



European Securities and
Markets Authority

Call for Evidence

Competition, choice and conflicts of interest in the credit rating industry



Responding to this call for evidence

This call for evidence should be read by all those involved in the credit rating industry. It is particularly targeted at the following market participants and the groups and trade associations who represent them:

1. Corporate and sovereign issuers of financial instruments requesting credit ratings.
2. Credit rating agencies issuing credit ratings.
3. Institutional investors and other users of credit ratings.

There are specific questions for corporate and sovereign issuers in section 4 of the call for evidence, followed by questions for credit rating agencies in section 5 and for investors in section 6. ESMA invites respondents to provide information about each relevant set of questions using the template response forms provided for each group.

Responses are most helpful to ESMA where they clearly indicate which question is being answered and provide evidence in support of the response, such as concrete examples of practices experienced, data or costs estimates.

ESMA will consider all responses received by **31 March 2015**.

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

Publication of responses

All contributions received will be published following the close of the call for evidence, unless you request otherwise. Please clearly and prominently indicate in your submission any part that you do not wish to be publically disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the heading [Legal Notice](#).

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Acronyms used

CEREP	ESMA Central Repository for publishing credit rating activity and performance statistics
Commission	The European Commission
CRA	Credit rating agency
CRA Regulation	Regulation 1060/2009 on credit rating agencies as amended
ESMA	European Securities and Markets Authority
EU	European Union

Executive Summary

Reasons for publication

This call for evidence is being published to collect information from market participants about the functioning of the credit rating industry and the evolution of the markets for structured finance instruments as required by Regulation 1060/2009 on credit rating agencies as amended (the CRA Regulation). ESMA is seeking evidence about competition, choice and conflicts of interests in the credit rating agency industry in general as well as about the impact of a number of specific provisions of the CRA Regulation.

Contents

Sections 1 and 2 of the call for evidence explain its background and purpose. Section 3 gives an introduction to the different sets of questions provided. This is followed by the questions for consideration by corporate and sovereign issuers in Section 4, questions for credit rating agencies in Section 5 and for institutional investors and other users of credit ratings in Section 6.

Next Steps

ESMA will carefully consider all responses to the Call for Evidence received by the deadline of 31 March 2015. The evidence obtained will be analysed by ESMA as part of the development of the Technical Advice to be provided to the European Commission pursuant to Articles 39(4) and 39(5) of the CRA Regulation.

1 Background

1. The European Securities and Markets Authority (ESMA) has been solely responsible for the registration and supervision of CRAs in the European Union (EU) and the enforcement of Regulation 1060/2009 on Credit Rating Agencies as amended (the CRA Regulation) since 2011.¹
2. One of ESMA's tasks under the CRA Regulation is the provision of Technical Advice to the European Commission (the Commission). ESMA may seek input from a variety of sources in order to provide this advice, as well as drawing on its supervisory experience.
3. Articles 39(4) and 39(5) of the CRA Regulation require ESMA to provide Technical Advice about the functioning of the credit rating industry and the evolution of the markets for structured finance instruments. These Articles are set out in full in Annex I of the call for evidence. The Articles request information on a number of general issues as well as about the impact of some specific provisions of the CRA Regulation.
4. ESMA will produce Technical Advice on the issues referred to Articles 39(4) and 39(5) of the CRA Regulation by September 2015.

2 Purpose

5. The purpose of this call for evidence is to collect information from market participants as an input into ESMA's Technical Advice.
6. The general issues to be considered are:
 - (1) The appropriateness of existing and alternative remuneration models for credit rating agencies (CRAs).
 - (2) Choice of and competition between CRAs.
 - (3) Whether it is necessary and appropriate to propose further measures to stimulate competition between CRAs.
 - (4) The impact of market concentration levels on the overall stability of the financial sector.
7. In addition, a number of specific provisions of the CRA Regulation will be assessed in order to determine whether they are effective or whether they should be amended or extended:

¹ See Regulation 513/2001 of 11 May 2011 recital 5 and 6 and Article 40(a) and Recital 5 of Regulation 1095/2010 establishing a European Supervisory Authority (European Securities and Markets Authority) of 24 November 2010, OJ L 331/84 of 15.12.2010 (the ESMA Regulation).

- The policies and procedures, shareholder caps and rotation obligations to mitigate conflicts of interest.
 - The disclosure obligations for structured finance instruments.
 - The length of the agreements between CRAs and issuers for issuing credit ratings on re-securitisations, the mandatory rotation of CRAs rating re-securitisations and the exemption from this mandatory rotation.
8. Questions regarding the need to propose measures to reduce overreliance on credit ratings as set out in Article 39(5)(g) are not included in this call for evidence as Technical Advice on this point is being prepared through ESMA's ongoing work with the Joint Committee of the European Supervisory Authorities on contractual reliance on external credit ratings. The Joint Committee has issued a discussion paper on this subject. Credit institutions, insurance and reinsurance entities, investment firms, investment managers, central counterparties and the National Authorities who supervise them are invited to submit comments on the Joint Committee's discussion paper by 27 February 2015.²

