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**November 17, 2010**

**By Electronic Mail**

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

**Re: Rule Proposal relating to disclosure for asset-backed securities required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (File No. S7-24-10) (the "Release")**

Dear Ms. Murphy:

Moody's Investors Service ("**MIS**") appreciates the opportunity to provide comments to the Securities and Exchange Commission ("**Commission**") on the Release, which was published in response to Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "**Dodd-Frank Act**" or "**Act**"). We limit our comments to that portion of the Release that addresses Section 943(1) of the Act, which requires each nationally recognized statistical rating organization ("**NRSRO**") to include in any report accompanying a credit rating of an asset-backed security ("**ABS**"), as that term is defined in the Act, "a description of—(A) the representations, warranties, and enforcement mechanisms available to investors; and (B) how they differ from the representations, warranties, and enforcement mechanisms in issuances of similar securities."

We appreciate the desire to protect investors and increase the transparency of information provided to them. We are concerned, however, that Section 943(1) casts NRSROs in a role that contradicts both the function that we serve in the capital markets, as well as the objective of the Act to reduce reliance on ratings.[1] We believe that ABS should be defined in a more limited manner than proposed in the Release. Finally, with regard to the specific mandates, we suggest that:

(1) Certain terms in Section 943(1)(A) should be clarified and NRSROs should be permitted to fulfill its mandate by referencing the representations, warranties ("**R&Ws**") and enforcement mechanisms in the transaction documents so that NRSRO disclosures are more useful for the investor, and

(2) Rather than establishing a rigid rules-based system, the Commission's final rule should encourage best practices to evolve in the market around R&Ws and permit

[1] See, e.g., Sections 939 and 939A of the Act and the Joint Explanatory Statement of the Committee of Conference for the Act.

NRSROs to fulfill the requirements in Section 943(1)(B) by using industry standards where they exist.

## I. Limit NRSROs Role in Interpreting 943(1)

We recognize that Section 943(1) places certain disclosure requirements on NRSROs with respect to issuer R&Ws. However, we believe these obligations are ill placed and broadly inconsistent with the important goal of reducing reliance on NRSROs in the US market. We therefore suggest that in interpreting Section 943(1), the SEC consider limiting the NRSROs' role as much as statutorily permissible. Specifically, rather than providing the market with a comparative analysis or setting market standards for R&Ws, the NRSROs' role should be limited to evaluating R&Ws as part of their credit analysis, only to the extent relevant. Moreover, to the extent there is a governmental desire to assess, comment on and set standards for R&Ws made by issuers, we believe the Commission or another governmental organization is better suited to provide such an analysis.

There are two important reasons for our recommendation. First, while credit ratings are one means of disseminating information about debt securities to the broader market, the issuer itself is the most important source of information about any security. After all, the issuer has first-hand knowledge about all of its information, and the investors in the primary market purchase the security from the issuer. As a result, NRSROs are neither the appropriate nor the best means of distributing information about issuer R&Ws because it is the issuers – *not* the NRSROs – who make the R&Ws for the benefit of investors.

Second, the proper role of NRSROs in the debt market is to be an unbiased commentator and to provide predictive opinions on just one characteristic of an entity or obligation – its relative credit quality. While we typically evaluate the credit implications of R&Ws and the financial strength of the provider of the R&Ws, a thorough evaluation of R&Ws is not necessarily part of the normal course of credit analysis for every type of ABS security. In assessing the credit risk of ABS, a more comprehensive analysis of the R&Ws may be warranted in certain asset classes (e.g., residential mortgage backed securities ("**RMBS**"))[2], and not others (e.g., collateralized debt obligations) where the R&Ws might be less relevant to credit risk. As a result, historically, investors have not expected – and we have not provided – the type of comparative analysis of R&Ws that is required under Section 943(1)(B). Therefore, by requiring NRSROs to identify, review and contrast which R&Ws the market should view as the standard, Section 943(1) attributes a greater role to NRSROs than that of market commentators on credit risk.

In our view, placing such an obligation on NRSROs blurs the role and function of NRSROs in the market. Such a governmental mandate increases the potential that market participants will inappropriately rely on NRSROs as arbiters of a host of different risks, some of which may not have any direct connection with credit analysis.

