

## I

(Resolutions, recommendations and opinions)

## OPINIONS

## EUROPEAN CENTRAL BANK

## OPINION OF THE EUROPEAN CENTRAL BANK

of 21 April 2009

on a proposal for a regulation of the European Parliament and of the Council on credit rating agencies

(CON/2009/38)

(2009/C 115/01)

**Introduction and legal basis**

1. On 17 December 2008 the European Central Bank (ECB) received a request from the Council of the European Union for an opinion on a proposal for a regulation of the European Parliament and of the Council on credit rating agencies <sup>(1)</sup> (hereinafter 'the proposed regulation') <sup>(2)</sup>.
2. The ECB's competence to deliver an opinion is based on Article 105(4) of the Treaty establishing the European Community. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

**General observations**

3. The ECB welcomes the objectives of the proposed regulation <sup>(3)</sup> and supports the agreement recently reached at the G20 meeting of finance ministers and central bank governors on 14 March 2009 <sup>(4)</sup> as part of the internationally coordinated initiatives to strengthen the regulatory framework for credit rating agencies. The ECB is of the view that regulatory initiatives concerning credit rating agencies should have the following objectives <sup>(5)</sup>. First, the level of transparency for the issuance of ratings and their ongoing monitoring should be improved to allow better comparison of credit rating agencies' rating assessments and promote greater competition in the credit rating industry. Second, the rating process should fulfil adequate standards of quality and integrity. In particular, from a financial stability perspective, it is of the utmost importance for the rating process not to lead to excessive volatility of ratings, which could result in a sharp re-pricing of assets and impair market confidence. Third,

<sup>(1)</sup> COM(2008) 704 final, 12 November 2008. Available at [www.eur-lex.europa.eu](http://www.eur-lex.europa.eu)

<sup>(2)</sup> This opinion is based on the version of 12 November 2008 on which the ECB was formally consulted. The proposed regulation has been subject to further amendments in the Council working group.

<sup>(3)</sup> The ECB notes that the proposed regulation is based on Article 95 of the Treaty and not on Article 47(2), which forms the legal basis for directives.

<sup>(4)</sup> See the Communiqué — Meeting of Finance Ministers and Central Bank Governors, United Kingdom, 14 March 2009. Available at [www.g20.org](http://www.g20.org)

<sup>(5)</sup> See the Eurosystem's contribution to the public consultation on the Commission's draft directive/regulation on credit rating agencies, September 2008 (hereinafter 'the Eurosystem's contribution'), available on the ECB's website at [www.ecb.europa.eu](http://www.ecb.europa.eu)

the integrity and independence of credit rating agencies should be safeguarded by ensuring that conflicts of interest are either avoided or are properly addressed within a transparent regulatory framework.

#### *Scope of the proposed regulation*

4. The proposed regulation is expected to apply to 'credit ratings that are intended for use for regulatory purposes or otherwise' by regulated financial sector institutions (credit institutions, investment firms; insurance, assurance and reinsurance undertakings; undertakings for collective investment in transferable securities (UCITS) and institutions for occupational retirement provision) and are disclosed publicly or distributed by subscription<sup>(6)</sup>. Moreover, these regulated institutions will only be allowed to use, for regulatory purposes, credit ratings which are issued by credit rating agencies established in the EU and registered in accordance with the proposed regulation<sup>(7)</sup>.

While the ECB supports the wide scope of the proposed regulation, it has the following observations.

First, the expression 'for use for regulatory purposes or otherwise' indicates a preference for a wide scope, but both the explanatory memorandum accompanying the proposed regulation and the Commission's impact assessment advocate a narrower approach, under which the proposed regulation would only cover credit ratings used for regulatory purposes<sup>(8)</sup>. The Commission argues that the proposed approach would be 'proportionate' since it 'targets not all credit rating agencies but only those whose ratings are used for regulatory purposes by financial institutions, i.e. those with a potentially high impact on the financial system'<sup>(9)</sup>. However, the proposed regulation alternates between, on the one hand, the objective of introducing 'a common approach to ensuring the high quality of credit ratings to be used in the Community'<sup>(10)</sup> and 'all ratings used by financial institutions governed by Community legislation are of high quality and issued by credit rating agencies subject to stringent requirements'<sup>(11)</sup> and, on the other hand, the more limited objective of requiring registration only for the credit rating agencies established in the Community and seeking to ensure that their credit ratings are used for regulatory purposes by financial institutions in the EU<sup>(12)</sup>. Furthermore, the proposed regulation does not clarify the rules applicable to securities for which a prospectus has been published under Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC<sup>(13)</sup> and which are rated under the proposed regulation.

Second, in its statement of scope, the proposed regulation defines 'regulatory purposes' mainly by reference to the most prominent example of recourse to credit ratings in financial regulation, i.e. Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions (recast)<sup>(14)</sup>, under which credit institutions are entitled to use the ratings as one of the references for the calculation of their capital requirements for solvency purposes<sup>(15)</sup>. The ECB understands that such an approach would cover credit ratings which have 'a potentially high impact on the financial system'<sup>(16)</sup>. In this respect, on 14 March 2009, the G20 finance ministers and central bank governors agreed

<sup>(6)</sup> Article 2(1) of the proposed regulation.

