

February 10, 2012

Manager, Financial Services Unit
Retail Investor Division
The Treasury
Langton Crescent
Parks ACT 2600

**Re: Discussion Paper: Development of the Retail Corporate Bond Market -
Streamlining Disclosure and Liability Requirements ("Discussion Paper")**

I write on behalf of Moody's Investors Service Pty, Ltd., Australia ("MIS"), and we appreciate the opportunity to comment on the Discussion Paper. Our feedback focuses on the following two questions that the Treasury has posed:

1. Should the entity or the bond issue be required to have an investment grade rating (if available)? If so, how would an investment grade rating be defined and mandated?

MIS strongly opposes the use of a ratings-based test for determining whether an issuer can use a streamlined prospectus. We believe that such a test could increase the risk of investors using credit ratings as a gauge of something other than relative credit risk.

2. What other measures could the Government or the Australian Securities and Investments Commission ("ASIC") take to enable the provision of credit ratings to retail investors?

MIS's credit ratings are intended for use by wholesale market participants, who we expect to use our credit ratings as a supplement to, not a replacement for, their own credit analysis. We believe there is a higher risk that retail investors will over-rely on credit ratings or use them for purposes for which they are not intended. We think these risks would be greater if the Government encouraged retail investors to use credit ratings, especially under a licensing regime that characterized credit rating agencies ("CRAs") as financial advisers to the retail market. Accordingly, we recommend against the Government or ASIC facilitating the provision of credit ratings directly to retail investors, since this likely would be interpreted as the Government encouraging retail investors to rely on ratings.

Discussion

Credit ratings only address credit risk

MIS believes that it is essential for potential users of credit ratings to understand what ratings do and do not address. We have been clear that our credit ratings should be used primarily as a gauge of relative default probabilities and expected credit loss. MIS consistently has discouraged the market from using our credit ratings as indicators of price, measures of liquidity, or as advice or recommendations to buy or sell securities – all of which are influenced by factors unrelated to credit.

Likewise, an issuer's receipt of a relatively high credit rating should not be used as a proxy for

“quality”¹ (except in the limited sense of “relative creditworthiness”), for an issuer being considered “well-known”, for the quality, extent or timeliness of the information that it makes available to the public, and/or for the likelihood that it will comply with securities law disclosure requirements. Therefore, we are strongly opposed to any regulations that would reduce an issuer’s disclosure obligations or its directors’ liability exposure on the basis that the issuer had received one or more relatively high credit ratings. We think that such provisions would increase the incentives for users of credit ratings to rely upon them for purposes for which they were not intended.

In this regard, we note that the United States Securities and Exchange Commission (“SEC”) recently changed its rules on short-form prospectus eligibility to replace ratings-based criteria with alternative tests.² These new tests focus, in essence, on whether the issuer is a major issuer of publicly traded securities in U.S. capital markets that is subject to the SEC’s continuous disclosure requirements and current and timely in the filing of its required reports with the SEC.³ In addition to being subject to the discipline of the securities regulatory framework, such an issuer is likely to be widely followed by market commentators and therefore subject to market disciplinary forces. These sources of regulatory and market discipline likely reduce the risk of an issuer’s disclosures being late or inadequate. The SEC’s criteria address more directly the issue of whether an issuer provides sufficient, credible information to the market on a timely basis and, therefore, are better-suited than credit ratings to serve as eligibility criteria for a short-form prospectus disclosure regime.

MIS’s credit ratings are intended for use by wholesale market participants

To meet market needs over time, credit ratings that are widely used by market participants have developed important attributes, including the following:

- Insightful and robust analysis
- Symbols that succinctly communicate opinions
- Broad coverage across markets, industries and asset classes, enabling comparability

These attributes have enabled credit ratings to serve as a point of reference and common language of credit that can be used to compare credit risk across jurisdictions, industries and asset classes, thereby facilitating the efficient flow of capital worldwide and improving knowledge of credit risk.