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[2] For instance, MIS will not rate RMBS transactions where the loan level R&W provider has been assessed as "unacceptable" by MIS or where the R&W provider does not have sufficient net worth. See *Moody's Criteria for Evaluating Representations and Warranties in U.S. Residential Mortgage Backed Securitization (RMBS)*, November 24, 2008, as updated on October 5, 2009.

## II. Narrow the Proposed Definition of Asset-Backed Securities

From a practical standpoint, we suggest that the Commission take a consistent approach in defining the term "ABS." In particular, as the Commission is aware, there are presently a number of different statutory[3] and regulatory text, rules[4] and rule proposals[5] that use the term ABS. If these documents define the term in different ways, there is a significant risk of market confusion and potential market disruption. Moreover, we believe it is important that regulators consider and strive for global consistency.

We therefore ask that the Commission consider limiting the term ABS at this stage in the manner described below. If at some later stage a broader multi-agency decision is taken to broaden the term, we are hopeful that all of the agencies that seek to either regulate the ABS market or its use by regulated entities approach the sector in a consistent and harmonized manner.

### A. Municipal Bonds

Under the Dodd-Frank Act, ABS is defined as "a fixed-income or other security collateralized by any type of self-liquidating financial asset (including a loan, a lease, a mortgage, or a secured or unsecured receivable) that allows the holder of the security to receive payments that depend primarily on cash flow from the asset." In the Release, the Commission proposes that under this definition, "if a municipal entity issues securities collateralized by a self-liquidating pool of loans that allow holders of the securities to receive payments that depend primarily on cash flow from those loans, that security would fall within the definition…." For the following interrelated reasons, we do not believe that Congress intended for the term "ABS" to capture securities issued by municipal issuers.

*First,* in analyzing the intent of Congress, we note that Subtitle D of the Act is entitled, "Improvements to the Asset-Backed Securitization Process." The market has never grouped municipal issuers into ABS. Importantly, in reading the various provisions of Subtitle D, on the whole they do not aim to capture the activities of municipal issuers, nor are they reflective of the various terms-of-art used in the municipal sector. Indeed, the language of the Subtitle is very much that of the typical structured finance market.

*Second,* while certain municipal bonds that finance loans may technically be collateralized by a self-liquidating pool of loans, they are not "securitized" in the traditional sense, and consequently the market has not historically considered them as ABS. By way of example, while both state Housing Finance Agencies ("**HFAs**") and RMBS are backed by pools of single family mortgage loans, they contrast with respect to certain key features.[6]

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[3] See Subtitle D of Dodd-Frank Act, entitled, "Improvement to the Asset-Backed Securitization Process."

[4] See, e.g., Rule 17g(5).

[5] See, e.g., Regulation AB.

[6] For a more detailed analysis of these differences, please refer to, MIS's Special Comment, *Housing 101: HFA Single Family Bonds versus RMBS – Differences Lead to Variation in Performance* (June 2009). See also

The most notable difference with respect to Section 943(1) is the management and ownership of HFA loan pools. Unlike RMBS, where the owner of the loans usually creates a trust and then sells the mortgage loans to that trust, the HFAs own and manage the loan pools that back their bonds. Succinctly put, there is no sale or special purpose vehicle. The question of whether there should be "skin in the game" is moot; the HFAs always have significant skin in the game. Indeed, HFA loans and the associated bonds are reported in the financial statements of the HFA thereby demonstrating that they are the HFA's assets and liabilities. In addition, in many cases, HFA management advises the trustee in the management of many of the aspects of the flow of funds for HFA-issued bonds whereas in an RMBS, the trustee directs the funds strictly according to the structured bond documents.

Another important difference is the purpose of state HFAs: they are agencies or authorities created by state law that are charged with helping persons and families of low or moderate income attain affordable housing. In issuing bonds, HFAs lower their borrowing costs and make below market rate mortgage loans to qualifying first-time homebuyers. RMBS, in contrast, does not have this public policy mandate.

