IOSCO STATEMENT OF PRINCIPLES REGARDING THE ACTIVITIES OF CREDIT RATING AGENCIES

A STATEMENT OF THE TECHNICAL COMMITTEE OF THE INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS

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Credit rating agencies (CRAs, or ratings agencies) issue opinions on the future creditworthiness of a particular company, security or obligation as of a given date. These opinions tend to be relied upon by investors, lenders, and others, and, accordingly, CRAs can have an effect on securities markets in a variety of ways. Credit ratings can affect issuers' access to capital, influence the structure of financial transactions, and determine the types of investments fiduciaries and others can make. Some regulators use the ratings issued by CRAs for various regulatory purposes.

Given the influence CRA opinions can have on securities markets, the activities of CRAs are of interest to investors, lenders, issuers and securities regulators alike. The core objectives of securities regulation, as described by IOSCO's "Objectives and Principles of Securities Regulation," are protecting investors, ensuring that securities markets are fair, efficient, and transparent, and reducing systemic risk. In offering informed, independent analyses and opinions, CRAs contribute to achieving these objectives.

Rating agencies that the market recognizes as credible and reliable can play a valuable role in global securities markets. Consequently, the Technical Committee has concluded that a set of IOSCO principles regarding the activities of CRAs would be a 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. As CRAs are regulated and operate differently in different jurisdictions, the following principles do not lay out a "one-size-fits-all" approach, but state high-level objectives for which ratings agencies, regulators, issuers and other market participants should strive in order to improve investor protection and the fairness, efficiency and transparency of the securities markets and reduce systemic risk.

The manner in which these principles are given effect will depend upon local market circumstances and each jurisdiction's legal system. In some cases, the principles may be best implemented through internal mechanisms at the CRA and promoted by borrowers, lenders and other market participants. Depending on the circumstances, the principles could be given effect through regulatory requirements. As a result, mechanisms for implementing the principles may take the form of any combination of:

- Government regulation;
- Regulation imposed by non-government statutory regulators;

— Industry codes; and,

— Internal rating agency policies and procedures.

The Technical Committee proposes to await future consideration of these alternatives in the major jurisdictions and take account of preferences of other sector supervisors before considering its preferred method of implementation. The Technical Committee proposes to review these developments within 18 months.

PRINCIPLES FOR THE ACTIVITIES OF CREDIT RATING AGENCIES

Quality and Integrity of the Rating Process

1. CRAs should endeavor to issue opinions that help reduce the asymmetry of information among borrowers, lenders and other market participants.

1.1. CRAs should adopt and implement written procedures and methodologies to ensure that the opinions they issue are based on a fair and thorough analysis of all relevant information available to the CRA, and that CRA analysts perform their duties with integrity. CRA rating methodologies should be rigorous, systematic, and CRA ratings should be subject to some form of validation based on historical experience.

1.2. CRAs should monitor on an ongoing basis and regularly update an analysis and rating once a rating is issued whenever new information becomes available that causes the rating agency to revise or terminate its opinion.

1.3. CRAs should maintain internal records to support their ratings.

1.4. CRAs should have sufficient resources to carry out high-quality credit assessments. They should have sufficient personnel to properly assess the entities they rate, seek out information they need in order to make an assessment, and analyze all the information relevant to their decision-making processes.

1.5. Analysts employed by ratings agencies should use the methodologies established by the CRA and be professional, competent, and of high integrity.

Independence and Conflicts of Interest

2. 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.

2.1. CRAs should adopt written internal procedures and mechanisms to (1) identify, and (2) eliminate, or manage and disclose, as appropriate, any actual or potential conflicts of *interest that may influence the opinions and analyses CRAs make or the judgment and analyses of the individuals the CRAs employ who have an influence on ratings decisions. CRAs are encouraged to disclose such conflict avoidance and management measures.*

2.2. *The credit rating a CRA assigns to an issuer should not be affected by the existence of or potential for a business relationship between the CRA (or its affiliates) and the issuer or any other party.*

2.3. *CRAs and CRA staff should not engage in any securities or derivatives trading presenting inherent conflicts of interest with the CRAs ratings activities.*

2.4. *Reporting lines for CRA staff and their compensation arrangements should be structured to eliminate or effectively manage actual and potential conflicts of interest. A CRA analyst should not be compensated or evaluated on the basis of the amount of revenue that a CRA derives from issuers that the analyst rates or with which the analyst regularly interacts.*

2.5. *The determination of a credit rating should be influenced only by factors relevant to the credit assessment.*

2.6. *CRAs should disclose the nature of the compensation arrangement that exists with an issuer that the CRA rates.*

Transparency and Timeliness of Ratings Disclosure

3. CRAs should make disclosure and transparency an objective in their ratings activities.

3.1. *CRAs should distribute in a timely manner their ratings decisions regarding publicly issued fixed-income securities or issuers of publicly traded fixed-income securities.*

3.2. *CRAs should disclose to the public, on a non-selective basis, any rating regarding publicly issued fixed income securities as well as any subsequent decisions to discontinue such a rating if the rating is based in whole or in part on material non-public information.*

3.3. *CRAs should publish sufficient information about their procedures and methodologies so that outside parties can understand how a rating was arrived at by the CRA. This information should include (but not be limited to) the meaning of each rating category and the definition of default and the time horizon the CRA used when making a rating decision.*

3.4. *CRAs should publish sufficient information about the historical default rates of CRA rating categories and whether the default rates of these categories have changed over time, so that interested parties can understand the historical performance of each category and if and how ratings categories have changed.*

3.5. *CRAs should disclose if a rating is unsolicited.*

Confidential Information

4. 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.

4.1. CRAs should adopt procedures and mechanisms to protect the non-public nature of information shared with them by issuers under the terms of a confidentiality agreement or otherwise under a mutual understanding that the information is shared confidentially.

4.2. CRAs should use non-public information only for purposes related to their rating activities or otherwise in accordance with their confidentiality agreements with the issuer.