



European Securities and  
Markets Authority

# Final Report

**Revision to Guidelines and Recommendations on the Scope of the  
CRA Regulation**







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## Legislative references, abbreviations and definitions

2013 Guidelines	Guidelines and Recommendations on the Scope of the CRA Regulation
CP	Consultation paper
CRA or CRAs	Credit Rating Agency or Credit Rating Agencies
CRA Regulation or CRAR	Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit ratings agencies as amended by Regulation (EU) No 513/2011 of the European Parliament and of the Council of 11 May 2011, Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011, Regulation (EU) No 462/2013 of the European Parliament and of the Council of 21 May 2013, and Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014
ESMA	European Securities and Markets Authority
EU	European Union
SMEs	Small and medium enterprises

## 1. Executive Summary

### Reasons for publication

1. In 2013, ESMA published its Guidelines and Recommendations on the Scope of the CRA Regulation (the 2013 Guidelines). The purpose of these Guidelines was to provide practical clarification on the scope of the CRA Regulation. Since the entry into force of these Guidelines, ESMA has developed its supervisory expertise and is in a position to expand upon the guidance that was provided under certain areas of the 2013 Guidelines. The purpose of these Guidelines is to deliver additional guidance in the specific case of private credit ratings.
2. In this regard, while the CRA Regulation sets out requirements for carrying out credit rating activities in the EU, it also establishes the scope of the Regulation and those rating activities that are exempted from the regulation's requirements. Specifically, Article 2(2)(a) states that the CRA Regulation does not apply to "private credit ratings produced pursuant to an individual order and provided exclusively to the person who placed the order and which are not intended for public disclosure or distribution by subscription". This point was elaborated upon in the 2013 Guidelines, where paragraph 14 set out that the recipient of a private credit rating is allowed to share the rating with "a limited number of third parties" on a strictly confidential basis.
3. With a view to addressing a lack of understanding on the practical application of this guidance and building on supervisory experience, ESMA proposes a refinement to the 2013 Guidelines in this area.
4. ESMA conducted a public consultation on these Guidelines in order to gather the views of CRAs and other relevant stakeholders. A number of amendments and clarifications have been introduced into the final Guidelines in order to take account of the views expressed during this consultation.

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5. The Guidelines provide additional clarification to paragraphs 14 and 15 of the 2013 Guidelines, in particular to the following key elements of private credit ratings:
  - How the term "produced pursuant to an individual order" should be interpreted and understood.
  - How the term "provided exclusively to the person who placed the order" should be interpreted and understood.
  - The boundaries on the sharing of a private credit rating with a "limited number of third parties".
  - The monitoring of the distribution of private credit ratings by the rating provider.



### **Next Steps**

6. The revised paragraphs 14 and 15 of the Guidelines set out in Annex I, together with the ancillary text in sections I and II, will be translated into all official languages of the EU and published on ESMA's website. ESMA will consider these Guidelines for the purpose of its supervision 18 months following the date of publication.

## **2. Feedback Statement**

1. A total of 15 responses were received to the Consultation Paper; from 12 CRAs registered with ESMA, 2 trade associations and one academic. This feedback statement provides a summary of the principal comments received.

### **Guidelines - General**

2. Respondents to the CP were broadly in support of ESMA's objectives to expand on the existing regulatory provisions on private credit ratings, in the interest of providing clarity to the market vis-à-vis the perimeter of the CRA Regulation. Comments were mainly focused on: (i) ESMA's expectations around pre-contractual process and initial interactions between the rating provider and requesting party; (ii) the use of the quantitative precedent from the Prospectus Regulation to define "a limited number of third parties" for the purposes of clarifying the boundaries on the sharing of a private credit rating; and (iii) the oversight duties imposed on rating providers to monitor the dissemination of private credit ratings to third parties.