3 Introduction

9. The CRA Regulation aims to enhance the integrity, transparency, responsibility, good governance and independence of credit rating activities to promote quality credit ratings and high levels of investor protection³ whilst seeking to stimulate competition between CRAs.⁴ The Regulation contains obligations for issuers, originators and sponsors of structured finance instruments as well as for CRAs.
10. The questions for consideration are set out in the following sections. Each section and subsection is introduced separately in order to help respondents understand the type of evidence that ESMA is seeking in response to each group of questions. Each set of questions is reproduced in the template response forms provided for ease of reference.
11. The questions in each of the following sections are directed at corporate and sovereign issuers, CRAs and investors respectively (hereinafter 'you' or 'your'). The purpose of each group of questions is explained under the subheadings below.
12. Respondents may need to disclose commercially sensitive information to ESMA in order to answer some of the questions asked. ESMA intends to present confidential information in anonymised and aggregated form in its Technical Advice so that individual respondents cannot be identified. In order to facilitate this process, ESMA therefore asks respondents to clearly indicate which parts of the answers to each question they believe to contain confidential information.

² [JC/DP/2014/01 Joint Committee Discussion Paper, The Use of Credit Ratings by Financial Intermediaries, 23 December 2014](#)

³ See Article 1 of the CRA Regulation.

⁴ See Recital 7 of Regulation 513/2001 of 11 May 2011 and Recital 11 of Regulation 462/2013 of 21 May 2013.

4 Questions for corporate and sovereign issuers

4.1 About your organisation

13. The questions in this part aim to obtain information about the nature of the organisation you represent and the different markets in which you are active. This information will help ESMA to put your responses in context and to compare responses from similar respondents.

Q1: Please provide the name of your organisation.

Q2: Please explain whether you issue instruments requiring credit ratings at local, national, EU and/or global level. If your organisation issues financial instruments at EU or global level, please provide a list of the jurisdictions in question.

4.2 Use of credit ratings and sensitivity to price increases

14. The questions in this part aim to understand how issuers and sovereigns use credit ratings, whether there are products similar to credit ratings which should be considered as substitutes and whether your demand for, or use of, credit ratings could change if the prices of credit ratings were to increase.

15. The purpose of these questions is to understand whether there are separate markets for the credit ratings of individual asset classes within the CRA industry. This will allow ESMA to assess how much market power the CRAs offering ratings for individual asset classes might have and what barriers to entry are faced by CRAs looking to start rating certain asset classes for the first time.

Q3: What criteria do you use to select a CRA? Do you use different CRAs to rate different instruments and/or in different jurisdictions? If so, please explain whether, and if so how, your criteria vary.

Q4: How many ratings do you solicit for each type of instrument you want to market in each jurisdiction? If more than one, please explain why.

Q5: When you seek multiple ratings for certain types of instrument, please explain:

(1) The criteria you use to choose which CRA(s) to engage to rate different types of instruments.

(2) How many CRAs can currently meet these criteria in your view, and why other CRAs cannot meet these criteria.

(3) Whether you apply the same criteria to select all of the CRAs engaged or whether you select a main CRA and then one or more secondary CRAs using different criteria. In particular, please explain whether the market share of the primary and/or secondary CRAs plays a part in this decision.

Q6: Under which circumstances would you consider seeking ratings from a CRA which has not previously rated a particular asset class? Please give reasons for your answer.

Q7: Please explain whether you present the credit risk of the instruments you are marketing by means other than credit ratings, and if so, please provide details.

Q8: Please explain how the prices of credit ratings and the other products and services provided by CRAs have changed since 2010.

Q9: Please explain how you would respond if your preferred CRA(s) increased the costs of providing credit ratings for different asset classes by 5-10%. If your answer would differ depending on the jurisdiction or asset class in question, please explain why.

4.3 Impact of provisions requiring the use of multiple credit rating agencies

16. The 2013 amendments to the CRA Regulation introduced a number of requirements on issuers and related third parties of structured finance instruments regarding the use of multiple credit ratings. These requirements are set out in Articles 8c and 8d of the CRA Regulation.

17. Article 8c of the CRA Regulation introduces an obligation for issuers or related third parties to obtain at least two credit ratings for structured finance instruments. This obligation was introduced with the aim of restoring market confidence in complex financial instruments and reducing reliance on single credit ratings.⁵

18. Article 8d of the CRA Regulation aims to increase competition in the markets for credit ratings by encouraging issuers or related third parties to use smaller credit rating agencies when they use multiple CRAs. Article 8d states that where issuers or related third parties intend to appoint at least two CRAs to rate an issuance or entity, they shall consider appointing at least one CRA with no more than 10% of the total market share where:

- The issuer or related third party finds that there is a CRA capable of rating the relevant issuance or entity; and

⁵ Recital 28 of Regulation 462/2013 of 21 May 2013.

- Such a CRA is available to rate the issuance or entity in question.

19. Where it is not possible to appoint at least one CRA with no more than 10% of the total market share, the issuer or related third party is required to document this.

20. The next question aims to understand whether these provisions have achieved their objectives and the impact they have had on your business.

