

July 25, 2008

Ms. Florence E. Harmon
Acting Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: File Number S7-13-08

Dear Ms. Harmon,

On behalf of Rapid Ratings International Inc. ("Rapid Ratings") we are pleased to submit these comments to the U.S. Securities and Exchange Commission (the "Commission") in response to Release No 34-57967, Proposed Rules for Nationally Recognized Statistical Rating Organizations ("NRSROs").

Rapid Ratings is a subscriber-paid credit rating firm that employs proprietary quantitative models to produce Financial Health Ratings (FHRs™) on listed and unlisted companies in the US and abroad using only historical corporate financial information.

We have had an excellent track record for the last 10 years in anticipating the deterioration, distress, default and turnaround of securities issuers months and years prior to issuer-paid rating agencies, CDS spreads, share prices and models which employ market signals.

Our niche in the market is to provide early warning signals about the creditworthiness and underlying financial health of issuers, a service of increasing importance since the collapse of Enron, WorldCom, Global Crossing and others. Rapid Ratings does not rate asset-backed securities.

We recognize that in the three related recommendations announced in June 2008 the Commission has completed an extensive review of the actions, and consequences of actions, of the NRSROs and other players involved in the recent structured products/sub-prime crisis. We believe that the largest of the NRSROs, and other market participants, clearly had a material role in the circumstances that led to the current credit volatility and general financial market dislocation.

The stated intent of the Credit Rating Agency Reform Act of 2006 (the "Rating Agency Act") was to "improve ratings quality for the protection of investors and in the public interest by fostering

accountability, transparency and competition in the credit rating industry.”¹ We agree that these are worthy and necessary goals. Although these goals were not wholly achieved by the Rating Agency Act, we commend the Commission’s efforts to bring transparency to aspects of the structured products ratings business now. The disclosure of ratings criteria and due diligence measures and the public availability of data on collateral underlying structured products are positive steps for providing insight and accountability into this industry.

However, we believe some aspects of the current proposed rules, specifically those addressing conflicts of interest, do not push far enough, and do not truly address the core issues of conflict at hand. We expand on this point further below.

More troubling is that it seems there has been an unintended consequence of the proposed rules amendments. Elements of the proposed rules run counter to the Commission’s stated objective to foster competition in the ratings business and do not assist in creating a “level playing field” for issuer-paid NRSROs and subscriber-paid NRSROs. In its efforts to increase transparency with the Proposed Rules, the Commission is erecting a significant new barrier to competition and fostering de facto support of the issuer-paid firms. As an inadvertent result of the Commission’s new proposals, subscriber-paid NRSROs would be materially disadvantaged.

The Commission estimates that approximately 30 rating agencies will register as NRSROs, a 200% increase from present numbers. We caution the Commission that, if all the proposed rules are passed following this comment period, this number is an unlikely, optimistic projection.

In the recent credit market turmoil one or more NRSROs withheld information from the market about certain risk factors affecting the likelihood of default and loss given default for certain structured products. This behavior is being addressed, among other things, by the requirement for all NRSROs to make all of their ratings and their rating actions available to the public. On the surface, this will mean that external, objective observers can assist the market to learn which rating agencies offer the most accurate and timely services. However, there is a major level playing field consequence that apparently was either overlooked or dismissed. If this proposal is enacted, and all NRSROs are required to present their ratings and ratings histories free of charge on their websites, it will severely undermine the business model of subscriber-paid NRSROs, regardless of the time lag (e.g. 6mo, 1yr, 2yr) embedded into the rule. This is a major new barrier to entry and creates a significant disincentive to apply for the NRSRO designation.

Our ratings are the foundations for our products, and not being compensated by issuers presents a key foundation for our unconflicted, independent voice. We must remember that a key economic motivation of the issuers in paying for ratings is to get their bonds sold. Thus, the issuers primarily pay for the “marketing” service the issuer-paid NRSROs provide (the “toll” to

¹ Report of the Senate Committee on Banking, Housing, and Urban Affairs to Accompany S. 3850, Credit Rating Agency Reform Act of 2006, S. Report No. 109-326, 109th Cong., 2d Sess. (Sept. 6, 2006)

access the capital markets), not for the information provided in the ratings. This of course is why the issuer-paid NRSROs are less affected by a requirement to provide free ratings; they've already been paid irrespective of whether the ultimate consumers (investors) of the ratings actually use, or even ask for, the ratings. Our business, in contrast, is built solely upon subscribers' requesting and paying for our ratings. We expand on this point further below.