### **Private credit ratings produced pursuant to an individual order (Question 1)**

3. A majority of respondents welcomed the introduction of a clarification of the level 1 provision "produced pursuant to an individual order". There was general consensus among respondents that requiring an explicit order for a private credit rating, as well as a formal bilateral relationship between the rating provider and the person contracting the service through a written agreement, would enhance clarity and transparency for market participants.
4. However, some respondents argued that the formal acceptance prerequisite on behalf of the rating provider would be redundant and create an unnecessary burdensome step in the client onboarding process. One of those respondents also argued that it is typically the rating provider who provides a contract, with the requesting party thereafter communicating its consent to the terms and conditions, and not the other way around, as per ESMA's proposed guidance.
5. One respondent asked for clarification on the applicability of the Guidelines to situations where a client is in possession of a public rating but wishes to convert this into a private credit rating through a contractual amendment. Similarly, another respondent gave an example of a situation where a client would initially request a private credit rating from a CRA and later request that such rating to be made public, asking for ESMA's views on this scenario in the context of the proposed guidance.
6. One respondent enquired about the applicability of the guidance to credit ratings that are produced internally, at the initiative of a CRA, to be used as an input for the creation of other credit ratings. Another respondent stated that the guidance should not apply to credit ratings raised internally within a bank and shared with other credit institutions for the purpose of a joint business transaction.

7. **ESMA Response:** To address these comments, ESMA has removed the acceptance requirement from the text of the Guidelines, on the basis that it may be onerous for the internal processes of rating providers. This has been done by replacing the term “the private credit rating should only be produced following (...) **a formal written acceptance by the rating provider**” from paragraph 14 with “(...) through a **written agreement** between the person placing the order and the rating provider”.
8. ESMA would like to take this opportunity to clarify that the Guidelines do not apply to situations where a client seeks to convert a credit rating of public nature into private through a contractual amendment. Likewise, internal ratings prepared at the instigation of a rating provider’s own employees are out of scope of the Guidelines, given the lack of an explicit external order for a private credit rating. In relation to the conversion of a private credit rating into a public rating, this would involve crossing the boundary into the scope of the CRA Regulation. ESMA would like to highlight that only a rating provider who is an ESMA-registered CRA and complies with the rules on organisation and conduct of business set forth in CRAR, can issue credit ratings for regulatory purposes in the EU.

#### **Private credit ratings provided exclusively to the person who placed the order (Question 2)**

9. The majority of respondents agreed with ESMA’s proposal for the written agreement between the parties to contain a provision indicating the exclusive delivery of the private credit rating to the person who placed the order. Few CRA respondents pointed out that their standard contracts for the provision of private credit ratings to clients already include provisions stating the private nature of such ratings.
10. Regarding the requirement for both parties to enter into a non-disclosure undertaking, two respondents raised specific concerns about its added value, on the basis of onerous implementation processes. Another respondent requested ESMA to clarify the expected content of such an undertaking. Furthermore, one respondent requested ESMA’s clarification as to whether it could simply take the form of an individual clause within the agreement, as opposed to requiring a standalone legal document.
11. One aspect in the CP that raised scepticism was ESMA’s views that, in a scenario where two or more persons request the same private credit rating at the same time, a specific analysis should be completed by the provider for each of the orders placed. One respondent, in particular, mentioned that the reference to “exclusive issuance” in the text of the Guidelines might suggest that the same rating could not be provided to a different client who places the same individual order.
12. **ESMA Response:** Regardless of contract templates used by certain rating providers already indicating the private nature of the relationship between a private credit rating provider and the requesting entity, ESMA intends to strengthen the obligation of exclusive issuance to the person who placed the order, by requiring an explicit provision in the agreement. To this end, it has amended the text of the Guidelines to reflect that “ESMA

expects (...) a **specific** provision indicating the exclusive issuance of the rating to the person who placed the order”.

13. ESMA considers that the non-disclosure undertaking can either take the form of a clause within the agreement to issue the private credit rating, or of a separate agreement signed between issuer and the person placing the order. ESMA does not feel the need to dictate the terms of such an agreement, leaving this to the discretion of rating providers.
14. Furthermore, ESMA would like to take this opportunity to clarify its view that, should there be two or more simultaneous orders raised for a private credit rating on the same instrument of the same issuer, there should be separate contractual and administrative processes in place for each client, making up different bilateral relationships, rather than one single multilateral relationship. Whilst the rating process may be the same and the output identical, the private credit rating should be customised to each requesting party.
15. No further changes to the text of the Guidelines have been made to reflect the above clarifications.

