FitchRatings

February 20, 2008

Re: *Financial stability and depositor protection: strengthening the framework*

We appreciate the opportunity to participate in the current consultation process and have provided below our response to the questions listed in the "*Credit Rating Agencies*" section of your consultation draft.

Question 2.6: Have the Authorities correctly identified the issues on which international work on credit rating agencies should focus?

We interpret the main issues identified in the report as:

-- The conflicts of interest driven by the 'issuer pays' business model, including the remuneration structures employed by the agencies;
-- The information content of ratings, including the transparency of rating assumptions and rating definitions;
-- Over-reliance on ratings by investors.

Conflicts of interest

Fitch acknowledges that potential conflicts of interest exist within its current model. These are summarised in Exhibit 6 of our Form NRSRO submission to the US Securities and Exchange Commission (attached). Equally, Fitch employs a number of policies and procedures to address and manage conflicts of interest, listed in Exhibit 7 of our Form NRSRO submission (attached). We would also concur with the observation regarding feasibility of alternative business models contained in paragraph 2.57 of the consultation draft. In the wide-ranging discussions with policymakers and financial market participants of recent months, we are not aware of any proposed business model (for example, 'investor pays') which would not also contain inherent conflicts of interest. These would in turn have to be managed by the CRAs in a similar fashion.

On a factual matter, we note that paragraph 2.55 of your consultation draft states that: "*Issuers individually do not explicitly pay for post-issuance monitoring costs for a particular rated security (although initial rating fees will be set at levels that will generally cover these).*" While it is the case that fees for certain transaction types include "up-front" inclusion of surveillance fees, this is not the case for the majority of transactions, which typically specify an ongoing, regular surveillance fee. Additional fees may also apply, post-closing of a structured finance transaction, if amendments and/or changes are made to or affect the rated securities which require us to undertake additional analysis. Global structured finance billings for Fitch for the financial year ended Sep. 30, 2007 arose approximately 83% from transaction fees and 17% from surveillance fees. As with the transaction fee, the level of these fees consider the relative level of complexity of the transaction, including additional counterparty opinions that may need to be updated to maintain surveillance on the transaction rating. The composition of fee billings reflects the fact that there are many structural and other qualitative factors required to be assessed at the initial transaction rating stage which do not typically require repeat analysis during the life of the transaction.

The consultation draft also makes reference in paragraph 2.58 to "*the provision of advice on the design of securitization products.*" While the rating process in structured finance is an iterative one, Fitch does not itself advise upon, design or structure transactions. Arrangers/originators choose the assets that are to be securitised. Models published by Fitch, as part of our commitment to make our methodologies transparent, are also sometimes used by arrangers/originators in their initial review of the assets that they wish to include in a transaction. The decision of which assets to allocate, and which ratings to target, nonetheless remains entirely that of the arranger or originator. The rating committee will not propose alternative assets to include in a transaction, suggest alternative rating levels that may be targeted, or develop alternative legal structures that could be applied.

Information content
We have directly addressed the consultation draft's proposals in our response to question 2.7 below. Fitch values the feedback we receive from the policymaking community, and has actively sought out the views of regulators and supervisors in addressing information content within new and complex areas of rating application. Combined with feedback from our regular dialogue with other rating users, we are fully aware of the importance of clarity in the communication of ratings as assessments of relative ordinal default risk and not commentaries on the pricing risk, liquidity risk, or other market risks related to the rated obligation. The challenge of providing clarity on the assumptions and limitations of a rating is not, however, limited to the articulation of our rating definitions. Consequently, at the level of the individual transaction, Fitch typically publishes detailed presale research reports which provide an outline of the assumptions made to arrive at the published ratings, supported by criteria reports which describe our approach to the asset class. We are currently reviewing how transparency may be increased in each of these areas.

Over-reliance on ratings by investors
Fitch currently makes all of its published ratings available to the public free of charge via its internet sites. We do not seek to control the distribution of rating information, but we do provide clear and explicit disclosure as to the limitations and nature of ratings in our distribution channels. From a public policy perspective, we believe this current approach is likely preferable to a business model where rating information was disclosed on a selective basis to investors. As a consequence, however, we are unable to influence the way in which users may apply our rating opinions.

We support any initiative to enhance transparency and require more public disclosure from originators that would help investors to make a fully informed decision. We believe that the structured finance market in both the US and Europe is often too opaque. Transparency can best be achieved by originators, servicers, issuers and arrangers making publicly available all information, both at issuance and throughout the life of a structured finance transaction, that they make available to rating agencies (in the context of their rating analysis). We further believe that the internet provides an excellent venue to host this information so that it is freely and publicly available to all interested parties. The public availability of this information would enable investors to make fully informed investment decisions without having to rely solely on credit ratings to determine credit risk and would allow investors to assess independently issues such as market and liquidity risk that credit ratings do not address.