The focus in the proposals mainly deals with the failings of the issuer-paid ratings model. This is appropriate given that, either by commission or omission, they were the source of some of the problems in the sub-prime crisis. Unfortunately, the discussion of solutions remains centered on fixing the issuer-paid model, where some of the problems are irremediable, and ignores the value of the solutions that can be brought to bear by creating a level playing field for subscriber-paid ratings firms.

Greater objectivity, independence and accountability from the dominant NRSROs are expected to flow from a reduction of the potential for conflicts of interest which arose, in part, from dominant NRSRO participation in the design of structured products such as residential mortgage-backed securities. But left unaddressed is the more compelling fact that the business model of the dominant NRSROs naturally invites conflict of interest because the rating agencies are paid directly by the issuers of securities. As long as regulations directly or indirectly favor issuer-pay NRSROs over subscriber-paid rating agencies, the potential to raise the ethical standards of the incumbent NRSROs will be undermined. Ironically before the 1970s, the subscriber-paid model, which has the best potential for protecting the interests of investors, was the dominant rating agency business model.

In the following pages we provide answers to many of the specific questions asked in the Proposed Rules as well as comments to some of the critical topics.

II. PROPOSED AMENDMENTS

A. Amendments to Rule 17g-5

1. Addressing the Particular Conflict Arising from Rating Structured Finance Products by Enhancing the Disclosure of Information Used in the Rating Process

a. The Proposed Amendment

from page 39: **Unsolicited Ratings**

Q: Would the information proposed to be required to be disclosed sufficient to permit the determination of an unsolicited credit rating? Conversely, would the proposed amendment require the disclosure of more information than would be necessary to permit the determination of an unsolicited credit rating? Commenters believing more information should be disclosed should specifically describe the additional information and the practicality of requiring its disclosure, while commenters believing that less information should be disclosed should specifically describe what information would be unnecessary and explain why it would be unnecessary to disclose.

A: This is not directly applicable to Rapid Ratings as we rate corporate entities from their publicly disclosed financials and private companies from financials provided to us from various customers. As such, we cannot comment sufficiently on the completeness of this disclosure for the purposes of conducting structured asset class ratings.

We note for the Commission that the very term “Unsolicited Ratings” has its origins in the issuer-paid paradigm and its continued use carries an issuer-paid bias and indeed a negative bias when unsolicited ratings were thought to be a coercive technique by a particular NRSRO to force unrated 144A issuers into paying for their ratings services. As stated on Page 30 “As used herein, an “unsolicited rating” is one that is determined without the consent and/or payment of the obligor being rated or issuer, underwriter, or arranger of the securities being rated.”

In Rapid Ratings’ estimation, our ratings are “solicited” because we are paid by our customers who want to have ratings on companies, and we provide those ratings from publicly available information without regard to a company’s desire to be rated (or not). We have no contact whatsoever with the companies we rate and have no insight into their views on our ratings. In fact, we rate companies based on financial statements’ being available and some are not even issuers of debt securities. Are our ratings solicited? They are not solicited by issuers but they are solicited by subscribers to our products.

Disclosure Requirements vs, Safe Harbor

Q: The proposed amendment would require the disclosure of information provided to an NRSRO by the “issuer, underwriter, sponsor, depositor, or trustee” based on the Commission’s preliminary belief that these would be the parties relevant to an NRSRO’s performance of the ratings process, i.e., that taken together, these are the parties that would provide all relevant information to the NRSRO. Are there other entities that should be included in this category?

And

Q: Should the Commission provide a “safe harbor” so that an NRSRO that obtained a representation from one or more parties to a transaction to disclose the required information would not be held in violation of the rule if the party did not fulfill its disclosure obligations under the representation?