<sup>(7)</sup> Article 4, first paragraph, of the proposed regulation.

<sup>(8)</sup> The use of credit ratings for other than regulatory purposes is already provided for in the proposed regulation (see Article 4, second paragraph, of the proposed regulation).

<sup>(9)</sup> See paragraph 2.2 of the explanatory memorandum. This is confirmed in paragraph 5.2.4 of the Commission Staff Working document accompanying the proposed regulation (Impact assessment), SEC(2008) 2745, 12 November 2008, available on the Commission's website at [www.ec.europa.eu](http://www.ec.europa.eu)

<sup>(10)</sup> Article 1. Recital 28, second sentence, of the proposed regulation refers to the requirement that competent authorities should have the necessary means to ensure that 'ratings for use within the Community are issued in compliance' with the proposed regulation.

<sup>(11)</sup> See recital 2 as well as recitals 6 and 38 of the proposed regulation.

<sup>(12)</sup> See Article 12(1) and recital 21 of the proposed regulation.

<sup>(13)</sup> OJ L 345, 31.12.2003, p. 64.

<sup>(14)</sup> OJ L 177, 30.6.2006, p. 1.

<sup>(15)</sup> See paragraph 1.1 of the impact assessment and recital 1 of the proposed regulation.

<sup>(16)</sup> See paragraph 2.2 of the explanatory memorandum.

on regulatory oversight, including registration of all credit rating agencies whose ratings are used for regulatory purposes<sup>(17)</sup>. However, as 'regulatory purposes' is not specifically defined, and as it is not specified whether it covers references to recourse to ratings in Community legislation (as implemented in national legislation) and in national laws, the ECB suggests that further clarification is needed. Finally, some provisions of the proposed regulation, such as the general obligation for credit rating agencies to disclose 'any credit rating'<sup>(18)</sup>, might conflict with the scope of the proposed regulation if it were limited to credit ratings used for regulatory purposes.

Third, the proposed regulation only applies to credit ratings that are distributed by subscription or disclosed publicly. Consistently with the rules applicable to External Credit Assessment Institutions (ECAIs) in Directive 2006/48/EC<sup>(19)</sup>, it is suggested clarifying that credit ratings are considered as publicly disclosed if they enable access at equivalent terms to potential users and allow for proper assessment by the public.

Fourth, credit ratings should be based on methodologies combining qualitative and quantitative approaches<sup>(20)</sup>. It is noted in this respect that the rating tools operated by third-party providers<sup>(21)</sup> are usually solely based on quantitative approaches and do not take into account qualitative information such as the information obtained through contacts with the assessed entities senior management and operational staff. In the context of the policy framework for monetary policy operations of the Eurosystem (which comprises the ECB and the national central banks of Member States that have adopted the euro (NCBs)), this type of credit assessment system is treated distinctly from the other sources of credit assessment such as ECAIs. Therefore, it should be considered whether the proposed regulation should specify that ratings produced by third-party providers operating rating tools do not fall within its scope.

### Specific observations

#### *Impact of the proposed regulation on central bank operations*

5. The ECB is directly concerned with the services that credit rating agencies provide in the context of the tasks and obligations of the Eurosystem with regard both to the conduct of monetary policy operations and to other central bank operations such as the management of foreign reserves and own funds management operations<sup>(22)</sup>. Article 18.1, second indent of the Statute of the European System of Central Banks and of the European Central Bank (hereinafter the 'Statute of the ESCB') provides that the ECB and NCBs may conduct credit operations with credit institutions and other market participants, with lending based on adequate collateral. An important eligibility criterion, for the purpose of monetary policy operations, is that assets must meet high credit standards and for this purpose the Eurosystem credit assessment framework (ECAAF) defines the procedures, rules and techniques ensuring that the Eurosystem requirement of high credit standards is met. In assessing the credit standard of eligible assets, the Eurosystem takes into account credit assessment information from credit assessment systems belonging to one of four sources: ECAIs, NCBs in-house credit assessment systems (ICASs)<sup>(23)</sup>, counterparties' internal ratings-based systems or third-party providers' rating tools<sup>(24)</sup>. The Eurosystem reserves the right to determine whether an issue, issuer, debtor or guarantor fulfils its requirements

<sup>(17)</sup> See footnote 4 of this opinion.

<sup>(18)</sup> Article 8(1) of the proposed regulation.

<sup>(19)</sup> Annex VI, Part 2.

<sup>(20)</sup> See in this respect Directive 2006/48/EC (Annex VI, Part 2) which provides that competent authorities should consider both qualitative and quantitative factors to differentiate between the relative degrees of risk expressed by each credit assessment.

