

Extract from the Credit Rating Services Bill with marked-up proposed amendments

CHAPTER 1 <sup>1</sup>

DEFINITIONS, OBJECTS AND APPLICATION

Definitions and interpretation

1. (1) In this Act, unless the context indicates otherwise—

“**associate**”, in relation to—

(a) a juristic person—

(i) which is a company, means its subsidiary and its holding company and any other subsidiary or holding company thereof as defined in section 1 of the Companies Act;

(ii) which is a close corporation registered under the Close Corporations Act, 1984 (Act No. 69 of 1984), means any member thereof as defined in section 1 of that Act;

(iii) which is not a company or close corporation, means another juristic person which would have been its subsidiary or holding company—

(aa) had it been a company; or

(bb) in the case where that other juristic person is not a company either, had both it and that other juristic person been a company;

(iv) means any person in accordance with whose directions or instructions its board of directors or, in the case where such juristic person is not a company, the governing body of such juristic person, acts; or

(b) any person—

(i) means any juristic person whose board of directors or, in the case where such juristic person is not a company, the governing body of such juristic person, acts in accordance with its directions or instructions; or

(ii) means a trust controlled or administered by the juristic person;

“**Companies Act**” means the Companies Act, 2008 (Act No. 71 of 2008);

“**credit rating**” means an opinion regarding the creditworthiness of—

(a) an entity;

(b) a security or a financial instrument; or

(c) an issuer of a security or a financial instrument, using an established and defined ranking system of rating categories, excluding any recommendation to purchase, sell or hold any security or financial instrument;

“**credit rating agency**” means a person incorporated under the Companies Act, and who is registered to provide credit rating services in terms of this Act;

“**credit rating services**” means, in relation to a credit rating, data and information analysis, evaluation, approval, issuing or review of credit ratings;

“**deputy registrar**” means the deputy registrar of credit rating agencies contemplated in section 21;

“**external credit rating**” means a credit rating issued by an external credit rating agency;

**Comment [N1]:** The amendment to the definition will ensure that only data analysis related to credit rating services will be captured by the definition.

<sup>1</sup> Please note:

(a) Insertions are marked in green underline.

(b) Deletions are marked in red strikethrough.

(c) Numbering of sections and subsections has not been amended to reflect proposed amendments in order to allow for comparability with Bill as tabled.

(d) Rationale for the proposed amendments will be found in the Cover Letter and in comments to the amendments.

(e) Terms used in the comments to the proposed amendments refer to terms used in the Cover Letter and/or Bill.

(f) For ease of reference, comments in this Annex reflect only a brief description of the relevant issue.

“**external credit rating agency**” means a person authorised or registered by a regulatory authority to perform credit rating services similar to those regulated under this Act and who is subject to the laws of a country other than the Republic, which laws—

(a) establish a regulatory framework which is approved by the registrar as being equivalent to that established by this Act; and

(b) are supervised and monitored by a regulatory authority;

“**Financial Services Board Act**” means the Financial Services Board Act, 1990 (Act No. 97 of 1990);

“**FSB official website**” means the website of the Financial Services Board established by section 2 of the Financial Services Board Act;

“**group**” means a group consisting of two or more juristic persons, irrespective of whether any of those persons is domiciled in the same country as any of the others, and one or more of which is a credit rating agency, where—

(a) each of the juristic persons is an associate of any one of the others; or

(b) the juristic persons are so interconnected that should one of them experience financial difficulties, another one or all of them would likely be adversely affected;

“**Minister**” means the Minister of Finance;

“**outsource**” means the contracting out of a function to an external provider in a manner that may materially impair the quality of the internal control of the credit rating agency and the ability of the registrar to supervise the compliance of the credit rating agency with its obligations under this Act;

“**person**” means any natural person, partnership or trust, and includes—

(a) an organ of state as defined in section 239 of the Constitution of the Republic of South Africa, 1996;

(b) any company incorporated or registered as such under any law; or

(c) anybody of persons, corporate or unincorporate;

“**prescribe**” means prescribe by the Minister by regulation, or by the registrar by rule or by notice in the Gazette, and “**prescribed**” has a corresponding meaning;

“**Promotion of Administrative Justice Act**” means the Promotion of Administrative Justice Act, 2000 (Act No. 3 of 2000);

“**publish**” means any direct or indirect communication transmitted by any medium, or any representation or reference written, inscribed, recorded, encoded upon or embedded within any medium, by means of which a person seeks to bring any information to the attention of a person, or all or part of the public, and “**published**”, “**publishes**” or “**made public**” has a corresponding meaning;

“**public regulation**” means any legislation, including subordinate legislation, or any registration, licence, directive or similar authorisation issued by a regulatory authority or pursuant to any statutory authority;

“**rating category**” means a rating symbol, such as a letter symbol or a numerical symbol which might be accompanied by appending identifying characters, used in a credit rating to provide a relative measure of risk to distinguish the different risk characteristics of the type of rated entity, issuer or financial instrument or other asset;

“**registrar**” means the registrar of credit rating agencies contemplated in section 21;

“**regulated person**” means a person that has been granted authority to conduct business or activities by a regulatory authority;

“**regulatory authority**” means an organ of state responsible for the supervision or enforcement of legislation dealing with the regulation of institutions and the provision of financial services, or a similar body designated in the laws of a country other than the Republic to supervise and enforce legislation of that country;

“**regulatory purposes**” means the use of credit ratings for the specific purpose of complying with national legislation or the listings requirements made by an exchange under section 12 of the Securities Services Act, 2004 (Act No. 36 of 2004);

“**rule**” means a rule made in terms of section 24;

“**structured finance instrument**” means a financial instrument or other assets resulting from a securitisation ~~transaction or~~ scheme as defined in section 1(1) of the Banks Act, 1990;  
“**this Act**” includes the regulations, ~~rules and any notices or directives issued, approval or exemption granted, determinations made, requirements determined or conditions imposed, or any other decision of the registrar~~; and  
“**website**” has the meaning set out in section 1 of the Electronic Communications and Transactions Act, 2002 (Act No. 25 of 2002).

**Comment [N2]:** The definition for “securitisation transaction” as defined in the Banks Act, 1990 may be of relevance.

**Comment [N3]:** As drafted, the definition is too broad and will lead to circular references in the Bill.

(2) For purposes of this Act, any reference to “**company**”, “**holding company**” or “**subsidiary**” means a reference to a company, holding company or subsidiary, as the case may be, as defined in the Companies Act, or a similar entity incorporated under the laws of a country other than the Republic.

(3) Any decision or other action of an administrative nature taken by the registrar that affects the rights of another person, including a regulated person, must comply with this Act and the Promotion of Administrative Justice Act ~~or this Act~~.

(4) Nothing in this Act deprives any person of any right that such person holds under the Promotion of Access to Information Act, 2000 (Act No. 2 of 2000) and the Promotion of Administrative Justice Act.

(5) (a) A credit rating agency that ~~publishes any information or any credit rating in the performance of credit rating services or~~ is required to publish, disclose, produce or provide a policy, code, document or information under this Act, must publish, disclose, produce or provide that ~~credit rating~~, information, policy, code or document—

**Comment [N4]:** Consideration may be given to limiting the scope as proposed in order to avoid inconsistency with section 20 of the Bill.

(i) in a prescribed form, if a form has been prescribed; ~~or~~

(ii) in plain language, if no form has been prescribed.

