
Annual Report on Nationally Recognized Statistical Rating Organizations

As Required by Section 6
of the Credit Rating Agency Reform Act of 2006



This is a report of the Staff of the U.S. Securities and Exchange Commission.

The Commission has expressed no view regarding the analysis, findings, or conclusions contained herein.

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ANNUAL REPORT ON NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATIONS

As Required by Section 6 of the Credit Rating Agency Reform Act of 2006

I. INTRODUCTION

The staff (the “Staff”) of the U.S. Securities and Exchange Commission (the “Commission” or “SEC”) is providing this report (“Report”) regarding nationally recognized statistical rating organizations (“NRSROs”) pursuant to Section 6 of the Credit Rating Agency Reform Act of 2006 (“Rating Agency Act”).¹ This Report reflects solely the Staff’s views. Section 6 of the Rating Agency Act requires the Commission to submit an annual report (“Annual Report”) to the Committee on Banking, Housing, and Urban Affairs of the U.S. Senate and the Committee on Financial Services of the U.S. House of Representatives (“Congressional Committees”) that, with respect to the year to which the Annual Report relates:

- identifies applicants for registration as NRSROs under Section 15E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”);²
- specifies the number of, and actions taken on, such applications; and
- specifies the views of the Commission on the state of competition, transparency, and conflicts of interest among NRSROs.

This Report generally focuses on the period from June 26, 2018 to June 25, 2019 (the “Report Period”). In addition to addressing the items specified in Section 6 of the Rating Agency Act, this Report provides an overview of certain Commission and Staff activities relating to NRSROs.

Information regarding the topics covered in this Report with respect to prior periods can be found on the Office of Credit Ratings (“OCR” or the “Office”) page of the Commission’s website.³

¹ Pub. L. No. 109-291, 120 Stat. 1327 (Sept. 29, 2006). The Rating Agency Act, among other things, added Section 15E to the Securities Exchange Act of 1934 to establish self-executing requirements on NRSROs and provide the Commission with the authority to implement a registration and oversight program for NRSROs. In June 2007, the Commission approved rules implementing such a program. See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations, Release No. 34-55857, 72 FR 33564 (Jun. 18, 2007), available at <https://www.sec.gov/rules/final/2007/34-55857.pdf>.

² Unless otherwise noted, all references to specific statutory sections and rules in this Report are to sections in the Exchange Act and related rules.

³ Prior Annual Reports can be found under “Annual Reports to Congress” in the “Reports and Studies” section of the OCR webpage, available at <https://www.sec.gov/ocr>.

II. STATUS OF REGISTRANTS AND APPLICANTS

Section 3(a)(62) defines a “nationally recognized statistical rating organization” as a credit rating agency that is registered under Section 15E and issues credit ratings certified by qualified institutional buyers, in accordance with Section 15E(a)(1)(B)(ix), with respect to:

- (i) financial institutions, brokers, or dealers;
- (ii) insurance companies;
- (iii) corporate issuers;
- (iv) issuers of asset-backed securities (as that term is defined in 17 CFR 229.1101(c));
- (v) issuers of government securities, municipal securities, or securities issued by a foreign government; or
- (vi) a combination of one or more categories of obligors described in any of clauses (i) through (v) above.

As of the date of this Report, there are nine credit rating agencies registered as NRSROs.⁴ The NRSROs, categories of credit ratings described in clauses (i) through (v) of Section 3(a)(62)(A) in which they are registered, and locations of their principal offices, as of the date of this Report, are listed below:⁵

NRSRO	Categories of Credit Ratings	Principal Office
A.M. Best Rating Services, Inc. ("A.M. Best")	(ii), (iii), and (iv)	U.S.
DBRS, Inc. ("DBRS")	(i) through (v)	U.S.
Egan-Jones Ratings Company ("EJR")	(i) through (iii)	U.S.
Fitch Ratings, Inc. ("Fitch")	(i) through (v)	U.S.
HR Ratings de México, S.A. de C.V. ("HR Ratings")	(i), (iii), and (v)	Mexico
Japan Credit Rating Agency, Ltd. ("JCR")	(i), (ii), (iii), and (v)	Japan
Kroll Bond Rating Agency, Inc. ("KBRA")	(i) through (v)	U.S.
Moody's Investors Service, Inc. ("Moody's")	(i) through (v)	U.S.
S&P Global Ratings ("S&P")	(i) through (v)	U.S.

During the Report Period, Morningstar Credit Ratings, LLC ("Morningstar") was also registered as an NRSRO in the categories of credit ratings described in clauses (i), (iii), and (iv) of Section 3(a)(62)(A). On July 2, 2019, Morningstar, Inc., the parent of Morningstar, completed an acquisition of DBRS. On November 15, 2019, Morningstar furnished a notice of

⁴ Section 15E(a) sets out registration procedures for a credit rating agency to voluntarily apply to be registered with the Commission as an NRSRO.

⁵ See the current Form NRSRO on each NRSRO's website for any updates to this information.

withdrawal from registration to the Commission (which became effective on December 30, 2019), and DBRS filed an update to Form NRSRO to add Morningstar as a credit rating affiliate. Given that Morningstar and DBRS operated separately during the Report Period and that Morningstar was separately registered as an NRSRO until December 30, 2019, this Report includes information reported by and about Morningstar and DBRS, individually.

For purposes of this Report only, we refer to Fitch, Moody's, and S&P as larger NRSROs and the other NRSROs (A.M. Best, DBRS, EJR, HR Ratings, JCR, KBRA, and Morningstar) as smaller NRSROs.

Applications for initial registration and for registration by current NRSROs in additional rating categories are filed on Form NRSRO ("Form NRSRO").⁶ In addition, Section 15E(b) requires NRSROs to promptly amend Form NRSRO if any information or document provided therein becomes materially inaccurate. This section also requires NRSROs to annually amend Form NRSRO to update ratings count and performance information, certify the continuing accuracy of the information and documents provided therein, and list any material change thereto during the previous calendar year. OCR Staff review such amendments to Forms NRSRO in light of the requirements of Section 15E(b), Rule 17g-1, and the instructions to Form NRSRO.

No complete applications for initial registration as an NRSRO or for registration by current NRSROs in additional rating categories were received during the Report Period.

As discussed in the December 2018 Annual Report, the Commission issued orders in connection with an application filed by EJR, on April 10, 2018, to re-register in the asset-backed securities and government securities credit ratings classes.⁷ Specifically, on July 9, 2018, the Commission issued an order instituting proceedings pursuant to Section 15E(a)(2)(A)(ii) to determine whether EJR's application should be granted or denied.⁸ On November 2, 2018, the

⁶ See Section 15E(a) and Rule 17g-1. Rule 17g-1 requires an applicant/NRSRO to use Form NRSRO for the following, as applicable:

- an initial application to be registered as an NRSRO;
- an application to register for an additional class of credit ratings;
- an application supplement;
- an update of registration pursuant to Section 15E(b)(1);
- an annual certification pursuant to Section 15E(b)(2); and
- a withdrawal of registration pursuant to Section 15E(e).

See also Form NRSRO, available at <https://www.sec.gov/about/forms/formnrsro.pdf>.

⁷ EJR had previously been registered in such ratings classes. See Order Granting Registration of Egan-Jones Rating Company to Add Two Additional Classes of Credit Ratings, Release No. 34-59056 (Dec. 4, 2008), available at <https://www.sec.gov/rules/other/2008/34-59056.pdf>. On January 22, 2013, EJR and its founder Sean Egan consented to a Commission order under which, among other things, EJR agreed to be barred from rating asset-backed and government securities issuers as an NRSRO, with the right to re-apply for registration in these classes after 18 months from the date of the order. See In the Matter of Egan-Jones Ratings Company and Sean Egan, Release No. 34-68703 (Jan. 22, 2013), available at <https://www.sec.gov/litigation/admin/2013/34-68703.pdf>.

⁸ See Order Instituting Administrative Proceedings Pursuant to Section 15E(a)(2)(A)(ii) of the Securities Exchange Act of 1934 and Notice of Hearing, Release No. 34-83610 (July 9, 2018), available at <https://www.sec.gov/litigation/admin/2018/34-83610.pdf>.

Commission issued an order dismissing the proceedings in response to EJR’s motion to dismiss the proceedings following EJR’s voluntary withdrawal of its application.⁹

III. ACTIVITIES RELATING TO NRSROs

A. Activities

The Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”)¹⁰ mandated the creation of OCR. OCR is responsible for the oversight of credit rating agencies registered with the Commission as NRSROs. OCR’s Staff includes professionals with expertise in a variety of areas that relate to its regulatory mission, such as corporate, municipal, and structured debt finance.¹¹

OCR’s responsibilities – as mandated by the Dodd-Frank Act – include, among other things, conducting an examination of each NRSRO at least annually in eight specified review areas.¹² Information regarding the examinations is included in OCR’s annual examination reports.¹³

OCR also monitors trends and developments affecting the credit rating industry. For example, OCR Staff may meet with NRSROs to discuss rating and industry developments and with the boards of directors of NRSROs to discuss, among other things, compliance and oversight matters. OCR Staff also may meet with a variety of other market participants, including investors, issuers, regulators, and industry organizations, to discuss matters relevant to the credit rating industry.

During the Report Period, OCR Staff continued to participate in meetings that involved rating agency regulators globally, including those of the supervisory colleges that were formed for the largest internationally-active credit rating agencies. The supervisory colleges were formed to enhance communication among credit rating agency regulators globally with respect to examinations of the relevant credit rating agencies.¹⁴ During the Report Period, each college held an in-person meeting and conducted quarterly calls. OCR Staff also conducted additional discussions with international regulators, as appropriate.

⁹ See Order Dismissing Proceedings, Release No. 34-84530 (Nov. 2, 2018), available at <https://www.sec.gov/litigation/opinions/2018/34-84530.pdf>.

¹⁰ See Pub. L. No. 111-203, 124 Stat. 1376 (2010).

¹¹ See Section 15E(p)(2) for a description of OCR staffing requirements.

¹² See Section 15E(p)(3) for a description of the scope of the required examinations.

¹³ The examination reports can be found under “Summary Examination Reports” in the “Reports and Studies” section of the OCR webpage, available at <https://www.sec.gov/ocr>.

¹⁴ See Supervisory Colleges for Credit Rating Agencies, Final Report (July 2013), available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD416.pdf>. The SEC serves as chair of the colleges for S&P and Moody’s, and OCR Staff represents the SEC in this regard. The European Securities and Markets Authority serves as chair of the college for Fitch.

