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Proposal for a

REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

On amending Regulation (EC) No 1060/2009 on credit rating agencies

{SEC(2010) 678}

{SEC(2010) 679}

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE PROPOSAL

Experience of the financial crisis has exposed important failures in financial supervision, both in particular cases and in relation to the financial system as a whole. The European Commission has piloted a fundamental overhaul of financial supervision in Europe with the objective of establishing a more efficient, integrated and sustainable European system of supervision. This builds on the findings of the group of high level experts, chaired by Mr Jacques de Larosière, former general director of the International Monetary Fund, and mandated by President Barroso to make recommendations to strengthen European supervisory arrangements. The Group presented its report on 25 February 2009 and its recommendations were endorsed by the Commission in its Communication to the Spring European Council of March 2009¹.

The key elements of the reform proposed by the Commission are :

1. Establishing a *European System of Financial Supervisors (ESFS)*, consisting of a network of national financial supervisors working in tandem with new European Supervisory Authorities (ESAs), created by transforming the existing European supervisory committees² in a European Banking Authority (EBA), a European Insurance and Occupational Pensions Authority (EIOPA), and a European Securities and Markets Authority (ESMA), thereby combining the advantages of an overarching European framework for financial supervision with the expertise of local micro-prudential supervisory bodies that are closest to the institutions operating in their jurisdictions, and
2. Establishing a European Systemic Risk Board (ESRB), which shall monitor and assess potential threats to financial stability that arise from macro-economic developments and from developments within the financial system as a whole. To this end, the ESRB would provide an early warning of system-wide risks that may be building up and, where necessary, issue recommendations for action to deal with these risks.

In particular, concerning credit rating agencies, the De Larosière Group was of the view that it would be far more rational to entrust the Committee of European Securities Regulators (CESR) with the task of licensing credit rating agencies in the EU, monitoring their performance, and in the light of this imposing changes.

In its Communication of 27 May 2009 on European Financial Supervision³, the Commission therefore proposed that a European Supervisory Authority should be given the responsibility for the authorisation and supervision of certain entities with pan-European reach, e.g., credit rating agencies. These responsibilities could include such powers as those of investigation, on-site inspections and supervisory decisions. These responsibilities would be defined in the

¹ Commission Communication on Driving European Recovery of 4.3.2009, COM(2009) 114 final

² These are the Committee of European Banking Supervisors (CEBS), the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) and the Committee of European Securities Regulators (CESR).

³ Commission Communication on European Financial Supervision of 27.5.2009, COM(2009) 252 final

Regulation on Credit Rating Agencies⁴ of the European Parliament and of the Council. The Commission's suggestion was endorsed by the European Council at its meeting in June 2009 stating clearly that ESMA "should also have supervisory powers for credit rating agencies"⁵.

Against this background, Article 39 and recital 51 of the Regulation on credit rating agencies of the European Parliament and of the Council (CRA Regulation) state that the current supervisory architecture should not be considered as the long-term solution for the oversight of credit rating agencies and that even if colleges of competent authorities are expected to streamline supervisory cooperation and convergence in this area in the Community, they may not substitute all the advantages of more consolidated supervision of the credit rating industry. The European Parliament and the Council requested the Commission to put forward by 1 July 2010 a report and any legislative proposal needed to tackle the shortcomings identified as regards supervisory coordination and cooperation arrangements.

It is important to note that this proposal does not introduce any changes to the Regulation on credit rating agencies concerning the substantive conditions that CRAs have to fulfil in order to be registered and later on an ongoing basis. Similarly, the conditions under which ratings issued from credit rating agencies located in third countries may be used in the Union (via the endorsement⁶ and certification mechanisms,⁷ as foreseen in the CRA Regulation) are not subject of the proposed amendments but will remain as provided for in the current CRA Regulation.

2. CONSULTATION OF INTERESTED PARTIES

Two open consultations were conducted in the development of the legislative package of proposals on the new European financial supervisory structure, which included elements related to the Regulation on credit rating agencies. Firstly, following the report of the high-level group chaired by Jacques de Larosière and the publication of the 4 March 2009 Commission Communication, the Commission organised a first consultation from 10 March to 10 April 2009 as input to its Communication on Financial Supervision in Europe published on 27 May 2009. A summary of the public submissions received can be found on:

http://ec.europa.eu/internal_market/consultations/docs/2009/fin_supervision/summary_en.pdf

Secondly, from 27 May to 15 July 2009, the Commission organised another consultation round, inviting all interested parties to comment on the more detailed reforms presented in the Communication on Financial Supervision in Europe of 27 May 2009. The responses received were for the greater part supportive of the suggested reforms, with comments on detailed aspects of the proposed ESRB and ESFS. A summary of the public submissions received can be found on:

http://ec.europa.eu/internal_market/consultations/2009/fin_supervision_may_en.htm

⁴ Regulation on Credit Rating Agencies adopted by the European Parliament and the Council on xx September 2009.

⁵ European Council of 18/19. June 2009, Presidency conclusions, N. 20.

⁶ Article 4 (3) of the Regulation on credit rating agencies

⁷ Article 5 of the Regulation on credit rating agencies

3. IMPACT ASSESSMENT

The May Commission Communication on Financial Supervision in Europe was accompanied by an impact assessment analysing the main policy options for establishing the ESFS and ESRB. A second impact assessment has been executed to examine the impact of the proposals related to the new European financial supervisory structure adopted by the Commission in September 2009 which includes also an assessment of the establishment of the European Securities and Markets Authority and changes in the supervisory structure of credit rating agencies. A proportionate impact assessment report has been produced for this proposal. It can be found on:

http://ec.europa.eu/internal_market/securities/agencies/index_en.htm

4. LEGAL ELEMENTS OF THE PROPOSAL

4.1. Legal basis

The proposal is based on Article 114 TFEU.

4.2. Subsidiarity and proportionality

The tasks to be conferred on ESMA are closely linked to the measures put in place as a response to the financial crisis and to those announced in the Commission Communications of 4 March and 27 May 2009. Community action can address the weaknesses highlighted by the crisis and provide a system that is in line with the objective of a stable and single EU financial market for financial services – giving to ESMA the necessary supervisory powers for the registration and oversight of credit rating agencies. The traditional division between the competent authority of the home Member State and the other competent authorities was not considered a long-term solution for the oversight of credit rating agencies given the global nature of credit ratings, which are used throughout the European Union. A more consolidated supervision of the credit rating industry had been considered as more advantageous when the Regulation on Credit Rating Agencies was adopted; however at that moment the existing legal framework was not adequate to create such a structure. The Commission proposal for a Regulation establishing a European Securities and Markets Authority (ESMA) creates the adequate framework to give ESMA the necessary powers to perform the tasks for the registration and oversight of credit rating agencies.

However, as the Regulation covers not only the supervision of credit rating agencies – to be done by ESMA –, but also the supervision of the use of credit ratings by individual entities which are supervised at national level, national supervisors will remain responsible for the supervision of the use of credit ratings by those individual entities. As national supervisors will be able to collect specific information about the use of credit ratings, they should be able, to request ESMA to examine the withdrawal of a credit rating agency's registration or the suspension of the use of credit ratings. However, national competent authorities will not have the power to take supervisory measures towards credit rating agencies where they are in breach of the Regulation.

Moreover, competent authorities will have an obligation to cooperate with ESMA, when ESMA considers it necessary; therefore Member States will have to maintain the competent authorities they have designated under the CRA Regulation. The provisions do not go beyond what is strictly necessary to achieve the objectives pursued. The provisions are in accordance

with the principles of subsidiarity and proportionality as set out in Article 5 of the Treaty, as the objectives of the proposal cannot be sufficiently achieved by the Member States and can therefore be better achieved by the Community.

A Regulation amending the current Regulation is the most appropriate instrument.

4.3. Detailed explanation of the proposal

The Regulation on Credit Rating Agencies is to be revised in order to introduce centralised oversight of credit rating agencies operating in the EU. ESMA is to 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. Therefore, it is necessary to replace throughout the text any reference to competent authorities in charge of the registration and supervision of credit rating agencies by a reference to ESMA. However, some specific supervisory powers related to the use of credit ratings will remain in the remit of national competent authorities. Further, the Commission retains its competence to enforce the Treaties and in particular Title VII Chapter 1 of the Treaty on the Functioning of the European Union regarding the common rules on competition in accordance with the provisions adopted for the implementation of those rules.

4.3.1. Amendments to Title I (Subject matter, scope and definitions)

In order to align the Regulation with the new proposal for a Directive on Alternative Investment Fund Managers, alternative investment funds have been listed in Article 4(1) in order to treat them in the same way as the other EU financial institutions with regard to the use of credit ratings. This implies that in case alternative investment funds use credit ratings for regulatory purposes, those credit ratings must have been issued by a credit rating agency registered or certified under this Regulation.

4.3.2. Amendments to Title II (Issuing of Credit Ratings)

In order to avoid possible conflicts of interest arising for the CRA under the issuer-pays model which are particularly virulent regarding the rating of structured finance instruments, to enhance transparency and to increase competition among CRAs, issuers of structured finance instruments or related third parties should be required to give access to the information which they have given to the CRA they hired for the purpose of rating structured finance instruments to competing CRAs. Provided they satisfy certain organisational and confidentiality conditions, competing CRAs should be given access, upon request, by the rated entity or a related third party to the information given for the purposes of rating structured finance instruments to the CRAs it hires. The competing CRA being granted access to information should not use it for any other purposes than for the rating and should be required to provide a minimum number of unsolicited ratings, in order to ensure that the request for access to this information does not pursue other purposes.

Contrasting to the other substantive requirements in the CRA Regulation which are addressed to credit rating agencies and its staff, this rule imposes disclosure requirements to issuers of structured finance instruments. All registered credit rating agencies will have the possibility to access the information necessary for issuing unsolicited ratings of structured finance instruments. This will lead to more competition in the rating market and increase the number of ratings per instrument so that users of ratings will be able to rely on more than one rating for the same instrument.

The Commission notes that the US (SEC Rule 17g-5 published on 4 December 2009 and coming into force in June 2010) has also introduced a similar system. Given the global role and activities of CRAs, it is necessary to ensure that similar rules are applied to CRAs operating in multiple jurisdictions in order to maintain a level playing field and a sufficient level of competition between CRAs. Furthermore, these new provisions are expected to mitigate conflicts of interests due to the issuers-pay model. In this context, in view of its potential benefits and the fact that they seem to constitute a good practice at international level, the impact in terms of costs of the aforementioned new provisions is likely not to be substantial. Implementing measures are needed to specify further the requirements that a credit rating agency has to fulfil for being granted access to the website, including its capacity to ensure the confidentiality of the data.

4.3.3. Amendments to Title III (Surveillance of credit rating activities)

4.3.3.1. Amendments to Chapter I (Registration procedure) of Title III

As a result of introduction of the new, single supervisory authority for the oversight of credit rating agencies, existing provisions, which envisage a college type of supervisory co-ordination and ultimate, formal decision-making by a competent authority of the home Member State, are to be eliminated. The transfer to ESMA of supervisory competences is expected to better address in the EU framework the challenge of ensuring effective and efficient oversight of those entities that often develop multi-jurisdictional presence and have wide-ranging cross border impact. Consequently, in the context of the proposed centralised EU-level supervision the colleges of supervisors, which were envisaged to streamline supervisory co-operation and convergence, are no longer necessary. The creation of ESMA will improve and streamline the procedure for registration, making it simpler (as a result of eliminating redundant consultation steps between authorities in the college and with CESR) and thus it is possible to reduce the time limits in the different stages of the registration process.