A: No other entities should be included. Ultimately the responsibility should lie with the NRSRO to disclose or verify that all information to which they have been privy is disclosed, regardless of the discloser unless the disclosure breaches property rights or promotes breach of contract. If the NRSRO is not the elected party performing the disclosure, it should not be exempt from this responsibility. If, for instance, the arranger/investment bank assumed the responsibility for the disclosure and de facto indemnified the NRSRO from this responsibility that could be construed as, or be manipulated into, a “gift.” The arranger prepared to assume this responsibility/liability could become a favored counterparty for the NRSRO. This type of

potential behavior could become a competitive tool for the arranger and curry favor from the NRSRO. Essentially, assumption of liability is a valuable currency.

From page 40 **Asset Disclosure**

Q: Should the Commission also require the disclosure of information about the steps, if any, that were taken by the NRSRO, issuer, underwriter, sponsor, depositor, or trustee to verify information about the assets underlying or referenced by the security or money market instrument, or, if no such steps were taken, a disclosure of that fact?

A: Yes. The current NRSROs have not comported themselves in a way that fosters benefit of doubt in their due diligence or inclination towards forthcoming disclosure. Requiring their participation in full asset disclosure is seemingly necessary.

Competition Implications of Disclosure Timing Issues

Q: Would the disclosure of the initial information on the pricing date provide enough time for other NRSROs to determine unsolicited ratings before the securities were sold to investors? If not, would it be appropriate to require that this information be disclosed prior to the pricing date? Alternatively, would it be more appropriate to require NRSROs hired by the arranger to wait a period of calendar or business days (e.g. 2, 4, 10 days) after the asset pool is settled upon by the arranger before issuing the initial credit rating in order to provide other NRSROs with sufficient time to determine an unsolicited rating?

A: Rapid Ratings does not have an opinion on the time necessary required to rate structured products from first receipt of data. However, if the Commission is attempting to promote greater due diligence by the investment community buying these products, it is incumbent upon the Commission to enable multiple sources of information to be digested by market participants. If not, the Commission is inadvertently promoting the buyers' reliance on the handful of NRSRO's ratings (with which they are most familiar) alone in the shortest time frame to act in order to accept pricing. This is counterproductive to the stated goal of promoting greater investor research and due diligence. Allowing for a lead period is essential to have any other ratings system digest and provide an opinion (fundamental or quantitative) on the data underlying the structured product.

We note that most investors cannot perform thorough due diligence on many complex structured products from a prospectus alone. Given the nature of the underlying data to which the issuer-paid NRSROs have been privy in the ratings process that is not included in the prospectus, investors have necessarily deepened their reliance on these agencies. Full disclosure of information is the only way to provide alternate analytical opinions/ratings and to promote satisfactory due diligence by securities' buyers.

Disclosure of Verification Steps

Q: Should the Commission also require the disclosure of the results of any steps taken by the NRSRO, issuer, underwriter, sponsor, depositor, or trustee to verify information about the assets underlying or referenced by a structured finance product? Alternatively, should the

Commission require a general disclosure of whether any steps were taken to verify the information and, if so, a description of those steps?

A: Yes. Please see both answers immediately above.

Unsolicited Ratings and Related Disclosure Issues

Q: Do NRSROs obtain information about the underlying assets of structured products – particularly in the surveillance process – from third-parties such as vendors rather than from issuers, underwriters, sponsors, or trustees? If so, would it be necessary to require the disclosure of this information as proposed or can the goals of the proposed amendments in promoting unsolicited ratings be achieved under current practices inasmuch as the information necessary for surveillance can be obtained from third-party vendors, albeit for a fee?

A: Yes. Please see answers above.

2. Rule 17g-5 Prohibition on Conflict of Interest Related to Rating an Obligor or Debt Security where Obligor or Issuer Received Ratings Recommendations from the NRSRO or Person Associated with the NRSRO

From page 61 Conflict of Interest for Issuer-Paid Rating Agencies

Q: Is this type of conflict one that could be addressed through disclosure and procedures to manage it instead of prohibiting it? Should the Commission, rather than prohibiting it, add this type of conflict to the list of conflicts in paragraph (b) of Rule 17g-5, which, under paragraph (a) of the rule, must be addressed through disclosure and procedures to manage them?

