Association for
Financial Professionals®

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Good morning, Chairman Shelby, Ranking Member Sarbanes, and members of the Committee. I am Jim Kaitz, President and CEO of the Association for Financial Professionals. AFP welcomes the opportunity to participate in today's hearing on the role of credit rating agencies in the capital markets.

The Association for Financial Professionals (AFP) represents more than 14,000 finance and treasury professionals representing more than 5,000 organizations. Organizations represented by our members are drawn generally from the Fortune 1000 and the largest of the middle-market companies from a wide variety of industries. Many of our members are responsible for issuing short- and long-term debt and managing corporate cash and pension assets for their organizations. In these capacities, our members are significant users of the information provided by credit rating agencies. Acting as both issuers of debt and investors, our members have a balanced view of the credit rating process, and have a significant stake in the outcome of the examination of rating agency practices and their regulation.

AFP believes that the credit rating agencies and investor confidence in the ratings they issue are vital to the efficient operation of global capital markets. Before outlining the consequences of inaction, it is useful to provide some background on how we got to where we are today and summarize AFP's research on this important issue.

BACKGROUND

For nearly 100 years, rating agencies have been providing opinions on the creditworthiness of issuers of debt to assist investors. The Securities and Exchange Commission (SEC) and banking regulators also rely on ratings from rating agencies. In 1975, the SEC recognized Moody's, Standard & Poor's, and Fitch, the three major rating agencies in existence at that time, as the first nationally recognized statistical rating organizations (NRSRO). The SEC and other regulators use the ratings from the NRSROs to determine whether certain regulated investment portfolios, including those of mutual funds, insurance companies and banks, meet established credit quality standards. As a result, companies that hope to have their debt purchased by these portfolios must have a rating from an NRSRO. From 1975 to 1992, the SEC recognized four other rating agencies, but each of these entrants consequently merged with Fitch. The SEC did not recognize any new agencies from 1992 until April 2003, when Dominion Bond Rating Service received recognition from the SEC, becoming the fourth NRSRO.

Some market participants have argued that the NRSROs did not adequately warn investors of the impending failure of Enron, WorldCom, Parmalat, and other companies. For example, in 2001, the rating agencies continued to rate the debt of Enron as "investment grade" days before the company filed for bankruptcy. These failures occurred despite the fact that credit rating agencies (CRAs) have access to non-public information because of their exemption from Regulation Fair Disclosure (Reg FD). As a result of the corporate scandals of 2001, Congress, in the Sarbanes-Oxley Act required the Securities and Exchange Commission (SEC) to conduct a study on credit rating agencies examining the role of rating agencies in evaluating debt issuers, the importance of that role to investors and any impediments to accurate appraisal by credit rating agencies. Sarbanes-Oxley also required the study to determine whether there are any barriers to entry into the credit rating market and whether there are conflicts of interest that hinder the performance of the rating agencies.

In January 2003, the SEC released the Sarbanes-Oxley required study, which identified five major issues that the SEC stated it would examine further: information flow, potential conflicts of interest, alleged anti-competitive or unfair practices, reducing potential barriers to entry and ongoing oversight. Following the study, the SEC issued, for public comment, a concept release exploring these issues on June 4, 2003. As of this hearing, the SEC has not issued any proposed rules.

In September 2002, AFP surveyed senior level corporate practitioners and financial industry service providers on their views regarding the quality of the NRSROs' ratings, the role the SEC should take in regulating the agencies, and the impact additional competition may have on the marketplace for ratings information. In that survey, many financial professionals indicated that the ratings generated by the NRSROs were neither accurate nor timely.

In September 2004, AFP once again surveyed senior level financial professionals regarding the accuracy and timeliness of the NRSROs' analyses and on the potential role regulators may have in promoting competition among credit rating agencies[1].

Key findings of the 2004 AFP Rating Agency Survey include:

- Eighty-seven percent of responding organizations with debt indicate that credit providers require them to obtain and maintain a rating from at least one of the four NRSROs.
- Many financial professionals believe that the ratings of their organizations are either inaccurate or are not updated on a timely basis.
- A third of corporate practitioners believe the ratings on their organization's debt are inaccurate.
- Fifty-two percent of financial professionals indicate that the cost of credit ratings has increased by at least 11 percent over the past three years, including 19 percent that indicate that costs have increased at least 25 percent over that time period.
- While many responding organizations are confident in the accuracy of the ratings they use for investments, they are less confident in the timeliness of the same ratings.
- Financial professionals believe the Securities and Exchange Commission (SEC) should take a greater role in overseeing the credit rating agencies along with encouraging greater competition in the field.

