

Credit rating agencies

2008/0217(COD) - 16/09/2009 - Final act

PURPOSE: to regulate of the Credit Rating Agencies.

LEGISLATIVE ACT: Regulation (EC) No 1060/2009 of the European Parliament and of the Council on credit rating agencies.

CONTENT: following a first reading agreement with the European Parliament, the Council adopted this Regulation introducing a legal framework for credit rating agencies. The Regulation is aimed at ensuring that credit ratings used in the EU for regulatory purposes are of the highest quality, and issued by agencies that are subject to stringent requirements. It comes in response to calls from both the European Council and the G-20. This Regulation is part of a package

The Council also adopted:

- [a directive updating capital requirements for banks](#)
- [a regulation on cross-border payments](#)
- [a directive on electronic money](#)
- [a decision](#) establishing Community programme to support activities in the field of financial services, financial reporting and auditing

which constitute a significant part of the work programme it launched in response to the financial crisis.

Credit rating agencies play an important role in securities and banking markets, as their ratings are used by investors, borrowers, issuers and governments in taking decisions on investment and financing. They are however considered to have failed to reflect early enough in their ratings the worsening of market conditions in the run-up to the financial crisis. Credit rating agencies are considered to have failed, first, to reflect early enough in their credit ratings the worsening market conditions, and second, to adjust their credit ratings in time following the deepening market crisis. The most appropriate manner in which to correct those failures is by measures relating to conflicts of interest, the quality of the credit ratings, the transparency and internal governance of the credit rating agencies, and the surveillance of the activities of the credit rating agencies. The users of credit ratings should not rely blindly on credit ratings but should take utmost care to perform own analysis and conduct appropriate due diligence at all times regarding their reliance on such credit ratings.

The Regulation is aimed at ensuring that credit ratings used in the EU for regulatory purposes are of the highest quality, and issued by agencies that are subject to stringent requirements. Currently, credit rating agencies are only to a limited extent subject to EU legislation and most Member States do not regulate their activities, although their ratings are used by financial institutions which themselves are subject to EU rules. The agencies, most of which have their headquarters outside the EU, may however apply a voluntary code of conduct issued by the International Organisation of Securities Commissions.

This Regulation introduces a **common regulatory approach** in order to enhance the integrity, transparency, responsibility, good governance and reliability of credit rating activities, contributing to the quality of credit ratings issued in the Community, thereby contributing to the smooth functioning of the internal market while achieving a high level of consumer and investor protection. It lays down conditions

for the issuing of credit ratings and rules on the organisation and conduct of credit rating agencies to promote their independence and the avoidance of conflicts of interest.

It is also aimed at:

- ensuring that credit rating agencies avoid conflicts of interest in the rating process, or at least manage them adequately;
- improving the quality of methodologies used by credit rating agencies and the quality of their ratings;
- increasing transparency by setting disclosure obligations for credit rating agencies;
- ensuring an efficient registration and surveillance framework, avoiding ‘forum shopping’ and regulatory arbitrage between EU jurisdictions.

The Regulation lays down conditions for the issuance of credit ratings which are needed to restore market confidence and increase investor protection. It introduces **a registration procedure for credit rating agencies** to enable European supervisors to control the activities of rating agencies whose ratings are used by credit institutions, investment firms, insurance, assurance and reinsurance undertakings, collective investment schemes and pension funds within the Community.

Credit rating agencies will have to comply with rigorous rules to make sure (i) that ratings are not affected by conflicts of interest, (ii) that credit rating agencies remain vigilant on the quality of the rating methodology and the ratings and (iii) that credit rating agencies act in a transparent manner. The Regulation also includes an **effective surveillance regime** whereby European regulators will supervise credit rating agencies.

New rules include the following:

- credit rating agencies may not provide advisory services;
- they will not be allowed to rate financial instruments if they do not have sufficient quality information to base their ratings on;
- they must disclose the models, methodologies and key assumptions on which they base their ratings;
- they will be obliged to publish an annual transparency report;
- they will have to create an internal function to review the quality of their ratings;
- in order to ensure the independence of the credit rating process from the business interest of the credit rating agency as a company, credit rating agencies should ensure that at least one third, but no less than two, of the members of the administrative or supervisory board are independent .

The Committee of European Securities Regulators (CESR): CESR will receive applications for registration and effectively inform the competent authorities in all Member States. CESR should also provide advice in respect of the completeness of the application to the competent authority of the home Member State. The examination of applications for registration should be carried out at national level by the relevant competent authority

Furthermore, CESR must ensure coherence in the application of the Regulation. It will enhance and facilitate the cooperation and coordination of competent authorities in supervisory activities and issue guidance where appropriate. CESR will therefore establish a mediation mechanism and peer review in order to facilitate a coherent approach by the competent authorities.

Credit ratings issued in third countries: the Regulation provides for the use of credit ratings issued in third countries for regulatory purposes in the Community provided that they comply with requirements which are as stringent as the requirements provided for in the Regulation. The Regulation introduces an endorsement regime allowing credit rating agencies established in the Community and registered in accordance with its provisions to endorse credit ratings issued in third countries. When endorsing a credit

rating issued in a third country, credit rating agencies must determine and monitor, on an ongoing basis, whether credit rating activities resulting in the issuing of such a credit rating comply with requirements for the issuing of credit ratings which are as stringent as those provided for in this Regulation, achieving the same objective and effects in practice.

Colleges of competent authorities: the college should represent the effective platform for an exchange of supervisory information among competent authorities, coordination of their activities and supervisory measures necessary for the effective supervision of credit rating agencies. In particular, the college should facilitate the monitoring of the fulfilment of conditions for the endorsement of credit ratings issued in third countries, certification, outsourcing arrangements, and exemptions provided for in this Regulation. The activities of the college should contribute to the harmonised application of rules under this Regulation and to the convergence of supervisory practices.

Exchange of information: the competent authorities shall, without undue delay, supply each other with the information required for the purposes of carrying out their duties under this Regulation.

Reports: by 7 December 2012, the Commission shall make an assessment of the application of this Regulation, including an assessment of the reliance on credit ratings in the Community, the impact on the level of concentration in the credit rating market, the cost and benefit of impacts of the Regulation and of the appropriateness of the remuneration of the credit rating agency by the rated entity (issuer-pays model), and submit a report thereon to the European Parliament and the Council. By 7 December 2010, the Commission shall, in the light of developments in the regulatory and supervisory framework for credit rating agencies in third countries, present a report to the European Parliament and to the Council concerning the effects of those developments and of the transitional provisions on the stability of financial markets in the Community.

Transitional provisions: credit rating agencies operating in the Community before 7 June 2010 (existing credit rating agencies), which intend to apply for registration under this Regulation, shall adopt all necessary measures to comply with its provisions by 7 September 2010. Credit rating agencies shall submit their application for registration no earlier than 7 June 2010. Existing credit rating agencies shall submit their application for registration by 7 September 2010.

ENTRY INTO FORCE: 07/12/2009.

APPLICATION: from 07/12/2009. However: Article 4(1) (use of credit ratings) shall apply from 7 December 2010 and certain parts of Article 4(3) (endorsement of rating issued in third country) shall apply from 7 June 2011.