Q10: Please explain the impact on your business of the following obligations and provide an estimate of your costs of complying with each of these obligations from 2013 to present where possible:

(1) to appoint at least two CRAs to provide ratings of structured finance instruments; and

(2) to document the CRAs appointed.

4.4 Quality and independence of credit ratings

21. One of the aims of the CRA Regulation is to increase the quality of credit ratings by seeking to reduce the conflicts of interest inherent where issuers pay for the rating of their financial instruments.⁶

22. The questions in this part aim to understand whether corporate and sovereign issuers support the issue of credit ratings by CRAs using alternative business models and to assess the impact of the CRA Regulation on increasing the quality and independence of credit ratings overall.

Q11: Do you provide information to CRAs who issue ratings by subscription which are paid for by investors as well as for the ratings that you pay for? What are the advantages and disadvantages of these different business models from your perspective?

Q12: Please explain whether there are other models which would allow CRAs to seek payment for the credit ratings they issue, giving reasons for your answer.

Q13: What are the average durations of your agreements with CRAs for credit ratings and your agreements with CRAs for ancillary services? Please explain whether this differs by asset class and/or jurisdiction and how this has changed since 2010.

⁶ See Recital 10 of Regulation 462/2013 of 21 May 2013.

- Q14: Please describe the process you would typically follow when seeking a credit rating for a new financial instrument you wished to market, explaining how this process has changed since 2010, if at all. In particular:**
- (1) how many CRAs you would contact or hold preliminary discussions with;**
 - (2) how you would compare the ratings and ancillary services being offered by different CRAs.**
- Q15: Once you have chosen your preferred CRA, please explain your involvement in the process of preparing, issuing and subsequently reviewing the rating of your instrument.**
- Q16: Do you give CRAs more detailed information about how the instruments for which you are seeking ratings are developed and how they subsequently perform in practice now than you did before 2010? If so, please explain what kinds of additional information you now provide.**
- Q17: Do CRAs currently give you more information about how their credit ratings are developed, issued and revised and how their credit ratings compare to the market performance of the rated instruments than they did before 2010? If so, please explain what additional information you receive and whether this makes it easier for you to compare the ratings products and other services being offered by different CRAs.**
- Q18: Please explain what, if any, further measures could be taken to increase the quality and independence of ratings, giving reasons for your answer.**

4.5 Disclosure obligations for complex financial instruments

23. The 2013 amendments to the CRA Regulation introduced, in Article 8b, a joint obligation on issuers, originators and sponsors to publish information on the credit quality and performance of the underlying assets of structured finance instruments.
24. The expression '*structured finance instrument*' is defined as a financial instrument or other assets resulting from a securitisation transaction or scheme '*whereby the credit risk associated with an exposure or pool of exposures is tranced, having both of the following characteristics:*
- (a) payments in the transaction or scheme are dependent upon the performance of the exposure or pool of exposures; and*

(b) the subordination of tranches determines the distribution of losses during the ongoing life of the transaction or scheme.⁷

25. Commission Delegated Regulation 2015/3 of 30 September 2014 sets out the disclosure requirements for issuers, originators and sponsors of structured finance instruments.⁸ Although this Delegated Regulation will only apply from 1 January 2017, its aim to improve transparency is clear. In this part ESMA therefore asks questions which seek to understand the benefits and costs of extending these disclosure obligations to other asset classes.

Q19: Please explain whether you would welcome an obligation for issuers to disclose details of the credit quality and performance of other financial credit products in addition to those foreseen by Article 8b of the CRA Regulation, giving reasons for your answer. If so, please explain to which products this obligation should be extended.

Q20: Please provide an estimate of the likely costs to your business of complying with Article 8b as currently formulated, and in the event that it were to be extended to the other instruments listed in your answer to question 19 above.

4.6 Mandatory rotation

26. The 2013 amendments to the CRA Regulation introduced a mandatory rotation provision for CRAs issuing ratings on re-securitisations, which can be found in Article 6b of the CRA Regulation. Article 6b provides that CRAs may enter into ratings agreements for re-securitisations with a maximum length of four years, after which time they are prevented from rating new re-securitisations with underlying assets from the same originator for a period of four years.

27. The CRA Regulation notes that the implementation of a rotation mechanism should remove the incentive for a CRA to issue favourable credit ratings to issuers on the basis of their existing relationships and could encourage other CRAs to start rating these instruments.⁹

28. As the provision was also designed to help stimulate competition, Article 6b2(b) of the CRA Regulation explains that mandatory rotation will cease to apply where at least four CRAs each rate more than 10% of the total number of outstanding re-securitisations.¹⁰

29. Although this provision has only recently entered into force, the questions in this part are designed to help ESMA understand the extent to which it has already been used and assess its likely future impact. They also aim to assess the appropriateness of

⁷ Article 4(1)(61) of Regulation No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation No 648/2012, OJ L 176, 27.6.2013.

⁸ OJ L 57, 6.1.2015, p. 2.

⁹ See Recital 12 of Regulation 462/2013 of 21 May 2013.