A: We agree with the Commission’s statement on page 60 of the proposed rules release that “The information provided by the NRSRO during the rating process allows the arranger to better understand the relationship between model outputs and the NRSRO’s decisions with respect to necessary credit enhancement levels to support a particular rating. The arranger then can consider the feedback and determine independently the steps it will take, if any, to adjust the structure, credit enhancement levels, or asset pool. However, if the feedback process turns into recommendations by the NRSRO about changes the arranger could make to the structure or asset pool that would result in a desired credit rating, the NRSRO’s role would transition from an objective credit analyst to subjective consultant.”

However, we think the preamble to the third question on page 61 addresses this question accurately “The Commission recognizes that the line between providing feedback during the rating process and making recommendations about how to obtain a desired rating may be hard to draw in some cases.”

We believe that in practice this separation is extremely difficult to police. There is a fine line between an arranger’s receiving advice and receiving multiple rounds of feedback from which “advice” can be derived. At the least this should be prohibited, but even this will only be a partial measure and will not completely insulate the entities from the potential of a conflict.

These intrinsic conflicts of interest can be overcome by the use of subscriber-paid rating agencies, assuming they have access to the data necessary to conduct the rating.

From page 61

Q: “Would there be practical difficulties for an NRSRO that is part of a large conglomerate in monitoring the business activities of persons associated with the NRSRO such as affiliates located in other countries to comply with the proposed requirement? If so, given the greater separation between the NRSRO and these types of persons associated with the NRSRO, should the Commission require instead that, for these types of persons associated with the NRSRO only, the NRSRO disclose this conflict and manage it through information barriers rather than prohibit it?”

A: To the extent rules and restrictions exist for an NRSRO’s activities, it should be required to maintain these standards throughout its global network. Further, the discipline with which such an entity manages the “firewall” between its parent and the NRSRO should be the discipline applied in managing subsidiaries and JVs globally. These NRSROs should be required to maintain records of internal audit procedures of such firewalls.

3. Rule 17g-5 Prohibition on Conflict of Interest Related to the Participation of Certain Personnel in Fee Discussions

The Commission’s addressing this conflict issue is of paramount importance, although there is little it can do to eliminate the conflict as long as the current issuer-paid revenue model is employed by NRSROs.

As stated on Page 62, “The Commission is proposing to amend Rule 17g-5 by adding a new paragraph (c)(6) of Rule 17g-5 to address the conflict of interest that arises when a fee paid for a rating is discussed or arranged by a person within the NRSRO who has responsibility for participating in determining credit ratings (including analysts and rating committee members) or for developing or approving procedures or methodologies used for determining credit ratings, including qualitative and quantitative models.”

“While the incentives of the persons discussing fees could be based primarily on generating revenues for the NRSRO; the incentives of the persons involved in the analytical process should be based on determining accurate credit ratings.”

While the primary functions can be divided, it is impossible for an analyst to ignore the broader implications of market share on the firm’s well being, their individual job security and compensation. We’d like to point out that based on the “Summary Report of Issues Identified in the Commission Staff’s Examinations of Select Credit Rating Agencies” released July 8, 2008, conflicts of interest regarding NRSRO staff involvement in market share considerations existed in at least one rating agency. The only fool-proof way to avoid this conflict is to move from an issuer-paid revenue model to the subscriber-paid model. If this cannot be achieved in the short-term, the objective should be to achieve this objective over the medium to long-term. For

example, systematic and progressive steps should be taken to withdraw NRSRO references in legislation, which have been proposed in the third release of Proposed Rule Amendments. Without such efforts, this inherent potential conflict among the issuer-paid agencies will always exist.

Q: Should the proposed prohibition also be extended to cover participation in fee negotiations by NRSRO personnel with supervisory authority over the NRSRO personnel participating in determining credit ratings or developing or approving procedures or methodologies used for determining credit ratings?

A: If the Commission is going to institute a separation it should strive for as pure a solution as possible; this means a complete separation. As stated above, this separation still does not solve the potential for a conflict to exist. However, anything short of a full separation further waters down an already imperfect solution.

From Page 63

Q: Instead of prohibiting this conflict outright, would disclosure and procedures to manage the conflict adequately address the conflict? If so, what specific disclosures should be required? What other measures should be required in addition to disclosures?

