



THE COMMITTEE OF EUROPEAN SECURITIES REGULATORS

Date: 30 November 2004

Ref.: CESR/04-638

PRESS RELEASE

CESR CONSULTS ON POTENTIAL REGULATORY APPROACHES FOR CREDIT RATING AGENCIES

CESR published today a consultation paper which discusses the issue of how to deal with credit rating agencies in a regulatory context within Europe. In particular, whether there are any market failures and whether there is a need for the introduction of some sort of recognition and/or regulation of rating agencies as these are generally not regulated in Europe today. CESR must provide its advice to the European Commission by 1st of April 2005, which will then assess the need, or not, for introducing European legislation or other solutions in this field.

The paper analyses a potential set of rules of conduct that might apply to rating agencies and, in particular, considers the various potential conflicts of interests that might arise as well as the fair presentation and methodologies of rating agencies, staff requirements and the relationship between issuers and credit rating agencies.

Amongst the various **potential conflicts of interest** which CESR discusses, a number arise in the context of the relationship between issuers and credit rating agencies. For example, ratings agencies are often remunerated by the issuers they rate and sometimes provide the issuer with ancillary services.

In relation to **methodologies** for example, CESR discusses a number of transparency requirements that could be placed on rating agencies. For example, one might wish to require ratings agencies to disclose and explain the key elements underlying the rating and to provide an explanation of the assumptions on which the rating is based and the factors to which the rating of this issuer is most susceptible to change.

A further key aspect of the consultation paper is the analysis on **how credit rating agencies and issuers might effectively work within the requirements of the Market Abuse Directive**, in relation to the handling of confidential and market sensitive information.

Finally the consultation paper explores the various ways one could approach the issues put forward by the European Commission and considers the impact this might have on competition in this sector. In particular, it indicates the following policy options which exist, namely, either to:

- leave to the market itself to self regulate on the basis of codes of conduct that are developed by the market participants (drawing on standards established by IOSCO and others);
- have some third party assess compliance with the above mentioned codes;



- draw on the Basel II recognition process for using rating for capital adequacy and to assess the behaviour of rating agencies;
- put in place a formal registration mechanism and potentially, to establish ongoing supervision, either on a national or EU-wide level where credit rating agencies would, be assessed by European securities regulators on an ongoing basis.

Context

The decision to consider whether and, how, credit rating agencies might be regulated stems from discussions by Ministers of Finance and MEPs following Enron in 2002 and latterly the Parmalat scandal in 2004. This also arose in the context of CESR work to prepare the technical advice on implementing measures for the Market Abuse Directive particularly in relation to conflicts of interest and fair information. A further key dimension, which has led to consideration of this issue has been the Basle II agreements and the forthcoming Commission's Draft proposal on the review of capital requirements for banks and investment firms (CRD), which will reinforce at international and EU level, the deployment of credit ratings into banking legislation. As such the credit ratings given to issuers will have a material impact on banks which will have to hold differing capital requirements as a result of the ratings given by Credit Rating Agencies on issuers. A third dimension, is that discussions have been held in many public fora, including IOSCO, in recent years as well as in the United States Securities and Exchange Commission (SEC), which is currently working on this subject. Further co-ordinated work in this area by the EU will therefore maximise the opportunity for the convergence of principles, between the European and US regulatory approaches and those adopted internationally, in a coherent way. A summary of these various initiatives is annexed to the call for advice available on CESR website (Ref: CESR/04-394).

This request from the European Commission for CESR advice is of a policy nature and as such, CESR's final advice will include a number of possible options with pros and cons, rather than necessarily provide detailed implementing provisions (as usually required from CESR's in its technical advice for Level 2 implementing measures of an existing Directive).

Timetable

A timetable for CESR's work in this area is attached in the note to editors.

Responses to the consultation can be submitted online by 1 February, 2005 through CESR's website (www.cesr-eu.org) under the section 'Consultations'. A hearing will also take place at CESR's premises on 14 January 2005. To book a place for the hearing please use CESR's website.



Notes for Editors:

1. To develop the technical advice, CESR has formed a task force chaired by Ms Ingrid Bonde, Director General of the Swedish Finansinspektionen. Javier Ruiz del Pozo from the CESR secretariat acts as rapporteur.
2. The call for technical advice (Ref: CESR/04-394) identifies in particular four areas on which CESR should provide technical advice and these include:
 - Handling of potential conflicts of interests within rating agencies;
 - Transparency of rating agencies' methodologies;
 - The legal treatment of rating agencies' access to inside information; and
 - Concerns about the possible lack of competition in the market for provision of credit ratings.
3. In developing CESR's advice, CESR has and will continue to co-ordinate closely with fellow regulators both within the EU in the form of the fellow regulatory banking committee (CEBS), and internationally, with the SEC through its more regularised and intensive dialogue announced by CESR on 4 June 2004. CESR's proposal have also taken into account how this might interact with existing EU legislation and in particular, the Market Abuse Directive (which will come into effect by the end of 2005) and drawn heavily on the useful groundwork laid down by IOSCO and the Basle Committee.
4. CESR is an independent Committee of European Securities Regulators. The role of the Committee is to:
 - Improve co-ordination among securities regulators;
 - Act as an advisory group to assist the EU Commission, in particular in its preparation of draft implementing measures in the field of securities;
 - Work to ensure more consistent and timely day to day implementation of community legislation in the member states.
 - The Committee was established under the terms of the European Commission's decision of 6 June 2001 (2001/1501/EC). It is one of the two committees envisaged in the Final Report of the group of Wise Men on the regulation of European securities markets. Baron Alexandre Lamfalussy chaired this group. The report itself was endorsed by the European Council and the European Parliament. The relevant documents are available on the CESR website.

Each Member State of the European Union has one member on the Committee. The members are nominated by the Members States, and are the Heads of the national public authorities competent in the field of securities. The European Commission has nominated the Director General of the DG Market as its representative. Furthermore, the securities authorities of Norway and Iceland are also represented at a senior level.

5. For further information please contact:



CESR

Fabrice Demarigny
Secretary General of CESR

Or Victoria Powell
Information Officer

Tel : +33 (0)1.58 36 43 21

Fax: +33 (0)1.58 36 43 30

Email: secretariat@cesr-eu.org

Web site: www.cesr-eu.org

Indicative timetable for CESR's advice on Credit Rating Agencies