¹⁰ See Recital 15 of Regulation 462/2013 of 21 May 2013.

maintaining a rotation mechanism, whether, and if so how, it should be extended to other asset classes and what impact this would have on issuers.

Q21: Please provide details of any experience you have had of this rotation provision to date. If you have had experience of this provision, please provide an estimate of your costs of complying with it to date.

Q22: Please explain whether a 4-year contract term is appropriate for this rotation provision, and if not, what would be an appropriate length?

Q23: Please explain whether mandatory rotation should be extended to other asset classes. If so, please:

(1) list the asset classes to be covered and state the appropriate contract length for each;

(2) estimate the cost to your business of complying with the extension to each additional asset covered in your response to question 23(1) above;

(3) explain whether, and if so why an obligation should be introduced for CRAs to provide a handover file to the incoming CRA at the end of the maximum contract term.¹¹

Q24: Please explain, giving reasons for your answer, whether, and if so how, the exemption from the mandatory rotation provision should be maintained where at least four CRAs each rate more than 10% of the total number of outstanding re-securitisations.

4.7 Further measures to stimulate competition

30. The questions in this part aim to collect information about your experiences of competition between CRAs, and whether competition or interactions between credit rating agencies have changed since the CRA Regulation entered into force in 2010.

31. ESMA understands that CRAs may compete to win the business of issuers on a number of different parameters, such as price, quality of service, the offer of unsolicited ratings or the provision of ancillary services.

32. ESMA would like to take your views as to whether, and if so how, competition between credit rating agencies works in practice and whether it could be further stimulated without having a negative impact on the quality of credit ratings.

¹¹ See Recital 13 of Regulation 462/2013 of 21 May 2013.

Q25: Please explain whether, and if so how CRAs compete to win your business.

Q26: If you have been aware of competition between CRAs, please explain whether, and if so how, the nature of competition has changed between 2010 and present.

Q27: Have you seen other changes to the behaviour of CRAs since 2010? If so, please explain what these changes have been and to which products or services these changes related.

Q28: Should further measures be taken to stimulate competition between CRAs overall and/ or in respect of the rating of particular types of asset class such as structured finance instruments? If so, please explain what measures should be taken and what impact you think these would have on the quality of credit ratings.

4.8 Other evidence

33. If there is any other evidence or information that you would like to bring to ESMA's attention, please present it in this part.

5 Questions for credit rating agencies

5.1 About your organisation

34. The questions in this part aim to obtain information about the organisation you represent to help ESMA to put your responses in context and to compare responses from similar respondents.

Q1: Please provide the name of your organisation.

5.2 Minimising conflicts of interest

35. One of the aims of the CRA Regulation is to increase the quality of credit ratings by seeking to reduce the conflicts of interest inherent where issuers pay for the rating of their financial instruments.¹²

36. The questions in this part aim to understand the different ways that CRAs seek payment for the credit ratings issued and to assess the impact of the CRA Regulation on increasing the independence of credit ratings.

Q2: Please explain how you seek payment for the credit ratings you issue and whether you would consider issuing credit ratings under alternative models in the future.

(1) If not, please explain why you have not done so.

(2) If so, please explain whether these alternatives could be used in addition to or instead of your current model or models.

Q3: What was the average length of a credit rating agreement and an ancillary services agreement before June 2013 and after June 2013?

Q4: Please describe the process you would typically follow to win the right to rate a new financial instrument that an issuer wished to market, noting how this process differs under each alternative revenue model you use and explaining how this process has changed since 2010, if at all.

Q5: Please explain the process of preparing to issue a rating, and the involvement of the issuer in this process, noting how this process differs under each alternative revenue model you use and explaining how this process has changed since 2010, if at all.

¹² See Recital 10 of Regulation 462/2013 of 21 May 2013.

5.3 Transparency and disclosure requirements for credit rating agencies

37. The CRA Regulation aims to enhance transparency and investor protection by requiring CRAs to disclose information to the public on the methodologies, models and key ratings assumptions that they use, to provide information to ESMA's Central Repository (CEREP) about the past performance of credit ratings and to publish an annual transparency report giving information about how the CRA is structured and how its revenues are generated.

38. The questions in this part aim to evaluate the impact of increased transparency through these disclosure requirements on CRAs.

Q6: Do you have more information about how other CRAs approach their business development overall and specifically how they develop issue and review credit ratings than you did before 2010? If so, please explain:

(1) where this information comes from;

(2) what impact it has on your overall business development strategy; and

(3) what impact it has on how you issue and review credit ratings?

Q7: Please explain whether you issue unsolicited credit ratings, giving reasons for your answer. If your answer differs for different asset classes, please explain why.

Q8: Please explain what impact unsolicited ratings have on competition between CRAs, giving reasons for your answer.

5.4 Disclosure obligations for issuers, originators and sponsors

39. The 2013 amendments to the CRA Regulation sought to increase transparency through the introduction in Article 8b of a joint obligation on issuers, originators and sponsors to publish information on the credit quality and performance of the underlying assets of structured finance instruments.