4.3.3.2. Amendments to Chapter II (Surveillance by ESMA) of Title III

In order to facilitate day-to-day application of the Regulation, ESMA should be empowered to propose draft technical standards to be endorsed by the Commission on: (i) the registration process, including on the information set out in Annex II; (ii) the information that the credit rating agency must provide for the application for certification and for the assessment of its systemic importance to the financial stability or integrity of financial markets referred to in Article 5 of the Regulation; and (iii) the presentation of the information, including structure, format, method and period of reporting, that credit rating agencies shall disclose in accordance with Article 11(2) and point 1 of Part II of Section E of Annex I of the Regulation.

In order to ensure sufficient supervisory and enforcement capacity, ESMA is to be empowered to require all necessary information from CRAs and other persons related to credit rating activity. It will be able to start investigations into the potential breaches of the Regulation and in the remit of those it must be able to exercise supervisory powers such as examining records and other relevant material and taking copies/extracts thereof, requiring oral explanations, hearing a person, requiring records of telephone and data traffic. The ESMA must also be able to conduct on-site inspections. The rights of defence of the persons concerned shall be fully respected in the proceedings. In particular, ESMA must give the persons concerned the opportunity of being heard on the matters to which ESMA has taken objection.

4.3.3.3. Amendments to Chapter III (Cooperation between ESMA and competent authorities) of Title III

Competent authorities are to keep the oversight responsibilities regarding the use of credit ratings by the supervised entities (like credit institutions, or insurance undertakings) which employ those credit ratings for regulatory purposes. Those national authorities remain best placed to examine how the supervised entities use credit ratings in their day-to-day activity and to take appropriate action, where necessary.

National supervisory authorities must also contribute to the supervisory activity of ESMA, by ensuring all necessary information exchange and co-operation, which may be required in the exercise of supervisory and enforcement powers of ESMA. They will be able to request ESMA to examine whether the conditions for withdrawal of a credit rating agency's registration are met and to request ESMA to examine the suspension of the use of credit ratings issued by a credit rating agency, which they consider to be in a serious and persistent breach of the Regulation on credit rating agencies.

Where necessary or appropriate for reasons of efficiency, in its supervisory activity ESMA must be able to seek the assistance of a competent supervisory authority at national level. Assistance by competent authorities should be provided when ESMA is carrying out investigations and on site inspections.

ESMA may also delegate specific supervisory tasks to competent national authorities e.g. when supervisory measures have to be undertaken at the remote premises of a CRA or would require knowledge and experience with respect to local conditions, including foreign language skills. Delegation of tasks should be used in order to prevent disproportionate costs for ESMA and the supervised CRAs. Possible tasks that may be delegated include the carrying out of specific investigatory tasks and on-site inspections, the assessment of an application for registration, but also tasks related to day-to-day supervision. Delegation of tasks will not affect the responsibility of ESMA which may give instructions to the authority to which it has delegated a task. ESMA should further specify in guidelines the areas in which it intends to make use of the power to delegate tasks, including the delegation procedures to be applied and any compensation to be granted to the competent authority for carrying out the tasks.

4.3.4. *Amendments to Title IV (Penalties, Committee procedure, reporting and transitional and final provisions)*

4.3.4.1. Amendments to Chapter I (Penalties, Committee procedure and reporting) of Title IV

As the necessary underpinning to its supervisory authority, ESMA may propose to the Commission to impose periodic penalty payments. This coercive measure is to help achieve that: (i) an infringement is put to an end, (ii) complete and correct information which ESMA has requested is supplied; (iii) credit rating agencies and other persons submit to an investigation. ESMA may also propose fines to be adopted by the Commission, where, intentionally or negligently, some of the provisions of the Regulation on credit rating agencies listed in Annex III have been breached. Detailed criteria for establishing the amount of the fines as well as procedural aspects related to fines will be set out in a delegated act.

In addition to proposing sanctions, ESMA shall also be empowered to adopt supervisory measures where a credit rating agency has committed a breach of the Regulation. Those measures include the temporary prohibition of the issuing of credit ratings and the suspension of the use of the credit ratings concerned until the infringement has been put to an end. As a

last resort measure, ESMA is empowered to withdraw the registration of a credit rating agency.

In addition, ESMA has the power to require the credit ratings agencies to bring an infringement to an end and to issue public notices. Those measures shall be applied in cases which do not justify the adoption of a sanction or more severe supervisory measure, taking account of the principle of proportionality. Sanctions, penalty payments and supervisory measures are complementary parts of an effective enforcement regime.

The committee procedures have been aligned with the Lisbon Treaty.

4.3.4.2. Amendments to Chapter II (Transitional and final provisions) of Title IV

Once ESMA will be in place and operational, the competent authorities of the Member States will have to terminate their competences and duties related to the supervisory and enforcement activity in the field of credit rating agencies which had been conferred to them by the Regulation on credit rating agencies.

Clear rules have also to be established for the transmission of files and working documents from competent authorities to ESMA.

5. BUDGETARY IMPLICATION

An overall overview of the budgetary implications of the proposals setting up ESMA was presented in September 2009 in the impact assessment report and accompanying legislative financial statements accompanying such legislative proposals (see the legislative financial statement added to the proposal on the setting up of the European Securities Markets Authority). The specific implications on ESMA concerning the direct supervision and oversight of credit rating agencies are specified in the legislative financial statements accompanying this proposal. Both financial statements are to be considered together. Specific budgetary implications for the Commission are also assessed in the financial statement accompanying this proposal.

The proposal has implications for the Community budget.

Proposal for a

REGULATION (EU) No .../... OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

On amending Regulation (EC) No 1060/2009 on credit rating agencies

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 114 thereof,

Having regard to the proposal from the European Commission⁸,

After transmission of the draft legislative act to the national Parliaments,

Having regard to the opinion of the European Economic and Social Committee⁹,

Acting in accordance with the ordinary legislative procedure¹⁰,

Whereas:

- (1) At the request of the Commission, a report published on 25 February 2009 by a high-level group of experts chaired by J. de Larosière concluded that the supervisory framework of the financial sector in Europe needed to be strengthened to reduce the risk and severity of future financial crises and recommended far-reaching reforms to the structure of supervision, including the creation of a European System of Financial Supervisors, comprising three European Supervisory Authorities, one for the securities sector, one for the insurance and occupational pensions sector and one for the banking sector, and the creation of a European Systemic Risk Board.
- (2) The Commission Communication of 4 March 2009, "Driving European Recovery"¹¹ proposed to bring forward draft legislation creating a European System of Financial Supervisors, and the Commission Communication of 27 May 2009 "European Financial Supervision"¹² provided more detail about the possible architecture of such a new supervisory framework, highlighting the specificity of the supervision of credit rating agencies.
- (3) The European Council, in its conclusions of 19 June 2009, recommended that a European System of Financial Supervisors, consisting of a network of national financial supervisors

⁸ OJ C , , p. .

⁹ OJ C , , p. .

¹⁰ OJ C , , p. .

¹¹ COM(2009) 114 final.

¹² COM(2009) 252 final.

working in tandem with the new European Supervisory Authorities, the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA), and the European Securities and Markets Authority (ESMA), be established aimed at upgrading the quality and consistency of national supervision, strengthening oversight of cross-border groups through the setting up of supervisory colleges and establishing a European single rule book applicable to all financial market participants in the internal market. It stressed that the European Securities and Markets Authority should have supervisory powers for credit rating agencies. Further, the Commission should retain its competence to enforce the Treaties and in particular Title VII Chapter 1 of the Treaty on the Functioning of the European Union regarding the common rules on competition in accordance with the provisions adopted for the implementation of those rules.

- (4) The scope of the European Securities and Markets Authority's action should be clearly defined so that financial market participants can identify the authority competent in the field of activity of credit rating agencies. The European Securities and Markets Authority should assume general competence in matters relating to the registration and on-going supervision of registered credit rating agencies.
- (5) In order to reinforce competition between credit rating agencies, to help avoiding possible conflicts of interest under the issuer-pays model, which are particularly virulent regarding the rating of structured finance instruments, and to enhance transparency and the quality of ratings for structured finance instruments, registered or certified credit rating agencies should have the right to access a list of structured finance instruments that are being rated by their competitors. The information for this rating should be provided by the issuer or a related third party for the purpose of the issuance of unsolicited competing ratings on structured finance instruments. The issuance of such unsolicited ratings should promote the use of more than one rating per structured finance instrument. Access to the websites should only be granted if a credit rating agency is able to ensure the confidentiality of the requested information.
- (6) As credit ratings are used throughout the Union, the traditional distinction between home competent authority and the other competent authorities and the use of a college type of supervisory co-ordination is not the most adequate for the supervision of credit rating agencies. With the setting up of the European Securities and Markets Authority, it is no longer necessary to maintain such a structure. The registration process should be thus streamlined and time limits should be accordingly reduced.
- (7) The European Securities and Markets Authority should be responsible for the registration and on-going supervision of credit rating agencies, however it should not be responsible for the oversight of the users of credit ratings. National competent authorities should thus remain responsible for the supervision of the use of credit ratings by financial institutions and other entities (such as credit institutions, investment firms, insurance undertakings, assurance undertakings, reinsurance undertakings, undertakings for collective investment in transferable securities, institutions for occupational retirement provision and alternative investment funds), which are supervised at national level in the context of the application of other financial services directives, and the use of credit ratings in prospectuses.
- (8) There is a need to introduce an effective instrument to establish harmonised technical standards to facilitate the application of this Regulation in the day to day practice and to ensure a level playing field and an adequate protection of investors and consumers across the Union. As a

body with highly specialised expertise, it is efficient and appropriate to entrust the European Securities and Markets Authority with the elaboration of draft technical standards.

- (9) In the field of credit rating agencies, draft technical standards should be proposed concerning the registration process, the information that the credit rating agency must provide for the application for certification and for the assessment of its systemic importance to the financial stability or integrity of financial markets and the presentation of the information, including structure, format, method and period of reporting, that credit rating agencies shall disclose in accordance with this Regulation. The draft technical standards have to be adopted by the Commission to give them binding legal effect, in accordance with Regulation .../... [ESMA].
- (10) In areas not covered by technical standards, the European Securities and Markets Authority should have the power to issue non-binding guidelines on issues related to the application of this Regulation.
- (11) In order to effectively carry out its duties, the European Securities and Markets Authority should have the right to request all necessary information directly from financial market participants. Member States' authorities should be obliged to assist the European Securities and Markets Authority in enforcing such requests.
- (12) In order to effectively exercise its supervisory powers, the European Securities and Markets Authority should have the right to conduct investigations and on-site-inspections. When exercising its supervisory powers, the European Securities and Markets Authority should give the persons which are subject to proceedings an opportunity of being heard in order to respect their rights of defence.
- (13) Competent authorities should assist and cooperate with the European Securities and Markets Authority. The latter may delegate specific supervisory tasks to competent authorities for instance where a supervisory task requires knowledge and experience with respect to local conditions, which are more easily available at national level. Possible tasks that may be delegated include the carrying out of specific investigatory tasks and on-site inspections, the assessment of an application for registration, but also specific tasks related to day-to-day supervision. The details of such delegation, including the procedures and any compensation to be granted to the national competent authorities should be specified in guidelines.
- (14) It is necessary to ensure that competent authorities are able to request the European Securities and Markets Authority to examine whether the conditions for withdrawal of a credit rating agency's registration are met and to request from the European Securities and Markets Authority the suspension of the use of ratings in case a credit rating agency is considered to be in a serious and persistent breach of the Regulation. The European Securities and Markets Authority should assess the request and take any appropriate measure.
- (15) The European Securities and Markets Authority should be able to propose to the Commission to impose periodic penalty payments. The purpose of those periodic penalty payments should be to achieve that an infringement established by the European Securities and Markets Authority is put to an end, that complete and correct information which the European Securities and Markets Authority has requested is supplied and that credit rating agencies and other persons submit to an investigation. Moreover, for deterrence purposes and to compel credit rating agencies to comply with the Regulation, the Commission should also be able to impose fines, following a request of the European Securities and Markets Authority, where intentionally or negligently,

specific provisions of the Regulation have been breached. The fine shall be dissuasive and proportionate to the nature and seriousness of the breach, the duration of the breach and the economic capacity of the credit rating agency concerned. Detailed criteria for establishing the amount of the fines as well as procedural aspects related to fines should be set out by the Commission in a delegated act. Member States should only remain competent for laying down and implementing the rules on penalties applicable to the infringement of the obligation of financial firms to use, for regulatory purposes only credit ratings issued by credit rating agencies registered in accordance with this Regulation.

