the applicable time period. This number must be expressed as a percent of the total number of obligors, securities, and/or money market instruments assigned a credit rating at that notch as of the period start date and the percent must be entered in the *Default* column. To determine this percent, the Applicant/NRSRO must classify an obligor, security, or money market instrument as having gone into *Default* if the conditions in either (a) or (b) (or in both (a) and (b)) are met:

(a) The obligor failed to timely pay principal or interest due according to the terms of an obligation during the applicable period or the issuer of the security or money market instrument failed to timely pay principal or interest due according to the terms of the security or money market instrument during the applicable period; or

(b) The Applicant/NRSRO classified the obligor, security, or money market instrument as having gone into default using its own definition of "default" during the applicable period.

An obligor, security, or money market instrument that goes into in *Default* as defined in this paragraph (4)(B)(iii) must be classified as in *Default* even if the Applicant/NRSRO assigned a credit rating to the obligor, security, or money market instrument at a notch above default in its rating scale on or after the event of *Default* or withdrew the credit rating on or after the event of *Default.*

(iv) The Applicant/NRSRO must determine the number of obligors, securities, and money market instruments assigned a credit rating at that notch as of the period start date that *Paid Off* (see explanation below) at any time during the applicable time period. This number must be expressed as a percent of the total number of obligors, securities, and/or money market instruments assigned a credit rating at that notch as of the period start date and the percent must be entered in the *Paid Off* column. To determine this percent, the Applicant/NRSRO must classify an obligor, security, or money market instrument as *Paid Off* if the conditions in either (a) or (b) are met;

(a) The obligor extinguished the obligation during the applicable time period by paying in full all outstanding principal and interest due on the obligation according to the terms of the obligation (e.g., because the obligation matured, was called, or was prepaid); and the Applicant/NRSRO withdrew the credit rating because the obligation was extinguished; or

(b) The issuer of the security or money market instrument extinguished its obligation with respect to the security or money market instrument during the applicable time period by paying in full all outstanding principal and interest due according to the terms of the security or money market instrument (e.g., because the security or money market instrument matured, was called, or was prepaid); and the Applicant/NRSRO withdrew the credit rating for the security or money market instrument because the obligation was extinguished.

(v) The Applicant/NRSRO must determine the number of obligors, securities, and money market instruments assigned a credit rating at that notch as of the period start date for which the Applicant/NRSRO withdrew a credit rating assigned to the obligor, security, or money market instrument at any time during the applicable time period for a reason other than *Default* (as described in paragraph (4)(B)(iii)) or *Paid-Off* (as described in paragraph (4)(B)(iv)). This number must be expressed as a percent of the total number of obligors, securities, and/or money market instruments assigned a credit rating at that notch as of the period start date and the percent must be entered in the *Withdrawn (other)* column. The Applicant/NRSRO must classify the obligor, security, or money market instrument as *Withdrawn (other)* even if the Applicant/NRSRO assigned a credit rating to the obligor, security, or money market instrument after withdrawing its credit rating.

Exhibit 2. Provide in this Exhibit a general description of the procedures and methodologies used by the Applicant/NRSRO to determine credit ratings, including unsolicited credit ratings within the classes of credit ratings for which the Applicant/NRSRO is seeking registration or is registered. The description must be sufficiently detailed to provide users of credit ratings with an understanding of the processes employed by the Applicant/NRSRO in determining credit ratings, including, as applicable, descriptions of: Policies for determining whether to initiate a credit rating; a description of the public and non-public sources of information used in determining credit ratings, including information and analysis provided by third-party vendors; 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 any asset-backed or securities transaction is relied on in determining credit ratings; the quantitative and qualitative models and metrics used to determine credit ratings, including 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 securities transaction factor into the determination of credit ratings; the methodologies by which credit ratings of other credit rating agencies are treated to determine credit ratings for securities or money market instruments issued by an asset pool or as part of any asset-backed or mortgaged-backed securities transaction; the procedures for interacting with the management of a rated obligor or issuer of rated securities or money market instruments; the structure and voting process of committees that review or approve credit ratings; procedures for informing rated obligors or issuers of rated securities or money market instruments about credit rating decisions and for appeals of final or pending credit rating decisions; procedures for monitoring, reviewing, and updating credit ratings, including how frequently credit ratings are reviewed, whether different models or criteria are used for ratings surveillance than for determining initial ratings, whether changes made to models and criteria for determining initial ratings are applied retroactively to existing ratings, and whether changes made to models and criteria for performing ratings surveillance are incorporated into the models and criteria for determining initial ratings; and procedures to withdraw, or suspend the maintenance of, a credit rating. An Applicant/NRSRO may provide in Exhibit 2 the location on its corporate Internet Web site where additional information about the procedures and methodologies is located.