40. The expression '*structured finance instrument*' is defined as a financial instrument or other assets resulting from a securitisation transaction or schemes '*whereby the credit risk associated with an exposure or pool of exposures is tranching, having both of the following characteristics:*

(a) payments in the transaction or scheme are dependent upon the performance of the exposure or pool of exposures; and

*(b) the subordination of tranches determines the distribution of losses during the ongoing life of the transaction or scheme’.*¹³

41. Commission Delegated Regulation 2015/3 of 30 September 2014 sets out the disclosure requirements for issuers, originators and sponsors of structured finance instruments.¹⁴ Although this Delegated Regulation will only apply from 1 January 2017, its aim of improving transparency is clear. In this part ESMA therefore wishes to understand the benefits and costs of extending these disclosure obligations to other asset classes.

Q9: Please explain whether the requirements of the CRA Regulation for issuers, originators and sponsors to make information available through a website, including information regarding the creditworthiness and performance of structured finance instruments, should be extended to other asset classes, giving reasons for your answer. If so, please explain to which products this obligation should be extended and what impact such an extension would have on your business, if any.

5.5 Multiple credit ratings

42. The 2013 amendments to the CRA Regulation introduced a number of further requirements on issuers and sponsors of structured finance instruments to obtain multiple credit ratings. These requirements are set out in Articles 8c and 8d of the CRA Regulation.

43. Article 8c of the CRA Regulation requires issuers to obtain at least two credit ratings for structured finance instruments. This obligation was introduced with the aims of restoring market confidence in complex financial instruments and reducing reliance on single credit ratings.¹⁵

44. Article 8d of the CRA Regulation aims to increase competition in the markets for credit ratings by encouraging issuers to use smaller credit rating agencies when they use multiple CRAs. Article 8d states that where issuers or related third parties intend to appoint at least two CRAs to rate an issuance or entity, they shall consider appointing at least one CRA with no more than 10% of the total market share where:

- The issuer or related third party finds that there is a CRA capable of rating the relevant issuance or entity; and
- Such a CRA is available to rate the issuance or entity in question.

45. The questions in this part aim to understand whether these provisions have achieved their objectives and the impact they have had on your business.

¹³ Article 4(1)(61) of Regulation No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation No 648/2012, OJ L 176, 27.6.2013.

¹⁴ OJ L 57, 6.1.2015, p. 2.

¹⁵ Recital 28 of Regulation 462/2013 of 21 May 2013.

Q10: Please explain what impact the following obligations on issuers have had on your business from 2013 to present:

(1) to seek two or more credit ratings for structured finance instruments;

(2) to consider using a CRA with less than 10% market share where two or more CRAs are to be appointed.

Q11: Please explain whether these obligations should be extended to some or all other rated instruments, giving reasons for your answer, and explaining which instruments where relevant.

Q12: In cases where you are aware that issuers seek multiple credit ratings for particular instruments, please explain whether you use the same strategy to compete with other CRAs to be the provider of the first credit rating as to provide the second or third rating, giving reasons for your answer.

5.6 Mandatory rotation

46. The 2013 amendments to the CRA Regulation introduced a mandatory rotation provision for CRAs issuing ratings on re-securitisations, which can be found in Article 6b of the CRA Regulation. Article 6b provides that CRAs may enter into ratings agreements for re-securitisations with a maximum length of four years, after which time they are prevented from rating new re-securitisations with underlying assets from the same originator for a period of four years.

47. The CRA Regulation notes that the implementation of a rotation mechanism should remove the incentive for a CRA to issue favourable credit ratings to issuers on the basis of their existing relationships and could encourage other CRAs to start rating these instruments.¹⁶

48. As the provision was also designed to help stimulate competition, Article 6b 2(b) of the CRA Regulation explains that mandatory rotation will cease to apply where at least four CRAs each rate more than 10% of the total number of outstanding re-securitisations.¹⁷

49. Although this provision has only recently entered into force, the questions in this part are designed to help ESMA understand the impact of this provision and the extent to which it has already been used. They also aim to assess the appropriateness of maintaining a rotation mechanism, whether, and if so how, it should be extended to other asset classes and what impact this would have on issuers and CRAs.

¹⁶ See Recital 12 of Regulation 462/2013 of 21 May 2013.

¹⁷ See Recital 15 of Regulation 462/2013 of 21 May 2013.

- Q13:** Please provide details of any experience you have had of this rotation provision to date. If you have had experience of this provision, please provide an estimate of your costs of complying with it to date.
- Q14:** Please explain whether a 4-year contract term is appropriate for this rotation provision, and if not, what would be an appropriate length?
- Q15:** Please explain whether mandatory rotation should be extended to other asset classes. If so, please:
- (1)** list the asset classes to be covered and state the appropriate contract length for each;
 - (2)** estimate the cost to your business of complying with the extension to each additional asset class covered in your response to question 15(1) above;
 - (3)** explain whether, and if so why an obligation should be introduced for CRAs to provide a handover file to the incoming CRA at the end of the maximum contract term.¹⁸
- Q16:** Please explain, giving reasons for your answer, whether, and if so how, the exemption from the mandatory rotation provision should be maintained where at least four CRAs each rate more than 10% of the total number of outstanding re-securitisations.

