

*Excerpts from the testimony of Alex J. Pollock to the Joint Economic Committee of the United States Congress, May 14, 2008.*

### Remove Government Support for Rating Agencies

The credit rating agencies say that they are in the business of publishing opinions about the future. In this I believe they are right, and I have a good deal of sympathy with the thought that in the course of financial events, some such opinions will prove to have been mistaken, even disastrously mistaken. So when it comes to opinions about the future, more opinions and competition is likely to uncover new insights into credit risks and new methods of analysis.

A particularly desirable form of increased competition would be from ratings agencies paid solely by investors, as opposed to those paid for by the issuers of securities, as many commentators have suggested.

But here is a larger question: Since all opinions are liable to error, and opinions based on models are liable to systemic error of vast proportions—as the subprime bust makes apparent—why should the U.S. government want to enshrine certain opinions as having preferred, preferential, indeed mandatory, status? It shouldn't.

I suggest that all regulatory requirements to use the ratings of certain preferred rating agencies be eliminated. Banks and other regulated investors should instead be responsible for developing their own prudent standards, which would probably entail the use of credit ratings as part of a credit management system—but without government sponsorship of the dominant firms.