These differences extend more broadly to other types of municipal bonds collateralized by a self-liquidating pool, such as state revolving funds and municipal bond banks. In defining ABS, consideration should be given to such distinctions, which have shaped the definition of ABS globally.

**B. Foreign Issues**

We believe that the Commission should not make 943(1) applicable to foreign issuers that are not issuing securities into the US market. At present, the Release and the Act are silent on the reach of Section 943(1). While it is reasonable to apply Section 943 to securities issued within the United States, making the rule applicable to non-US issued securities is problematic. Foreign jurisdictions may have different standards for R&Ws than in the United States, thus applying these requirements to foreign jurisdictions could present consistency issues. Moreover, because the rules may differ regarding the disclosure obligation of issuers, imposing the requirements of 943 may create conflict of law concerns for both NRSROs and non-US issuers. For instance, in some jurisdictions, issuers are not required to disclose R&Ws. Thus, in those jurisdictions, if the NRSRO were to describe and compare R&Ws in a report accompanying its credit rating, the NRSRO could be disclosing non-public issuer information in violation of not only its own internal policies and potentially a contractual relationship, but also of local law. We therefore believe that the Commission require 943(1) type disclosure only with respect to issuances within the United States.

**C. Private Market**

The Release and the Act are silent as to whether Section 943(1) applies to the private placement market. We believe that Section 943(1) should be limited to the public market to the

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MIS's Special Comment, *Subprime Residential Mortgage Securitizations: Frequently Asked Questions* (April 2007).

extent that the R&Ws that the issuer provides to the NRSRO are confidential, as they typically are in a 144a placement, for example.[7] Thus, if the R&Ws were described upon the publication of the ratings, an NRSRO could be placed in the situation of either failing to comply with Section 943(1) or violating not only an internal policy to not disclose confidential information, but also potentially breaching a confidentiality agreement.

If the Commission believes that it is important for such disclosure to be made, then we suggest that it modify Rule 144a so that issuers would be mandated to disclose the R&Ws in the first instance.

## III. Section 943(1) Requirements

As explained at the outset of this letter, Section 943(1) includes two disclosure mandates for NRSROs in any report accompanying an ABS credit rating. First, the NRSRO must describe the R&Ws and enforcement mechanisms available to investors. Second, the NRSRO must describe how they differ from the R&Ws and enforcement mechanisms in issuances of similar securities.

1) Description of R&W

With regard to the first requirement of Section 943(1), Question 35 in the Release asks:

> *"In the case of a registered ABS transaction, should we allow NRSROs to satisfy the requirement to disclose representations, warranties and enforcement mechanisms by referring to disclosure about those matters that is included in a prospectus prepared by an issuer?"*

We believe the answer is yes.

The description of R&Ws and enforcement mechanisms could be more than 30 pages in and of itself. And, of course, that does not include the pages needed for a comparison. Additional rules and regulations have required NRSROs to add more information to their rating announcements, and Section 932(s) of the Dodd-Frank Act[8] will increase the amount of information NRSROs disclose along with their credit ratings. While we support increasing transparency, we question whether the growing volume of the NRSRO disclosures have become – or are becoming – so cumbersome as to reduce the usefulness of ratings communication to the markets, which need the relevant information rather than simply more information. As a result, we recommend that the Commission balance the need for transparency with the need for relevance. Specifically, inundating NRSROs' communications with the market with so many separate and discrete disclosure requirements undermines the ability of investors to efficiently access and absorb relevant information. We are concerned that the lengthy disclosures required by Section 943(1), which as explained above is typically unnecessary for credit analysis and is inconsistent with NRSROs' role in the market, could obscure the credit-related information we disclose.

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[7] Below we discuss the issue of the confidential nature of R&Ws with respect to the public market.

[8] Section 932(s) requires the Commission to develop rules regarding a disclosure form that will accompany all credit ratings. The form is to include information such as the main assumptions in the methodologies of NRSROs and potential limitations of credit ratings, among other things.

Consequently, we recommend that in the interest of market efficiency and efficacy it would be beneficial for investors to have the specifics of the R&Ws included by reference. Consistent with this view, if this provision were to extend to those transactions that fall outside the scope of a registered ABS transaction, 144a transactions, for example, we suggest that NRSROs should likewise be permitted to comply with the Section 943(1)(A) mandate by referencing the location of the R&Ws and enforcement mechanisms in the offering documents.