5.7 Compliance costs

50. This question seeks to understand the impact of some of the provisions and objectives of the CRA Regulation on your business overall.

51. Although a number of provisions only entered into force in 2013, such as Article 6a on conflicts of interest and Article 6b on mandatory rotation, any estimates that you can provide will help ESMA to assess whether the benefits of the CRA Regulation outweigh the costs of compliance for market participants or are likely to do so in the future.

- Q17.** Please provide an estimate of your overall costs of complying with the CRA Regulation each year from their date of entry into force to present. Where possible, please estimate how these costs are split between compliance with:
- (1)** The conflicts of interest provisions (Articles 6, 6a and 7);
 - (2)** The transparency and disclosure requirements (Articles 8 and 10-12);
 - (3)** The mandatory rotation provision (Article 6b);

¹⁸ See Recital 13 of Regulation 462/2013 of 21 May 2013.

(4) Other requirements of the CRA Regulation (please specify).

5.8 Market dynamics and competition between credit rating agencies

52. The aim of improving the functioning of the markets within the credit rating agency sector was a major driving force behind the development of the CRA Regulation. The CRA Regulation seeks to achieve this aim by stimulating competition between CRAs, through registration and disclosure requirements as well as through specific provisions regarding the use of multiple credit ratings mandatory rotation of CRAs.

53. The questions in this part aim to collect further information about competition between credit rating agencies and barriers to market entry and whether these have changed since the CRA Regulation entered into force in 2010.

54. ESMA would like to understand who you see as your closest competitors, meaning those who, in your view, provide credible alternatives to each of the different types of services you provide.

55. ESMA would also like to understand how your position within the CRA sector has changed over time in your view, and what you would attribute these changes to, for example business development strategy, changes in demand, innovation, market transparency, general or specific regulatory changes.

56. ESMA would also like to take your views as to whether, and if so how, competition between CRAs could be stimulated, without having a negative impact on the quality of credit ratings.

Q18: Please list your closest competitors in the provision of financial corporate and non- financial corporate ratings, sovereign ratings, structured finance ratings and ancillary services.

Q19: Please explain whether, and if so on which parameters, you compete against these competitors and other CRAs to win the business of issuers or investors, depending on the revenue model you use.

Q20: Please explain whether you would be able to start offering credit ratings for asset classes not currently rated by your CRA if you wanted to diversify your business. If so, please explain what resources would you need and estimate how long would it take to enter the market for a new asset class? If not, please explain why this would not be possible.

Q21: Please explain how your presence in and overall market shares within the CRA sector have evolved between 2010 and present. Please explain to which factors you would attribute this evolution.

Q22: Have you seen other changes to competition between CRAs for the issue of credit ratings for different asset classes and in the markets for ancillary services since 2010? If so, please explain these changes and the impact they have had on your business.

Q23: Should further measures be taken to stimulate competition between CRAs overall and/ or in respect of the rating of particular types of asset class such as structured finance instruments? If so, please explain what measures could be taken without having a negative impact on the quality of credit ratings.

5.9 Other evidence

57. If there is any other evidence or information that you would like to bring to ESMA's attention, please present it here.

6 Questions for investors and other users of credit ratings

6.1 About your organisation

58. The questions in this part aim to obtain information about the nature of the organisation you represent and the different markets in which you are active. This information will help ESMA to put your responses in context and to compare responses from similar respondents.

Q1: Please provide the name of your organisation.

Q2: Please explain whether you invest in instruments with credit ratings at local, national, EU and/or global level. If your organisation invests in instruments at EU or global level, please provide a list of the jurisdictions covered.

Q3: Please explain whether you invest in CRAs or related companies, and if so, provide a list of these and your percentage shareholding in each.

6.2 Due diligence and use of credit ratings

59. The CRA Regulation aims to increase investor protection and reduce reliance on credit ratings through a number of transparency and disclosure requirements.

60. The questions in this part aim to understand what impact the CRA Regulation has had on how you use credit ratings in the course of your business and whether there is other information which you could use to assess credit risk instead of credit ratings.

Q4: Please explain the due diligence process you follow and the types of information you consider in order to decide which instruments to invest in.

Q5: Please explain whether your overall use of credit ratings in the course of your business or in making investment decisions has increased or decreased since 2010, giving reasons for your answer.

Q6: Please explain whether and if so what information you use to assess the quality of credit ratings.

Q7: Please explain whether and if so to what extent you use internal rating models in addition to or instead of credit ratings in your business or investment decisions.

Q8: Do issuers or CRAs currently give you more information about how their credit ratings are developed, issued and revised and how their credit ratings compare to the market performance of the rated instruments than they did before 2010?

If so, does this additional information make it easier for you to understand and compare:

- (1) the ratings products and other services being offered by different CRAs;
and**
- (2) the quality of the credit risk analysis carried out on rated instruments?**

Q9: Are there other sources of information which you would use to make investment decisions instead of credit ratings?

Q10: Please explain whether and if so how your business uses unsolicited credit ratings, giving reasons for your answer.

