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**COMMISSION STAFF WORKING DOCUMENT**  
*Accompanying the document*

**Report from the Commission to the Council and the European Parliament**  
**on the feasibility of a network of smaller credit rating agencies**

## **Section 1- Data on CRAs market**

**Table 1. List of CRAs registered and certified by ESMA (as of 31 August 2013)**

<b>Credit Rating Agency</b>	<b>Country of residence</b>	<b>Status</b>	<b>Effective date of registration</b>
Euler Hermes Rating GmbH	DE	Registered	16/11/2010
Japan Credit Rating Agency Ltd	JP	Certified	06/01/2011
BCRA-Credit Rating Agency AD	BG	Registered	06/04/2011
Feri EuroRating Services AG	DE	Registered	14/04/2011
Creditreform Rating AG	DE	Registered	18/05/2011
Scope Credit Rating GmbH (formerly PSR Rating GmbH)	DE	Registered	24/05/2011
ICAP Group SA	GR	Registered	07/07/2011
GBB-Rating Gesellschaft für Bonitätsbeurteilung mbH	DE	Registered	28/07/2011
ASSEKURATA Assekuranz Rating-Agentur GmbH	DE	Registered	18/08/2011
Companhia Portuguesa de Rating, S.A. (CPR)	PT	Registered	26/08/2011
AM Best Europe-Rating Services Ltd. (AMBERS)	UK	Registered	08/09/2011
DBRS Ratings Limited	UK	Registered	31/10/2011
Fitch	DE, ES, FR, IT, PL, UK (2 entities)	Registered	31/10/2011
Moody's	CY, DE, ES, FR, IT, UK	Registered	31/10/2011
Standard & Poor's	FR, IT, UK	Registered	31/10/2011
CRIF S.p.A.	IT	Registered	22/12/2011
Capital Intelligence (Cyprus) Ltd	CY	Registered	08/05/2012
European Rating Agency, a.s.	SK	Registered	30/07/2012
Axesor SA	ES	Registered	01/10/2012
CERVED Group S.p.A.	IT	Registered	20/12/2012
Kroll Bond Rating Agency	US	Certified	20/03/2013
The Economist Intelligence Unit Ltd	UK	Registered	03/06/2013
Dagong Europe Credit Rating Srl (Dagong Europe)	IT	Registered	13/06/2013
Spread Research SAS	FR	Registered	01/07/2013

Source: ESMA website (<http://www.esma.europa.eu/page/List-registered-and-certified-CRAs>)

**Table 2. EU outstanding corporate, financials and insurance credit ratings by country of issuer (as of 31 December 2012)**

Country of issuer	AM Best Europe	ASSETA	BCRA	Capital Intelligence	CERVED	CPR	Credit reform	CRIF	DBRS	Euler Hermes Rating	GBB	ICAP	JCR	Scope Credit Rating	Fitch	Moody's	Standard & Poor's
Austria	1						3							4	16	27	33
Belgium	2								5						25	23	45
Bulgaria			23												8		6
Cyprus	1			6											6	8	8
Czech Republic				8										1	5	6	9
Denmark									2						19	22	37
Estonia																3	1
Finland	1												2		19	18	41
France	13								7				2	1	95	129	296
Germany	27	41					83		10	28	185		1	60	134	141	344
Greece				12								1958			9	2	16
Hungary				6											4	1	12
Iceland																2	3
Ireland	25								8						31	68	83
Italy	2				29078			62	1					5	88	55	126
Latvia																1	
Liechtenstein	4														1	1	4
Lithuania															1		2

Country of issuer	AM Best Europe	ASSEKURATA	BCRA	Capital Intelligence	CERVED	CPR	Credit reform	CRIF	DBRS	Euler Hermes Rating	GBB	ICAP	JCR	Scope Credit Rating	Fitch	Moody's	Standard & Poor's
Luxembourg	7						5								47	120	83
Malta	1														4	1	5
Netherlands	2						1		8					1	63	175	158
Norway									2						29	26	39
Poland	1			10											20	7	21
Portugal						7			7						25	19	28
Romania				6											9		1
Slovakia				4											4	2	1
Slovenia	1			12										3	12	2	4
Spain	5								10				1		86	57	75
Sweden	2								9					1	16	48	89
United Kingdom	67						1		23				2	1	467	343	444
<b>Total</b>	<b>162</b>	<b>41</b>	<b>23</b>	<b>64</b>	<b>29078</b>	<b>7</b>	<b>93</b>	<b>62</b>	<b>92</b>	<b>28</b>	<b>185</b>	<b>1958</b>	<b>8</b>	<b>77</b>	<b>1243</b>	<b>1307</b>	<b>2014</b>

Source: CEREP

**Table 3. Classes of EU outstanding ratings (as of 31 December 2012)**

Credit Rating Agency	Types of ratings issued	Corporate	Financials	Insurance	Sovereign and Public Finance	Structured Finance
AM Best Europe-Rating Services Ltd. (AMBERS)	2	Yes	No	Yes	No	No
ASSEKURATA Assekuranz Rating-Agentur GmbH	1	No	No	Yes	No	No
BCRA-Credit Rating Agency AD	3	No	Yes	Yes	Yes	No
Capital Intelligence (Cyprus) Ltd	2	No	Yes	No	Yes	No
CERVED Group S.p.A.	1	Yes	No	No	No	No
Companhia Portuguesa de Rating, S.A. (CPR)	2	Yes	Yes	No	No	No
Creditreform Rating AG	1	Yes	No	No	No	No
CRIF S.p.A.	1	Yes	No	No	No	No
DBRS Ratings Limited	4	Yes	Yes	No	Yes	Yes
Euler Hermes Rating GmbH	2	Yes	Yes	No	No	No
European Rating Agency, a.s.	1	No	No	No	Yes	No
Feri EuroRating Services AG	1	No	No	No	Yes	No
GBB-Rating Gesellschaft für Bonitätsbeurteilung mbH	1	No	Yes	No	No	No
ICAP Group SA	1	Yes	No	No	No	No
Japan Credit Rating Agency Ltd	3	Yes	Yes	No	Yes	No
Scope Credit Rating GmbH	1	Yes	No	No	No	No
Fitch	5	Yes	Yes	Yes	Yes	Yes
Moody's	5	Yes	Yes	Yes	Yes	Yes
Standard & Poor's	5	Yes	Yes	Yes	Yes	Yes

Source: CEREP

**Table 4. EU outstanding credit ratings (as of 31 December 2011 and 31 December 2012)**

Credit Rating Agency	Corporate		Financials		Insurance		Sovereign and Public Finance		Structured Finance		Total		Variation 2012/2011
	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	
AM Best Europe-Rating Services Ltd. (AMBERS)	18	13	0	0	154	149	0	0	0	0	172	162	-5,8%
ASSEKURATA Assekuranz Rating-Agentur GmbH	0	0	0	0	45	41	0	0	0	0	45	41	-8,9%
BCRA-Credit Rating Agency AD	0	0	12	16	6	7	4	5	0	0	22	28	27,3%
Capital Intelligence (Cyprus) Ltd	0	0	68	64	0	0	28	6	0	0	96	70	-27,1%
CERVED Group S.p.A.	57782	29078	0	0	0	0	0	0	0	0	57782	29078	-49,7%
Companhia Portuguesa de Rating, S.A. (CPR)	8	6	0	1	0	0	0	0	0	0	8	7	-12,5%
Creditreform Rating AG	78	93	0	0	0	0	0	0	0	0	78	93	19,2%
CRIF S.p.A.	62	62	0	0	0	0	0	0	0	0	62	62	0,0%
DBRS Ratings Limited	10	13	76	79	0	0	20	60	317	443	423	595	40,7%
Euler Hermes Rating GmbH	24	25	4	3	0	0	0	0	0	0	28	28	0,0%
European Rating Agency, a.s.	0	0	0	0	0	0	6	6	0	0	6	6	0,0%
Feri EuroRating Services AG	0	0	0	0	0	0	25	25	0	0	25	25	0,0%
GBB-Rating Gesellschaft für Bonitätsbeurteilung mbH	0	0	182	185	0	0	0	0	0	0	182	185	1,6%
ICAP Group SA	3190	1958	0	0	0	0	0	0	0	0	3190	1958	-38,6%

