ROADMAP

Title of the initiative: **Revision of the Regulation on Credit Rating Agencies to entrust exclusive supervisory powers to ESMA**
Type of initiative (CWP/Catalogue/Comitology): **CWP (Non- Strategic)**
Lead DG/contact person/details: **DG MARKT/G3/**
Expected date of adoption of the initiative (month/year): **May 2010**
Date of modification:
Version No:

Initial IA screening & planning of further work

A. Context and problem definition

(i) What is the political context of the initiative? (ii) How does this initiative relate to past and possible future initiatives, and to other EU policies?

The supervisory framework was one of the most difficult subjects in the negotiations of the Regulation on credit rating agencies, successfully concluded on 23 April 2009. The resulting compromise – creating an admittedly complex and heavy structure – has responded to many national sensitivities of the Member States in this matter. The **Conclusions of the European Council of 18-19th June 2009** supported the creation of an ESRC (renamed European Systemic Risk Board, henceforth ESRB) and an ESFS, consisting of three new European Supervisory Authorities. Moreover, the conclusions **emphasised that the European Supervisory Authorities should have direct supervisory powers for credit rating agencies**[1].

The Commission proposal for a Regulation establishing a European Securities and Markets Authority[2] (ESMA) establishes[3] that ESMA shall execute any exclusive supervisory powers over entities with Community-wide reach or economic activities with Community-wide reach entrusted to it in the legislation referred to in its scope of action. It mentions that "for that purpose, the Authority shall have appropriate powers of investigation and enforcement as specified in the relevant legislation, as well as the possibility of charging fees." The "general approach" reached in the ECOFIN Council on 2nd December on the proposal for a Regulation establishing ESMA has confirmed the abovementioned European Council conclusions, although restricting its scope only to CRAs. The European Parliament is currently working on its opinion; in line with the Framework Agreement between the two institutions, the Commission reserves its position pending the delivery of that opinion.

What are the main problems identified?

The following shortcomings of the current supervisory framework for CRAs have been identified:

- CRAs are expected to deal with multiple supervisors within the EU (no "one-stop-shop" for supervised entities)
- Decision-making process for supervisors is heavy and complex
- There are risks of conflicts over competences
- There are risks of divergent and inconsistent application by competent authorities in the Member States
- Resources of individual supervisors fragmented and likely to be inadequate

[1] European Council 18-19 June 2009, Presidency conclusions, p.8, available at: http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/108622.pdf
[2] COM(2009) 503 of 23.9.2009
[3] Article 6(3)

Who is affected?

Credit rating agencies, national supervisors and the future European Securities and Markets Authority.

(i) Is EU action justified on grounds of subsidiarity? (ii) Why can the objectives of the proposed action not be achieved sufficiently by Member States (necessity test)? (iii) As a result of this, can objectives be better achieved by action by the Community (test of EU Value Added)?

The current supervisory model will become operative by end-2010 and was established as a crucial element of the EU compromise solution to address the weaknesses in the CRA sector highlighted by the financial crisis. Accordingly, Community action would be required to make changes to the current framework or to provide for a new system that would respond better to the objective of a stable and single EU financial market for financial services. The solutions discussed will aim at producing a response that will be both effective and efficient, and will seek to respect the principle of subsidiarity.

B. Objectives of EU initiative

What are the main policy objectives?

The CRAs business is a global one: it is difficult to establish where a specific credit rating has been produced or issued; it is nearly impossible to delimit with certainty the territorial impact of a credit rating in use. Moreover, when dealing with a group of CRAs, there may be conflicts of interest and deficiencies in the way ratings are elaborated in the group itself that cannot be assessed at the level of each individual subsidiary. Therefore, it is necessary to develop a holistic approach going beyond the subsidiary level, to set up a single central authority at the EU entrusted with the registration and supervision of CRAs. The combination of:
a) a centralised authorisation/coordination in decision making processes and
b) delegation of tasks
is the most cost-efficient solution (i.e. central authorisation eliminates national discrepancies and delegation of tasks ensures proximity of the supervisor to the CRA).

Having those overall objectives in mind, it should be aimed that any proposed changes in the organisation and functioning of the supervision of CRAs ensure the fulfilment of the following, operational-level objectives:

- Ensuring efficient supervision through the creation of a single point of contact and clear competences among national supervisors
- Ensure a consistent application
- Ensure efficiency gains
- Ensure better alignment of incentives for the supervisory authorities to cope with the pan European activity of supervised entities

The CRA Regulation would be revised in order to introduce centralised oversight of credit rating agencies operating in the EU.

The ESMA would assume general competence in matters relating to the registration and on-going supervision of registered credit rating agencies as well as matters related to ratings issued by rating agencies established in third countries that operate in the EU under the certification or endorsement regimes. Those responsibilities would involve use of administrative measures and sanctions by the European supervisory authority, either directly or with the involvement of the Commission.

