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Committee of European Securities Regulators
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RESPONSE TO THE COMMITTEE OF EUROPEAN SECURITIES REGULATORS' CONSULTATION PAPER RELATING TO THE GUIDANCE REQUIRED IN TERMS OF THE EUROPEAN UNION REGULATION ON CREDIT RATING AGENCIES ("THE REGULATION")

Moody's Investors Service ("**MIS**") wishes to thank the Committee of European Securities Regulators ("**CESR**") for the opportunity to comment on the draft "Guidance on Registration Process, Functioning of Colleges, Mediation Protocol, Information set out in Annex II, Information set for the application for Certification and for the assessment of CRA systemic importance" ("**the Draft Guidance**").

In this cover letter, we raise our primary in-principle concerns and, in the Annex, we respond to the questions raised in the Consultation Paper.

I Obligations for credit rating agencies ("CRAs") that extend beyond the scope of the Regulation

MIS is concerned that the Draft Guidance introduces requirements in a number of areas that exceed the scope of the Regulation. We would remind CESR of Article 14(5), where it states:

> *Competent authorities shall not impose requirements for the registration which are not provided for in this Regulation.*

In this response, MIS identifies a number of areas where the Draft Guidance goes beyond the scope of the Regulation. We note in particular the guidance on endorsement, historical information, registration requirements and various on-going obligations. These are developed further in the submission.

II The proposed administration of the endorsement process is not supported by the Regulation

Extra-territorial reach extended beyond the conduct of credit rating activities and into third country regulatory systems

Based on non-public, informal advice from the EU Commission ("**the Commission**"),[1] CESR has issued Draft Guidance that radically alters the meaning of Article 4(3) of the Regulation. Article 4(3)(b) is unambiguous in requiring the "*conduct* of credit rating activities" to fulfil "...requirements which are at least as

[1] We would request the Commission to publish its informal advice.

stringent as" those in Articles 6-12 of the Regulation.[2] CESR's Draft Guidance however proposes to convert this conduct standard for a third country CRA into an obligation on the third country's legislature or regulator to introduce *regulation* that is "at least as stringent as" that in the EU.

In our view, the Commission's interpretation of Article 4(3) introduces the prospect of market disruption if non-EU jurisdictions are either unwilling or unable to adopt regulations equivalent to the EU in accordance with the timetable established by the Regulation. The participation of EU financial institutions in global capital markets could be handicapped as exposures in those markets will have to be treated as unrated for regulatory capital adequacy purposes. Furthermore, the flow of EU investment capital to important economic partners might well be interrupted. We request that in interpreting the Regulation, CESR consider the potential effects on global capital markets and of collective efforts to restore financial stability.

It is also not clear how Article 4(3)(b), or the rest of Article 4(3), could accommodate such an interpretation. We strongly believe that a system where a registered and supervised non-EU CRA voluntary adopts the EU conduct standards should be sufficient for endorsement purposes. The EU CRA will retain responsibility for the endorsement of those ratings and the EU competent authorities will have, at all times, the ability to supervise this endorsement process and to co-operate with third country regulators in ensuring the requirements under Article 4(3) are met on an ongoing basis.

III Historical information

The Draft Guidance requires a CRA to provide in certain cases up to 3 years of historical information, which implies that CESR has adopted an interpretation of certain provisions of the Regulation that is retroactive in nature. We believe that such a retroactive approach conflicts with Article 40 of the Regulation which clearly states that an existing CRA operating in the EU that intends to apply for registration under the Regulation *"shall adopt all necessary measures to comply with its provisions by 7 September 2010."*

In our view, no negative inferences may be drawn on historical information. The argument is put forward by CESR that historical information will help assess the effectiveness of internal controls. However, historical information has no bearing on the effectiveness of internal controls at the time of the application. Moreover, the test is whether the applicant CRA is in compliance with the obligations relating to it under the Regulation *at the date stipulated in the Regulation*, and not whether the CRA was in compliance with non-existent standards in relation to past CRA activity. Consequently, we do not believe that information or data pre-dating the entry into force of the Regulation will serve a meaningful purpose for CESR's evaluation.

Furthermore, MIS believes that the principle of legal certainty should provide market participants, such as MIS, with confidence that EU legislation should not take effect from a point in time prior to its publication. MIS has operated on the legitimate expectation that our structure, operations, systems and functions were adequate for

[2] In other words, the CRA must fulfil requirements "as stringent as" (conduct) and is not required to be subject to requirements "as stringent as" (regulatory system). A means of a CRA evidencing the conduct contemplated in Article 4(3)(b) could be through an equivalence finding of the relevant non-EU jurisdiction by the Commission, however, this should not preclude the requirement being met through the conduct of the non-EU CRA in cases where the Commission has not published an equivalence decision or where it has published a negative equivalence decision.

our corporate needs under the pre-existing self-regulatory framework in the EU to which we voluntarily submitted. We could not have foreseen that future regulation would require these systems to be reengineered in order to present data retroactively in accordance with newly created legislative obligations.

Consequently, we would urge CESR to reconsider its retroactive interpretation of the Regulation and delete the bracketed text in the Draft Guidance.

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MIS would like to thank CESR for affording us the opportunity to comment on the Draft Guidance. Please do not hesitate to contact me should you wish to discuss the contents of this letter in more detail.

Frédéric Drevon
Head of Europe, Middle East and Africa ("EMEA")
Senior Managing Director

ENCL.

Annex

Question 1 (paragraphs 10-19)
General issues applicable to the registration process

We have no objection to the proposed definition of working day.