A: Disclosure alone is completely insufficient.

Q: Would there be practical difficulties in separating analytic and fee discussions for a small NRSRO, including one that has limited staff, that are significant enough that the Commission should consider a different mechanism to address the conflict? If so, what sort of mechanism and with what conditions? Should the Commission adopt an exemption from the prohibition for small NRSROs and, instead, require them to disclose the conflict and establish procedures to manage it? For example, the exemption could apply to NRSROs that have less than 10, 20, or 50 associated persons. Commenters that endorse an exemption for small NRSROs should provide specific details as to how the Commission should define an NRSRO as “small” for purposes of the exemption. For example, for purposes of the Final Regulatory Flexibility Analysis for the Adopting Release the Commission concluded that an NRSRO with total assets of \$5 million or less was a “small” entity for purposes of the Regulatory Flexibility Act. Would that be an appropriate way to define a small NRSRO for purposes of this exemption?

A: We believe that if NRSROs are paid by issuers their size is irrelevant. The conflict of interest potential is not alleviated through disclosure for either large or small NRSROs. In general, new entrants into the ratings space will be disinclined to enter as issuer-paid agencies, so this is likely a moot point. However, if a new entrant does indeed pursue this revenue model, they should be able to factor into their business model and cost structure an infrastructure to accommodate this regulatory requirement

4. Rule 17g-5 Prohibition of Conflict of Interest Related to Receipt of Gifts

We believe these measures (and the questions posed on Pages 66 and 67) are, by and large, superficial changes when the conflicts of interests run deeper than these recommendations address.

B. Amendments to Rule 17g-2

1. A Record of Rating Actions and the Requirement that they be made Publicly Available

From pages 72-74

Q: Is the six-month delay before publicly disclosing a rating action sufficiently long to address the business concerns of the subscriber-based NRSROs and the issuer-paid NRSROs? Should the delay be for a longer period such as one or two years or even longer? Alternatively, is six months too long and should it be a shorter period of time such as three months or even shorter?

A: Unfortunately, the requirement to publicly disclose ratings data disproportionately disadvantages the subscriber-paid ratings companies. We believe that this one recommendation is, in fact, anti-competition because it creates a major new regulatory barrier to entry and de facto support of the issuer-paid agencies. This runs against the grain of the objectives in the Credit Rating Agency Reform Act of 2006 and it runs counter to the Commission's and Chairman Cox's stated goal to foster competition. The Chairman's goal of having 30 NRSROs in the coming years will almost certainly fail if this amendment is passed. The market does not need a dozen more issuer-paid rating agencies with their embedded conflicts of interest. It needs more subscriber-paid rating agencies which offer independent, objective, timely and accurate information that investors can count on to objectively quantify their risks. When investors lose confidence in the integrity of the investment process, economic growth slows and the potential for market instability increases.

A two year ratings embargo is more tolerable than a 6 month period but is not ultimately the point. Subscriber-paid businesses survive and grow based on their ability to package their ratings and to sell them to interested parties. Sometimes these sales are of historical data or include historical data. Releasing these for free is detrimental to a company like ours.

Rapid Ratings employs a proprietary electronic risk profiling system that takes advantage of historical data to generate degrees of differences in profiles across risk categories in order to assess current versus future risk. It is a technically advanced, econometrically calibrated global benchmarking credit risk system with forward looking (1-3 years ahead) projections based on profiles developed from historical data of companies at various stages of the business cycle. Given this insight, it is easy to understand how our historical ratings are of great and actionable value for years after their initial production.

It is unclear if the intent of the Commission's recommendations is to have this requirement extend beyond the structured products asset class. If it is intended to have this requirement extend to corporate ratings, and if this amendment is passed, Rapid Ratings is unlikely to apply for NRSRO status. Our system is a series of complex, econometrically calibrated, quantitative models. The methodology is proprietary and is our key intellectual property. The obvious revenue impact aside, the more data we produce for free, general consumption, and further facilitate its use by publishing in XBRL, the more we open ourselves to attempts at IP theft.

