

# EUROPEAN PARLIAMENT

2004



2009

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*Committee on Legal Affairs*

**2008/0217(COD)**

10.3.2009

## **OPINION**

of the Committee on Legal Affairs

for the Committee on Economic and Monetary Affairs

on the proposal for a regulation of the European Parliament and of the Council  
on Credit Rating Agencies  
(COM(2008)0704 – C6-0397/2008 – 2008/0217(COD))

Rapporteur: Sharon Bowles

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## SHORT JUSTIFICATION

The Commission proposal seeks to establish a legally binding registration and surveillance regime for credit rating agencies issuing credit ratings mainly intended for use for regulatory purposes by credit institutions, investment firms, insurance, assurance and reinsurance undertakings, collective investment schemes and pension funds. The main objective of the proposal is to ensure that credit ratings used in the Community are independent, objective and of the highest quality.

The draughtsperson raises the following main points within the JURI usual sphere of competences:

### **Is it correct for the proposal be based on article 95 of the Treaty establishing the European Community as proposed, or should it be based on its article 47(2)?**

Article 95 relates to the establishment and functioning of the internal market.

Article 47(2) of the Treaty, which is part of Chapter 2 on Freedom of establishment, relates to 'Free circulation of persons, services and capital' and the entirety of the harmonising measures for financial services in the European Union have hitherto been adopted on the legal basis of article 47(2). This is in particular the case for credit institutions (Directive 2006/48/EC), investment firms (Directive 2004/39/EC), assurance undertakings (Directive 2002/83), reinsurance undertakings (Directive 2005/68/EC), undertakings for collective investment in transferable securities (UCITS-under recast), institutions for occupational retirement (Directive 2003/41/EC).

For consistency, the objective of the current proposal, to set up the conditions under which credit rating agencies can establish and operate within the European Union, would also appear to fall under article 47(2).

### **Should the proposal be in the form of a Regulation or a Directive?**

The reasons for preferring a Regulation to a Directive in the current context and financial climate, and in order to get a consistent and rapid implementation are understood. However article 47.2 prescribes that the coordination concerning the taking-up and pursuit of the stipulated activities or professions be enacted solely by way of Directives, and excludes the use of Regulations.

If the case for having a Regulation in this particular instance is thought compelling, and therefore Article 95 is maintained as the basis, its implications should be considered.

### **Governance Criteria**

Within the governance criteria in Section A of the annex it is proposed that non-executive directors undertake certain responsibilities aimed at ensuring independence of ratings. This is a role in essence to protect external parties: investors and markets. It is not clear whether this is in all circumstances a proper function for a non-executive director who also represents the

shareholders. In some Member States it may be possible for non-executive directors to have such a function, but there is no need to be so prescriptive and the draughtsperson proposes that the administrative or supervisory board be subject to persons performing an independent monitoring function. This could be non-executive directors if that is appropriate. For a group of rating agencies there is no need for duplication, the function could be for the whole group.

## Civil Liability

The present proposal suggests that the regulation will facilitate litigation. The draughtsperson considers that there is no reason to extend the current civil liabilities available within Member States which in general already cover cases of gross negligence and malpractice. Indeed it would be dangerous to encourage, or facilitate, litigation that might influence rating decisions and give rise to a route to blackmail and undermine the very independence that it is sought to ensure and maintain. Caution is urged in this area and amendment is proposed to clarify that there is no intention to extend the current regime of liability.

## AMENDMENTS

The Committee on Legal Affairs calls on the Committee on Economic and Monetary Affairs, as the committee responsible, to incorporate the following amendments in its report:

### Amendment 1

#### Proposal for a regulation Recital 13

##### *Text proposed by the Commission*

(13) Long lasting relationships with the same rated entities or *its* related third parties could compromise independence of analysts **and persons approving credit ratings**. Therefore those analysts **and persons** should be subject to a rotation mechanism.

##### *Amendment*

(13) Long lasting relationships with the same rated entities or related third parties could compromise *the* independence of analysts **who are in direct contact with issuers**. Therefore those analysts should be subject to a **mandatory** rotation mechanism.

##### *Justification*

*Conflict of interests for analysts that are in frequent contact with issuers should be prevented. The rating committees are not in direct contact and have valuable sectoral expertise.*

## Amendment 2

### Proposal for a regulation Recital 15

#### *Text proposed by the Commission*

(15) In order to ensure the quality of ratings, a credit rating agency should take measures to ensure that the information it use in assigning a rating is reliable. For this purpose, a credit rating agency may envisage, among other elements reliance on independently audited financial statements and public disclosures; verification by reputable third party services; random sampling examination by the credit rating agency of the information received; or contractual provisions clearly stipulating liability for the rated entity or its related third parties, if the information provided under the contract is knowingly materially false or misleading or if the rated entity or its related third parties fail to conduct reasonable due diligence regarding the accuracy of the information as specified under the terms of the contract.