**Comment [N5]:** Please see end note.

(b) For the purposes of this Act, a credit rating, policy, code, document or information is in plain language if it is reasonable to conclude that a person of the class of persons for whom the credit rating, policy, code, document or information is intended, with average literacy skills and experience in dealing with credit ratings, credit rating services and credit rating agencies, could be expected to understand the content, significance and import of the credit rating, information, policy, code, document or information without difficulty, having regard to—

(i) the context, ~~comprehensiveness and consistency of the credit rating, information, policy, code, document or information~~;

(ii) the ~~organisation, form and style of the credit rating, policy, code, document or information~~;

(iii) the ~~vocabulary, usage and sentence structure of the credit rating, policy, code, document or information~~; and

(iv) the ~~use of any illustrations, examples, headings or other aids to reading and understanding the credit rating, policy, code, document or information~~.

(6) If, in terms of this Act, a credit rating, policy, code, document, information, record or statement is required to be—

(a) retained, it is sufficient if an electronic original or reproduction of that credit rating, policy, code, document, information, record or statement is retained as provided for in sections 15 and 16 of the Electronic Communications and Transactions Act, 2002 (Act. No. 25 of 2002); or

(b) published, disclosed, produced or provided, it is sufficient if—

(i) an electronic original or reproduction of that credit rating, policy, code, document, information, record or statement is published, disclosed, produced or provided by electronic communication in such a manner and form that the credit rating, policy, code, document, information, record or statement can conveniently be printed by the recipient within a reasonable time and at a reasonable cost; or

(ii) a notice of the availability of that credit rating, policy, code, document, information, record or statement, summarising its content and satisfying any prescribed requirements, is delivered to each

intended recipient of the policy, code, document, information, record or statement, together with instructions for receiving the complete policy, code, document, information, record or statement.

## Objects of Act

2. The objects of this Act are to—

- (a) ensure responsible and accountable credit rating agencies;
- (b) protect the independence, integrity, transparency and reliability of the credit rating process and credit ratings;
- (c) improve investor protection;
- (d) improve the fairness, efficiency and transparency of financial markets; and
- (e) reduce systemic risk.

**Comment [N6]:** As a critical foundation of the Bill, reference should be made to this important principle in the objects of the Act.

## Application of Act

3. (1) Subject to subsection (4), this Act applies to—

- ~~(a) credit rating services performed in the Republic;~~
- ~~(b) credit ratings that are published in the Republic; and~~
- ~~(c) any person that performs credit rating services or issues credit ratings that are published in the Republic.~~

**Comment [N7]:** Please refer to paragraph I of the Cover Letter.

(2) ~~With effect from a date determined by the Minister by notice in the *Gazette*, a person may not perform credit rating services or issue a credit rating that is published in the Republic, unless that person is registered as a credit rating agency in terms of this Act.~~

**Comment [N8]:** Please refer to a proposed new section 36 of the Bill which includes the necessary transitional provision regarding to the use of credit rating ratings.

(3) This Act does not create a general obligation for—

- (a) all securities or financial instruments to be credit-rated;
- (b) financial institutions or investors to invest only in entities, securities or financial instruments that are credit-rated.

(4) This Act 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.

## Use of credit ratings

4. (1) A regulated person must for regulatory purposes only use credit ratings that are issued ~~or endorsed~~ by credit rating agencies ~~which are registered in accordance with this Act or by any external credit rating agency in the same group as a credit rating agency.~~

**Comment [N9]:** Please refer to paragraph I of the Cover Letter.

(2) The registrar shall publish a list of external credit rating agencies whose credit ratings may be used for regulatory purposes under this section.

Furthermore, the definition for “credit rating agency” refers only to registered CRAs.

## CHAPTER 2

### REGISTRATION OF CREDIT RATING AGENCY

#### Application for registration

5. (1) An application for registration as a credit rating agency must be made in the form and manner prescribed by the registrar, and must be lodged with the registrar and be accompanied by—

- (a) a certificate of incorporation of the applicant under the Companies Act;

(b) details of its—

- (i) registration, authorisation or approval in countries other than the Republic to undertake credit rating services, if applicable;
- (ii) ownership structure, organisational structure and corporate governance;
- (iii) subsidiaries, if any;
- (iv) resources and expertise to perform credit rating services;
- (v) programme of operations, including indications of where the main business activities are expected to be carried out, branches to be established, and the type of business that will be undertaken;
- (vi) expected outsourcing arrangements, including details of the persons that will be assuming outsourcing functions;
- (vii) policies and procedures to identify, manage and disclose any conflicts of interests;
- (viii) compensation and performance evaluation arrangements; and
- (ix) ~~compliance with or adherence to~~ the code of conduct ~~it proposes to adopt~~ ~~prescribed~~ in terms of section 11;

(c) a description of the procedures and methodologies to be used to issue and review credit ratings;

(d) information to satisfy the registrar that the applicant, its directors and ~~rating analysts~~ ~~employees~~ comply with the fit and proper requirements prescribed by the registrar, in respect of—

- (i) personal character qualities of honesty and integrity;
- (ii) competence; ~~and~~
- (iii) operational ability; ~~and~~
- (iv) ~~financial soundness~~;

(e) the application fee prescribed by the registrar; and

(f) any other information prescribed by the registrar.

(2) An applicant must promptly amend its application for registration and inform the registrar if, during the application process, the information contemplated in subsection (1) becomes inaccurate.

(3) The registrar may exempt an applicant who, or whose holding company, or a related company in the same group, is registered, authorised or approved by a foreign regulatory authority as a credit rating agency from providing some or all of the information required under subsection (1), if—

(a) the applicant requests an exemption;

(b) the applicant provides proof of such registration, authorisation or approval; and

(c) the registrar is satisfied that such registration, authorisation or approval was granted in accordance with public regulation that is equivalent to this Act.

~~(4) The registrar must give notice of the receipt of an application for registration on the FSB official website, which notice must state—~~

~~(a) the name of the applicant; and~~

~~(b) the period within which objections to the application may be lodged with the registrar.~~

(5) The registrar may—

(a) require an applicant to furnish additional information and require that information or any information that accompanied the application to be verified; and

(b) take into consideration any other information regarding the applicant, derived from any other source, including another regulatory authority.

(6) (a) The registrar must, after consideration of an application and after consultation with any local regulatory authority that relies on, refers to or uses credit ratings in its supervision and regulatory activities—

- (i) if satisfied that an applicant complies with the requirements of this Act, grant the application; or
- (ii) if not so satisfied, subject to paragraph (b), refuse the application.

**Comment [N10]:** The proposed language requires a CRA to adopt *and adhere* to a code of conduct based broadly on a relevant international code of conduct. The IOSCO Code is drafted on a “comply-or-explain” basis, allowing for CRAs to publish any deviations of a CRA’s own code of conduct from the IOSCO Code. The implication of the word “adhere” could be interpreted to create an obligation to comply strictly with the relevant Code.

**Comment [N11]:** Requiring all employees to undergo a fitness and propriety test is unnecessary. For example, administrative or secretarial staff, which have no analytical responsibilities, should not be required to meet fitness and propriety tests.

Any fitness and propriety test should be limited to senior management and analytical staff employed by the CRA.

**Comment [N12]:** The response of National Treasury to informal comments on the draft of this Bill noted that the intention of this paragraph was to ensure that that analytical staff are competent and appropriately qualified. There is no objection to such an objective, however, it is unclear why a financial soundness test is required to meet this objective. CRAs do not offer advice or hold a fiduciary duty to customers and we therefore propose the deletion of the financial soundness criterion under the fitness and propriety test.

**Comment [N13]:** The FSB should not be required to announce the receipt of an application for registration under the resulting Act.

- (b) If an application for registration is refused, the registrar must—
- (i) notify the applicant of the refusal;
  - (ii) provide the applicant with written reasons for the refusal; and
  - (iii) advise the applicant of the right to appeal, in accordance with section 33.