Credit Rating Agency	Corporate		Financials		Insurance		Sovereign and Public Finance		Structured Finance		Total		Variation 2012/2011
	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012	
Japan Credit Rating Agency Ltd	6	6	4	2	0	0	38	38	0	0	48	46	-4,2%
Scope Credit Rating GmbH	2	77	0	0	0	0	0	0	0	0	2	77	3750,0%
<i>Sub-total</i>	<i>61180</i>	<i>31331</i>	<i>346</i>	<i>350</i>	<i>205</i>	<i>197</i>	<i>121</i>	<i>140</i>	<i>317</i>	<i>443</i>	<i>62169</i>	<i>32461</i>	-47,8%
Fitch	613	628	604	560	57	55	351	355	5156	4861	6781	6459	-4,7%
Moody's	758	764	525	500	41	43	239	247	4910	4438	6473	5992	-7,4%
Standard & Poor's	914	953	685	703	361	358	217	215	5144	4705	7321	6934	-5,3%
<i>Sub-total</i>	<i>2285</i>	<i>2345</i>	<i>1814</i>	<i>1763</i>	<i>459</i>	<i>456</i>	<i>807</i>	<i>817</i>	<i>15210</i>	<i>14004</i>	<i>20575</i>	<i>19385</i>	-5,8%
<b>Grand Total</b>	<b>63465</b>	<b>33676</b>	<b>2160</b>	<b>2113</b>	<b>664</b>	<b>653</b>	<b>928</b>	<b>957</b>	<b>15527</b>	<b>14447</b>	<b>82744</b>	<b>51846</b>	-37,3%

Source: CEREP

NB. Table 4 provides an overview of outstanding ratings by rating class at the end of 2011 and 2012. For all rating classes other than structured finance, the data refers to rated entities. For structured finance ratings the numbers refer to total number of issuances.

**Table 5. Outstanding sovereign ratings issued in the EU by rating type (as of 31 December 2011 and 31 December 2012)**

Credit Rating Agency Name	Sovereigns		Sub-sovereigns / municipalities		Supranational organizations		Public entities		Total	
	2011	2012	2011	2012	2011	2012	2011	2012	2011	2012
BCRA-Credit Rating Agency AD	0	0	4	5	0	0	0	0	4	5
Capital Intelligence (Cyprus) Ltd	28	6	0	0	0	0	0	0	28	6
DBRS Ratings Limited	20	60	0	0	0	0	0	0	20	60
European Rating Agency, a.s.	0	0	6	6	0	0	0	0	6	6
Feri EuroRating Services AG	25	25	0	0	0	0	0	0	25	25
Japan Credit Rating Agency Ltd	34	34	4	4	0	0	0	0	38	38
<i>Sub-total</i>	<i>107</i>	<i>125</i>	<i>14</i>	<i>15</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>0</i>	<i>121</i>	<i>140</i>
Fitch	88	88	248	250	15	17	0	0	351	355
Moody's	74	77	88	75	0	1	77	94	239	247
Standard & Poor's	120	120	91	88	0	0	6	7	217	215
<i>Sub-total</i>	<i>282</i>	<i>285</i>	<i>427</i>	<i>413</i>	<i>15</i>	<i>18</i>	<i>83</i>	<i>101</i>	<i>807</i>	<i>817</i>
<b>Grand Total</b>	<b>389</b>	<b>410</b>	<b>441</b>	<b>428</b>	<b>15</b>	<b>18</b>	<b>83</b>	<b>101</b>	<b>928</b>	<b>957</b>

Source: CEREP - As CEREP collects both long term and short term ratings assigned to the same entity certain CRAs may have more than 27 ratings assigned across the 27 EU Member States. **Note:** With the exception of BCRA, all the remaining Credit Rating Agencies in this table provide ratings for more than one Member State.

**Table 6. Solicitation type by product (as of 31 December 2012)**

Credit Rating Agency	Corporate		Financials		Insurance		Sovereign and Public Finance		Structured Finance		Total EU outstanding ratings	
	Solicited	Unsolicited	Solicited	Unsolicited	Solicited	Unsolicited	Solicited	Unsolicited	Solicited	Unsolicited	Solicited	Unsolicited
AM Best Europe-Rating Services Ltd. (AMBERS)	13	0	0	0	149	0	0	0	0	0	162	0
ASSEKURATA Assekuranz Rating-Agentur GmbH	0	0	0	0	41	0	0	0	0	0	41	0
BCRA-Credit Rating Agency AD	0	0	16	0	7	0	5	0	0	0	28	0
Capital Intelligence (Cyprus) Ltd	0	0	0	64	0	0	0	6	0	0	0	70
CERVED Group S.p.A.	0	29078	0	0	0	0	0	0	0	0	0	29078
Companhia Portuguesa de Rating, S.A. (CPR)	6	0	1	0	0	0	0	0	0	0	7	0
Creditreform Rating AG	93	0	0	0	0	0	0	0	0	0	93	0
CRIF S.p.A.	0	62	0	0	0	0	0	0	0	0	0	62
DBRS Ratings Limited	12	1	77	2	0	0	42	18	443	0	574	21
Euler Hermes Rating GmbH	25	0	3	0	0	0	0	0	0	0	28	0
European Rating Agency, a.s.	0	0	0	0	0	0	6	0	0	0	6	0
Feri EuroRating Services AG	0	0	0	0	0	0	0	25	0	0	0	25
GBB-Rating Gesellschaft für Bonitätsbeurteilung mbH	0	0	185	0	0	0	0	0	0	0	185	0
ICAP Group SA	0	1958	0	0	0	0	0	0	0	0	0	1958
Japan Credit Rating Agency Ltd	6	0	1	1	0	0	38	0	0	0	45	1
Scope Credit Rating GmbH	36	41	0	0	0	0	0	0	0	0	36	41
<b>Sub-total</b>	<b>191</b>	<b>31140</b>	<b>283</b>	<b>67</b>	<b>197</b>	<b>0</b>	<b>91</b>	<b>49</b>	<b>443</b>	<b>0</b>	<b>1205</b>	<b>31256</b>
Fitch	518	110	550	10	47	8	296	59	4861	0	6272	187
Moody's	760	4	499	1	43	0	232	15	4438	0	5972	20

Credit Rating Agency	Corporate		Financials		Insurance		Sovereign and Public Finance		Structured Finance		Total EU outstanding ratings	
	Solicited	Unsolicited	Solicited	Unsolicited	Solicited	Unsolicited	Solicited	Unsolicited	Solicited	Unsolicited	Solicited	Unsolicited
Standard & Poor's	951	2	690	13	316	42	189	26	4705	0	6851	83
<i>Sub-total</i>	<i>2229</i>	<i>116</i>	<i>1739</i>	<i>24</i>	<i>406</i>	<i>50</i>	<i>717</i>	<i>100</i>	<i>14004</i>	<i>0</i>	<i>19095</i>	<i>290</i>
<b>Grand Total</b>	<b>2420</b>	<b>31256</b>	<b>2022</b>	<b>91</b>	<b>603</b>	<b>50</b>	<b>808</b>	<b>149</b>	<b>14447</b>	<b>0</b>	<b>20300</b>	<b>31546</b>

**Table 7 - Development of employment by CRAs USA**

2012 Summary report of the Securities and Exchange Commission staff's Examinations of each nationally recognized statistical rating agency

NRSRO	Credit Analysts			Credit Analyst Supervisors*			Total		
	2010	2011	Variation 2011/2010	2010	2011	Variation 2011/2010	2010	2011	Variation 2011/2010
A.M. Best	77	82	6.49%	43	41	-4.65%	120	123	2.50%
DBRS	75	84	12.00%	20	34	70.00%	95	118	24.21%
EJR	2	2	0.00%	3	3	0.00%	5	5	0.00%
JCR	27	24	-11.11%	30	33	10.00%	57	57	0.00%
KBRA	9	22	144.44%	4	6	50.00%	13	28	115.38%
Morningstar	17	26	52.94%	7	10	42.86%	24	36	50.00%
R&I	74			4			78		
<b>sub-total</b>	281	240	-14.59%	111	127	14.41%	392	367	-6.38%
Fitch	712	758	6.46%	337	338	0.30%	1049	1096	4.48%
Moody's	1088	1124	3.31%	116	128	10.34%	1204	1252	3.99%
S&P	1109	1172	5.68%	236	244	3.39%	1345	1416	5.28%
<b>Total</b>	3190	3294	3.26%	800	837	4.62%	3990	4131	3.53%

\*Some credit analyst supervisors may also have analytical responsibilities.