During the Report Period, the Fixed Income Market Structure Advisory Committee (“FIMSAC”)¹⁵ established a Credit Ratings Subcommittee to consider the role of credit ratings issued by NRSROs in the corporate bond and municipal securities markets.¹⁶ At the FIMSAC meeting on July 29, 2019, the FIMSAC considered issues relating to NRSRO competition and NRSRO compensation models.¹⁷ At the FIMSAC meeting on November 4, 2019, the FIMSAC again considered the issue of NRSRO compensation models.¹⁸

In addition, the SEC’s Investor Advisory Committee (“IAC”)¹⁹ met on July 25, 2019 to discuss the SEC’s approach to regulation in areas with limited competition, including the credit rating agency industry.²⁰ The IAC met on September 19, 2019 to discuss increased leverage and related SEC regulatory implications, including the role of NRSROs in the leveraged loan and CLO markets.²¹ At the IAC meeting on November 7, 2019,²² Chairman Jay Clayton suggested future topics of focus for the committee, including questions related to credit rating agencies.²³

¹⁵ In November 2017, the Commission formed the FIMSAC to provide the Commission with diverse perspectives on the structure and operations of the U.S. fixed income markets, as well as advice and recommendations on matters related to fixed income market structure. The FIMSAC’s current charter is available at: <https://www.sec.gov/spotlight/fixed-income-advisory-committee/fimsac-charter-nov-2019.pdf>.

¹⁶ Topics that may be considered by the Credit Ratings Subcommittee include, but are not limited to, (1) the use of credit ratings by various market participants and the implications of ratings changes for these market participants, (2) the costs and benefits of the current model for credit rating issuance, (3) the U.S. regulatory regime for credit rating agencies registered as NRSROs, and (4) issuances of unsolicited credit ratings and the publication of commentaries. See <https://www.sec.gov/spotlight/fixed-income-advisory-committee/fixed-income-market-structure-advisory-committee-subcommittees.htm>.

¹⁷ See webcast of Fixed Income Market Structure Advisory Committee Meeting, SEC (July 29, 2019), available at https://www.sec.gov/video/webcast-archive-player.shtml?document_id=fimsac072919.

¹⁸ See webcast of Fixed Income Market Structure Advisory Committee Meeting, SEC (Nov. 4, 2019), available at https://www.sec.gov/video/webcast-archive-player.shtml?document_id=fimsac110419.

¹⁹ Section 911 of the Dodd-Frank Act established the Investor Advisory Committee to advise the Commission on regulatory priorities, the regulation of securities products, trading strategies, fee structures, the effectiveness of disclosure, and on initiatives to protect investor interests and to promote investor confidence and the integrity of the securities marketplace. The Dodd-Frank Act authorizes the Committee to submit findings and recommendations for review and consideration by the Commission. See <https://www.sec.gov/spotlight/investor-advisory-committee.shtml>.

²⁰ See webcast of Investor Advisory Committee Meeting, SEC (July 25, 2019), available at https://www.sec.gov/video/webcast-archive-player.shtml?document_id=iac072519.

²¹ See webcast of Investor Advisory Committee Meeting, SEC (Sept. 19, 2019), available at https://www.sec.gov/video/webcast-archive-player.shtml?document_id=iac091919.

²² See webcast of Investor Advisory Committee Meeting, SEC (Nov. 7, 2019) available at https://www.sec.gov/video/webcast-archive-player.shtml?document_id=iac110719.

²³ See Chairman Jay Clayton, Remarks to the SEC Investor Advisory Committee (Nov. 7, 2019), available at <https://www.sec.gov/news/public-statement/clayton-remarks-investor-advisory-committee-110719> (noting interest in issues such as reliance by retail investors on credit rating agencies, whether credit rating agencies are appropriately disclosing, monitoring and managing their conflicts, whether investors are harmed by compensation models of credit rating agencies, and whether there are alternative payment models that would better align the interests of rating agencies with those of investors).

B. Commission Orders and Releases and Staff Publications

The Commission and the Staff, as applicable, issued the following orders, releases, and publications relating to NRSROs or credit ratings in general from the start of the Report Period to December 31, 2019:

- Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Release No. 34-86590 (Aug. 7, 2019), 84 FR 40247 (Aug. 14, 2019).²⁴ The Commission adopted an amendment to Rule 17g-5(a)(3) that provides for an exemption from the rule with respect to credit ratings for certain structured finance products where the issuer is a non-U.S. person and the NRSRO has a reasonable basis to conclude that the structured finance product will be offered and sold exclusively outside the United States. In the adopting release, the Commission directed the Staff to further evaluate the effectiveness of Rule 17g-5(a)(3) with respect to ratings of structured finance products that are not eligible for relief under the exemption. The Commission also adopted conforming amendments to similar exemptions in Rule 17g-7(a) and Rule 15Ga-2.
- 2018 Summary Report of Commission Staff's Examinations of Each Nationally Recognized Statistical Rating Organization, dated December 2018, as required under Section 15E(p)(3)(C).²⁵ The report summarizes essential findings of the examinations conducted by Staff under Section 15E(p)(3)(C), generally focusing on the period from January 1, 2017 through December 31, 2017.
- Annual Report on Nationally Recognized Statistical Rating Organizations, dated December 2018, as required by Section 6 of the Rating Agency Act.²⁶ The Annual Report addresses the matters described in the first paragraph under Section I. of this Report, generally covering the period from June 26, 2017 to June 25, 2018.
- Order Dismissing Proceedings, Release No. 34-84530 (Nov. 2, 2018).²⁷ The Commission issued an order dismissing the proceedings to determine whether EJR's application for registration in the asset-backed securities and government securities credit ratings classes should be granted or denied. The Commission issued the order in response to EJR's motion to dismiss the proceedings following EJR's voluntary withdrawal of its application.

²⁴ Available at <https://www.sec.gov/rules/final/2019/34-86590.pdf>.

²⁵ Available at https://www.sec.gov/files/nrsro-summary-report-2018_0.pdf.

²⁶ Available at <https://www.sec.gov/files/2018-annual-report-on-nrsros.pdf>.

²⁷ Available at <https://www.sec.gov/litigation/opinions/2018/34-84530.pdf>.

- Proposed Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Release No. 34-84289 (Sept. 26, 2018), 83 FR 50297 (Oct. 5, 2018).²⁸ The Commission proposed an amendment to Rule 17g-5(a)(3) that would provide for an exemption from the rule with respect to credit ratings for certain structured finance products where the issuer is a non-U.S. person and the NRSRO has a reasonable basis to conclude that the structured finance product will be offered and sold exclusively outside the United States. The Commission also proposed conforming amendments to similar exemptions in Rule 17g-7(a) and Rule 15Ga-2.
- Orders Instituting Cease-and-Desist Proceedings. On August 28, 2018, the Commission issued the following orders pertaining to proceedings regarding certain rating practices at Moody's:
 - Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order, Release No. 34-83965 (Aug. 28, 2018).²⁹ The Commission instituted settled administrative proceedings against Moody's concerning its internal control structure with regard to the use of certain models in its methodology for rating residential mortgage-backed securities.
 - Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order, Release No. 34-83966 (Aug. 28, 2018).³⁰ The Commission instituted settled administrative proceedings against Moody's concerning its policies and procedures designed to define and consistently apply credit rating symbols.
- Order Granting Temporary Conditional Exemption for Japan Credit Rating Agency, Ltd. from Certain Requirements of Section 15E(t) of the Securities Exchange Act of 1934, Release No. 34-83884 (Aug. 17, 2018).³¹ The Commission granted JCR a temporary, conditional exemption from certain corporate governance requirements under Section 15E(t). The exemption expires on August 20, 2021 and thereafter renews until August 20, 2023, unless the Commission determines otherwise.
- Final Rule: Disclosure Update and Simplification, Release Nos. 33-10532, 34-83875, and IC-33203 (Aug. 17, 2018), 83 FR 50148 (Oct. 4, 2018).³² The Commission adopted amendments, effective November 5, 2018, to certain disclosure requirements that have become redundant, duplicative, overlapping, outdated, or superseded, in light of other Commission disclosure requirements, U.S. Generally Accepted Accounting Principles ("U.S. GAAP"), or changes in the information environment. The amendments include a

²⁸ Available at <https://www.sec.gov/rules/proposed/2018/34-84289.pdf>.

²⁹ Available at <https://www.sec.gov/litigation/admin/2018/34-83965.pdf>.

³⁰ Available at <https://www.sec.gov/litigation/admin/2018/34-83966.pdf>.

³¹ Available at <https://www.sec.gov/rules/exorders/2018/34-83884.pdf>.

³² Available at <https://www.sec.gov/rules/final/2018/33-10532.pdf>.

change to Rule 17g-3 to conform the financial statement reporting requirements applicable to NRSROs to U.S. GAAP.

- Order Instituting Administrative Proceedings Pursuant to Section 15E(a)(2)(A)(ii) of the Securities Exchange Act of 1934 and Notice of Hearing, Release No. 34-83610 (July 9, 2018).³³ The Commission issued an order instituting proceedings pursuant to Section 15E(a)(2)(A)(ii) to determine whether EJR's application for registration in the asset-backed securities and government securities credit ratings classes should be granted or denied.

IV. COMPETITION

A. Select NRSRO Statistics

Sections 1. through 3. below summarize and discuss certain information reported by NRSROs on Form NRSRO or pursuant to Rule 17g-3 that provides insight into the state of competition among NRSROs. While this information indicates that Moody's, S&P, and Fitch continue to account for the highest percentages of outstanding ratings, other information suggests that smaller NRSROs have gained market share in certain asset classes.³⁴

1. NRSRO Credit Ratings Outstanding

Each NRSRO annually reports the number of credit ratings outstanding, as of the end of the preceding calendar year, in each rating category for which it is registered.³⁵ This information, for the calendar year ending December 31, 2018, is summarized in Charts 1 through 4 below and can be useful in determining the breadth of an NRSRO's coverage with respect to issuers, obligors, and securities or money market instruments within a particular rating category.

Chart 1 depicts the number of credit ratings each NRSRO had outstanding in each rating category for which it was registered as of December 31, 2018. Chart 2 shows the percentage of credit ratings each NRSRO had outstanding across all rating categories and also breaks out the percentages for each NRSRO in each of the rating categories. Chart 3 illustrates the relative size of each rating category based on the aggregate number of ratings reported outstanding by all NRSROs. Chart 4 depicts the percentage of ratings each NRSRO had outstanding across all rating categories other than the government securities category.

³³ Available at <https://www.sec.gov/litigation/admin/2018/34-83610.pdf>.

³⁴ As discussed in Section IV.B.1. of this Report, information available on the websites of Commercial Mortgage Alert (<https://www.cmalert.com/>) and Asset-Backed Alert (<https://www.abalert.com/>) regarding NRSRO market shares in the asset-backed securities category indicates that some of the smaller NRSROs have developed significant market shares in such category over the past few years. In addition, Section IV.B.2. of this Report provides examples of certain asset classes in which it has been reported that smaller NRSROs have gained market share.

