



Credit Rating Agencies

6th Tokyo Roundtable on Capital Market Reform in Asia
(September 28, 2004)

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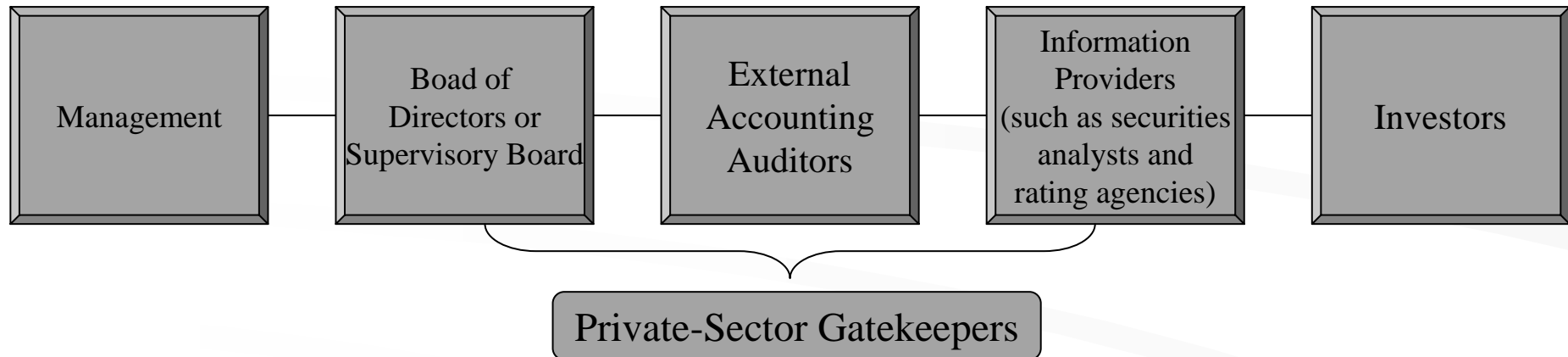
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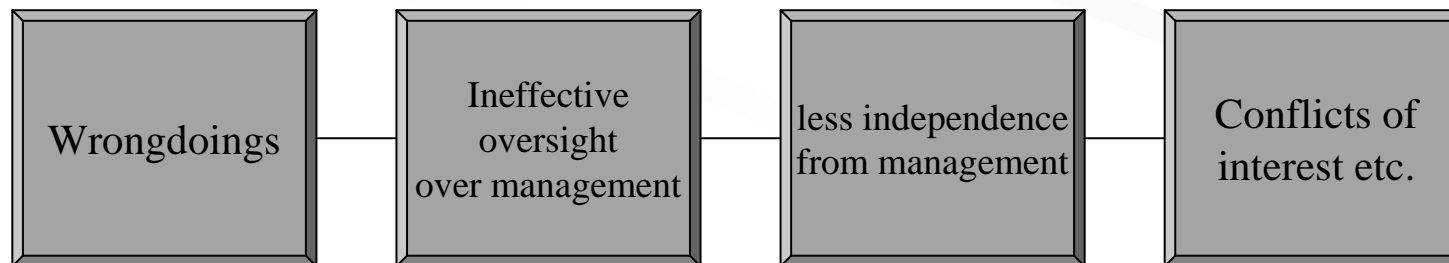


I. Financial Reporting Supply Chain

1. Structure of Chain



2. Problems (Pointed out)





II. Important Issues relating to CRAs

Transparency

Conflicts of Interest

Competition



III . Recent International Regulatory Developments (1)

IOSCO

Basel Committee on Banking Supervision

U.S. SEC

EU



III . Recent International Regulatory Developments (2)

IOSCO

1. IOSCO Statement of Principles Regarding the Activities of CRAs (September 25, 2003)

[Basic Purposes]

- Useful tool for securities regulators, ratings agencies and others wishing to improve how CRAs operate and how the opinions CRAs assign are used by market participants
- The manner in which these Principles are given effect will depend upon local market circumstances and each jurisdiction's legal system.
- Mechanism for implementing the principles may take the form of any combination of government regulations, regulation imposed by non-government statutory regulators, industry codes, and internal rating agency policies and procedures.