Questions 2 & 3 (paragraphs 20-28)
Application for registration
A. Structure of the application for groups of credit rating agencies
B. Language of the application for credit rating agencies established in more than one Member State

MIS considers it regrettable that in the Draft Guidance CESR has not chosen to identify a more practical application of the language regime in Article 15(3) that still meets the administrative law requirements of individual Member States. We foresee significant translation obligations during this application process, which will likely fall away once the European Securities and Markets Agency is established. These translation obligations will inevitably place the strict deadlines in the Regulation for the application process under significant pressure. Furthermore, in our view, the administrative requirement in Article 15(3) can be met in a less burdensome manner than the structure proposed in the Draft Guidance.

To address these language concerns, MIS proposes a three-tier structural format to the documentation submitted for CRA registration contemplated in paragraph 24:

(a) Formal application - reflecting the details listed under paragraph 168 of the Draft Guidance which would constitute the formal application of the CRA and will be translated into the relevant official languages in jurisdictions where this is required by law in compliance with Article 15(3);
(b) First Annex - containing general information including the information that is common to all the members of the group of CRAs and may be submitted in a language customary in the sphere of international finance;
(c) Second Annex - containing separate specific unique information for each of the applicants within the group of CRAs (for example, if that subsidiary intends to endorse; apply for an exemption etc) and may be submitted in a language customary in the sphere of international finance.

24. *This means that for a group of CRAs, the structure of the pack to submit would be the following:*
- *Formal application for each of the applicants containing the details listed in paragraph 168 of this Guidance in a language which is required under the law of the relevant home Member State and also in a language customary in the sphere of international finance;*
- *General part including all the disclosures that are common for all the CRAs members of the group in a language customary in the sphere of international finance*
- *Separate sections including the specific additional disclosures (for example, application for exemption) for each of the applicants ~~(if there are 7 members of the group there would be 7 sections - i.e. for the subsidiary in Germany, for the subsidiary in Spain, etc)~~ in a language customary in the sphere of international finance*

It is MIS's opinion that the proposed structure of the application above would meet the requirements of the Regulation. Based on our experience when applying for ECAI recognition, we believe such an approach meets the requirements of the relevant administrative regimes in the Member States.

We also confirm our understanding of paragraph 26 "This would be the pack the college would use in its examination process" to mean that the submission of the application in a language customary in the sphere of international finance would start the administrative process and that any translation required could be submitted at a later stage but should be submitted before a final decision is taken by the home competent authority. We suggest, however, that the resulting Guidance express clearly that the application for registration will be deemed complete without any additional translations at the time of the submission of the application.

Question 4. (paragraphs 29-36)
Application for registration
C. Language of the application for credit rating agencies established only in one Member State and whose college is composed only of the home competent authority of that Member State

MIS offers no comment.

Question 5. (paragraphs 38-39):
Application for registration
D. Format of the application

MIS offers no comment.

Question 6 (paragraphs 45-46)
Assessment and decision on the completeness of the application for registration
B. College assessment on the completeness of the application
(a) Beginning of the assessment period

MIS would propose that the calculation of the dates begins from the date on which CESR sends the application to the Member States so as to avoid the situation where the timeline for consideration by Member States would begin on different dates. We would also request to be notified by CESR on the submission of the application by CESR to Member States so as to allow an applicant to calculate the relevant time periods envisaged under the Regulation. Finally, we would encourage CESR to insert a provision that it will circulate the applications immediately, but in any event, within 5 days after receipt from the applicant as contemplated in Article 15.4.

> *45. Article 15.5 provides 25 working days to the competent authority of the home Member State and the members of the college for assessment of the application. CESR considers that this period should begin from the date* *that CESR sends the application to* ~~*of receipt by*~~ *the authorities* *by electronic mail* ~~*of the application from CESR*~~ *(and not from the day CESR has received the application from the applicant). Otherwise the authorities could have only 20 days (or less if CESR does not transmit the applications in time) to decide that the application is complete or to require additional information if that is not the case. CESR will endeavour to circulate the applications immediately,* *but in any event within 5 working days,* *after reception from the applicant.* *CESR will duly notify the applicant of the date of transmission of the application to the competent authorities to allow for transparency in the calculation of the time periods envisaged under the Regulation*

Question 7 (paragraphs 47-48)
Assessment and decision on the completeness of the application for registration
B. College assessment on the completeness of the application
(b) Notification of the completeness of the application in case of groups of CRAs

We have no objection to this approach but would request that the minimum timeframe by which an incomplete application may be corrected should not be less than 20 working days.

> *48. CESR proposes that the members of the college should jointly examine the joint application from the group of CRAs and decide whether it is complete. Therefore the decision will be taken in relation to the whole group of CRAs. Then the home competent authority of the mandated rating agency -designated by the group according to Article 15.2 will notify that decision to the mandated rating agency on behalf of all home competent authorities. In case the application is not complete, the home competent authority of the mandated rating agency will notify to the mandated CRA the deadline (agreed by the college), which shall not be less than 20 working days, by which the group of CRAs will have to provide the additional information.*

Question 8 (paragraphs 49-50)
Assessment and decision on the completeness of the application for registration
B. College assessment on the completeness of the application
(c) Non complete applications – Deadline for applicants to provide additional information and deadline for competent authorities to assess the additional information requested

MIS offers no comment.

Question 9 (paragraph 51)
Examination of the application for registration of a CRA by the competent authorities
A. Period of examination

MIS offers no comment.