### **Sharing private credit ratings with a limited number of third parties (Question 3)**

16. ESMA received a large number of responses to this question. While a minority of respondents supported the proposed guidance as is, the majority put forward refinements to improve the feasibility of the requirements. Specifically, respondents questioned the difficulty of keeping a reliable count of third party natural persons accessing a private credit rating, with a few respondents claiming this would be an easy limit to exceed.
17. Other respondents claimed that the definition of “a limited number of third parties” in the revised Guidelines is narrower than that of “a restricted circle of investors” from the Prospectus Regulation that ESMA seeks to replicate. Another respondent expressed their doubts that ESMA would be able to introduce an element contained in a “level 1” legal act (Prospectus Regulation) other than its underlying, predicate text (CRA Regulation) into a “level 3” text (ESMA Guidelines) by analogy.
18. Some respondents argued that ESMA’s reference in the CP to the “objective and justified reasons” for third parties to receive a private credit rating should be explained further, notably in relation to the resulting obligations for the rating provider.
19. Some respondents requested a clarification on the limit of 150 third party recipients for a private credit rating, in terms of whether this would amount to the limit per EU Member State or in total.
20. There were also calls from two respondents for ESMA to actively consider the nature of investors in its proposed definition of “a limited number of third parties”. In line with the Prospectus Regulation’s exemption for publishing a prospectus, both suggested that the distribution should be restricted to qualified investors, with one respondent adding “who have their own internal credit assessment models”.

21. Some respondents suggested more flexibility around the proposed quantitative limit for distribution to third parties by the receiving party. For instance, through the exclusion from the count of (i) informal sharing within an organisation; or (ii) dissemination to third parties such as accountants, legal counsel, auditors and regulators. Other respondents suggested alternative means of rendering the requirement less onerous, such as setting the 150 limit on an annual basis before the count replenishes to zero, or being allowed to replace one third party recipient by another, with the 150 limit applying on an ongoing basis.
22. **ESMA Response:** With regard to the quantification of the term “a limited number of third parties” contained in the 2013 Guidelines, ESMA has decided to amend the wording of the Guidelines to “ESMA expects that (...) this number should be limited and can never exceed **a total of 150 persons.**” ESMA’s initial intention in the CP to not replicate the term “legal persons” in paragraph 15, when defining the quantitative limit, was to avoid imposing an obligation upon rating providers of keeping two separate counts for third parties (i.e. one for individuals in possession of the private credit rating, another for legal entities). However, it accepts that this may have caused confusion and could possibly have been seen as a deviation from the definition of the Prospectus Regulation (encompassing both “natural” and “legal” persons), which ESMA has based its limit on. As such, by adding the term “a total of” and removing the repeated reference to “natural persons” from the guidance, ESMA seeks to clarify that not only each individual employee receiving a rating within a legal entity, but also the legal entity itself, should effectively be counted as a third party for the purposes of reaching the 150 limit. Moreover, the term “a total of” also clarifies that this limit is not applicable per Member State, but rather as a whole.
23. ESMA notes that no additional obligations arise for rating providers in relation to the qualitative criterion provided in the CP for the sharing of a private credit rating with third parties (“objective and justified reasons”). Although it is expected that the contracting party adheres to these principles, this reference has not been added to the text of the Guidelines, as it is already implicit from the proposed guidance in paragraph 14 (“ESMA expects that the receiving party only shares the private credit rating on a confidential basis and with a selected and definite number of natural or legal persons”).
24. In response to the various calls for ESMA to allow for greater flexibility or to establish further exceptions<sup>1</sup> to the proposed quantitative limit, ESMA considers these would, in practice, result in a potentially unlimited increase to the 150 legal or natural person threshold. ESMA deems that this could effectively amount to a number of receiving parties that would not be consistent with the legal definition of private credit ratings under the CRA Regulation, according to which they are “not intended for public disclosure or distribution by subscription”.

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<sup>1</sup> The only exception foreseen is the dissemination of the private credit rating for legal, statutory or judicial reasons, for instance to statutory auditors, supervisory authorities or law enforcement.