III . Recent International Regulatory Developments (3)

[Principles]

① Quality and Integrity of the Rating Process

- CRAs should endeavor to issue opinions that help reduce the asymmetry of information among borrowers, lenders and other market participants. [Five Principles]

② Independence and Conflicts of Interest

- CRA ratings decisions should be independent and free from political or economic pressures and from conflicts of interest arising due to the CRA's ownership structure, business or financial activities, or the financial interests of the CRA's employees. CRAs should, as far as possible, avoid activities, procedures or relationships that may compromise or appear to compromise the independence and objectivity of the credit rating operations. [Six Principles]

③ Transparency and Timeliness of Ratings Disclosure

- CRAs should make disclosure and transparency an objective in their ratings activities. [Five Principles]

④ Confidential Information

- CRAs should maintain in confidence all non-public information communicated to them by any issuer, or its agents, under the terms of a confidentiality agreement or otherwise under a mutual understanding that the information is shared confidentially. [Two Principles]



III . Recent International Regulatory Developments (4)

2. Report on the Activities of CRAs (September 25, 2003)

- Role of CRAs
- Overview of CRA Questionnaire and Questionnaire Responses
- Overview of Key Issues for Securities Regulators
- The Technical Committee's Statement of Principles regarding the Activities of CRAs



III . Recent International Regulatory Developments (5)

3. Code of Conduct Regarding the Activities of CRAs (to be finalized around November 2004)

[Basic Purposes (Draft)]

- A set of robust, practical measures that serve as a guide to and a framework for implementing the Principles' objectives
- Model upon which individual CRA codes of conduct should be based
- Helping ensure that a converged standard of CRA conduct existed throughout the world, irrespective of market circumstances and legal and regulatory structures



III . Recent International Regulatory Developments (6)

[Draft Code of Conduct]

① Quality and Integrity of the Rating Process

- A. Quality of the Rating Process
- B. Monitoring and Updating
- C. Integrity of the Rating Process

② CRA Independence and Avoidance of Conflicts of Interest

- A. General
- B. CRA Procedures and Policies
- C. CRA Analyst and Employee Independence

③ CRA Responsibilities to the Investing Public and Issuers

- A. Transparency and Timeliness of Rating Disclosure
- B. Treatment of Confidential Information
- C. Disclosure of the Code of Conduct



III . Recent International Regulatory Developments (7)

Basel II (June 26, 2004)

- **The Standardized Approach measures credit risk, supported by external credit assessments.**

- **National supervisors are responsible for determining an eligible external credits assessment institution (ECAI).**

- **Eligibility Criteria**
 - ① Objectivity
 - ② Independence
 - ③ International access / Transparency
 - ④ Disclosure
 - ⑤ Resources
 - ⑥ Credibility



III . Recent International Regulatory Developments (8)

U.S. SEC Concept Release (June 4, 2003)

- ① Alternatives to the NRSRO (Nationally Recognized Statistical Rating Organizations) Designation
- ② Recognition Criteria
- ③ Examination and Oversight of NRSROs
- ④ Conflicts of Interest
- ⑤ Alleged Anticompetitive, Abusive, and Unfair Practices
- ⑥ Information Flow



III . Recent International Regulatory Developments (9)

EU

- **Resolution by the European Parliament on role and methods of rating agencies (February 2004)**
- **Resolution by the German Federal Parliament on improving the integrity, independence and transparency of rating agencies through a code of conduct (March 2004)**
- **EC's call to CESR (Committee of European Securities Regulators) for technical advice on possible measures concerning CRAs by April 1, 2005**
 - Interests and conflicts of interest for CRAs
 - Fair presentation of credit ratings
 - Relationship between issuers and rating agencies
 - Possible entry barriers to the market for the provision of credit ratings
 - Use of ratings in European legislation and in private contracts
 - Registration



IV. CRAs System in Japan (1)

1. Designated Rating Agencies System in Japan

○ The Commissioner of the FSA designates certain CRAs as Designated Rating Agencies (“DRA”).

The following matters are to be considered for designation :

- Rating records
- Personal structure
- Organization
- Rating methods
- Capital structure
- Neutrality from issuers
- Others



IV. CRAs System in Japan (2)

- **Ratings assigned by DRAs are used in regulations.**
 - regulatory capital requirements (banks, securities companies, insurance companies)
 - defining investment grade securities for mutual funds and purchasing of stocks by the Banks' Shareholding Purchase Corporation
 - determining whether issuers can use the reference system of the securities registration system or the self registration system for public offerings of corporate bonds

- **DRAs system is not regulation or supervision over CRAs.**



IV. CRAs System in Japan (3)

2. Current DRAs in Japan

- Rating and Investment Information, Inc. (R&I)
- Japan Credit Rating Agency, Ltd. (JCR)
- Moody's Investments Securities, Inc. (Moody's)
- Standard and Poor's Credit Market Securities (S&P)
- Fitch Ratings Limited (Fitch)