- (16) In case of a breach committed by a credit rating agency, the European Securities and Markets Authority should be empowered to take a range of supervisory measures, including, but not limited to, to require the credit rating agency to bring an infringement to an end, to suspend the use of ratings, to temporarily prohibit a credit rating agency from issuing ratings and – as a last resort - to withdraw the registration when the credit rating agency continues to seriously infringe the provision of this Regulation. The supervisory measures should be applied by the European Securities and Markets Authority taking into account the nature and seriousness of the breach and the principle of proportionality. Sanctions, penalty payments and supervisory measures are complementary parts of an effective enforcement regime.
- (17) For reasons of legal certainty, it is appropriate to establish clear transitional measures for the transmission of files and working documents from national competent authorities to the European Securities and Markets Authority.
- (18) The Commission should be empowered to adopt delegated acts in accordance with Article 290 of the Treaty in respect of the amendment and further specification of the criteria for assessing the equivalence of the regulatory and supervisory framework of a third country in order to take into account the developments on financial markets, the adoption of a regulation on fees and the amendment of the annexes.
- (19) Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data applies to the processing of personal data carried out in application of this Regulation by Member States and operators to which this Regulation applies.
- (20) The protection of individuals with regard to the processing of personal data is governed by Regulation (EC) No 45/2001 of the European Parliament and of the Council of 18 December 2000 on the protection of individuals with regard to the processing of personal data by the Community institutions and bodies and on the free movement of such data¹³, which is fully applicable to the processing of personal data for the purposes of this Regulation carried out in application of this Regulation by Union bodies and agencies.
- (21) Since the objectives of the action to be taken, i.e. setting up an efficient and effective supervisory framework for credit rating agencies by entrusting one single supervisory authority with the supervision of rating activities in the Union, providing a single point of contact for credit rating agencies and ensuring the consistent application of the rules, cannot be sufficiently achieved at the Member State level but can be better achieved at the Union level, taking into account the pan European structure and impact of the rating activities to be supervised, the

¹³ OJ L 8, 12.1.2001, p. 1.

Union may adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty on European Union. In accordance with the principle of proportionality, as set out in that Article, this Regulation does not go beyond what is necessary in order to achieve those objectives.

- (22) Supervision of credit rating agencies by ESMA should only start once ESMA has been established. Therefore the applicability of this Regulation shall be deferred until Regulation .../...establishing ESMA has entered into force.
- (23) Regulation (EC) No 1060/2009 on credit rating agencies should therefore be amended accordingly,

HAVE ADOPTED THIS REGULATION:

Article 1
Amendments to Regulation (EC) No 1060/2009

Regulation (EC) No 1060/2009 is amended as follows:

1. Article 4 is amended as follows:

- (a) The first subparagraph of paragraph 1 is replaced by the following:

"Credit institutions as defined in Directive 2006/48/EC, investments firms as defined in Directive 2004/39/EC, insurance undertakings subject to Council Directive 73/239/EEC¹⁴, assurance undertakings as defined in Directive 2002/83/EC of the European Parliament and of the Council¹⁵, reinsurance undertakings as defined in Directive 2005/68/EC of the European Parliament and the Council¹⁶, undertakings for collective investment in transferable securities (UCITS) as defined in Directive 2009/65/EC, institutions for occupational retirement provision as defined in Directive 2003/41/EC and alternative investment funds as defined in Directive 2010/.../EC may use credit ratings for regulatory purposes only if they are issued by credit rating agencies established in the Union and registered in accordance with this Regulation."

- (b) Paragraph 3 is amended as follows:

- (i) Points (b), (c) and (d) are replaced by the following:

"(b) the credit rating agency has verified and is able to demonstrate on an ongoing basis to the European Securities and Markets Authority (hereinafter referred to as "ESMA") that the conduct of credit rating activities by the third-country credit rating agency resulting in the issuing of the credit rating to be endorsed fulfils requirements which are at least as stringent as the requirements set out in Articles 6 to 12;

¹⁴ OJ L 228, 16.8.1973, p. 3.

¹⁵ OJ L 345, 19.12.2002, p. 1.

¹⁶ OJ L 323, 9.12.2005, p. 1.

(c) the ability of ESMA to assess and monitor the compliance of the credit rating agency established in the third country with the requirements referred to in point (b) is not limited;

(d) the credit rating agency makes available on request to ESMA all the information necessary to enable ESMA to supervise on an ongoing basis the compliance with the requirements of this Regulation;"

(ii) Point (h) is replaced by the following:

"(h) there is an appropriate cooperation arrangement between ESMA and the relevant competent authority of the credit rating agency established in a third country. ESMA shall ensure that such cooperation arrangements shall specify at least:

(i) the mechanism for the exchange of information between ESMA and the relevant competent authority of the credit rating agency established in a third country ; and

(ii) the procedures concerning the coordination of supervisory activities in order to enable ESMA to monitor credit rating activities resulting in the issuing of the endorsed credit rating on an ongoing basis."

2. Article 5 is amended as follows:

(a) Paragraph 2 is replaced by the following:

"2. The credit rating agency referred to in paragraph 1 may apply for certification. The application shall be submitted to ESMA in accordance with the relevant provisions of Article 15."

(b) The first subparagraph of paragraph 3 is replaced by the following:

"ESMA shall examine and decide on the application for certification in accordance with the procedure set out in Article 16. The certification decision shall be based on the criteria set out in points (a) to (d) of paragraph 1 of this Article."

(c) Paragraph 4 is replaced by the following:

"4. The credit rating agency referred to in paragraph 1 may also apply to be exempted:

(a) on a case-by-case basis from complying with some or all of the requirements set out in Section A of Annex I and Article 7(4) if the credit rating agency is able to demonstrate that the requirements are not proportionate in view of the nature, scale and complexity of its business and the nature and range of its issuing of credit ratings;

(b) from the requirement of physical presence in the Union where such a requirement would be too burdensome and disproportionate in view of the nature, scale and complexity of its business and the nature and range of its issuing of credit ratings.

An application for those exemptions shall be submitted by the credit rating agency jointly with the application for certification. When assessing that application, ESMA shall take into consideration the size of the applicant credit rating agency referred to in paragraph 1, having regard to the nature, scale and complexity of its business and the nature and range of its

issuing credit ratings, as well as the impact of the credit ratings issued by the credit rating agency on the financial stability and integrity of the financial markets of one or more Member States. On the basis of those considerations, ESMA may grant such exemption to the credit rating agency referred to in paragraph 1."

(d) Paragraph 5 is deleted.

(e) In paragraph 6, the third subparagraph is replaced by the following:

" The Commission shall specify further or amend the criteria set out in points (a), (b) and (c) of the second subparagraph in order to take account of developments on financial markets. Those measures shall be adopted by means of delegated acts in accordance with Article 38a and subject to the conditions of Articles 38b and 38c."

(f) Paragraphs 7 and 8 are replaced by the following:

"7. ESMA shall establish cooperation agreements with the relevant competent authorities of third countries whose legal and supervisory frameworks have been considered equivalent to this Regulation in accordance with paragraph 6. Such arrangements shall specify at least:

(a) the mechanism for the exchange of information between ESMA and the competent authorities of third countries concerned; and

(b) the procedures concerning the coordination of supervisory activities.

8. Articles 20 and 24 shall apply *mutatis mutandis* to certified credit rating agencies and to credit ratings issued by them."

3. Article 6(3) is amended as follows:

(a) The introductory part of the first subparagraph is replaced by the following:

"At the request of a credit rating agency, ESMA may exempt a credit rating agency from complying with the requirements of points 2, 5 and 6 of Section A of Annex I and Article 7(4) if the credit rating agency is able to demonstrate that those requirements are not proportionate in view of the nature, scale and complexity of its business and the nature and range of issue of credit ratings and that:"

(b) The second subparagraph is replaced by the following:

"In the case of a group of credit rating agencies, ESMA shall ensure that at least one of the credit rating agencies in the group is not exempted from complying with the requirements of points 2, 5 and 6 of Section A of Annex I and Article 7(4)."

4. The following Articles 8a and 8b are inserted:

*"Article 8a
Information on structured finance instruments*

1. The issuer of a structured finance instrument or a related third party shall provide to the credit rating agency it appoints, on a password-protected website that it shall manage, all information

necessary for the credit rating agency to initially determine or monitor a credit rating of a structured finance instrument according to the methodology set out in Article 8(1).

2. Where other credit rating agencies registered or certified according to this Regulation request access to the information referred to in paragraph 1, they shall be granted access without delay provided that they meet all of the following conditions:
 - (a) they have the systems and organisational structure in place to ensure the confidentiality of this information;
 - (b) they provide ratings on a yearly basis for at least 10% of the structured finance instruments for which they request access to information referred to in paragraph 1.
3. In order to ensure a coherent application of this Article, the Commission shall adopt in accordance with the regulatory procedure referred to in Article 38(2) detailed rules specifying in particular the conditions of access and the requirements of the website in order to ensure the accuracy and the confidentiality of data and the protection of personal data in accordance with Directive 95/46/EC.

Article 8b
Access to rating information

1. A credit rating agency registered in the Union shall maintain a password-protected website containing:
 - (a) a list of the structured finance instruments for which it is in the process of providing a credit rating, identifying the type of the structured finance instrument, the name of the issuer and the date when the rating process was initiated;
 - (b) a link to the password protected website on which the issuer of the structured finance instrument or a related third party provides the information required under Article 8a(1), as soon as it is in possession of this link.
2. A credit rating agency shall grant access without delay to the password protected website referred to in paragraph 1 to any credit rating agency registered or certified under this Regulation provided that the credit rating agency requesting access complies with the requirements set out in Article 8a (2)."
5. Article 9 is replaced by the following:

"Article 9
Outsourcing

Outsourcing of important operational functions shall not be undertaken in such a way as to impair materially the quality of the credit rating agency's internal control and the ability of ESMA to supervise the credit rating agency's compliance with obligations under this Regulation."

6. Article 10(6) is replaced by the following:

"6. A credit rating agency shall not use the name of ESMA or any competent authority in such a way that would indicate or suggest endorsement or approval by that authority of the credit ratings or any credit rating activities of the credit rating agency."

7. In Article 11, paragraphs 2 and 3 are replaced by the following:

"2. A credit rating agency shall make available in a central repository established by ESMA information on its historical performance data including the ratings transition frequency and information about credit ratings issued in the past and on their changes. A credit rating agency shall provide information to that repository on a standard form as provided for by ESMA. ESMA shall make that information accessible to the public and shall publish summary information on the main developments observed on an annual basis.

3. A credit rating agency shall provide annually to ESMA information relating to matters set out in point 2 of Part II of Section E Annex I."

8. Article 14 is amended as follows:

(a) Paragraph 2 is replaced by the following:

"2. The registration shall be effective for the entire territory of the Union once the registration decision issued by ESMA as referred to in Article 16(3) or Article 17(3) has taken effect."

(b) The second subparagraph of paragraph 3 is replaced by the following:

"A credit rating agency shall, without undue delay, notify ESMA of any material changes to the conditions for initial registration, including any opening or closing of a branch within the Union."

(c) Paragraphs 4 and 5 are replaced by the following:

"4. Without prejudice to Articles 16 or 17, ESMA shall register the credit rating agency if it concludes from the examination of the application that the credit rating agency complies with the conditions for the issuing of credit ratings set out in this Regulation, taking into consideration Articles 4 and 6."