(7) The registrar may grant an application for registration subject to any condition that the registrar may determine, which condition may not be inconsistent with this Act.

(8) The registrar must, on granting an application, issue a certificate of registration to the credit rating agency and publish a notice of the registration on the FSB official website.

(9) A credit rating agency must ensure that—

(a) a reference to the fact that such a certificate of registration is held, is contained in all credit rating announcements ~~business documentation and advertisements~~ published by the credit rating agency in the Republic; and

(b) its certificate of registration is at all times available to any person requesting proof of its registration status under authority of a law or for the purpose of entering into a business relationship with the credit rating agency concerned.

### **Suspension and cancellation of registration**

6. (1) The registrar may, after consultation with any local regulatory authority that relies on, refers to or uses credit ratings in its supervision and regulatory activities, at any time, suspend or cancel the registration of a credit rating agency if the registrar is ~~satisfied~~, on the basis of available facts and information, that the credit rating agency—

- (a) expressly renounces the registration or has provided no credit rating services for the preceding six months;
- (b) has obtained the registration by providing false information or by any other irregular means;
- (c) no longer meets the conditions under which it was registered;
- (d) has failed to comply with any condition imposed under this Act;
- (e) has failed to comply with any directive issued under this Act; or
- (f) has been liquidated.

(2) (a) If the registrar suspends or cancels the registration of a credit rating agency under subsection (1), the registrar may do so subject to any conditions that the registrar may determine, which conditions may not be inconsistent with this Act.

(b) The registrar may revoke any suspension under subsection (1) if the registrar is satisfied that the credit rating agency has complied with all the conditions to which the suspension was made subject.

(3) Subject to the provisions of the Promotion of Administrative Justice Act, the registrar must, before the suspension or cancellation of a registration—

(a) notify the credit rating agency in writing of the registrar's intention to suspend or cancel the registration and the reasons therefor;

(b) give the credit rating agency 30 days' written notice, calculated from the date on which the notice was given, to make representations on why its registration should not be suspended or cancelled; and

(c) consider any representations received.

**Comment [N14]:** A CRA publishes a number of research pieces globally that may find application in South Africa or may be authored in South Africa but published on its website. A strict reading of this sub-section would require a CRA to confirm its registration status in all such publications which we do not understand to be the objective of the Bill. We propose that a CRA be required to include a statement to the effect that it is registered under the resulting Act in all credit rating announcements published specifically in South Africa.

- (4) (a) The registrar must notify the credit rating agency of its decision and publish a notice of any suspension or cancellation of registration, the reasons therefor and any conditions attached thereto on the FSB official website and any other appropriate media.
- (b) The suspension or cancellation of the registration of a credit rating agency takes effect on a date specified in the notice contemplated in paragraph (a).
- (c) If a credit rating agency has appealed against a suspension or cancellation of registration, the registrar must not publish the notice contemplated in paragraph (a) until the appeal process has been finalised.

- (5) (a) Credit ratings issued by a credit rating agency whose registration has been suspended or cancelled, may continue to be used for regulatory purposes for—
- (i) 14 days after the publication of the notice contemplated to in subsection (4)(a), if credit ratings of such credit rating agency, securities, financial instrument or issuer were issued by other credit rating agencies registered under this Act; or
- (ii) three months after the publication of the notice contemplated in subsection (4)(a), if no credit ratings of such credit rating agency, securities, financial instrument or issuer were issued by other credit rating agencies registered under this Act.
- (b) The registrar may extend the period referred to in paragraph (a)(ii), in order to mitigate any potential market disruption or to ensure financial stability.

### CHAPTER 3 DUTIES OF CREDIT RATING AGENCY

#### Duties

7. (1) A credit rating agency must—

- (a) comply with this Act;
- (b) provide the registrar with any information required in terms of this Act, ~~and any additional information requested by the registrar;~~
- (c) within 14 days of becoming aware of any material change, inform the registrar if any information submitted in respect of its application under section 5 changes in a material manner;
- (d) be organised in a way that ensures that its business interest does not impair the independence and integrity of its credit ratings or the accuracy of its credit rating services;
- (e) have sound administrative and accounting procedures, internal control mechanisms, effective procedures for risk assessment, and effective control and safeguarding arrangements for information-processing systems;
- (f) establish appropriate and effective organisational and administrative arrangements to—
- (i) prevent, identify, eliminate ~~or~~ manage and disclose any conflicts of interest of the credit rating agency, its analysts and employees; and
- (ii) protect confidential information made available to it by issuers, including prohibiting its analysts and employees from using such information to enter into transactions;
- (g) employ appropriate systems, resources and procedures to ensure continuity and regularity in the performance of its credit rating services;
- (h) regularly monitor and evaluate the adequacy and effectiveness of its systems, internal control mechanisms and arrangements and take appropriate measures to address any deficiencies;
- (i) prior to issuing a credit rating on a new type of product, be satisfied that ~~ensure that at all times~~ it has the necessary knowledge and experience to issue credit ratings and perform its credit rating services; and
- (j) establish a unit within its organisation whose function is to communicate with investors, potential investors and the public about any questions, concerns or complaints that it may receive.

**Comment [N15]:** The remit granted to the registrar to require a CRA to “provide any information requested by the registrar” is unduly broad and should be deleted.

**Comment [N16]:** Although we understand that National Treasury would prefer to have the registrar be the guardian of any materiality threshold, it seems impractical for a CRA to report any change in the application papers on an ongoing basis. It would be an undue administrative burden on a CRA to monitor every change, however minor, and be required to report that to the registrar.

**Comment [N17]:** Given the nature of the CRA business, it is impossible to “eliminate” all conflicts of interest. A requirement to eliminate conflicts of interest AND “manage and disclose any conflicts of interest” is not achievable and we therefore propose the introduction of the word “or”.

**Comment [N18]:** An adjustment is required to this subsection in order to ensure that the subsection does not have unintended consequences. As drafted, if a CRA does not decide to assign a credit rating to a new highly complex instrument, it will be admitting that it does not have the knowledge to issue credit ratings (in this case a subset thereof) and may be found to have breached the resulting Act.

## Appointment of directors

8. (1) A credit rating agency must, within 14 days after the appointment of a director, inform the registrar of the appointment and furnish the registrar with such information on the appointment as the registrar may require.

(2) The provisions of subsection (1) may not be construed as rendering the appointment of a director of a credit rating agency subject to the approval of the registrar.

(3) If the registrar wishes to terminate the employment of a director, the registrar shall notify the credit rating agency and director concerned in writing of his or her intention and of the grounds for the proposed termination;

(4) The written notice referred to in paragraph (3) shall notify such parties that they are entitled to submit written representations to the registrar in response to that notice.

(5) Any notified party shall be entitled, but not obliged, to make written representations to the registrar's written notice within 14 working days of receipt of the registrar's notice, or within such longer period as the registrar may, upon written application by the affected party concerned, allow.

(6) The registrar shall, within 14 working days of receipt of a written representation referred to in paragraph (4)-

(i) consider the representation;

(ii) decide whether or not the appointment of the director should be terminated for the reasons contemplated in paragraph (3); and

(iii) give notice to the affected parties of his or her decision in writing.

(7) If, after having considered any written representation in respect of the director concerned, the registrar remains of the view that such officer's appointment should be terminated, or if no such written representation is submitted to the registrar within the period allowed under paragraph (5), the registrar shall refer the matter to the Arbitration Foundation of South Africa or its successor-in-law; or any other body designated by the registrar

by means of a notice in the *Gazette* (referred to below as the "Arbitrator") for arbitration.