³⁵ Annual certifications on Form NRSRO must be filed with the Commission on EDGAR pursuant to Rule 17g-1(f) and made publicly and freely available on each NRSRO's website pursuant to Rule 17g-1(i). The number of outstanding credit ratings for each rating category for which an NRSRO is registered is reported on Item 7A of Form NRSRO.

Comparing the number of ratings *outstanding* for established NRSROs and newer NRSROs may not provide as comprehensive a picture of the state of competition as comparing the number of ratings *issued* by such NRSROs in a given period. Certain NRSROs (particularly the larger NRSROs) have a longer history of issuing ratings and their ratings include those for debt obligations and obligors that were rated well before the establishment of the newer entrants.³⁶ Consequently, the information described in Section IV.B. of this Report (relating to recent market share developments in the asset-backed securities rating category) may provide additional insight regarding how newer entrants are competing with more established rating agencies, specifically in the asset-backed securities rating category.

There are additional limitations to assessing the state of competition in each rating category and in the aggregate based on the number of outstanding ratings. For instance, some NRSROs have pursued business strategies to specialize in particular rating categories or sub-categories³⁷ and may not desire to issue ratings in certain of the other NRSRO rating categories. Also, the reported information does not reflect any credit ratings being issued by NRSROs in rating categories in which they are not registered with the Commission, nor does it reflect ratings issued by an affiliate of an NRSRO unless the affiliate is identified as a credit rating affiliate on Item 3 of Form NRSRO.

Further, the outstanding ratings reported by the NRSROs are based on their own determinations of the applicable categories and number of ratings, which are not necessarily consistent among NRSROs. In addition, to the extent NRSROs have adjusted their ratings count disclosures in accordance with the amended instructions to Form NRSRO, it may be more difficult to draw comparisons to ratings counts disclosed in prior years.³⁸

³⁶ The ratings counts disclosed on Item 7A of Form NRSRO include outstanding credit ratings, regardless of when they were issued. As a result, the ratings counts of the more established NRSROs may include credit ratings that were issued before the newer entrants began issuing credit ratings. These earlier ratings will continue to be included in the disclosed ratings counts until the rated securities are repaid or the credit ratings are otherwise withdrawn. Because outstanding ratings are included in the ratings counts, historical results factor significantly into the disclosed number of ratings, making it more difficult to discern current-year trends and identify gains achieved by the newer entrants.

³⁷ For example, A.M. Best has traditionally focused on credit ratings with respect to insurance companies and their affiliates.

³⁸ Effective January 1, 2015, Item 7A of Form NRSRO and the corresponding instructions were amended to clarify the manner in which the number of outstanding credit ratings should be calculated and presented. The clarifying amendments are designed to ensure that disclosures on Item 7A of Form NRSRO are consistent across NRSROs. The change in instructions may have caused some NRSROs to modify the way they count ratings for purposes of Item 7A of Form NRSRO, which may affect comparisons to disclosures made in prior years. See Nationally Recognized Statistical Rating Organizations, Release No. 34-72936 (Aug. 27, 2014), 79 FR 55077 (Sept. 15, 2014) at 55220-22 (discussing the clarifying amendments to Item 7A of Form NRSRO).

Chart 1 provides the number of outstanding credit ratings reported by each NRSRO in its annual certification for the calendar year ending December 31, 2018, in each of the five categories identified in Section 3(a)(62) for which the NRSRO is registered, as applicable.

Chart 1: Number of Outstanding Credit Ratings as of December 31, 2018 by Rating Category*						
NRSRO	Financial Institutions	Insurance Companies	Corporate Issuers	Asset-Backed Securities	Government Securities	Total Ratings
A.M. Best	N/R	7,196	1,052	5	N/R	8,253
DBRS	12,384	160	2,869	16,132	19,586	51,131
EJR	10,469	910	7,715	N/R	N/R	19,094
Fitch	36,862	3,260	19,560	32,902	195,667	288,251
HR Ratings	604	N/R	278	N/R	361	1,243
JCR	887	70	2,619	N/R	306	3,882
KBRA	932	70	0	11,226	88	12,316
Moody's	37,315	2,462	29,783	50,055	571,308	690,923
Morningstar	18	N/R	175	3,120	N/R	3,313
S&P	58,989	6,562	54,510	36,838	901,312	1,058,211
Total	158,460	20,690	118,561	150,278	1,688,628	2,136,617

* N/R indicates that the NRSRO was not registered in the applicable rating category as of the reporting date.

Source: NRSRO annual certifications for the 2018 calendar year, Item 7A on Form NRSRO

Chart 2 displays the percentage of each NRSRO’s outstanding credit ratings of the total outstanding credit ratings of all NRSROs, for each rating category in which the NRSRO was registered, as reported by each NRSRO in its annual certification for the calendar year ending December 31, 2018.³⁹

Chart 2: Percentage by Rating Category of Each NRSRO’s Outstanding Credit Ratings of the Total Outstanding Credit Ratings of all NRSROs, as of December 31, 2018*						
NRSRO	Financial Institutions	Insurance Companies	Corporate Issuers	Asset-Backed Securities	Government Securities	Total Ratings
A.M. Best	N/R	34.8%	0.9%	0.0%	N/R	0.4%
DBRS	7.8%	0.8%	2.4%	10.7%	1.2%	2.4%
EJR	6.6%	4.4%	6.5%	N/R	N/R	0.9%
Fitch	23.3%	15.8%	16.5%	21.9%	11.6%	13.5%
HR Ratings	0.4%	N/R	0.2%	N/R	0.0%	0.1%
JCR	0.6%	0.3%	2.2%	N/R	0.0%	0.2%
KBRA	0.6%	0.3%	0.0%	7.5%	0.0%	0.6%
Moody’s	23.5%	11.9%	25.1%	33.3%	33.8%	32.3%
Morningstar	0.0%	N/R	0.1%	2.1%	N/R	0.2%
S&P	37.2%	31.7%	46.0%	24.5%	53.4%	49.5%

* N/R indicates that the NRSRO was not registered in the applicable rating category as of the reporting date. Percentages have been rounded to the nearest one-tenth of one percent.

Source: NRSRO annual certifications for the 2018 calendar year, Item 7A on Form NRSRO

The larger NRSROs account for 95.4% of all the ratings outstanding as of December 31, 2018—slightly lower than their 95.8% share as of December 31, 2017.⁴⁰ The share of outstanding credit ratings that were issued by the larger NRSROs decreased in each category, most significantly in the asset-backed securities category, which decreased by 4.1%.

Notably, Chart 2 also shows that A.M. Best, one of the smaller NRSROs, had the most credit ratings outstanding in the insurance category. In each of the past five years, A.M. Best reported that it had the most credit ratings outstanding in the insurance category.⁴¹

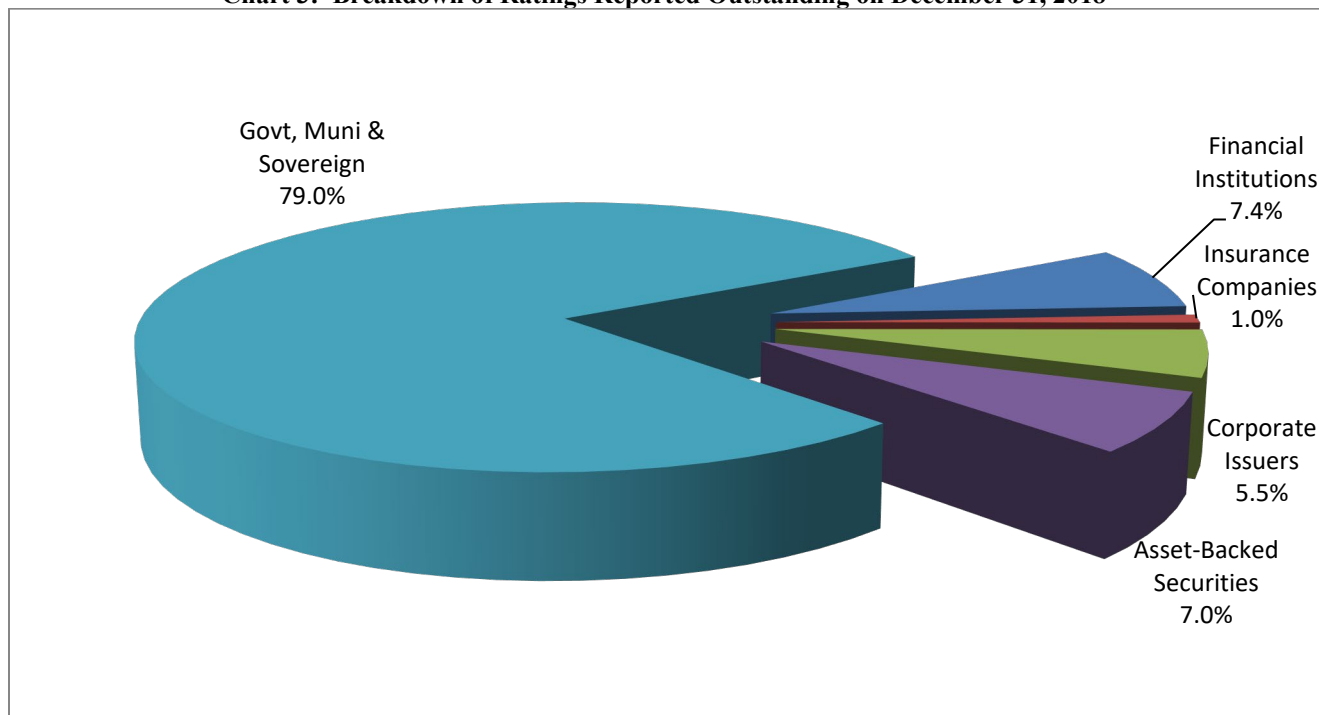
³⁹ For example, according to Chart 1, A.M. Best reported that it had 7,196 insurance company credit ratings, and the total of the credit ratings in that category reported by all NRSROs was 20,690. Dividing 7,196 by 20,690 equals (approximately) 0.3478 or 34.8% (which is the percentage of NRSRO insurance company ratings attributable to A.M. Best, as shown on Chart 2).

⁴⁰ In 2007, the year when NRSROs began reporting outstanding ratings on Form NRSRO, these three NRSROs accounted for 98.8% of all outstanding ratings.

⁴¹ See Annual Reports for prior years, which can be found under “Annual Reports to Congress” in the “Reports and Studies” section of the OCR webpage, available at <https://www.sec.gov/ocr>.

Chart 3 depicts the percentages of outstanding credit ratings attributable to each rating category, as reported by each NRSRO in its annual certification for the calendar year ending December 31, 2018.