Q: Should the rule require that a notice be published along with the XBRL Interactive Data File warning that because of the permitted delay in updating the record some of the credit ratings in the record may no longer reflect the NRSRO's current assessment of the creditworthiness of the obligor or debt security? For example, the notice could explain that the information in the record is six months old and state that the credit ratings contained in record may not be up-to-date.

A: Please see above answer.

Q: Are there ways in which the NRSROs should be required to sort the credit ratings contained on the record such as by asset class or type of ratings?

A: Please see above answer.

Q: What mechanisms are appropriate for identifying rated securities? Are there other identifiers in addition, or as an alternative, to CUSIP or CIK number that could be used in the rule?

A: Please see above answer. The numerical identifiers for companies and securities should be free.

Q: Should the Commission allow the ratings action data to be provided in a format other than XBRL, such as pipe delimited text data ("PDTD") or eXtensible Markup Language ("XML")? Is there another format that is more widely used or would be more appropriate than XBRL for NRSRO data? What are the advantages/disadvantages of requiring the XBRL format?

A: Please see above answer.

Q: Should the Commission require that the information on the assets underlying a structured finance products discussed in Section II.A.1.a above be provided in a specific format such as PDTD, XML, or XBRL? Again, is there another format that is more widely used or would be more appropriate for such data? What are the advantages/disadvantages of requiring a specific format?

A: Please see above answer.

Q: Should the Commission take the lead in creating the new tags that are needed for the XBRL format or should it allow the tags to be created by another group and then review the tags? How long would it take to create new tags?

A: Please see above answer.

Q: The Commission anticipates that the data provided by NRSROs would be simple and repetitive (i.e. the data would be name, CUSIP, date, rating, date, rating, etc.). Is there a need for more detailed categories of data?

A: Please see above answer.

Q: What would be the costs to an NRSRO to provide data in the XBRL format? Would there be a cost burden on smaller NRSROs? Is there another format that would cost less but still allow investors and analysts to easily download and analyze the data?

A: Please see above answer.

Q: Should the Commission institute a test phase for providing this information in an XBRL format (such as a voluntary pilot program, similar to what it is currently doing for EDGAR filings)? How long should this test phase last?

A: Please see above answer.

Q: Where is the best place to store the data provided by NRSROs? Currently, information that needs to be made publicly available is stored on each NRSRO's Web site. Should the Commission create a central database to store the information? If so, should it use the EDGAR database or should it create a new database?

A: Please see above answer.

One alternative solution to this performance disclosure issue is to determine a series of measures against which all NRSROs would be required to test their results uniformly. The ratings data behind the tests could be disclosed to the Commission with confidentiality protected. Then the standardized results could be released into the market. While this will not facilitate creative members of the public to do their own testing of the data, it will allow significant protection to the NRSROs giving up their intellectual property.

2. A Record of Material Deviation from Model Output

From page 78

Q: Are there certain types of rated products (e.g., corporate debt, municipal bonds) which generally employ a quantitative model as a substantial component of the ratings process?

Commenters should identify the types of bonds and a general description of the models used to rate them.

A: Rapid Ratings currently provides Financial Health Ratings on companies and banks (most issue bonds while some have no debt securities), not on any particular issue. Our system is entirely quantitative and has no analyst overrides under any circumstances. We anticipate introducing a system for rating securities in the coming months strictly using our quantitative tools.

Page 78

Q: Are there alternative types of records that may be created or retained by an NRSRO that would allow the Commission to understand when and why an NRSRO's final rating differed materially from the rating implied by the model?

A: It is possible for NRSROs to keep all output from their models and to provide disclosure on deviations created by analysts' overrides. These data, if provided to the Commission, would allow the Commission to determine if, over time, an NRSRO altered the standards for their fundamental override of quantitative models or whether the NRSRO maintained consistent standards for deviating from its model.

3. Records Concerning Third-Party Analyst Complaints

From page 80

Q: In addition to the proposed recordkeeping requirement, should the Commission require the NRSROs to publicly disclose when an analyst has been re-assigned from the responsibility to rate an obligor or the securities of an issuer, underwriter, or sponsor?