Question 10 (paragraphs 52-54)
Examination of the application for registration of a CRA by the competent authorities
B. CESR's advice on the compliance of the CRA with the requirements for the registration

MIS offers no comment

Question 11 (paragraph 55)
Examination of the application for registration of a CRA by the competent authorities
C. Exemptions

MIS proposes that the resulting Guidance addresses the situation where a request for exemption is declined by one Member State. MIS proposes that the college process for consideration of the application for a group of CRAs is not interrupted by

a negative exemption decision and that the decision on registration is duly taken by each home Member State subject to the entity affected by the exemption decision being required to put in place the required function within a defined period of time. We would note that if an exemption is not granted, there is likely to be a significant delay because, for example, the governance arrangements could take a 3-6 month period to put in place.

Question 12 (paragraph 56)
Adoption of a fully reasoned registration or refusal decision by the competent authority of the home Member State
A. Common format for notifications of decisions

MIS supports the proposal to develop a common format for notification of regulatory decisions.

Question 13 (paragraphs 57-61)
Notification of the decision on the registration, refusal of registration or the withdrawal of registration of a credit rating agency
A. Transparency of the registration procedure

MIS notes that it is not standard practice within the EU for administrative decisions declining registration to be made public and that typically any administrative decision would only take effect (together with timelines related thereto) on disclosure thereof to affected parties. MIS understands, however, that a decision to decline registration to existing CRAs will need to be made public. We would propose that any such publication shall only disclose the fact of refusal of registration and that in no circumstances will the decision together with the reasons therefore be published. To aide the interpretation of paragraph 60, we propose the insertion of the word "another":

> *60. Another issue arises regarding the withdrawal of a registration. According to Article 20 (4), the decision on the withdrawal of registration shall take immediate effect throughout the Community, subject to the transitional period for the use of credit rating agencies referred to in Article 24 (2). This means that EU banks and other regulated entities will have to stop using for regulatory purposes the ratings of the CRA concerned in a period not exceeding ten working days if another registered CRA has rated the same instrument or issuer or three months if there are no ratings of the same instrument or issuer by other registered CRAs. Once the authority of the home Member State has notified the withdrawal to the Commission, the list of registered CRAs will be updated within 30 days. This means that the abovementioned period of 10 days might have expired before the list of registered CRAs is updated.*

In our view, the notification by the competent authority to CESR, the Commission, other competent authorities and the applicant/registered CRA (as applicable) regarding the refusal or withdrawal of registration should be in accordance with the administrative law requirements of the relevant home Member State and include the reasons for any decision as contemplated in Articles 16(7) and 17(7). In this regard, we would expect a notice issued in terms of Article 18 (1) and (2) to include:

- full reasons for any decision with evidence on which the reasons are based;
- the competent authority's understanding of the relevant provisions of the Regulation on which the decision is based;
- the process followed and details of the reasoning process that led to the decision, including:

- o full and detailed disclosure of any dissenting opinions which should be appropriately identified;
- o members of the college which participated in any meetings discussing the decision.

Question 14 (paragraph 62)
Notification of any material changes to the conditions for initial registration

We would note that under paragraph 155 of the Draft Guidance:

> *A material change is any change that may affect the substance of the information submitted in the application. In any event all changes that may affect compliance with the requirements of the Regulation are material.*

We do not believe it is necessary for a closed list of what constitutes a "material change" to be reflected in the Draft Guidance. However, we are concerned that this definition is significantly wider than the use of the concept of materiality in Article 14.3 as instructed by Recital 52. We therefore suggest incorporating the examples of material changes provided in the Regulation in order to contextualise the concepts of materiality in the definition and ensure consistency between the Regulation and the Draft Guidance. We also suggest changing the words "substance of the information" to "substantive information" because the former offers no guidance as to the materiality of the information. The definition in the Draft Guidance may be amended as follows:

> *155. A material change is any change that may affect the substantive ~~substance of the~~ information submitted in the application, for example, inter alia, the opening or closing of a branch within the European Union. ~~In any event~~ In addition, all changes that may affect compliance with the requirements of the Regulation including without limitation changes in the endorsement regime or outsourcing arrangements are material.*

Question 15 (Paragraphs 65-68)
Procedures with competent authorities

MIS has fundamental concerns with the proposed endorsement procedure. Article 4(3) states that a CRA "established in the Community and registered in accordance with the Regulation" may endorse only when the conditions in Article 4(3) are met. We can find no requirement in the Article that suggests a pre-approval of each non-EU CRA's regulatory system prior to an EU CRA endorsing the non-EU CRA's credit ratings and any such requirement would exceed the scope of the Regulation. Such an approach is clearly set out in Article 5 for the certification process but is absent from Article 4(3). Consequently, the information request contained in Annex II should relate to the information that will enable the relevant competent authority to assess whether a CRA has the appropriate infrastructure to fulfil the endorsement requirements of Article 4(3) as opposed to whether it may endorse ratings from a specific non-EU jurisdiction.

Question 16 (Paragraphs 69-72)
Endorsement procedure

As stated above, we do not believe that the relevant competent authorities have the necessary authority to pre-approve the endorsement of ratings per jurisdiction since there is no enabling provision in the Regulation to this effect. Paragraphs 70 and 71 seem to better reflect the intention of the legislature:

70. It seems neither practical nor necessary for authorities to check beforehand every rating that is going to be endorsed. However, the CRA should be in a position to prove at any time that all the endorsements it has issued comply with the requirements of the Regulation.
71. In any case the EU CRA when publishing the endorsed rating must clearly identify that it is an endorsed rating. However, the Regulation does not require the CRA to publish alongside the rating any further information about the rationale for the endorsement or the endorsement processes it has followed.

In our view, the Regulation limits the endorsement decision to the procedure contemplated in paragraph 70 (i.e. *ex post facto* review by competent authorities) and not the extension thereof as found in paragraph 72.