**Table 8 US rating market of smaller CRAs**

Number of Credit Ratings Outstanding by Category of Credit Rating

Source: NRSRO Annual Certifications for the

Year Ended December 31, 2010 and December 31,

2011

NRSRO	Financials			Insurance			Corporate			Asset-Backed Sec	
	Year	2010	2011	Variation 2011/2010*****	2010	2011	Variation 2011/2010	2010	2011	Variation 2011/2010	2010
A.M. Best	N/R**	N/R	N/R	5062	4826	-4.66%	2043	1910	-6.51%	54	56
				93.90%	94.50%	0.60%	18.38%	22.77%	4.39%	0.29%	0.21%
DBRS	14941	21695	45.20%	156	151	-3.21%	3863	4037	4.50%	10091	9889
	46.39%	56.96%	10.57%	2.89%	2.96%	0.06%	34.75%	48.13%	13.38%	54.60%	37.94%
EJR	89	101	13.48%	47	51	8.51%	877	962	9.69%	13	13
	0.28%	0.27%	-0.01%	0.87%	1.00%	0.13%	7.89%	11.47%	3.58%	0.07%	0.05%
JCR	159	163	2.52%	30	27	-10.00%	495	478	-3.43%	N/R	N/R
	0.49%	0.43%	-0.07%	0.56%	0.53%	-0.03%	4.45%	5.70%	1.25%		
KBRA	16515	16127	-2.35%	48	52	8.33%	1002	1001	-0.10%	0***	40
	51.28%	42.34%	-8.93%	0.89%	1.02%	0.13%	9.01%	11.93%	2.92%		0.15%
Morningstar	N/R	N/R	N/R	N/R	N/R	N/R	N/R	N/R	N/R	8322	16070
										45.03%	61.65%
R&I****	503	N/R	N/R	48	N/R	N/R	2836	N/R	N/R	N/A	N/R
	1.56%			0.89%			25.51%				
<b>Sub-Total</b>	<b>32207</b>	<b>38086</b>	<b>18.25%</b>	<b>5391</b>	<b>5107</b>	<b>-5.27%</b>	<b>11116</b>	<b>8388</b>	<b>-24.54%</b>	<b>18480</b>	<b>26068</b>
<b>% for Smaller CRAs</b>	<b>15.39%</b>	<b>18.15%</b>	<b>2.76%</b>	<b>27.24%</b>	<b>24.47%</b>	<b>-2.77%</b>	<b>11.20%</b>	<b>8.50%</b>	<b>-2.69%</b>	<b>6.11%</b>	<b>9.09%</b>
Fitch	61550	54586	-11.31%	1657	4010	142.00%	13385	14427	7.78%	64535	58315
Moody's	61581	56486	-8.27%	4540	3953	-12.93%	30285	30439	0.51%	101546	93913
S&P	54000	60700	12.41%	8200	7800	-4.88%	44500	45400	2.02%	117900	108400
<b>Total</b>	<b>209338</b>	<b>209858</b>	<b>0.25%</b>	<b>19788</b>	<b>20870</b>	<b>5.47%</b>	<b>99286</b>	<b>98654</b>	<b>-0.64%</b>	<b>302461</b>	<b>286696</b>

\* HR Ratings de México, S.A. de C.V entered the market in 2012,

no data is available at this point

\*\*N/R indicates the CRA is not registered for that category of securities.

\*\*\* KBRA is registered in the asset-backed securities category, although it reported no outstanding ratings in this category as of December 31, 2010.

**Table 9**

Name	Group structure	Type of ancillary Services
<b>Euler Hermes Rating GmbH</b> <a href="http://www.ehrg.de/en/">http://www.ehrg.de/en/</a>	Independent daughter company of Euler Hermes and Allianz	Rating Advisor (advises the issuer as to what CRA to report) (Beste Bonität), Economic Research
<b>Japan Credit Rating Agency, Ltd.</b> <a href="http://www.jcr.co.jp/english/">http://www.jcr.co.jp/english/</a>	Single legal entity	Customer Credit Assessment Service, JCR SME Rating, Strength of the Financial Institutions for the Local Government, Quantitative Model for SME Credit Risk Evaluation, Priority Assessment, Credit Assessment Based on Assumption, S Provision of General Information and Knowledge about Rating Information and Other Information to Subscribers
<b>Feri EuroRating Services AG</b> <a href="http://frr.feri.de/en/">http://frr.feri.de/en/</a>	Single legal entity	Research services (Economic Forecasts, Databases, S Consulting services (Evaluation, Valuation and Susta assistance in the selection of investment funds, as investment certificates)
<b>BCRA-Credit Rating Agency AD</b> <a href="http://www.bcra-bg.com/about_us.php?lang=en">http://www.bcra-bg.com/about_us.php?lang=en</a>	Single legal entity	Credit Report (information and opinion on the creditworthiness Limit (equivalent to the allowable increase of short-term non-financial enterprise Firm can regularly serve). Also SMEs and physical persons, risk assessment and analysis
<b>Creditreform Rating AG</b> <a href="http://www.creditreform.de/Deutsch/Rating/1_Wir_ueber_uns/Wir_ueber_uns_eng.jsp">http://www.creditreform.de/Deutsch/Rating/1_Wir_ueber_uns/Wir_ueber_uns_eng.jsp</a>	Part of the Creditreform Group: <i>Microm</i> - Consumer Marketing; <i>Boniversium</i> - Consumer Information; <i>Creditreform</i> - Portfolio Management; <i>Creditreform</i> - Compliance Services and <i>Immo Check</i> - Real Estate Valuation.	Start-Up-Ratings, Pre-Ratings (first assessment without <i>Bonitätssiegel</i> (different type of display of ratings for segment), Financial Statement Ratings, technical support the analysis of financial statements, score cards of b analysis of different regions in Germany and score cards Creditreform-Group
<b>Scope Ratings GmbH</b> <a href="http://www.scoperatings.com/index?lang=en">http://www.scoperatings.com/index?lang=en</a>	Part of the Scope Group which also consists of <i>Scope Analysis</i> (Investment and management analysis) and <i>Scope Capital Services</i>	

	(intra-group services).	
<b>ICAP Group SA</b> <a href="http://www.icap.gr/Default.aspx?id=0&amp;nt=0&amp;lang=2">http://www.icap.gr/Default.aspx?id=0&amp;nt=0&amp;lang=2</a>	Single legal entity	Besides the Credit Risk Services (Rating, Scores, Business Information Exchange network) ICAP offers Marketing Management Consulting (Financial Studies), Human resources and Receivables Management (done by <i>Cycle Credit</i> 100% su
<b>GBB-Rating Gesellschaft für Bonitätsbeurteilung mbH</b> <a href="http://www.gbb-rating.de/">http://www.gbb-rating.de/</a>	Single legal entity	
<b>ASSEKURATA Assekuranz Rating-Agentur GmbH</b> <a href="http://www.assekurata.de/">http://www.assekurata.de/</a>	part of ASSEKURATA Solutions GmbH which offers Management Consulting and Market Research	
<b>ARC Ratings, S.A.</b> (previously Companhia Portuguesa de Rating, S.A.) <a href="http://www.cprating.pt/">http://www.cprating.pt/</a>	Single legal entity	
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	the EU. <a href="http://www.ambest.com/">http://www.ambest.com/</a>	
<b>DBRS Ratings Limited</b> <a href="http://www.dbrs.com/">http://www.dbrs.com/</a>	Single legal entity	Besides rating DBRS provides company reports, industry assessments and data-feed services. Same services in Europe,
<b>CRIF S.p.A.</b> <a href="http://www.criflendingsolutions.com/Pages/default.aspx">http://www.criflendingsolutions.com/Pages/default.aspx</a>	CRIF Lending Solutions is a group organized in four divisions: <i>CRIF ACTION</i> (Consumer Lending, Business Lending, Merchant Lending, Online Lending, Account Lending), <i>CRIF Achieve</i> (Data Management, Performance Analytics, Decision Optimization, Change Management), <i>CRIF Synergy</i> (Business Process Management, Business Rules Management, Data Access, Characteristic Development, Scoring Development, Configurable Loan Origination System) and <i>CRIF Select</i> (Direct Lending, Indirect Lending, Indirect Leasing, Merchant Lending, Auto Dealer Services).	
<b>Capital Intelligence (Cyprus) Ltd</b> <a href="http://www.ciratings.com/">http://www.ciratings.com/</a>	Single legal entity	in-depth business reports
<b>European Rating Agency, a.s.:</b> <a href="http://www.euroratings.co.uk/">http://www.euroratings.co.uk/</a>	Single legal entity	
<b>Axesor SA</b> <a href="http://idiomas.axesor.es/">http://idiomas.axesor.es/</a>	Single legal entity	Database on companies, Company Reports and Reports on Companies
<b>CERVED Group S.p.A.</b> <a href="http://www.cerved.com/xportal/web/eng/home-">http://www.cerved.com/xportal/web/eng/home-</a>	The Cerved Group SpA was created by a consortium of the private	Competitors Analysis