A: All Rapid Ratings' Financial Health Ratings are produced by our quantitative system and we employ no analysts. However, we believe that this disclosure should be required of the NRSROs as it is integral to the full disclosure of the issuer-paid NRSRO's relationship with their customers (issuers and investment banks).

From page 81

Q: Should the Commission require NRSROs to retain any communications containing a request from an obligor, issuer, underwriter, or sponsor that the NRSRO assign a specific analyst to a transaction in addition to the proposed requirement to retain complaints about analysts?

A: Yes

4. Clarifying Amendment to Rule 17g-2(b)(7)

From Page 81

Q: Should the Commission delete the term “maintaining” from paragraph (b)(7) and proposed new paragraph (b)(8) of Rule 17g-2 as it has the same meaning as “monitoring?”

A: Yes

C. Amendments to the Instructions for Form NRSRO

We note that “the Commission preliminarily believes it can prescribe generic requirements for the performance statistics that would accommodate the different procedures and methodologies used by the NRSROs.” We also note that the new performance measures required are largely directed at the credit rating agencies that have rated asset-backed securities as specified under Section 3(a)(62)(B)(iv) of the Credit Rating Agency Reform Act of 2006. The requirements do not suggest strong confidence by the SEC in the traditional rating agencies. Yet these requirements will set a precedent that may very well impose excessive compliance costs on small rating agencies, notably subscriber-paid rating agencies, that have not stumbled in the market. The Commission should treat this as a “preliminary exercise” and not as cast in stone until it is clear that the compliance cost burden on small NRSROs and new entrants is not excessive.

D. Amendment to Rule 17g-3 (Report of Credit Rating Actions)

From page 96

Q: Could the performance statistics currently required in Exhibit 1 to Form NRSRO, as well as the proposed enhancements to those statistics, be used to target potential problem areas in an NRSRO’s credit rating processes in the same manner as this proposed report thereby making the report redundant?

A: The most important actions that the Commission can take to improve rating performance in the market place are: (1) to create a level playing field between the issuer-paid rating agencies and the subscriber-paid rating agencies; (2) prevent new barriers to entry during these current proposals; and (3) systematically eliminate NRSRO references in regulations throughout the US.

Q: Should the Commission also require NRSROs to furnish an “early warning” report to the Commission when the number of downgrades in a class of credit ratings passes a certain percentage threshold (e.g. 5%, 10%, 15%, or 20%) within a number of calendar or business days (e.g. 2, 5, 10, or 15 days) after the threshold is passed, similar to the broker-dealer notification rule (See 17 CFR 240.17a-11)?

A: By the time that a traditional issuer-paid rating agency starts to downgrade large numbers of assets or companies it is only confirming to the world a crisis of which much of the market is already aware. The Commission should not confuse the quantity of action with the quality of action. The secrets of credit risk in the market are not uncovered by the quantity of upgrades or downgrades by the traditional rating agencies. They are discovered by (1) using the right tools to determine credit risk, and (2) minimizing or eliminating conflicts of interest through enhanced competition by independent rating agencies.

III. PROPOSED NEW RULE 17g-7 (SPECIAL REPORTING OR USE OF SYMBOLS TO DIFFERENTIATE CREDIT RATINGS FOR STRUCTURED FINANCE PRODUCTS)

Our views on the proposed 17g-7 are broad and cover all the respective questions posed in this section of the release.

We support paragraph (a) of the proposed Rule 17g-7 requiring (from Page 97) “an NRSRO to publish a report accompanying every credit rating it publishes for a security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction that describes the rating methodology used to determine the credit rating and how it differs from a rating for any other type of obligor or debt security and how the risks associated with a security or money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction are different from other types of rated obligors and debt securities.” We believe that this is a reasonable proposal and would alleviate some of the potential misconceptions about the nature of some ratings and/or the asset classes being rated.

However, we disagree that concern should be paid to the (from Page 97) “...possible risk associated with this approach is that investors would come to view such reports as “boilerplate” and therefore would not review them.” Users of these ratings should bear the responsibility of treating these reports with due consideration. If they begin treating the reports as “boilerplate,” that would be no worse than how they presently consider the current NRSRO’s ratings.

