EUROPEAN COMMISSION

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C/2009/5488

Dott. Antonio Malaschini

Segretario Generale
Senato della Repubblica
Piazza Madama
00186 Roma

Mr. Secretary General,

Thank you for your letter of 2nd April 2009 informing the European Commission about the concerns raised by the Italian Senate as regards the Commission's proposal for a Regulation on Credit Rating Agencies, adopted by the Commission on 12th November 2008[1]. The European Commission appreciates the support to this very important initiative intended to help restoring financial markets' confidence and to enhance investor protection in the European Union.

Concerning the state of play of the legislative co-decision procedure, I would like to inform you that on 23rd April 2009, the European Parliament and the Council agreed on the text of the Regulation on Credit Rating Agencies[2]. The text is to be formally adopted by the Council in the coming weeks.

Concerning the specific issues raised in your letter related to the content of the proposal, I would like to comment, taking into account the outcome of the co-decision process, on the scope of the proposal, the treatment of conflicts of interest, the disclosure requirements, the supervisory structure and the third country regime.

Scope of the proposal (Articles 2 and 4).The text agreed covers credit ratings issued by credit rating agencies registered in the European Union, which are disclosed publicly or distributed by subscription. There are four exemptions to the scope: private credit ratings, credit scores related to obligations arising from consumer, commercial and industrial relationships, credit ratings produced by export credit agencies and credit ratings produced by central banks fulfilling the conditions specified in the Regulation. The four exemptions introduced are either not credit ratings *stricto sensu* or not linked to the financial crisis. Moreover, the scope is complemented by a provision requiring financial institutions to use, for regulatory purposes, ratings issued by credit rating agencies

[1] COM(2008) 704 final.

[2] Please find the text at: http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P6-TA-2009-0279+0+DOC+XML+V0//EN&language=EN

registered according to the Regulation (with the special treatment for endorsed ratings and certified credit rating agencies from third countries).

Treatment of conflicts of interest (Articles 5 and 6; Annex I Sections A, B and C).The text agreed does not differ much from the Commission initial proposal. Credit rating agencies will be required to prevent conflicts of interest and/or to manage these conflicts adequately where they are unavoidable in order to ensure the independence of credit ratings. They will have to disclose conflicts of interest in a complete, timely, clear, concise, specific and prominent manner and record all significant threats to the rating agency's independence or that of its employees involved in the credit rating process, together with the safeguards applied to mitigate those threats. Credit rating agencies will have to implement adequate internal policies and procedures to insulate employees involved in credit rating from conflicts of interest and ensure the quality, integrity and thoroughness of the rating and review process at all times. Moreover, credit rating agencies will not be allowed to provide consultancy or advisory services to the rated entity or any related third party regarding the corporate or legal structure, assets, liabilities or activities and they will only be entitled to provide the ancillary services listed in Annex I, Section B of the Regulation, in case they do not present conflicts of interest with the rating activity.

Disclosure requirements (Articles 7, 8 and 9; Annex I Section D and E). The text agreed maintains the disclosure obligations of the Commission initial proposal. Credit rating agencies will be required to provide information regarding the rating process both in general and with respect to a specific issuer/financial instrument. Credit rating agencies will also be required to disclose to the public how they operate internally and how they address certain key challenges in their activity: relations with clients, conflicts of interest, ancillary services, communication policy (including the disclosure of ratings) and analytical staff issues (remuneration, staff adequacy). These on-going disclosures will be underpinned by an annual transparency report, which will reflect any findings and developments in the listed areas. Moreover, some specific disclosures only to competent authorities will help them to perform their supervisory tasks.

Supervisory structure (Articles 12-30). The text agreed introduces a system of supervision based on colleges of competent authorities which gives the possibility to all concerned competent authorities to participate in the process of registration and supervision of a credit rating agency or a group of credit rating agencies. This structure respects the same underlying principles as the structure originally envisaged in the Commission proposal. We acknowledge that, in the long run, the supervisory structure should be revisited taking inspiration from the conclusions of the High Level Group on Financial Supervision chaired by J. de Larosière, which recommends entrusting the Committee of European Securities Regulators (CESR) with the task of monitoring the performance of credit rating agencies at EU level. Therefore, a robust review clause has been introduced for the review of the supervisory structure in one year time.

Third country regime (Articles 4 and 4a). Due to the global nature of credit rating agencies, it has been considered necessary to find a solution for the use in the Community of credit ratings issued in third countries in order to avoid disturbances in the functioning of financial markets. The text agreed introduces provisions on the treatment of credit ratings issued by credit rating agencies established in third countries. The solution consists of an endorsement regime and an equivalence mechanism, and ensures that credit ratings issued in third countries may be used in the Community only when issuing credit rating agencies, which operate outside the EU and have an objective reason to elaborate them in a third country, (1) comply with legal requirements which are as

stringent as the requirements provided for in this Regulation and (2) are subject to effective supervision in their country of establishment.

The endorsement regime is made available for credit rating agencies that are affiliated or work closely with EU-established credit rating agencies. The equivalence mechanism is also made available for smaller credit rating agencies from third countries with no presence or affiliation in the EU, provided they are not systemically important for the financial stability or integrity of the financial markets of one or more Member States. This specific registration process (certification) will take into consideration the size of the applicant credit rating agency, in view of the nature, scale and complexity of its business and the nature and range of issuance of its credit ratings, and might allow for exempting such credit rating agency from certain organisational requirements or from the obligation to have a physical presence in the European Union. The underlying objective is to foster competition and the entrance of new players in a market where there are currently very few players.

I believe that the final text of the Regulation will help address one of the problems that contributed to this crisis and thus will offer some prospect of restoring market confidence. It will, in particular, improve the integrity, transparency, responsibility and good governance of the credit rating activities and introduce a strong supervisory regime which will definitely improve the functioning of our financial markets.

Yours sincerely

Margot WALLSTRÖM
Vice-President of the European Commission