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September 30, 2014

The Honorable Tim Johnson
Chairman
The Honorable Mike Crapo
Ranking Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Jeb Hensarling
Chairman
The Honorable Maxine Waters
Ranking Member
Committee on Financial Services
House of Representatives

Subject: *Securities and Exchange Commission: Nationally Recognized Statistical Rating Organizations*

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on major rules promulgated by the Securities and Exchange Commission (Commission) entitled “Nationally Recognized Statistical Rating Organizations” (RIN: 3235-AL15). We received them on September 2, 2014. They were published in the *Federal Register* as final rules on September 15, 2014. 79 Fed. Reg. 55,078.

The final rules, in accordance with the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and to enhance oversight, adopts amendments to existing rules and new rules that apply to credit rating agencies registered with the Commission as nationally recognized statistical rating organizations (NRSROs); adopts a new rule and form that applies to providers of third-party due diligence services for asset-backed securities; and adopts amendments to existing rules and a new rule that 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, in these final rules, also adopts certain technical amendments to existing rules.

Enclosed is our assessment of the Commission’s compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rules. Our review of the procedural steps taken indicates that the Commission complied with the applicable requirements.

If you have any questions about this report or wish to contact GAO officials responsible for the evaluation work relating to the subject matter of the rules, please contact Shirley A. Jones, Assistant General Counsel, at (202) 512-8156.

signed

Robert J. Cramer
Managing Associate General Counsel

Enclosure

cc: Kevin M. O'Neill
Deputy Secretary
Securities and Exchange Commission

REPORT UNDER 5 U.S.C. § 801(a)(2)(A) ON MAJOR RULES
ISSUED BY THE
SECURITIES AND EXCHANGE COMMISSION
ENTITLED
"NATIONALLY RECOGNIZED STATISTICAL
RATING ORGANIZATIONS"
(RIN: 3235-AL15)

(i) Cost-benefit analysis

The Commission discussed costs and benefits associated with provisions of the final rules in the rules and in its submission to GAO. The Commission stated that there will be costs associated with the amendments and new rules adopted related to governance of NRSROs. These costs will be primarily incurred by NRSROs. Initial and ongoing direct costs, including compliance costs, may vary among the NRSROs depending on the size and complexity of their business activities (for example, number of credit ratings outstanding, number of analysts, or number of classes of credit ratings). Among other costs, NRSROs also may incur training costs in order to make their personnel aware of the changes in internal controls, policies, and procedures required by the amendments and new rules. These costs are difficult to quantify because they depend significantly on how the required changes differ from the internal policies and procedures currently in place within each NRSRO.

According to the Commission, to the extent that the amendments and new rules improve the quality of credit-related information, they may have effects related to allocative efficiency and capital formation. As a result of these amendments and new rules, users of credit ratings could make more efficient investment decisions based on higher-quality information. Market efficiency also may improve if credit ratings become more informative and the additional information is reflected in asset prices. To the extent that the amendments and rules will be effective in enhancing the integrity and quality of NRSRO credit ratings, users of these credit ratings may benefit from an enhanced confidence in the quality of the creditworthiness assessments reflected in the credit ratings, which may have positive effects on the willingness of investors to participate in the securities markets and thereby enhance capital formation, as capital efficiently flows to more productive uses. The benefits in terms of efficiency and capital formation arising from the rules enhancing governance and the integrity of credit ratings are likely to be greater for asset-backed securities, where the inherent conflict of interest in the issuer-pay model is more acute, and, as a result of the amendments and new rules, investors may become less reluctant to invest in asset-backed securities.

The Commission states that the requirements are primarily designed to enhance disclosure and should have economic benefits, relative to the baseline that existed before the amendments and rules were adopted, in terms of promoting the transparency of credit ratings and NRSRO activities and, therefore, NRSRO accountability. This should benefit users of credit ratings, including investors. According to the Commission, the amendments and rules also should enhance disclosure requirements with respect to asset-backed securities for the benefit of users of credit ratings, including investors in these securities.