(8) The registrar shall make the request for arbitration referred to in paragraph (7) -

(i) in writing; and

(ii) within three working days after the expiry of the 14 day period referred to in paragraph (6) or, if the affected parties do not submit any written representations to the registrar within the period allowed under paragraph (6), within three working days after the expiry of that period.

(9) The Arbitrator shall determine whether or not adequate reasons exist for the termination, by the registrar, of the appointment of the director concerned.

(10) If under paragraph (9) the Arbitrator decides that adequate reasons exist for the termination of the appointment, the Arbitrator shall confirm the termination of the appointment in writing addressed to the registrar and the director concerned, whereupon the termination shall immediately take effect.

(11) If under paragraph (9) the Arbitrator determines that adequate reasons do not exist for the termination of the appointment, the Arbitrator shall reject the termination by written notice to the registrar and to the director concerned, whereupon the appointment of the person in question shall continue with full force and effect.

~~(3) If the registrar is of the opinion that a director does not meet the prescribed fit and proper requirements contemplated in section 5(1)(d), the registrar may instruct a credit rating agency to remove that director from the board of the credit rating agency, and if so instructed, the credit rating agency must remove the director.~~

~~(4) The registrar must, before instructing a credit rating agency to remove a director from its board, give notice, to the credit rating agency concerned, and, unless it is impracticable to do so, also notify the director concerned.~~

~~(5) The registrar must consider any representations received from the credit rating agency or director, as the case may be, regarding the instructions to remove such director.~~

**Comment [N19]:** We believe a more proportionate provision in this regard can be found in the Banks Act, 1990. It is also unclear why a lower level of protection is afforded to directors of a CRA than to those of a bank in South Africa especially given the need to ensure the independence of CRAs as reflected in section 20 of the Bill.

~~(6) The credit rating agency must ensure that the director concerned does not in any way, directly or indirectly, take part in the management of the credit rating agency, pending the final outcome of any action under section 33.~~

### Methodologies, models and key rating assumptions

9. A credit rating agency must—

- (a) adopt, implement and enforce adequate measures to ensure that the credit ratings it issues, are based on a thorough analysis of all the information that is available to it and that is relevant to its analysis according to its rating methodologies;
- (b) use rating methodologies that are rigorous, systematic, continuous and subject to validation based on historical experience, including back-testing;
- (c) regularly review its methodologies, models and key rating assumptions such as mathematical or correlation assumptions, any significant changes or modifications to them and the appropriateness of those methodologies, models and key rating assumptions if they are used or are intended to be used for the assessment of new financial instruments; and
- (d) establish internal arrangements to monitor the impact of changes in macro-economic or financial market conditions on credit ratings.

### Credit ratings

10. (1) A credit rating agency must—

- (a) publish any credit rating or any decision to discontinue a credit rating impartially and in a timely manner~~timeously~~;
- (b) when publishing a credit rating—
  - (i) state clearly and prominently any attributes and limitations of the credit rating; and
  - (ii) provide an explanation of the key elements underlying the credit rating ~~that an investor, a potential investor or a member of the public, as the case may be, is able to understand how a rating was arrived at;~~ and
- (c) monitor its credit ratings ~~and regularly review its credit ratings.~~

- (2) A credit rating agency must, when issuing a credit rating for a structured finance instrument, ensure that the rating categories that are attributed to structured finance instruments are clearly differentiated, using an additional symbol which distinguishes them from rating categories used for any other entities, securities, financial instruments or issuers.
- (3) A credit rating agency must disclose its policies and procedures regarding unsolicited credit ratings.
- (4) A credit rating agency must refrain from issuing a credit rating if, in the opinion of the credit rating agency, the lack of reliable data, the complexity of a new type of financial instrument or the quality of information available may result in a non-credible credit rating.

### Code of conduct

11. (1) A credit rating agency must adopt and; publish ~~and adhere to~~ a code of conduct that—

- (a) adopts the principles contained in a relevant international code of conduct prescribed by the registrar; and
  - (b) describes how the code of conduct will be enforced.
- (2) A credit rating agency must publish any changes to its code of conduct.

**Comment [N20]:** A requirement for a CRA to provide an explanation of the key elements of a credit rating “so that an investor, potential investor or member of the public is able to understand” is a standard that is unachievable because this is based on an objective criterion. Although we strive for our credit ratings to be understandable to the intended audience, no amount of information will ensure that the category of persons understand a particular rationale for a credit rating.

**Comment [N21]:** Please see Note 10.

(3) A credit rating agency must publish on an annual basis any material deviations of its code of conduct from that of the code of conduct prescribed by the registrar in subsection (1) (a) and the reasons therefor.

### Outsourcing and other services

12. (1) A credit rating agency may not, without ~~the~~ prior written notification to approval ~~of~~ the registrar, outsource any of its operational functions, save for outsourcing to an entity in the same group as the credit rating agency.

(2) A credit rating agency may provide services ancillary to its credit rating services, as prescribed by the registrar.

### Disclosures

13. (1) A credit rating agency must disclose to the public and its subscribers—

(a) the practices, procedures, processes, methodologies, a description of the models and key rating assumptions it uses in its credit ratings and credit rating services and any material modification thereto;

(b) its code of conduct;

(c) the general nature of its compensation arrangements; and

(d) its policy on publishing credit ratings and other related communication.

(2) A credit rating agency must, every 12 months, disclose to the public and its subscribers data about the historical default rates of its rating categories.

(3) A credit rating agency must provide prominent links to the disclosures contemplated in subsections (1) and (2) on its website.

(4) A credit rating agency must annually disclose to the registrar—

(a) a list of its 20 largest clients, and the percentage of revenue that each of those 20 clients, individually or together with affiliates, contribute to the total annual revenue of the credit rating agency; and

(b) the name of any client who, individually or together with affiliates, contributes more than ten percent to the total annual revenue of the credit rating agency.

### Records

14. A credit rating agency must arrange for adequate records and, where appropriate, audit trails of its credit rating services, which must be kept for a minimum period of ~~five~~ years or such longer period as may be prescribed in any other applicable law.

### Annual report

15. (1) A credit rating agency must annually publish a report to the public, which report must include at least the following:

(a) Detailed information on its legal structure and ownership;

(b) a description of its internal control mechanisms that ensures the quality of the credit rating services;

(c) a description of its record-keeping policy;

(d) ~~the outcome of the annual internal review undertaken by its independent compliance unit;~~

(e) financial information on its revenue sources, divided into fees from credit rating services and non-credit rating services, ancillary services and other services; and

(f) any other prescribed information.

**Comment [N22]:** Models used by CRAs are their intellectual property. Legislatively obliging their disclosure will negatively impact a CRA's competitive ability and may be contrary to South African law creating a form of compulsory licensing, thereby negating any rights to intellectual property. We are also concerned that this outcome would not respect the primacy of our property rights. Contrary to the response of National Treasury to the initial informal public consultation, this is not standard international practice. Attention is drawn to recital 25 of the EU Regulation:

See further, Annex 1, Section E of the EU Regulation which refers to a "description of models " to be published as opposed to the model itself.

We would propose the amendment of this provision to require disclosure of a description of the models used in the assignment of credit ratings.

**Comment [N23]:** Consequential amendment following the amendments to section 16(6).

**Comment [N24]:** It remains unclear what is meant by "ancillary and other services".

(2) The annual report contemplated in subsection (1) must be—

- (a) submitted to the registrar ~~together with the audited financial statements of the credit rating agency;~~ and
- (b) published within three months after the end of each financial year and must remain available on the website of the credit rating agency for at least five years.

**Comment [N25]:** Please see section 17(3) which requires audited financial statements to be submitted to the registrar six months following year-end which would be a more practical regulatory standard.