Chart 3: Breakdown of Ratings Reported Outstanding on December 31, 2018*



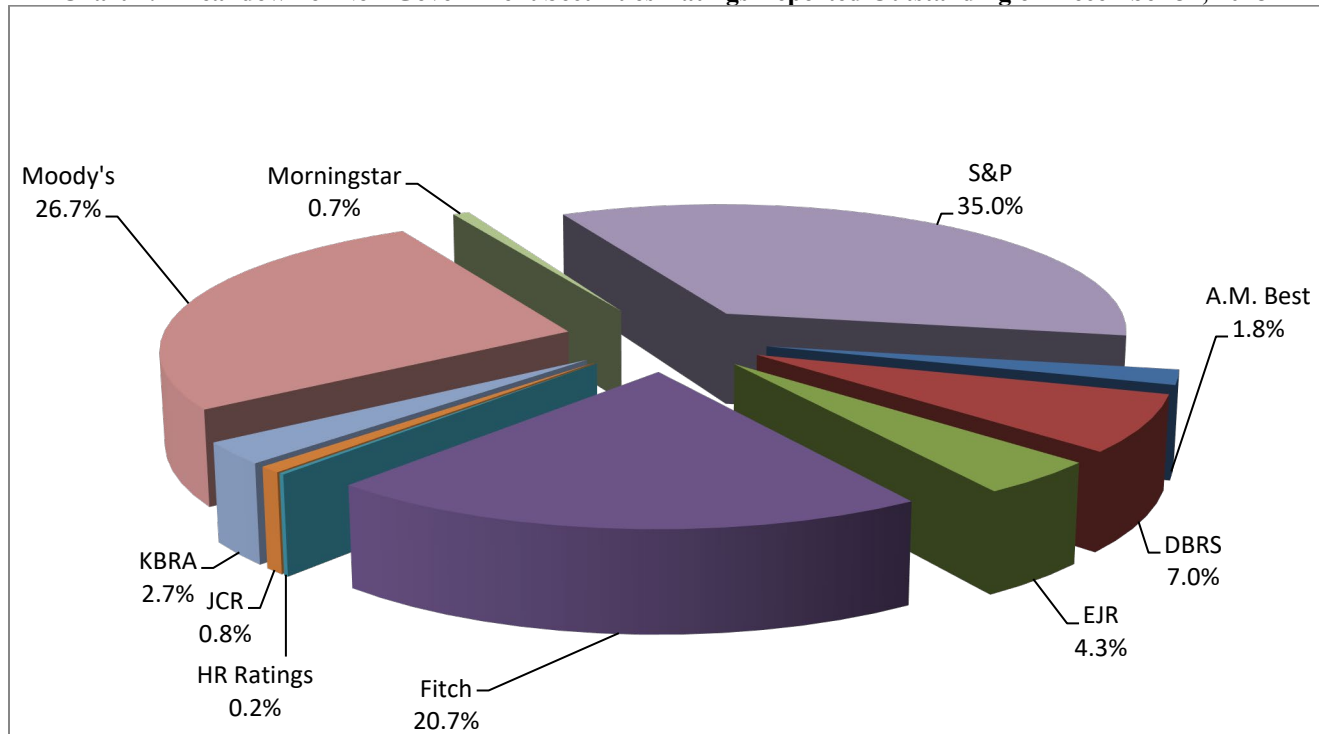
* Percentages have been rounded to the nearest one-tenth of one percent.

Source: NRSRO annual certifications for the 2018 calendar year, Item 7A on Form NRSRO

As illustrated by Chart 3, as of December 31, 2018, a large proportion of the aggregate credit ratings reported to be outstanding were in the government securities category, which may be attributable to the large number of government bond issuers and their multiple debt offerings. The government securities category accounted for 79.0% of the total number of credit ratings reported across all categories and, as shown on Chart 2, is also the most concentrated rating category, with Moody's and S&P accounting for 87.2% of all outstanding government ratings.

Chart 4 depicts the percentages of the credit ratings outstanding that are attributable to each NRSRO over all the rating categories other than the government securities category, as reported by each NRSRO in its annual certification for the calendar year ending December 31, 2018.

Chart 4: Breakdown of Non-Government Securities Ratings Reported Outstanding on December 31, 2018*



* Percentages have been rounded to the nearest one-tenth of one percent.

Source: NRSRO annual certifications for the 2018 calendar year, Item 7A on Form NRSRO

A comparison of Chart 4 to Chart 2 (which shows each NRSRO's share of outstanding ratings over all the rating categories, including government securities) illustrates that there is less concentration in the non-government securities rating categories. S&P's and Moody's percentage share of all outstanding ratings declines by 14.5 and 5.6 percentage points, respectively, when government securities are excluded. Fitch's percentage share of outstanding ratings, on the other hand, increases by 7.2 percentage points when government securities are excluded. The percentage share for all the remaining NRSROs also increases when government securities are excluded.

Further, when government securities are included in the total calculation, each of the smaller NRSROs except for one (i.e., DBRS) has less than 1.0% of all outstanding ratings, making it difficult to assess their relative market shares. When government securities are excluded, a clearer picture of the relative percentage shares of the smaller NRSROs in the categories in which they are active can be observed, as illustrated in Chart 4. The percentage share of each smaller NRSRO for all rating categories other than government securities as of

December 31, 2018 did not change significantly compared to their percentage share as of December 31, 2017.⁴²

As discussed above, Charts 1 through 4 reflect the number of credit ratings outstanding as of December 31, 2018, which may include credit ratings that were issued years ago. As a result, the measure may not be indicative of the current market position of each NRSRO with respect to newly issued credit ratings. For a discussion of recent market share developments in the asset-backed securities rating category and other developments that could impact NRSRO market share, see Section IV.B. of this Report.

2. NRSRO Analytical Staffing Levels

Chart 5 reports the number of credit analysts (including credit analyst supervisors) and the number of credit analyst supervisors employed by each of the NRSROs, as reported on Exhibit 8 of Form NRSRO.⁴³

Chart 5: NRSRO Credit Analysts and Credit Analyst Supervisors		
NRSRO	Credit Analysts (Including Credit Analyst Supervisors)	Credit Analyst Supervisors
A.M. Best	147	52
DBRS	314	66
EJR	17	9
Fitch	1,269	302
HR Ratings	45	7
JCR	64	34
KBRA	156	33
Moody's	1,714	242
Morningstar	82	12
S&P	1,557	128
Total	5,365	885

Source: Exhibit 8 on Form NRSRO, as in effect as of each NRSRO's annual certification for the 2018 calendar year filed on or before March 31, 2019.

⁴² A comparison of Chart 4 in this Report with Chart 4 in Section IV.A.1.(a) of the December 2018 Annual Report (available at <https://www.sec.gov/files/2018-annual-report-on-nrsros.pdf>) shows that each smaller NRSRO's total market share (excluding government securities) as of December 31, 2018 remained constant or increased modestly (the largest increase was 0.7% by KBRA) compared to the market shares as of December 31, 2017.

⁴³ Effective January 1, 2015, the instructions for Exhibit 8 of Form NRSRO were amended to clarify that NRSROs must include credit analyst supervisors in the total number of credit analysts disclosed on Exhibit 8. This amendment was designed to enhance consistency of the disclosures on Exhibit 8 of Form NRSRO.

The larger NRSROs report employing 4,540 credit analysts (including supervisors), which is approximately 84.6% of the total number employed by all of the NRSROs. Although the smaller NRSROs in the aggregate employ only approximately 15.4% of all credit analysts employed by NRSROs, this percentage has increased steadily in recent years.⁴⁴ During this time, some of the smaller NRSROs have reported significant increases in their analytical staff. The trend in the number of rating analysts employed by an NRSRO can indicate, among other things, the state of the NRSRO's business or its business outlook—i.e., NRSROs that are increasing their staff may be experiencing or anticipating an increase in ratings volumes or planning to enter new markets.⁴⁵

3. NRSRO Revenue

The total revenue reported to the Commission⁴⁶ by all of the NRSROs for their 2018 fiscal year was approximately \$7.0 billion, which is comparable to the approximately \$7.1 billion reported in the 2017 fiscal year. Chart 6 shows the percentage of total NRSRO revenues since 2015 that were accounted for by the larger NRSROs in the aggregate and by the smaller NRSROs in the aggregate.

Chart 6: NRSRO Revenue Information: Fiscal Year Percentage of Total Reported NRSRO Revenue				
	2015	2016	2017	2018
S&P, Moody's, and Fitch	93.7%	94.4%	94.1%	93.5%
All Other NRSROs	6.3%	5.6%	5.9%	6.5%
Total	100.0%	100.0%	100.0%	100.0%

Source: Financial reports provided to the Commission under Rule 17g-3(a)(3) for the fiscal years ended 2015-2018. For the preparation of this Report, if an NRSRO reported revenue in a foreign currency, the revenue was converted to U.S. dollars using the average exchange rate over all U.S. banking days in the fiscal year of such NRSRO.

⁴⁴ Based on reports by the NRSROs on their annual certifications for the applicable calendar year, the smaller NRSROs employed approximately 11.4% of all NRSRO analysts in 2014, 12.8% of all NRSRO analysts in 2015, 14.6% of all NRSRO analysts in 2016, and 15.2% of all NRSRO analysts in 2017.

⁴⁵ Changes in the number of analysts employed could also indicate, for example, a change in the complexity of rating engagements or evolving business models.

⁴⁶ Under Rule 17g-3(a)(3), each NRSRO is required to file annually with the Commission an unaudited report providing revenue information, including revenue from determining and maintaining credit ratings, revenue from subscribers, revenue from granting licenses or rights to publish credit ratings, and revenue from other services and products. These reports are not required to be made publicly available.