#### **Monitoring the distribution of private credit ratings (Question 4)**

25. ESMA received several comments on the expectation that rating providers monitor client actions. In this regard, respondents expressed concerns in relation to the level of liability for a rating provider in case the receiving entity abusively engages in the dissemination of the private credit rating beyond “a limited number of third parties”.
26. ESMA received a question from one respondent on whether the periodic monitoring of public sources to ascertain whether a private credit rating would have entered the public domain, would satisfy the standard of “appropriate controls” for the monitoring of the distribution to third parties. Similarly, another respondent enquired whether relying on contractual provisions and engaging with clients would not be more proportionate measures for rating providers to adopt.
27. One respondent suggested that the rating provider, upon becoming aware of a breach of the 150 limit for distribution to third parties, should inform both the requesting party and ESMA about this event.
28. **ESMA Response:** ESMA would like to clarify a number of examples that would satisfy its proposal of “appropriate controls” to be implemented by the rating provider to monitor the distribution limit of the private credit rating. For instance, the roll-out of email tracking tools, password-protected websites or other secure online file sharing solutions, such as private document exchange platforms; or non-IT solutions, such as the continuous engagement with the receiving party, where it is able to demonstrate that it has complied with the contractual provision on the limited dissemination of the rating. In relation to the monitoring of public sources of information, as put forward by one respondent, ESMA considers that it does not meet the requirement, unless cumulated with the latter example provided (engagement with the receiving party), as the distribution of a private credit rating to a potentially unlimited number of third parties can still occur despite the absence of a publication.
29. In case of becoming aware of a breach of the third party distribution limit, rating providers and other parties are encouraged to report this event to ESMA as an infringement of the perimeter of CRAR.

#### **Views on ESMA’s proposed approach and enhanced clarity for market participants (Question 5)**

30. ESMA received a limited number of responses to this question. Respondents generally expressed support for the proposal and concurred that the guidance would clarify ESMA’s expectations for market participants on the use and distribution of private credit ratings.

**ESMA Response:** No changes have been made to reflect responses to this question.

## Views on Cost Benefit Analysis (Question 6)

31. Most respondents were in favour of ESMA's preference for Option 2 (targeted update to the 2013 Guidelines) under the outlined Cost Benefit Analysis, recognising the importance of a public consultation. Two respondents argued that the cost benefit analysis did not sufficiently consider the cost of implementation for rating providers of appropriate controls, particularly with regard to IT costs. One respondent highlighted that these costs could be high and disproportionate to the size and operations of smaller CRAs.

**ESMA Response:** In response to question 4, ESMA has provided examples of "appropriate controls" where the rating provider would not incur in IT costs. As a result, other than minor language fixes, ESMA did not consider a change to the cost benefit analysis necessary.

### General comments

32. ESMA received a response indicating the text should be more precise in targeting both credit rating agencies and non-CRA providers of private credit ratings, as numerous references to CRAs alone can be found in paragraphs 14 and 15.

33. Respondents also asked for the guidance to apply on a prospective basis for new private credit ratings, notably those issued/received following the date of effective application of the Guidelines.

34. One respondent expressed concerns over the strict limits on the distribution of private credit ratings and the onerous monitoring requirements for rating providers, claiming these could make private placement markets less attractive to investors, which is detrimental to the financing of SMEs. Another respondent claimed that Guidelines imposing obligations on ESMA-registered entities may not be the best way to address the risks around the activities of non-CRAs.

35. One respondent suggested that ESMA allows sufficient time for the implementation of the revised Guidelines by the market.

36. **ESMA Response:** ESMA agrees with the remark made on nomenclature. To accommodate the clarification that the guidance applies equally to CRAs and non-CRA private credit rating providers, ESMA has replaced all references in paragraphs 14 and 15 of the Guidelines to "credit rating agency" or "credit rating agencies" to the broader term "rating provider". As a result, ESMA further notes that it has changed the scope of the Guidelines, adding "financial market participants providing private credit ratings produced pursuant to an individual order and provided exclusively to the person who placed the order and which are not intended for public disclosure or distribution by subscription" as targeted addressees of the text.

37. ESMA agrees that the revised guidance is forward looking and only applies to future private credit ratings.

38. ESMA would like to clarify that it has duly observed the principle of proportionality in its approach, as well as the overall objectives of the CMU Action Plan. ESMA believes these would be better achieved with a good functioning of the CRA Regulation, where the boundaries between private and public/regulated credit ratings is clear, in line with the spirit of the guidance. Moreover, ESMA underlines that the Guidelines apply equally to CRAs and non-CRA rating providers, as it has identified that the market as a whole would welcome and benefit from such a clarification.
39. ESMA has decided to allow for an implementation period of 18 months following the date of publication and translation of the text into all official languages of the EU, in order to provide sufficient time for CRAs and other market participants to adapt to the new requirements.
40. As a result of the entry into force of the revised version of the ESMA Founding Regulation<sup>2</sup> on 1 January 2020, a distinction is made between Guidelines (addressed to all National Competent Authorities or all financial market participants) and Recommendations (addressed to one or more National Competent Authorities or one or more financial market participant), under Article 16(1). As such, ESMA has removed all references to “Recommendations” from the 2013 Guidelines in Annex I.