Further, we strongly disagree with the Commission that (from Page 98) “...preliminarily believes that permitting an NRSRO to comply with the rule by differentiating its structured finance product rating symbols would be an equally effective alternative. The differentiated symbol would alert investors that a structured product was being rated and, therefore, raise the question of how it differs from other types of debt instruments.” The Commission also states that it “is not proposing to require that specific rating symbols be used to distinguish credit ratings for structured finance products. An NRSRO would be permitted to choose the appropriate symbol.” We believe that this is a very problematic proposal. The goal of the Commission and the market at large should be to have risks measured accurately by NRSROs, not to allow for a further and confusing disaggregation of rating systems and measures. In so doing, the Commission will inadvertently create greater confusion among investors and other users of these ratings. The NRSROs should be required to be consistent in their use of rating scales and rating notches across all assets and this can only be accomplished by enforcing apples to apples comparisons.

Further, investors should not be buying structured securities thinking they are buying vanilla paper. If there are truly institutional investors that would buy a CDO Squared thinking they are buying a vanilla bond, natural selection will eliminate that problem in the short to medium term. Adding potentially dozens of new ratings scales to the landscape to protect the few

investors that do not properly conduct due diligence is not the answer. It is only a diversion from effective action.

Have all of the options for dealing with structured products been considered? We think that this discussion is only just beginning rather than ending. For example, Ed Grebeck has recommended that structured finance products be treated as alternative assets (subject to separate underwriting due diligence and analysis by purchaser), from a regulatory standpoint. This would force structured finance debt-buyers to build dedicated teams and buy knowledgeable or exit the activity. To prevent "regulatory arbitrage", all structured finance deals on the books today can retain zero capital charge through maturity. All structured finance deals acquired from tomorrow and thereafter would require higher charges.

That is worth considering. The door should not be closed to new ideas about how to deal with the risk that arose in this complex market. If we are not careful, the solutions proposed today will become the genesis of tomorrow's problems. More thought needs to be given to long-term solutions, as opposed to short-term fixes.

Summary

In brief, the SEC is pursuing an important but only partial encirclement of the conflict of interest problem which fails to address the main problem that the dominant NRSROs are paid by issuers and are thus conflicted in their core business. Secondly, while there are a number of welcome transparency enhancements, there is a fundamental flaw that threatens the entry of subscriber-paid rating agencies. That flaw forces the subscriber-based rating agencies to disclose all their ratings, clearly curtailing their primary source of revenue.

The Commission will have succeeded in its regulatory revisions if the dominant NRSROs complain about the results, rather than cautiously welcoming them, and if the new entrants to the NRSRO market sense that they face a level playing field between issuer-paid rating agencies and investor-paid rating agencies. If not, then this round of regulatory change will be only another exercise in postponing more effective remedies.

These regulatory interventions are becoming more frequent. That should be a signal that fundamental and sustainable change is required that does not disproportionately benefit the incumbent NRSROs that have so disproportionately contributed to the current crisis.

Based on past experience, once finalized, federal regulations affecting the rating agencies can be anticipated to have an effect that will endure for several decades. The regulatory steps taken now should: (1) demonstrate that the highest value is to increase non-conflicted competition, (2) open the door to new technology which will add fresh air to a market that is stale from oligopoly control, (3) recognize that regulatory barriers to entry have grown significantly since 1975 and should now be reduced rather than increased, (4) chart a bold new course that cannot be thwarted by the intense lobbying that inevitably accompanies such a high

level of government scrutiny and intervention, and (5) live up to the promise of the Credit Rating Agency Reform Act of 2006.

Rapid Ratings has Buy-Side and Sell-Side customers in credit and equity businesses covering risk management and portfolio management disciplines, as well as corporate clients performing counterparty risk management. For none of these do we need an NRSRO designation. There may indeed be value for firms like ours to be recognized as NRSROs, but while the NRSRO framework still tilts in the direction of supporting the issuer-paid agencies, the designation's value proposition is not entirely clear.

We are of course available to speak on these matters in more detail at the Commission's request.

Regards,



James H. Gellert
Chairman and CEO
Rapid Ratings International Inc.



Dr. Patrick J. Caragata
Founder and Executive Vice Chairman
Rapid Ratings International Inc.