<a href="#">eng.jsp</a>	equity funds Bain Capital and Clessidra. It comprises <i>Cerved BI, Lince, Centrale dei Bilanci, Databank</i> (Marketing Solutions), <i>Finservice, Jupiter</i> (Credit Valuation, Credit Management, Asset Management) and <i>Consit</i>	
<b>Kroll Bond Rating Agency</b> <a href="https://www.krollbondratings.com/index.php">https://www.krollbondratings.com/index.php</a>	Single legal entity	
<b>The Economist Intelligence Unit Ltd</b> <a href="http://www.eiu.com/">http://www.eiu.com/</a>	EIU is part of the Economist Group	Country Analysis, Country Risk Service, Industry Analysis research consultancy is offered by the subsidiaries <i>Bazian</i> and
<b>Dagong Europe Credit Rating Srl (Dagong Europe)</b> <a href="http://www.dagongeuropa.com/">http://www.dagongeuropa.com/</a>	It is part of Dagong Global Credit Rating Co., Ltd.	Besides Ratings they offer Credit Risk Research and Credit In
<b>Spread Research</b> <a href="http://www.spreadresearch.com/">http://www.spreadresearch.com/</a>	Single legal entity	Spread Research offers Credit News flow and Investment Rec
<b>Egan-Jones Ratings Company</b> <a href="http://www.egan-jones.com/">http://www.egan-jones.com/</a>	Single legal entity	<i>Egan-Jones Proxy Services</i> (subsidiary) provides research, services
<b>Morningstar</b> <a href="http://corporate.morningstar.com/US/asp/home2.aspx?xmlfile=7083.xml">http://corporate.morningstar.com/US/asp/home2.aspx?xmlfile=7083.xml</a>	Single legal entity	Access to Databases and Indexes. Investment management. In

<b>HR Ratings de México, S.A. de C.V</b> <a href="http://www.hrratings.com/en/index">http://www.hrratings.com/en/index</a>	Single legal entity with branches in the US and Mexico	
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Source: based on the information contained on the websites of the respective credit rating agencies

## **Section 2 Situation of the smaller CRAs on the global rating market**

This section presents an overview of the credit market in the EU and the US, focusing on the competitive position of the 19 smaller registered and 2 certified CRAs compared to the larger CRAs. It also provides data on the evolutions of the business model of smaller CRAs in the EU and the US in terms of geographical coverage and product portfolios.

### **2.1. Situation of the smaller CRAs in the EU<sup>1</sup>**

#### **2.1.1. Classes of ratings issued**

None of the smaller CRAs is active in all of the 5 classes of ratings (corporates, financial institutions, insurance companies, sovereigns, and structured finance products). The majority of the smaller CRAs cover only one or two of these classes of ratings (see Table 3 in Annex). Only 2 of the smaller CRAs cover more than 2 rating classes, namely DBRS, which is active in four out of five rating classes, and BCRA, which covers three rating classes. The prevalent rating type among the smaller CRAs is corporate ratings (issued by all such CRAs except six), while their scope of operations is limited as regards financial ratings (7), insurance ratings (3), sovereign ratings (6), and structured finance ratings (1).

#### **2.1.2. Geographical scope of activity**

In terms of geographical coverage, only 6 out of 19 smaller CRAs (AM Best, Capital Intelligence, Creditreform, DBRS, JCR and Scope) have coverage that goes beyond one Member State when referring to corporate ratings (see Table 2 in Section 1). For the sovereign ratings type, three of the smaller CRAs cover more than one Member State (Capital Intelligence, Feri and JCRA) (see Table 5 in Section 1). Conversely, the larger CRAs cover geographically all EU Member States in both rating types.

The CRA Regulation allows registered CRAs to endorse credit ratings issued in non-EU countries. The Regulation requires ESMA to verify that the requirements of third-country CRA regimes are “as stringent as” the European regulatory framework. Currently, CRAs can endorse ratings issued in the US, Canada, Mexico, Argentina, Brazil, Australia, Singapore, Hong Kong, and Japan.

As of end 2012, of the smaller CRAs, only DBRS endorses ratings from third countries, which constitute the majority of its ratings. This is due to that fact that the main analytical resources of this CRA being located in Canada.

#### **2.1.3. Number of outstanding credit ratings**

The data on credit ratings outstanding at the end of 2012 (see Table 4 in Section 1), shows that seven smaller CRAs issue mainly corporate ratings, while in 3 other cases smaller CRAs issue mainly financial ratings. Two other smaller CRAs issue mainly insurance and sovereign ratings,

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<sup>1</sup> This section of the report is based on the data provided by ESMA in its Technical Advice on the feasibility of a network of smaller CRAs.

while in the case of one smaller CRA structured finance ratings represent the major area of operation.

With reference to corporate ratings, CERVED is by far the largest issuer of ratings in number of ratings outstanding (93% of total ratings assigned by smaller CRAs to corporate issuers), followed at a distance by ICAP (6,2%), while the eight other CRAs together assign, in total, less than 1% of the number of this type of ratings. The number of credit ratings assigned to corporate issuers by CERVED and ICAP is also higher than the number of such ratings assigned by larger CRAs.

CERVED's and ICAP's high number of total outstanding corporate ratings can be explained by the particularities in the reporting standards to CEREP<sup>2</sup> and that these two CRAs are mainly active in the segment of rating smaller corporates compared to the bigger CRAs. The CEREP database solely refers to the number of rated entities, not the actual number of financial debt contracts rated. Given that small companies have less numerous debt issuances that are rated than large companies, and that the effect of multiple rated debt issuances by large corporations is not fully reflected in the database, the proportion of outstanding ratings appears much higher for CRAs which have as their customer base mainly smaller corporations.

As regards the smaller CRAs that are focused on financial, insurance and sovereign ratings, these account for approximately 17%, 30% and 15%, respectively in the total number of rated issuers. GBB and AM Best focus nearly exclusively on financial and insurance ratings, respectively. For financial ratings, as of end 2012 GBB issued 53% of the ratings assigned to financial issuers for smaller CRAs and at the same time only 37% of the ratings of the same type issued by Moody's (the smallest of the larger CRAs in this segment). As regards ratings to corporate insurance issuers, AM Best assigned 76% of all ratings issued by smaller CRA's and a higher number than Fitch and Moody's, representing overall 23% of the total number of issuers in this segment. The same observations can be made regarding this data as in the paragraph above, as the CEREP dataset refers to the number of rated entities and not the total number of issuances.

Finally, of the smaller CRAs, only DBRS was active in the structured finance market as of end 2012. The number of structured finance ratings of DBRS constituted 3% of the total number of structured finance ratings, representing 10% of the total number of issuances rated by larger credit rating agencies. From 2011 to 2012, DBRS's structured finance ratings issuances increased significantly.

From the change in the number of outstanding credit ratings from 2011 to 2012, that following can be observed: a decline in corporate and structured finance ratings; a modest increase in sovereign ratings; and relative stable numbers in financials and insurances rating classes. The decline in corporate ratings was exclusively driven by the strong decrease in outstanding ratings of CERVED and ICAP. The vast majority of the other smaller CRAs, as well as the larger ones increased their total number of outstanding corporate ratings. As regards structured finance

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<sup>2</sup> Central Repository of rating data reported by CRAs to ESMA according to Commission Delegated Regulation (EU) No 448/2012 of 21 March 2012 supplementing Regulation (EC) No 1060/2009 of the European Parliament and of the Council with regard to regulatory technical standards for the presentation of the information that credit rating agencies shall make available in a central repository established by the European Securities and Markets Authority

ratings whilst the larger CRAs decreased their numbers, the only smaller CRA active in this segment, DBRS, increased its number of outstanding ratings. The increase in sovereign ratings was driven by the smaller CRAs, particularly by DBRS.