### Independent compliance unit

**16.** (1) A credit rating agency or the group to which the credit rating agency belongs to, must establish and maintain a permanent, independent and effective compliance unit approved by the registrar.

(2) A credit rating agency must—

- (a) ensure that the compliance unit has the necessary authority, resources, expertise and access to all relevant information; and
- (b) appoint a compliance officer who is responsible for the compliance unit and for any compliance reporting, and inform the registrar of such appointment and the details of that person.

(3) A compliance officer must—

- (a) monitor and report to the registrar on the compliance of the credit rating agency and its employees in respect of the obligations of the credit rating agency under this Act and any codes, policies, procedures or systems required to be established under this Act;
- (b) advise and assist the credit rating agency in complying with its obligations under this Act;
- (c) submit reports directly to the board of the credit rating agency;
- (d) review compliance with policies and procedures to manage conflicts of interest and assess the risk of non-compliance for the integrity of the credit rating process;
- (e) review compliance with internal controls with regard to the procedures and methodologies for determining credit ratings, including quantitative and qualitative models used in the rating process; and
- (f) ~~in consultation with the board of the credit rating agency, resolve, avoid or mitigate any conflicts of interest that may arise~~ refer any material conflicts of interest that the compliance officer becomes aware of to the board of the credit rating agency.

**Comment [N26]:** Many CRA group compliance officers do not report into the boards of directors of any subsidiary of the group. They do however submit reports to the board.

**Comment [N27]:** The responsibility to resolve, avoid or mitigate conflicts of interest should lie with the senior management of a CRA. The compliance officer is responsible for identifying conflicts of interest and in assisting management in resolving or mitigating these conflicts but should not be held responsible for this function, even in consultation with the board of directors.

(4) A compliance officer may not—

- (a) perform credit ratings;
- (b) participate in the development of rating methodologies or models;
- (c) perform marketing or sales functions; or
- (d) participate in establishing compensation levels, other than for employees working for the compliance officer.

(5) The compensation of a compliance officer by the credit rating agency may not be linked to the business performance of the credit rating agency, and shall be structured in a manner that ensures independence of judgment.

- (6) ~~(a) A compliance officer must annually prepare a compliance report on the compliance of the credit rating agency with this Act and any codes, policies, procedures or systems required to be established under this Act.~~
- ~~(b) The compliance officer must submit a compliance report to the registrar, together with the audited financial statements of the credit rating agency.~~
- ~~(7) The compliance officer must submit any other reports to the registrar in a prescribed manner.~~

**Comment [N28]:** Section 32 makes any contravention of the Act a criminal offence. Any report submitted by the compliance officer under section 16 would infringe the CRA's right against self-incrimination as protected under the Constitution. See also subsection (8).

**Comment [N29]:** The proposed subsection amounts to an open-ended power provided to the registrar to prescribe "any other reports". We believe that any such power should be limited in scope to the information or reports prescribed in the resulting Act.

~~(8) Despite anything to the contrary contained in any law, a compliance officer must report to and inform the registrar in writing of any irregularity or suspected irregularity in the conduct or the affairs of the credit rating agency or any breach of this Act.~~

(9) If the appointment of a compliance officer is terminated, the compliance officer must—

(a) submit to the registrar a statement of what the compliance officer believes to be the reasons for that termination; and

~~(b) if the compliance officer would, but for that termination, have had reason to submit to the registrar a report contemplated in subsection (8), submit such a report to the registrar.~~

~~(10) The registrar may direct a credit rating agency to terminate the appointment of a compliance officer, if the compliance officer fails to comply with any provision of this section in a material manner.~~

**Comment [N30]:** Consequential change to proposed amendment to section 16(8) of the Act.

**Comment [N31]:** If this section is retained we would propose that same administrative protections offered to the directors of the CRA as proposed under the revised section 8 of the Bill should be apply to a compliance officer if that officer breaches section 16 in a material manner.

### Accounting and auditing requirements

17. (1) Except to the extent exempted by the registrar, a credit rating agency must annually prepare, in respect of the relevant financial year of the credit rating agency, financial statements reflecting—

(a) the financial position of the credit rating agency at its financial year-end;

(b) the results of operations, the receipt and payment of cash and cash equivalent balances;

(c) all changes in equity for the period then ended, and any additional components required in terms of International Financial Reporting Standards issued by the International Accounting Standards Board or a successor body; and

(d) a summary of significant accounting policies and explanatory notes on the matters referred to in paragraphs (a) to (c).

(2) A credit rating agency must cause the statements contemplated in subsection (1) to be audited and reported on by an external auditor in accordance with auditing pronouncements as defined in section 1 of the Auditing Profession Act, 2005 (Act No. 26 of 2005).

(3) The credit rating agency must submit its audited financial statements to the registrar within six months after its financial year-end.

(4) The provisions of section 16 (8), (9) and (10) apply, with the necessary changes, to the external auditor of a credit rating agency.

## CHAPTER 4

### ENDORSEMENT OF EXTERNAL CREDIT RATINGS

**Comment [N32]:** Please see paragraph I in the Cover Letter.

#### Requirements for endorsement of external credit ratings

~~18. (1) A credit rating agency may, subject to the approval of the registrar, endorse credit ratings issued by an external credit rating agency in countries other than the Republic for use in the Republic, if —~~

~~(a) the credit rating services resulting in the issuing of the credit rating to be endorsed are undertaken partly or entirely—~~

~~(i) by the credit rating agency; or~~

~~(ii) by an external credit rating agency belonging to the same group as that credit rating agency;~~

~~(b) the credit rating agency has verified and is able to demonstrate on an ongoing basis to the registrar that the external credit rating agency is authorised or registered by a regulatory authority to perform credit rating services similar to those regulated under this Act and is subject to the laws of a country other than the Republic, which laws —~~

~~(i) establish a regulatory framework equivalent to that established by this Act; and~~

~~(ii) are supervised by a regulatory authority;~~

~~(c) the ability of the registrar to assess and monitor the compliance of the external credit rating agency with the regulatory framework referred to in paragraph~~

- ~~(b) is not limited;~~  
~~(d) the credit rating agency provides the registrar, on the registrar's request, with all information necessary to enable the registrar to monitor, on an ongoing basis, compliance with this Act;~~  
~~(e) there is an objective reason for the credit ratings to be issued in a country other than the Republic, or by an external credit rating agency; and~~  
~~(f) an agreement contemplated in section 29 has been entered into between the registrar and the relevant regulatory authority of the external credit rating agency, which agreement, at least, provides for—~~  
~~(i) mechanisms for the exchange of information; and~~  
~~(ii) procedures for the coordination of regulatory activities to facilitate the monitoring of credit rating activities resulting in the issuing of the endorsed credit rating on an ongoing basis.~~
- ~~(2) A credit rating endorsed under this section is deemed—~~  
~~(a) to be a credit rating issued by a credit rating agency registered under this Act; and~~  
~~(b) to have been issued when the credit rating is published on the website of the credit rating agency or by other means, or is distributed by subscription and presented and disclosed in accordance with the requirements of this Act.~~
- ~~(3) A credit rating agency that endorsed a credit rating under this section remains fully responsible for that credit rating and for compliance with this Act.~~
- ~~(4) (a) A credit rating agency must apply to the registrar in the manner prescribed, for the approval of the external credit rating agencies whose credit ratings it intends to endorse under this section.~~  
~~(b) If the registrar is of the opinion that a credit rating cannot be endorsed in accordance with this section or the requirements of this Act, the registrar may instruct the credit rating agency not to endorse the credit rating.~~
- ~~(5) A credit rating agency may not use endorsement with the intention of avoiding the requirements of this Act.~~

## CHAPTER 5

### LIABILITY AND INDEPENDENCE OF CREDIT RATING AGENCIES

#### Liability of credit rating agencies

19. (1) The delictual liability of a credit rating agency that issues a credit rating or performs credit rating services is limited to liability arising directly from wrongful intent, fraud or gross negligence only may be delictually liable to an investor or a member of the public, in respect of a credit rating issued or credit rating services performed in the ordinary course of business in terms of this Act, for any loss, damages or costs sustained as a result of such credit rating or a credit rating service.

