Christopher Cox, S.E.C. chairman, said the commission was examining whether the credit agencies had acted impartially.

**Debt-Rating Agencies Are Under Scrutiny by S.E.C.**

By STEPHEN LABATON

WASHINGTON, Sept. 26 — The Securities and Exchange Commission has opened an investigation into whether the credit-rating agencies improperly inflated their ratings of mortgage-backed securities because of possible conflicts of interest, the head of the commission told Congress on Wednesday.

At a hearing before the Senate Banking Committee, the chairman, Christopher Cox, said the commission was examining whether the credit agencies had "compromised their impartiality" when they simultaneously marked up various mortgage-backed securities and provided advice to Wall Street investment firms about how to package them so as to gain higher credit ratings. The credit agencies also receive fees from the investment firms.

Mr. Cox said President Bush had instructed an interagency committee headed by Treasury Secretary Henry M. Paulson Jr. to examine the role of the rating agencies in lending practices by the mortgage industry.

Mr. Cox was the first witness in two days of Congressional hearings on the roles of the two major credit-rating agencies, Moody's Investors Service and Standard & Poor's, in the growing problems plaguing the subprime mortgage lending markets. In recent months, the agencies have quickly, though critics say belatedly, downgraded hundreds of mortgage-bond ratings.

With the explosive growth in the market for mortgage-backed securities, the ratings agencies have come to play a central role in the housing market. After a homeowner gets a mortgage, the lending institution usually sells the loan to a Wall Street firm, known as an underwriter, where it is repackaged with other loans and sold to investors as a mortgage-backed security. Rating agencies grade those securities to let investors know the chances of default.

As the subprime market has been rocked by a wave of mortgage defaults and worthless mortgage-backed securities, the rating agencies have come under renewed scrutiny by regulators and lawmakers.

After criticism of the credit agencies for their role in the corporate accounting scandals earlier in the decade, Congress adopted a law last year that gave the S.E.C. new authority to inspect and punish the agencies. But the new law also prevents the commission from regulating the procedures and methods the agencies use to determine ratings.

Although there is no expectation that Congress will rewrite the new law soon, executives from the rating agencies tried to defend themselves from an onslaught of criticism from Democrats and Republicans on the Banking Committee.

"It seems to me that credit rating agencies are playing both coach and referee," said Senator Robert Menendez, Democrat of New Jersey.

Senator Charles E. Schumer, Democrat of New York, dismissed the observation of one of the heads of a rating agency who had told him in a private meeting that the agencies had done nothing wrong. "To say nothing went wrong, that ain't going to fly," he said. "We need to find ways to prevent this crisis from happening again." He proposed that the system be changed so that investors, rather than underwriters, pay the credit agencies' fees.

Senator Richard C. Shelby of Alabama, the senior Republican on the committee, joined other lawmakers in complaining that
the credit agencies were being paid by the underwriters instead of investors. "It seems to me that money's trumping ethics," Mr. Shelby said.

But executives from the credit agencies said that while the agencies may have miscalculated the quantity of low-quality loans, their mistakes were unintentional and not the product of any conflicts of interest.

"We have learned hard lessons from the recent difficulties in the subprime mortgage area," said Vickie A. Tillman, an executive vice president at Standard & Poor's. "Some have questioned whether the 'issuer pays' model has led S.&P. and others to issue higher, or less rigorously analyzed, ratings so as to garner more business. There is no evidence — none at all — to support this contention with respect to S.&P."

Michael Kanef, head of the asset-backed finance rating group at Moody's Investors Service, said his company likewise had no conflicts of interest that led to inflated ratings. "The integrity and objectivity of our rating processes is of utmost importance to us," he said. "Our continued reputation for objective and independent ratings is essential to our role in the marketplace."