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TO: Commercial Mortgage Securities
Association

FROM: Scott A. Sinder
Rhonda M. Bolton

RE: SEC Re-Proposal of Certain Reforms Concerning Credit Rating Agencies

I. Overview

You have asked us to review the Securities and Exchange Commission (“SEC”)’s re-proposal of certain rule changes concerning credit rating agencies to assist you in determining whether CMSA should comment on the proposals. The rule changes now being considered by the SEC would:

- 1) require arrangers of structured finance products to maintain password-protected Internet websites that will provide “third party” NRSROs with the information the arrangers have given to hired NRSROs for use in determining or monitoring a credit rating. This is a new approach to effectuate the earlier proposal to make deal information available to “third party” NRSROs so that they could develop independent ratings; and,
- 2) require nationally recognized statistical rating organizations (“NRSROs”) to disclose credit rating histories for all outstanding credit ratings issued by the NRSRO on or after June 26, 2007.

CMSA did not oppose the theory behind the first proposal when it was previously advanced by the SEC. At the time, however, the proposal did not include a requirement that

arrangers maintain a website with deal information for access by third-party NRSROs. Given that the first proposal has now been modified to put the onus on arrangers to make information available to third-party NRSROs, CMSA may wish to focus on this proposal to determine whether it would pose an unacceptable new burden for arrangers.

CMSA also did not oppose the second proposal when it was initially advanced by the SEC, although CMSA did seek a clarification that the proposed credit rating history disclosure would not supplant disclosures that NRSROs already make concerning CMBS. The SEC did not address the clarification CMSA requested. CMSA may, therefore, wish to reiterate the request in this rulemaking proceeding.

Comments on these rule changes are due March 26, 2009.

II. Disclosure of Information Provided to/Relied Upon By an NRSRO

The SEC has made changes to its original proposal that would have required an NRSRO to disclose all information provided by a structured finance product's issuer, sponsor, or underwriter (i.e., "arrangers") to the NRSRO for the purpose of determining and monitoring a rating. CMSA did not object to adoption of this requirement when it was first proposed by the SEC. However, CMSA did suggest that the SEC modify the requirement so that it would not require public disclosure of confidential or proprietary borrower information that is provided to NRSROs. CMBS also suggested that servicers be among those entities required to provide information under the new rule, as servicers are the primary sources of information during the surveillance process in the CMBS markets.

It appears that the SEC took CMSA's concerns into consideration, but the resulting proposal may impose an undesirable added burden on arrangers. The rule as now proposed

specifies that the information given by arrangers to NRSROs for use in rating and surveillance need only be disclosed to other NRSROs and not to others.

Significantly, however, the mechanism for disclosure is modified so that NRSROs would be required to maintain a password-protected Internet website listing all deals they are working on, which database would be accessible only to other NRSROs. If a “third-party” NRSRO wishes to obtain data that the hired NRSRO is relying on to determine or monitor a rating, that “third-party” NRSRO must request the data from the arranger. Any third-party NRSRO seeking access to the information would be required to certify to the SEC that it is accessing such information solely for the purpose of developing its own ratings, that it will keep the information confidential, and that it will determine ratings for at least 10% of the deals for which it is obtaining information

For its part, the arranger would be required to post all of the information it is providing to the hired NRSRO on a password-protected Internet website so that the information could be accessed by third-party NRSROs, and would be required to provide the hired NRSROs with a representation that the arranger is doing so. With respect to the information the arranger is expected to make available, that information is described in the proposal as the written (not oral) information disclosed to the hired NRSRO to determine the initial rating or for surveillance, such as characteristics of the assets in the pool underlying or referenced by the structured finance product; legal documentation setting forth the capital structure of the trust, payment priorities with respect to the tranche securities issued by the trust, all applicable covenants regarding trust activities; and information concerning performance of underlying assets in the pool.

Depending on whether arrangers would consider it an unreasonable burden to be required to maintain the website contemplated in this proposed rule, CMSA may wish to comment on this proposal.

III. Disclosure of Credit Rating Histories

The SEC previously amended its rules to require NRSROs to disclose, in XBRL format on a six month delay, ratings action histories for a randomly selected 10% of “issuer-paid” credit ratings¹ for each rating class for which it has issued 500 or more issuer-paid ratings. The new proposal would change the parameters of this disclosure obligation to require NRSROs to disclose, on a twelve month delay, ratings history information for 100% of their current issuer-paid ratings that are determined after June 25, 2007 (the effective date of the Rating Agency Act).

At the time the ratings history disclosure requirement was first proposed, CMSA did not object to it although CMSA requested clarification that the new requirement would be in addition to, and not in lieu of, the current posting of rating actions done by NRSROs that serve CMBS markets. The SEC did not respond to CMSA’s clarification request. Accordingly, if this concern is still relevant for CMSA, it may wish to use the present rulemaking proceeding to reiterate its request for a clarification that the rating history disclosure requirement is in addition to the postings currently done to serve CMBS markets.

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¹ “Issuer-paid” credit ratings are defined as those paid for by the obligor being rated or by the issuer, underwriter or sponsor being rated.