Recently, other organizations have taken steps to address credit rating agency reform issues. The International Organization of Securities Commissions (IOSCO) in September 2003 issued a Statement of Principles regarding the manner in which rating agency activities are conducted. In December 2004, IOSCO released Code of Conduct Fundamentals for Credit Rating Agencies.

In July 2004, the Committee of European Securities Regulators (CESR), at the request of the European Commission, issued a call for evidence on possible measures concerning credit rating agencies. The Committee intends to approve and publish its final advice to the European Commission in March 2005.

[1] For complete copies of both survey results visit the AFP Website at www.AFPOnline.org.

CONSEQUENCES OF INACTION

Why is reforming the credit rating system so important? Along with the SEC and other regulators that have incorporated the NRSRO designation into their rules, institutional and individual investors have long relied on credit ratings when purchasing individual corporate and municipal bonds. Further, nearly every mutual fund manager that individuals and institutional investors have entrusted with over $8 trillion relies to some degree on the ratings of nationally recognized agencies. Rating actions on corporate debt also have an indirect but sizeable impact on the stock prices of rated companies.

Debt issuers rely on the credit rating agencies to understand the company's finances, strategic plans, competitive environment and any other relevant information about the company in order to issue ratings that accurately reflect the company's creditworthiness. These ratings determine the conditions under which a company can raise capital to maintain and grow their business. Credit ratings also allow others that deal with the issuer to make an informed assessment of the issuer as a potential trading partner, and are a valuable part of the issuer's external communications with the market.

While credit rating agencies have long played a significant role in the operation of capital markets, the Administration's recent single-employer pension reform proposal would further increase the importance of the NRSROs and their impact on Americans. The proposal would tie pension funding and Pension Benefit Guaranty Corporation (PBGC) premiums to a plan sponsor's financial condition as determined by existing credit ratings. In some cases, plan sponsors would be prohibited from increasing benefits or making lump sum payments based on their credit rating and funded status. Such a proposal would further codify the NRSRO designation and even further empower the rating agencies.

Despite the increasing reliance on credit ratings, even after more than ten years of examining the role and regulation of credit rating agencies, the Securities and Exchange Commission has not has not taken any meaningful action to address the concerns of issuers and investors. These concerns include questions about the credibility and reliability of credit ratings and conflicts of interest and abusive practices in the rating process. Chairman Shelby and members of the Committee, these issues are far too important for the SEC to remain silent while the world waits for it to take action.

As I noted earlier, the credit rating agencies and investor confidence in the ratings they issue are vital to the operation of global capital markets. As evidenced in AFP's research, confidence in rating agencies and their ratings has diminished over the past few years. Addressing issues such as the lack of a defined process by which an agency can become an NRSRO, eliminating potential conflicts of interest, and effective marketplace competition will begin to restore the much-needed confidence in the credit ratings system.

When the SEC recognized the first nationally recognized statistical rating organization (NRSRO) in 1975 without enumerating the criteria by which others could be recognized, it created an artificial barrier to entry to the credit ratings market. This barrier has led to a concentration of market power with the recognized rating agencies and a lack of competition and innovation in the credit ratings market. Only the SEC can remove the artificial barrier to competition it has created. Therefore, AFP strongly recommends that the SEC maintain the NRSRO designation and clearly articulate the process by which qualified credit rating agencies can attain the NRSRO designation.

Not only has the SEC bestowed a significant competitive advantage, it has failed to exercise any meaningful oversight of the recognized agencies. In nearly thirty years since creating the NRSRO designation, there has been no review of the ongoing credibility and reliability of the ratings issued by the NRSROs. The SEC must improve its ongoing oversight of the rating agencies to ensure that they continue to merit NRSRO status.

The SEC further empowered the rating agencies when it exempted them from Regulation Fair Disclosure (FD). Through this exemption, the rating agencies have access to non-public information about the companies they rate. Again, the Commission has done nothing to ensure that those who are granted this powerful exemption do not use the non-public information inappropriately. The SEC must require that NRSROs have policies in place to protect this valuable and privileged information. Again, this should be part of the SEC's ongoing oversight of the rating agencies.

As highlighted in recent media reports, rating agencies continue to promulgate unsolicited ratings of debt issuers. Because unsolicited ratings are issued without the benefit of access to company management or non-public information about the issuer, the resulting ratings are often not an accurate reflection of an organization's financials condition. Credit ratings are critical to an organization's ability to issue debt and issuers often feel compelled to participate in the rating process and pay for the rating that was never solicited. The potential for abuse of these unsolicited ratings by the rating agencies must be addressed by the SEC.