Q11: Please explain whether, and if so how, your approaches to the issues raised in questions 4-10 above have changed since 2010.

6.3 Independence and quality of credit ratings

61. One of the aims of the CRA Regulation is to increase the quality of credit ratings by seeking to reduce the conflicts of interest inherent where issuers pay for the rating of their financial instruments.¹⁹

62. The questions in this part aim to understand the different ways that CRAs can seek payment for the credit ratings issued and to assess the impact of the CRA Regulation on increasing the quality and independence of credit ratings.

Q12: Please explain in which circumstances you currently pay for credit ratings. If you do not currently pay for credit ratings, please explain whether, and if so under which circumstances, you would be willing to pay for credit ratings.

Q13: Irrespective of whether you pay for credit ratings, please explain the circumstances in which links or existing relationships between an issuer of a particular instrument and a CRA would have an impact on how you would use a credit rating of that instrument.

Q14: Please explain whether the quality of credit ratings has increased or decreased since 2010, giving reasons for your answer.

Q15: Please explain what, if any, further measures could be taken to increase the quality of ratings, giving reasons for your answer.

¹⁹ See Recital 10 of Regulation 462/2013 of 21 May 2013.

6.4 Multiple credit ratings

63. The 2013 amendments to the CRA Regulation introduced a number of requirements on issuers and sponsors of structured finance instruments to obtain multiple credit ratings. These requirements are set out in Articles 8c and 8d of the CRA Regulation.

64. Article 8c of the CRA Regulation requires issuers to obtain at least two credit ratings for structured finance instruments. This obligation was introduced with the aims of restoring market confidence in complex financial instruments and reducing reliance on single credit ratings.²⁰

65. Article 8d of the CRA Regulation aims to increase competition between CRAs by encouraging issuers to use smaller CRAs when they use multiple CRAs. Article 8d states that where issuers or related third parties intend to appoint at least two CRAs to rate an issuance or entity, they shall consider appointing at least one CRA with no more than 10% of the total market share where possible (hereinafter 'small CRA').

66. The question in this part aim to understand whether these provisions have achieved their objectives and the impact they have had on your business.

Q16: Please explain what impact multiple credit ratings of the same instrument have on your investment or business decisions.

Q17: Please explain whether in your view, issuers should be obliged to obtain multiple credit ratings in respect of some or all asset classes and if so, how many ratings per asset class should be required.

Q18: Please explain whether you would use ratings from a small CRA, giving reasons for your answer. Please explain whether, and if so how, your approach to this issue has changed since 2010.

Q19: Please explain whether you would use ratings from a CRA who has not previously rated a particular asset class, giving reasons for your answer. Please explain whether, and if so how, your approach to this issue has changed since 2010.

6.5 Disclosure requirements for structured finance instruments

67. The 2013 amendments to the CRA Regulation sought to increase transparency through the introduction in Article 8b of a joint obligation on issuers, originators and sponsors to publish information on the credit quality and performance of the underlying assets of structured finance instruments.

²⁰ See Recital 28 of Regulation 462/2013 of 21 May 2013.

68. The expression 'structured finance instrument' is defined as a financial instrument or other assets resulting from a securitisation transaction or schemes 'whereby the credit risk associated with an exposure or pool of exposures is tranced, having both of the following characteristics:

(a) payments in the transaction or scheme are dependent upon the performance of the exposure or pool of exposures; and

(b) the subordination of tranches determines the distribution of losses during the ongoing life of the transaction or scheme'.²¹

69. Commission Delegated Regulation 2015/3 of 30 September 2014 sets out the disclosure requirements for issuers, originators and sponsors of structured finance instruments.²² Although this Delegated Regulation will only apply from 1 January 2017, its aim of improving transparency is clear. In this part ESMA therefore wishes to understand the benefits and costs of extending these disclosure obligations to other asset classes.

Q20: Please explain whether the requirements of the CRA Regulation for issuers, originators and sponsors to make information available through a website, including information regarding the creditworthiness and performance of structured finance instruments, are sufficient or should be extended to other asset classes, giving reasons for your answer. If so, please explain to which products this obligation should be extended.

6.6 Mandatory rotation

70. The 2013 amendments to the CRA Regulation introduced a mandatory rotation provision for CRAs issuing ratings on re-securitisations, which can be found in Article 6b of the CRA Regulation. Article 6b provides that CRAs may enter into ratings agreements for re-securitisations with a maximum length of four years, after which time they are prevented from rating new re-securitisations with underlying assets from the same originator for a period of four years.

71. The CRA Regulation notes that the implementation of a rotation mechanism should remove the incentive for a CRA to give favourable credit ratings to issuers on the basis of their existing relationships and could encourage other CRAs to start rating these instruments.²³

²¹ Article 4(1)(61) of Regulation No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation No 648/2012, OJ L 176, 27.6.2013.

²² OJ L 57, 6.1.2015, p. 2.

²³ See Recital 12 of Regulation 462/2013 of 21 May 2013.