<sup>(21)</sup> See paragraph 5 of this opinion and paragraph 6.3.1 of Annex I to Guideline ECB/2000/7 of 31 August 2000 on monetary policy instruments and procedures of the Eurosystem (OJ L 310, 11.12.2000, p. 1) (see the unofficial consolidated text produced by the Office for Official Publications of the European Communities available on the ECB's website at [www.ecb.europa.eu](http://www.ecb.europa.eu)).

<sup>(22)</sup> See the Eurosystem's contribution, p. 2.

<sup>(23)</sup> For ICASs, see also paragraphs 6 and 7 of this opinion.

<sup>(24)</sup> See Section 6.3.1 of Annex I to Guideline ECB/2000/7.

for high credit standards on the basis of any information it may consider relevant and may reject assets on such grounds. To ensure the consistency, accuracy and comparability of the four credit assessment sources used in the ECAF, the Eurosystem has devised acceptance criteria for each of the sources used and regularly monitors their credit assessment performance against the Eurosystem's benchmark for high credit standards <sup>(25)</sup>.

In this context, the ECB recommends clarifying in a recital that the provisions of the proposed regulation applicable to credit rating agencies are without prejudice to the right of the Eurosystem or the rights of national central banks of Member States that have not adopted the euro, under their national legislation to define the procedures, rules and criteria ensuring that the requirement of high credit standards for assets eligible for monetary policy operations is met and to determine, as appropriate, the conditions for the use of credit ratings in central bank operations.

#### *Exemptions for NCBs' in-house credit assessment systems*

6. The proposed regulation does not apply to credit ratings issued by public bodies whose credit ratings are not publicly disclosed and are not paid for by the rated entity <sup>(26)</sup>. As mentioned above <sup>(27)</sup>, when assessing credit standards of eligible assets, the Eurosystem takes into account credit assessments derived from different sources, including ICASs operated by some NCBs. These ICASs are important for the implementation of the Eurosystem's monetary policy. For instance, credit claims constitute a substantial source of the assets accepted as collateral by the Eurosystem and the debtors of these debt obligations are often medium-sized companies which are only rated by these ICASs <sup>(28)</sup>. The ECB considers that it would not be proportionate to subject these ICASs to the registration procedure provided for under the proposed regulation. Moreover, it would not be relevant or appropriate to apply some of the provisions of the proposed regulation to credit ratings issued by NCBs. In the case of ICASs, their credit ratings are (i) not publicly disclosed and (ii) not paid for by the rated entity. The ECB therefore sees merit in extending the above exemption from the proposed regulation to credit ratings produced by national central banks and it suggests amending the proposed regulation accordingly.
  
7. The ECB agrees that these systems should benefit from an exemption from the proposed regulation where they operate according to conditions which are equivalent to the requirements in the proposed regulation and which ensure the adequate integrity and independence of credit rating activities. In the context of the Eurosystem monetary policy framework for market operations, these systems are already subject to in-depth validation and comprehensive performance monitoring by the Eurosystem which may suspend or exclude them in circumstances it defines <sup>(29)</sup>. Therefore, the ECB is of the view that the above condition should be considered as being automatically met when an ICAS is validated by the ECB for the purpose of Eurosystem monetary policy operations. As regards credit ratings issued by national central banks which comply with the two above criteria, but where the ECB has not assessed the ICAS in question, a procedure should be introduced to check the compliance of the ICAS with the 'equivalence' criterion. The ECB suggests that, in such cases, the national central banks could ask the Commission for an exemption and, to ensure the uniform application of the above criteria, the Commission should consult the ECB before deciding on the exemption to benefit from the ECB's expertise in this area. The ECB suggests amending the proposed regulation and including a corresponding recital to reflect this procedure.

#### *Supervision and registration of credit rating agencies and recognition of ECAIs*

8. Directive 2006/48/EC allows credit institutions to use external credit assessments provided by ECAIs in determining risk weights under the standardised approach <sup>(30)</sup> and under the ratings-based method

<sup>(25)</sup> See Section 6.3.1 of Annex I to Guideline ECB/2000/7.

<sup>(26)</sup> Article 2(2) of the proposed regulation.

<sup>(27)</sup> See paragraph 5 of this opinion.

<sup>(28)</sup> See 'The single list in the collateral framework of the Eurosystem', ECB Monthly Bulletin, May 2006, pp. 75-87 and the Eurosystem's contribution, p. 9.

<sup>(29)</sup> See Section 6.3.4 of Annex I to Guideline ECB/2000/7.

<sup>(30)</sup> Articles 78 to 83 and Annex VI.

for securitisation<sup>(31)</sup>. The interaction between the regime for credit rating agencies under the proposed regulation and the established process for recognising ECAIs under Directive 2006/48/EC could be an issue of concern and should be appropriately addressed. In particular, it should be clarified that the registration of a credit rating agency under the proposed regulation constitutes a condition for eligibility as an ECAI under Directive 2006/48/EC. Furthermore, appropriate amendments to Directive 2006/48/EC should be introduced, as suggested in the Eurosystem contribution<sup>(32)</sup>, with a view to avoiding 'the duplication of procedures and costly overlapping requirements' and ensuring legal consistency. For instance, the requirements of objectivity, independence, ongoing review, transparency and disclosure related to the methodology for assigning credit assessments<sup>(33)</sup> should already be considered as fulfilled by credit rating agencies registered under the proposed regulation.