Finally, an NRSRO is also in a position to compel companies to purchase ancillary services. These ancillary services include ratings evaluations and corporate governance reviews. Further, the revenue derived from these services has the potential to taint the objectivity of the ratings. You need look no further than the equity research and audit professions to understand why these potential abusive practices and conflicts of interest must be addressed by the SEC.

RECOMMENDATIONS

To address many of the questions raised by the SEC and market participants, the Association for Financial Professionals, along with treasury associations from the United Kingdom and France, released a Code of Standard Practices for Participants in the Credit Rating Process.

A copy of the Code is attached to my testimony. Importantly, the Code contains recommendations for regulators, as well as rating agencies and issuers. To be clear, the Code is a private sector response intended to complement rather than replace regulation

Earlier in my testimony, I touched upon many of the regulatory recommendations contained in the Code. I'd like to take this opportunity to provide more detailed regulatory recommendations. Specifically, we recommend establishing transparent recognition criteria based on whether a credit rating agency can consistently produce credible and reliable ratings over the long-term. Establishing clearly defined recognition criteria is a crucial step to removing barriers to entry and enhancing competition in the credit ratings market.

In the Code, we also urge regulators to require that rating agencies document internal controls that protect against conflicts of interest and anti-competitive and abusive practices, and ensure against the inappropriate use of non-public information to which the rating agencies are privy because of their exemption from Regulation FD. Regulatory recommendations also include improving ongoing oversight of approved rating agencies to ensure that NRSROs continue to meet the recognition criteria.

For rating agencies, the Code includes suggestions to improve the transparency of the rating process, protect non-public information provided by issuers, protect against conflicts of interest, address the issue of unsolicited ratings, and improve communication with issuers and other market participants.

Finally, recognizing that the credibility and reliability of credit ratings is heavily dependent on issuers providing accurate and adequate information to the rating agencies, the Code of Standard Practices outlines issuer obligations in the credit rating process. These obligations are intended to improve the quality of the information available to the rating agencies during the initial rating process and on an ongoing basis, and to ensure that issuers respond appropriately to communications received from rating agencies.

A reasonable regulatory framework that minimizes barriers to entry and is flexible enough to allow innovation and creativity will foster competition among existing NRSROs and those that may later be recognized and restore investor confidence in the rating agencies and global capital markets. Rather than excessively prescriptive regulatory regimes, innovation and private sector solutions, such as AFP's Code of Standard Practices, are the appropriate responses to many of the questions that have been raised about credit ratings.

Restoring issuer and investor confidence in the credit ratings process is critical to global capital markets. Chairman Shelby and members of the Committee, we strongly recommend that you hold the SEC accountable by demanding immediate action on the issues that have been raised here today. If the SEC does not act immediately to aggressively address each of the concerns we have outlined, we urge you act to restore investor confidence in the credit ratings process through action by this Committee. We commend you, Mr. Chairman, and the Committee for recognizing the importance of this issue to investors and global capital markets and hope that this hearing will compel the SEC to act.

Code of Standard Practices for Participants in the Credit Rating Process

Association of Corporate Treasurers (United Kingdom)

Association for Financial Professionals (United States)

Association Francaise Des Tresoriers D'Entreprise (France)

With the Support of the International Group of Treasury Associations and Euro Associations of Corporate Treasurers:

This Code of Standard Practices for Participants in the Credit Rating Process has been developed by The Association of Corporate Treasurers (ACT), London, England, The Association for Financial Professionals (AFP), United States, Association Française Des Trésoriers D'Entreprise (AFTE), Paris, France.

Executive Summary

Background

Credit rating agencies (CRAs) play an important role in the efficient operation of the global capital markets. Investors and lenders rely on CRAs to provide a clear measure of the creditworthiness of debt issuers and borrowers, while debt issuers rely on CRAs to issue ratings that accurately reflect the company's relative creditworthiness. Companies also use credit ratings to evaluate trading partners, financial counterparties, and potential business partners; and in many jurisdictions, regulators also rely on CRAs for determining regulatory capital requirements and permitted investments. Yet for the credit rating process to work properly, a critical nexus of transparency and trust must be exhibited by all of these parties – the issuers, the credit rating agencies, and the regulators who oversee both.

During the past two years, however, CRAs, and the credit rating process itself, have been the subject of significant criticism. CRAs have come under fire for failing to warn investors of the dangers and ultimately disastrous collapse of large global companies, including, for example, Parmalat, Enron, and WorldCom. These events have led some to question whether the CRAs are meeting the needs of market participants.