Further revenue information is available for NRSROs that are owned, in whole or in part, by public companies. The following information is from the 2018 annual reports of public companies with an ownership interest in an NRSRO:

- Moody's Corporation, the owner of Moody's, reported a 2% decline in external revenue at Moody's compared to 2017 results. The decline, according to the report, reflects lower non-financial corporate and infrastructure rated issuance volumes reflecting the confluence of unfavorable market factors and a decline in U.S. public finance issuance resulting from certain provisions in the Tax Cuts and Jobs Act enacted into U.S. law on December 22, 2017. The report notes that the decline in revenue at Moody's was partially offset by benefits from a favorable product mix and pricing increases, an increase in new ratings mandates, and demand for floating rate instruments (most notably in the first half of 2018) which resulted in strong collateralized loan obligation formation. The structured finance and financial institution groups of Moody's had an increase in revenue compared to 2017 results.⁴⁷
- S&P Global Inc. ("S&P Global"), which is S&P's parent company, indicated that revenue at S&P decreased by 4% compared to its 2017 results, due to a decline in transaction revenue. S&P Global attributed the decreased revenue to lower corporate bond issuance in the U.S. and Europe, but noted an increase in structured finance revenue (driven by increased U.S. collateralized loan obligation issuance in the first half of 2018) and bank loan revenue. Non-transaction revenue at S&P also increased due to an increase in surveillance fees, higher entity credit rating revenue, and increase in royalty revenue, and an increase in Ratings Evaluation Service activity.⁴⁸
- Morningstar, Inc. indicated that revenue at Morningstar increased compared to 2017 results, noting that Morningstar completed 138 new-issue ratings, primarily of structured finance securities, representing a 49.2% increase in the asset value of the issues rated during 2018 compared to 2017.⁴⁹

Recent regulatory filings also show declines in revenue at Moody's and S&P in the first half of 2019. Moody's Corporation reported a 4% decrease in external revenue at Moody's in the first half of 2019, as compared to the first half of 2018, due to lower refinancing activity in the bank loan sector and the collateralized loan obligation assets class primarily resulting from higher borrowing costs. The decline in revenue at Moody's was partially offset by higher revenue from rating both investment grade and high-yield corporate debt.⁵⁰ S&P Global reported a 2% decline

⁴⁷ See Moody's Corporation Annual Report on Form 10-K for the year ended December 31, 2018, available at https://www.sec.gov/Archives/edgar/data/1059556/000119312519048576/d679514d10k.htm#toc679514_26.

⁴⁸ See S&P Global Inc. Annual Report on Form 10-K for the year ended December 31, 2018, available at <https://www.sec.gov/Archives/edgar/data/64040/000006404019000059/spgi-20181231x10k.htm#sF7DABB9B419F5005829C23896EFBA35A>. S&P describes its Rating Evaluation Service as an assessment of the potential credit impact of strategic or financial initiatives under consideration by an entity. See S&P Global Ratings: Ratings Evaluation Service (RES), available at https://www.spratings.com/en_US/products/-/product-detail/rating-evaluation-service-res-.

⁴⁹ See Morningstar, Inc. Annual Report on Form 10-K for the year ended December 31, 2018, available at https://www.sec.gov/Archives/edgar/data/1289419/000128941919000035/morn_10kx12312018.htm#s0D8303B472BA5093B033CC33FE508D3F.

⁵⁰ See Moody's Corporation Quarterly Report on Form 10-Q for the period ended June 30, 2019, available at <https://www.sec.gov/ix?doc=/Archives/edgar/data/1059556/000105955619000004/mco-20190630.htm>.

in revenue at S&P in the first half of 2019, as compared to the first half of 2018, noting that transaction revenue decreased due to lower bank loan ratings revenue, which was partially offset by higher corporate bond ratings revenue. As reported by S&P Global, transaction revenue was also unfavorably impacted by a decrease in structured finance revenue driven by decreased collateralized loan obligations and other asset-backed securities issuance.⁵¹

Recent regulatory filings have also shown revenue growth at two smaller NRSROs. Morningstar, Inc. indicated that transaction-based revenue at Morningstar increased in the first half of 2019, compared to the first half of 2018, primarily due to growth in the asset-value of new-issue ratings in structured finance securities.⁵² Further, following completion of its acquisition of DBRS, Morningstar, Inc. disclosed certain financial information of DBRS. This information shows that revenue at DBRS for the annual period ended November 30, 2018 increased by 4.9%, compared to the annual period ended November 30, 2017, and that revenue for the three month period ended February 28, 2019 increased by 5.3%, compared to the three month period ended February 28, 2018.⁵³

B. Recent Developments in the State of Competition Among NRSROs

1. Market Share Observations in the Asset-Backed Securities Rating Category

As noted in Section IV.A.1. of this Report, the number of ratings recently issued by NRSROs may give a clearer picture of competition than the number of ratings each NRSRO currently has outstanding. For example, Chart 2 indicates that, as of December 31, 2018, the smaller NRSROs collectively have 20.3% of the ratings outstanding in the asset-backed securities rating category. However, the market share data discussed in this Section IV.B. show that higher market share percentages have been obtained by smaller NRSROs in ratings issuance with respect to certain types of asset-backed securities. This market share data continues the growth trend the Staff has observed since the 2012 Annual Report for some smaller NRSROs in the asset-backed securities rating category.

Sections (a) and (b) below discuss NRSRO market share information with respect to certain asset-backed securities, as reported on the Commercial Mortgage Alert and Asset-Backed Alert websites.⁵⁴ Commercial Mortgage Alert shares information on one category of asset-

⁵¹ See S&P Global Inc. Quarterly Report on Form 10-Q, for the period ended June 30, 2019, available at <https://www.sec.gov/ix?doc=/Archives/edgar/data/64040/000006404019000162/spgi-2019630x10q.htm>.

⁵² See Morningstar, Inc. Quarterly Report on Form 10-Q for the period ended June 30, 2019, available at <https://www.sec.gov/ix?doc=/Archives/edgar/data/1289419/000128941919000162/morn10q06302019.htm>.

⁵³ See Morningstar, Inc. Amendment No. 1 to Current Report on Form 8-K/A dated July 2, 2019, available at https://www.sec.gov/ix?doc=/Archives/edgar/data/1289419/000141057819001286/tv529468_8k.htm.

⁵⁴ See Commercial Mortgage Alert website, available at <https://www.cmalert.com/> and Asset-Backed Alert website, available at <https://www.abalert.com/>. The information in Charts 7 through 13 is based on these websites as of November 5, 2019. Although the information available on these websites may provide insight into recent developments regarding the state of competition among NRSROs in the asset-backed securities rating category, it has certain limitations. For instance, the information is presented using the number of transactions with respect to which an NRSRO has reported issuing a credit rating and the aggregate dollar amount thereof, rather than indicating where an NRSRO may have rated fewer than all tranches of a particular transaction.

backed securities: CMBS.⁵⁵ Asset-Backed Alert reports NRSRO market share information on three categories of asset-backed securities: (i) ABS;⁵⁶ (ii) MBS;⁵⁷ and (iii) CLOs.⁵⁸

(a) CMBS

Charts 7 through 10 provide information concerning U.S.⁵⁹ CMBS ratings by NRSROs, as reported in Commercial Mortgage Alert. NRSRO market share varies between the conduit CMBS and single borrower CMBS segments,⁶⁰ the two segments that account for most of the non-agency⁶¹ U.S. CMBS transactions rated by NRSROs. The charts include reported market share information for total non-agency U.S. CMBS transactions,⁶² U.S. conduit CMBS transactions, U.S. single borrower CMBS transactions, and agency CMBS transactions⁶³ for calendar year 2017, calendar year 2018, and the first half of calendar year 2019.

⁵⁵ The “CMBS” category is comprised of transactions collateralized by mortgages or leases on commercial or multi-family income-producing properties (excluding commercial real estate collateralized debt obligations). See Commercial Mortgage Alert website, available at <https://www.cmalert.com/>.

⁵⁶ The “ABS” category is comprised of securities that are collateralized by assets of some kind (excluding the following: CMBS; MBS; Fannie Mae and Freddie Mac issues (other than risk transfer transactions); issuances by municipalities; tax exempt issues; issues that are fully retained by an affiliate of the deal sponsor; commercial paper and other continuously offered securities such as medium-term notes; CLOs and other collateralized debt obligations; and refinancings of previously offered securities). See Asset-Backed Alert website, available at <https://www.abalert.com/>.

⁵⁷ The “MBS” category is comprised of securities secured by U.S. first-lien mortgages on residential properties (excluding Fannie Mae and Freddie Mac issues, securities secured by non-performing or re-performing mortgages, subprime mortgages, or mortgages financing single-family rental businesses, and refinancings of previously offered securities). See id.

⁵⁸ The “CLO” category is comprised of arbitrage collateralized loan obligations secured by broadly syndicated corporate loans and middle market collateralized loan obligations secured by loans to small to medium sized enterprises. See id.

⁵⁹ References to “U.S.” CMBS, MBS, ABS, and CLO issuance and market shares in this Section IV.B.1. and Section IV.B.2. reflect securities issued for sale primarily in the U.S., which include securities issued publicly and those issued under Rule 144A under the Securities Act of 1933, as amended (the “Securities Act”). See Asset-Backed Alert website, available at <https://www.abalert.com/>; Commercial Mortgage Alert website, available at <https://www.cmalert.com/>.

⁶⁰ The term “conduit” refers to a financial intermediary that functions as a link, or conduit, between the lender(s) originating loans and the ultimate investor(s). The conduit makes loans or purchases loans from third party correspondents under standardized underwriting parameters and once sufficient volume has accumulated, pools the loans for sale to investors in the CMBS market. See https://www.crefc.org/uploadedFiles/Site_Framework/Industry_Resources/Glossary%20Revised%202014%20Update.pdf. In contrast, a single borrower transaction includes commercial mortgage loans made to a single borrower.

⁶¹ “Non-agency” CMBS refers to CMBS that are not issued or guaranteed by Fannie Mae, Freddie Mac, or Ginnie Mae. “Agency” CMBS generally refers to CMBS that are issued or guaranteed by such entities.

⁶² Total U.S. CMBS transactions include conduit CMBS, single-borrower CMBS, and other types of CMBS, such as distressed/non-performing CMBS transactions and re-securitizations of CMBS transactions.

⁶³ Only agency CMBS transactions with a rating from one or more NRSROs are included for determining NRSRO market share in the agency CMBS category. See Commercial Mortgage Alert website, available at <https://www.cmalert.com/>.

