Plenary 2

Regulating Credit Rating Agencies

Mr. David Brown

Chair of the Ontario Securities Commission

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Panel Discussion
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"Regulating Credit Rating Agencies"

Speaking notes of David A. Brown, Moderator

- A few brief opening remarks to set the stage
    - Have asked the panelists to speak for about 10 minutes each
    - Then open the subject to discussion among panelists and members of the audience
- Credit ratings have long been an important component of the process of capital raising and capital allocation
    - Issuers and corporate borrowers rely on them to help raise capital – to the extent credit ratings can help remove some of the uncertainties about an issuers future ability to service its instruments, the cost of capital should be reduced
    - Lenders and investors use credit ratings in assessing the risks of lending money to an issuer – Credit Rating Agencies help to redress some of the information asymmetry in the marketplace – collect and review information about the issuer, the market in which the issuer operates and the overall economy
    - Institutional investors and fiduciary investors (such as managers of trust funds or pensions) use CRA ratings to allocate investments in a diversified risk portfolio
    - Government regulators use them for a variety of purposes, including in setting minimum capital requirements for financial sector intermediaries
- In discussing the role of Credit Rating Agencies it is important to understand what a credit rating is, and just as importantly what it is not
    - What it is:
        - an assessment of the probability that an issuer will make timely payments on future financial obligations

- It is not:
    - a credit history listing past defaults or failures; this is more the purview of credit bureaus
    - not a buy or sell recommendation such as are issued by securities analysts
    - not an opinion on the value of our issuer's equity securities
- In short – a CRA rating is a probabilistic opinion about future credit risk

* Following the massive corporate failures in the US in late 2001 and early 2002, the roles of CRAs came under government and market scrutiny. Although this review started in the US, it was quickly taken up by other countries in which credit ratings played an important role in their markets.

* To assist in this process and provide a global perspective, the IOSCO Technical Committee formed a Task Force to examine key issues regarding the role CRA's play in securities markets

* Last month, the Technical Committee published a Report describing the functions and operations of CRAs and the ways in which market participants rely on them. The Report also provides an overview of factors for securities regulators to consider in deciding whether, and if so how, to regulate CRAs and to use credit ratings in securities regulation

* Perhaps more importantly, the Technical Committee released at the same time a "Statement of Principles Regarding the Activities of Credit Rating Agencies". These principles set out high level standards in four key areas that are intended to improve investor protection and market transparency.

* We are fortunate that our hosts have assembled a distinguished panel of experts representing a cross-section of participants in this debate
    - Raymond McDaniel is President of Moody's Investor Services Inc.
    - Vickie Tillman is Executive Vice President of Standard & Poor's and heads up S & P's Ratings Services
    - Naohiko Matsuo is with the Financial Services Agency in Japan and was a member of the IOSCO Task Force on CRAs
    - Kwang Chung is with Korea Corporate Governance Service and is a professor of Business Administration at Chung-Agu University, Korea

- The panelists will give some opening remarks on their perspectives on the role of CRAs and some of the issues dealt with in the IOSCO Principles and Report.

- I expect we'll see a divergence of views on some of the key elements of this debate

- Most financial services regulators do not regulate credit rating agencies

  - One of the questions left open in the IOSSCO Technical Committee Report in whether CRAs should be regulated

  - I'm sure our panelists will have some views on this issue

  - Not wishing to leave anything to chance, our hosts have titled this panel "Regulating Credit Rating Agencies"