



European Securities and
Markets Authority

Consultation Paper

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





Table of Contents

Responding to this paper	3
Legislative references, abbreviations and definitions	4
1. Executive Summary	5
2. Introduction	7
3. Scope of CRAR and Private Credit Ratings	9
4. Conclusion	14
5. Next Steps	16
Annex I Guidelines	17
Annex II Cost Benefit Analysis	23
Annex III List of Questions	27

Responding to this paper

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex III. Comments are most helpful if they:

- respond to the question stated;
- indicate the specific question to which the comment relates;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

ESMA will consider all comments received by 11 March 2022.

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

The collection of confidential responses is without prejudice to the scope of Regulation (EC) No 1049/2001. Possible requests for access to documents will be dealt in compliance with the requirements and obligations laid down in Regulation (EC) No 1049/2001.

Data protection

Information on data protection can be found at <https://www.esma.europa.eu/data-protection> under the heading Data Protection.

Who should read this paper?

This paper may be of interest to rated entities, issuers of debt instruments, users of credit ratings, credit rating agencies and entities interested in applying to be a registered CRA, as well as other financial market participants not in the scope of the CRA Regulation.

Legislative references, abbreviations and definitions

2013 Guidelines	Guidelines and Recommendations on the Scope of the CRA Regulation
CMU	Capital Markets Union
CP	Consultation Paper
CRA	Credit Rating Agency
CRA Regulation	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

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 this Consultation Paper is to propose additional guidance specifically relating to 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.

Contents

4. The proposed guidance provides additional clarification to paragraphs 14 and 15 of the 2013 Guidelines,. In particular, it addresses 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 ratings producer.



Next Steps

5. ESMA will consider the responses it receives to this CP by 11 March 2022 and expects to publish a final report by end of Q2 2022.

2. Introduction

1. As part of its supervisory activities, ESMA continuously monitors the perimeter of the CRA Regulation. Throughout this work, ESMA has identified a need to clarify the scope of the Regulation vis-à-vis the practices of certain market participants pertaining to the use and dissemination of private credit ratings.
2. In order to provide the envisaged guidance, ESMA has engaged over the past year with market authorities, CRAs, trade associations and other financial market participants to assess the current practices relating to the use of private credit ratings, particularly in the context of private placement markets. The purpose of this has been to identify possible inconsistencies in the interpretation of the different requirements of a private credit rating and to define necessary policy outcomes to address these inconsistencies.
3. Based on the feedback received, ESMA is proposing to clarify its expectations regarding the regulatory provisions "produced pursuant to an individual order" and "provided exclusively to the person who placed the order" as well as the boundaries related to the sharing of a private credit rating with "a limited number of third parties".
4. As such, the purpose of this Consultation Paper is to propose guidance, through a targeted update to the 2013 Guidelines, to address the existing lack of clarity surrounding the definition of private credit ratings.
5. For consistency purposes, ESMA also wishes to seize this opportunity to update the terminology of the 2013 Guidelines that refer to "private ratings", instead of the term "private credit ratings" used in the CRA Regulation.

Lack of clarity in the definition of private credit ratings

6. Article 2 (2) (a) of the CRA Regulation establishes that the requirements of the Regulation do not apply to private credit ratings, defining these as "*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*".
7. There are a number of elements of this provision that present practical obstacles to understanding the scope and boundaries of private credit ratings.
8. First, the term "produced pursuant to an individual order" lacks precision as to whether the word "produced" might be interpreted as the private credit rating either being "created" (prepared) or "issued" (delivered) and whether the provision of the rating should only happen after the client request.
9. Second, the term "individual order" is silent on how an "individual order" can be considered as having been placed (i.e. verbal or written agreement) and on the nature of the requesting party, for example whether it refers to the client of the rating producer such as the issuer, or, the rated entity itself.

10. Third, the term “provided exclusively to the person who placed the order” raises questions in terms of its applicability to more complex scenarios, such as two or more clients submitting an order for the same private credit rating.