#### 2.1.4. Number of outstanding sovereign ratings

Out of the six smaller CRAs active in this area (see data in Table 5 in Section 1 on subclasses of sovereign rated issuers in 2011 and 2012), four were active in the provision of sovereign ratings<sup>3</sup> and three provided sub-sovereign ratings<sup>4</sup>. Only one smaller CRA issued ratings in both these classes. As regards both sovereign ratings and sub-sovereign ratings, the proportion of ratings provided by smaller CRAs increased between 2011 and 2012. This is mainly explained by the significant increase in the number of sovereign ratings issued by DBRS in this period. None of the smaller CRAs rated supra-national organisations<sup>5</sup> or public entities.

#### 2.1.5. Solicited and unsolicited ratings

The CRA Regulation allows credit rating agencies to distribute solicited and/or unsolicited ratings. Generally, unsolicited ratings are provided by CRAs that operate on the basis of an "investor-pays" model. By the end of 2012, five smaller CRAs (Capital Intelligence, CERVED, CRIF, Feri, and ICAP) distributed only unsolicited ratings through their "investor-pays" model (see Table 6 in Section 1). On the other hand, eight CRAs (AM Best, Assekurata, BCRA, CPR, Creditreform, Euler Hermes, ERA, and GBB) issue only solicited ratings. Like the larger CRAs, DBRS and Scope had both solicited and unsolicited ratings outstanding.

#### 2.1.6. Provision of ancillary services by smaller CRAs

An analysis of information published on the websites of the smaller CRAs about the types of services they provide to the market, shows that the majority of smaller CRAs offer a large number of ancillary services (i.e. scoring and other consulting services) in parallel to rating services. The survey presented in Section 1 (Table 9) shows that those CRAs providing only rating services are normally part of a group, while ancillary services are often provided by other entities of the same group.

## **2.2. Situation of the smaller CRAs in the US rating market**

### 2.2.1. Number of registered CRAs and scope of their activities

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<sup>3</sup> These are local or foreign currency credit ratings where the entity rated is a State.

<sup>4</sup> These are credit ratings where the issuer of the debt or financial obligation, debt security or other financial instrument is a regional or local authority of a State.

<sup>5</sup> Rated entity is the issuer is an international financial institution established by two or more States which has the purpose of mobilising funding and providing financial assistance for the benefit of the members of that international financial institution which are experiencing or threatened by severe financing problems

There are currently seven smaller CRAs active in the United States market that have successfully registered with the Securities and Exchange Commission (SEC) as a nationally recognized statistical rating organization (NRSRO)<sup>6</sup>.

**NRSRO Date of Registration**

A.M. Best Company, Inc. (A.M. Best)	September 24, 2007
DBRS, Inc. (DBRS)	September 24, 2007
Egan-Jones Ratings Company (EJR)	December 21, 2007
Japan Credit Rating Agency, Ltd. (JCR)	September 24, 2007
Kroll Bond Rating Agency, Inc. (KBRA)	February 11, 2008
Morningstar Credit Ratings, LLC (Morningstar)	June 23, 2008
HR Ratings de México, S.A. de C.V	November 5, 2012

Source: SEC<sup>7</sup>

This is considerably less than in the EU (where there are 21 registered or certified smaller CRAs). However, while there are less smaller CRAs active in the US market, those CRAs tend to have a broader scope of operation in terms of classes of ratings. In the EU, out of the 16 active CRAs only one (DBRS) is active in four of the five classes<sup>8</sup> and only two (BCRA and Japan Credit Rating Agency) are active in three classes, while four are active in two rating classes and nine are active in only one rating class. In the US the picture is different as for the six CRAs for which data was available, three are active in all rating classes (DBRS, EJR, KBRA), one was active in four classes, another one in three and only one was only active in one class. This could imply that while there are less smaller CRAs in the US, these cover a larger part of the rating market.

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<sup>6</sup> HR Ratings de México, S.A. de C.V was only registered on 5 November 2012. There was no data available on the activity of this CRA at the time of writing of this report.

<sup>7</sup> Source: <http://www.sec.gov/news/studies/2012/nrsro-summary-report-2012.pdf>, p.4

<sup>8</sup> Those are: Corporate, Financials, Insurance, Sovereign and Public Finance, Structured Finance (EU)/Asset backed Securities (US)

Number of Outstanding Credit Ratings by Category of Credit Rating Source: NRSRO Annual Certifications for the Year Ended December 31, 2011						
NRSRO	Financial Institutions	Insurance Companies	Corporate Issuers	Asset-Backed Securities	Government Securities	Total Ratings
A.M. Best	N/R	4,826	1,910	56	N/R	6,792
DBRS	21,695	151	4,037	9,889	15,798	51,570
EJR	101	51	962	13	9	1,136
Fitch	54,586	4,010	14,427	58,315	217,198	348,536
JCR	163	27	478	N/R	54	722
KBRA	16,127	52	1,001	40	58	17,278
Moody's	56,486	3,953	30,439	93,913	814,087	998,878
Morningstar	N/R	N/R	N/R	16,070	N/R	16,070
S&P	60,700	7,800	45,400	108,400	948,300	1,170,600
<b>Total</b>	<b>209,858</b>	<b>20,870</b>	<b>98,654</b>	<b>286,696</b>	<b>1,995,504</b>	<b>2,611,582</b>

\*N/R indicates the NRSRO is not registered for that category of securities.

Source: SEC<sup>9</sup>

### 2.2.2. Number of outstanding ratings of smaller CRAs<sup>10</sup>

The number of total outstanding ratings issued by smaller CRAs in the US market is 3.6% with a slight increase between 2010 and 2011. The relative increase is the result of an absolute increase in ratings as well as a decrease in ratings of the bigger CRAs over this period.

In the rating class of financial institutions, smaller CRAs account for approximately 18% of the total number of ratings. Four smaller CRAs are active in this rating class but the market is effectively split in two with DBRS accounting for 57% and KBRA accounting for 42% of the ratings issued by smaller CRAs.

The total number of outstanding ratings from smaller CRAs in the *insurance* rating class is the highest among all five classes (25%). The concentration in this segment is also the highest with A.M. Best accounting for almost 95% of the ratings even though five smaller CRAs are active here.

The corporate sector is more balanced with five active smaller CRAs and only one of those has less than 5% of the outstanding ratings. Overall, the smaller CRAs account for approximately 8,5% of all outstanding ratings in this rating class, with DBRS accounting for 48% of those ratings.

The rating class of asset-backed securities is characterised by a duopoly structure with Morningstar accounting for 61,65% of all smaller CRAs' ratings and DBRS accounting for 38%. Smaller CRAs issue 9% of all ratings in this category, while in total 5 smaller CRAs are active in this segment.

<sup>9</sup> Source: <http://www.sec.gov/news/studies/2012/nrsro-summary-report-2012.pdf>, p.5

<sup>10</sup> The following part is based on Table 8 in the Annex

The sector of government securities is the sector where smaller CRAs have the lowest number of outstanding ratings (0,8%). Four smaller CRAs are active in this segment but DBRS accounts for 99% of all ratings.

While most of the smaller CRAs are active in multiple market segments, they specialise in one. KBRA is very dominant in the rating of financial institution issuers but plays a minor role in the four other market segments. A.M. Best focuses on the insurance segment. Meanwhile, Morningstar only issues ratings with regard to asset-backed securities, accounting for 61,65% of all ratings from smaller CRAs in that category. DBRS dominates the sector of government securities. DBRS is the only CRA that is also very strong if not dominant in other classes (financial institutions, corporate issuers, asset-backed securities). In this sense, it has a business model which is a lot closer to the business structure of the larger CRAs than the other smaller CRAs. In the corporate sector there is no clear dominance of one or fewer smaller CRAs since all of them have a certain share of this market segment.

As mentioned earlier, the market share of smaller CRAs in the US has increased from 2010 to 2011 by 0,68% to 3,58%. Considering each segment individually, the respective shares of the financial institutions, asset-backed securities, and government securities have increased, while the insurance and the corporate segments registered a slight decrease.

### 2.2.3. Smaller CRAs active in both EU and US markets

There are four smaller CRAs which are registered in the US as well as the EU market. All of them are active in more rating classes in the US market than in the EU. Japan Credit Rating is active in all classes in the US except for asset-backed securities. In the EU it is not active in structured finance and insurance.