Some specific supervisory powers related to the use of credit ratings would remain in the remit of national competent authorities.

As a result of the initiative we expect considerable simplification of the supervisory framework for CRAs. With a single supervisor at the EU level, rating agencies will have only one public authority to interact with in matters of compliance with the CRA Regulation – their costs of compliance should decrease. It also means that the risks of overlapping competences and inconsistent application will be avoided. Substantial efficiency gains are expected as the same functions of surveillance and enforcement will not need to be repeated at the level of each Member State - their freed administrative capacity and resources could thus be directed to other areas of financial supervision. Decision-making on supervision/enforcement matters will be streamlined leading to more effective oversight of CRAs.

Do the objectives imply developing EU policy in new areas or in areas of strategic importance?

There is already legislation in the field of CRAs, however it is a novelty in the financial services sector to entrust an EU central authority with exclusive supervisory and enforcement powers over financial institutions, i.e. CRAs.

C. Options

(i) What are the policy options? (ii) What legislative or 'soft law' instruments could be considered?
(iii) Would any legislative initiatives go beyond routine up-date of existing legislation? Does the action proposed in the options cut across several policy areas or impact on action taken/planned by other Commission departments?

This initiative is strongly linked with the progress on the Commission's legislative proposals to strengthen financial supervision in Europe, currently under negotiation with the Council and the EP. At a later point it may be necessary to adapt our stance on the specific aspects of the reform of CRA supervision, according to the developments on that other file.

The policy options assessed are the following:
- Status quo (current CRA Regulation)
- College structure and ESMA
- ESMA to assume direct oversight of groups of CRAs or all EU-based CRAs, including a sub-option on CRAs (groups of CRAs) with legal presence in more than one Member State and a second one on all EU-based CRAs.

Certain risks are related to the complexity and novel character of the measures that may be proposed (e.g. direct supervisory and enforcement powers for an EU supervisory authority), as the new authority will be entrusted with powers which have not yet been entrusted to other agencies. Those risks are being mitigated by intensified process of early consultations and analyses within DG MARKT and with other Commission services.

Explain how the options respect the proportionality principle

We have taken into account the principle of proportionality in the identification and analysis of options, assessing also the new proposal in the context of smaller national credit rating agencies.

D. Initial assessment of impacts

What are the significant impacts likely to result from each policy option (cf. list of impacts in the Impact Assessment Guidelines pages 32-37), even if these impacts would materialise only after subsequent Commission initiatives?

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The ESMA will need to be adequately structured and resourced to perform the envisaged tasks. In an impact assessment of September 2009 (accompanying proposals related to the new European financial supervisory structure adopted by the Commission) the needs of the ESMA were considered when identifying the optimal solutions in terms of organisation, structure and financing. In particular, the estimated budget of the ESMA in the first year of operation (2011) already included appropriations for "Supervision of entities with a Community-wide reach", referring to the possibility of direct supervision of CRAs by that Authority.

Could the options have impacts on the EU-Budget (above 5 Mio €) and/or should the IA also serve as the ex-ante evaluation, required by the Financial Regulation?

The proposal will have an impact on the EU-Budget, as the ESMA is to be financed in part (40%) by the EU Budget. The Impact Assessment will not serve as an ex-ante evaluation.

Could the options have significant impacts on (i) simplification, (ii) administrative burden or on (iii) relations with third countries?

The registration procedures for CRAs will be streamlined. There will be a reduction of administrative burden to CRAs, as they will have to report only to a central authority. Concerning third countries, it will be easier for CRAs based in third countries to deal with one single supervisor.

E. Planning of further impact assessment work

When will the impact assessment work start?

Work on the IA started in December 2009.

(i) What information and data are already available? (ii) Will this impact assessment build on already existing impact assessment work or evaluations carried out? (iii) What further information needs to be gathered? (iv) How will this be done (e.g. internally or by an external contractor) and by when?
(v) What type and level of analysis will be carried out (cf. principle of proportionate analysis)?

The IA builds on existing impact assessments (e.g. the IA on the original proposal for a Regulation on CRAs and the IA on the proposal to set up the European supervisory authorities).

Which stakeholders & experts have been/will be consulted, how and at what stage?

Preliminary consultation on the desirability of EU-level supervision for CRAs was held in August 2008, on the occasion of tabling the CRA Regulation proposal by the Commission. Work on this proposal benefited from a number of analyses (including the de Larosière report (The High Level Group on financial supervision in the EU of 25.02.2009) and numerous exchanges with stakeholders. Member States and supervisors have been consulted at several stages of the process. CRAs were consulted initially.