9. The proposed regulation provides that each Member State must designate a competent authority for the purposes of the regulation<sup>(34)</sup>. Under Directive 2006/48/EC, national banking supervisory authorities retain the authority to recognise credit rating agencies as ECAIs in accordance with the requirements laid down by the Directive<sup>(35)</sup>. If, as suggested in the de Larosière Group Report<sup>(36)</sup>, the Committee of European Securities Regulators (CESR) or the authorities designated by the proposed regulation assume responsibility for the registration and oversight of credit rating agencies, they should consult the relevant banking supervisory authorities about registration and supervision as well as the possible application of sanctions. When reviewing Directive 2006/48/EC the Community legislator could assess whether, based on experience with the regime for ECAIs<sup>(37)</sup>, the mechanisms for recognition of these institutions need to be further simplified, taking into account possible synergies with the registration and surveillance framework for credit rating agencies in the proposed regulation.

#### *Cooperation between competent authorities and the exchange of information*

10. The proposed regulation lays down a framework for the registration and surveillance of credit rating activities based on close coordination between the national authorities. The ECB observes that CESR's role is limited to providing advice to the competent authority of the home Member State (i) regarding draft registration decisions or draft refusal decisions<sup>(38)</sup> and (ii) in the cases provided for in the proposed regulation<sup>(39)</sup> or if the authorities intend to take supervisory measures<sup>(40)</sup>. In this respect, the ECB notes the concerns expressed in the de Larosière Group Report that 'the system of licensing and oversight contained in this proposal is too cumbersome' and 'The allocation of work between the home and host authorities, in particular, is likely to lack effectiveness and efficiency'<sup>(41)</sup>. Moreover, the de Larosière Group Report proposes giving responsibility for the licensing and direct supervision of EU-wide institutions, such as credit rating agencies, to the EU authority into which CESR will be transformed. While the Eurosystem has already expressed its support for CESR to play a coordinating role<sup>(42)</sup>, the role of CESR in relation to credit rating agencies may need to be further reviewed in the light of the forthcoming implementation of the de Larosière Group's recommendations<sup>(43)</sup>.

<sup>(31)</sup> Articles 94 to 101 and Annex IX.

<sup>(32)</sup> See p. 5.

<sup>(33)</sup> See in particular Articles 81 and 97 as well as Annex VI, Part 2, of Directive 2006/48/EC.

<sup>(34)</sup> Article 19(1).

<sup>(35)</sup> Under Article 81, an ECAI which provides the external credit assessment may be recognised by the competent authorities as eligible for the purpose of determining the risk weighting of an exposure. If an ECAI has been recognised as eligible by the competent authorities of a Member State, the competent authorities of other Member States may decide to recognise that ECAI as eligible without carrying out their own evaluation.

<sup>(36)</sup> See the Report of 25 February 2009 of the High Level Group chaired by Jacques de Larosière on financial supervision in the EU (hereinafter the 'de Larosière Group Report'), paragraph 67 (available at [www.europa.eu](http://www.europa.eu)).

<sup>(37)</sup> See the Committee of European Banking Supervisors (CEBS) Guidelines of 20 January 2006 on the recognition of External Credit Assessment Institutions (available on the CEBS' website at [www.c-eps.org](http://www.c-eps.org)).

<sup>(38)</sup> See Article 15 of the proposed regulation.

<sup>(39)</sup> See Article 18 of the proposed regulation.

<sup>(40)</sup> See Articles 21 and 22 of the proposed regulation.

<sup>(41)</sup> See de Larosière Group Report, paragraph 67.

<sup>(42)</sup> See the Eurosystem's contribution, p. 5.

<sup>(43)</sup> The de Larosière Group Report suggests that 'the task of licensing CRAs in the EU, monitoring their performance, and in the light of this imposing changes' should be entrusted to CESR, paragraph 67.

11. The ECB stresses that any coordinating arrangement established for the regulation and supervision of credit rating agencies should be designed to allow for an appropriate level of involvement by the Eurosystem, given its keen interest in the implementation of central bank operations and from a financial stability perspective. In this respect, it suggests introducing gateways in the proposed regulation, similar to those inserted in the Community framework for the exchange of information between the competent authorities and the central banks of the ESCB<sup>(44)</sup>. The ECB therefore proposes an amendment in line with its recommendation in Opinion CON/2009/17<sup>(45)</sup>. Moreover, the ECB would welcome the introduction of the mandatory consultation of the CEBS, as well as the Committee of European Insurance and Occupational Pensions Supervisors, prior to the publication of guidance for national competent authorities<sup>(46)</sup>.