(2) Subsection (1) does not affect any additional or other liability of a credit rating agency to an investor or member of the public, arising from a contractual relationship or the application of any law other than this Act.

~~(3) A credit rating agency may not, through a contract, agreement or in any other way, limit or reduce the liability that such credit rating agency may incur in terms of this subsection (1) or in terms of the common law.~~

(3) Subject to subsection (1), a contravention of any provision of this Act does not give rise to any right of action for damages by any person.

#### Independence

20. No person, including the registrar, may hinder, interfere with, obstruct or improperly attempt to influence a credit rating, the content of a credit rating, or any methodology, model or key assumption used by a credit rating agency to derive a credit rating.

Comment [N33]: Please see paragraph II in the Cover Letter.

## CHAPTER 6

### ADMINISTRATION OF ACT

#### Registrar and deputy registrar of credit rating agencies

21. The executive officer and deputy executive officer contemplated in section 1 of the Financial Services Board Act are the registrar and deputy registrar of credit rating agencies, respectively, and have the powers and functions provided for under this Act or any other applicable law.

#### Delegation and assignment

22. (1) The registrar may in writing—

(a) delegate any of the powers and functions assigned to the registrar under this Act; and  
(b) assign any of the duties or functions imposed on the registrar under this Act, to a deputy registrar or any other person, except the power to make rules and issue a directive.

(2) The delegation or assignment contemplated in subsection (1)—

(a) is subject to any limitations or conditions that the registrar may impose; and  
(b) does not divest the registrar of the responsibility concerning the exercise of the delegated power.

(3) The registrar may confirm, vary or revoke any decision taken by a deputy registrar or any other person, subject to any rights that may have vested as a consequence of the delegation.

#### Powers and functions of registrar

23. (1) The registrar, in addition to the other powers and functions conferred on the registrar in terms of this Act, and subject to subsection (2) and section 20—

- (a) must supervise and enforce compliance with this Act;
- (b) must take such steps as the registrar considers necessary, in accordance with the requirements of this Act and other applicable legislation, to protect investors in their dealings with credit ratings, credit rating services and credit rating agencies;
- (c) may by notice require any person, including a credit rating agency, to furnish the registrar, within a specified period, with specified information or documents reasonably necessary for exercising his or her powers under this Act;
- (d) may impose conditions that are consistent with this Act in respect of any registration or approval granted or requirement imposed by the registrar, and may amend or withdraw such conditions;
- (e) may, on the written request of a credit rating agency, extend any period within which any documentation, information or report must be submitted to the registrar;
- (f) must determine the ~~form, manner and~~ period, if a period is not specified in this Act, within which any documentation, information or report that a credit rating agency is required to publish, disclose, provide or submit under this Act must be published, disclosed, provided or submitted;
- (g) may, despite the provisions of any law, furnish information acquired by the registrar under this Act to any person charged with the performance of a function under any law, including a regulatory authority and provided that such person to which the disclosure is made is an organ of state which undertakes to keep such information confidential save to the extent necessary to perform such function;
- (h) may issue guidelines on the application and interpretation of this Act; and
- (i) may take any measures that the registrar considers necessary for the proper performance and exercise of the powers and functions of the registrar for the implementation of this Act, in accordance with the requirements of this Act and other applicable legislation.

Comment [N34]: Please see note 4.

Comment [N35]: The relevant regulatory authority may not have the necessary defences to protect confidential information in the case of a request for such information thereby exposing otherwise confidential information to public disclosure.

(2) The registrar must, in performing his or her powers and functions under this Act or any other applicable law—

(a) act in a manner which—

- (i) is compatible with the objects of this Act; and
- (ii) is most appropriate for meeting the objects of this Act; and

(b) have regard to—

- (i) international supervisory standards;
- (ii) the principle that a restriction which is placed on a credit rating agency, the issuing of credit ratings or the performance of credit rating services, should be proportionate to the purpose for which it is intended;
- (iii) the international nature of credit rating agencies, credit ratings and credit rating services;
- (iv) the principle that competition between regulated persons should not be impeded or distorted; and
- (v) the need to use resources in the most effective and cost-efficient manner.

## Rules

24.(1) Subject to section 20, the registrar may, by notice in the *Gazette*, make rules **within the scope of this Act** with regard to—

- (a) organisational requirements for credit rating agencies;
- (b) the independence of credit rating agencies and the avoidance of conflicts of interest by credit rating agencies;
- (c) the quality and integrity of credit ratings;
- (d) the presentation of credit ratings;
- (e) additional obligations in relation to credit ratings of structured finance instruments;
- (f) ~~the design of methodologies and models;~~
- (g) ~~rating assumptions;~~
- (h) additional disclosures;
- (i) adequate and appropriate record-keeping;
- (j) fraudulent and misleading advertising, canvassing and marketing;
- (k) ~~suitable guarantees, professional indemnity or fidelity insurance cover, and mechanisms for adjustments of such guarantees or cover;~~
- (l) the control or prohibition of incentives given or accepted by a credit rating agency;
- (m) ~~the responsibilities of credit rating agencies to investors and the public;~~ and
- (n) any matter that the registrar is required or permitted to prescribe in terms of this Act.

(2) The rules contemplated in subsection (1)—

- (a) apply to credit rating agencies, credit ratings, ~~endorsed credit ratings~~ or credit rating services generally; and
- (b) are limited in application to a particular type of credit rating agency, credit rating or credit rating services.

(3) (a) Before the registrar makes any rule under this section, the registrar must publish a draft of the proposed rule in the *Gazette*, together with a notice calling for public comment in writing within a period stated in the notice, which period may not be less than 30 days from the date of publication of the notice.

(b) If the registrar alters a draft rule because of any comment, the registrar need not publish the alteration before making the rule.

**Comment [N36]:** The following categories of rules are concerning:

1. Independence concerns: rules on the design of methodologies and models, rating assumptions.
2. Scope concerns: professional indemnity or fidelity insurance (where it is unclear why this is needed given the role of CRAs).

~~(4) The registrar may, within the scope of this Act and in exceptional circumstances relating to the potential for market disruption or financial instability and provided that, if in the opinion of the registrar it would impair the achievement of the objects of the Act if a rule is not published immediately, publish that rule without complying with subsection (3)(a), provided that the notice of publication indicates—~~

~~(a) the reason why circumstances necessitated publication of the a rule without giving notice as contemplated in subsection (3)(a); and~~

~~(5b) that a—Any person who is aggrieved by the rule in subsection (4) may make representation to the registrar within a period stated in the notice, which may not be less than 30 days from the date of publication of the notice.~~

### Inspections and on-site visits

~~25. (1) The registrar may—~~

~~(a) authorise any suitable person to conduct an on-site visit of the business of a credit rating agency to determine compliance with this Act; and~~

~~(b) instruct an inspector appointed in terms of section 2 of the Inspection of Financial Institutions Act, 1998 (Act No. 80 of 1998), to carry out an inspection as contemplated in section 3 of that Act.~~

~~(2) A person conducting an on-site visit in terms of subsection (1)(a) may—~~

~~(a) at any time during business hours—~~

~~(i) enter the premises of the credit rating agency or associate for the purpose of ensuring compliance with this Act;~~

