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Standard & Poor's Requests Comments On Proposed Criteria For Rating Nonbank Financial Institutions

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NEW YORK (Standard & Poor's) Aug. 14, 2014--Standard & Poor's Ratings Services is requesting comments on its proposed framework for rating nonbank financial institutions (NBFI) globally. The proposed criteria, outlined in "Request For Comment: Nonbank Financial Institutions Rating Methodology," articulate the steps in determining the issuer credit rating (ICR) on an NBFI.

The proposed criteria draw upon Standard & Poor's bank criteria in many ways, in particular in placing heightened emphasis on economic risk and industry risk in setting the starting point, or anchor, in rating an institution. We propose to then add to or subtract notches from the anchor for entity-specific factors, such as business position; capital, leverage, and earnings; risk position; and funding and liquidity, to determine the group credit profile

(GCP) or stand-alone credit profile (SACP). In certain cases, a low factor assessment, such as "weak," may cap the SACP or GCP or rating. Lastly, the criteria would then apply our view of potential extraordinary support or intervention, including from an entity's government or group, to arrive at the ICR.

SCOPE OF THE PROPOSAL

The proposed criteria apply to securities firms and certain financial companies, which we collectively refer to as NBFIs. Securities firms (or brokers) include regional and independent securities firms. NBFIs include retail- and wholesale-focused broker-dealers, which typically do not have banks in their organizational hierarchies, or, if they do, the bank is not a main factor in the business profile. They may benefit from prudential bank regulation, but lending is a minor portion of their business. Securities firms that benefit from prudential bank regulation and have substantial lending operations, or are global, large, and complex, are typically not in scope (they are typically rated under our bank criteria).

Most financial companies in scope are referred to as finance companies (fincos). We define fincos as firms (financial institutions sometimes affiliated with a holding company) that are typically not registered as banks and that make loans to individuals or businesses. They are typically non-depository financial institutions and fund their investment (and lending) activities from the sale of securities. Fincos are neither special purpose vehicles (SPVs) nor investment funds. We propose to rate certain fincos under the NBFIs criteria when we believe their greatest risks relate to asset quality, funding and liquidity, and tangible capital--some of the primary risks banks face. We believe these companies are more likely to default because of problems relating to their balance sheets--rather than an inability to service their debt obligations with operating cash flows.

IMPACT ON OUTSTANDING RATINGS

We expect these criteria, if implemented as proposed, to result in rating changes. Our preliminary testing indicates that our ratings on more than half of approximately 130 NBFIs (securities firms and fincos) covered under these criteria would remain unchanged. We anticipate that about one-tenth would experience rating changes of two or more notches--evenly distributed between upgrades and downgrades--and the remainder, slightly more than one-third, would experience rating changes of one notch--distributed about evenly between upgrades and downgrades.

DETAILS

The proposed criteria are available on RatingsDirect, "Request For Comment: Nonbank Financial Institutions Rating Methodology," as well as on S&P.com at: http://www.standardandpoors.com/en_US/web/guest/ratings/ratings-criteria/-/articles/criteria/financial-institutions/filter/request-for-comment. Also see our related articles on securities firms and fincos, titled "Industry And Idiosyncratic Risks For Finance Companies Are Generally Higher Relative To Banks" and "Industry Risk For Securities Firms Is Generally Higher Than For Banks."

RESPONSE DEADLINE

We encourage interested market participants to submit their written comments on the proposed criteria by Sept. 24, 2014, to <http://www.standardandpoors.com/criteriaRFC/en/us> (you may need to log in or register first). We will review and take such comments into consideration before publishing our definitive criteria once the comment period is over. Generally, Standard & Poor's Ratings Services (Ratings Services) may, in cases when the commenter has not requested confidentiality, publish comments in their entirety, except when the full text, in our view, would be unsuitable for reasons of tone or substance.

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