(ii) Agency actions relevant to the Regulatory Flexibility Act (RFA), 5 U.S.C. §§ 603-605, 607, and 609

The Commission stated that it is sensitive to the costs and burdens the amendments and new rules will have on all entities, including small entities. Consequently, the amendments and new rules contain certain modifications from the proposals designed to alleviate as appropriate some of the concerns regarding small entities. The Commission believes that the amendments and new rules being adopted, as modified from the proposal, strike an appropriate balance between minimizing the costs and burdens on small entities, and implementing the policies and requirements addressed by title IX, subtitle C of the Dodd-Frank Act. Moreover, the Commission states that it believes the choices it has made in implementing title IX, subtitle C of the Dodd-Frank Act have resulted in amendments and new rules that are appropriate for entities of all sizes. The Commission estimated that all 15 providers of third-party due diligence services subject to the new requirements are small entities and that the new requirements applicable to issuers will not have a significant economic impact on a substantial number of small entities.

(iii) Agency actions relevant to sections 202-205 of the Unfunded Mandates Reform Act of 1995, 2 U.S.C. §§ 1532-1535

As an independent regulatory agency, the Commission is not subject to the Act.

(iv) Other relevant information or requirements under acts and executive orders

Administrative Procedure Act, 5 U.S.C. §§ 551 et seq.

On May 18, 2011, the Commission proposed for comment, amendments to existing rules and new rules in accordance with title IX, subtitle C of the Dodd-Frank Act and to enhance the oversight of NRSROs. 76 Fed. Reg. 33,420 (June 8, 2011). The Commission stated that it received comments on the overall economic effects of the proposed amendments and new rules. Generally, commenters expressed concerns that the potential cumulative burden and costs associated with the proposed amendments and new rules could be so onerous that they would have negative effects on competition by imposing an excessive burden on smaller NRSROs and raising barriers to entry for credit rating agencies that seek to register as NRSROs. The Commission responded to the comments in the final rules.

Paperwork Reduction Act (PRA), 44 U.S.C. §§ 3501-3520

The Commission determined that these final rules contains information collection requirements under the Act. The titles for the existing collections of information affected by the rules are:

- Rule 17g-1, Application for registration as a nationally recognized statistical rating organization; Form NRSRO, and Form NRSRO Instructions (OMB Control Number 3235-0625);
- Rule 17g-2, Records to be made and retained by nationally recognized statistical rating organizations (OMB Control Number 3235-0628);
- Rule 17g-3, Annual financial reports to be furnished by nationally recognized statistical rating organizations (OMB Control Number 3235-0626);
- Rule 17g-5, Conflicts of interest (OMB Control Number 3235-0649);
- Rule 17g-7, Disclosure requirements (OMB Control Number 3235-0656);

- Rule 17g–8, Policies and procedures (a new collection of information);
- Rule 17g–9, Standards of training, experience, and competence for credit analysts (a new collection of information);
- Rule 17g–10, Certification of providers of third-party due diligence services in connection with asset-backed securities; Form ABS Due Diligence–15E (a new collection of information);
- Form ABS–15G (OMB Control Number 3235–0675);
- Rule 15Ga–2 (a new collection of information);
- Regulation S–T, General Rules and Regulations for Electronic Filing (OMB Control Number 3235–0424); and
- Form ID (OMB Control Number 3235–0328).

The Commission estimated that the total burden for purposes of PRA for NRSRO respondents resulting from the rule amendments and new rules will be approximately 74,062 industry-wide one-time hours, \$7,908,800 industry-wide external one-time costs, 725,456 industry-wide annual hours, and \$725,600 industry-wide external annual costs. In addition, the Commission estimated that the burden resulting from a request for an exemption under paragraph (f) of Rule 17g–5 will be approximately 150 hours in internal burden and \$20,000 in external costs; and the burden resulting from publishing information about material changes to an NRSRO’s credit rating procedures and methodologies or a notice of significant errors identified in a procedure or methodology as described in paragraph (a)(4) of Rule 17g–8 will be approximately 20 hours in internal burden. The Commission estimated that the total burden for purposes of PRA for respondents that are providers of third-party due diligence services resulting from the rule amendments and new rules will be approximately 3,375 industry-wide one-time hours, \$450,000 industry-wide external one-time costs, and 238 industry-wide annual hours. The Commission further estimated that the total burden for purposes of PRA for issuer and underwriter respondents resulting from the rule amendments and new rules will be approximately 33,600 industry-wide one-time hours and 834 industry-wide annual hours.

Statutory authorization for the rule

The Commission promulgated these final rule under the authority of 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. No. 111–203 §§ 936, 938, and 943).

Executive Order No. 12,866 (Regulatory Planning and Review)

As an independent regulatory agency, the Commission is not subject to the review requirements of this Order.

Executive Order No. 13,132 (Federalism)

As an independent regulatory agency, the Commission is not subject to the review requirements of this Order.