Some have asserted that regulators should take a larger role in regulating the CRAs and should encourage competition in the market for credit ratings. Yet both credit rating agencies and government regulators have been slow to respond to the call for reform. For example, while the U.S. Securities and Exchange Commission (SEC) issued its first concept release a decade ago and a new concept release in June 2003 on rating agencies and the use of credit ratings under U.S. Federal securities laws, it has yet to take any definitive action. Regulators in Europe are in the process of addressing the issue as well. Meanwhile, IOSCO has published its Code of Conduct Fundamentals for Credit Rating Agencies[1]

As a result of the continuing concerns over the credit rating process, a series of initiatives arose independently. In response to the SEC's June 2003 concept release, the Association for Financial Professionals (AFP) in the U.S. and the Association of Corporate Treasurers (ACT) in the United Kingdom called for improved regulation, improved internal controls and an industry code of practice for all those involved in the credit rating process. At the same time the Association Francaise Des Tresoriers D'Entreprise (AFTE) developed and shared a best practices guide that it had used in conversations with the CRAs and relevant authorities. Recognizing the various efforts and in light of the global need to restore confidence to the credit rating process, it was agreed in

[1] http://www.iosco.org/pubdocs/pdf/IOSCOPD180.pdf

September 2003 in Slovakia at the meeting of the International Group of Treasury Associations that AFP, ACT and AFTE would bring forward a single global proposal for improving rating industry practice.

The Code of Standard Practices for Participants in the Credit Rating Process

AFP, ACT and AFTE are jointly releasing this Code of Standard Practices for Participants in the Credit Rating Process. The final Code of Standard Practices follows an Exposure Draft that was issued in April 2004 to solicit comment from the widest number of those involved with credit ratings, including issuers, users, CRAs, regulators, and others with a professional interest in credit ratings. The Associations, along with the International Group of Treasury Associations (IGTA) and Euro Associations of Corporate Treasurers (EACT), believe that this Code of Standard Practices, coupled with a minimum regulatory framework, is the most efficient and flexible solution to restoring confidence in credit rating agencies and the information they provide to global capital markets.

These Associations are the leading corporate finance organizations in their respective countries, representing nearly 19,000 treasury and finance professionals from many of the largest companies in the world. Treasury and finance professionals rely on the CRAs when their companies issue debt and when they make investment decisions. Their relationship with the CRAs provides them with a unique view on both the strengths and weaknesses of the agencies' practices.

The Code includes three sections: regulatory recommendations, rating agency code of standard practices, and issuer code of standard practices.

For CRAs, the Code includes recommendations to improve the transparency of the rating process, protect non-public information that is provided to CRAs, protect against conflicts of interest, address the issue of unsolicited ratings, and improve communication with issuers and other market participants.

Regulatory recommendations focus on the credibility and reliability of ratings, transparency in the rating agency recognition process and improving ongoing regulatory oversight of approved rating agencies. Regulatory recommendations also include removing barriers to competition in the credit rating agency marketplace.

Finally, recognizing that the credibility and reliability of credit ratings is heavily dependent on issuers providing accurate and adequate information to the CRAs, the Issuer Code of Standard Practices outlines issuer obligations in the credit rating process. These obligations are intended to improve the quality of the information available to the CRAs during the initial rating process and on an ongoing basis, and to ensure that issuers respond appropriately to communications received from CRAs.

This Code of Standard Practices is an important, collaborative, and global private-sector response to many of the issues that have been raised about the credit rating process and the agencies themselves. While certain of the points below would usefully be incorporated into regulation in a jurisdiction where CRAs are regulated, the majority are better incorporated into codes of standard practices developed by individual rating agencies and issuers In jurisdictions where CRAs are regulated, the Code is intended to serve as a complement to, rather than a substitute for, government regulation.

The Associations welcome comments and suggestions on the Code of Standard Practices. Comments and suggestions should be directed to any or all of the following:

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Code of Standard Practices for Participants in the Credit Rating Process

Introduction

Credit rating agencies (CRAs) play an important role in the efficient operation of global capital markets. In addition to any credit analysis done internally, investors depend on the CRAs to analyze all public information and any non-public information the agency has gathered about a company to form a meaningful assessment of the creditworthiness of the company. These ratings, which are commonly paid for by the issuers, are used by individuals, professional investment managers, and corporate finance professionals when selecting securities for themselves or their organizations and by financial institutions when determining whether to lend to a prospective borrower and, if so, at what terms. CRAs also play an important role for companies when evaluating counterparties for financial transactions, in evaluating actual or potential suppliers or customers for non-financial goods and services, and in similarly evaluating partners, collaborators, or joint venture prospects.