The fact that credit rating symbols condense a significant amount of complex and nuanced information into a symbol system has led some people to conclude mistakenly that credit ratings are “simple” enough for anyone to use. In fact, MIS’s credit ratings are designed to be used by wholesale market participants, who are likely to have the knowledge and skills to formulate their own credit judgments and use our credit ratings to enrich, not replace, their own analysis.

Our business is very different from that, for example, of an equity research house that makes information available to financial planners to pass on to retail clients or an expert who provides a report to a client for inclusion in materials that will be circulated to retail investors. In such circumstances, the research house or expert produces information designed to be used by retail investors (among others). By contrast, MIS’s credit ratings and research are prepared with wholesale market participants in mind. This is why we applied for and obtained a wholesale-only financial services licence (“AFSL”) in Australia.

¹ Accordingly, we disagree with the statement in paragraph 33 of the Discussion Paper that “an investment grade rating is arguably a proxy for ‘quality’.”

² See SEC Release, *Security Ratings*, Release No. 3309245; 34-64975; File No. S7-18-08, August 3, 2011.

³ Some of these criteria are similar to some of the proposed issuer eligibility criteria set out in paragraphs 23-24 of the Discussion Paper.

The Discussion Paper states that many stakeholders consider it undesirable that ratings can be accessed by wholesale market participants, retail brokers and financial planners but not retail customers. We believe that the complex and nuanced nature of credit opinions makes this difference in access appropriate, particularly in Australia, where CRAs are required to be licensed as financial advisors. In our view, Australian retail investors may inadvertently be encouraged to misconstrue credit ratings provided by a CRA holding a retail AFSL as recommendations to buy or sell securities. We also believe that, in such an environment, some retail investors could over-emphasize credit ratings and/or use them as a gauge of risks other than credit risk. Such a result would be contrary to the efforts of Australian and other regulators globally to reduce the risk of over-reliance on credit ratings.⁴

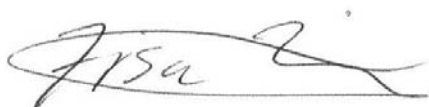
We believe that the better solution is to require issuers wishing to access retail markets to provide more information about credit risk in a format that can be understood by retail investors.⁵ After all, these issuers control the relevant information and would benefit directly from accessing retail markets.

Some might argue that requiring issuers to provide detailed disclosures about credit risk is inappropriate because it could lead to “information overload”. In other words, while enhanced disclosures might help sophisticated investors, it would make the prospectus harder to understand for many others (particular retail investors), who, in turn, will either ignore the detailed disclosure or refrain from entering the market. In MIS’s view, if the concern is that detailed disclosure will overwhelm some investors or make them more reluctant to read the prospectus, the solution is not to limit the information disclosed (or permit issuers to convey information about credit risk through disclosure of a credit rating). Such a solution would only serve to create a false sense of security and create the impression that the security is easy to understand and, therefore, suitable for retail investors. Rather, MIS believes that issuers should provide information to investors that highlights the complexities and risks of particular products, so that investors can make informed judgments about whether they understand those complexities and risks and are comfortable assuming such risks by investing in the product.

For the reasons set out above, therefore, MIS would be opposed to the Government or ASIC taking any steps that could be perceived as encouraging retail investors to rely on credit ratings.

Once again, we appreciate the opportunity to comment on the Discussion Paper. We would be pleased to discuss our comments further with the Treasury or its staff.

Sincerely,



Farisa Zarin
Managing Director
Global Regulatory Affairs

⁴ This concern about the potential for investors to over-rely on ratings is highlighted in the Discussion Paper at paragraph 33. As a member of the G20, the Australian Government has endorsed the Financial Stability Board’s October 2010 *Principles for Reducing Reliance on Credit Ratings*.

⁵ We note that the Discussion Paper requests feedback on its proposals regarding the types of disclosures that bond issuers could be required to provide in prospectuses, such as disclosures about credit risk.