A.M. Best is active in insurance, corporate and asset-backed securities in the US but only in insurance and corporate in the EU. DBRS is active in all classes in the US but not in insurance on the EU market. KBRA is certified by ESMA and hence active in both markets. It was only certified in the March 2013 so there is no data available at the time of writing.

### 2.2.4. Evolution of staff levels in smaller CRAs

Table 7 in Section 1 indicates a slight increase in the market share is mirrored by an increase in the number of employees of smaller CRAs. Yet the overall number of analysts employed by smaller CRAs declined due to one agency leaving the market (R&I). Despite the drop in the total number of ratings issued between 2010 and 2011 in the US, it is noteworthy that all agencies, smaller and larger increased the number of employed analysts.

### 2.2.5. Smaller CRAs which have recently entered or left the US market<sup>11</sup>

In 2012, HR Ratings de México, S.A. de C.V. entered the US market. It is only registered for government securities.

In May 2010 Realpoint LLC registered for the rating of asset-backed securities was acquired by Morningstar and in August 2010, LACE Financial Corp. was acquired by Kroll Bond Rating (KBRA). LACE was active in all rating classes.

Also in May 2010, Rating and Investment Information, Inc. (R&I) left the market. It was active in all rating classes.

### 2.2.6. Regulatory exceptions currently granted to smaller CRAs<sup>12</sup>

Currently, there is only one exemption granted to smaller CRAs, namely the temporary and conditional exemption from the Conflict of Interest Prohibition in Rule 17g-5(c)(1) of the Securities and Exchange Act of 1934.

This rule prohibits a NRSRO from issuing or maintaining a credit rating solicited by a person who, in the most recently ended fiscal year, provided the NRSRO with net revenue equalling or exceeding 10% of the total net revenue of the NRSRO for the fiscal year.

The possible exemption of this rule is not per se aimed only at smaller CRAs, although, it has so far only been applied to smaller CRAs. The SEC has in the past granted three temporary exemptions from Rule 17g-5(c)(1), all of which to smaller CRAs (Realpoint LLC, KBRA and LACE). Currently, this exemption applies to Morningstar Credit Ratings, LLC (“Morningstar”).

Morningstar traditionally operated mainly under the “subscriber-pays” business model, where individual fees are traditionally lower compared to “issuer-pays” business model. After Morningstar acquired Realpoint, it expanded the scope of its activities, initiating an issuer-pays ratings service for initial ratings on commercial mortgage-backed securities. In the early stages of its expansion, the fees associated with a single issuer-paid engagement have exceeded 10% of its total net revenue for the fiscal year. The SEC granted the exemption from this restriction considering that it would pose a substantial constraint on the firm’s ability to compete effectively with large rating agencies.

Such restriction rule does not exist in the EU, where only disclosure of individual fees per client is required together with a list of major clients with 1,5 times higher growth rate of individual fees than the overall growth rate of total fees of the CRA (but only if for the same financial year the client accounts for more than 0,25% of the worldwide total revenues of the CRA at global level)<sup>13</sup>. The disclosure of this information gives the opportunity to the supervisor (ESMA) to further monitor on an individual basis if certain levels of individual fees could be a potential

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<sup>11</sup> Source: <http://www.sec.gov/divisions/marketreg/ratingagency.htm>

<sup>12</sup> Source: <http://www.sec.gov/rules/other/2012/34-66514.pdf>

<sup>13</sup> CRA Regulation, Annex I, Section E, point 2.a and 2.b.

threat to independence. Taking the above into account, similar objectives exist in the US and the EU, aiming at enhancing competition and ensuring the respect of independence rules, though achieved through different means.

### **Section 3 Potential barriers of entry and growth for smaller CRAs in the EU and legislative measures under the CRA III Regulation to tackle these barriers**

The Impact Assessment, accompanying the CRA III legislative proposal<sup>14</sup>, identified a number of market entry barriers and barriers to growth having an overall negative impact on the growth potential of smaller CRAs. The stakeholder consultation and fact-finding carried out confirmed the existence of these barriers, while potential additional issues were raised.

The CRA III Regulation, which entered into force on 20 June 2013, enhanced considerably the way credit rating agencies are governed within the EU. Although the whole CRA III Regulation applies to all CRAs alike, there are some measures on strengthening competition in the rating industry, which are particularly important for smaller CRAs. The majority of those measures also aim to tackle the identified barriers of entry and growth.

However, in some cases this report could not fully assess the impact of those measures, taking into account the short time period since the entry into force of CRA III Regulation as well as the fact that some of them are still not effectively applied since their implementation envisages implementing and delegated acts<sup>15</sup>.

#### **3.1. Reputation and insufficient visibility of smaller CRAs**

Smaller CRAs identified reputation and insufficient visibility towards the investors' and issuers' community as the most important market barriers. Subsequently, the CRA III package included a number of measures aimed at tackling these barriers and helping smaller CRAs to build up their reputation and be more visible on the market.

##### **3.1.1. Registration and supervision of CRAs by ESMA**

The carrying out of any credit rating activities in the EU is only possible upon registration with ESMA<sup>16</sup>, being subject to on-going supervision. The successful registration of a CRA with ESMA is a guarantee for the market that the respective CRA complies with all the requirements of the CRA Regulation at the moment of registration. Furthermore, the subsequent on-going supervision ensures that CRAs also comply with the legislative framework over time. Although

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<sup>14</sup> Impact Assessment SEC(2011) 1354, accompanying the Proposal for a Regulation amending Regulation (EC) No 1060/2009 on credit rating agencies and a Proposal for a Directive amending Directive 2009/65/EC on coordination on laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) and Directive 2011/61/EU on Alternative Investment Fund Managers, Page 17, 4.3. Limited choice of rating agencies and ratings for issuers and investors, available at: [http://ec.europa.eu/internal\\_market/securities/docs/agencies/SEC\\_2011\\_1354\\_en.pdf](http://ec.europa.eu/internal_market/securities/docs/agencies/SEC_2011_1354_en.pdf)

<sup>15</sup> Some of the measures require the development and adoption of Implementing and Regulatory Technical Standards (i.e. the European Rating Platform, disclosure requirements for issuers of structured finance instruments, mapping of credit rating scales by EBA/ EIOPA) or the preparation of reports to assess their feasibility (Report on the feasibility of mapping of ratings to be prepared by ESMA by 21 June 2015).

<sup>16</sup> This requirement was introduced in the CRA Regulation in 2011 (article 14 Requirement for registration)

ESMA cannot interfere with the content of the CRAs' methodologies, it shall guarantee that CRAs consistently apply their methodologies, including verifying the execution of back-testing and analysing its results<sup>17</sup>.

Therefore, especially for new entrants on the CRA market, being registered with ESMA as a precondition for performing credit rating activities plays the role of a quality label, ensuring that minimum quality standards are met by the registered CRA. Registration with ESMA indirectly facilitates building up reputation on the market.

### 3.1.2. Establishment of the European Rating Platform by ESMA<sup>18</sup>

As from 21 June 2015, data from registered and certified CRAs on all available ratings or rating outlooks and preliminary ratings will be published, on a centralised website of the European Rating Platform (ERP), operated by the European Securities and Markets Authority (ESMA).

The ERP should allow investors, issuers and other interested parties to have access to up-to-date rating information and to easily compare all solicited and non-solicited credit ratings that exist (from smaller and larger CRAs) with regard to a specific rated entity. The ERP should also incorporate ESMA's central repository with a view to create a single platform for all available solicited and non-solicited credit ratings per instrument and for information on historical performance data, currently published on the central repository.

The content and presentation of the information to be reported, including structure, format, method and timing of reporting, will be defined in a regulatory technical standard to be prepared by ESMA and adopted by the European Commission.

This measure, once fully implemented, will give smaller CRAs increased visibility to the market, and facilitate gaining reputation. This should also help investors to consult ratings of smaller CRAs and consider all ratings to make their own credit risk assessment and before taking their own investment decision.

However, in order not to undermine the ability of credit rating agencies to operate under the investor-pays model, credit ratings paid by the investor should not be included in the European rating platform.