Debt issuers expect the CRAs to understand the company's finances, strategic plans, competitive environment and any other relevant information about the company in order to issue ratings that:

- allow the company to place securities at terms that are reflective of its relative creditworthiness;
- allow others that deal with the issuer to make an informed assessment of the issuer as a potential trading partner; and
- are a valuable part of the issuer's external communications with the market.

In many jurisdictions, ratings are also used to determine regulatory capital requirements and permitted investments.

In November 2002, the Association for Financial Professionals (AFP) released its "Rating Agencies Survey: Accuracy, Timeliness, and Regulation[2]." AFP's survey, which received over 700 responses, found that a significant minority of treasury and finance professionals from companies with rated debt believe that their company's credit ratings are neither accurate nor timely. Respondents believe that their company's ratings are more reflective of the industry in which it operates rather than of the company's financial condition[3]. Those responsible for investing or lending money on their organization's behalf also reported a lack of

[2] http://www.afponline.org/pub/pdf/ratings_survey.pdf
[3] The Associations recognize that credit ratings are developed through a combination of quantitative and qualitative factors, not solely the reported or proforma financial statements of an issuer.

confidence in the accuracy and timeliness of the ratings of the companies in which they invest or to whom they extend credit.

Efforts to improve investor and issuer confidence in the CRAs have been proceeding on multiple fronts. In the United States, the effort has focused primarily on the way in which the Securities and Exchange Commission (SEC) regulates the CRAs that it recognizes as nationally recognized statistical rating organizations (NRSRO). AFP submitted a comment letter in response to an SEC Concept Release, "Rating Agencies and the Use of Credit Ratings under the Federal Securities Laws[4]." In the comment letter[5], AFP called on the SEC to remove artificial barriers to entry into the credit ratings market. AFP also recommended that the SEC periodically review each CRA it recognizes in order to ensure that they continue to be issuers of credible and reliable ratings and have in place effective internal controls. AFP commented that the SEC should minimize further regulation and allow market forces to determine acceptable standards for many practices.

In the United Kingdom, the Association of Corporate Treasurers (ACT) in its response[6] to the SEC Concept Release espoused the concept of an industry code of practice as a key factor in CRA regulation and conduct of business. Neither the United Kingdom's Financial Services Authority nor the European Union grants a regulatory imprimatur that parallels the NRSRO designation in the United States. However, the regulation of CRAs by the United States Securities and Exchange Commission affects the practices of the CRAs in the United Kingdom and other jurisdictions, and thus concerns issuers and investors in the UK. The ACT believes that a robust code of conduct to which issuers, investors and CRAs can provide input would serve to underpin regulation, to minimize the need for regulation and help to avoid fragmentation arising from differences in national and regional regulatory regimes.

In March 2003, the French Association of Corporate Treasurers (AFTE) developed and shared with the European Association of Corporate Treasurers (EACT)[7] a best practices guide that it has used in conversations with the CRAs and relevant authorities. The AFTE met with each of the three CRAs in Paris to discuss ways in which it might contribute to improving the relations between CRAs, issuers, and the market. In addition to developing best practices for CRAs, the AFTE has also begun a dialogue to identify the responsibilities of issuers to the agencies in recognition of the important role that the issuers play in the process.

While the tactics of each of these associations have been different, the goal of the three is quite similar. Each is seeking to improve the relationship between

[4] http://www.sec.gov/rules/concept/33-8236.htm
[5] http://www.afponline.org/pub/pdf/clkatz072803.pdf
[6] http://www.treasurers.org/technical/papers/resources/actcommentssec.pdf
[7] The EACT brings together the national treasury associations of the Euro currency zone.

issuers and the CRAs, improve the quality of the ratings they promulgate, and restore investor confidence in global capital markets.

At its meeting in September 2003 in Slovakia, the International Group of Treasury Associations (which brings together the treasury associations of 26 countries) asked the AFP, ACT and AFTE to bring forward proposals for improving rating industry practice. This paper puts forth a recommendation that reflects the common elements of the stances of the three associations.

We hope that this paper will be a contribution to the development of industry practice. While certain of the points below would usefully be incorporated into regulation in a jurisdiction where CRAs are regulated, the majority are better incorporated into codes of standard practices developed by individual rating agencies and issuers. Such a code of standard practices should, however, incorporate the substance of all the points given that some jurisdictions do not regulate CRAs. CRAs should publish their codes of standard practice to demonstrate to investors, issuers, and regulators that they have adopted the recommendations. The CRA's code of standard practices could also be a recital in rating agency contracts with issuers or a representation to issuers precedent to the contracts.