~~(ii) search the premises of the credit rating agency or associate for any document that contains any information relevant to the administration or enforcement of this Act, and the credit rating agency or associate must, upon request, provide any such document;~~

~~(iii) examine, make extracts from and copy any such document or, against the issue of a receipt, temporarily remove the document; or~~

~~(iv) seize any document against the issue of a receipt, which document indicates proof of failure to comply with any provision of this Act;~~

~~(b) require the credit rating agency or associate to produce at a specified time and place any specified documents of a specified description in the possession or under the control of the credit rating agency or associate; or~~

~~(c) require any person to provide any relevant and necessary information, and an explanation of that information.~~

~~(3) After an on-site visit or inspection has been carried out in terms of subsection (1), the registrar may direct the credit rating agency or associate concerned to take any steps, to refrain from performing or continuing to perform any act, or to terminate or remedy any contravention of or failure to comply with any provision of this Act.~~

~~(4) The registrar may, by notice on the FSB official website, or by means of any other appropriate public media, make known—~~

~~(a) the status and outcome of an inspection;~~

~~(b) the details of an inspection, if disclosure is in the public interest;~~

~~(c) the outcome and details of an on-site visit, if disclosure is in the public interest.~~

### Directives

~~26. (1) The registrar may, in order to ensure proper implementation and administration of this Act, or to protect investors and the public in general, issue a directive to a credit rating agency—~~

~~(a) to implement specific practices, procedures or processes;~~

~~(b) to take specific actions or measures;~~

~~(c) to desist from undertaking specific practices, procedures, processes, actions or measures; or~~

**Comment [N37]:** There is no objection to the registrar being empowered to publish subordinate legislation on an expedited manner if exceptional circumstances warrant. However, it must be recognised that such an expedited procedure is a limitation of a right otherwise afforded to a CRA under the resulting Act. It is therefore proposed that the resulting Act permit the adoption of this expedited procedure only in exceptional circumstances.

**Comment [N38]:** Person conducting the inspection

The Inspection of Financial Institutions Act, 1998 (“the FI Act”) contains a detailed legislative framework for the appointment of an inspector by the registrar. The framework governing an inspection by the registrar should fall within the scope of the FI Act.

Publication of inspection

Although we understand that the power afforded to the registrar to publish details of the existence of an inspection or the outcome of the inspection prior to any enforcement action and prior to the necessary administrative law rights of the defendant being duly exercised is a similar provision found in other laws administered by the FSB, we believe that the standard proposed in the Bill is too low.

The proposal in the Bill that provides for an announcement of the commencement of any inspection has the potential to materially affect the reputation and therefore business interests of the affected CRA. Furthermore, this seems to be in direct contrast to the requirements under section 6(3)(c) of the Bill which prohibits the registrar from publishing a decision subject to an appeal.

**Comment [N39]:** The registrar should only be permitted to issue a directive in order to ensure the implementation of the resulting law. Therefore, it would appear therefore that the additional power granted under this section “to protect investors and the public in general” is overly broad and potentially grants unlimited power to the registrar to issue directives that go beyond the limits of subordinate legislation.

(d) generally prohibiting certain practices, procedures, processes, actions or measures.

(2) A directive contemplated in subsection (1) may—

- (a) apply to credit rating agencies, credit ratings or credit rating services generally;
- (b) apply to a specific credit rating agency, credit rating or credit rating service; or
- (c) be limited in its application to a particular type of credit rating agency, ~~whether local or external~~, a credit rating service published or performed in the Republic, or a credit rating, whether relating to an opinion regarding—
  - (i) an entity;
  - (ii) securities or a financial instrument; or
  - (iii) an issuer of securities or a financial instrument.

(3) A directive issued in terms of subsection (1) takes effect on the date determined by the registrar in the directive, and may take effect immediately.

(4) The registrar may amend, cancel or revoke any previously issued directives.

(5) The registrar must, where a directive is issued to ensure the protection of investors, potential investors or the public in general, publish the directive in the *Gazette* and in any other media that the registrar deems appropriate.

## Exemptions

**27.** (1) The registrar may exempt any credit rating agency or external credit rating agency from, or in respect of, any provision of the Act or allow that a duty imposed under this Act be fulfilled by a person in the same group of a credit rating agency if the registrar is satisfied that—

- (a) practicalities impede the strict application of a specific provision of the Act; and
- (b) the granting of the exemption will not—
  - (i) conflict with the public interest;
  - (ii) unduly prejudice the interests of—
    - (aa) the clients of credit rating agencies;
    - (bb) the users of credit ratings or credit rating services; or
    - (cc) regulatory authorities that rely on, refer to or use credit ratings in their supervision and regulation activities; and
  - (iii) frustrate the achievement of the objects of this Act.

(2) An exemption contemplated in subsection (1) may apply to credit rating agencies generally or a specific credit rating agency, or may be limited in its application to a particular type of credit rating agency.

(3) The registrar may, at any time by notice to the credit rating agency or external credit rating agency concerned on the FSB official website, withdraw, wholly or in part, and on any ground which the registrar deems sufficient, any exemption granted under subsection (1).

## Fees and penalties

**28.** (1) (a) The registrar may by notice on the FSB official website determine the fees payable to the registrar by any person, or category of persons seeking a decision, applying for registration or the performance of any other act by the registrar under this Act, and the registrar may in a similar manner amend, substitute or withdraw any such notice.

(b) The fees are payable in the manner, and are subject to the requirements, determined by the registrar by notice on the FSB official website.

**Comment [N40]:** Please see our comments in paragraph I of the Cover Letter.

Furthermore, the standard imposed on the registrar is likely to be too restrictive and we propose minor qualifying wording to give effect to the intention of the section.

Finally, we propose a formal clarification in the resulting Act that a CRA may, subject to the approval of the registrar, leverage the resources of its group companies to comply with the resulting Act.

(2) (a) A person who is liable to pay the fees contemplated in subsection (1)(a) and who fails to pay the amount due on the date or within the period specified, must pay interest on the amount outstanding at the prescribed rate.

(b) The fees and interest owed in respect thereof are regarded as debts due to the registrar and may be recovered by the registrar by way of a judicial process in a competent court.

(3) The registrar may impose an administrative penalty on a credit rating agency for failure to submit, to the registrar within a period specified in terms of this Act, any statement, report, return or other document or information required to be submitted in terms of this Act, such penalty to be prescribed by the registrar for every day during which the failure continues.

(4) The registrar must, before imposing a penalty, by written notice to the credit rating agency—

(a) inform the credit rating agency of the intention of the registrar to impose a penalty;

(b) specify the particulars of the alleged failure;

(c) set out the reasons for the intended imposition of a penalty;

(d) specify the amount of the penalty intended to be imposed; and

(e) call upon the credit rating agency to show cause within a period specified by the registrar why the penalty should not be imposed.

(5) If the registrar, after consideration of representations made by the credit rating agency, decides to impose a penalty, the registrar must notify the credit rating agency in writing that it may—

(a) pay the penalty within a stipulated period; or

(b) appeal to appeal board in accordance with section 33 against the imposition of the penalty.

(6) If a credit rating agency fails to pay the penalty or to note an appeal within the periods stipulated in the notice contemplated in subsection (5), the registrar may, by way of civil action in any competent court, recover the amount of the penalty from the credit rating agency concerned.

### **Cooperation with regulatory authorities**

**29.** (1) The registrar may—

(a) liaise with any regulatory authority on matters of common interest;

(b) negotiate agreements with any regulatory authority to—

(i) coordinate and harmonise the reporting and other obligations of credit rating agencies, external credit rating agencies and groups as defined in section 1;

(ii) provide mechanisms for the exchange of information in accordance with domestic law; and

(iii) provide procedures for the coordination of regulatory activities to facilitate the monitoring of credit rating activities resulting in the issuing of the endorsed credit rating on an ongoing basis;

(c) participate in the proceedings of any regulatory authority; and

(d) advise or receive advice from any regulatory authority.