5. ESMA shall not impose requirements regarding registration which are not provided for in this Regulation."

9. Articles 15 to 20 are replaced by the following:

*"Article 15
Application for registration*

1. The credit rating agency shall submit an application for registration to ESMA. The application shall contain information on the matters set out in Annex II.

2. Where a group of credit rating agencies applies for registration, the members of the group shall mandate one of their members to submit all the applications to ESMA on behalf of the group. The mandated credit rating agency shall provide the information on the matters set out in Annex II for each member of the group.
3. A credit rating agency may submit its application in any of the official languages of the Union.
4. Within ten working days of receipt of the application, ESMA shall assess whether the application is complete. If the application is not complete, ESMA shall set a deadline by which the credit rating agency is to provide additional information.

After assessing an application as complete, ESMA shall notify the credit rating agency accordingly.

"Article 16

Examination of the application for registration of a credit rating agency by ESMA

1. ESMA shall, within 30 working days of the notification referred to in the second subparagraph of Article 15(4) examine the application for registration based on the compliance of the credit rating agency with the conditions set out in this Regulation.
2. ESMA may extend the period of examination by fifteen working days, in particular if the credit rating agency envisages either of the following:
 - (a) endorsing credit ratings as referred to in Article 4(3);
 - (b) using outsourcing;
 - (c) exemption from compliance in accordance with Article 6(3).
3. Within 40 working days of the notification referred to in the second subparagraph of Article 15(4), and within 55 working days thereof where paragraph 2 of this Article applies, ESMA shall adopt a fully reasoned registration or refusal decision.
4. The decision issued by ESMA pursuant to paragraph 3 shall take effect on the fifth working day following its adoption.

Article 17

Examination of the applications for registration of a group of credit rating agencies by ESMA

1. ESMA shall, within 40 working days of the notification referred to in the second subparagraph of Article 15(4) examine the applications for registration based on the compliance of those credit rating agencies with the conditions set out in this Regulation.
2. ESMA may extend the period of examination by fifteen working days, in particular if any of credit rating agencies in the group envisages either of the following:

- (a) endorsing credit ratings as referred to in Article 4(3);
 - (b) envisages using outsourcing;
 - (c) exemption from compliance in accordance with Article 6(3).
3. Within 50 working days of the notification as referred to in the second subparagraph of Article 15(4), and within 65 working days thereof where paragraph 2 of this Article applies, ESMA shall adopt fully reasoned individual registration or refusal decisions.
 4. The decisions issued by ESMA pursuant to paragraph 3 shall take effect on the fifth working day following their adoption.

Article 18
Notification of the decision on the registration,
refusal of registration or the withdrawal of registration
of a credit rating agency

1. Within 5 working days of the adoption of a decision under Articles 16, 17 or 20 ESMA shall notify the credit rating agency concerned. Where ESMA refuses to register the credit rating agency or withdraws the registration of the credit rating agency, it shall provide full reasons in its decision.
2. ESMA shall communicate to the Commission and the competent authorities any decision under Article 16, 17 or 20.
3. ESMA shall publish on its website a list of credit rating agencies registered in accordance with this Regulation. That list shall be updated within 5 working days following the adoption of a decision under Articles 16, 17 or 20.

Article 19
Registration and supervisory fees

1. ESMA shall charge fees to the credit rating agencies which shall fully cover ESMA's expenditure necessary for the registration and supervision of credit rating agencies in accordance with this Regulation and the regulation on fees referred to in paragraph 2.
2. The Commission shall adopt by means of delegated acts in accordance with Article 38a a regulation on fees. That regulation shall determine in particular the type of fees and the matters for which fees are due, the amount of the fees and the way in which they are to be paid. The amount of a fee charged to a credit rating agency shall be proportionate to its size and economic strength.

*"Article 20
Withdrawal of registration*

1. ESMA shall withdraw the registration of a credit rating agency where the credit rating agency:
 - (a) expressly renounces the registration or has provided no credit ratings for the preceding six months;
 - (b) has obtained the registration by making false statements or by any other irregular means;
 - (c) no longer meets the conditions under which it was registered; or
 - (d) has seriously or repeatedly infringed the provisions of this Regulation governing the operating conditions for credit rating agencies.
2. The competent authority of a Member State in which credit ratings issued by the credit rating agency concerned are used and which considers that one of the conditions referred to in paragraph 1 has been met may request ESMA to examine whether the conditions for withdrawal of registration are met. If ESMA decides not to withdraw the registration of the credit rating agency concerned, it shall provide full reasons.
3. The decision on the withdrawal of registration shall take immediate effect throughout the Union, subject to the transitional period for the use of credit ratings referred to in Article 24(2)."
10. The title of the Chapter II in Title III is replaced by "Surveillance by ESMA".
11. Article 21 is replaced by the following:

*"Article 21
European Securities and Markets Authority*

1. Without prejudice to Article 25a, ESMA shall ensure that provisions of this Regulation are applied.
2. ESMA shall issue and update guidelines on:
 - (a) the application of the endorsement regime under Article 4(3);
 - (b) the assessment of compliance of credit rating methodologies with the requirements set out in Article 8(3).
 - (c) the cooperation between ESMA and the competent authorities for the purpose of this regulation including the procedures and detail relating to the delegation of tasks.
3. By [nine months after the entry into force of this Regulation.], ESMA shall propose draft technical standards for endorsement by the Commission according to Article 7 of Regulation .../... [ESMA] on:

- (a) the registration process, including on the information set out in Annex II;
 - (b) information that the credit rating agency must provide for the application for certification and for the assessment of its systemic importance to the financial stability or integrity of financial markets referred to in Article 5.
 - (c) the presentation of the information, including structure, format, method and period of reporting, that credit rating agencies shall disclose in accordance with Article 11(2) and point 1 of Part II of Section E of Annex I.
4. ESMA shall publish, annually and for the first time by 1 January 2012, a report on the application of this Regulation. That report shall contain, in particular, an assessment of the implementation of Annex I by the credit rating agencies registered under this Regulation.
5. ESMA shall cooperate with the European Banking Authority established by Regulation .../...¹⁷ and the European Insurance and Pensions Authority established by Regulation .../...¹⁸ and shall consult those Authorities before issuing guidance and proposing draft technical standards referred to in paragraphs 2 and 3."
12. Article 23 is replaced by the following:

*"Article 23
Non interference with content of ratings*

In carrying out their duties under this Regulation, neither ESMA nor any other public authorities of a Member State shall interfere with the content of credit ratings or methodologies."

13. The following Articles 23a, 23b and 23c are inserted:

*"Article 23a
Requests for information*

- 1. ESMA may require credit rating agencies, persons involved in credit rating activities, rated entities and related third parties, third parties to whom the credit rating agencies have outsourced certain functions or activities and persons otherwise related or connected to credit rating agencies or credit rating activities to provide all information that is necessary in order to carry out its duties under this Regulation.
- 2. Where requesting information referred to in paragraph 1, ESMA shall refer to this Article as the legal basis of the request and state the purpose of it, specify what information is required and fix the time-limit within which it is to be provided. It shall also indicate the penalties provided for in Article 36b in case the production of the required information is incomplete or where the answers to questions asked are incorrect or misleading.

¹⁷ OJ L 25, 29.1.2009, p. 23.

¹⁸ OJ L 25, 29.1.2009, p. 28.

3. The persons referred to in paragraph 1 or their representatives and, in the case of legal persons or associations having no legal personality referred to in paragraph 1, the persons authorised to represent them by law or by their constitution shall supply the information requested on behalf of the persons referred to in paragraph 1 concerned. . Representatives shall remain fully responsible if the information supplied is incomplete, incorrect or misleading.

Article 23b
General investigations

1. ESMA may conduct all necessary investigations of persons referred to in Article 23a(1). To that end, the officials and other persons authorised by ESMA shall be empowered:
 - (a) to examine any records, data, procedures and any other material relevant to the execution of its tasks;
 - (b) to take copies of or extracts from such records, data, procedures and other material;
 - (c) to ask for an oral explanation;
 - (d) to summon and hear a person;
 - (e) require records of telephone and data traffic;
 - (f) interview any person for the purpose of collecting information relating to the subject matter of an investigation.
2. The persons referred to in Article 23a(1) shall submit to investigations launched by decision of ESMA. The persons authorised for the purpose of the investigations referred to in paragraph 1 shall exercise their powers upon production of a written authorisation specifying the subject matter and purpose of the investigation. That authorisation shall also indicate the periodic penalty payments provided for in Article 36b in case the production of the required records, data, procedures or any other material is not provided or incomplete or where the answers to questions asked are incorrect or misleading.
3. In good time before the investigation, ESMA shall inform the competent authority of the Member State in whose territory the investigation is to be carried out of the investigation and of the identity of the authorised persons. Officials of the competent authority of the Member State concerned shall, at the request of ESMA, assist those authorised persons to carry out their duties.

Article 23c
On-site inspections

1. In order to carry out its duties under this Regulation, ESMA may conduct all necessary on-site inspections with or without announcement at the premises of persons referred to in Article 23a (1).
2. The officials and other persons authorised by ESMA to conduct an on-site inspection may enter any business premises and land of the persons subject to the investigation decision

adopted by ESMA and shall have all the powers stipulated in Article 23b(1). They shall have also the power to seal any business premises and books or records for the period and to the extent necessary for the inspection.

3. The officials and other persons authorised by ESMA to conduct an on-site inspection shall exercise their powers upon production of a written authorisation specifying the subject matter and purpose of the inspection and the periodic penalty payments provided for in Article 36b in case the persons concerned do not submit to the inspection. In good time before the inspection, ESMA shall give notice of the inspection to the competent authority of the Member State in whose territory it is to be conducted.
4. The persons referred to in Article 23a(1) shall submit to on-site inspections ordered by decision of ESMA. The decision shall specify the subject matter and purpose of the inspection, appoint the date on which it is to begin and indicate the periodic penalty payments provided for in Article 36b. The ESMA shall take such decisions after consulting the competent authority of the Member State in whose territory the inspection is to be conducted.
5. Officials of, as well as those authorised or appointed by the competent authority of the Member State in whose territory the inspection is to be conducted shall, at the request of ESMA, actively assist the officials and other persons authorised by ESMA. To this end, they shall enjoy the powers set out in paragraph 2.
6. ESMA may also require competent authorities of the Member States to carry out specific investigatory tasks and on-site inspections as provided for in this Article and in Article 23b(1) on its behalf. To this end, competent authorities shall enjoy the same powers as ESMA as set out in this Article and in Article 23b(1).
7. Where the officials and other accompanying persons authorised by ESMA find that a person opposes an inspection ordered pursuant to this Article, the Member State concerned shall afford them the necessary assistance, requesting where appropriate the assistance of the police or of an equivalent enforcement authority, so as to enable them to conduct their on-site inspection.
8. If the assistance provided for in paragraph 7 requires authorisation from a judicial authority according to national rules, such authorisation shall be applied for including by anticipation.
9. Where authorisation as referred to in paragraph 8 is applied for, the national judicial authority shall control that the ESMA decision is authentic and that the coercive measures envisaged are neither arbitrary nor excessive having regard to the subject matter of the inspection. In its control of the proportionality of the measures, the national judicial authority may ask ESMA for detailed explanations, in particular on the grounds ESMA has for suspecting infringement of this Regulation, as well as on the seriousness of the on-site inspection and on the nature of the involvement of the person concerned. However, the national judicial authority may not call into question the necessity for the inspection as such nor demand that it be provided with the information in ESMA's file. The lawfulness of ESMA's decision shall be subject to review only by the Court of Justice following the procedure set out in Regulation XX/2010 [ESMA]".