We note the publication by the International Organization of Securities Commissions (IOSCO) of principles for the regulation of rating agencies[8] and generally support those principles. We believe that regulation should only provide a minimal fail-safe framework for CRA regulation and that the more flexible and adaptable industry code of standard practices must play a complementary role to such regulation.

The associations also commented[9] on and generally support IOSCO's *Code of Conduct Fundamentals for Credit Rating Agencies*[10], which were issued in draft form in October 2004 and finalized in December 2004. The Associations welcome IOSCO's effort and found the Code Fundamentals broadly consistent with the Associations' Code of Standard Practices. However, IOSCO notes that it has focused primarily on the integrity of the rating process:

> "While aspects of the Code Fundamentals deal with a CRA's duties to issuers, the essential purpose of the Code Fundamentals is to promote investor protection by safeguarding the integrity of the rating process. The Code Fundamentals do not address the equally important obligations issuers have of cooperating with and providing accurate and complete information to the marketplace and the CRAs they solicit to provide ratings. While aspects of the Code Fundamentals deal with a CRA's duties

8 http://www.iosco.org/news/pdf/IOSCONEWS59.pdf
9 http://www.afponline.org/pub/pdf/cl_20041207_IOSCO.pdf
10 http://www.iosco.org/pubdocs/pdf/IOSCOPD180.pdf

> to issuers, the essential purpose of the Code Fundamentals is to promote investor protection by safeguarding the integrity of the rating process."

The Associations believe that their Code of Standard Practices addresses many of the broader issues that were not addressed by IOSCO. Along with the International Group of Treasury Associations (IGTA) and Euro Associations of Corporate Treasurers (EACT), the Associations believe that this Code of Standard Practices for Participants, coupled with a minimum regulatory framework and the IOSCO Code Fundamentals, is the most efficient and flexible solution to restoring confidence in credit rating agencies and the information they provide to global capital markets.

The Associations urge all participants in the industry to adopt the provisions of the Code of Standard Practices. They urge issuers with solicited credit ratings to encourage the CRAs they deal with to incorporate the Code's provisions in their own practice. They urge CRAs to indicate to issuers with solicited ratings that they expect the issuers to observe the Code's issuer recommendations. Users of ratings are also urged to indicate to issuers and CRAs that they look at adherence to the Code of Standard Practices as a minimum expectation of those they invest in or rely on for rating information.

The Associations hope that the Code of Standard Practices for Participants in the Credit Ratings Process and IOSCO's Code of Conduct Fundamentals will be embraced by market participants and make a meaningful contribution to resolving issues raised about the credit ratings process.

Code of Standard Practices for Participants in the Credit Rating Process

Regulatory Recommendations

1. In jurisdictions where regulators grant recognition or approval to CRAs, the regulators should strive to eliminate unnecessary regulatory burdens and barriers to entry.

1.1. Regulators should establish and clearly communicate specific criteria that CRAs must meet in order to be recognized or approved. These criteria, along with documented processes and procedures, will eliminate unnecessary regulatory barriers to entry into the ratings market and may stimulate new competition.

1.2. The criteria that CRAs must meet to receive regulatory approval should be based on whether the agency can consistently produce credible and reliable ratings over the long-term, not on methodology. The determination of whether ratings are credible and reliable may be based on market acceptance, quantitative analysis, or other methods developed by relevant regulators.

1.3. The criteria for recognition should also require a CRA seeking regulatory approval to document its internal controls designed to protect against conflicts of interest and anti-competitive and abusive practices and to ensure against the inappropriate use of all non-public information to which rating agencies are privy.

1.4. Regulators should periodically review each recognized CRA to ensure that it continues to meet the recognition criteria.

1.5. It is unlikely, at least in the short-run, that a newly-recognized CRA could displace an established CRA or make it practical for an issuer to not receive a rating from one of the established CRAs. However, with additional competition or even the threat of additional competition resulting from the removal of barriers to entry, regulators should allow market forces to determine the appropriate frequency of rating reviews, acceptable methodologies, appropriate staffing levels and qualifications, and other points about which there is no wide agreement.

1.6. Regulators should not prescribe methodologies that CRAs may use, but require that each CRA document and adhere to its chosen, published methodologies, while recognizing that many judgements are involved in arriving at ratings other than purely statistical ratings.

1.7. Because of their access to non-public information, regulators should require CRAs to document and implement policies and procedures to prevent the disclosure of non-public information to outside parties that might benefit from this information.

1.8. In cases where a CRA is a parent, subsidiary or affiliate of a publisher or other organization that might benefit from non-public information, regulators should require that the CRA document strong firewalls that prevent the use of this information by these affiliated businesses.