Initial ESMA Guidance

11. ESMA provided guidance on the interaction of private credit ratings and the CRA Regulation within the 2013 Guidelines. The purpose of this guidance was to ensure that market participants understood whether they were engaging in credit rating activities that might require registration with ESMA.

12. This guidance was provided in two distinct parts. A first part, in paragraph 14, that provided guidance on the extent to which a recipient of a private credit rating may share that rating:

- *The recipient of a private 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.*

13. A second part, in paragraph 15, provided guidance on what steps an entity issuing a private credit rating must take to ensure a private credit rating is not shared to an extent that it could enter the public domain:

- *When issuing private ratings, credit rating agencies should assess whether the person who placed the order, as recipient of the private 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.*

14. The 2013 Guidelines supported this guidance with a practical example of a bank circulating a private credit rating to a restricted number of other banks for the purpose of a transaction.

15. However, the guidance provided in the 2013 Guidelines does not provide clarity as to what “a limited number of third parties” means in practice. In addition, while the 2013 Guidelines set out the need for the rating producer to assess whether the 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*”, they are silent on the possible monitoring duties of the rating producer with regards to the distribution to third parties by the client.

16. As a result, CRAs and non-CRA ratings’ producers¹ offering private credit rating products are uncertain as to their scope and boundaries, resulting in potential non-compliance with the definition of private credit ratings consistent with the spirit of the CRA Regulation.

¹ In the updated Guidelines and Recommendations on the Scope of the CRA Regulation, paragraphs 14 and 15, references to CRAs should be read and understood as applying both to credit rating agencies and to financial institutions, such as credit institutions, investment firms or insurance undertakings; and non-financial institutions, such as credit assessment firms, producing and distributing internal ratings that meet the requirements of private credit ratings under Article 2 (2) (a) CRAR. Both are referred to as “ratings producers” for the purposes of this CP.

17. This lack of clarity also hampers ESMA's ability to monitor and enforce the perimeter of the CRA Regulation appropriately as the rules governing the use and provision of private credit ratings – outside the scope of the Regulation – are unclear.

18. With a view to addressing the above issues, the topic of private credit ratings was included in ESMA's 2022 Annual Work Programme², where the development of the EU Capital Markets Union is highlighted as one of its strategic priorities.

Update to ESMA Guidance

19. With this Consultation Paper, ESMA is proposing further guidance through an update to paragraphs 14 and 15 of the 2013 Guidelines. By providing this additional clarification, ESMA is providing practical guidance on the application of the scope of the CRA Regulation to activities relating to private credit ratings that are “produced pursuant to an individual order”, “provided exclusively to the person who placed the order” and shared with “a limited number of third parties”, as well as its expectations on the monitoring of the dissemination of private credit ratings by the requesting party.

20. In doing so, ESMA seeks to:

- Clarify what are the constituting factors of private credit ratings and which are their acceptable boundaries, taking into account ESMA's past experience in specific cases.
- Ensure the transparency of ESMA's expectations on the use and dissemination practices of private credit ratings from market participants in different EU Member States.
- Ensure more straightforward and effective management of potential infringements of the perimeter of the CRA Regulation by non-CRA rating producing entities.

21. Finally, by further elaborating upon the application of these provisions, ESMA believes it will contribute to ensuring a level playing field with regards to the arrangements that market participants need to adopt to differentiate private from public credit ratings in the context of private placements, where private credit ratings are commonly used. This will contribute to the CMU initiative of removing barriers to the development of European markets for private placements, to promote easier and cheaper access to funding for small and medium-sized companies.

3. Scope of the CRA Regulation and Private Credit Ratings

22. With a view to introducing this guidance, ESMA has carried out an assessment of the market practice relating to private credit ratings by undertaking a desk-based review. This

² [27 September 2021 ESMA Annual Work Programme 2022.](#)

involved feedback gathering and extensive engagement with national competent authorities, CRAs, trade associations and other financial market participants.