Question 2.7: Do you agree with the Authorities' proposals to improve the information content of credit ratings?
In response to the individual proposals made by the Authorities in paragraph 2.59:

"Publish information on the expected loss distributions of structured products, to illustrate the tail risks around them."
We are currently considering whether we could publish expected loss distributions for certain structured finance products. As discussed with the Bank of England in July of last year, this approach may lend itself more easily to some asset classes than to others (for example, it would be manifestly easier for those asset classes where the analytical process already creates a stochastic distribution of losses). Additionally, there would be challenges in ensuring that such distributions could be readily communicated to users in a concise and unambiguous format.

"Provide a summary of the information provided by originators of structured products"
As noted above, we support any initiative to enhance transparency and make available more public disclosure from originators for the benefit of investors. We do not think, however, that it should be the responsibility of the rating agencies to disclose the originator's data. Our Code of Conduct prohibits us from disclosing confidential information, consistent with the IOSCO Code of Conduct Fundamentals for Credit Rating Agencies.

"Produce explicit probability ranges for their scores on probability of default"
We have been recognised, or are currently applying for recognition, as an External Credit Assessment Institution ("ECAI") in all major markets where we operate. One part of this recognition process involves an explicit comparison between the historical default experience of an ECAI against a target band of cardinal default rates. This comparison is repeated on a regular basis going forward in assessing the performance of ECAIs over time. As we intend to maintain our ECAI status in future, we will be subject to a de facto review of our cardinal default process by every bank supervisory authority in whose jurisdiction we are recognised as an ECAI. Additionally, we are considering how we may better communicate publicly the analysis we carry out internally of the movements in historical default and transition rates, relative to long-term trends.

"Develop separate measurements for products on dimensions other than credit risk"
As discussed with the Bank of England at our July 2007 meeting, we are currently investigating whether we could provide opinions with respect to risk elements other than credit risk. For example, we have been working on ways to measure rating volatility, including stability scores. In fact, Fitch was the first agency to introduce such scores, after a lengthy development period, in early 2006. At the time we initiated Stability Scores, these were designed precisely to highlight the differing performance characteristics of instruments which carried the same rating on the 'AAA' scale. At the time, it is fair to say the market was less interested in rating stability, or indeed rating differentiation, given the then-prevailing appetite for risk. As a result, penetration of the Stability Score concept in the market was limited. In the meantime, we have worked on revising the Stability Scores to broaden the scope of products covered. Equally, it is fair to assume the market is now more sensitised to risk differentiation than it was in March 2006. As a result, we will be proposing an enhanced version of the Stability Score process in due course.

More generally, Fitch has done much work researching the best way in which to reflect additional risks affecting issuers and transactions. Our discussions with institutional investors, central banks and other interested parties have indicated a marked preference for discrete scales for discrete dimensions of risk (i.e., one scale covering default risk, one scale covering loss severity, etc.) rather than combinations of risks on the same scale. Examples of successful multiple-scale sectors include our bank and insurance sectors, with a range of Support, Individual and Financial Strength ratings complementing the mainstream Issuer Default Ratings. In contrast, other areas where multiple scales have been introduced have seen more muted investor uptake. It is important to note that we cannot 'force' usage of any of our scales, and equally – and reluctantly sometimes – we will withdraw scales for which we perceive low investor demand.

"[Bank of England proposal] CRAs consider adopting the same scoring definitions"
We would note that the topic of diverging definitions has been extensively reviewed as part of the wider debate surrounding comparability of rating scales over the past several years. In general, the distinctions in rating definitions among rating agencies are modest. The most independent review of this topic has been done in the context of the above-noted ECAI recognition process, which includes a "mapping" or correspondence table, established by each bank supervisory authority to plot rating agencies' scales against default rates prescribed by the Basel II process. This process also results in a mapping table plotting the ratings of one agency against the ratings of other agencies. It is important to note that this process did not result in pressure from the user base to standardise rating definitions.

The topic of common definitions has also been raised more recently at hearings in October 2007, convened by the Committee on the Global Financial System, at the Bank of England's offices, involving investors, arrangers and central bank representatives. The consensus was that the current modest variation in rating definitions reflected a healthy variety in methodological approaches and at the same time did not provide material obstacles to comprehension or application of the ratings by users. Movement towards a stricter homogeneity of output would likely not serve the market well and would reduce investor choice. In addition, there would be a variety of practical problems – for example, how (and by whom) would such a set of common definitions and related criteria be developed and maintained.

We believe, however, that the market may benefit from a common definition of default for purposes of the production of transition and default studies by the rating agencies and any other interested parties. A common definition of default may provide investors and all interested parties the ability to more readily compare these studies against each other and thereby more accurately assess the relative performance of rating agencies.

Question 2.8: Do you agree with the Authorities that the preferred approach to restoring confidence in ratings of structured products is through market action and, where appropriate, changes to the IOSCO Code of Conduct on Credit Rating Agencies?

We concur with the Authorities conclusion in paragraph 2.61 that the preferred approach is market action, reinforced where necessary through enhancements to the IOSCO Code of Conduct Fundamentals and by extension to the CRAs' codes of conduct. We would also concur with the Authorities conclusion in paragraph 2.56 that any actions to address concerns are coordinated internationally, to reflect the global nature of the CRAs' work.

Sincerely yours,