



Timing of DOJ Probe Into S&P Ratings Service Is Suspicious

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Did the U.S. Department of Justice decide to investigate Standard & Poor's investment rating service in retaliation for S&P's decision to strip the United States of its longstanding "AAA" rating?

The New York Times reported earlier this week about the existence of an ongoing probe of Standard & Poor's that is focusing on whether top managers there chose to overrule their subordinates during the mortgage crisis and to give inappropriately high ratings to dubious mortgage-backed securities such as collateralized debt obligations (CDOs).

Although S&P has often successfully invoked the First Amendment in response to previous investigations of its ratings, it might find that a difficult defense to raise in this DOJ investigation. The probe reportedly centers on conflict-of-interest issues. Currently, ratings agencies like S&P make money by charging fees to the companies that put together and sell the investments, not by charging investors. The concern is that S&P might have handed out high ratings to please their customers, thus leaving investors under the false impression that the mortgage-backed securities were sound.

According to the *Times*, the investigation is civil rather than criminal. Still, even a civil complaint against S&P could be very damaging to it and could permanently change the way that ratings agencies on Wall Street do business.

The timing of the inquiry is certainly suspicious. After the ratings downgrade earlier this month, top Obama administration economic officials expressed harsh criticism of S&P's methods, saying that the ratings agency had made a \$2 trillion mathematical error in its calculations. It makes a great deal of sense to draw the conclusion that the administration might now want to reduce the power of the ratings agencies and to subject them to public criticism.

Members of Congress, from both parties, are already investigating why S&P cut the rating when it did, and the DOJ investigation could be yet another effort to strike back at the agency.

On the other hand, the *Times* report notes that the investigation began in early summer, before the AAA rating was cut. Also, *Business Week* has reported that the inquiry also involves Moody's, a ratings service that competes with S&P but did not downgrade U.S. debt.

The DOJ is not commenting, of course, on the ongoing investigation. While no person or corporation should be exempt from government scrutiny, we think the government needs to come clean. If it has a legitimate case against Standard & Poor and its role in the mortgage crisis, it should explain that — soon.

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