#### *Amendment*

(15) In order to ensure the quality of ratings, a credit rating agency should take measures to ensure that the information it *uses* in assigning a rating is reliable. ***The role of a credit rating agency is not to audit data produced and due diligence conducted by issuers and third parties, but rather it must satisfy itself that the sources that it relies upon justify that trust, for example, due to their professional independence or reputation.*** For this purpose, a credit rating agency may envisage, among other elements reliance on independently audited financial statements and public disclosures; verification by reputable third party services; random sampling examination by the credit rating agency of the information received; or contractual provisions ***in the transaction documents*** clearly stipulating liability for the rated entity or its related third parties, if the information provided under the contract is knowingly materially false or misleading or if the rated entity or its related third parties fail to conduct reasonable due diligence regarding the accuracy of the information as specified under the terms of the contract.

#### *Justification*

*There is a need to avoid confusion over the role of rating agencies with respect to the due diligence conducted by other parties and on which the rating agencies rely.*

### Amendment 3

#### Proposal for a regulation Recital 35

*Text proposed by the Commission*

***(35) The stricter and clearer legal framework within which credit rating agencies will operate should also facilitate recourse to civil actions in respect of credit rating agencies in appropriate cases, in accordance with the applicable regimes of liability of the Member States.***

*Amendment*

***(35) This Regulation is without prejudice to national law governing the right of civil action in respect of credit rating agencies.***

### Amendment 4

#### Proposal for a regulation Article 2 – paragraph 1

*Text proposed by the Commission*

1. This Regulation shall apply to credit ratings that are intended for use for regulatory purposes ***or otherwise*** by credit institutions as defined in Directive 2006/48/EC, investment firms as defined in Directive 2004/39/EC of the European Parliament and of the Council, insurance undertakings subject to Council Directive 73/239/EEC, assurance undertakings as defined in Directive 2002/83/EC of the European Parliament and of the Council, reinsurance undertakings as defined in Directive 2005/68/EC of the European Parliament and the Council, undertakings for collective investment in transferable securities (UCITS) as defined in Directive [2009/XX/EC] or institutions for occupational retirement provision as defined in Directive 2003/41/EC of the European Parliament and of the Council and are disclosed publicly or distributed by subscription.

*Amendment*

This Regulation shall apply to credit ratings that are intended for use for regulatory purposes by credit institutions as defined in Directive 2006/48/EC, investment firms as defined in Directive 2004/39/EC of the European Parliament and of the Council, insurance undertakings subject to Council Directive 73/239/EEC assurance undertakings as defined in Directive 2002/83/EC of the European Parliament and of the Council, reinsurance undertakings as defined in Directive 2005/68/EC of the European Parliament and the Council, undertakings for collective investment in transferable securities (UCITS) as defined in Directive [2009/XX/EC] or institutions for occupational retirement provision as defined in Directive 2003/41/EC of the European Parliament and of the Council and are disclosed publicly or distributed by subscription.

*Justification*

*The regulation's scope of application must be clearly defined by use for regulatory purposes.*

*The most adversely impacted by too wide a scope will be investors and other users.*

## **Amendment 5**

### **Proposal for a regulation**

#### **Article 6 – paragraph 4 – subparagraph 1**

##### *Text proposed by the Commission*

4. A credit rating agency shall ensure that analysts ***and persons approving credit ratings*** shall not be involved in providing the credit rating services to the same rated entity or its related third parties for a period exceeding four years. For that purpose it shall establish a rotation mechanism ***with regard to those analysts and persons***.

##### *Amendment*

4. A credit rating agency shall ensure that analysts ***who are in direct contact with issuers*** shall not be involved in providing the credit rating services to the same rated entity or its related third parties for a period exceeding four years. For that purpose it shall establish a rotation mechanism.

##### *Justification*

*Conflict of interests for analysts that are in frequent contact with issuers should be prevented. The rating committees are not in direct contact and have valuable sectoral expertise.*

## **Amendment 6**

### **Proposal for a regulation**

#### **Article 6 – paragraph 4 – subparagraph 2**

##### *Text proposed by the Commission*

The period after which the analysts ***and persons approving credit ratings*** may be ***involved in providing the credit rating services to*** the rated entity or related third parties referred to in the first subparagraph may not be shorter than two years.

##### *Amendment*

The period after which the analysts may be ***in direct contact again with*** the rated entity or related third parties referred to in the first subparagraph, ***in order to provide credit rating services***, may not be shorter than two years.

