November 7, 2017

Dear Representative:

On behalf of Americans for Financial Reform (AFR), we are writing to urge you to vote against H.R. 3911, which is being considered on the House floor today under suspension of the rules.[1] HR 3911 would weaken oversight of major credit rating agencies such as S&P and Moody's which were at the center of the 2008 financial crisis.

The failure of credit rating agencies to properly assess the underlying risks of securities played a central role on the last financial crisis. In the run-up to the crisis, these agencies pursued business from issuers of securities by issuing inflated ratings of hundreds of thousands of toxic securities based on subprime mortgages. The ratings agencies certified these flawed securities as high quality, investment grade assets. This created hundreds of billions in investor losses when these securities were revealed as extraordinarily risky and unstable.

In the aftermath of the financial crisis, the largest credit rating firms paid over $2 billion in penalties to U.S. federal and state authorities for the fraudulent ratings of mortgage-backed securities and collateralized debt obligations.[2]

As part of the post-financial crisis efforts to enhance the accountability and transparency of nationally recognized statistical rating organizations, the Dodd-Frank Financial Reform Act required the SEC to establish the Office of Credit Ratings (OCR). The OCR is required to conduct yearly examinations of each nationally recognized rating agency to ensure they were not influenced by conflicts of interest and to promote accuracy in the ratings issued.

Since the post-crisis reforms did not actually change credit rating firms' business model -- i.e. they continue to be paid by the issuers of the same instruments they are grading -- those yearly evaluations are an essential protection for the users of the credit ratings as well as for the public interest in avoiding future episodes of financial instability.

By inserting the language "as appropriate" into the requirement described above, H.R. 3911 effectively eliminates the mandatory yearly examinations. Instead, it leaves examinations as a purely optional exercise for the SEC, meaning that the Office of Credit Ratings need not

[1] Americans for Financial Reform is an unprecedented coalition of more than 200 national, state and local groups who have come together to reform the financial industry. Members of our coalition include consumer, civil rights, investor, retiree, community, labor, faith based and business groups. A list of coalition members is available at http://ourfinancialsecurity.org/about/our-coalition/.

[2] U.S. Department of Justice, *Justice Department and State Partners Secure $1.375 Billion Settlement with S&P for Defrauding Investors in the Lead Up to the Financial Crisis.* Press Release, February 3, 2015. Accessed November 6, 2017. Available at http://bit.ly/2zmvxWg; and *Justice Department and State Partners Secure Nearly $864 Million Settlement with Moody's Arising from Conduct in the Lead up to the Financial Crisis.* Press Release, January 13, 2017. Accessed November 6, 2017. Available at http://bit.ly/2iREtaU.

regularly evaluate these firms' compliance with their stated rating methodologies, their management of conflicts of interest, or their ethics policies.

This legislation would also open the possibility of credit rating agencies challenging the SEC in court, if they felt the examinations were not "appropriate". In previous cases, such as challenges to commodity position limits, courts have interpreted the "as appropriate" language to require cost-benefit justifications for regulatory actions.[3] If H.R. 3911 passed, even if the SEC was willing to aggressively carry out examinations of rating agencies, it could be subject to court challenge.

Credit rating agencies' own employees have stated they "sold [their] souls to the devil for revenue" and described their rating practices in the run-up to the crisis as a "scam."[4] Watering down the language in the mandate for annual examinations would make it easier these firms to go back to the pre-crisis shady practices in detriment of investors and the safety of our economy. We urge you to reject it.

For more information please contact AFR's Policy Director, Marcus Stanley, at marcus@ourfinancialsecurity.org or 202-466-3672.

Sincerely,

Americans for Financial Reform

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[3] See: "International Swaps and Derivatives Association v. U.S. Commodity Futures Trading Commission." U.S. District Court for the District of Columbia, Memorandum Opinion. Available at http://bit.ly/2yapb8W.
https://secure.fia.org/downloads/USDC-DC_Position-Limits-Rule-Injunction_092812.pdf

[4] Peter Lattman, "Suit Charges 3 Credit Ratings Agencies with Fraud in Bearn Stearns Case." *The New York Times,* November 11, 2013. Accessed November 6, 2017. Available at http://nyti.ms/2h92Mlq.