72. As the provision was also designed to help stimulate competition, Article 6b2(b) of the CRA Regulation explains that mandatory rotation will cease to apply where at least four CRAs each rate more than 10% of the total number of outstanding re-securitisations.²⁴

73. Although this provision has only recently entered into force, the questions in this part are designed to help ESMA understand the impact of this provision and the extent to which it has already been used. They also aim to assess the appropriateness of maintaining a rotation mechanism, whether, and if so how, it should be extended to other asset classes and what impact this would have on issuers and CRAs.

Q21: Please provide details of any experience you have had of this rotation provision to date.

Q22: Please explain whether a 4-year contract term is appropriate for this rotation provision, and if not, what would be an appropriate length?

Q23: Please explain whether mandatory rotation should be extended to other asset classes. If so, please:

(1) list the asset classes to be covered and state the appropriate contract length for each;

(2) explain whether, and if so why an obligation should be introduced for CRAs to provide a handover file to the incoming CRA at the end of the maximum contract term.²⁵

Q24: Please explain, giving reasons for your answer whether, and if so how, the exemption from the mandatory rotation provision should be maintained where at least four CRAs each rate more than 10% of the total number of outstanding re-securitisations.

6.7 Competition between credit rating agencies

74. The aim of improving the functioning of the markets within the CRA sector was a major driving force behind the development of the CRA Regulation. The CRA Regulation seeks to achieve this aim by stimulating competition between CRAs, through registration and disclosure requirements as well as through specific provisions regarding the use of multiple credit ratings and the mandatory rotation of CRAs.

75. The questions in this part aim to collect further information about competition between credit rating agencies and whether competition between CRAs has changed since the CRA Regulation entered into force in 2010.

²⁴ See Recital 15 of Regulation 462/2013 of 21 May 2013.

²⁵ See Recital 13 of Regulation 462/2013 of 21 May 2013.

76. ESMA would also like to take your views as to whether, and if so how, competition between CRAs could be stimulated without having a negative impact on the quality of credit ratings.

Q25: Please explain whether you are aware of any competition between CRAs. If so, please explain on which of the following parameters CRAs currently compete:

- (1) quality of rating;**
- (2) relationship with issuers;**
- (3) investor relationships;**
- (4) by asset class;**
- (5) by price to issuer;**
- (6) by level of rating;**
- (7) through the offer of ancillary or non-ratings services; and/or**
- (8) other (please specify).**

Q26: If you have been aware of competition between CRAs, please explain whether, and if so how, the nature of competition between them has changed between 2010 and present.

Q27: Should further measures be taken to stimulate competition between CRAs overall and/ or in respect of the rating of particular types of asset class such as structured finance instruments? If so, please explain what measures could be taken without having a negative impact on the quality of credit ratings.

6.8 Other evidence

77. If there is any other evidence or information that you would like to bring to ESMA's attention, please present it here.

Annex I Mandate to provide Technical Advice

1. Article 39(5) of the CRA Regulation provides that:

'The Commission shall, after obtaining technical advice from ESMA, review the situation in the credit rating market. Following that review, the Commission shall, by 1 January 2016, submit a report to the European Parliament and to the Council, accompanied by a legislative proposal if appropriate, assessing, in particular:

- (a) Whether there is a need to extend the scope of the obligations referred to in Article 8b to include any other financial credit products;*
- (b) Whether the requirements referred to in Articles 6, 6a and 7 have sufficiently mitigated conflicts of interest;*
- (c) Whether the scope of the rotation mechanism referred to in Article 6b should be extended to other asset classes and whether it is appropriate to use differentiated lengths of periods across asset classes;*
- (d) The appropriateness of existing and alternative remuneration models;*
- (e) Whether there is a need to implement other measures to foster competition in the credit rating market;*
- (f) The appropriateness of additional initiatives to promote competition in the credit rating market against the background of the evolution of the structure of the sector;*
- (g) Whether there is a need to propose measures to reduce overreliance on ratings.²⁶*
- (h) The market concentration levels, the risks arising from high concentration and the impact on the overall stability of the financial sector.'*

2. Article 39(4) of the CRA Regulation states that:

'The Commission shall, after obtaining technical advice from ESMA, review the situation in the credit rating market for structured finance instruments, in particular the credit rating market for re-securitisations. Following that review, the Commission shall, by 1 July 2016 submit a report to the European Parliament and to the Council, accompanied by a legislative proposal if appropriate, assessing in particular:

- (a) The availability of sufficient choice to comply with the requirements set out in Articles 6b and 8c;*

²⁶ Input for this section of the report will be provided from the reducing reliance on ratings work currently underway to produce the reports set out in Article 39(b).

(b) Whether it is appropriate to shorten or extend the maximum duration of the contractual relationship referred to in Article 6b(1) and the minimum period before the credit rating agency may re-enter into a contract with an issuer or a related third party for the issuing of credit ratings on re-securitisations referred to in Article 6b(3);

(c) Whether it is appropriate to amend the exemption referred to in the second sub paragraph of Article 6b(2).'

3. ESMA received a request for Technical Advice from the European Commission by letter of 22 December 2014 which covered the Technical Advice to be provided in accordance with Articles 39(b)1 as well as Article 39(4) and 39(5) of the CRA Regulation.