*Waivers for local credit rating agencies*

12. The Eurosystem's contribution noted that an alternative and less stringent treatment for local rating agencies, which mainly deal with corporate issuances, may be considered in the proposed regulation and that waiving some requirements for local agencies could allow flexibility and help maintain diversity in the population of credit rating agencies, ensuring a diversity of opinions<sup>(47)</sup>. If such exemption were considered for smaller credit rating agencies in the context of the co-decision procedure, it would be necessary to ensure that larger credit rating agencies could not exploit such an exemption by slicing up their business. The ECB would also support an assessment of the impact of the application of the proposed regulation on the level of concentration in the credit rating market<sup>(48)</sup>.

*Establishment by CESR of a central repository*

13. The proposed regulation provides that credit rating agencies must make available in a central repository established by CESR information 'on their historical performance data and information about past credit rating activities'<sup>(49)</sup>. The ECB stands ready to assist the Commission and CESR in creating this repository which will be relevant to the performance by the ESCB of its activities. A balance should be found between the level of information required to meet the needs of users and the compliance costs for credit rating agencies.

The ECB also makes the following recommendations. First, for the sake of clarity it might be appropriate to distinguish in two separate articles of the proposed regulation: (i) the provisions concerning disclosure requirements applicable to credit rating agencies, and (ii) those relating to the establishment by CESR of a central repository and the nature of the data and information to be contained in this repository. Second, it is desirable to further clarify the types of data and information which will be made available in the repository. The ECB understands that this information will include 'data about the historical default rates of its rating categories'<sup>(50)</sup>. Third, the collection of this information by CESR, its storage conditions, the arrangements for the management of the repository and access to it and any possible changes to the requirements applicable to this repository and to credit rating agencies in the future should be further examined. This might require introducing more detailed provisions or extending recourse to comitology in the proposed regulation to allow the adoption of

<sup>(44)</sup> See the Commission's proposal for a Directive of the European Parliament and of the Council amending Directives 2006/48/EC and 2006/49/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management (COM(2008) 602 final), 1 October 2008. Available at [www.eur-lex.europa.eu](http://www.eur-lex.europa.eu)

<sup>(45)</sup> ECB Opinion CON/2009/17 of 5 March 2009 at the request of the Council of the European Union on a proposal for a Directive of the European Parliament and of the Council amending Directives 2006/48/EC and 2006/49/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management. See paragraphs 13 and 14 of the opinion and the proposed amendment 5.

<sup>(46)</sup> See Article 18 of the proposed regulation.

<sup>(47)</sup> See the Eurosystem's contribution, p. 4.

<sup>(48)</sup> This would require an amendment to Article 34 of the proposed regulation.

<sup>(49)</sup> See Article 9(2) of the proposed regulation.

<sup>(50)</sup> Under the proposed regulation, credit rating agencies must disclose these data every six months and whether the default rates of these categories have changed over time (Annex I, Section E, Part II, point 1 of the proposed regulation).

technical measures specifying the principles applicable to the repository's organisation and functioning. CESR should also examine possible synergies with other initiatives. Fourth, the repository should ensure that 'relevant, standardised data on credit rating agencies' performance is available to allow market participants to make industry-wide comparisons'<sup>(51)</sup>. The ECB recommends mandating CESR to produce statistics monitoring the historical performance of credit ratings and to publish its findings periodically. The ECB also suggests structuring and storing the above data in a comparable format identifying securities and their ratings, at an instrument and issuer level, on the basis of the International Securities Identification Number for issues and a standardised identifier for issuers. Furthermore, it is necessary to ensure that investors are better able to assess the credit risks of their portfolios, i.e. investors should be enabled to draw their own conclusions on statistical interdependencies, such as correlations, between categories of credit ratings in relation to the various types of rated entities or instruments.

*Additional legal and technical comments*

14. In the proposed regulation, a rating category is defined as 'a rating symbol used for identifying different credit ratings for each class of credit ratings in order to distinguish the different risk characteristics of the different types of rated entities, issuers and financial instruments'<sup>(52)</sup>. Moreover, the proposed regulation provides that a credit rating agency must provide the 'class of credit ratings for which the credit rating agency is applying to be registered'<sup>(53)</sup>. These provisions could be further simplified as suggested in the Annex to this opinion.
  
15. The proposed regulation provides that a credit rating agency must monitor credit ratings and review them 'where necessary'<sup>(54)</sup>. The specification of a minimum frequency for reviewing credit ratings would reinforce the commitment and obligation of credit rating agencies to regularly and actively monitor all ratings they have issued. The ECB therefore recommends such a review at least annually. The proposed regulation also provides that, following changes in ratings methodologies, credit rating agencies must 're-rate all credit ratings that have been based on those methodologies, models or assumptions'<sup>(55)</sup>. The ECB suggests clarifying that this requirement only applies to credit ratings still in use.
  
16. Independent non-executive members of the administrative or supervisory board play a crucial role in credit ratings' independence and quality. The proposed regulation provides that these non-executive members should have the specific tasks of ensuring that there are no conflicts of interest and of monitoring the compliance and governance processes, including the review function<sup>(56)</sup>. The review function consists in periodically reviewing the methodologies and models that the credit rating agency uses and significant changes to the methodologies as well as their appropriateness for the assessment of new financial instruments<sup>(57)</sup>. In view of the importance of these tasks, the ECB recommends that applications for registration should also include information on the independent non-executive members of the administrative or supervisory board<sup>(58)</sup>.
  
