

## **ESMA Level II Measures and Reports under the CRA Regulation 3 May 2017**

Economic and Monetary Affairs Committee  
European Parliament

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Dear Members of the European Parliament

Ladies and Gentlemen

I would like to thank your Committee for hosting this scrutiny session on level II measures and reports under the CRA Regulation. I am grateful for this opportunity to share with you some of the experience and insights ESMA has gained through its work on these important and challenging items.

In my remarks, I will first provide some context on the CRA Regulation and ESMA's level II work. I will then walk you through the technical standards and advices provided under CRA 3. Finally, I will discuss where we are focusing our policy work in the near future.

To begin, let me start by providing you with a general overview of the credit rating agencies legal framework and related ESMA work. The first CRA regulation, introduced in 2009, was a much-needed piece of EU legislation that, for the first time, established a supervisory framework for this crucial set of financial market participants. This was a key element in addressing the failings that had led to the financial crisis in 2008. It has played, and will continue to play, a key role in ensuring investor protection, financial stability and the smooth functioning of the internal market

ESMA entered onto the scene with the CRA 2 Regulation and became the sole European supervisor for credit rating agencies in 2011. In that initial stage, our priority was to establish ESMA as a credible and effective supervisor of all credit rating agencies registered in the EU.

The level II measures at this point were focused on putting in place the reporting structures and supervisory standards necessary to establish this new regime.

With the introduction of CRA 3 in 2013, we were required to go further both in our supervisory activities and in developing and refining the legal framework for CRAs. In this stage, ESMA was asked to develop technical standards for ambitious and innovative IT platforms as well as technical advice on a number of complex industry-wide issues, with the aim of increasing transparency and investor protection. From this vantage point almost four years later, I am pleased to say that all of the technical standards requested of ESMA have been delivered.

Of all these technical standards, perhaps the most visible to outside observers is the European Ratings Platform. This went live in December 2016. With this website ESMA now hosts a portal that allows consumers and investors to see all credit ratings for any given issuance or entity, for free and in one place. This platform represents a big step forward in improving access to credit rating data and streamlines what had been a difficult and onerous process for investors.

Not as visible but just as important to ensuring investor protection is the technical standard for supervising fees charged by CRAs to their clients. The information now being collected under this standard will enable ESMA to undertake effective oversight of fees charged by credit rating agencies, to check for discriminatory pricing practices, ensure compliance with the principle of fair competition and further mitigate conflicts of interest.

Our final technical standard under CRA 3 sought to establish a platform designed to increase the transparency of Structured Finance Instruments, by means of standardised reporting templates. Although published in the official journal on 2 January 2015 and due to go-live on 2 January this year, the standard was de-facto overtaken by developments, with the Commission's proposal for Simple Transparent and Standard (STS) securitisation Regulation. On a positive note, we anticipate that the work undertaken here will be able to inform any forthcoming level II measures under this new proposal.

In addition to the development of technical standards, ESMA provided the Commission with technical advice on a number of complex areas such as the dynamics within the CRA market and the viability of alternatives to credit ratings. While I will not go into the specific findings of each of these pieces of advice, I would like to pass on some of the key messages.

Regarding over-reliance on credit ratings, as we highlighted in our technical advice, it will be difficult to fully address this issue as long as key pieces of EU legislation maintain references

to credit ratings. At the same time, we feel it is important to recognise the ongoing importance of credit ratings to investors lacking the resources to employ market based pricing measures or other alternatives. For this reason, we have advocated a focus on mitigating mechanistic reliance on credit ratings, rather than their outright replacement.

To ensure this message is effectively embedded, we have worked closely with our colleagues in EBA and EIOPA to develop a set of good supervisory practices for supervisors in this area, which were published in December 2016.

Regarding our Technical Advice on Competition, Choice and Conflicts of Interest in the CRA industry. We have noted that in spite of some of the initiatives introduced in CRA 3, the CRA market in the EU remains concentrated among three or four of the largest CRAs. For our part, we will continue to work with our members to ensure that those provisions intended to encourage competition, function as effectively as possible. Most recently, this has involved developing a supervisory briefing to ensure our members adopt a harmonised approach to the Regulation's provisions for the appointment of smaller CRAs.

I would also like to draw your attention to this technical advice's findings regarding the effectiveness of ESMA's sanctioning powers. In this area, we believe there is scope to refine these powers in order to increase CRA's accountability and ensure a more effective, proportionate and dissuasive sanctioning regime. This could be achieved, for example, if all requirements of the CRA Regulation had a corresponding infringement, and if fines were based on CRA's turnover. We believe such a change is crucial to increasing the credibility of the existing supervisory framework.

Finally, I would like to talk about an area we intend to focus on in the near future. As you will have seen just last month, ESMA issued a Consultation Paper on the revision of its Guidelines on the Endorsement regime for credit ratings in the EU. Endorsement is a regime that allows credit ratings issued by a third-country CRA, and endorsed by an EU CRA, to be used for regulatory purposes in the EU. Given that a substantial proportion of the credit ratings in the EU are introduced through the endorsement regime, the revision of our guidelines by June 2018 is necessary to ensure that these ratings continue to meet the high standards envisaged in the CRA Regulation and expected by ESMA.

To conclude I would like thank you for your interest in ESMA's work under the CRA Regulation. We are committed to the active monitoring of the Regulation's effectiveness in order to ensure



that it continues to deliver a high level of protection for investors and users of ratings, financial stability and the smooth functioning of the single market.

In carrying out this role, we will draw on our supervisory experience and use all available policy tools including, should it be necessary, proposing the revision of existing technical standards.

I look forward to answering any questions you may have.