Chart 7: Rating Agency Market Share for Total Non-Agency U.S. CMBS Issued in 2017, 2018, and First Half of 2019*

1H 2019 Rank	NRSRO	1H-2019 Issuance (\$Mil.)	No. of deals	Market Share (%)	2018 Issuance (\$Mil.)	No. of deals	Market Share (%)	2017 Issuance (\$Mil.)	No. of deals	Market Share (%)
1	Fitch	22,336.8	29	57.2	50,465.4	63	65.6	57,482.6	65	65.5
2	Moody's	19,104.2	28	48.9	32,894.5	44	42.7	54,655.4	61	62.2
3	S&P	16,183.4	27	41.4	34,764.4	58	45.2	38,294.1	59	43.6
4	KBRA	16,116.9	22	41.3	30,302.0	38	39.4	45,747.2	52	52.1
5	Morningstar	11,812.1	20	30.2	12,300.8	21	16.0	11,246.2	21	12.8
6	DBRS	9,113.3	15	23.3	27,259.2	38	35.4	26,361.7	35	30.0
	Total Rated Market	39,067.6	66		76,978.8	122		87,812.4	121	

Source: <https://www.cmalert.com/rankings.pl?Q=78>

Chart 8: Rating Agency Market Share for U.S. Conduit CMBS Issued in 2017, 2018, and First Half of 2019*

1H 2019 Rank	NRSRO	1H-2019 Issuance (\$Mil.)	No. of deals	Market Share (%)	2018 Issuance (\$Mil.)	No. of deals	Market Share (%)	2017 Issuance (\$Mil.)	No. of deals	Market Share (%)
1	Fitch	18,207.8	21	100.0	40,292.1	44	100.0	48,522.9	52	100.0
2	KBRA	12,808.0	15	70.3	22,609.6	26	56.1	30,425.7	33	62.7
3	S&P	9,878.4	11	54.3	19,358.5	19	48.0	9,411.2	10	19.4
4	Moody's	8,329.4	10	45.7	20,933.7	25	52.0	45,617.1	49	94.0
5	DBRS	4,249.3	5	23.3	17,682.5	18	43.9	17,918.3	19	36.9
6	Morningstar	3,069.4	3	16.9	0.0	0	0.0	2,175.6	2	4.5
	Total Rated Market	18,207.8	21		40,292.1	44		48,522.9	52	

Source: <https://www.cmalert.com/rankings.pl?Q=78>

Chart 9: Rating Agency Market Share for U.S. Single Borrower CMBS Issued in 2017, 2018, and First Half of 2019*

1H 2019 Rank	NRSRO	1H-2019 Issuance (\$Mil.)	No. of deals	Market Share (%)	2018 Issuance (\$Mil.)	No. of deals	Market Share (%)	2017 Issuance (\$Mil.)	No. of deals	Market Share (%)
1	Moody's	10,375.6	17	51.5	11,795.9	18	33.7	9,038.3	12	24.8
2	Morningstar	8,742.8	17	43.4	11,585.2	20	33.1	8,668.4	18	23.7
3	S&P	6,305.0	16	31.3	14,409.7	37	41.2	26,301.6	45	72.1
4	DBRS	4,555.0	8	22.6	9,279.4	18	26.5	7,924.3	15	21.7
5	Fitch	4,129.0	8	20.5	9,783.2	18	27.9	8,959.7	13	24.5
6	KBRA	2,909.6	6	14.4	7,692.4	12	22.0	14,864.9	17	40.7
	Total Rated Market	20,151.6	42		35,003.2	73		36,499.6	64	

Source: <https://www.cmalert.com/rankings.pl?Q=78>

* Charts 7 through 9 reflect market share percentages based on dollar amounts of issuance. The sum of the market share percentages exceeds 100% since more than one NRSRO may rate a particular transaction.

Chart 10: Rating Agency Market Share for Agency CMBS Issued in 2017, 2018, and First Half of 2019*

1H 2019 Rank	NRSRO	1H-2019 Issuance (\$Mil.)	No. of deals	Market Share (%)	2018 Issuance (\$Mil.)	No. of deals	Market Share (%)	2017 Issuance (\$Mil.)	No. of deals	Market Share (%)
1	DBRS	5,740.6	4	49.9	6,118.9	5	25.0	2,811.1	2	12.3
2	S&P	5,677.1	4	49.3	2,649.6	2	10.8	6,758.3	5	29.5
3	Morningstar	3,089.1	2	26.8	5,514.0	4	22.6	5,559.4	4	24.2
4	Moody's	2,932.9	2	25.5	9,011.3	7	36.9	5,484.5	5	23.9
5	Fitch	2,902.8	2	25.2	14,256.1	11	58.3	11,890.7	10	51.9
6	KBRA	2,683.1	2	23.3	11,343.0	9	46.4	13,359.0	10	58.3
	Total Rated Market	11,512.8	8		24,446.4	19		22,931.5	18	

Source: <https://www.cmalert.com/rankings.pl?Q=78>

* Chart 10 reflect market share percentages based on dollar amounts of issuance. The sum of the market share percentages exceeds 100% since more than one NRSRO may rate a particular transaction.

As illustrated in Charts 7 through 9 above, the larger NRSROs generally obtained the highest market shares in rating non-agency U.S. CMBS transactions, but smaller NRSROs have achieved significant market shares as well. In the first half of 2019, each NRSRO active in rating U.S. CMBS had market shares greater than 23%. As discussed below, KBRA has continued to obtain high market share in the U.S. conduit CMBS segment and Morningstar has continued to expand its market share in the U.S. single borrower CMBS segment.

KBRA had the second highest market share in the U.S. conduit CMBS segment in both 2018 and the first half of 2019. In each of 2017, 2018, and the first half of 2019, KBRA has rated more than half of these transactions. Also of note in this segment, S&P has continued to gain market share after having been subject to a one-year timeout from marketing or rating new issue U.S. conduit CMBS transaction in accordance with a settlement, dated January 21, 2015, between S&P and the Commission regarding charges relating to S&P's ratings on certain conduit transactions.⁶⁴ S&P had the third-highest market share in this segment during the first half of 2019, rating more than half of the transactions over that period.

The relative size (proportionate to total U.S. CMBS issuance) of the U.S. single borrower segment has increased significantly in recent years and in the first half of 2019 accounted for more than half of all non-agency U.S. CMBS transactions. Morningstar has gained market share in this segment, achieving the second highest market share in the first half of 2019.

Chart 10 shows a relatively competitive landscape between the larger and smaller NRSROs with respect to credit ratings of agency CMBS transactions. In the first half of 2019, DBRS and S&P obtained the two highest market shares in this segment, each rating just under half of the transactions issued.

⁶⁴ See In the Matter of Standard & Poor's Ratings Services, Release Nos. 33-9705 and 34-74104 (Jan. 21, 2015), available at <https://www.sec.gov/litigation/admin/2015/33-9705.pdf>.

(b) ABS/MBS/CLO

Charts 11 through 13 provide information concerning U.S. ABS, U.S. MBS, and U.S. CLO ratings by NRSROs, as reported in Asset-Backed Alert. The charts include reported market share information for these transactions for calendar years 2017 and 2018 and the first half of calendar year 2019.

Chart 11: Rating Agency Market Shares for U.S. ABS Issued in 2017, 2018, and First Half of 2019*										
1H 2019 Rank	NRSRO	1H-2019 Issuance (\$Mil.)	No. of deals	Market Share (%)	2018 Issuance (\$Mil.)	No. of deals	Market Share (%)	2017 Issuance (\$Mil.)	No. of deals	Market Share (%)
1	S&P	96,135.9	150	56.2	184,537.0	296	57.8	160,648.6	242	57.0
2	Fitch	80,856.5	97	47.3	154,877.9	205	48.5	154,302.3	207	54.7
3	Moody's	75,809.0	105	44.3	153,641.5	215	48.2	139,030.5	192	49.3
4	DBRS	43,118.6	66	25.2	70,430.8	130	22.1	67,840.5	133	24.1
5	KBRA	29,175.8	77	17.1	55,990.1	147	17.5	48,783.3	124	17.3
6	Morningstar	15,083.0	35	8.8	25,506.3	53	8.0	14,879.0	33	5.3
	Total Rated Market	170,943.7	276		319,051.9	555		281,880.8	472	

Source: <https://www.abalert.com/rankings.pl?Q=102>

Chart 12: Rating Agency Market Shares for U.S. MBS Issued in 2017, 2018, and First Half of 2019*										
1H 2019 Rank	NRSRO	1H-2019 Issuance (\$Mil.)	No. of deals	Market Share (%)	2018 Issuance (\$Mil.)	No. of deals	Market Share (%)	2017 Issuance (\$Mil.)	No. of deals	Market Share (%)
1	Moody's	7,406.5	18	68.8	17,245.2	36	67.3	14,305.9	27	74.9
2	KBRA	4,622.9	12	42.9	11,757.3	27	45.9	6,967.5	15	36.5
3	DBRS	4,386.0	10	40.7	13,137.5	27	51.3	9,878.9	15	51.7
4	Fitch	2,961.4	10	27.5	10,610.4	28	41.4	7,155.7	15	37.5
5	S&P	2,324.7	5	21.6	5,302.4	8	20.7	3,114.5	4	16.3
6	Morningstar	284.1	1	2.6	2,229.3	2	8.7	0.0	0	0.0
	Total Rated Market	10,771.4	31		25,617.1	60		19,099.0	39	

Source: <https://www.abalert.com/rankings.pl?Q=102>

* Charts 11 and 12 reflect market share percentages based on dollar amounts of issuance. The sum of the market share percentages exceeds 100% since more than one NRSRO may rate a particular transaction.

Chart 13: Rating Agency Market Shares for U.S. CLO Issued in First Half of 2017, 2018, and First Half of 2019*

1H 2018 Rank	NRSRO	1H-2019 Issuance (\$Mil.)	No. of deals	Market Share (%)	2018 Issuance (\$Mil.)	No. of deals	Market Share (%)	2017 Issuance (\$Mil.)	No. of deals	Market Share (%)
1	Moody's	45,718.5	96	68.7	89,008.4	171	66.8	104,818.6	186	88.3
2	Fitch	43,927.4	88	66.0	99,947.4	183	75.0	78,518.5	139	66.2
3	S&P	34,336.3	68	51.6	64,030.1	117	48.0	50,092.9	91	42.2
4	Morningstar	2,518.0	5	3.8	10,077.8	18	7.6	9,301.3	13	7.8
5	KBRA	2,498.6	5	3.8	0.0	0	0	0.0	0	0
6	DBRS	0.0	0	0	1,784.7	4	1.3	1,040.0	3	0.9
	Total Rated Market	66,541.6	137		133,308.6	251		118,674.8	214	

Source: <https://www.abalert.com/rankings.pl?Q=102>

* Chart 13 reflects market share percentages based on dollar amounts of issuance. The sum of the market share percentages exceeds 100% since more than one NRSRO may rate a particular transaction.

Chart 11 shows that smaller NRSROs, in particular DBRS and KBRA, have built significant market share rating U.S. ABS.⁶⁵ DBRS has consistently attained a market share of over 20% in each of 2017, 2018, and the first half of 2019, and KBRA has maintained a market share of approximately 17% during the same time period.

Chart 12 shows that ratings by KBRA and DBRS continue to represent a large portion of the U.S. MBS market obtaining the second and third highest market shares in both 2018 and the first half of 2019.

Chart 13 shows that the larger NRSROs have the highest market shares in the U.S. CLO segment. However, Morningstar attained some market share in the U.S. CLO segment, and KBRA began rating such transactions in the first half of 2019.

2. Other Asset-Backed Securities Market Share Observations⁶⁶

As illustrated above, some of the smaller NRSROs have gained market share in the asset-backed securities rating category. In particular, these NRSROs have gained market share rating asset-backed securities backed by discrete asset types, in particular newer or esoteric asset types.

For instance, smaller NRSROs are significant raters of securities backed by unsecured consumer loans, including consumer loans originated through marketplace lending platforms.

⁶⁵ See Section IV.B.2. of this Report for a discussion of specific asset classes where the smaller NRSROs have reported success in gaining market share.