2) Comparison of R&W

With regard to the second requirement of Section 943(1), Question 33 of the Release asks:

> *"Should we require the proposed disclosure to include comparisons to industry standards in addition to similar securities?"*

We believe that to the extent that such industry standards exist, the NRSRO should have the option to fulfill the requirements of Section 943(1)(B) by comparing the R&Ws and enforcement mechanisms to the industry standard. The Commission's rulemaking should promote the development of best practices in the market so that investors are able to review comparisons that are uniform, meaningful and transparent.[9] This approach could also mitigate some of the concerns described earlier about having NRSROs function outside of their proper role. Moreover, requiring NRSROs to compare R&Ws and enforcement mechanisms to *both* industry standards and similar securities would significantly weigh down the rating announcement, obscuring the credit opinions that NRSROs provide.

3) Type of R&W

We believe that Congress intended Section 943(1) to include those R&Ws that the issuer makes about the underlying assets and not R&Ws concerning other aspects of the transaction, *e.g.*, corporate or governance representations. The broad aim of Section 943 is to improve transparency around underwriting. Section 943(2) – which requires the "securitizer" to disclose fulfilled and unfulfilled repurchase requests – clearly states that the Section's purpose is to allow investors to "identify asset originators with clear underwriting deficiencies." Demand and repurchase activity can indicate poor underwriting as repurchase requests are the standard remedy in the event of a breach of R&Ws relating to the underlying assets in the pool. In contrast, the standard remedy for a breach of other R&Ws is contractual damages. Consequently, we believe the adopted rule should clarify that the R&Ws referenced in Section 943(1) are limited to those concerning the underlying pool assets. Similarly, we believe that Congress intended to mandate disclosure of only those enforcement mechanisms that exist in the event of a breach of the R&Ws. Therefore, the Commission should expressly define this scope in the adopted rule.

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[9] Of course, while ASF has developed model R&Ws for RMBS, and the Commercial Real Estate Finance Council is working on "best practices" for R&Ws for CMBS, industry standards do not yet exist for most asset classes.

4) Timing of R&W disclosure

Finally, in adopting the final rules for Section 943, we recommend that the Commission consider some of the logistics about the timing of the disclosures. Specifically, in the structured finance market, ratings are often published before the issuer publicly discloses the documents containing R&Ws. As discussed above, the R&Ws that an issuer provides to the NRSRO are typically confidential. Thus, if the R&Ws were described upon the publication of the ratings, the NRSRO may be disclosing confidential information in violation of not only of an internal policy to keep information confidential, but also a confidentiality agreement. We therefore ask that the NRSRO be permitted to disclose the information about R&Ws and enforcement mechanisms only after the issuer has disclosed such information. Moreover, to the extent that the R&Ws and enforcement mechanisms change in the interim, we do not believe that NRSROs should be required to conduct a second analysis.

## IV. Implementation

The Release seeks comment on the appropriate timing for compliance and effectiveness of the proposals, if adopted. We support the Commission's view that the implementing rules for Section 943(1) should apply only to new issuance. This would mean that the requirement would exist only at the initial issuance (i.e., that the disclosure would be made only once) and that it would not have a retroactive application.

In determining the appropriate date for implementation, we request that the Commission consider that NRSROs likely will need to hire attorneys and/or train existing employees to conduct this type of analysis, and that developing benchmarks in order to conduct the comparison mandated under Section 943(1)(B) is a time-intensive undertaking that involves considerable analysis. A comparison would need to consider not only the different types of R&Ws and enforcement mechanisms that exist, but also issues such as knowledge qualifiers and language choice. We therefore believe that NRSROs should be given at least six months to conduct the analysis required for Section 943(1)(B).

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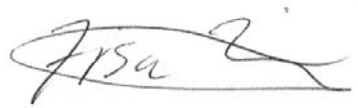
We appreciate the opportunity to comment on the Release. We would be pleased to discuss our comments further with the Commission or its staff.

Sincerely,



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