17. The proposed regulation requires credit rating agencies to retain records which set out the respective rights and obligations of the credit rating agency and the rated entity 'for at least the duration of the relationship with that rated entity'<sup>(59)</sup>. The ECB recommends maintaining this obligation for at least two years after the end of the relationship, to allow for *ex post* examination when required by the competent authorities<sup>(60)</sup>.

<sup>(51)</sup> Paragraph 2.5.4 of the explanatory memorandum.

<sup>(52)</sup> See Article 3(1)(f). See also recital 24, last sentence, of the proposed regulation and the reference to 'a subcommittee specialised in the field of credit ratings of each of the asset classes rated by credit rating agencies'.

<sup>(53)</sup> See Annex II, point 4, of the proposed regulation.

<sup>(54)</sup> See Article 7(4).

<sup>(55)</sup> See Article 7(5)(c).

<sup>(56)</sup> See Annex I, Section A, point 2, fifth sub-paragraph.

<sup>(57)</sup> See Annex I, Section A, point 7, first sub-paragraph of the proposed regulation.

<sup>(58)</sup> See Annex II of the proposed regulation.

<sup>(59)</sup> See Annex I, Section B, point 9.

<sup>(60)</sup> Compare with Annex I, Section B, point 8 of the proposed regulation.

18. Further assessment should be made as to whether the rules in the proposed regulation preventing employees directly involved in the credit rating process from joining rated entities are sufficiently strict to prevent or limit these practices. It is therefore suggested that employees directly involved in the credit rating process should not take up a key management position with the rated entity before 18 (instead of six) months have lapsed since the credit rating was issued <sup>(61)</sup>.
19. The reference to 'debt issue' should be replaced by 'financial instrument' <sup>(62)</sup>.
20. In its transparency report, a credit rating agency must make annually available financial information on its revenue, divided into fees from credit rating and non credit rating services with a comprehensive description of each <sup>(63)</sup>. To the extent these 'non credit rating services' constitute 'ancillary services', this should be reflected in the proposed regulation <sup>(64)</sup>.

### **Drafting proposals**

Where the above advice would lead to changes in the proposed regulation, drafting proposals are set out in the Annex.

Done at Frankfurt am Main, 21 April 2009.

*The President of the ECB*  
Jean-Claude TRICHET

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<sup>(61)</sup> See Annex I, Section C, points 6 and 7 of the proposed regulation.

<sup>(62)</sup> See Annex I, Section E, Part II, point 2, last sub-paragraph.

<sup>(63)</sup> See Annex I, Section E, Part III, point 7 of the proposed regulation.

<sup>(64)</sup> See Annex I, Section B, point 4.



## ANNEX

## Drafting proposals

Text proposed by the Commission (1)	Amendments proposed by the ECB (2)
<b>Amendment 1</b>	
New recital 2a	
‘No current text’	‘This Regulation should in no way affect the right of the European Central Bank (ECB) and the national central banks of Member States that have adopted the euro (hereinafter the ‘Eurosystem’) or the rights of the national central banks of Member States that have not adopted the euro, under their national legislation, to define the procedures, rules and criteria which ensure that the requirement of high credit standards for assets eligible for monetary policy operations is met and to determine, as appropriate, the conditions for the use of credit ratings in the context of central bank operations.’
<i>Justification — See paragraph 5 of the opinion</i>	
<b>Amendment 2</b>	
New recital 2b	
‘No current text’	‘In-house credit assessment systems of national central banks of the ESCB may be exempted from the application of this Regulation provided that credit ratings produced by these systems comply with the criteria provided for in this Regulation. The validation of these systems by the ECB for the purposes of Eurosystem monetary policy operations should constitute a guarantee that they fulfil conditions equivalent to the requirements provided for by this Regulation and which ensure the independence and integrity of their credit rating activities. In other cases, an exemption should be requested from the Commission by national central banks of the ESCB. The Commission’s Decision should be taken after consultation of the ECB to ensure uniform application of the exemption criteria.’
<i>Justification — See paragraphs 6 and 7 of the opinion</i>	
<b>Amendment 3</b>	
Article 2	
‘2. This Regulation shall not apply to private credit ratings. It shall not apply to credit ratings issued by public bodies whose credit ratings are not publicly disclosed and not paid by the rated entity.’	‘2. This Regulation shall not apply to <b>either</b> :  (a) private credit ratings. <del>It shall not apply to credit ratings issued by public bodies whose credit ratings are not publicly disclosed and not paid by the rated entity.</del> <b>produced on an individual order and provided exclusively to the person that ordered them and which are not intended for public disclosure or distribution by subscription; or</b>