23. On the basis of this assessment, ESMA understands that a private credit rating can be requested for different purposes. These can range from a bank requesting a private credit rating on several entities in order to benchmark its own system through a second party opinion, to an investor requesting a private credit rating to support an investment decision in relation to an unlisted security.
24. Whilst a private credit rating can be procured for reasons other than the credit assessment of a specific business transaction, it is in the context of these that ESMA guidance was particularly necessary, given their attractiveness in private placement markets. Furthermore, the participation of several stakeholders beyond the rating producer, issuer and investor (e.g. co-investors, syndicate members, underwriters, bookrunners or consultants) in these transactions created complexities related to the further dissemination of the private credit rating to these third parties.

Produced pursuant to an individual order

25. ESMA notes that market participants have expressed confusion as to the meaning of the term “produced” and whether an individual order for the private credit rating should precede the provision of the credit rating or not.
26. For instance, ESMA has received questions from market participants in private placement markets, in relation to the origin of the “individual order”. Notably, whether it should be implicitly derived from a client (to support his/her assessment of the borrower’s credit standing) or can originate internally (created at the instigation of the employee responsible for the client).
27. As such, ESMA wishes to provide more clarity in relation to the “produced pursuant to an individual order” element. ESMA expects a specific, explicit and prior demand for a credit rating from a client, before the private credit rating is created by the rating producer and, thereafter, provided to the requesting party.
28. This bilateral relationship between the person placing an order and the rating producer should be a written agreement, in the form of a request for a private credit rating, followed by a formal acceptance to provide it.
29. ESMA therefore proposes the following:

Providing an update to paragraph 14 of the 2013 Guidelines to require the private credit rating to only be produced following an explicit request for it, formalising this bilateral relationship through a written agreement between the person placing the order and the rating producer.

Q1: Do you agree with ESMA’s interpretation of “produced pursuant to an individual order”? If you do not agree, please explain.

Provided exclusively to the person who placed the order

30. ESMA's assessment has indicated that market participants are unclear as to whether there are exceptions to the private credit rating being exclusively provided to the person who placed the order or whether the rating producer can deliver the rating to more than one client.
31. Notably, ESMA's findings point to a lack of clarity in relation to a scenario under which two or more clients would place an individual order at the same time for the same private credit rating.
32. ESMA has also noted uncertainty as to the extent to which the duty of confidentiality applies. For instance, whether rating producers being under banking secrecy obligations could preclude the need to put in place specific confidentiality arrangements with clients, as further dissemination of the ratings would not be allowed in the first place.
33. ESMA reiterates that no exception is foreseen to the exclusive provision of the rating to the requesting party other than that set out in paragraph 14 of the 2013 Guidelines, allowing the client to share a private credit rating with a limited number of third parties on a strictly confidential basis.
34. ESMA's expectation is that the agreement between rating producers and clients should, in any case, contain a specific provision explicitly indicating the exclusive issuance of the rating to the requestor. ESMA also expects the latter to sign a non-disclosure undertaking to prevent the sharing of the private credit rating with more than "a limited number of third parties".
35. ESMA expects each private credit rating to be customised to the client requesting it, as opposed to the possibility of being addressed simultaneously to multiple parties forming a pool of clients. In the case where two or more clients submit the same individual order for a private credit rating, there should be a specific analysis on behalf of the rating producer for each of the orders placed. ESMA notes that, while the two analyses may still result in a similar output, the provider should not simply deliver the previous assessment to the following client. Given the unlikelihood of this scenario, however, ESMA has decided not to explicitly include this clarification in the current revision of the 2013 Guidelines.
36. ESMA therefore proposes the following:

Providing an update to paragraph 14 of the 2013 Guidelines to recommend the inclusion of a provision indicating the exclusive issuance of the rating to the person who placed the order and the existence of a Non Disclosure Agreement signed by the latter.