14. Articles 24 and 25 are replaced by the following:

*"Article 24
Supervisory measures by ESMA*

1. Where there is one of the breaches listed in Annex III committed by a registered credit rating agency, ESMA shall take one or more of the following decisions:
 - (a) withdraw the registration of that credit rating agency in accordance with Article 20;
 - (b) temporarily prohibit that credit rating agency from issuing credit ratings with effect throughout the Union, until the infringement has been brought to an end;
 - (c) suspend the use, for regulatory purposes, of the credit ratings issued by that credit rating agency with effect throughout the Union, until the infringement has been brought to an end;
 - (d) require the credit rating agency to bring the infringement to an end;
 - (e) require the issuer of structured finance instruments or the related third party to provide access to credit rating agencies requesting it to the website it manages according to Article 8a(1);
 - (f) issue public notices.
2. Where taking the decisions referred to in points (b) to (f) of paragraph 1, ESMA shall take into account the nature and seriousness of the breach, including:
 - (i) the duration and frequency of the breach;
 - (ii) whether the breach has revealed serious or systemic weaknesses in the credit rating agency's procedures or of the management systems or internal controls;
 - (iii) whether financial crime was facilitated, occasioned or otherwise attributable to the breach;
 - (iv) the loss or risk of loss caused to investors.

In addition, ESMA may refer matters for criminal prosecution to the relevant national authorities.
3. Credit ratings may continue to be used for regulatory purposes following the adoption of measures in points (a) and (c) of paragraph 1 during a period not exceeding:
 - (a) ten working days if there are credit ratings of the same financial instrument or entity issued by other credit rating agencies registered under this Regulation; or
 - (b) three months if there are no credit ratings of the same financial instrument or entity issued by other credit rating agencies registered under this Regulation.

ESMA may extend the period referred to in point (b) of the first subparagraph by three months in exceptional circumstances relating to the potential for market disruption or financial instability.

4. Without prejudice to Article 20, ESMA shall communicate any decision taken pursuant to paragraph 1, without undue delay, to the competent authorities and the Commission and it shall publicly disclose any such decision on its website within 5 working days from the date when it was taken."

Article 25

Hearing of the persons concerned

1. Before taking decisions as provided for in Article 24(1) ESMA shall give the persons which are the subject of the proceedings the opportunity of being heard on the matters to which ESMA has taken objection. ESMA shall base its decisions only on objections on which the parties concerned have been able to comment.

The obligation referred to in the first subparagraph does not apply if urgent action is needed in order to prevent significant damage to the financial system in which case ESMA may adopt interim decisions. In such a case ESMA has to give the persons concerned the opportunity of being heard as soon as possible after having taken its decision.

2. The rights of defence of the persons concerned shall be fully respected in the proceedings. They shall be entitled to have access to ESMA's file, subject to the legitimate interest of other persons in the protection of their business secrets. The right of access to the file shall not extend to confidential information and internal documents of ESMA."
15. The title of Chapter III in Title III is replaced by the following: "Cooperation between ESMA and Competent Authorities"
16. The following Article 25a is inserted:

"Article 25a

Competent authorities responsible for the supervision and enforcement of Article 4(1) (the use of credit ratings)

1. The competent authorities shall be responsible for the supervision and enforcement of Article 4(1).
2. In order to carry out their duties with regard to the establishment of any breach of Article 4(1), the competent authorities shall, in conformity with national law, have all the supervisory and investigatory powers that are necessary for the exercise of their functions. They shall exercise their powers:
 - (a) directly;
 - (b) in collaboration with other authorities, including ESMA; or
 - (c) by application to the competent judicial authorities.

3. In order to carry out their duties with regard to the establishment of any breach of Article 4(1), the competent authorities shall, in conformity with national law, have the power in their supervisory capacity to:
 - (a) access any document in any form and to receive or take a copy thereof;
 - (b) demand information from any person and if necessary to summon and question a person with a view to obtaining information;
 - (c) carry out on-site inspections with or without announcement; and
 - (d) require records of telephone and data traffic."
17. Articles 26 and 27 are replaced by the following:

*"Article 26
Obligation to cooperate*

ESMA and the competent authorities shall cooperate where it is necessary for the purposes of this Regulation.

*Article 27
Exchange of information*

1. The competent authorities shall, without undue delay, supply the ESMA and each other with the information required for the purposes of carrying out their duties under this Regulation.
 2. ESMA may transmit to the competent authorities responsible for supervising the undertakings referred to in Article 4(1), central banks, the European System of Central Banks and the European Central Bank, in their capacity as monetary authorities, the European Systemic Risk Board and, where appropriate, to other public authorities responsible for overseeing payment and settlement systems, confidential information intended for the performance of their tasks. Similarly, such authorities or bodies shall not be prevented from communicating to ESMA information that ESMA may need in order to carry out its duties under this Regulation."
18. Articles 28 and 29 are deleted.
 19. Articles 30, 31 and 32 are replaced by the following:

*"Article 30
Delegation of tasks from ESMA to competent authorities*

ESMA may delegate specific supervisory tasks to the competent authority of a Member State. Those supervisory tasks may in particular include information requests in accordance with Article 23a and investigations and on-site inspections in accordance with Article 23c(6).

Delegation of tasks shall not affect the responsibility of ESMA.

Article 31
Notifications and suspension requests by competent authorities

1. Where a competent authority is convinced that acts contrary to the provisions of this Regulation are being, or have been, carried out on its territory or on the territory of another Member State, it shall give notice of that fact in as specific manner as possible to ESMA.

ESMA shall take appropriate action. It shall inform the notifying competent authority of the outcome and, so far as possible, of significant interim developments.

2. Without prejudice to the duty to notify set out in paragraph 1, where the notifying competent authority considers that a registered credit rating agency, whose credit ratings are used within its territory breaches the obligations arising from this Regulation and the breaches are sufficiently serious and persistent to have a significant impact on the protection of investors or stability of the financial system in that Member State, the notifying competent authority may request ESMA to impose suspension of the use of credit ratings of the credit rating agency concerned for regulatory purposes by persons referred to in Article 4(1). The notifying competent authority shall provide ESMA with full reasons for its request.

In case ESMA considers that the request is not justified, it shall inform the notifying competent authority. In case ESMA considers that the request is justified, it shall take appropriate measures to resolve this issue.

Article 32
Professional secrecy

1. The obligation of professional secrecy shall apply to all persons who work or who have worked for ESMA, and for the competent authorities or for any other person to whom ESMA has delegated tasks, including auditors and experts contracted by ESMA. Information covered by professional secrecy shall not be disclosed to another person or authority except where such disclosure is necessary for legal proceedings.
2. All the information exchanged under this Regulation between ESMA, the competent authorities and other authorities and bodies mentioned in Article 27(2) shall be considered confidential, except where ESMA or the competent authority or other authority or body concerned states at the time of communication that such information may be disclosed or where such disclosure is necessary for legal proceedings."
20. Article 33 is deleted.
21. Articles 34 and 35 are replaced by the following:

"Article 34
Agreement on exchange of information

ESMA may conclude cooperation agreements on exchange of information with the competent authorities of third countries only if the information disclosed is subject to guarantees of professional secrecy which are at least equivalent to those set out in Article 32.

Such exchange of information shall be intended for the performance of the tasks of those competent authorities.

With regard to transfer of personal data to a third country, ESMA shall apply Regulation (EC) No 45/2001.

Article 35

Disclosure of information from third countries

ESMA may disclose the information received from competent authorities of third countries only if ESMA has obtained the express agreement of the competent authority that has transmitted the information and, where applicable, the information is disclosed only for the purposes for which that competent authority gave its agreement or where such disclosure is necessary for legal proceedings."

22. In Chapter 1 of Title IV, the title is amended as follows:

"Penalties, fines, periodic penalty payments, committee procedure, delegated powers and reporting"

23. In Article 36, the first subparagraph is amended as follows:

"1. Member States shall lay down the rules on penalties applicable to infringements of the provisions of Article 4(1) of this Regulation and shall take all measures necessary to ensure that they are implemented. The penalties provided for shall be effective, proportionate and dissuasive."

24. The following Articles 36a to 36d are inserted:

"Article 36a

Fines

1. At ESMA's request, the Commission may by decision impose on a credit rating agency a fine where, intentionally or negligently, the credit rating agency has committed one of the breaches listed in Annex III.
2. The fines referred to in paragraph 1 shall be dissuasive and proportionate to the nature and seriousness of the breach, the duration of the breach and the economic capacity of the credit rating agency concerned. The amount of the fine shall not exceed 20% of the annual income or turnover of the credit rating agency of the preceding business year.
3. Notwithstanding paragraph 2, where the credit rating agency has directly or indirectly gained a quantifiable financial benefit from the breach, the amount of the fine has to be at least equal to that benefit.
4. The Commission shall adopt by means of delegated acts in accordance with Article 38a detailed rules for the implementation of this Article, specifying in particular:
 - (a) detailed criteria for establishing the amount of the fine;
 - (b) the procedures for enquiries, associated measures and reporting, as well as rules of procedure for decision-making, including provisions on rights of defence, access to file,

legal representation, confidentiality and temporal provisions and the quantification and collection of fines.

Article 36b

Periodic penalty payments

1. At ESMA's request, the Commission may, by decision, impose on the persons referred to in Article 23a(1) periodic penalty payments in order to compel them:
 - (a) to put an end to an infringement, in accordance with a decision taken pursuant to Article 24(1)(d);
 - (b) to supply complete and correct information which has been requested by decision pursuant to Article 23a;
 - (c) to submit to an investigation and in particular to produce complete records, data, procedures or any other material required and to complete and correct other information provided in an investigation launched by decision taken pursuant to Article 23b;
 - (d) to submit to an on-site inspection ordered by decision pursuant to Article 23c.
2. The periodic penalty payments provided for shall be effective and proportionate. The amount of the periodic penalty payments shall be imposed for each day of delay. It shall not exceed 5% of the average daily turnover in the preceding business year and shall be calculated from the date stipulated in the decision.

Article 36c

Hearing of the persons concerned

1. Before taking decision on a fine or periodic penalty payment as provided for in Articles 36a and 36b, the Commission shall give the persons which are the subject of the proceedings the opportunity of being heard on the matters to which the Commission has taken objection. The Commission shall base its decisions only on objections on which the parties concerned have been able to comment.
2. The rights of defence of the persons concerned shall be fully respected in the proceedings. They shall be entitled to have access to the Commission's file, subject to the legitimate interest of other persons in the protection of their business secrets. The right of access to the file shall not extend to confidential information and internal documents of the Commission."

Article 36d

Provisions common to fines and periodic penalty payments

1. The Commission shall disclose to the public every fine and periodic penalty payment that has been imposed according to Articles 36a and 36b.
2. Fines and periodic penalty payments imposed pursuant to Articles 36a and 36b are of an administrative nature.

Article 36e
Review by the Court of Justice

The Court of Justice shall have unlimited jurisdiction to review decisions whereby the Commission has fixed a fine or imposed a periodic penalty payment. It may annul, reduce or increase the fine or periodic penalty payment imposed."

25. Articles 37 and 38 are replaced by the following:

"Article 37
Amendments to Annexes

The Commission may amend the Annexes by means of delegated acts in accordance with Article 38a and subject to the conditions of Articles 38b and 38c in order to take account of developments, including international developments, on financial markets, in particular in relation to new financial instruments.

Article 38
Committee procedure

1. The Commission shall be assisted by the European Securities Committee established by Commission Decision 2001/528/EC¹⁹.
 2. Where reference is made to this paragraph, Article 5 and Article 7 of Decision 1999/468/EC shall apply, having regard to the provisions of Article 8 thereof.
 3. The period laid down in Article 5(6) of Decision 1999/468/EC shall be set at three months."
26. The following Articles 38a, 38b and 38c are inserted:

"Delegating powers

Article 38a
Exercise of the delegation

1. The powers to adopt the delegated acts referred to in the third subparagraph of Article 5(6), Article 19(2), Article 36a(4) and Article 37 shall be conferred on the Commission for an indeterminate period of time.
2. As soon as it adopts a delegated act, the Commission shall notify it simultaneously to the European Parliament and to the Council.
3. The powers to adopt delegated acts are conferred on the Commission subject to the conditions laid down in Articles 38b and 38c.