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<sup>2</sup> Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority).

## **Annex I Guidelines on the Scope of the CRA Regulation**

### **Acronyms used**

CRAs Credit Rating Agencies

EBA European Banking Authority

NCAs National Competent Authorities as defined in the CRA Regulation, Art. 3(1)(p)

SCA Sectoral Competent Authorities as defined in the CRA Regulation, Art. 3(1)(r)



## I. Scope

### Who?

1. These guidelines are addressed to:
  - a. Credit rating agencies (as defined in the Article 3(1)(a) of the CRA Regulation);
  - b. NCAs and SCAs; and
  - c. Financial market participants providing private credit ratings produced pursuant to an individual order and provided exclusively to the person who placed the order and which are not intended for public disclosure or distribution by subscription.

### When?

2. These Guidelines will be published in all EU official languages.

## II. Purpose

3. The purpose of these guidelines is to provide a clarification of the scope of the CRA Regulation, in particular of the provisions thereof concerning the following specific matters:
  - a. obligation to register;
  - b. credit rating activities and exemptions from registration;
  - c. private credit ratings;
  - d. establishment of branches in third countries;
  - e. specific disclosure recommendations for credit scoring firms and CRAs established in third countries;
  - f. enforcement of the scope of the CRA Regulation and Cooperation with National Competent Authorities.

## III. Compliance and reporting obligations

### Status of the Guidelines

4. This document contains Guidelines issued under Article 16 of the ESMA Regulation. In accordance with Article 16(3) of the ESMA Regulation competent authorities and financial market participants must make every effort to comply with the Guidelines.
5. Competent authorities to whom the Guidelines are addressed should incorporate them into their supervisory practices, including where particular guidelines within the document are directed primarily at financial market participants.

6. As regards all the other chapters of these Guidelines, NCAs and financial market participants are required to comply with the provisions of the CRA Regulation, while ESMA has the duty to ensure the application thereof.
7. The clarifications provided in the present Guidelines are relevant for the application of the provisions of the CRA Regulation.

#### **Reporting requirements under art. 16 of ESMA Regulation**

8. Competent authorities to which paragraph 26 of these guidelines is addressed must notify ESMA to [info@esma.europa.eu](mailto:info@esma.europa.eu) whether they comply or intend to comply with the Guidelines, with reasons for non-compliance, within two months of the date of their publication by ESMA in all the EU official languages. In the absence of a response by this deadline, competent authorities will be considered as non-compliant. A template for notifications is available from the ESMA website.

#### **IV. Obligation to register under Art. 2(1), 3(b), 4, 5, and 14(1) of the CRA Regulation**

9. Credit rating agencies without a physical presence in the EU and fulfilling the prerequisites of Article 5 of the CRA Regulation shall obtain certification from ESMA before distributing credit ratings for regulatory purposes in the EU.
10. Credit rating agencies established in the EU that are carrying out credit rating activities in the EU without prior registration are operating in breach of Article 2(1) and 14(1) of the CRA Regulation. Any credit rating agency that intends to carry out credit rating activities shall immediately apply for registration by ESMA. Entities must not issue credit ratings until they are registered as CRAs. Such obligations also apply to legal entities established in the EU which employ rating analysts providing rating services to a third-country entity.
11. Only a legal person can apply for registration. A natural person cannot apply for registration.
12. ESMA shall take a supervisory measure according to Article 24 of the CRA Regulation against credit rating agencies that operate without registration or, where appropriate, certification in the Union and impose a fine pursuant to Article 36a and Annex III.54 of the CRA Regulation.

