**S&P Global Ratings Europe response to ESMA’s Consultation Paper on Guidelines on Internal Controls**

Introduction

S&P Global Ratings Europe Ltd. (“SPGRE”) appreciates the opportunity to submit comments on the Consultation Paper concerning the Guidelines on Internal Controls for Benchmark Administrators, Credit Rating Agencies (“CRAs”) and Market Transparency Infrastructures (“Draft Guidelines”). In this response, reference is made to 2020 Guidelines on Internal Controls for CRAs (“Current Guidelines).

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| Question 1: Do you have any comments on the proposed Guidelines under the section on IC Framework? In providing your comments, please refer to the general principle, component and/or characteristic that you are commenting on. |

CRAs have been subject to the Current Guidelines for five years and have well defined understanding of the segregation of duties. The proposed segregation of duties is set out in 1.3.1, and, for CRAs in footnotes 18 and 33, however, significantly differs from the Current Guidelines. It is not explained why this is the case, and none of the ‘contributing sources’ cited in paragraph specifically addresses segregation of duties at CRAs.

We would like to point out that footnote 18 is almost identical to the proposed segregation of duties in the 2019 Consultation Paper (“2019 CP”) on the Current Guidelines. Specifically, the proposal in the 2019 CP that persons ‘responsible for the development of credit rating methodologies, models or key rating assumptions are not involved in their implementation’ was not retained in the Current Guidelines but is reintroduced here.

Such segregation of duties would have an adverse impact on the quality and robustness of methodologies, for CRAs whose credit rating analysts contribute to the development of methodologies in their areas of expertise. Their specific expertise significantly enhances the quality and robustness of the methodologies they help create. Given that these analysts do not participate in the final approval process of the methodologies they have contributed to, we do not consider their contribution to constitute a conflict of interest or risk. Furthermore, it is important to recall that SPGRE’s credit ratings are determined by credit rating committees, rather than by an individual analyst, thereby further mitigating potential concerns regarding impartiality. We therefore suggest that ESMA retains the current wording concerning the segregation of duties.

We believe that the documented controls and control testing outlined in section 1.3.3 are unnecessarily prescriptive due to the specific items mandated for inclusion in control documentation. Generally, controls should be documented with clear accountability and sufficient detail to facilitate effective monitoring and testing. Furthermore, control activities should be embedded into relevant policies and procedures that responsible functions must adhere to in their day-to-day operations, as referenced in section 1.3.6 and paragraphs 30 and 31 on page 15.

We consider that it is important to note that the requirements set out in section 1.3.3 may be addressed across multiple documents rather than consolidated into a single document, such as policies and procedures, in particular in relation to control documentation and control testing. The procedures and documentation for control testing and the associated control information included in testing documentation may be further divided by the first, second, and third lines of defence, depending on their respective roles and areas of expertise.

It is stated in section 1.3.3 (ii) that the documentation of controls should set out ‘the associated risk(s)’, whereas the Current Guidelines state ‘the associated material risk(s)’. We query why ESMA has broadened the scope of the ‘associated risk(s)’, reverting to the 2019 CP which had also proposed this broader scope. In the Final Report accompanying the Current Guidelines, however, it is stated in paragraph 11 that ‘ESMA has further clarified that the scope of the risk management activities it expects CRAs to carry out should be, at a minimum, those risks that could materially impact a CRA’s ability to meet its obligations under CRAR.’ We therefore suggest that ESMA reverts to the wording of the Current Guidelines.

With respect to the authorisations and approvals set out in section 1.3.5, ‘processes’ are not the only methods that can be used to ensure appropriate authorization or approval authority in our view. We propose the section to read ‘the supervised entity should have authorisation process *or mechanisms* to ensure that only authorised individuals have access to information and tools on a need to know and least privilege basis’.

Furthermore, so as to determine a more precise rather than overly broad scope, we suggest the second sentence focus on *key* rather than ‘all’ business activities. Such an amendment would be appropriate in our view as footnotes 20 and 35 narrowly describes specific activities of CRAs, similar to the Current Guidelines. We therefore suggest this section to be revised to read: ‘The supervised entity should also have processes *or mechanisms* in ~~all~~ *key* business activities to ensure that activities are approved and executed only by staff members acting within the scope of their authority. The supervised entity should also have processes *or mechanisms* in ~~all~~ *key* business activities to ensure that activities are approved and executed only by staff members acting within the scope of their authority.’

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| Question 2: Are there any other comments you wish to raise on this section? |

No.

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| Question 3: Do you have any comments on the proposed Guidelines under this section on IC Functions? In providing your comments, please refer to the general principle, component and/or characteristic that you are commenting on |

No.

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| Question 4: Do you have any comments on ESMA’s approach to proportionality for Internal Control Functions? |

In our view, the principle of proportionality should not only consider the size and scale of the supervised entity but should also consider the relative risk of underlying business processes as identified by the supervised entity. In particular that the type and maturity of control activities may vary depending on the nature, scale and complexity of an underlying business process and its relative risk to the organization.

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| Question 5: Are there any other comments you wish to raise on this section? |

Finally, we note that ESMA does not comment on the application of the Draft Guidelines to entities not yet supervised by ESMA but for which ESMA has been granted a supervisory mandate such as EU Green Bond Standards External Reviewers or ESG Rating Providers as these are not cited as being in scope of the Draft Guidelines. It is stated in paragraph 11 that ESMA takes ‘a consistent approach to its supervisory assessments of internal control practices across the entities it supervises’, and we therefore anticipate that the Guidelines may eventually apply to such entities and any future supervisory mandate.

Beyond the principle of proportionality outlined in section 3.3 of the Draft Guidelines, ESMA should avoid creating unduly burdensome requirements that might go beyond the requirements imposed by the respective legislations under which these industries are regulated. Therefore, before subjecting new industries or actors to the Guidelines, ESMA should conduct a consultation so that the specifies of these activities are appropriately considered.