##### *Justification*

*Conflict of interests for analysts that are in frequent contact with issuers should be prevented. The rating committees are not in direct contact and have valuable sectoral expertise.*

## Amendment 7

### Proposal for a regulation

#### Article 20 – paragraph 3 – point a

*Text proposed by the Commission*

(a) have access to any document in any form and to receive or take a copy thereof;

*Amendment*

(a) have access to any document in any form and to receive or take a copy thereof ***for use in their supervisory capacity***;

## Amendment 8

### Proposal for a regulation

#### Article 20 – paragraph 3 – point b

*Text proposed by the Commission*

(b) demand information from any person and if necessary to summon and question a person with a view to obtaining information;

*Amendment*

(b) demand information from any person and if necessary to summon and question a person with a view to obtaining information ***for use in their supervisory capacity***;

## Amendment 9

### Proposal for a regulation

#### Article 20 – paragraph 3 – subparagraph 1 a (new)

*Text proposed by the Commission*

*Amendment*

***When exercising these powers the same rules concerning professional secrecy and legal professional privilege shall apply under the laws of the Member State as apply in other supervisory procedures for financial markets.***

## Amendment 10

### Proposal for a regulation

#### Article 21 – paragraph 1 – introductory part

*Text proposed by the Commission*

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*Amendment*

1. The competent authority of the home



Member State may take the following measures:

Member State may take the following measures *in the event of a breach of this Regulation*:

## Amendment 11

### Proposal for a regulation Article 28 – paragraph 1

*Text proposed by the Commission*

1. The obligation of professional secrecy shall apply to all persons who work or who have worked for the competent authority or for any authority or person to whom the competent authority has delegated tasks, including auditors and experts contracted by the competent authority. Information covered by professional secrecy may not be disclosed to any other person or authority except when such disclosure is necessary for legal proceedings.

*Amendment*

1. The obligation of professional secrecy shall apply to all persons who work or who have worked for the competent authority, ***the CESR*** or for any authority or person to whom the competent authority has delegated tasks, including auditors and experts contracted by the competent authority. Information covered by professional secrecy may not be disclosed to any other person or authority except when such disclosure is necessary for legal proceedings.

## Amendment 12

### Proposal for a regulation Article 31 – paragraph 1 a (new)

*Text proposed by the Commission*

*Amendment*

***An infringement of the provisions of this Regulation does not of itself give any right of action for damages by third party litigants and such claims may only be made in accordance with the applicable national law on civil liability.***

*Justification*

*The new paragraph which follows the first paragraph is introduced for the avoidance of doubt. The test should be that expounded in the first paragraph as implemented in national law.*

## Amendment 13

**Proposal for a regulation**  
**Article 31 – paragraph 2 a (new)**

*Text proposed by the Commission*

*Amendment*

***The CESR shall promote convergence in the rules applicable to infringements of the provisions of this Regulation.***

*Justification*

*CESR should work towards convergence in the rules applicable to infringements of the provisions of this Regulation so to avoid arbitrage.*

**Amendment 14**

**Proposal for a regulation**  
**Article 31 a (new)**

*Text proposed by the Commission*

*Amendment*

***Article 31a***

***Complaints***

***The CESR shall ensure that procedures are set up which allow issuers, investors and other interested parties to submit complaints about the fulfilment of the requirements and conditions laid down in this Regulation. All complaints shall be dealt with diligently and in confidence.***

*Justification*

*Instead of undue litigation procedures, effective complaints procedures should be stimulated and established. CESR should be authority in charge in order to prevent arbitrage.*

**Amendment 15**

**Proposal for a regulation**  
**Article 31 b (new)**

*Text proposed by the Commission*

*Amendment*

***Article 31b***

***Out-of-court redress***

***1. Member States shall encourage the***

*setting-up of appropriate and effective complaints and redress procedures for the out-of-court settlement of disputes between credit rating agencies and issuers, investors and, where appropriate, other interested parties concerning the fulfilment or non-fulfilment of the requirements and conditions laid down in this Regulation.*

*2. Member States shall encourage these bodies to cooperate in the resolution of cross-border disputes.*

*3. The CESR shall promote convergence in the complaints and redress procedures.*

*Justification*

*Instead of undue litigation procedures, effective complaints procedures should be stimulated and established.*

**Amendment 16**

**Proposal for a regulation**

**Annex I - Section D - Chapter I - point 3 – subparagraph 2 a (new)**

*Text proposed by the Commission*

*Amendment*

*In the event of changes in the quality of information available for monitoring an existing rating, this shall be publicised and appropriate revision to the rating shall be made.*

## PROCEDURE

<b>Title</b>	Credit rating agencies
<b>References</b>	COM(2008)0704 – C6-0397/2008 – 2008/0217(COD)
<b>Committee responsible</b>	ECON
<b>Opinion by</b> Date announced in plenary	JURI 20.11.2008
<b>Rapporteur</b> Date appointed	Sharon Bowles 19.1.2009
<b>Discussed in committee</b>	12.2.2009
<b>Date adopted</b>	9.3.2009
<b>Result of final vote</b>	+: 16 -: 0 0: 0
<b>Members present for the final vote</b>	Monica Frassoni, Giuseppe Gargani, Neena Gill, Klaus-Heiner Lehne, Manuel Medina Ortega, Eva-Riitta Siitonen, Francesco Enrico Speroni, Diana Wallis, Tadeusz Zwiefka
<b>Substitute(s) present for the final vote</b>	Vicente Miguel Garcés Ramón, Jean-Paul Gauzès, Kurt Lechner, Georgios Papastamkos, Gabriele Stauner, Ieke van den Burg
<b>Substitute(s) under Rule 178(2) present for the final vote</b>	Bill Newton Dunn