Exhibit 3. Provide in this Exhibit a copy of the written policies and procedures established, maintained, and enforced by the Applicant/NRSRO to prevent the misuse of material, nonpublic information pursuant to Section 15E(g) of the Exchange Act and 17 CFR 240.17g–4. Do not include any information that is proprietary or that would diminish the effectiveness of a specific policy or procedure if made publicly available.

Exhibit 4. Provide in this Exhibit information about the organizational structure of the Applicant/NRSRO, including, as applicable, an organizational chart that identifies, as applicable, the ultimate and sub-holding companies, subsidiaries, and material affiliates of the Applicant/NRSRO; an organizational chart showing the

divisions, departments, and business units of the Applicant/NRSRO; and an organizational chart showing the managerial structure of the Applicant/NRSRO, including the designated compliance officer identified in Item 4.

Exhibit 5. Provide in this Exhibit a copy of the written code of ethics the Applicant/NRSRO has in effect or a statement of the reasons why the Applicant/NRSRO does not have a written code of ethics in effect.

Exhibit 6. Identify in this Exhibit 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).

Exhibit 7. Provide in this Exhibit a copy of the written policies and procedures established, maintained, and enforced by the Applicant/NRSRO to address and manage conflicts of interest pursuant to Section 15E(h) of the Exchange Act. Do not include any information that is proprietary or that would diminish the effectiveness of a specific policy or procedure if made publicly available.

Exhibit 8. Provide in this Exhibit the following information about the Applicant/NRSRO's credit analysts and the persons who supervise the credit analysts:

- The total number of credit analysts (including credit analyst supervisors).
- The total number of credit analyst supervisors.
- A general description of the minimum qualifications required of the credit analysts, including education level and work experience (if applicable, distinguish between junior, mid, and senior level credit analysts).
- A general description of the minimum qualifications required of the credit analyst supervisors, including education level and work experience.

Exhibit 9. Provide in this Exhibit the following information about the designated compliance officer (identified in Item 4) of the Applicant/NRSRO:

- Name.
- Employment history.
- Post secondary education.
- Whether employed by the Applicant/NRSRO full-time or part-time.

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 person 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. For purposes of this Exhibit:

Net revenue means revenue earned by the Applicant for any type of service or product provided to the person, regardless of whether related to credit rating services, and net of any rebates and allowances the Applicant paid or owes to the person; and

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. An NRSRO is not required to make this Exhibit publicly available on its corporate Internet Web site, 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. (Note: After registration, Exhibit 10 should not be updated with the filing of the annual certification. Instead, similar information must be filed with the Commission not more than 90 days after the end of each fiscal year pursuant to Exchange Act Rule 17g–3).

Exhibit 11. Provide in this Exhibit the financial statements of the Applicant, which must include a balance sheet, an income statement and statement of cash flows, and a statement of changes in ownership equity, audited by an independent public accountant, for each of the three fiscal or calendar years ending immediately before the date of the Applicant's initial application to the Commission, subject to the following:

- If the Applicant is a division, unit, or subsidiary of a parent company, the Applicant may provide audited consolidated financial statements of its parent company.
- If the Applicant does not have audited financial statements for one or

more of the three fiscal or calendar years ending immediately before the date of the initial application, the Applicant may provide unaudited financial statements for the applicable year or years, but must provide audited financial statements for the fiscal or calendar year ending immediately before the date of the initial application.

Attach to the unaudited financial statements a certification by a person duly authorized by the Applicant to make the certification that the person has responsibility for the financial statements and that to the best knowledge of the person making the certification the financial statements fairly present, in all material respects, the Applicant's financial condition, results of operations, and cash flows for the period presented.

An NRSRO is not required to make this Exhibit publicly available on its corporate Internet Web site, 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. (Note: After registration, Exhibit 11 should not be updated with the filing of the annual certification. Instead, similar information must be filed with the Commission not more than 90 days after the end of each fiscal year pursuant to Exchange Act Rule 17g–3).

Exhibit 12. Provide in this Exhibit the following information, as applicable, and which is not required to be audited, regarding the Applicant's aggregate revenues for the fiscal or calendar year ending immediately before the date of the initial application:

- Revenue from determining and maintaining credit ratings;
- Revenue from subscribers;
- Revenue from granting licenses or rights to publish credit ratings; and
- Revenue from all other services and products offered by your credit rating organization (include descriptions of any major sources of revenue).

An NRSRO is not required to make this Exhibit publicly available on its corporate Internet Web site, 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. (Note: After registration, Exhibit 12 should not be updated with the filing of the annual certification. Instead, similar information must be filed with the Commission not more than 90 days after the end of each fiscal year pursuant to Exchange Act Rule 17g–3).

