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January, 23, 2012

Jennifer Johnson
Secretary
Board of Governors
Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, DC 20551

Delivered via email: regs.comments@occ.treas.gov

Re: Risk-Based Capital Guidelines: Market Risk; Alternatives to Credit Ratings for Debt and Securitization Positions [DocketID QCC-2010-0003]

Comments from Robert Kane, CEO, Bondview

Thank you for giving us the opportunity to comment on your notice of proposed rule making (NPR); amendment to market risk NPR published on January 11, 2011: Risk-Based Capital Guidelines: Market Risks; Alternatives to Credit Ratings for Debt and Securitization Positions.

Who We Are

BondView is a leading independent web-based advocate for both professional and retail investors in the municipal bond marketplace.

We wanted to comment on this regulation because we offer an alternative rating solution that has been in use by both professional and retail investors for almost two years. We built, implemented and currently maintain this working alternative rating system. It is based upon "Market Ratings" that measure the default risk for each and every bond in the municipal marketplace. We publish these alternative ratings for free at www.bondview.com for investors to use. We want to share our experiences in the hope this model could serve as a reference point for implementing alternatives to credit ratings for other investment assets.

In summary, we suggest that rather than mandate alternative ratings as a replacement for approved credit ratings agencies, the marketplace would be better served by a hybrid approach that includes alternative ratings based on market implied ratings. This would provide the marketplace with a published "early warning system" that can signal when credit ratings need to be re-evaluated so as to reflect marketplace realities. In this way, these dual rating systems can provide reciprocal checks and balances.

Some Concerns With The Traditional Rating Agency Approach

Credit ratings have traditionally been provided by a handful of for-profit companies ("rating agencies"), with Moody's and Standard & Poor's dominating the marketplace. The issuers of bonds contract with one or more rating agencies who provide their assessment of credit strength. The rating agencies conduct their evaluation and publish a bond's rating so it is known prior to the sale of the bonds.

In a perfect world, rating agencies would change their rating, up or down, depending on material changes in the credit strength of the issuer. However, the sheer volume of outstanding issues in the fixed-income markets makes it impossible for ongoing surveillance to be done cost effectively using the traditional ratings agency approach. The $3.7 trillion dollar municipal marketplace is made up of about 50,000 different issuers who have issued 1.5 million bonds. Despite this market size and its importance to investors, many municipal bonds either currently are not rated or have never been rated. In addition, the rating agencies rely heavily on financial audits and other issuers' disclosures that are often out of date by the time they are released. Many high profile defaults have occurred without the issuer being downgraded. When this happens it is a disservice to investors.

Market-Based Ratings

The market-based rating approach differs in that it's centered on assessing the credit strength of an issuer by determining the bond's relative default risk. This is done by comparing a bond's yield to the yield of a Treasury instrument of the same maturity. A Treasury instrument is used as the baseline for a riskless investment since the U.S. Government has never defaulted on a debt obligation. The spread between the yield of the bond and a comparable Treasury security defines the relative default risk. In addition, there are techniques that can used to improve rating accuracy by categorizing similar bonds using additional criteria including state, market sector and tax treatment.

Advantages of the Market-Based Approach

The financial literature is replete with studies demonstrating the superiority of market ratings to agency ratings. These studies have been performed primarily by academic researchers that use statistical techniques based on actual ratings and trade data. The studies show that agency ratings lag market ratings in predicting defaults. Market ratings provide an earlier warning than do agency ratings. In our own experience the advantage of the market-based rating approach is its objectivity, timeliness and accuracy. The rating, which is the relative default risk, is based on actual market trades. It is a purely unbiased determination. In addition, since the relative default risk is based on spreads that change daily as the securities are traded, the rating of each bond also changes daily. This approach solves the timeliness issue since bonds are constantly re-rated. The rating agency approach generally is to re-rate bonds on a less timely basis with years sometimes going by before a bond is re-rated. In the meantime, high profile defaults occur without an issuer being downgraded. When this happens it is a disservice to all investors.

Conclusion

We have additional opinions based on our real world experience that we would be happy to share with the committee about the benefits and limitations of alternative ratings using market implied ratings.

In summary, we suggest that rather than mandate alternative ratings as a replacement for approved credit ratings agencies, the marketplace would be better served by a hybrid approach that includes alternative ratings based on market implied ratings. This would provide the marketplace with a published "early warning system" that can signal when credit ratings need to be re-evaluated so as to reflect marketplace realities. In this way, these dual rating systems can provide reciprocal checks and balances.

The traditional rating agency approach for rating the credit quality of bonds has suffered a major loss of confidence over the past five years. Both issuers and the investing public are searching for alternatives to complement or replace the current rating agency model. Our market-based approach, driven by advances in technology and required disclosure of trade data and financial reports, is now poised for use by investors on internet platforms at a reasonable cost. This new approach provides for objective ratings that are more accurate and timely than those provided by rating agencies.

It is clearly in the interest of the investing public, and for the proper functioning of the municipal bond marketplace, for a market-based rating approach to be utilized, in addition to, or in lieu of, the traditional rating agency approach.

Should you have any questions or desire any clarification concerning the matters addressed in this letter, please do not hesitate to contact me at (866) 261 9533 or Robert@bondview.com.

Sincerely,

Robert Kane
CEO
Bondview.com