Q2: Do you agree with ESMA's interpretation of "provided exclusively to the person who placed the order"? If you do not agree, please explain.

A limited number of third parties

37. The 2013 Guidelines introduced the concept of “a limited number of third parties”, without providing clarity as to what this means in practice.
38. ESMA’s findings have shown that, as a result, certain ratings producers in private placement markets may share private credit ratings with an extensive number of credit institutions, co-financing institutions, subsidiaries and other third parties. In addition, ESMA has found the possibility for the development of a secondary market for these transactions, with potential further distribution by the market participants. In summary, ESMA has identified that, in the context of private placement markets, private credit ratings can potentially be shared with a large number of third parties in a manner which could effectively constitute public disclosure or distribution by subscription.
39. Similarly, all CRAs offering private credit ratings products that ESMA engaged with, were unclear in relation to the numerical equivalent of “a limited number of third parties”. At the same time, two of them have proactively set a maximum ceiling for further distribution of the private credit rating by the client.
40. Hence, ESMA has concluded that quantitative and qualitative criteria should be included in the 2013 Guidelines to allow a better assessment of the public or private nature of a credit rating with respect to redistribution to third parties. From a qualitative angle, ESMA believes there should be objective and justified reasons for third parties to receive a private credit rating. On the quantitative side, the distribution process should not allow the sharing of the private credit rating with a considerably enlarged number of third parties.
41. To account for the qualitative element, ESMA expects objective and justified reasons for a third party to receive a private credit rating, such as a link to the specific business transaction in question. For instance, there should be a kind of debtor-credit relationship between the third party and the issuer and/or an expression of interest by the third party to the issuer regarding the provision of credit.
42. For the quantitative aspect, ESMA proposes the application by analogy of the EU prospectus regime’s exemption for publishing a prospectus if the offering is addressed to “a restricted circle of investors”, in accordance with Recital 15 of the Prospectus Regulation³:
- *Where an offer of securities is addressed exclusively to a restricted circle of investors who are not qualified investors, drawing up a prospectus represents a disproportionate burden in view of the small number of persons targeted by the offer, thus no prospectus should be required. That would apply for example in the case of an offer addressed to a limited number of relatives or personal acquaintances of the managers of a company.*

³ [Regulation \(EU\) 2017/1129 of the European Parliament and of the Council of 14 June 2017.](#)

43. Under Article 1 (4) of the Prospectus Regulation, if the offering is addressed to fewer than 150 natural or legal persons, the obligation to publish a prospectus does not apply:

- *The obligation to publish a prospectus set out in Article 3(1) shall not apply to any of the following types of offers of securities to the public: (...) an offer of securities addressed to fewer than 150 natural or legal persons per Member State, other than qualified investors.*

44. Similarly, using this proxy, ESMA proposes that the requestor of a private credit rating is only allowed to distribute the rating to up to 150 natural persons (“a limited number of third parties”), on a strictly confidential basis, with further dissemination only being allowed for legal, statutory or judicial reasons, for instance to auditors, supervisory authorities or law enforcement.

45. Additionally, ESMA considers the 150 limit adequate as the topic of offerings allows for a similar context as private placements (where private credit ratings can primarily be used). It is also ESMA’s understanding that the number at hand has been well accepted and not challenged in the past by market participants in the context of the Prospectus Regulation.

46. Furthermore, this would be aligned with current market practices, as CRAs interviewed by ESMA who have chosen to define this limit, have also proactively adopted the proxy of 150 contained in the Prospectus Regulation to clarify their understanding of the ability to share a private credit rating with “a limited number of third parties”.

47. Finally, ESMA would like to clarify that although it has chosen to adopt the Prospectus Regulation’s “natural or legal persons” terminology, it only proposes to count natural persons for the purposes of establishing a limit of third parties for the dissemination of a private credit rating. This will mean that each individual employee of a legal entity, receiving the rating within that legal entity, is effectively counted as a third party for the purposes of reaching the 150 limit.