1.9. Regulators should not stipulate a frequency (e.g., annually, semi-annually) with which CRAs must update ratings, but require agencies to disclose the date of the last formal review and when they last updated each rating.

Rating Agency Code of Standard Practices

2. Credit rating agencies should take steps to enhance the transparency of the rating process.

2.1. Each CRA should widely publicize its methodologies for both short-term and long-term ratings on a periodic basis and prior to any changes in such methodologies.

2.2. While recognizing that all credit ratings, apart from purely statistical ratings, involve matters of judgement, a CRA should document and adhere to its published methodologies.

2.3. Each CRA should widely publicize any changes in its methodologies prior to the release of any rating announcement that might be the consequence of these changes.

2.4. Each CRA should publish the definition and historical default rates of each rating symbol it uses.

2.5. Each CRA should provide a guide to the methodology applicable to each company it rates prior to the assignment of a rating and preceding the implementation of any changes to the methodology.

2.6. Each CRA should provide a guide to its appeals process, if any, applicable to each company it rates prior to the assignment of a rating and preceding the implementation of any changes to the appeals process.

2.7. CRAs should make available information on the qualifications and experience of the analyst assigned to a company, as well as the sector(s) and other companies this analyst covers. This information should be updated from time to time as necessary.

3. Confidential information gathered by CRAs during the development of ratings should be protected and not otherwise be publicly disseminated.

3.1. Because of their access to non-public information, CRAs should document and implement policies and procedures to prevent the disclosure of non-public information to outside parties that might benefit from this information.

3.2. In cases where a CRA is a parent, subsidiary or affiliate of a publisher or other organization that might benefit from non-public information, the CRA should document strong firewalls that prevent the use of this information by these affiliated businesses.

3.3. In jurisdictions where the use of non-public information is not already restricted through law or regulation, analysts and other agency staff privy to non-public information should be required, in so far as is consistent with applicable law on employment and restraint of trade, to sign a pre-employment non-disclosure agreement. This non-disclosure agreement should prohibit them from using their access to such information in future employment in securities markets or as journalists reporting or commenting on those markets such that they might benefit from this information.

4. Credit rating agencies should establish and document policies and procedures to protect against potential conflicts of interest.

4.1. CRAs should have an ownership structure that is not likely to create opportunities for conflicts of interest to arise.

4.2. There should be a distinct and absolute separation of duties between rating analysts and agency staff responsible for raising revenue from solicited ratings.

4.3. There should be a distinct and absolute separation of duties between rating analysts and staff responsible for raising revenue from rating advisory services.

4.4. Rating analyst compensation should be wholly independent of the revenue generated from issuers or any related entities for rating or any ancillary services provided by the CRA.

5. Credit rating agencies should clearly distinguish between solicited and unsolicited ratings and disclose when a rating was last updated.

5.1. CRAs should disclose whether each rating was solicited or unsolicited, and whether the issuer participated in the rating process. Whether a rating was solicited or unsolicited should be disclosed each time a rating is published.

5.2. CRAs should disclose whether a rating is based purely on statistical analysis of published information, statistical analysis of published information confirmed through conversations between a qualified analyst and the issuer, or analysis of published information and non-published information gathered during discussions between the CRA and the issuer.

5.3. CRAs should disclose when they last conducted a review with the issuer and when each rating was last updated.

6. Rating agencies should improve communication with issuers and the market.

6.1. Issuers should be given an opportunity to review the text of any rating action affecting their securities prior to public release to correct any factual errors in reported information and to remove any non-public information erroneously included in the text.

6.2. The CRA should disclose to the issuer and, in summary form, the users of ratings the key assumptions and fundamental analysis underlying the rating action, as well as any other information that materially influenced the rating action and that could influence future rating actions. Care must be taken by the CRA to avoid disclosure of any confidential non-published information received from the issuer.

6.3. Any financial figures that are materially restated from the issuer's published financial statements by CRAs and included in public releases should be fully explained to facilitate issuer and investor understanding of ratings.

6.4. As the analyst's recommendation can be called into question and overridden by members of the rating committee, CRAs should provide and communicate a methodology for issuers to provide feedback directly to the rating committee on key assumptions and fundamental analysis, as well as any other information that may have materially influenced the rating action.

6.5. CRAs should commit to completing the rating process in a timely manner in order to allow an issuer to effectively execute any scheduled debt issues or other capital markets activities that were communicated to the CRA in advance of or during the rating process.