⁶⁶ Unless noted otherwise, all market share percentages in this Section IV.B.2. are based on dollar amounts of issuance. The information in this Section IV.B.2. from the Asset-Backed Alert database was obtained from the database on November 5, 2019.

KBRA and DBRS had the two highest market shares in this category during the Report Period, rating 71.9% and 45.2%, respectively, of the transactions priced during such period.⁶⁷

Another example of market share gains achieved by smaller NRSROs in discrete asset classes is KBRA's rating of securitizations backed by aircraft-lease receivables. KBRA rated each of the fifteen aircraft-lease receivables transactions (with an aggregate principal amount of \$7.3 billion) that priced during the Report Period.⁶⁸ KBRA has rated each aircraft-lease receivables transaction (forty-two in total) issued from December 2015 through the end of the Report Period.⁶⁹

KBRA was also active rating whole-business securitizations during the Report Period, rating 33.3% of such transactions.⁷⁰ KBRA's market share in the whole-business category was even greater when measured by the number of transactions rather than dollar amounts of issuance; KBRA rated six of the eleven transactions issued during the Report Period.⁷¹

Smaller NRSROs have also been able to gain market share in rating more traditional types of asset-backed securities. DBRS has gained the largest market share among the smaller NRSROs with respect to the more traditional types of asset-backed securities (aside from the MBS and CMBS categories). For example, DBRS rated 50.5% of the transactions backed by student loans that priced during the Report Period.⁷² DBRS also rated a sizable minority of one of the larger asset-backed securities asset classes—i.e., credit card transactions.⁷³ DBRS rated 28.6% of the credit card asset-backed securities priced during the Report Period.⁷⁴

DBRS has also been able to gain market share in auto-related asset-backed securities. During the Report Period, DBRS rated 56.3% of the auto-fleet lease transactions, 26.0% of the subprime auto loan transactions, 14.8% of the auto lease transactions, and 6.7% of the prime auto loan transactions that priced during the Report Period.⁷⁵ KBRA has also established a market share presence in some of these auto-related asset-backed security categories, rating 8.7% of the

⁶⁷ See Asset-Backed Alert database. The Asset-Backed Alert database indicates that 44 unsecured consumer loan transactions totaling \$15.6 billion priced during the Report Period.

⁶⁸ See id.

⁶⁹ See id.

⁷⁰ See id. The Asset-Backed Alert database indicates that 11 whole-business securitization transactions totaling \$8.9 billion priced during the Report Period. Morningstar also rated a whole-business securitization transaction representing 3.8% of the transactions during the Report Period. See id.

⁷¹ See id.

⁷² See id. The Asset-Backed Alert database indicates that 35 student loan transactions totaling \$20.7 billion priced during the Report Period.

⁷³ The Asset-Backed Alert database lists 55 credit card transactions totaling \$34.3 billion that priced during the Report Period.

⁷⁴ See Asset-Backed Alert database.

⁷⁵ See id. For the Report Period, the Asset-Backed Alert database lists 18 auto-fleet lease transactions totaling \$11.5 billion, 60 subprime auto loan transactions totaling \$33.4 billion, 40 auto lease transactions totaling \$28.1 billion, and 92 prime auto loan transactions totaling \$79.8 billion.

auto-fleet lease transactions and 30.3% of the subprime auto loan transactions during the Report Period.⁷⁶

Smaller NRSROs have also achieved notable market share in certain types of residential mortgage-backed securities not included in Chart 12. DBRS rated all of the securities backed by non-performing or re-performing mortgages that priced in the Report Period.⁷⁷ Additionally, each of Morningstar, DBRS, and KBRA were active rating securities backed by subprime mortgages and risk transfer securities during the Report Period. For securities backed by subprime mortgages, Morningstar rated 50.1%, DBRS rated 27.0%, and KBRA rated 19.8% of such transactions.⁷⁸ For risk transfer securities, Morningstar rated 42.5%, DBRS rated 36.6%, and KBRA rated 13.3% of such transactions.⁷⁹

C. Barriers to Entry

Despite the notable progress made by smaller NRSROs in gaining market share in some types of asset-backed securities over the past few years (see Section IV.B. of this Report), barriers to entry continue to exist in the credit ratings industry, presenting competitive challenges for the smaller NRSROs.⁸⁰

One such potential barrier referred to by certain smaller NRSROs is the minimum ratings requirements that specify use of the ratings of particular rating agencies in the investment management contracts of some institutional fund managers and the investment guidelines of some fixed income mutual fund managers, pension plan sponsors, and endowment fund managers.⁸¹ The effect of these requirements can be to increase the demand and liquidity for securities bearing the ratings of specified rating agencies.⁸² Historically, many of these guidelines refer to the ratings from the larger NRSROs by name (i.e., S&P, Moody's, and Fitch).

⁷⁶ See id.

⁷⁷ See id. The Asset-Backed Alert database indicates that 25 non-performing or re-performing mortgage backed securities transactions totaling \$19.6 billion priced during the Report Period. Morningstar was also active in this asset class, rating 8.2% of such transactions. See id.

⁷⁸ See id. The Asset-Backed Alert database indicates that 39 subprime mortgage backed securities transactions totaling \$14.6 billion priced during the Report Period.

⁷⁹ See id. The Asset-Backed Alert database indicates that 34 risk transfer transactions totaling \$28.6 billion priced during the Report Period.

⁸⁰ See Shankar Ramakrishnan and Philip Scipio, Big three in credit ratings still dominate business, May 4, 2016, available at <https://www.reuters.com/article/uscorpbonde-ratings-idUSL2N17U1L4>.

⁸¹ See letter from KBRA to the Commission, dated August 19, 2014, available at <https://www.sec.gov/comments/s7-18-11/s71811-88.pdf>. This barrier to entry was also mentioned during the SEC's Credit Ratings Roundtable held on May 14, 2013. At the roundtable, a representative of Morningstar mentioned that, according to a study conducted by Morningstar, approximately 42% of open-end fixed income funds with investment guidelines that reference ratings specifically refer to S&P, Moody's, or a "major NRSRO." See Credit Rating Roundtable, May 14, 2013, available at <https://www.sec.gov/spotlight/credit-ratings-roundtable.shtml>.

⁸² The effect of including particular NRSROs in investment guidelines was highlighted in an article concerning a loan securitization. In the article, an issuer referred to the fact that many institutional buyers are limited to purchasing securities rated by one of the larger NRSROs, and that a larger NRSRO's rating expanded the number of entities which could purchase the rated securities. See Tracy Alloway, Peer-to-Peer Lender Wins Landmark Rating, Fin. Times, July 10, 2014 at Companies and Markets, p. 18.

Despite reports in recent years that investors are increasingly changing their guidelines to allow for investments in securities rated by a wider group of NRSROs,⁸³ investment guidelines continue to be identified as a factor impacting the selection of NRSROs to rate certain transactions.⁸⁴

A related barrier to entry is the inclusion requirements of some fixed income indices. To be included in certain of these indices, securities must be rated by specific NRSROs. Certain investment companies try to closely track the performance of the indices by purchasing the securities included in them, and can thus increase the demand for securities bearing the ratings of specific NRSROs. For instance, Fitch announced that its ratings had been added to the J.P. Morgan High-Yield Bond Indices, noting that investors rely on such indices to determine which bonds suit their level of credit risk.⁸⁵

Market participants and academics have identified various other barriers to entry in the credit rating industry, including economic and regulatory barriers.⁸⁶ Among the regulatory barriers to entry for NRSROs are the costs associated with complying with the statutory provisions implemented by the Rating Agency Act and the Dodd-Frank Act and the related rules adopted by the Commission, including the rules and rule amendments that the Commission adopted pursuant to the Dodd-Frank Act (the “NRSRO Amendments”).⁸⁷ Commenters on the proposed NRSRO Amendments expressed concerns that certain of the requirements would be burdensome for smaller NRSROs to implement and could raise barriers to entry for credit rating agencies that seek to register as NRSROs.⁸⁸ In connection with the NRSRO Amendments, the Commission acknowledged that, despite efforts to limit the impact on small entities, the Dodd-Frank Act contained requirements, including those implemented by the NRSRO Amendments, which impose costs on NRSROs and may consequently create barriers to entry and have negative impacts on competition.⁸⁹ As discussed in more detail in a prior Annual Report, the NRSRO Amendments as adopted by the Commission include various changes intended to address concerns regarding barriers to entry, including standards allowing NRSROs to tailor particular requirements to their business models, size, and rating methodologies.⁹⁰

⁸³ See, e.g., Big Investors Accept More Rating Agencies, Asset-Backed Alert, May 19, 2017.

⁸⁴ See Fitch Leads Rankings: S&P Gains on Moody’s, Commercial Mortgage Alert, July 20, 2018.

⁸⁵ See Fitch Ratings Joins J.P. Morgan High Yield Bond Indices, Fitch Ratings, June 28, 2017.

⁸⁶ See, e.g., Section IV.C. of the March 2012 Annual Report, available at <https://www.sec.gov/divisions/marketreg/ratingagency/nrsroannrep0312.pdf>.

⁸⁷ See Nationally Recognized Statistical Rating Organizations, Release No. 34-72936 (Aug. 27, 2014), 79 FR 55077 (Sept. 15, 2014) (“Adopting Release”), available at <https://www.govinfo.gov/content/pkg/FR-2014-09-15/pdf/2014-20890.pdf>.

⁸⁸ See Adopting Release, 79 FR at 55090, 55154, 55161, and 55254-55. See also comment letters received with respect to the NRSRO Amendments as proposed, available at <https://www.sec.gov/comments/s7-18-11/s71811.shtml>.

⁸⁹ See Adopting Release, 79 FR at 55254.

⁹⁰ See Section IV.C. of the December 2015 Annual Report, available at <https://www.sec.gov/ocr/reportspubs/annual-reports/2015-annual-report-on-nrsros.pdf>.

V. TRANSPARENCY

Congress described the Rating Agency Act as an Act to improve ratings quality for the protection of investors and in the public interest “by fostering accountability, transparency, and competition in the credit rating agency industry.”⁹¹ Section 932 of the Dodd-Frank Act is entitled “Enhanced regulation, accountability, and transparency of NRSROs.” Both Acts contain various provisions designed to increase the transparency—through clear disclosure open to public scrutiny—of, among other things, NRSROs’ credit rating procedures and methodologies, business practices, and credit ratings performance. Under Exchange Act rules, NRSROs are required to disclose:

- standardized performance statistics;⁹²
- consolidated information about credit rating histories;⁹³
- information about material changes and significant errors in the procedures and methodologies used to determine credit ratings;⁹⁴
- information about specific rating actions;⁹⁵ and
- clear definitions of each symbol, number, or score in the rating scale used by the NRSRO.⁹⁶

NRSROs must also disclose certain information in connection with each rating action.⁹⁷ Such information includes, among other things, the version of the procedure or methodology used to determine the credit rating, a description of the types of data that were relied upon for purposes of determining the credit rating, an assessment of the quality of information available and considered in determining the credit rating, and information on the sensitivity of the credit ratings to assumptions made by the NRSRO.⁹⁸

In addition to or in connection with required disclosures, NRSROs often issue press releases and reports at the time of a rating action to describe the rationale behind such rating action, and make versions of the methodologies for determining credit ratings available on their websites.⁹⁹ The availability of underlying methodologies, together with a report discussing the analysis supporting the rating action, provides additional transparency into the credit rating process.