### 3.1.3. Mappings of rating scales by ESMA

ESMA is required by the CRA Regulation to report by 21 June 2015 on the possibility to establish one or more mappings of credit ratings,<sup>19</sup> after consulting the European Banking Authority (EBA) and the European Insurance and Occupational Pensions Authority (EIOPA).

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<sup>17</sup> Article 22a CRA Regulation.

<sup>18</sup> Article 11a CRA Regulation.

<sup>19</sup> Article 21(4b) CRA Regulation.

This should ensure better comparability of credit ratings, taking into account differences in methodologies. Eventually, credit ratings from smaller CRAs would acquire visibility and comparability with credit ratings from larger CRAs.

In addition, the exercises of the mapping of rating scales by EBA and EIOPA will have a positive impact on the visibility of smaller CRAs (see also section on mapping of credit rating scales by EBA and EIOPA).

#### 3.1.4. Mandatory use of smaller CRAs in case of double ratings

It has been the practice in recent times for issuers or related third parties to seek credit ratings from two or more credit rating agencies. Therefore, with the aim to encourage the use of smaller CRAs, the CRA III Regulation requires issuers, when appointing at least two CRAs for rating the same instrument, to consider appointing one smaller CRA with less than 10% of the total market share and which could be evaluated by the issuer or a related third party as capable of rating the relevant issuance or entity. The issuer is also obliged to document the non-appointment of such a CRA rule on a comply-or-explain<sup>20</sup> basis.

This measure aims at providing new opportunities for market entrants and smaller CRAs which have the technical capacity to provide these rating services but lack the reputation or enough visibility in order to have access to new market segments. They are thereby given an opportunity to potentially expand their business and build up their reputation. The informed choice of issuers regarding the appointment of a second smaller CRAs is to be facilitated by the publication of a list of CRAs with less than 10% of the total market share by ESMA.

#### 3.1.5. Double ratings for structured finance instruments (SFIs)<sup>21</sup>

Due to the complexity of structured finance instruments, credit rating agencies have not always succeeded in ensuring a sufficiently high quality of credit ratings issued on such instruments. This has led to a loss of market confidence in this type of credit ratings. In order to regain confidence, the CRA III Regulation requires issuers or related third parties to engage at least two different credit rating agencies for the provision of credit ratings on structured finance instruments, which could lead to different and competing assessments.<sup>22</sup> This will contribute to reduce the over-reliance on a single credit rating.

Combined with the requirement to appoint one smaller CRAs in case of double ratings (see point above), this offers smaller CRAs the possibility to gain market access in the SFIs segment. Also taking into account that only one of the smaller CRAs, registered or certified in the EU, is active in this segment of the market today, this measure creates an opportunity for smaller CRAs to expand and build up a reputation in a new product segment of the rating market.

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<sup>20</sup> Articles 8d CRA Regulation

<sup>21</sup> Article 8c CRA Regulation

<sup>22</sup> Recital 28 CRA III Regulation

Pursuant to Article 39(4) CRA Regulation, 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 and by 1 July 2016 submit a report to the European Parliament and to the Council.

### 3.1.6. Rotation of CRAs in the area of re-securitisation<sup>23</sup>

The CRA III Regulation requires issuers of structured finance products with underlying re-securitised assets, in the "issuer-pays" model, to switch to a different agency every four years. Although there is currently only a limited number of credit rating agencies active in the credit rating market for re-securitisations, the rotation mechanism is expected to open the market to competition and be a driver for creating more dynamics in that market. The credit rating market for re-securitisations is dominated by a few large credit rating agencies but there are also other smaller credit rating agencies who have been building up expertise in this area

Taking into account that CRAs with less than 50 employees are exempted from the obligation to rotate, this measure creates business opportunities for them, since they could potentially attract new business from bigger CRAs which are subject to rotation.

With regard to rotation, the CRA Regulation provides that the European Commission shall assess the impact of the implementation of this measure and the need to extend its scope of application to other asset classes in a report to the European Parliament and the Council by 1 January 2016.<sup>24</sup>

## **3.2. Regulatory requirements for the use of credit ratings**

In the majority of instances, smaller CRAs have thus far not been recognised as External Credit Assessment Institutions (ECAIs) by banking supervisory authorities, the European Central Bank (ECB), the European Investment Bank (EIB) and the European Bank for Reconstruction and Development (EBRD). Subsequently, their ratings are not taken into account in the existing mappings of rating scales, which does not allow them to be used together with ratings from larger CRAs for the calculation of regulatory capital requirements for banks or in risk-based requirements for insurance and reinsurance undertakings. As an example, the system of mapping of rating scales carried out by the ECB, Eurosystem, includes only the 4 largest CRAs. This is considered by smaller CRAs as an important barrier of entry.

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<sup>23</sup> Article 6b CRA Regulation.

<sup>24</sup> Article 39(5) CRA Regulation

### 3.2.1. Recognition of CRAs as ECAIs and mapping of credit rating scales by European Banking Authority (EBA)

Measures to tackle this barrier of entry for small CRAs in the banking sector have been already adopted as part of the CRD IV package<sup>25</sup>. The Capital Requirements Regulation (CRR)<sup>26</sup> contains a definition of ECAIs including all CRAs registered or certified with ESMA<sup>27</sup> and is applicable since 1 January 2014.

At the same time, EBA, in cooperation with ESMA and EIOPA, is developing Regulatory Technical Standards (RTS) in order to finalise the mapping of rating scales of all CRAs<sup>28</sup>, which will make it possible for this measure to take effect and allow the use also of credit ratings from smaller CRAs by banks for the calculation of regulatory capital requirements under the CRD IV Package<sup>29</sup>. The draft RTS should be submitted to the European Commission by 1 July 2014.

Once finalised and fully effective, this measure will be beneficial for new market entrants or smaller CRAs since their ratings can be used by credit institutions in the context of the calculation of regulatory capital,, which will give them access to new clients.

### 3.2.2. Recognition of CRAs as ECAIs and mapping of credit rating scales by EIOPA

The current legislative framework in the area of insurance and reinsurance undertakings does not contain references to ratings. However, in a similar way to the banking sector the Omnibus II Directive<sup>30</sup> foresees the limited use of external credit ratings to rank credit risks in the implementing measures on the standard formula Solvency Capital Requirement calculation. This measure will be implemented through the set-up of a mapping system of rating scales of ECAIs, which although it may slightly differ from the EBA mapping system as regards the number of credit quality steps, will give equal market access to smaller and larger CRAs.

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<sup>25</sup> The CRD IV package transposes – via a Regulation and a Directive – the global standards on bank capital (commonly known as the Basel III agreement) into the EU legal framework

<sup>26</sup> Regulation (EU) 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 (EU) No 648/2012, OJ L 176, 27.6.2013, p.1

<sup>27</sup> Article 4 (98) CRR: “ external credit assessment institution' or 'ECAI' means a credit rating agency that is registered or certified in accordance with Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies ( 1 ) or a central bank issuing credit ratings which are exempt from the application of Regulation (EC) No 1060/2009”

<sup>28</sup> Article 136(1) and (3) CRR

<sup>29</sup> Article 135(1) CRR provides that "An external credit assessment may be used to determine the risk weight of an exposure under this Chapter only if it has been issued by an ECAI or has been endorsed by an ECAI in accordance with Regulation (EC) No 1060/2009."

<sup>30</sup> COM PROPOSAL 2011/0006(COD) DIRECTIVE 2014/.../EU OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Directives 2003/71/EC and 2009/138/EC and Regulations (EC) No 1060/2009, (EU) No 1094/2010 and (EU) No 1095/2010 in respect of the powers of the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority) will introduce the such provisions in Directive 2009/138/EC (Solvency II) in Article 109a and Article 111.

### **3.3. Asymmetry in access to information**

Due to their position on the rating market, smaller CRAs often do not get the same level of information as their larger competitors, which are approached on a more regular basis by potential issuers. This in turn prevents them from the opportunity to issue unsolicited ratings and build up their reputation by increasing their visibility in new segments of the rating market.

Taking the above into consideration and with the aim to increase transparency on the market, the CRA III Regulation contains a requirement that issuers must disclose on an on-going basis specific information on financial structured products, especially the major elements of the underlying assets<sup>31</sup>. Apart from increasing transparency for investors, this measure is likely to reinforce the competition between credit rating agencies, because it could lead to an increase in the number of unsolicited credit ratings, and eventually can be beneficial specifically to smaller CRAs not always having access to relevant information. This will contribute to increasing their visibility in the market towards issuers and investors alike.