48. ESMA therefore proposes the following:

Providing an update to paragraph 15 of the 2013 Guidelines to clarify that the receiving party may share the rating confidentially with a selected and definite number of natural or legal persons, up to a maximum limit of 150 natural persons.

Q3: Do you agree that setting a 150 natural persons limit for sharing the private credit rating with third parties would be adequate? If you do not agree, please explain.

Monitoring the distribution of private credit ratings

49. The only existing obligation placed on ratings producers in relation to the requesting party, under paragraph 15 of the Guidelines and Recommendations on the Scope of the CRA Regulation, is that they:
- *Assess whether the person who placed the order, as recipient of the private 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.*
50. In general, ESMA expects that adequate controls are put in place by the ratings producer to ensure that the limit of third-party recipients is adhered to by the receiving party.
51. Monitoring arrangements to ensure that the limit of third-party recipients is not breached could entail the adoption of an appropriate IT solution (for instance, a password-protected website or third-party private document exchange platform). ESMA's findings have shown that several CRAs have put in place automatic controls for the tracking of distribution of private credit ratings provided to the client. At the same time, ESMA acknowledges that the costs of implementing a technological solution may be disproportionate for certain CRAs and non-CRA rating producers, considering the low market demand for these products and how highly dependent such a control would be on the delivery method of the private credit rating to the client (i.e. the number of third party recipients is easier to monitor if the rating is provided through a document release system than through letters or e-mails).
52. Also bearing in mind the difficulty of controlling any eventual informal sharing of the rating between individuals, and so as not to place an excessive burden on rating producers, ESMA's expectations are that the subsequent chains of distribution of the private credit rating should be monitored by the ratings producer on a best-efforts basis.
53. ESMA therefore proposes the following:

Providing an update to paragraph 15 of the 2013 Guidelines to require appropriate controls to be implemented by the ratings producer to allow for the monitoring of the distribution of the private credit rating to third parties.

Q4: Do you agree with the onus on the rating producer to monitor the distribution of the private credit ratings to third parties? If you do not agree, please explain.

Terminology under the CRA Regulation and the 2013 Guidelines

54. Even though the 2013 Guidelines are predicated on the CRA Regulation, the terminology used to refer to private credit ratings differs. Whilst Article 2 (2) (a) of the CRA Regulation

refers to “private credit ratings”, the 2013 Guidelines refer to the term “private ratings” throughout the text.

55. ESMA proposes the replacement of the references to “private rating(s)” in the 2013 Guidelines by the term “private credit rating(s)”, in line with the body of the CRA Regulation. This clarification seeks no material impact, other than enhancing consistency between level 1 and level 3 guidance.

Questions for Rating Producers (CRAs and non-CRAs)

- 1. Do you agree with ESMA’s interpretation of “produced pursuant to an individual order”? If you do not agree, please explain.**
- 2. Do you agree with ESMA’s interpretation of “provided exclusively to the person who placed the order”? If you do not agree, please explain.**
- 3. Do you agree that setting a 150 natural persons limit for sharing the private credit rating with third parties would be adequate? If you do not agree, please explain.**
- 4. Do you agree with the onus on the rating producer to monitor the distribution of the private credit ratings to third parties? If you do not agree, please explain.**

Question for Issuers and Users of Private Credit Ratings

- 5. Do you agree that ESMA’s proposed approach is reflective of your interactions with rating producers and that the market would benefit from such a clarification?**

4. Conclusion

56. With this revised guidance, ESMA seeks to enhance the clarity of existing regulatory provisions concerning private credit ratings. In particular, ESMA aims to prevent the misuse of private credit ratings by rating producers and other financial market participants through an additional clarification of the various elements comprising its definition.
57. ESMA welcomes the views of all stakeholders on whether the proposed update to the Guidelines and Recommendations on the Scope of the CRA Regulation will facilitate their understanding of the scope and boundaries of private credit ratings.