(2) The registrar may, without detracting from the generality of subsection (1), enter into a written agreement, including a memorandum of understanding, with a foreign regulatory authority in whose country a subsidiary or holding company of a credit rating agency is incorporated, which cooperation agreement may include—

(a) a provision that the registrar or foreign regulatory authority may conduct an on-site examination or an inspection of a credit rating agency, or external credit rating agency or any member of a group as defined in section 1;

(b) a provision that the registrar and foreign regulatory authority may share information relating to the financial condition and performance of the institutions contemplated in paragraph (a);

(c) a provision that the registrar or foreign regulatory authority—

(i) be informed of adverse assessments of qualitative aspects of the operations of a credit rating agency or the institutions contemplated in paragraph (a); or

(ii) may provide information regarding significant problems that are being experienced within a credit rating agency or the institutions contemplated in paragraph (a); and

(d) such other matters as the registrar may deem relevant.

(3) The registrar shall ensure that in dealing with foreign regulatory authorities under subsections (1) and (2) all information disclosed to a foreign regulator-

(a) is necessary for the supervisory activities of the foreign regulator;

(b) falls within the powers of competence of the foreign regulator to request such information in its own jurisdiction; and

(c) is subject to protection of confidentiality provisions equivalent to the protection afforded to information disclosed to the executive officer under the Financial Services Board Act.

## CHAPTER 7

### ENFORCEMENT ACTIONS AND REMEDIES

#### Enforcement committee

30. The registrar may, despite and in addition to taking any step that the registrar may take under this Act, refer any contravention of this Act to the enforcement committee established in terms of section 10(3) of the Financial Services Board Act.

#### Civil action

31. The registrar may, when satisfied on the basis of available facts and information that a person has contravened ~~or not complied with any provision of this Act~~, or is likely so to contravene ~~or not to comply~~, apply to a court for an order—

(a) restraining such person from continuing to commit any such act or omission;

(b) restraining such person from committing such an act in future; or

(c) requiring the person to take such remedial steps as the court deems necessary to rectify the consequences of the act or omission.

#### Offences and penalties

32. Any person who—

(a) ~~deliberately~~ contravenes ~~or fails to comply with a provision of~~ sections 3(2) or 4 ~~or any other provision~~ of this Act;

(b) deliberately makes a materially misleading, false or deceptive statement, or ~~deliberately~~ conceals any material fact with respect to any information required to be disclosed under this Act; or

(c) in the execution of duties imposed by this Act, ~~deliberately~~ gives an auditor or compliance officer information which he or she knows to be ~~is~~ false ~~or~~ misleading or knowingly conceals any material fact, is guilty of an offence and on conviction liable to a fine or to imprisonment for a period not exceeding 10 years or to both a fine and such imprisonment.

Although we recognise that such protections are entrenched in the IOSCO Multilateral Memorandum of Association, this MMoU is of limited scope and does not govern bilateral information sharing relationships between regulators.

**Comment [N42]:** The extension of this section will effectively result in a criminal offence for any breach of the resulting Act. This, coupled with the lack of a state of mind test in many of the provisions, is unduly severe and disproportionate. Please see paragraph III in the Cover Letter.

## Right of appeal

33. (1) Whenever the registrar makes a decision in terms of this Act which adversely affects the rights of a person, the registrar must inform the affected person of that person's right to appeal in accordance with section 26 of the Financial Services Board Act.

(2) Any person who feels aggrieved by any decision of the registrar made in terms of this Act, may appeal in the prescribed manner to the appeal board established in terms of section 26(A) of the Financial Services Board Act, and in accordance with section 26 of that Act.

## CHAPTER 8

### GENERAL PROVISIONS

#### Regulations

34. The Minister may make regulations not inconsistent with this Act with regard to any matter that is required or permitted to be prescribed in terms of this Act.

#### Saving of rights

35. Subject to section 19 of this Act, no provision of this Act, and no act performed under or in terms of any provision thereof, may be construed as affecting any right of a person to seek appropriate legal redress in terms of common law or any other relevant legislation, whether relating to civil or criminal matters, in respect of a credit rating or credit rating agency.

#### Transitional measures

36. (1) Credit rating agencies providing credit rating services in South Africa before 1 January 2012 which intend to apply for registration under this Act, shall adopt all necessary measures to comply with its provisions within twelve (12) months of the date of commencement of this Act.

(2) Credit rating agencies shall submit their application for registration within six (6) months from the date of commencement of this Act.

(3) Credit rating agencies falling under subsection (1) may continue issuing credit ratings which may be used for regulatory purposes unless registration is finally refused after an appeal in terms of section 33 or if no appeal against the registrar's refusal is made within the required period for an appeal. Where registration is finally refused after an appeal in terms of section 33 or if no appeal against the registrar's refusal is made within the required period for an appeal, section 6 shall apply.

#### Amendment of law

36. The law referred to in the Schedule is hereby amended to the extent specified in the third column thereof.

#### Short title and commencement

37. This Act is called the Credit Rating Services Act, 2012.

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#### End Note:

#### Note on "plain language" requirement under section 1(5) of the Bill

The "plain language" requirement in section 1(5) of the Bill is unnecessary and could lead to confusion among market participants about how credit ratings should and should not be used. The concern regarding this requirement is listed below:

**Comment [N43]:** CRAs have been conducting credit rating services in South Africa for a long period and the resulting Act requires a transitional mechanism to allow time for an application for registration to be prepared and for these CRAs to adjust any processes to comply with the resulting Act.

First, it is unnecessary because financial market professionals have the resources and power to request that CRAs communicate their opinions in a way that these professionals find useful. Simply put, if a CRA does not communicate its opinions in a way that market professionals find helpful, the credit ratings will not be used and issuers will not request ratings from the CRA.

Second, the “plain language” requirement could lead to confusion among market participants about how credit ratings should, and should not, be used. Plain language requirements in financial services regulation typically are associated with products and services intended for use by retail customers. Credit ratings are designed for use by market professionals. Such an interpretation could result to CRAs being encouraged or required to over-simplify a necessarily complex analysis, which would not benefit the market as a whole.

Third, a requirement to meet plain language standards implies that the FSB will monitor CRAs’ compliance with such a requirement. It would be very difficult for the regulator to conduct such a review without evaluating and commenting on about the meaning of words used in such publications. This would jeopardise one of the key attributes of credit ratings and could potentially lead to market participants discounting the credibility of credit ratings produced in South Africa.

Finally, neither the International Organization of Securities Commissions (“IOSCO”) *Code of Conduct Fundamentals for Credit Rating Agencies* (“IOSCO Code”), the *European Regulation on Credit Rating Agencies*, nor the rules adopted by the United States Securities and Exchange Commission impose plain language requirements on CRA publications. For the reasons set out above, therefore, we recommend that these provisions in the Bill be deleted.

In its response document to submissions received during the informal consultation on the Draft Bill, National Treasury stated that the intention behind this paragraph is to protect trustees of pension funds who may not be finance market professionals. It is not appropriate for trustees to rely solely on the opinion of a CRA and a CRA’s opinion should form part of a toolbox of measures that a trustee or other investor should consider before making an investment. If a trustee does not understand the opinion of the CRA they should take professional advice as to the meaning of such an opinion. Although we strive to make our credit ratings understandable to users we do not believe that the standard, which is better suited to the retail consumer market, is appropriate as a legislative standard for CRAs.

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