¹⁹ OJ L 191, 13.7.2001, p. 45.

Article 38b
Revocation of the delegation

1. The delegation of power referred to in the third subparagraph of Article 5 (6), Article 19(2), Article 36a(4) and Article 37 may be revoked at any time by the European Parliament or by the Council.
2. The institution which has commenced an internal procedure for deciding whether to revoke the delegation of power shall inform the other legislator and the Commission at the latest one month before the final decision is taken, stating the delegated powers which could be subject to revocation and the reasons for a revocation.
3. The decision of revocation shall put an end to the delegation of the powers specified in that decision. It shall take effect immediately or at a later date specified therein. It shall not affect the validity of the delegated acts already in force. It shall be published in the *Official Journal of the European Union*.

Article 38c
Objections to delegated acts

1. The European Parliament and the Council may object to the delegated act within a period of two months from the date of notification. At the initiative of the European Parliament or the Council this period shall be extended by one month.
2. If, on expiry of that period, neither the European Parliament nor the Council has objected to the delegated act the delegated act shall enter into force at the date stated therein.

The delegated act may be published in the *Official Journal of the European Union* and enter into force before the expiry of that period if the European Parliament and the Council have both informed the Commission of their intention not to raise objections.

3. If the European Parliament or the Council objects to the adopted delegated act, it shall not enter into force. The institution which objects shall state the reasons for objecting to the delegated act."
27. Article 39 is amended as follows:
- (a) Paragraph 2 is deleted.
 - (b) Paragraph 3 is replaced by the following:
- "3. By 1 July 2011, the Commission shall, in the light of developments in the regulatory and supervisory framework for credit rating agencies in third countries, present a report to the European Parliament and to the Council concerning the effects of those developments and of the transitional provisions referred to in Article 40 on the stability of financial markets in the Union."

28. The third paragraph of Article 40 is replaced by the following:

"Existing credit rating agencies may continue issuing credit ratings which may be used for regulatory purposes by the financial institutions referred to in Article 4(1) unless registration is refused. Where registration is refused, Article 24(2) and (3) shall apply".

29. The following Article 40a is inserted:

*"Article 40a
Transitional measures related to ESMA*

1. All competences and duties related to the supervisory and enforcement activity in the field of credit rating agencies, which were conferred to the competent authorities of the Member States, whether acting as competent authorities of the home Member State or not, and their colleges where those have been established, shall be terminated on [*one month after the entry into force of this Regulation*].
 2. Any files and working documents related to the supervisory and enforcement activity in the field of credit rating agencies, including any on-going examinations and enforcement actions shall be taken over by ESMA on ... [*one months after the entry into force of this Regulation*].
 3. The competent authorities and colleges referred to in paragraph 1 shall ensure that any existing records and working papers shall be transferred to ESMA [*one month after the entry into force of this Regulation*]. Those competent authorities and colleges shall also render all necessary assistance and advice to ESMA to facilitate effective and efficient transfer and taking up of supervisory and enforcement activity in the field of credit rating agencies.
 4. ESMA shall act as the legal successor of competent authorities and colleges referred to in paragraph 1 in any administrative or judicial proceedings that result from supervisory and enforcement activity pursued under this Regulation prior to [*one month after the entry into force of this Regulation*].
 5. Where judicial review of a decision, which was taken by a competent authority referred to in paragraph 1 under this Regulation, is on-going on [*one month after the entry into force of this Regulation*], the case shall be transferred to the General Court, unless the judgement of the court reviewing that decision in the Member State is to be rendered within two months after [*one month after the entry into force of this Regulation*]."
30. Annex I is amended in accordance with Annex I to this Regulation.
31. A new Annex III is added as set out in Annex II to this Regulation.

*Article 2
Entry into force*

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States from the day of entry into force of the Regulation .../... [ESMA].

Done at Brussels,

For the European Parliament
The President

For the Council
The President

Annex I

Annex I to Regulation (EC) No 1060/2009 is amended as follows:

1. In Section A, the last subparagraph of point 2 is replaced by the following:

"Opinions of the independent members of administrative or supervisory board issued on the matters referred to in points (a) to (d) shall be presented to the board periodically and shall be made available to ESMA on request."

2. In Section B , the first subparagraph of point 8 is replaced by the following:

"Records and audit trails referred to in point 7 shall be kept at the premises of the registered credit rating agency for at least five years and be made available upon request to ESMA."

Annex II

The following Annex III is added to Regulation (EC) No 1060/2009:

"ANNEX III

SANCTIONS

Breaches

- I. *Breaches related to conflicts of interest, organisational or operational requirements*
- a) The CRA infringes Article 6(2) in connection with Annex I Section B point 3 by issuing a credit rating or in the case of an existing credit rating by not disclosing immediately that the credit rating is potentially affected in the situations described in point 3 (a) to (d).
 - b) The CRA infringes Article 6(2) in connection with Annex I Section B point 4 first subparagraph by providing consultancy or advisory services.
 - c) The CRA infringes Article 6 (2) in connection with Annex I Section B point 4 third subparagraph by not ensuring that the provision of an ancillary service does not present a conflict of interest with its credit rating activity
 - d) The CRA infringes Article 4(3) by endorsing a credit rating issued in a third country without the conditions as listed in Article 4(3)(a) to (h) being satisfied
 - e) The CRA infringes Article 6(2) in connection with Annex I Section A point 2 third subparagraph by not appointing the required number of independent members of the administrative or supervisory board.
 - f) The CRA infringes Article 6(2) in connection with Annex I Section A point 2 fourth subparagraph first or second sentence by setting a compensation system for independent members linked to the business performance of the CRA or by setting the term of office for a period exceeding five years.
 - g) The CRA infringes Article 6(2) in connection with Annex I Section A point 6 by not ensuring that the conditions enabling the compliance function to discharge its responsibilities properly and independently as defined in Annex I Section A point 6 (a) to (d) are satisfied.
 - h) The CRA infringes Article 7(2) by not ensuring that a person mentioned in that Article initiates or participates in negotiations regarding fees or payments.
 - i) The CRA infringes Article (3) in connection with Annex I Section C point 1 by not ensuring that a relevant person does not buy or sell or engage in a transaction with an affected financial instrument.
 - j) The CRA infringes Article 7(3) in connection with Annex I Section C point 2 by not ensuring that a relevant person does not participate or influences the determination of a credit rating.

- k) The CRA infringes Article 7(3) in connection with Annex I Section C point 3(b), (c) and (d), by not ensuring that a relevant person does not disclose or use or share confidential information.
- l) The CRA infringes Article 7(3) in connection with Annex I Section C point 4 by not ensuring that a relevant person does not solicit or accept money, gifts or favours.
- m) The CRA infringes Article 7(3) in connection with Annex I Section C point 7 by not ensuring that a relevant person does not take up a key management position.
- n) The CRA infringes Article 7(4) in connection with Annex I Section C point 8(a) by not ensuring that the lead rating analyst is not involved in credit rating activities related to the same rated entity or its related third parties for a period exceeding four years.
- o) The CRA infringes Article 7(4) in connection with Annex I Section C point 8(b) by not ensuring that the rating analyst is not involved in credit rating activities related to the same rated entity or its related third parties for a period exceeding five years.
- p) The CRA infringes Article 7(4) in connection with Annex I Section C point 8(c) by not ensuring that a person approving credit ratings is not involved in credit rating activities related to the same rated entity or its related third parties for a period exceeding seven years.
- q) The CRA infringes Article 7(4) in connection with Annex I Section C point 8 second subparagraph by not ensuring that a relevant person is not involved in credit rating activities within two years of end of the periods mentioned.
- r) The CRA infringes Article 7(5) by introducing compensation and performance evaluation contingent on the amount of revenue that the CRA derives from the rated entities or related third parties.
- s) The CRA infringes Article 8(5) by not monitoring its credit ratings or by not reviewing its credit ratings or methodologies on an ongoing basis and at least annually.
- t) The CRA infringes Article 8(6) b) by not or not timely reviewing the affected credit ratings when methodologies, models or key rating assumptions are changed
- u) The CRA infringes Article 8(6)(c) by not re-rating a credit rating if the overall combined effect of the changes of the methodologies, models or ratings assumptions affects this credit rating.
- v) The CRA which requests access to the website of an issuer of a structured finance instrument or a related third party infringes Article 8a(2)(a) if it does not have the systems and the organisational structure in place to ensure the confidentiality of the information thus obtained.
- w) The CRA infringes Article 8a(2)(b) where it fails to provide, on a yearly basis, ratings for at least 10% of the structured finance instruments for which it has requested access to the information on the website provided by the issuer or related third party.
- x) The CRA infringes Article 10(2) in connection with Annex I Section D Part I point 4 second paragraph by issuing a credit rating or not withdrawing an existing rating.

II. *Breaches related to obstacles to the supervisory activities*

- a) The CRA infringes Article 6(2) in connection with Annex I Section B point 7(a) to (h) by not arranging for records or audit trails as required by these provisions.
- b) The CRA infringes Article 6(2) in connection with Annex I Section B point 8 first subparagraph by not keeping records or audit trails for at least five years or by not making available those records or audit trails to the competent authorities.
- c) The CRA infringes Article 6(2) in connection with Annex I Section B point 9 by not retaining the records for the duration of the relationship with the rated entity or its related third party.
- d) The CRA infringes Article 11(2) by not making available the required information or by not providing that information in the required format.
- e) The CRA infringes Article 11(3) in connection with Annex I Section E Part II point 2 by not providing the required lists.
- f) The CRA infringes the second subparagraph of Article 14(3) by not or not timely notifying ESMA of any material changes to the conditions for initial registration.

III. *Breaches related to disclosure provisions*

- a) The CRA infringes Article 6(2) in connection with Annex I Section B point 2 by not disclosing the names of the rated entities or related third parties from which it receives more than 5 % of its annual revenue.
- b) The CRA infringes Article 6(2) in connection with Annex I Section B point 4 third subparagraph by not disclosing in the final report an ancillary service provided for the rated entity or its related third party.
- c) The CRA infringes Article 8(1) by not disclosing the methodologies, models and key rating assumptions it uses in its credit rating activities.
- d) The CRA infringes Article 8(6) a) by not disclosing immediately the likely scope of affected credit ratings when methodologies, models or key rating assumptions are changed.
- f) The CRA infringes Article 8b(1) by not disclosing immediately on the password-protected website the information according to Article 8b(1)(a) and (b).
- g) The CRA infringes Article 8b(2) by not granting access to the website to registered or certified credit rating agencies fulfilling the conditions of Article 8a(2).
- h) The issuer of a structured finance instrument or a related third party infringes Article 8a(2) by not providing access to the password-protected website that it manages to credit rating agencies fulfilling the conditions under Article 8 a(2).
- i) The CRA infringes Article 8a(2) by imposing on the issuer or the related third party any provisions aiming at preventing access to the website to any credit rating agencies requesting it and fulfilling the conditions under Article 8a(2).

- j) The CRA infringes Article 10(2) in connection with Annex I Section D Part I point 1, point 2((a) to (e), point 4 first subparagraph or point 5 or Part II points 1, 2, 3 or 4 by not providing the information as required by these provisions when presenting a rating.
- k) The CRA infringes Article 10(2) in connection with Annex I Section D Part I point 3 by not informing the rated entity at least 12 hours before publication of the credit rating.
- l) The CRA infringes Article 10(3) by not ensuring that an additional symbol is used which distinguishes credit ratings for structured finance instruments from other credit ratings.
- m) The CRA infringes Article 10(4) by not disclosing its policies and procedures regarding unsolicited credit ratings.
- n) The CRA infringes Article 10(5) by not providing the information as required by this Article or by not identifying an unsolicited credit rating.
- o) The CRA infringes Article 11(1) by not disclosing or updating information relating to matters set out in Annex I, Part I, Section E.
- p) The CRA infringes Article 12 by not or not timely publishing a transparency report including information set out in Part III of section E of Annex I."