Text proposed by the Commission <sup>(1)</sup>	Amendments proposed by the ECB <sup>(2)</sup>
	<p>(b) credit ratings issued by central banks and which meet all of the following conditions:</p> <ul style="list-style-type: none"> <li>(i) are not paid by the rated entity;</li> <li>(ii) are not disclosed to the public;</li> <li>(iii) are issued according to conditions equivalent to the requirements provided for by this Regulation and which ensure the adequate integrity and independence of credit rating activities; this shall be deemed to be the case where the credit ratings are produced by a national central bank's in-house credit assessment system validated by the ECB for the purpose of Eurosystem monetary policy operations, and listed on the ECB's website.</li> </ul> <p>3. A national central bank of the ESCB which issues a credit rating complying with the criteria set out in paragraph 2(b) but for which the in-house credit assessment system has not been validated by the ECB shall request an exemption from the application of this Regulation from the Commission. To ensure the uniform application of paragraph 2(b), the Commission shall consult the ECB before taking such decision.</p> <p>The Commission shall publish on its website the list of central banks benefiting from the exemption.</p> <p>4. A credit rating agency wishing to be recognised as eligible as an External Credit Assessment Institution within the meaning of Directive 2006/48/EC must be registered as a credit rating agency under this Regulation, unless it only issues credit ratings of the kind referred to in paragraph 2.</p> <p>5. For the purposes of paragraphs 1 and 2, credit ratings shall be considered as publicly disclosed if they enable access at equivalent terms to potential users and allow for a proper assessment by the public.'</p>

*Justification — See paragraphs 4, 6, 7 and 8 of the opinion*

#### Amendment 4

Article 3(1)

<p>'(f) "rating category" means a rating symbol used for identifying different credit ratings for each class of credit ratings in order to distinguish the different risk characteristics of the different types of rated entities, issuers and financial instruments;'</p>	<p>'(f) "rating category" means <del>a rating symbol</del> an <b>indicator</b> used for <b>measuring, within a ranking system defined by the credit rating agency and for each type of rated entity, issuer or instrument, identifying different credit ratings for each class of credit ratings in order to distinguish the different risk characteristics of the different types of rated entities, issuers and financial instruments; the credit rating corresponding to the relative risk characteristics of the rated entity, issuer or instrument and represented by symbols, numbers or other designations;</b>'</p>
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*Justification — See paragraph 14 of the opinion*

#### Amendment 5

Article 7

<p>'Rating methodologies</p> <p>1. A credit rating agency shall disclose to the public the methodologies, models and key rating assumptions it uses in the rating process.</p>	<p>'Rating methodologies</p> <p>1. A credit rating agency shall disclose to the public the methodologies, models and key rating assumptions it uses in the rating process, <b>and the qualitative and quantitative factors on which the credit rating agency's methodologies are based.</b></p>
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Text proposed by the Commission (1)	Amendments proposed by the ECB (2)
<p>...</p> <p>4. A credit rating agency shall monitor credit ratings and review its credit ratings where necessary. A credit rating agency shall establish internal arrangements to monitor the impact of changes in macroeconomic or financial market conditions on credit ratings.</p> <p>5. When rating methodologies, models or key ratings assumptions are changed a credit rating agency shall:</p> <p>...</p> <p>(c) re-rate all credit ratings that have been based on those methodologies, models or assumptions.'</p>	<p>...</p> <p>4. A credit rating agency shall monitor credit ratings and review its credit ratings where necessary. <b>Such a review shall be made at least annually.</b> A credit rating agency shall establish internal arrangements to monitor the impact of changes in macroeconomic or financial market conditions on credit ratings.</p> <p>5. When rating methodologies, models or key ratings assumptions are changed a credit rating agency shall:</p> <p>...</p> <p>(c) re-rate <del>all</del> credit ratings <b>in use</b> that have been based on those methodologies, models or assumptions.'</p>

*Justification — See paragraphs 4 and 15 of the opinion*

#### **Amendment 6**

Article 9(2)

<p>'2. Credit rating agencies shall make available in central repository established by CESR information on their historical performance data and information about past credit rating activities. The repository shall be open to the public.'</p>	<p><del>'2. Credit rating agencies shall make available in central repository established by CESR information on their historical performance data and information about past credit rating activities. The repository shall be open to the public.'</del></p>
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*Justification — See paragraph 13 of the opinion*

#### **Amendment 7**

New Article 9a

<p>'No current text'</p>	<p><b>'CESR Central repository</b></p> <p><b>1. Credit rating agencies shall make available in the central repository established by CESR information on their historical performance data (including data about the historical default rates of rating categories) and information on past credit rating activities.</b></p> <p><b>2. The repository shall be open to the public.</b></p> <p><b>3. To ensure the uniform application of paragraphs 1 and 2, the Commission shall adopt implementing measures in accordance with the procedure defined in Article 33(3).</b></p> <p><b>The Commission shall in particular specify:</b></p> <ul style="list-style-type: none"> <li>— <b>the type of data and information which shall be made available in the central repository,</b></li> <li>— <b>the periods covered by such historical performance data and information,</b></li> <li>— <b>the time limits within which such information shall be made available,</b></li> <li>— <b>the conditions under which such data and information shall be stored,</b></li> </ul>
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Text proposed by the Commission <sup>(1)</sup>	Amendments proposed by the ECB <sup>(2)</sup>
	<ul style="list-style-type: none"> <li>— the format under which such data and information shall be communicated and presented,</li> <li>— the arrangements for the management of the repository,</li> <li>— the conditions for access to the facility.</li> </ul> <p>4. On the basis of the information contained in the central repository, CESR shall produce statistics for monitoring the historical performance of credit ratings agencies. The statistics produced by CESR shall be published periodically.</p> <p>5. CESR shall take into account possible synergies with other relevant initiatives.'</p>