Exhibit 13. Provide in this Exhibit the approximate total and median annual compensation of the Applicant's credit analysts for the fiscal or calendar year ending immediately before the date of this initial application. In calculating total and median annual compensation, the Applicant may exclude deferred compensation, provided such exclusion is noted in the Exhibit.

An NRSRO is not required to make this Exhibit publicly available on its corporate Internet Web site 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. (Note: After registration, Exhibit 13 should not be updated with the filing of the annual certification. Instead, similar information must be filed with the Commission not more than 90 days after the end of each fiscal year pursuant to Exchange Act Rule 17g–3).

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. NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATION [Section 3(a)(62) of the Exchange Act]—A credit rating agency that:

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

7. PERSON WITHIN AN APPLICANT/NRSRO—The person filing or furnishing, as applicable, 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).

8. 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.

8. 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.

19. Section 249b.400 and Form ABS Due Diligence-15E are added to read as follows:

§ 249b.400 Form ABS Due Diligence-15E, Certification of third-party provider of due diligence services for asset-backed securities

Note: The text of Form ABS Due Diligence-15E will not appear in the Code of Federal Regulations.

BILLING CODE 8011–01–P

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM ABS DUE DILIGENCE-15E

CERTIFICATION OF PROVIDER OF THIRD-PARTY DUE DILGENCE SERVICES FOR ASSET-BACKED SECURITIES

Pursuant 17 CFR 240.17g-10, this Form must be used by a person providing third-party due diligence services in connection with an asset-backed security to comply with Section 15E(s)(4)(B) of the Securities Exchange Act of 1934 (15 U.S.C. 78o-7(s)(4)(B)). Section 15E(s)(4)(B) of the Securities Exchange Act of 1934 requires a person providing the due diligence services to provide a written certification to any nationally recognized statistical rating organization that produces a credit rating to which such due diligence services relate.

Item 1. Identity of the person providing third-party due diligence services

Legal Name:_____

Business Name (if Different):_____

Principal Business Address:_____

_____

Item 2. Identity of the person who paid the person to provide due diligence services

Legal Name:_____

Business Name (if Different):_____

Principal Business Address:_____

_____

Item 3. Credit rating criteria

If the manner and scope of the due diligence performed by the third party satisfied the criteria for due diligence published by a nationally recognized statistical rating organization, identify the nationally recognized statistical rating organization and the title and date of the published criteria (more than one nationally recognized statistical rating organization can be identified).

Identity of NRSRO	Title and Date of Criteria

Item 4. Description of the due diligence performed

Provide a description of the scope and manner of the due diligence services provided in connection with the review of assets that is sufficiently detailed to provide an understanding of the steps taken in performing the review. Include in the description: (1) the type of assets that were reviewed; (2) the sample size of the assets reviewed; (3) how the sample size was determined and, if applicable, computed; (4) whether the quality or integrity of information or data about the assets provided, directly or indirectly, by the securitizer or originator of the assets was reviewed and, if so, how the review was conducted; (5) whether the origination of the assets conformed to stated underwriting or credit extension guidelines, standards, criteria or other requirements was reviewed and, if so, how the review was conducted; (6) whether the value of collateral securing such assets was reviewed and, if so, how the review was conducted; (7) whether the compliance of the originator of the assets with federal, state and local laws and regulations was reviewed and, if so, how the review was conducted; and (8) any other type of review conducted with respect to the assets. This description should be attached to the Form and contain the heading "Item 4." Provide this description regardless of whether the due diligence performed satisfied the criteria for minimum due diligence published by a nationally recognized statistical rating organization.

Item 5. Summary of findings and conclusions of review

Provide a summary of the findings and conclusions that resulted from the due diligence services that is sufficiently detailed to provide an understanding of the findings and conclusions that were conveyed to the person identified in Item 2. This description should be attached to the Form and contain the heading "Item 5."

CERTIFICATION

The undersigned has executed this Form ABS Due Diligence 15E on behalf of, and on the authority of, the person identified in Item 1 of the Form. The undersigned, on behalf of the person, represents that the person identified in Item 1 of the Form conducted a thorough review in performing the due diligence described in Item 4 attached to this Form and that the information and statements contained in this Form, including Items 4 and 5 attached to this Form, which are part of this Form, are accurate in all significant respects.

Name of Person Identified in Item 1:_____

By:_____
(Print name of duly authorized person) (Signature)

Date:_____

By the Commission.

Dated: May 18, 2011.

Elizabeth M. Murphy,

Secretary.

[FR Doc. 2011–12659 Filed 6–7–11; 8:45 am]

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