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ESMA/2011/97
Guidelines on the application of the endorsement regime under Article
4 (3) of the Credit Rating Regulation 1060/2009

Dear Sirs,

BVI¹ welcomes ESMA's consultation on guidelines for foreign CRA endorsement pursuant to Article 4 (3) of the Credit Rating Regulation 1060/2009.

We wish to reiterate below the concerns we raised last year with the European Commission on this matter. BVI wrote to the Commission to underline its disagreement with its interpretation of the endorsement process.

The proposed ESMA interpretation of the endorsement process will directly limit the investment choices of European money market funds (MMF). Fund managers need to directly apply CRA ratings from July 2011 in the day to day management of their funds as required by the CESR MMF Guidelines issued in May 2010.

Beyond MMF management, our members are especially concerned that the orderly management of investment funds and portfolios for credit institutions

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¹ BVI Bundesverband Investment und Asset Management e.V. represents the interests of the German investment fund and asset management industry. Its 85 members manage currently assets of some EUR 1.8 trillion both in mutual funds and mandates. BVI's ID number in the EU register of interest representatives is 96816064173-47. For more information, please visit www.bvi.de.

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might be severely hampered going forward if this issue cannot be resolved. Our members currently manage well over 120bn Euros in assets on behalf of credit institutions. The efficient management of these funds will be curtailed as the range of available CRA ratings will be much more limited than today. The recognition of ratings issued in the US is of particular importance to investment managers due to the impact on their bank clients' regulatory capital positions and on the European financial markets.

We may also see negative consequences in management of insurance and pension fund assets by our members in the future to the extent that insurance capital requirements may rely on ratings. In any case, already today investment in structured finance by German insurers is limited by the credit rating of the issue.

Comments on Draft ESMA Guidelines

We continue to believe that the endorsement process was created as a deliberately flexible mechanism to allow the continued use of all ratings issued by the largest credit rating agencies, subject to these CRAs assuming responsibility for the application of requirements "at least as stringent as the requirements" applicable within the EU, irrespective of the country of issuance of the rating or of the analyst's location. A CRA seeking endorsement for ratings issued by lead analysts working with the non-EU part of such CRA should only need to verify and demonstrate to ESMA that the CONDUCT of the non-EU CRA parts is subject to (voluntary) rules that are as stringent as the EU law requirements in Art. 6 to 12 of the EU Credit Rating Regulation. Art 4(3)(b) clearly specifies that it applies only to the CONDUCT of the non-EU CRA. It does not apply directly to the foreign CRA underlying regulatory environment. In our opinion the regulation of the country of incorporation of the non-EU part of the endorsing CRA only needs to follow the EU regulatory requirements to the extent that they are expressly provided for Art. 4(3)(a)-(h). Otherwise there would be no real difference between the endorsement and the full registration approach and consequently no need for the specific regulation of endorsement as provided for in Art. 4(3).

The above described interpretation endorsement regime is expressly supported by the EP (see MEP Klinz, CRA report dd. 23.3.2011 at no. 16).

Consideration of the Cost Benefit Analysis

On the ESMA cost benefit analysis, we would like to mention that the cost of the above described endorsement regime will be much lower than the strict endorsement test proposed by ESMA. We also would like to point out that the analysis is based on very questionable arguments to the extent that your analysis assumes that other nations like the US will quickly adapt their CRA regulation in full to the EU legal standard or that foreign rating agencies will relocate analysts to the EU.

In particular, we are concerned about the availability of endorsed ratings issued by lead analysts based in the US after 7 June 2011. In spite of the welcome efforts of the three large CRAs to increase their issuance of ratings outside the US during the past few years, we need to recognize that today the amount of ratings issued by the large CRAs in Europe may not be sufficient. For example, Moody's Investor Service issued – based on the jurisdiction of the lead analyst – in the US more than 19,000 (issue) ratings on financial institutions (excluding structured finance) and about 24,000 ratings on corporates, including insurance companies by the end of 2009. During the same year about 47,000 (issue) ratings on financial institutions (excluding structured finance) but less than 5,000 ratings on corporates, including insurance companies, were issued by Moody's lead analysts based in the EU. These numbers give an indication of the magnitude of the problem, especially of securing the refinancing of the corporate sector if ratings issued by lead analysts in the US could not be endorsed by EU-based CRAs after June 2011.

If ESMA does not yield on the proposed interpretation, we have to assume that the economic costs as detailed by a number of banks in their responses to the first ESMA consultation on this subject in January 2011 will hit all European banks on a more or less similar scale depending on the business model. This will result in less financing of their activities in markets which cannot easily be covered by ratings under the strict endorsement regime.

We have liaised with the European Banking Federation (EBF) on this matter and support their detailed arguments in full.

We are happy to answer any questions you may have in relation to this matter. Our response can be made public.

Yours sincerely

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