The Commission shall, by January 2016, review and report on the appropriateness of extending the scope of that disclosure requirement to other financial credit products<sup>32</sup>. For example, there are other financial products, such as covered bonds and other secured debt, where the risk to a large extent depends on the characteristics of any underlying collateral and where it could be relevant to provide the market with more information about the collateral.

### **3.4 Barriers to international development**

Smaller CRAs reported the lack of cross-border access to markets outside the EU (e.g. Japan and Russia) as a barrier for growth to other geographical markets. Many third countries require local presence in order to be able to use ratings (mainly banks when investing into products rated in the EU). This leads to a competitive disadvantage for smaller CRAs since through certification their peers from those countries (which have been declared equivalent to the EU) could have their ratings accepted on the EU market.

### **3.5. Compliance costs as a barrier of entry and growth for smaller CRAs?**

The existing legislative framework on the rating market implies compliance costs for smaller and bigger CRAs alike. However, it envisages several exemptions for smaller CRAs in order to avoid that those costs become disproportionate for them and represent too heavy a burden or even a barrier of entry to the market. This section of the report analyses the importance of compliance costs for smaller CRAs as a potential barrier of entry. It also assesses how those costs increase with the growth in size of the CRAs and if they risk becoming a barrier for their growth once certain exemption thresholds are reached by smaller CRAs.

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<sup>31</sup> Article 8b CRA Regulation

<sup>32</sup> Article 39(5) CRA Regulation

### 3.5.1. Exemptions from certain requirements for smaller CRAs

There are several exemptions envisaged under the legislative framework in order to alleviate the compliance burden for smaller CRAs and to make respective costs more proportionate to the size of the CRA. In order to be eligible for these exemptions, CRAs need to comply with certain pre-conditions and be below of certain thresholds, (10 million euros turnover in the case of exemptions from fees payable to ESMA for registration and supervision as well as 50 employees in the case of certain compliance costs-see also section on compliance costs as a barrier of entry and growth). This approach aims at helping smaller CRAs to preserve their competitiveness and facilitate their entry into the CRA market.

### 3.5.2. Registration and supervisory fees

In order to assess the significance of compliance costs as a financial burden for smaller CRAs the European Commission requested ESMA to provide an indication of the compliance costs for all registered CRAs. The following paragraphs provide information on the costs linked to registration and on-going supervision by ESMA and other compliance costs, as well as an analysis of their potential impact on the competitiveness of smaller CRAs.

The CRA Regulation states that ESMA shall charge registration and supervisory fees to the CRAs to fully cover ESMA's necessary expenditure relating to the registration and supervision of credit rating agencies and the reimbursement of any costs incurred by competent authorities as a result of a delegation of supervisory tasks<sup>33</sup>. In addition, the CRA Regulation specifies that the amount of registration and supervisory fees shall be proportionate to the turnover of the credit rating agency concerned.

As regards supervisory fees, the Commission Delegated Regulation<sup>34</sup> stipulates that a registered credit rating agency shall be exempted from paying an annual supervisory fee where its total revenues as published in its most recent audited accounts is less than EUR 10 million, or in case it belongs to a group of credit rating agencies with aggregate total revenues of less than EUR 10 million. As specified in Recital 3 of the Delegated Regulation, annual supervisory fees should not become a burden for new entrants to the credit rating market. Moreover, small CRAs are expected to produce significantly less supervisory costs than larger ones according to the Delegated Regulation. In this context it should be noted that in the first year of registration, CRAs pay a supervisory fee of EUR 500 for each complete month in the time period between the date of registration and the end of the financial year<sup>35</sup>.

The same proportionality principle applies for the registration and certification fees. The Commission Delegated Regulation provides that registration fee must be proportionate with the size and activity of the CRAs, with respect to whether the CRA intends to issue structured

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<sup>33</sup> Article 19 CRA Regulation

<sup>34</sup> Article 5(1) of Commission Delegated Regulation (EU) No 272/2012 of 7 February 2012 supplementing Regulation (EC) No 1060/2009 of the European Parliament and of the Council with regard to fees charged by the European Securities and Markets Authority to credit rating agencies, OJ L 90, 28.3.2012, p. 6

<sup>35</sup> Article 6(8) Commission Delegated Regulation

finance instruments ratings, whether a CRA has branches and whether it plans to endorse ratings<sup>36</sup>.

As regards registration fees, under the terms of the CRA Regulation most of the smaller CRAs have been registered by the National Competent Authorities before registration and supervision by ESMA was introduced in 2011, and therefore no registration fee was paid to ESMA. So far only 4 of the 22 registered CRAs have been registered directly by ESMA (Axesor, EIU, Dagong Europe and Spread Research) as well as one of the two certified CRAs (Kroll). Registration fees have varied between EUR 2.000 EUR and EUR 40.000 according to the CRAs' size and organisational features.

The Commission Delegated Regulation also provides that for the purposes of the calculation of the annual supervisory fee the applicable turnover shall be the revenues of a CRA, as published in its audited accounts generated from rating activities and ancillary services<sup>37</sup>. The applicable turnover is determined by ESMA from the audited turnover generated from rating activities and ancillary services in the previous financial year. Only two of the smaller CRAs were not covered by the exemption and contributed to the supervisory fees charged by ESMA. Smaller CRAs accounted for 4% of the total supervisory fees charged by ESMA<sup>38</sup>.

### 3.5.3. Other compliance costs<sup>39</sup>

According to the CRA Regulation, a credit rating agency that has fewer than 50 employees can request to ESMA to be exempted from complying with the requirements regarding independent non-executive directors, the independent compliance function and analyst rotation, thus lowering the regulatory costs for such CRAs. CRAs with fewer than 50 employees qualify for requesting exemptions if they can “demonstrate that those requirements are not proportionate in the view of the nature, scale and complexity of its business and the nature and range of issue of credit ratings”<sup>40</sup>. Following such a request for exemption, ESMA assesses whether all requirements are fulfilled.

As of end July 2013, five registered smaller CRAs had more than 50 employees, i.e., 14 registered CRAs had less than 50 employees.

So far, all of the 14 smaller CRAs have been granted by ESMA one or more of the following exemptions:

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<sup>36</sup> Article 6 Commission Delegated Regulation

<sup>37</sup> Article 3 Commission Delegated Regulation

<sup>38</sup> Two other CRAs also paid supervisory fees as they had applicable turnover above EUR 10 million, however these accounted for minor amounts: Japan Credit Rating (paid the fixed fee applicable for certified CRAs), and EIU which paid the applicable fixed supervisory fee for the first year of registration.

<sup>39</sup> This section of the report is based on the data provided by ESMA in its Technical Advice on the feasibility of a network of smaller CRAs.

<sup>40</sup> Article 6(3) CRA Regulation

- Exemption to have an independent non-executive director<sup>41</sup>: 11 CRAs;
- Exemption to have an independent compliance function<sup>42</sup>: 6 CRAs;
- Exemption to have an analyst rotation requirement<sup>43</sup>: 9 CRAs.

As regards the independent compliance function exemption, in most cases, smaller CRAs do not employ more than one full-time compliance officer. In some cases CRAs that have been granted this exemption have deemed it necessary to have an internal compliance officer for operational reasons. In the other cases, the CRAs that have obtained the said exemption use outsourced consultants or board members to undertake the compliance tasks.

Since the entry into force on 20 June 2013 of the CRA III Regulation, CRAs can also request to ESMA to be exempted from the obligation to establish a review function<sup>44</sup>. As of 31 August 2013, ESMA has not granted such an exemption due to lack of requests.

In conclusion, while the CRA regulation introduces requirements for all CRAs which could potentially result in additional compliance costs for smaller CRAs, registration and supervisory costs can be considered proportionate to the activities of smaller CRAs. Hence, they do not constitute a barrier of entry for smaller CRAs. Furthermore, the potential increase in compliance costs for those smaller CRAs reaching the exemption thresholds (50 employees and 10 million euro turnover) is most likely not a potential barrier to growth since the respective increase of those compliance costs is expected to be relative to the size of their activities.

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<sup>41</sup> Annex 1, Section A, point 2 CRA Regulation

<sup>42</sup> Annex 1, Section A, point 5&6 CRA Regulation

<sup>43</sup> Article 7(4) CRA Regulation

<sup>44</sup> Annex 1, Section A, point 9 CRA Regulation