*Justification — See paragraph 13 of the opinion*

#### **Amendment 8**

Article 18(2)

'2. By (within one year after entry into force of this Regulation) CESR shall issue guidance on:'	'2. By (within one year after entry into force of this Regulation) <b>and after consulting the Committee of European Banking Supervisors and the Committee of European Insurance and Occupational Pensions Supervisors,</b> CESR shall issue guidance on:'
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*Justification — See paragraph 11 of the opinion*

#### **Amendment 9**

New Article 23a

'No current text'	<p><b>'Exchange of information</b></p> <p>1. The competent authorities shall, without undue delay, provide each other with any information which is required for the purposes of carrying out their duties under this Regulation.</p> <p>2. The competent authorities may transmit information including information of a confidential nature to the competent authorities responsible for the supervision of institutions referred to in Article 2(1) and to central banks of the ESCB when this information is relevant for the exercise of their respective tasks, including the conduct of monetary policy, the oversight of payments, clearing and securities settlement systems, and safeguarding financial stability; likewise such authorities or central banks shall not be prevented from communicating to the competent authorities relevant information as may be needed for the performance of their functions provided for in this Regulation.'</p>
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*Justification — See paragraph 11 of the opinion*

Text proposed by the Commission (1)	Amendments proposed by the ECB (2)
<b>Amendment 10</b>	
New Article 33(3)	
‘No current text’	‘ <b>3. Where reference is made to this paragraph, Articles 5 and 7 of Decision 1999/468/EC shall apply, having regard to the provisions of Article 8 thereof, provided that the implementing measures adopted in accordance with that procedure do not modify the essential provisions of this Regulation.</b> ’
<i>Justification — See paragraph 13 of the opinion</i>	
<b>Amendment 11</b>	
Annex I, Section B, point 9	
‘9. Records which set out the respective rights and obligations of the credit rating agency and the rated entity or its related third parties under an agreement to provide services shall be retained for at least the duration of the relationship with that rated entity or its related third parties.’	‘9. Records which set out the respective rights and obligations of the credit rating agency and the rated entity or its related third parties under an agreement to provide services shall be retained for at least <del>the duration</del> <b>two years after the expiry</b> of the relationship with that rated entity or its related third parties.’
<i>Justification — See paragraph 17 of the opinion</i>	
<b>Amendment 12</b>	
Annex I, Section C, point 7	
‘7. Employees directly involved in the credit rating process shall not take up a key management position with the rated entity or its related third party before 6 months have lapsed since the credit rating.’	‘7. Employees directly involved in the credit rating process shall not take up a key management position with the rated entity or its related third party before <del>6</del> <b>18</b> months have lapsed since the credit rating.’
<i>Justification — See paragraph 18 of the opinion</i>	
<b>Amendment 13</b>	
Annex I, Section E, Part II, point 2	
‘...  For the purposes of the first subparagraph of point 2 “client” shall mean a company, its subsidiaries, and associated companies in which the company has holdings of more than 20 %, as well as any other entities in respect of which it has negotiated the structuring of a debt issue on behalf of a client and where a fee was paid, directly or indirectly, to the credit rating agency for the rating of that debt issue.’	‘...  For the purposes of the first subparagraph of point 2 “client” shall mean a company, its subsidiaries, and associated companies in which the company has holdings of more than 20 %, as well as any other entities in respect of which it has negotiated the structuring of a <del>debt issue</del> <b>financial instrument</b> on behalf of a client and where a fee was paid, directly or indirectly, to the credit rating agency for the rating of that <b>financial instrument</b> <del>debt issue</del> .’
<i>Justification — See paragraph 19 of the opinion</i>	

Text proposed by the Commission <sup>(1)</sup>	Amendments proposed by the ECB <sup>(2)</sup>
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**Amendment 14**

Annex II

'4. class of credit ratings for which the credit rating agency is applying to be registered;	'4. <del>class type</del> of credit ratings for which the credit rating agency is applying to be registered;
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*Justification — See paragraph 14 of the opinion*

**Amendment 15**

Annex II, new point 7a

'No current text'	<b>'Information on the independent non-executive members of the administrative or supervisory board;'</b>
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*Justification — See paragraph 16 of the opinion*

<sup>(1)</sup> Strikethrough in the body of the text indicates where the ECB proposes deleting text.

<sup>(2)</sup> Bold in the body of the text indicates where the ECB proposes inserting new text.