Question 17 (paragraph 73)
Registration without the conditions for endorsement being met

The first sentence of paragraph 73 appropriately captures the intention of legislature in not creating a linkage between registration and jurisdiction-specific endorsement. MIS disagrees, however, with the conclusion reached in the second sentence presupposing the need for pre-jurisdiction approval by the competent authorities before endorsement under Article 4(3) for the reasons mentioned above.

73. As endorsement is an activity that is voluntary for the CRA that applies for registration, CESR considers that the applicant CRA should be registered if it complies with all the conditions for registration even if those required for endorsement are not met. ~~This would mean that the registered CRA would not be able to endorse any ratings until it demonstrates to the college full compliance with all the conditions under Article 4.3~~.

Question 18 (paragraph 74)
Transparency regarding the third-country CRAs whose ratings may be endorsed by EU CRAs

MIS disagrees with the proposal because it follows the construction that pre-approval of jurisdictions is necessary for endorsement. We agree with the construction of the first two sentences of paragraph 74, however, the remainder of the paragraph is superfluous (since endorsed credit ratings will be disclosed) and seeks to extend the scope of the Regulation.

74. As stated above, Article 4.2 requires CRAs to clearly identify the credit ratings that have been endorsed. But it does not require the endorsing CRA to identify in its publication the third-country CRA that issued the endorsed rating. ~~It seems that financial institutions wishing to use ratings for regulatory purposes would have an interest in knowing the list of third-country CRAs whose ratings may be endorsed by a registered EU CRA (as authorised by the authority of the home Member State)~~.

Question 19 (paragraphs 76-81)
Procedure with competent authorities

MIS offers no comment.

Question 20 (paragraph 82)
Language of the application for certification

MIS offers no comment

Question 21 (paragraphs 83-84)
Systemic importance

MIS offers no comment

Question 22 (paragraph 85)
Withdrawal of the certification

MIS offers no comment

Question 23 (paragraphs 86-90)
Relationship between equivalence and endorsement
A. Should endorsed ratings and ratings issued by certified CRAs be subject to different requirements?

The foundations for (i) an endorsement decision in terms of the conduct of credit rating activities of the non EU-CRA and (ii) an equivalence decision in terms of the regulatory system of the non-EU CRA jurisdiction, should be objective. However, the actual decision is made by two distinct parties; equivalence by the Commission and endorsement by the EU CRA subject to *ex post facto* review by competent authorities of any endorsement decision.

A means of a CRA evidencing the conduct contemplated in Article 4(3)(b) could be through an equivalence finding of the relevant non-EU jurisdiction by the Commission, however, this should not preclude the requirement being met through the conduct of the non-EU CRA in cases where the Commission has not published an equivalence decision or where it has published a negative equivalence decision.

Question 24 (paragraph 91)
Relationship between equivalence and endorsement
B. What impact would a decision on equivalence have on the condition set out in Article 4.3(b) for endorsement?

MIS supports the notion that a positive equivalence decision by the Commission under the certification framework will satisfy the "at last as stringent as" criterion under the endorsement framework. However, the opposite does not hold true and notwithstanding a negative equivalence decision by the Commission, an EU CRA should be able to endorse a rating on the strength of the conduct of that non-EU CRA meeting the endorsement requirement under Article 4(3)(b).

Questions 25 and 26 (paragraphs 92-100)
Relationship between equivalence and endorsement
B. What impact would a decision on equivalence have on the condition set out in Article 4.3(b) for endorsement?

We disagree with the Commission's informal view as outlined in the Draft Guidance that the third country regulatory system needs to meet the test of "as stringent as" for the reasons set out in the cover letter. The logic drawn by the Commission that "...the requirements as stringent as the requirements set out in Articles 6-12 of the Regulation are established by law or regulation, not on a voluntary basis" referred to in paragraph 97 does not follow. We would argue that such a view exceeds the scope of the Regulation.

Although we agree with the spirit of paragraph 99, we disagree with the conclusion that the only reason that endorsement would still be possible after a Commission finding of not equivalent is because of a change in law subsequent to the Commission's decision. Instead, we believe that it would indeed be possible for the requirements in Article 4(3)(b) to be met notwithstanding a negative decision by the Commission and without a subsequent change in law because the *conduct* of credit rating activities of the non-EU CRA may meet the endorsement requirement under Article 4(3)(b).

Question 27 (paragraphs 104-105)
Language of the disclosures and the transparency report

We strongly disagree with the proposal of CESR in extending the language regime under Article 15(3) to Articles 11(1) and (3) and 12 since this would amount to an inappropriate extension to the scope of the Regulation. Article 15(3) creates a specific obligation regarding language for the registration application which is a procedure vis-à-vis the administration of the application whereas Articles 11 and 12 deal with disclosure obligations which have, amongst others, the purpose to ensure transparency for market-players. Article 15(3) can therefore not be extended to such disclosure obligations. Even if there is an argument that CESR does have legitimate authority to extend the scope of the language regime, we would argue that Articles 11 and 12 have the same objective as that suggested by CESR regarding the CEREP[3] and we would conclude that a similar exemption should apply for all the disclosure requirements under Articles 11 and 12 of the Regulation.

Question 28 (paragraphs 106-108)
Means of publication

We have no objection to the disclosures made pursuant to Article 11(1) being published on the website of the CRA.

Question 29 (paragraphs 109-112)
Timing for the publication or submission of the information

MIS understands that by requiring "updates of this information [to] be published immediately" in paragraph 110, CESR is referring to the annual updates as contemplated Article 11(1). We would request that the resulting Guidance provides clarity in this regard.

The Draft Guidance in paragraph 111 states that CRAs should provide a list of clients. We understand such list to be the lists referred to in paragraph 102.