#### **V. Credit rating activities and exclusions from the scope of the CRA Regulation (Art. 2 and 3 of the CRA Regulation)**

13. Credit ratings, as defined in Article 3(1)(a) of the CRA Regulation, include quantitative analysis and sufficient qualitative analysis, according to the rating methodology established by the credit rating agency. A measure of creditworthiness derived from summarising and expressing data based only on a pre-set statistical system or model, without additional substantial qualitative rating-specific analytical input from a rating analyst should not be considered as a credit rating.
14. A rating which is provided to different persons belonging to a list of subscribers does not fall within the definition of “**private credit rating**” in Article 2(2)(a) of the CRA Regulation. On the other hand, Article 2(2) of the CRA Regulation does not mean that any transmission of the rating to a third party by the person that ordered it would correspond to public disclosure or distribution by subscription. The recipient of a **private credit rating** is allowed to share the rating with a limited

number of third parties and on a strictly confidential basis – as long as such disclosure does not correspond to public disclosure or distribution by subscription – to ensure that the **private credit rating** is not disclosed further. For instance, when applying for a loan, the recipient of a **private credit rating** may share his rating with his bank on a strictly confidential basis, or a bank can circulate a **private credit rating** to a restricted number of other banks for the purposes of a business transaction. **The private credit rating should only be produced following an explicit order, formalised through a written agreement between the person placing the order and the rating provider<sup>3</sup>. ESMA expects this agreement to contain a specific provision indicating the exclusive issuance of the rating to the person who placed the order, who should sign a non-disclosure undertaking, precluding the dissemination of the rating to more than a limited number of third parties.**

15. In accordance with Article 2(2)(a) of the CRA Regulation, **rating providers** should ensure that the agreements for the issuance of **private credit ratings** cover the duty of confidentiality and limitations on the distribution of the ratings. When issuing **private credit ratings**, **rating providers** should assess whether the person who placed the order, as recipient of the **private credit rating**, has any intention to use the rating in a way that would bring it into the public domain or to use it for regulatory purposes. Where the **rating provider** can reasonably conclude that a **private credit rating** could be disclosed to the public, for instance taking into account that the same client already breached the duty of confidentiality in the past, ESMA recommends as a best practice that **rating providers** should put in place the necessary measures to avoid such disclosure or refrain from issuing that rating. **ESMA also expects that the receiving party only shares the private credit rating on a confidential basis and with a selected and definite number of natural or legal persons. This number should be limited and can never exceed a total of 150 persons. To ensure that this maximum limit is adhered to, appropriate controls should be implemented by the rating provider to allow for the monitoring of the distribution.**

## **VI. Establishment of branches outside the Union by registered credit rating agencies under art. 14(3) of the CRA Regulation**

16. Since branches do not have a separate legal personality from their parent, credit ratings issued in branches established outside the Union are deemed to be issued by their EU parent. Therefore, infringements by the branches of the CRA Regulation are attributable to the parent CRA which shall be the object of ESMA's supervisory measures, imposition of fines and/or periodic penalty payments.
17. ESMA might be prevented from performing its supervisory tasks if important operational functions of credit rating agencies were based and primarily operated outside the Union. Moreover, CRAs should demonstrate that there is an objective reason for credit ratings to be issued in branches set up outside the Union. For instance, the need to ensure an adequate presence in the third country in question. ESMA would take action according to Article 24, 36a, 36b in case of infringements by CRAs of Annex III part II points 2, 4, 5, 6, 7 and 8 of the CRA Regulation.
18. Important operational functions, as set out in Art. 9 of the CRA Regulation, should not be based or primarily operated in offices established in third-countries with no (or very limited) involvement of EU-based managers, systems or procedures of the credit rating agency. Important operational

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<sup>3</sup> Credit rating agencies and financial market participants providing private credit ratings produced pursuant to an individual order and provided exclusively to the person who placed the order and which are not intended for public disclosure or distribution by subscription.

functions include units or divisions in charge of elaboration and issuance of credit ratings, credit analysis, rating methodology development and review, compliance, internal quality control, data storage/record keeping and systems maintenance or support. However, the identification of important operational functions may require case-by-case consideration. As regards the compliance function, CRAs should ensure that their internal control system is fully operational also in third-country branches.

19. Credit rating agencies shall not establish branches in third countries to perform activities that are subject to supervision by ESMA if this prevents ESMA from conducting supervisory tasks in relation to such activities of those branches as set out in articles 23b to 23d of the Regulation, including the ability to carry out on-site inspections and investigations. In this respect:
  - a) credit rating agencies should cooperate with ESMA in case of inspections or investigations, including on-site visits, regarding credit ratings or credit rating activities carried out in non-EU branches;
  - b) ESMA will assess the need to enter into cooperation arrangements with the local competent regulators to ensure the adequate supervision of branches located outside the Union;
  - c) prior to establishing branches in third countries, credit rating agencies should ensure that those branches will abide immediately with any request set forth by the officials of ESMA in the exercise of powers pursuant to Articles 23b to 23d of the CRA Regulation, including granting of access to premises, systems and resources in case of on-site inspections and investigations.

