

PRESS RELEASE

ESMA issues Guidelines on endorsement and clarifies the use for regulatory purposes of credit ratings issued outside the European Union after 6 June 2011

ESMA issues today its Guidelines on endorsement (ESMA/2011/139) in a Final Report, including a Feedback Statement.

The Guidelines address how ESMA will implement the “*as stringent as*” test for credit ratings produced outside the European Union, in what are named “third countries”. These credit ratings are used by financial institutions to assess the risk of their exposures and in calculating their capital requirements. The test requires that the credit rating activities performed by Credit Rating Agencies (CRAs) outside the European Union are subject to requirements established by law which are “*as stringent as*” those applicable in the EU.

- *Key phases concerning the use of non EU credit ratings which are not endorsable*

ESMA’s Guidelines clarify that EU CRAs can continue to issue credit ratings produced outside the EU after the 6 June at least until the point of registration.

If at the point of a CRA’s registration, credit ratings issued outside the EU are not considered endorsable in the European Union, because an appropriate regulatory regime has not entered into force in the relevant third country (or the other necessary conditions as set out in the Regulation are not in place), the use of such credit ratings for regulatory purposes by financial institutions will still be possible for three months from that date.

ESMA will assess whether the use of such credit ratings can continue for another three month period, in order to avoid the potential for market disruption or financial instability. This would be communicated to the market as soon as the decision is taken.

According to Article 40 and Article 24 (2) the possibility to keep using credit ratings issued outside the EU for a period of three months (and potentially for a further 3 months), is embedded in the EU Regulation (please see the ‘notes for editors’ for further details).

- *Disclosure*

After registration, EU CRAs will be asked to indicate to the public those credit ratings issued in third countries which are not endorsable in the EU, and to clarify that these credit ratings can still be used for an initial period of three months. ESMA in turn will disclose relevant information concerning these circumstances to the public.



- *Implementing the conditions for endorsement*

In order to assess whether a third-country regulatory regime has met the conditions for endorsement, ESMA will continue to apply the approach outlined by CESR in June 2010 (Ref. CESR/10-347). This requires a third country to have adopted rules as "*stringent as*" those provided by the EU CRA legislation. It is a safeguard provided by the Regulation to ensure the quality of ratings used in the European Union.

However, as set out in the Guidelines, there will be flexibility in assessing the requirements applicable in the third country. The wording of the provisions will not need to be identical to those set out in the EU Regulation. ESMA will take a global and holistic view in assessing to what extent the third country legal framework achieves similar adequate regulatory effects and meets the same objectives as the EU Regulation.

Where the EU-Commission has recognised that the regulatory regime of a third country is equivalent to the EU Regulation, it is possible to refer to this decision in respect of the "*as stringent as*" test set out in Article 4 (3) (b).

In this regard, CESR (as ESMA's predecessor) has been mandated by the European Commission to review the equivalence of four countries (Australia, Canada, Japan, and the US). The Commission has identified Japan's regulatory regime as equivalent through a formal decision in September 2010. Regarding the US, no formal equivalence decision has yet been taken. However, ESMA is monitoring the improvements to the legislation anticipated by the Dodd-Frank Act and will be able to continue its assessment as soon as the draft secondary legislation is disclosed by the SEC.

In any event, when ESMA assesses the legal and regulatory framework of a third country and concludes the "*as stringent as*" test with a positive result, the credit ratings issued in that particular third country are eligible for endorsement also in the absence of a Commission equivalence decision.

ESMA has carried out some work on a number of other jurisdictions in order to assess the requirements of Article 4(3).



Notes for editors

1. In June 2010, CESR has issued its Guidance on “*Registration Process, Functioning of Colleges, Mediation Protocol, Information set out in Annex II, Information set for the application for Certification and for the assessment of CRAs systemic importance*” (CESR/10-347). The Guidance has touched for the first time on the implementation of the endorsement regime post 7 June 2011, when also the conditions set out in points (f), (g) and (h) of Article 4 (3) will enter into force.
2. The position expressed in June 2010 CESR’s Guidance supports that, after 7 June 2011, the “*as stringent as*” requirements mentioned in Article 4 (3) (b) of Regulation no. 1060/2009 will have to be established by law or regulation in the third countries where the endorsed ratings are issued. This position is consistent with the informal interpretation provided to CESR, and more restated to ESMA, by the Commission Services.
3. In light of the institutional change of CESR into ESMA from 1 January 2011, the coming legislative text amending the EU Regulation on CRAs has required ESMA (Article 21 (3)) to “*issue and update guidelines on the application of the endorsement regime under Article 4(3) of this Regulation by 7 June 2011*”.
4. In order to be able to comply with this obligation, and at the same time fulfil the procedural requirements spelled out in article 16 of its establishing Regulation (no 1095/2010/EU), ESMA has published a Call for Evidence on “*the criteria for endorsement (Article 21 (2)(a) of the draft amended CRA Regulation)*” (ESMA/2011/005) in January 2011, and a Consultation Paper on “*ESMA Guidelines on the application of the endorsement regime under Article 4 (3) of the Credit Rating Regulation 1060/2009*” (ESMA/2011/097), including cost/benefit analysis, in March 2011. Both documents, and in particular the Consultation Paper, have reiterated that the position expressed by CESR in June 2010 was the only one under consideration by ESMA.
5. Article 40 of the Regulation no. 1060/2009 on Credit Rating Agencies (CRAs) states that CRAs which have applied for registration before 7 September 2010 may continue to issue credit ratings that can be used for regulatory purposes by the financial institutions unless registration is refused.
6. These provisions apply also in regard of the credit ratings that EU CRAs endorse from third country CRAs, in accordance to Article 4(2) and (4) of the Regulation. Consequently, pending the decision on their registration, which also regards the endorsement of ratings, CRAs can keep endorsing ratings, and financial institutions may continue using these ratings for regulatory purposes.
7. If, when registering CRAs, national competent authorities decided to refuse the endorsement of ratings issued in particular countries, provided the conditions in Article 4(3) of the Regulation are not met, financial institutions may still continue using these credit ratings for regulatory purposes during a period of three months (Article 24 (2)).
8. Furthermore, according to the third subparagraph of Article 24 (2) of the Regulation, competent authorities may again extend the possibility to use those non-endorsable ratings for regulatory purposes in the Community for other additional three months, provided that exceptional circumstances occur that may imply potential market disruption or financial instability. The power to decide on this possible additional three months extension of the use for regulatory purposes of non-endorsable ratings in the Community will be transferred to ESMA by the coming amendment of the EU Regulation on CRAs.



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