Questions 30-32 (paragraphs 113-118)
Selection of facilitator

MIS offers no comment.

[3] See paragraph 105 of the Draft Guidance.

Question 33 (paragraphs 124-131)
Cross-college consistency

We would propose that paragraph 124 not only includes guidance that the majority position be reflected in any request to CESR for further advice, but also any minority views. This, we believe, will allow CESR to consider the full range of arguments put forward by the competent authorities and not be tempted into following the majority view as a matter of course.

MIS also supports the development of a regulatory work plan at the college as contemplated in paragraph 126. Given MIS' footprint in the EU, an alignment of regulatory workplans would be welcomed.

The fact that CESR has not implemented an appeal process for "decisions" taken at the college level is unexpected. We would support a process whereby "decisions" affecting registration, withdrawal and sanctions are not only subject to due administrative law process in giving CRAs an opportunity to be heard but also allowing CRAs an option to appeal a decision at college level before the formal administrative decision is taken by the home competent authority which will in and of itself be subject to home Member State administrative law provisions. We appreciate the provision for a "second deliberation" as contemplated in paragraph 131, however, this is only after any appeal process under national law. MIS requests an opportunity to appeal an initial "decision" reached by the college and prior to the home competent authority beginning the administrative process in terms of its national law and to be able to provide to CESR its views on the submission by the college facilitator to CESR.

Question 34 (paragraphs 132-135)
Decision Making
C. Supervisory measures/sanctions

We refer CESR to our request under Question 33 third paragraph, for an opportunity to appeal the informal college "decision" also in relation to supervisory measures/sanctions contemplated under Articles 24 and 25.

Question 35 and 36 (paragraphs 141-144)
Location of issuance and impact on supervisory responsibility

We would encourage CESR to adopt guidance on the location of rating based on three important principles:

(a) Fix the location of a rating at a point in time

In the interests of certainty and practicality, in our view, the location of the rating should be fixed at the time of issuance. This will avoid unnecessary duplication of process and avoid potentially market disruptive events if the location of the rating was to be subject to change over the life of a rating.

(b) Base the location of existing stock ratings on prior practice

MIS currently maintains our database of ratings on the location of the lead analyst. It would be extremely challenging and resource intensive to re-map each rated security into any new criteria. For this reason, we would propose to fix the location of the rating of the stock of ratings as the location of the lead analyst on the date of

application and going forward, according to the criteria that will be determined by the resulting Guidance.

(c) Clear regulatory responsibilities

The resulting criteria should ensure that there is certainty as to the EU regulator with primary supervisory responsibility for the supervision of the Regulation with respect to any particular rating.

Proposal

MIS would propose that the most effective means of identifying the location of the rating for the purposes of the Regulation will be either:

- The jurisdiction of the office where the lead analyst is based, this being the location where the primary analytical work is undertaken; or
- The jurisdiction of the office where the Chair of the rating committee is based, since the Chair is the person primarily responsible for ensuring that the various internal control measures are appropriately complied with at the time of, and during, the relevant rating committee.

Analysis of CESR proposals

We now discuss, in turn, each of the proposed indicators for location of the rating:

(i) *If the registered CRA has an office in the country in which the rated issuer/assets is/are listed this is the issuing CRA*

A rated issuer (assuming this to relate to its debt securities) may be listed and traded on various exchanges. If place of "listing" is used as a determining factor, there is a material risk of multiple places of listing (eg primary listing and secondary listing) being identified. It may also be the case that many securities are listed in one jurisdiction but actually relate to underlying referenced assets/primary business in another EU jurisdiction. This not only introduces endorsement/certification challenges but may also defeat the purpose of the Regulation.

Furthermore, the significant concern with such an approach is that it de-links the actual regulated activity of producing a rating from any regulatory oversight of the credit rating activity. For instance, if MIS rates a security issued in France but the lead analyst and the committee Chair is based in Germany, the majority of discussions and documents for that rating will be generated in the German office and not in the French office. However, CESR's guidance will establish this rating as being under the supervision of the French competent authority. Furthermore, any criteria that results in the location of a rating being deemed to be in a jurisdiction other than where the primary analysis or consideration of the rating occurs puts at risk the independence criteria at the heart of the Regulation.[4]

(ii) *If the registered CRA has an office in the country in which the issuer is incorporated (or assets are located), this is the issuing CRA*

Such an approach will suffer from similar de-linkage concerns identified under the second paragraph in (i) above.

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[4] Article 23(1).

Furthermore, a transaction where a special-purpose vehicle ("SPV") is created solely for the functions listed in the transaction documents, the domicile of the issuer SPV is identified primarily for accountancy, legal or tax reasons and not because of any association with the underlying assets/guarantor. Basing the location of the rating on such a criterion would, therefore, be of limited practical value for the purposes of this Regulation.

Significant problems could also be expected in identifying the location of the rating through location of assets where the rating relates to a security with either underlying assets based in multiple jurisdictions and/or underlying assets that will change over the life of the transaction. This introduces unnecessary uncertainty into the process of establishing the location of the rating which, for such an important classification for the purposes of the Regulation, would be unwelcome.

(iii) *The registered CRA of the employee that lead the rating discussion with the issuer is the issuing CRA*

This introduces a criterion of identifying the employee that leads the discussions with the issuer. There is no such categorisation in the Regulation and in our view this will serve to complicate the interpretation of the text. Furthermore, the interpretation of the Draft Guidance itself will be difficult because of the uncertainty as to what would constitute "leading of the discussions with the issuer". For example, for an Irish issuer using a French arranger, the support analyst could be located in Paris and the lead analyst located in London. The support analyst may initiate discussions with the issuer and be the central point for routine contact with the issuer. This could lead to a conflict between competent authorities over allocation of regulatory oversight.