5. Next Steps

58. ESMA is looking for feedback on this Consultation Paper by 11 March 2022. Upon finalisation of this revised guidance, ESMA will include it as an addition to paragraphs 14 and 15 of the existing Guidelines and Recommendations on the Scope of the CRA Regulation.
59. The 2013 Guidelines in Annex I will be translated into all official languages and published on ESMA's website. ESMA will apply these Guidelines for the purposes of its supervision 3 months from the date of publication.



Annex I Guidelines

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 and recommendations are addressed to:
 - a. Credit rating agencies (as defined in the Article 3 (1) (a) of the CRA Regulation);
 - b. NCAs and SCAs.

When?

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

II. Purpose

3. The purpose of these guidelines and recommendations 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 and Recommendations

4. This document contains Guidelines and Recommendations 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 and Recommendations.
5. Competent authorities to whom the Guidelines and Recommendations 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 and Recommendations, 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 whether they comply or intend to comply with the Guidelines and Recommendations, 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 exemptions from registration (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 an agreement consisting of a written request from the person placing the order and a formal written acceptance by the ratings provider. ESMA expects this agreement to contain a 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, credit rating agencies should ensure that the written requests for the issuance of private credit ratings together with the formal acceptance of the rating provider, cover the duty of confidentiality and limitations on the distribution of the ratings. When issuing private credit ratings, credit rating agencies 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 credit rating agencies 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 credit rating agencies 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 confidentially and with a selected and definite number of natural or legal persons. This number should be limited and can never exceed 150 natural persons. To ensure that this maximum limit is adhered to, appropriate controls should be implemented by the rating producer 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 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

22. 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.
23. 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.
24. 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

25. 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.

26. 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

1. Introduction

60. ESMA has decided to conduct a Cost Benefit Analysis (CBA) in relation to the review of the Guidelines and Recommendations on the Scope of the CRA Regulation.
61. 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.
62. 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.

Policy Objective	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.

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

Option 1	No Change.
Benefits	No change to existing guidance would maintain the status quo and contribute to the consistency and 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.
Compliance costs - IT - Training	For providers and distributors of private credit ratings the current approach delivers less on the scope of the CRA Regulation and poses problems to their consistent transposition in market participants policies and procedures. For

Staff	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.

Option 2	Targeted Revision of the 2013 Guidelines.
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 supervisory 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. ESMA foresees that EU registered CRAs, incumbent in the market for private credit rating products will have more established policies and procedures in this area than non-CRA ratings producing entities. As such, new ESMA

	<p>guidance may require a greater effort to adapt and 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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Option 3	Standalone Q&A.
Benefits	<p>Development of an ESMA Q&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	<p>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> <p>ESMA foresees that EU registered CRAs, incumbent in the market for private credit rating products 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 burden on the latter.</p>

Similarly, it is foreseen that smaller entities providing private credit ratings producing may also be more affected than larger ones, given the lower number of resources and IT capabilities that are available to them.

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.

Questions for all respondents

- 6. Do you have any comments on the CBA outlined under the preferred option?**

Annex III List of Questions

Q1	Do you agree with ESMA's interpretation of "produced pursuant to an individual order"? If you do not agree, please explain.
Q2	Do you agree with ESMA's interpretation of "provided exclusively to the person who placed the order"? If you do not agree, please explain.
Q3	Do you agree that setting a 150 natural persons limit for sharing the private credit rating with third parties would be adequate? If you do not agree, please explain.
Q4	Do you agree with the onus on the rating producer to monitor the distribution of the private credit ratings to third parties? If you do not agree, please explain.
Q5	Do you agree that ESMA's proposed approach is reflective of your interactions with rating producers and that the market would benefit from such a clarification?
Q6	Do you have any comments on the CBA outlined under the preferred option?