LEGISLATIVE FINANCIAL STATEMENT

to be used for any proposal or initiative submitted to the legislative authority

(Articles 28 of the Financial Regulation and 22 of the implementing rules)

1. FRAMEWORK OF THE PROPOSAL/INITIATIVE

- 1.1. Title of the proposal/initiative
- 1.2. Policy area(s) concerned in the ABM/ABB structure
- 1.3. Nature of the proposal/initiative
- 1.4. Objective(s)
- 1.5. Grounds for the proposal/initiative
- 1.6. Duration and financial impact
- 1.7. Management method(s) envisaged

2. MANAGEMENT MEASURES

- 2.1. Monitoring and reporting rules
- 2.2. Management and control system
- 2.3. Measures to prevent fraud and irregularities

3. ESTIMATED FINANCIAL IMPACT OF THE PROPOSAL/INITIATIVE

- 3.1. Heading(s) of the multiannual financial framework and expenditure budget line(s) affected
- 3.2. Estimated impact on expenditure
 - 3.2.1 Summary of estimated impact on expenditure
 - 3.2.2 Estimated impact on operational appropriations
 - 3.2.3 Estimated impact on appropriations of an administrative nature
 - 3.2.4 Compatibility with the current multiannual financial framework
 - 3.2.5 Third-party participation in financing
- 3.3. Estimated impact on revenue

I. FRAMEWORK OF THE PROPOSAL/INITIATIVE

1.1. Title of the proposal/initiative

Regulation (EC) No xxx of the European Parliament and of the Council amending Regulation (EC) N° 1060/2009 on credit rating agencies

1.2. Policy area(s) concerned in the ABM/ABB structure²⁰

Internal Market – Financial markets

1.3. Nature of the proposal/initiative

- The proposal/initiative relates to **a new action**
- The proposal/initiative relates to **a new action following a pilot project/preparatory action²¹**
- The proposal/initiative relates to **the extension of an existing action**
- The proposal/initiative relates to **an action redirected towards a new action**

1.4. Objectives

1.4.1 The Commission's multiannual strategic objective(s) targeted by the proposal/initiative

Entrusting ESMA with supervisory powers will make supervision of CRAs in the Community more efficient and effective.

This more effective supervisory framework will better ensure compliance of CRAs with the substantive requirements of the CRA Regulation thereby contributing to the general strategic objectives of the Commission in the field of financial services, namely to ensure the stability of financial markets, to enhance investor protection and to enhance transparency in financial markets.

1.4.2 Specific objective(s) and ABM/ABB activity(ies) concerned

Specific objective

The following objectives of the proposed measure have been identified:

1. Securing effective supervision of CRAs in the EU;
2. Streamlining the supervisory architecture for CRA oversight, and
3. Ensuring legal certainty for CRAs and investors.

Flowing from these objectives a number of operational objectives have been defined:

1. Ensure a single point of contact for CRAs and clear competences,
2. Ensure efficiency gains in registration and supervision process,

²⁰ ABM: Activity-Based Management – ABB: Activity-Based Budgeting.

²¹ As referred to in Article 49(6)(a) or (b) of the Financial Regulation.

3. Ensure a consistent application of substantive rules of the CRA Regulation,
4. Ensure better alignment of incentives for the supervisory authorities to cope with the pan European activity of supervised entities

ABM/ABB activity(ies) concerned

1.4.3 Expected result(s) and impact

Specify the effects which the proposal/initiative should have on the beneficiaries/groups targeted.

1. More effective supervision of CRA in the EU which will enhance quality and transparency of rating activity to the benefit of investors and financial stability
2. Single point of contact and clear competences reducing the burden for supervised entities and national supervisory authorities
3. Consistent application of substantive rules of CRA Regulation will improve legal certainty for CRA industry and improve the quality and transparency of rating activities.
4. Efficiency gains in registration and supervisors process. This will reduce the burden for supervised entities, supervisors and last not least the European taxpayers.

1.4.4. Indicators of results and impact

Specify the indicators for monitoring implementation of the proposal/initiative.

1. Expected result: More effective supervision of CRAs in the EU
 - Number of breaches of CRA Regulation
 - Number of sanctions and penalty payments imposed in reaction to breaches
 - Number of onsite inspections
 - Number of supervisory measures
2. Expected result: Establish a single point of contact for supervised CRAs and clear competences

Indicators:

- Number of supervisory authorities involved in the registration/supervisory process
- Number of conflicts of competences between authorities involved in supervising CRAs

3. Expected result: Consistent application of substantive rules of CRA Regulation

Indicators:

- Number of breaches of CRA Regulation
- Number of complaints received by the Commission from CRAs/users of ratings
- Number of appeals from CRAs to ESMA/ Courts

4. Expected result: Efficiency gains in registration and supervisory process

Indicator:

- Time period needed for registration (from submission of application to the issuance of registration decision)

- Time period to take supervisory measures (from detection of breach of a rule to the adoption of a supervisory measure)
- Number of staff involved in CRA supervision

1.5. Grounds for the proposal/initiative

1.5.1 Requirement(s) to be met in the short or long term

In the short term the ESMA shall be entrusted with the power to register and to supervise CRAs which will generate efficiency gains, more effective supervision and strengthen the consistent application of the CRA Regulation. In the long term the measure will lead to a better compliance of CRAs with the rules of the CRA Regulation thereby improving quality and transparency of the rating activity.

ESMA will be entrusted with CRA supervision for an undetermined period.

1.5.2 Added value of EU involvement

Though the supervisory framework currently prescribed by the CRA Regulation has not been put in place yet, it is already possible to identify certain shortcomings which underpin the need for Community involvement. Those deficiencies and their main consequences for CRAs and supervisors are (see Section 3 of impact assessment accompanying this proposal):

- Multiplicity of supervisors involved and risks of conflicts over competences;
- Risk of divergent and inconsistent application of the CRA Regulation in individual acts by competent authorities in the Member States;
- Burdensome and time-consuming registration and supervisory

Process;

- Risk of misaligned incentives and lack of Community perspective of national supervisors

As has been shown in the impact assessment, entrusting ESMA with registration and supervision of CRAs will remedy or significantly improve those problems.

1.5.3 Lessons learned from similar experiences in the past

It is the first time that direct supervisory powers over financial institutions are granted to a European Supervisory Authority.

1.5.4 Coherence and possible synergy with other relevant instruments

This proposal is coherent with the draft Regulation establishing a European Securities and Markets Authority (COM (2009) 503) of 23.09.2009.

1.6. Duration and financial impact

- Proposal/initiative of **unlimited duration**

1. 7. Management mode(s) envisaged²²

- Centralised direct management** by the Commission
- Centralised indirect management** with the delegation of implementation tasks to:
 - executive agencies
 - bodies set up by the Communities²³
 - national public-sector bodies/bodies with public-service mission
 - persons entrusted with the implementation of specific actions pursuant to Title V of the Treaty on European Union and identified in the relevant basic act within the meaning of Article 49 of the Financial Regulation
- Shared management** with the Member States
- Decentralised management** with third countries
- Joint management** with international organisations (*to be specified*)

If more than one management mode is indicated, please provide details in the "Comments" section.

Comments

2. MANAGEMENT MEASURES

2.1. Monitoring and reporting rules

Specify frequency and conditions.

Article 66 of the draft Regulation establishing the European Securities and Markets Authority provides for an evaluation of the experience acquired as a result of the operation of the Authority within three years from the effective start of its operation, which would include an assessment of ESMA's direct supervisory powers over CRAs. To this end, the Commission shall publish a general report that shall be forwarded to the European Parliament and to the Council.

2.2. Management and control system

2.2.1 Risk(s) identified

An impact assessment concerning this proposal on amendments to the Regulation on credit rating agencies has been carried out identifying costs and benefits of different policy options to address the identified problems.

The risk of financing ESMA's activities by industry fees in the first year of its operation (2011) has been eliminated by providing for financing by the Community budget/ Member States as foreseen in the ESMA Regulation (40/60 ratio).

²² Details of management modes and references to the Financial Regulation may be found on the BudgWeb site: http://www.cc.cec/budg/man/budgmanag/budgmanag_en.html

²³ As referred to in Article 185 of the Financial Regulation.

2.2.2 Control method(s) envisaged

Management and control systems as provided for in the draft ESMA Regulation will apply also with regard to the supervision of CRAs.

The final set of indicators to assess the performance of the European Securities and Markets Authority in the field of credit rating agencies will be decided by the Commission at the time of conducting the first required evaluation. For the final assessment, the quantitative indicators will be as important as the qualitative evidence gathered in the consultations. The evaluation shall be repeated every three years.

2.3. Measures to prevent fraud and irregularities

Specify existing or envisaged prevention and protection measures.

For the purposes of combating fraud, corruption and any other illegal activity, the provisions of Regulation (EC) No 1073/1999 of the European Parliament and of the Council of 25 May 1999 concerning investigations conducted by the European Anti-Fraud Office (OLAF) shall apply to the ESMA without any restriction.

The Authority shall accede to the Interinstitutional Agreement of 25 May 1999 between the European Parliament, the Council of the European Union and the Commission of the European Communities concerning internal investigations by the European Anti-Fraud Office (OLAF) and shall immediately adopt appropriate provisions for all staff of the Authority.

The funding decisions and the agreements and the implementing instruments resulting from them shall explicitly stipulate that the Court of Auditors and OLAF may, if need be, carry out on-the-spot checks on the beneficiaries of monies disbursed by the Authority as well as on the staff responsible for allocating these monies.

3. ESTIMATED FINANCIAL IMPACT OF THE PROPOSAL/INITIATIVE

3.1. Heading(s) of the multiannual financial framework and expenditure budget line(s) affected

- Existing expenditure budget lines

In order of multiannual financial framework headings and budget lines.

Heading of multiannual financial framework	Budget line	Type of expenditure	Contribution			
	Number 1A..... Competitiveness for Growth and Employment	DA/NDA ⁽²⁴⁾	from EFTA ²⁵ countries	from candidate countries ²⁶	from third countries	within the meaning of Article 18(1)(aa) of the Financial Regulation
	12.0404.01. ESMA Subsidy under Titles 1 and 2 (Staff and administrative expenditure)	Diff	YES	NO	NO	NO
	12.0404.02 ESMA- Subsidy under Title 3 (Operating expenditure)	Diff	YES	NO	NO	NO

²⁴ DA= Differentiated appropriations / DNA= Non-Differentiated Appropriations.

²⁵ EFTA: European Free Trade Association.

²⁶ Candidate countries and, where applicable, potential candidate countries from the Western Balkans.