## **VII. Specific disclosure recommendations for best practice relating to Art. 16 (1) of ESMA Regulation**

20. ESMA recommends as a best practice that credit scoring firms and CRAs that distribute credit scores to the public in the Union should provide clear and prominent disclosure that those scores are not credit ratings issued in accordance with the CRA Regulation. ESMA recommends that this disclosure should be provided also by export credit agencies that act under Article 2(2)(c) of the Regulation.
21. ESMA recommends as a best practice that where credit scoring firms and export credit agencies decide to publish such information, they should retain full responsibility for the disclosure indicated in the previous paragraphs when their credit scores or ratings are distributed to the public in the territory of the Union via agreement with third parties.
22. Credit scores or ratings are distributed to the public in the EU when they are disclosed to an undetermined or undeterminable generality of individuals domiciled in the EU for instance, through a press release. Credit scores or ratings are also distributed to the public when they are issued through a website registered with a domain corresponding to one of the Member States of the EU.

## **VIII. Enforcement of the rules concerning the scope of the CRA Regulation**

23. ESMA shall impose periodic penalty payments in order to compel the credit rating agency to put an end to the infringement of issuing credit ratings without being registered by ESMA, and impose



fines where appropriate, in accordance respectively with Articles 36(b) and 36(a) of the CRA Regulation.

24. Where a NCA or a SCA receives an application, request for information, or any other form of inquiry concerning the CRA Regulation, including on registration or certification, the Authority should immediately notify ESMA and refer the financial market participant that has submitted the request to ESMA as the sole competent supervisory authority in the Union.

## Annex II Cost Benefit Analysis

### I. Introduction

41. ESMA has decided to conduct a Cost Benefit Analysis (CBA) in relation to the review of the Guidelines on the Scope of the CRA Regulation.
42. The nature of the CBA is inherently qualitative, as ESMA is not able to quantify a monetary value for benefits or costs of the envisaged technical options at this stage.
43. Innovation considerations have been included in the analysis, in particular the market developments around the use and dissemination of private credit ratings from the time of the last guidance issued by ESMA. The proportionality of ESMA's proposed measures to address risks to investor protection, orderly markets and financial stability has also been taken into account. Environmental, social and governance related factors, in turn, were deemed not to be relevant in this context and have not been considered.

<b>Policy Objective</b>	Clarifying ESMA's guidance on the Scope of the CRA Regulation in relation to private credit ratings.
Option 1	No change. Market participants continue to rely on the existing guidance for private credit ratings provided by the 2013 Guidelines.
Option 2	Provide targeted update to the existing guidance on private credit ratings provided by the 2013 Guidelines.
Option 3	Provide standalone guidance on private credit ratings issued through a new ESMA Q&A on the topic.
Preferred Option	Option 2. Delivery of a targeted update to the 2013 Guidelines gives ESMA an opportunity to refine the formulation in the current guidance and receive feedback from relevant stakeholders through a public consultation.

### II. Clarifying ESMA's guidance on the Scope of the CRA Regulation in relation to private credit ratings

<b>Option 1</b>	<b>No Change.</b>
Benefits	No change to existing guidance would maintain the status quo and contribute to the continuity of ESMA's position on private credit ratings.
Costs to regulator	This baseline scenario would mean that elevated level of supervisory resources would continue to be required for perimeter monitoring activities. This is due to the level of bilateral engagement that is needed to communicate ESMA's current expectations on private credit ratings. For instance, to address market queries or remedy concerns around the provision of private credit ratings. Moreover, the unclarity around the current regulatory provisions make it more challenging for ESMA to act when confronted with borderline scenarios vis-à-vis the perimeter of CRAR.

Compliance costs – IT – Training Staff	For providers and distributors of private credit ratings, the current approach poses problems to the consistent transposition of the relevant regulatory provisions in market participants' policies and procedures. For example, an element of subjective assessment is currently required to judge what is meant by the guidance as "a limited number of third parties".
Other costs	For investors, issuers and other users of private credit ratings would remain unclear about the existing ESMA guidance relating to the definition of private credit ratings.
Innovation-related aspects	The existing ESMA guidance, published in 2013, is 9 years old and does not take into account certain market developments, notably the growing use of private credit ratings within private placement markets.