(iv) *The registered CRA that employs the lead analyst is the issuing CRA*

We would propose that this criterion or the location of the Chair of the rating committee be used as the sole determinant of the location of the rating. MIS typically allocates a transaction to a lead analyst based on the skills, experience, language and workload of analysts. The Chair of a rating committee is typically a senior analyst in the relevant line of business and is selected on the strength of experience and skills in credit analysis. Both of these roles are substantive roles in the production of a rating which is the activity regulated under the Regulation (issuance of ratings).

We further request CESR to provide clarity on the meaning of "an auditable trail of the process of establishing the credit rating" since we would not expect that every credit rating issued by MIS would require an audit of the location of the rating.

Finally, MIS can find no reference in the Regulation that would require CRAs to disclose the name and address of the office issuing the rating and the Member State in which the rating was issued and any such request would amount to an extension to the scope of the Regulation. Furthermore, this has the potential to introduce additional information noise into our disclosures that may serve to confuse investors who are likely to have no interest in where the rating was produced other than whether the rating requires endorsement to be used for regulatory capital purposes in the EU.

<u>Drafting suggestion</u>

> *143. CESR considers that it is necessary to define criteria for assessing where a rating has been issued to allow supervisory responsibility to be assigned and also to allow a*

correct implementation of the endorsement regime (market participants should bear in mind the definition will need to be applied to identifying the issuing location of non-EU ratings). CESR also believes it is important in order to prevent ongoing market disruptions for the location of the rating to be fixed at the time of initial issuance for ratings assigned as from the date of application. In order to avoid undue re-engineering of systems, CESR would allow existing CRAs to determine the location of the rating based on the principle applied by the applicant CRA prior to date of application and for that determination to be fixed on the date of application for registration. CESR will therefore use the following to determine the location of a rating:

(a) For the stock ratings (ratings assigned up to the date of application for registration), the location of the rating will be determined according to the principles adopted by the applicant CRA prior to registration. The location of rating for those ratings will be fixed according to that principle on the date of application.

(b) For the flow ratings (ratings assigned following the date under (a), the location of the rating will be the location of ~~has considered a number of possible criteria for identifying the issuing office and would request the view of market participants as to their validity and usefulness. The possible criteria identified are:~~

~~— If the registered CRA has an office in the country in which the rated issuer/assets is/are listed this is the issuing CRA.~~

~~— If the registered CRA has an office in the country in which the issuer is incorporated (or the assets are located) this is the issuing CRA.~~

~~— The registered CRA of the employee that lead the rating discussion with the issuer is the issuing CRA.~~

the registered CRA that employs the [lead analyst] / [rating committee chair] for that rating.

Once the determination in (b) is made, this location will be fixed, notwithstanding any change to the [lead analyst] / [rating committee chair] or his or her office of employment.

144. In the process of formulating a credit rating, CESR expects the CRA to identify the office of the CRA that issues the rating in accordance and in fulfilment of the conditions established for it under the decision to grant the CRA registration. This means that the CRA must implement the measures necessary for the establishment of a credit rating and such measures must include ~~an auditable trail of~~ the process of establishing each credit rating. ~~CESR further expects the name and address of the office elaborating the rating and issuing it, including the member state in which the agency has issued the rating must accompany each credit rating at all times.~~

Question 37 (paragraph 147)
Mediation mechanism

MIS offers no comment.

Questions 38-40 (paragraphs 148-212)
Guidance on the information set out in Annex II

We have set out our comments on Section VIII per the sub-numbered sections in the Draft Guidance.

1. General remarks applicable to the registration process

(a) Paragraph 148

MIS notes a minor grammatical error in the Paragraph:

148. As defined in Articles 14 and 15 of the Regulation, a credit rating agency shall apply for registration for the purposes of Article 2(1) provided that it is a legal person

established in the Community. The application shall contain information on the matters set out in Annex II.

(b) Paragraph 153

Applicants should be required to demonstrate compliance with the Regulation only and not, in addition to "information contained within this guidance", as reflected in this Paragraph because we believe the Draft Guidance exceeds the scope of the Regulation in a number of instances. During the public hearing held on 23 November 2009, CESR confirmed that the resulting Guidance would only be indicative.

(c) Paragraph 154

We believe that an applicant's subsidiaries which do not produce ratings are not relevant for the purposes of the application. We would propose an amendment, therefore:

154...Where the applicant has subsidiaries which do not produce ratings, ~~detailed~~ information on each of these are not required other than the disclosure in the organisational chart required under paragraph 168.

(d) Paragraph 159

MIS has long established policies that address various areas of our business practices. Some of these policies apply generally to all policies and practices such as the Moody's Code of Professional Conduct. We do not believe it is necessary or effective for these general principles to be repeated in every policy provided there is a policy that addresses the issue through, for example, a general policy. We therefore propose:

159. It is expected that ~~any of~~ the policies and procedures submitted with the application either individually or when read together will:
a. Indicate the person(s) responsible for the approval and maintenance of these policies and procedures.
b. Describe how compliance with these policies and procedures will be enforced and monitored, and the person(s) responsible for this.
c. Describe the measure(s) undertaken in the event of a breach of these policies and procedures.
d. Indicate the procedures, if any, for reporting a material breach of policies and procedures to the competent authorities.

(e) Paragraph 162

MIS confirms its understanding that the inclusion of additional ECAI requirements in the resulting Guidance will not affect any decision in terms of the Regulation and will also not introduce a reassessment of existing ECAIs under the ECAI framework.

2. General guidelines on the information to be submitted

MIS offers no comment.