6.6. Information provided to the CRA during the rating process and in regular meetings should be recorded by the agency, retained and made available to ratings analysts that may later be assigned to the company. As the principal rating agencies normally seek to rate through an economic cycle, records should be retained for at least that period as the agency understands it and some fundamental, structural information should be retained permanently or until it ceases to be relevant. During each formal review of an issuer, CRAs should confirm whether the information on record is still applicable or requires updating to ensure that the CRA is not rating based on outdated information.

6.7. CRAs should be expected to respond to issuer concerns about their rating in a timely and serious manner.

6.8. CRAs whose rating methodology relies upon access to management and to confidential non-public information should, as appropriate, refuse to rate, withdraw existing ratings or qualify ratings when they believe that the level, quality and completeness of access to management and information disclosed do not seem to fully satisfy their requirements and the provisions of section 7 below.

Issuer Code of Standard Practices

7. **Issuers should commit to cooperate actively with CRAs when a rating is solicited and to providing information to CRAs that will contribute to the initial and ongoing accuracy and timeliness of solicited ratings when the CRA's rating methodology involves access to management and to confidential, non-public information.**

7.1. Credit ratings and opinions are forward-looking and involve matters of judgement by the CRAs, and the credibility and reliability of these ratings and opinions are heavily dependent on an issuer's ability to provide adequate and timely information. Therefore, an issuer is responsible for providing information to CRAs that should include:

7.1.1. The issuer's business strategy;

7.1.2. The legal and management structure of the issuer and its parent company or subsidiaries, as well as its management processes;

7.1.3. The risks and opportunities of the issuer's business environment, as well as those peculiar to itself;

7.1.4. The issuer's approach to risk management and financing;

7.1.5. The issuer's financial policies;

7.1.6. Key financial data; and

7.1.7. Any other information or data that the issuer believes will help the CRAs to better understand its particular circumstances and outlook.

7.2. Issuers should provide adequate and timely information, in good faith, regarding any material change in the financial situation of the company.

7.3. Notwithstanding the requirement for full and timely communication to CRAs in 7.2, issuers should hold, at least once a year, a full review with CRAs in order to explain past performance and future prospects on a horizon relevant, in the issuer's opinion, with the nature of its business(es). In doing this, issuers should allow CRAs to access the appropriate level of management within their organization.

7.4. Issuers should inform CRAs about any corporate actions, including public debt issuances, prior to their launch. Issuers should provide

CRAs with all relevant information on these corporate actions in order to allow CRAs to issue, update or revise their opinion/rating, if any, in a timely manner.

7.5. Issuers should endeavor to address CRAs' questions and requests as quickly as possible and, in case of delayed answers, to inform CRAs accordingly.

7.6. Issuers should seek to react as quickly as practicable to communications submitted to them by a CRA prior to their public release by the CRA. While issuers should, in any case, make reasonable efforts to respond as quickly as possible, the time frame in which companies may review the text should be limited (but not less than four business hours) in order to ensure that investors receive timely information and to minimize the possibility of information leaks.

During this time, issuers should not take any pre-emptive action that would challenge or counter the release by the credit rating agency. In addition, issuers should not take advantage of the delay in the release of the rating action to the market by making any debt issuance other than the refinancing of maturing short-term debt.

About the Association of Corporate Treasurers (ACT)

Established in the UK in 1979, The ACT is a centre of excellence for professionals in corporate finance, treasury, risk, and cash management operating in the international marketplace. It has over 3,300 members from both the corporate and financial sectors and 1,500 students in more than 40 countries. Its examinations are recognized by both practitioners and bankers as the global standard setters for treasury education. The ACT promotes study and best practice in finance and treasury management. It represents the interests of non-financial sector corporations in financial markets to regulators, standards setters and trade bodies.

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About the Association for Financial Professionals

The Association for Financial Professionals (AFP) headquartered in Bethesda, Maryland, supports more than 14,000 individual members from a wide range of industries throughout all stages of their careers in various aspects of treasury and financial management. AFP is the preferred resource for financial professionals for continuing education, financial tools and publications, career development, certifications, research, representation to legislators and regulators, and the development of industry standards.

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About Association Française des Trésoriers d'Entreprise (AFTE)

Association Française des Trésoriers d'Entreprise (AFTE), founded in 1976, represents more than 1,400 members, including 1,050 Corporate Treasurers or Financial Managers of approximately 900 industrial and commercial companies; 450 members are based in the provinces. There are also 350 correspondent members. Its development is concentrated on five activities: technical committees, conferences, education, publications and representation of corporate treasurers. AFTE is a founding member of the Euro Associations of Corporate Treasurers (EACT).

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