<b>Option 2</b>	<b>Targeted Revision of the 2013 Guidelines.</b>
Benefits	ESMA foresees that the update to the 2013 Guidelines will benefit EU registered CRAs, entities producing non-CRA private credit ratings and issuers and investors who request private credit ratings. It is foreseen this will be achieved by providing greater clarity on the elements set out in Article 2(2)(a) of the CRA Regulation and paragraphs 14 and 15 of the 2013 Guidelines.
Costs to regulator	Issuing new guidance through an update to the 2013 Guidelines would entail dedicating resources to the development of this guidance. In addition it will require resources to ensure the new guidance is appropriately communicated to market participants and that it is incorporated in ESMA's internal procedures and ongoing supervisory activities.
Compliance costs – IT – Training Staff	The costs anticipated for EU registered CRAs and entities producing private credit ratings are: 1) those related to creating or updating internal policies and procedures relating to private credit ratings to reflect the revised Guidelines, and ensuring that relevant staff are provided with the necessary training; and 2) those related to the implementation or strengthening of controls to monitor the dissemination of private credit ratings to third parties. However, it is important to note that the means through which this is done (e.g. the roll-out of IT tools) has deliberately not been foreseen by ESMA. As such, firms have a degree of discretion on the choice of the adequate controls to implement.
Innovation-related aspects	Issuing new guidance would provide ESMA with an opportunity to reflect more recent market developments pertaining to the use and distribution of private credit ratings.
Proportionality-related aspects	Issuing updated Guidelines will provide entities producing private ratings, issuers, investors and other financial market participants with an opportunity to give ESMA input on the proportionality of its proposed measures.

	<p>ESMA foresees that established incumbents in the market for private credit rating products, such as EU-registered CRAs, will have more established policies and procedures in this area than non-CRA ratings producing entities. As such, new ESMA guidance may require a greater effort to adapt and place a burden on the latter. Similarly, it is foreseen that smaller entities producing private credit ratings may also be more affected than larger ones, given the lower number of resources and IT capabilities that are available to them.</p> <p>Finally, given the importance of private credit ratings to private placements, which can be relevant for SME financing, ESMA has ensured that its guidance is not overly prescriptive and remains proportionate to the required level of investor protection.</p>
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<b>Option 3</b>	<b>Standalone Q&amp;A.</b>
Benefits	<p>Development of an ESMA Q&amp;A is less resource-intensive to ESMA and industry than guidelines. Does not require a consultation paper, and allows for a swifter process of delivering guidance to the industry.</p> <p>Delivery of improved guidance on ESMA's expectations will benefit EU registered CRAs, entities producing private credit ratings and issuers and investors who request private credit ratings. This will be achieved by providing greater clarity on the elements set out in Article 2(2)(a) of the CRAR and paragraphs 14 and 15 of the Guidelines on the Scope of the CRA Regulation.</p>
Costs to regulator	Lack of public consultation involved in the delivery of a Q&A does not allow ESMA to receive industry feedback through an open public consultation prior to delivering guidance. This creates a risk that the Q&A is not sufficiently tailored to market reality.
Compliance costs - IT - Training Staff	Swifter delivery of the Q&A has the knock on effect that entities have limited lead in time to update their policies and procedures. The lack of a public consultation also removes the possibility of providing feedback.
Other costs	Issuing guidance through an ESMA Q&A would represent a lost opportunity for investors and users of private credit rating to provide their views through a response to a public consultation.
Innovation-related aspects	Revised guidance in the form of an ESMA Q&A would still allow for more recent market developments to be reflected, but to a lesser extent than under Option 2.
Proportionality-related aspects	Issuing guidance through an ESMA Q&A will result in a missed opportunity for ESMA to receive industry feedback on the proportionality of the guidance.

	<p>ESMA foresees that established incumbents in the market for private credit rating products, such as EU-registered CRAs, will have more established policies and procedures in this area than non-CRA ratings producing entities. As such, new ESMA guidance may require a greater effort to adapt and place a burden on the latter. Similarly, it is foreseen that smaller entities producing private credit ratings may also be more affected than larger ones, given the lower number of resources and IT capabilities that are available to them.</p> <p>Finally, given the importance of private credit ratings to private placements, which can be relevant for SME financing, ESMA has ensured that its guidance is not overly prescriptive and remains proportionate to the required level of investor protection.</p>
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