3. Guidance on requests for Historic Data and Information

MIS is comforted by the confirmation in paragraph 165 that competent authorities will assess an applicant at the time of application and not against the historical conduct

of business. We believe that such an approach is sound in law. As mentioned in the cover letter we do not agree that historical information will be helpful and important in assessing the effectiveness of internal controls and practices of CRAs.

4. General Information (Annex II point 1, 2, 3, 9)

(a) Paragraph 168; Bullet 6-7

It is unclear to MIS why certain requirements in the Draft Guidance create lower disclosure standards for an applicant CRA that is not part of a group of CRAs. While we recognise that a group application may be different in some respects in terms of format, we do not believe that disclosure standards should be lower for a single entity than they are for a group. By way of example it is not clear why only a group applicant must provide information on its parent structure and branches. This information would seem equally relevant for a single entity applicant with or without branches.

We propose the following amendment to bullet 7:

> *Where the applicant is not applying as part of a Group of CRAs an organisational chart of the CRA's group of companies (where applicable), including the legal status, full name and address of all entities within the CRA's group (e.g. parent entity, fellow subsidiaries, subsidiaries, branches). This should include ownership details of each entity within the group. If there is a holding company, please detail all the ownership links within the holding company. [~~and has one or several branches, the full name, legal status and address of each branch~~.]*

5. Business activities (Annex II point 14, 15)

(a) Paragraphs 170 and 171

The Draft Guidance creates lower disclosure standards for an applicant CRA that is not part of a group of CRAs and we refer you to point 4 above. In our view, it is not relevant whether a company other than the applicant is conducting ancillary services and propose the following amendment to bullet 4 of paragraph 171:

> *Where the applicant or its [~~parent company, subsidiaries, fellow subsidiaries or~~] branches are [is] planning to conduct any new ancillary services (non-rating business activity) in the future, a description of the new activity and the timeframe for setting up this new activity.*

6. Class/Type of credit ratings (Annex II point 4)

MIS offers no comment

7. Ownership structure (Annex II point 5)

MIS offers no comment.

8. Organisational structure (Annex II point 6)

The Regulation does not refer to the concept of a "senior rating analyst". Consequently, we believe that the Draft Guidance should seek the disclosure of our "Senior Management", a defined term in the Regulation.

Furthermore, we understand there to be a distinction between ancillary services and non-rating business and would therefore suggest that the bracketed "non-rating business" be deleted from paragraph 177.

9. Corporate governance (Annex II point 6)

(a) Paragraph 179

Since the third bullet under "B. Administrative and/or Supervisory Board" relates to historical information, we have treated this as bracketed text.

Furthermore, we would note that the Regulation does not require an Audit Committee or "Other Committees" to be established and we would propose the deletion of C and D under paragraph 179 on the basis that any such requirement is an extension to the scope of the Regulation.

It is also unclear to which functions the "risk assessment function" and "internal control/audit" would relate to and we refer you to part I of our cover letter since this requirement is an extension to the scope of the Regulation.[5]

10. Policies and procedures to identify and manage and disclose any conflicts of interests (Annex II point 11)

(a) Other information

Annex I Section B(2) requires the disclosure of rated entities and related parties from which a CRA receives more than 5% of its annual revenue as a disclosure standard to guard against conflicts of interest. The information sought under "Other Information" far exceeds any requirement under the Regulation by, firstly setting a new threshold of 3% in terms of revenue and number of ratings and extending this into applicant and Group of CRA level for each "type of credit rating". We believe this will be of little value given the 5% disclosure standard already set by the Regulation. We therefore propose the deletion of "Other Information".

11. Human Resources (Annex II point 8 and 12)

(a) The third bullet of "A" requires the listing of the number of years experience in the *rating industry*. Such information is not typically captured in our databases and MIS would potentially be required to review every analyst's résumé and hold discussions with each analyst which would amount to an extremely onerous requirement with limited value. MIS would be pleased to provide the number of years a lead rating analyst has worked for MIS.

We would also propose the deletion of the requirement to identify the number of rating committee members because this suggests a fixed rating committee. It would be impossible to draw a list of rating committee members because any such list would be dependent on the issuer and/or issuance to be rated. Typically all analysts, excluding those conflicted, within the relevant line of business in a CRA may attend rating committees (although some may not vote) and following enhancements to our process, analysts from other lines of business may also attend rating committees to ensure that all relevant factors are considered in assigning a rating. This makes the determination of the number of rating committee members at MIS fluid. Instead, we

[5] Annex I Section A(4) speaks to an "internal control mechanism" and "effective procedures for risk management" and not the creation of specific functions/divisions.

believe a more meaningful number would be the number of current lead analysts (as a term defined in the Regulation) and propose the following:

Number of lead rating analysts ~~[and rating committee members]~~. This should include further information on:

o seniority/rank

o type of rating analyst (primary vs. surveillance, where relevant)

o ~~[Number of years of experience in the rating industry]~~

o Type of credit rating produced or monitored (corporate, public/sovereign, structured finance). The corporate category should contain detail according to the following industry categories: financial institutions, insurance and corporate issuers.

(b) We would propose the limitation of the exercise under B, C and D to lead analysts only. In its current format, the results of the exercise are likely to be meaningless because of issues of double counting. One deal may be monitored by more than one rating analyst leaving that deal to be double-counted into more than one rating analysts' figures. Since "rating analysts" include support analysts who may be involved in a junior support capacity on a number of transactions, the figures are likely to show these support analysts as holding the most mandates. We would therefore propose the following amendment to "B. Corporate ratings" (with consequential changes to "C. Public finance ratings" and "D. Structured instruments ratings"

Number of corporate obligors rated and being monitored per lead rating analyst.