3.2. Estimated impact on expenditure

3.2.1 Summary of estimated impact on expenditure

EUR million (to 3 decimal places)

Heading of multiannual financial framework:	1A	Competitiveness for Growth and Employment
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DG: MARKT			Year 2011	Year 2012	Year 2013	TOTAL
• Operational appropriations						
12.0404.01.	Commitments	(1)	0,881	0	0	0,881
	Payments	(2)	0,881	0	0	0,881
12.0404.02.	Commitments	(1a)	0,120	0	0	0,120
	Payments	(2a)	0,120	0	0	0,120
Appropriations of an administrative nature financed from the envelop of specific programs ²⁷						
		(3)				
TOTAL appropriations for DG MARKT		Commitments	1,001	0	0	1,001
		=1+1a +3				
	Payments	=2+2a	1,001	0	0	1,001
		+3				

Heading of multiannual financial	5	" Administrative expenditure "
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²⁷ Technical and/or administrative assistance and expenditure in support of the implementation of EU programmes and/or actions (former "BA" lines), indirect research, direct research.

framework:		
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EUR million (to 3 decimal places)

		Year 2011	Year 2012	Year 2013					TOTAL
DG: MARKT									
• Human resources		0,488	0,488	0,488					1,464
• Other administrative expenditure									
TOTAL DG MARKT	Appropriations	0,488	0,488	0,488					1,464

TOTAL appropriations under for HEADING 5 of the multiannual financial framework	(Total commitments = Total payments)	0,488	0,488	0,488					1,464
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EUR million (to 3 decimal places)

		Year 2011	Year 2012	Year 2013					TOTAL
TOTAL appropriations under HEADINGS 1 to 5 of the multiannual financial framework	Commitments	1,489	0,488	0,488					2,465
	Payments	1,489	0,488	0,488					2,465

According to Article 48 (1) c) of the ESMA Regulation, the revenues of ESMA may also consist of any fees paid to the Authority in the cases specified in the relevant legislation. Article 19 of the proposal provides that ESMA's expenditure necessary for the registration and supervision of CRAs according to the Regulation shall be fully covered by fees charged to the credit rating agencies. The types of the fees, the matters for which fees are due and the amount of the fees shall pursuant to Article 19 (2) be determined by a Commission delegated act which will be adopted in the

course of 2011 and is supposed to enter into force beginning of 2012. In the transition year of 2011 resources for direct supervision of CRAs should be advanced by Member States and Community contributions according to the ratio foreseen in the draft ESMA Regulation (40 % Community and 60 % Member States contributions). The costs for CRA supervision in 2011 shall be claimed back from the CRA industry once the delegated act entered into force.

3.2.2 Estimated impact on operational appropriations

The proposal/initiative requires the use of operational appropriations, as explained below:

The specific objectives of the proposal are set out under 1.4.2. Given the type of objectives it is not possible to attribute concrete numerical outputs to each of them. Still the indicators outlined above will allow assessing whether the objectives of the proposal have been reached.

3.2.3 Estimated impact on appropriations of an administrative nature

3.2.3.1 Summary

The proposal/initiative requires the use of administrative appropriations, as explained below:

EUR million (to 3 decimal places)

	Year 2011	Year 2012	Year 2013						TOTAL
HEADING 5 of the multiannual financial framework									
Human resources	0,488	0,488	0,488						1,464
Other administrative expenditure	0	0	0						
Subtotal HEADING 5 of the multiannual financial framework	0,488	0,488	0,488						1,464
TOTAL	0,488	0,488	0,488						1,464

3.2.3.2 Estimated requirements of human resources

The proposal/initiative requires the use of human resources, as explained below:

Estimate to be expressed in full amounts (or at most to one decimal place)

	Year 2011	Year 2012	Year 2013					
• Establishment plan posts (officials and temporary agents)								
XX 01 01 01 (Headquarters and Commission's Representation Offices)	4	4	4					
• External personnel (in Full Time Equivalent unit: FTE)								
TOTAL	4	4	4					

Description of tasks to be carried out:

Officials and temporary agents	<ul style="list-style-type: none"> Adopt fining decisions and decisions on periodic penalty payments on CRAs on a proposal by ESMA according to Articles 36 and 36a of the proposal, including own enquiries, hearing of the CRAs and persons concerned, respond to requests for access to file, defend
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fining and periodic penalty payments decisions before Courts and collection of fines and periodic penalty payments.

- For 2011 all 4 posts will be redeployed inside DG MARKT. Given the budgetary constraints linked to the current Commission's commitment not to ask for new posts until 2013, the human resources required will be met by staff from the DG who are already assigned to management of the action and/or have been redeployed within the DG, together if necessary with any additional allocation which may be granted to the managing DG under the annual allocation procedure and in the light of budgetary constraints. At least one post will be redeployed using existing resources within the managing service (internal redeployment).

3.2.4 Compatibility with the current multiannual financial framework

- Proposal/initiative is compatible the current multiannual financial framework.
- Proposal/initiative will entail reprogramming of the relevant heading in the multiannual financial framework.

New action of the Commission

- Proposal/initiative requires application of the flexibility instrument or revision of the multiannual financial framework.

3.2.5 Third-party contributions

The proposal/initiative provides for the co-financing estimated below:

Appropriations in EUR million (to 3 decimal places)

	Year 2011	Year 2012	Year 2013	Total
<i>Specify the co-financing body</i>	60% of total needs by Member States, via EU National Supervisors (proposed ESMA standard financing mechanism)	No co-financing. CRA Supervision fully financed via fees		
TOTAL appropriations cofinanced	1,501	0	0	1,501

3.3. Estimated impact on revenue

- Proposal has financial implications on revenue. According to the proposal the Commission may impose fines and periodic penalty payments on CRAs (see Article 36, 36a). It is difficult to predict the amount of fines and periodic penalty payments that the Commission may impose on CRAs as it depends among other things on the future compliance of CRAs with the Regulation.

ANNEX to Legislative Financial Statement for Proposal for Regulation amending Regulation No 1060/2009 on credit rating agencies

Applied methodology and main underlying assumptions

The costs related to direct supervision of CRA by ESMA have been estimated according to three cost categories: the staff costs, the infrastructure costs and the operations costs, in line with the classification in the general draft budget of ESMA (see financial statement accompanying proposal for a regulation establishing ESMA from 23.09.2009 COM(2009) 503).

According to current estimations from the CESR secretariat and own Commission estimates the CRA oversight activity will require 12 new staff members (6 temporary agents and 6 seconded national experts) in addition to the 3 staff that are currently working on CRAs in CESR and that are covered by the draft budget for ESMA already provided for in the draft ESMA Regulation.

The need for increased staffing numbers reflects the new tasks related to direct supervision of CRAs which the authority will need to undertake in addition to its previous responsibilities in the area of CRAs (e.g. giving advice to the Commission, developing guidelines and binding technical standards, facilitate cooperation between national competent authorities, mediation).

These new tasks are set out in the proposed Regulation and further spelled out in the explanatory memorandum (4.3.3. and 4.3.4.). They include, but are not limited to, the registration of CRAs located in the Community, the certification of smaller CRAs located in third countries, day-to-day supervision of registered CRAs, requiring regular contacts with the management/ staff of the supervised entities, cooperation with third country supervisors regarding third country CRAs, responding to questions, complaints or requests by national competent authorities, CRAs or investors, monitoring of the compliance of CRAs with requirements set out in the CRA Regulation, requesting information from CRAs or persons involved in rating activities, conducting onsite inspections, examining records and hearing of persons on alleged breaches of the Regulation. ESMA will also have the power to withdraw the registration and take other supervisory measures as listed in Article 24 of the Regulation and to request the Commission to impose fines and periodic penalty payments on CRAs which are in breach of the Regulation, providing evidence about the breach and proposing the amount of the fine or the penalty payment.

According to our information ca. 50 CRAs will apply for registration and will, once registered, have to be supervised by the ESMA. Taking account of the number of CRAs to be supervised, the number, type and complexity of tasks to be fulfilled by ESMA and some general indications about the staff numbers that national competent authorities foresee for registration and supervision under the current framework, the number of 12 additional posts for CESR is appropriate.

The detailed breakdown of estimated staff numbers by various categories is presented in Table 3.

The impact of the location of ESMA in Paris has also been taken into account by applying the relevant correction coefficient reflecting the costs of living in Paris.

The evolution of the staff costs in subsequent years depends among other things on the number of supervised entities but from today's perspective we would not expect significant changes.

The figures under Title 2 relating to the cost of infrastructure have been based on the input from CESR and Commission estimates. The CESR provided estimates of their costs in this category, based on extrapolation of their real costs linked with running offices and administration in their current locations. Given that Paris is among the most expensive business locations in Europe, the estimated costs naturally exceed the average levels for the EU regulatory agencies. Costs for translations of registrations and other decisions will be significant as the EU language regime will fully apply to ESMA.

New operation costs linked to direct supervision of CRAs relate to the collection of information. This includes the operation of a new database for direct supervision of CRAs. In addition, the new ESMA power to undertake onsite inspections requires new resources.

The methods of calculating the budget of ESMA are presented in Table 2.

According to Article 48 (1) c) of the ESMA Regulation, the revenues of ESMA may also consist of any fees paid to the Authority in the cases specified in the relevant legislation. Article 19 of the proposal provides that ESMA's expenditure necessary for the registration and supervision of CRAs according to the Regulation shall be fully covered by fees charged to the credit rating agencies. The types of the fees, the matters for which fees are due and the amount of the fees shall pursuant to Article 19 (2) be determined by a Commission delegated act which will be adopted in the course of 2011 and is supposed to enter into force beginning of 2012. In the transition year of 2011 resources for direct supervision of CRAs should be advanced by Member States and Community contributions according to the ratio foreseen in the draft ESMA Regulation (40 % Community and 60 % Member States contributions). The costs for CRA supervision in 2011 shall be claimed back from the CRA industry once the delegated act entered into force.

Table 1: Estimated budget for the European Securities and Markets Authority related to direct supervision of CRAs

In thousands €

	2011	2012	2013
Title 1 - Staff costs	1574,8	1574,8	1574,8
Senior / expert staff:			
Temporary agents	847,8	847,8	847,8
Seconded national experts	507	507	507
Administrative and other support staff:			
Staff benefits	203,2	203,2	203,2
Staff training: general	7,2	7,2	7,2

Expenditure relating to staff recruitment	9,6	9,6	9,6
Title 2 - Building, equipment and administrative expenditure	628	628	628
Rental of buildings and associated costs	216	216	216
Information and communication technology	72	72	72
Movable property and associated costs	12	12	12
Current administrative expenditure	12	12	12
Postage / Telecommunications	36	36	36
Meeting expenses / Travelling expenses	180	180	180
Translations	100	100	100
Title 3 - Operations	300	300	300
Collection of information: development	150	150	150
On site inspections	150	150	150
TOTAL	2502,8	2502,8	2502,8
Of which Community contribution	1001,12	0	0
Of which Member States contribution (national supervisory authorities or ministries of finance)	1501,68	0	0
Fees and levy from CRA industry	0	2502,8	2502,8

Source: Commission and CESR, estimates and calculations

Table 2: Estimated budget of ESMA related to direct supervision of CRAs in the first year of operation (2011) incl. calculation assumptions

In thousands €

Title 1 - Staff costs			1574,8
Total staff:	12	Average annual cost per head (based on DG BUDG guidelines and 3L3 advice)	
Correction coefficient (cost of living adaptation)	Paris	1,158	
Temporary agents	6	141,3 (122x1,158)	847,8
Seconded national experts	6	84,5 (73x1,158)	507
Staff benefits	15% of total staff costs		203,2
Staff training: general	Average amount per person (COM data)	0,6	7,2
Expenditure relating to staff recruitment	3 candidates interviewed per post on average	0,8	9,6
Title 2 - Building, equipment and administrative expenditure			628
Rental of buildings and associated costs	CESR data and estimates	18	216
Information and communication technology	CESR data and estimates	6	72
Movable property and associated costs	CESR data and estimates	1	12
Current administrative expenditure	CESR data and estimates	1	12
Postage / Telecommunications	CESR data and estimates	3	36
Travel and meeting expenses	CESR data and estimates	15	180
Translations	Commission estimates		100
Title 3 - Operations			300

Collection of information		Set up and adaptation of IT systems (new system and database for direct supervision of CRAs)	150
On site inspections		CESR estimates	150
TOTAL			2502,8

Source: Commission and the CESR estimates and calculations

Table 3: Establishment Plan (preliminary)

Function group and grade	2011	2012	2013
AD 16			
AD 15			
AD 14			
AD 13			
AD 12			
AD 11	1	1	1
AD 10	1	1	1
AD 9	2	2	2
AD 8	1	1	1
AD 7	1	1	1
AD 6			
AD 5			
AD total	6	6	6

Source: Commission