Transparency may also be increased to the extent NRSROs publish commentaries or research. Annual Reports since 2013 have described commentaries issued by NRSROs to

⁹¹ See the preamble to the Rating Agency Act.

⁹² See Instructions for Exhibit 1 to Form NRSRO.

⁹³ See Exchange Act Rule 17g-7(b).

⁹⁴ See Exchange Act Rule 17g-8(a)(4).

⁹⁵ See Exchange Act Rule 17g-7(a).

⁹⁶ See Exchange Act Rule 17g-8(b)(2).

⁹⁷ See Exchange Act Rule 17g-7(a).

⁹⁸ See Exchange Act Rule 17g-7(a)(1)(ii).

⁹⁹ The reports accompanying a rating action are frequently available on a paid subscription basis, although some NRSROs provide access to such reports for free.

highlight differences in credit views that they may have with other NRSROs. The Annual Reports have mentioned that the commentaries can serve to enhance investors' understanding of the differences in ratings approaches used by NRSROs.

This Report Period saw an expansion of the range of NRSROs issuing commentaries, topics covered by the commentaries, and responses to the commentaries by the relevant NRSROs. For example, in the early part of the Report Period, Fitch issued a press release noting that it had increased unsolicited commentaries in recent months and signaled the possibility of its publishing more unsolicited commentaries.¹⁰⁰ This development, and the directness of some of the commentaries, may also indicate a state of increased competition among NRSROs—appearing to reflect an interest in demonstrating analytical skills and differentiating themselves from other NRSROs. For example, Fitch released a report in May 2019 critiquing ratings on recent U.S. marketplace lending asset-backed securities.¹⁰¹ In May 2019, KBRA released a report explaining that improvements in marketplace loan securitization platforms have resulted in more predictable credit performance across the industry and upward rating migration for marketplace lending securitizations.¹⁰²

Fitch also commented during the Report Period on residential mortgage-backed securities ratings issued by certain NRSROs that are higher than other agencies' ratings for a given credit enhancement level.¹⁰³ In response, one of the NRSROs questioned Fitch's assumptions and emphasized the importance of transparency in its ratings.¹⁰⁴ Fitch also commented on AAA ratings that two NRSROs assigned to a collateralized loan obligations with a large concentration in particular industries.¹⁰⁵

Another type of commentary issued during the Report Period described perceived constraints within ratings of other NRSROs. For example, KBRA issued commentaries relating to ceilings imposed by other NRSROs on certain municipal finance ratings, noting that the use of rating ceilings in municipal finance needlessly limits the rating for many credits,¹⁰⁶ and on rating downgrades by other NRSROs for certain banks operating in Puerto Rico, that in KBRA's view overestimated the likelihood of default.¹⁰⁷

¹⁰⁰ See More Unsolicited SF Comments Are Likely due to Late-Cycle Behaviour, Fitch Ratings, Oct. 15, 2018.

¹⁰¹ See Declining Credit Enhancement in US MPL ABS is Unwarranted, Fitch Ratings, May 13, 2019 (stating that, while asset quality remained relatively steady, credit enhancement levels of certain of these asset-backed securities meaningfully declined since 2017).

¹⁰² See Evolution of the Consumer Loan Marketplace Lending Sector, Kroll Bond Rating Agency, May 24, 2019.

¹⁰³ See Ratings 'Split' Emerging in New U.S. RMBS, Fitch Ratings, Aug. 15, 2018.

¹⁰⁴ See Alexander Saeedy, Fitch sounds off on methodology, ratings shopping in RMBS, globalcapital.com, Aug. 15, 2018 (Issue 1568), available at <https://www.globalcapital.com/article/b19jgp3tyw38pf/fitch-sounds-off-on-methodology-ratings-shopping-in-rmbs>.

¹⁰⁵ See CLO Concentration a Potential Risk, Fitch Ratings, Sept. 10, 2018.

¹⁰⁶ See KBRA Releases Comment – Municipal Default History: Rating Ceilings Do Not Hold Up, Kroll Bond Rating Agency, July 25, 2019.

¹⁰⁷ See KBRA Releases Report – Puerto Rico's Independent Banks: An Underappreciated Evolution, Kroll Bond Rating Agency, June 19, 2019.

In addition to responding to commentaries by a larger NRSRO, smaller NRSROs issued their own commentaries regarding the ratings of other NRSROs. For example, KBRA commented on the subordination levels DBRS applied in certain commercial real estate collateralized loan obligation ratings.¹⁰⁸

Also, in a monthly commercial mortgage-backed securities trend watch released in March 2019, KBRA questioned the subordination levels of a conduit commercial mortgage-backed security rating.¹⁰⁹ Morningstar responded that the commercial mortgages backing the deal in question were stronger than average and several of them had top ratings.¹¹⁰

VI. CONFLICTS OF INTEREST

NRSROs operate under one or more business models, each having potential conflicts of interest. Most of the NRSROs primarily operate under the “issuer-pay” model, which is subject to a potential conflict in that the credit rating agency may be influenced to determine more favorable (i.e., higher) ratings than warranted to retain the obligors or issuers as clients. Certain NRSROs may also operate under the “subscriber-pay” model, which means that investors pay a subscription fee to access the NRSRO’s ratings. This model is also subject to potential conflicts of interests. For example, an NRSRO may be aware that an influential subscriber holds a securities position (long or short) that could be advantaged if a credit rating upgrade or downgrade causes the market value of the security to increase or decrease or that a subscriber invests in newly issued bonds and would obtain higher yields if the bonds were to have lower ratings.

Section 15E and the related Commission rules address conflicts of interest.¹¹¹ For example, Rule 17g-5 identifies certain conflicts of interest that are prohibited under all circumstances¹¹² and other conflicts of interest that are prohibited unless an NRSRO has publicly disclosed the existence of the conflict and has implemented policies and procedures reasonably designed to address and manage such conflict.¹¹³

Among the conflicts of interest identified in Rule 17g-5 are conflicts involving individual credit analysts or other employees of the NRSRO. For example, an NRSRO is prohibited from issuing or maintaining a credit rating for a person where an employee of the NRSRO that participated in determining, or is responsible for approving, the credit rating directly owns securities or is an officer or director of the person that would be subject to the credit rating.¹¹⁴

¹⁰⁸ See DBRS Adjusts CLO Methodology, Gains Share, Commercial Mortgage Alert, June 28, 2019.

¹⁰⁹ See KBRA Releases Monthly CMBS Trend Watch, Kroll Bond Rating Agency, Mar. 7, 2019.

¹¹⁰ See Alan Tempkin, Bond Rating Triggers a Rare Rebuke as Kroll Scolds Morningstar, bloomberg.com, Mar. 11, 2019, available at <https://www.bloomberg.com/news/articles/2019-03-11/bond-grader-smackdown-kroll-questions-a-morningstar-cmbs-rating>.

¹¹¹ See, e.g., Section 15E(h) and Rule 17g-5.

¹¹² See Rule 17g-5(c).

¹¹³ See Rule 17g-5(a)(1)-(2); Rule 17g-5(b); and Form NRSRO, Exhibits 6-7. In addition, Section 15E(t)(3)(B) requires an NRSRO’s board of directors to oversee the establishment, maintenance, and enforcement of policies and procedures to address, manage, and disclose any conflicts of interest.

¹¹⁴ See Rule 17g-5(c)(2) and Rule 17g-5(c)(4).

Rule 17g-5(c)(8) is another example of a prohibited conflict of interest involving persons within an NRSRO. Under the Rule, an NRSRO is prohibited from issuing or maintaining a credit rating where a person within the NRSRO who participates in determining or monitoring the rating, or developing or approving procedures or methodologies used for determining the rating, also (a) participates in sales or marketing activities of the NRSRO or its affiliate or (b) is influenced by sales or marketing considerations.¹¹⁵

Other statutory provisions and Commission rules address potential conflicts of interest that may arise when a credit analyst seeks employment outside the NRSRO. Section 15E requires each NRSRO to have policies and procedures in place to provide for an internal “look-back” review process in order to determine whether any conflict of interest of a former employee influenced a credit rating in certain instances.¹¹⁶ Rule 17g-8(c) requires an NRSRO’s policies and procedures to address instances in which a “look-back” review determined that a conflict of interest influenced a credit rating. Such policies and procedures are required to be reasonably designed to ensure that the NRSRO will promptly determine whether a credit rating must be revised and promptly publish a revised credit rating or an affirmation of the credit rating, along with certain disclosures about the existence of the conflict.¹¹⁷

One of the conflict of interest rules concerns the issuer-pay conflict of interest relating to structured finance products. The Commission adopted Rule 17g-5(a)(3) in 2009 to address this conflict of interest. Since the June 2, 2010 compliance date of Rule 17g-5(a)(3), an exemption has been in effect with regard to structured finance products issued by non-U.S. issuers in transactions outside the United States. As described in the first bullet point under Section III.B. above, the Commission codified the exemption in August 2019. In the adopting release, the Commission directed the Staff to further evaluate the effectiveness of Rule 17g-5(a)(3) with respect to ratings of structured finance products that are not eligible for relief under the adopted exemption.¹¹⁸

The annual examinations conducted by Staff in accordance with Section 15E(p) are required to include, among other things, a review of the management of conflicts of interest by the NRSROs.¹¹⁹ Information regarding the examinations, including any essential findings with respect to the required review areas, is included in OCR’s annual examination reports.¹²⁰

VII. CONCLUSION

The Staff will continue to conduct its oversight function with respect to NRSROs, including the performance of Staff examinations, and engage in other activities in furtherance of OCR’s regulatory mission, as described in this Report.

¹¹⁵ See Rule 17g-5(c)(8).

¹¹⁶ See Section 15E(h)(4)(A).

¹¹⁷ See Rule 17g-8(c).

¹¹⁸ See Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Release No. 34-86590 (Aug. 7, 2019), 84 FR 40247 (Aug. 14, 2019) at 40250.

¹¹⁹ See Section 15E(p)(3)(B)(ii).

¹²⁰ The examination reports can be found under “Summary Examination Reports” in the “Reports and Studies” section of the OCR webpage, available at <https://www.sec.gov/ocr>.