12. Compensation and performance evaluation arrangements (Annex II point 13)

MIS offers no comment.

13. Description of the procedures and methodologies used to issue and review credit ratings (Annex II point 10)

(a) Paragraph 188 A (Development and review of rating methodologies); bullet 1; sub-bullet 3

We draw your attention to Annex 1 Section E I (5) which requires a "description of models" to be disclosed and not the model itself. We would propose an amendment to this sub-bullet in the following terms:

Procedures for disclosing rating methodologies, descriptions of models and key rating assumptions

(b) Paragraph 188 B (Issuance of ratings)

- Bullet 1 generally - It is unclear why the Draft Guidance does not require the disclosure of the role and responsibilities of the "person approving the rating" as contemplated in the Regulation and as distinct from the rating committee, rating analysts and the rating committee Chair. MIS' internal procedures do not necessarily result in the rating committee and/or rating committee Chair "approving" a rating. The administrative approval amounts to a stand-alone process over and above the rating committee.

- Bullet 1; sub-bullet 1 - MIS rating committees do not create or keep "minutes" for rating committees, however, the content of the analytical process in arriving at the rating is reflected in the rating committee memorandum and, where applicable, the rating committee addendum (which encapsulates the

result and rationale of the committee). We are able to provide a sample of these document types but not a sample of "minutes" of the rating committee.

- Bullet 1, sub-bullet 4 – The uniqueness of an issuer/issuance may require the departure from an otherwise "consistent use of a rating methodology, model or key rating assumption". We therefore suggest adding the words "or is otherwise appropriate" at the end of the sentence. The text would then read as follows:

  Determination of which methodology, models and key rating assumptions to use in issuing a rating and description of how this is being applied consistently or is otherwise appropriate

- Bullet 1; sub-bullet 5. It would be challenging to develop a policy on the determination of minimum information required to initiate and maintain a credit rating in addition to our rating methodologies and we would consider our rating methodologies to speak to this requirement. MIS would therefore propose the deletion of this sub-bullet as it is captured under sub-bullet 4.

  ~~*Determination of minimum information requirements to initiate and maintain a rating (both public and non-public information – where relevant)*~~

- Bullet 1; sub-bullet 6. MIS does not verify information in the sense of conducting a due diligence on the underlying information, and this is not a requirement under the Regulation.[6] From the CESR Open Hearing held on 23 November 2009, we understand that it was not the intention of CESR to extend the scope of the Regulation and create a due diligence obligation for CRAs and that the Guidance would be appropriately amended.

  In our view, the word "analysis" appropriately captures the intent of the Regulation and we propose, therefore, the deletion of the word "verification" from this sub-bullet:

  Collation and [~~,~~] analysis ~~and verification~~ (e.g. representations or warranties [~~and~~] where applicable) of information used to determine a rating, including (where applicable) reliance on analysis by another CRA or other third parties.

  and a consequential amendment under "C. Monitoring of credit ratings" Bullet 1; sub-bullet 3:

  Collation and [~~,~~] analysis ~~and verification~~ (e.g. representations or warranties [~~and~~] where applicable) of information used to monitor a rating, including (where applicable) reliance on analysis by another CRA or other third parties.

14. Description of the procedures and methodologies used to issue and review credit ratings – Disclosure requirements (Annex II point 10)

MIS offers no comment.

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[6] Annex I, Section D II(2) refers to the disclosure of whether a CRA has undertaken any due diligence or whether it has relied upon a third-party assessment:
"A credit rating agency shall state what level of assessment it has performed concerning the due diligence processes carried out at the level of underlying financial instruments or other assets of structured finance instruments. The credit rating agency shall disclose whether it has undertaken any assessment of such due diligence processes or whether it has relied on a third-party assessment, indicating how the outcome of such assessment impacts on the credit rating."

15. Financial Resources (Annex II point 7)

The second and third bullet of paragraph 192 relate to information that is historical in nature and we have read these to be bracketed text.

MIS also notes that it does not prepare financial statements or projections on "Group of CRAs" basis and would treat "where applicable" to mean that this would not be required for the application for registration.

16. Outsourcing (Annex II point 17)

The final bullet of paragraph 194 relates to historical information and we have treated this as bracketed text.

17. Policies on record keeping (no direct reference in Annex II)

MIS offers no comment other than to note that the requirement extends the scope of the Regulation.

18. Business Continuity Planning (no direct reference in Annex II)

The second bullet of paragraph 198 relates to historical information and we have treated this as bracketed text. We note that the requirement extends the scope of the Regulation.

19. Information Systems (no direct reference in Annex II)

It is unclear to MIS why the identity of the senior manager responsible for information systems is required. MIS notes that the Information Systems section is already an extension to the scope of the Regulation and we would question the need for the submission of this information.

20. Expected use of endorsement (Annex II point 16)

As per our arguments above, we do not agree that the application process involves a pre-approval of jurisdiction-specific endorsement decisions or requires the non-EU jurisdiction's *regulation* to meet the endorsement standard contemplated in Article 4(3)(b) of the Regulation. It would also be impractical to address the "objective reason for the credit rating to be elaborated in a third country". Essentially this indicates a per credit rating assessment which would not be achievable *ex ante* but only on an *ex post facto* basis – i.e. a review as to why a certain credit rating was issued out of a non-EU jurisdiction.

We would propose, therefore, the deletion of paragraphs 203-210 since they constitute an extension to the scope of the Regulation.

21. Application for exemptions from certain requirements of the Regulation

MIS offers no comment.

Question 41-42 (paragraphs 214-247)
Guidance for Certification

MIS offers no comment.