

Response to the call for Evidence on competition, choice and conflicts of interest in the credit rating industry

The AFTE (French Association of Corporate Treasurers) welcomes the opportunity to comment on this consultation.

Created in 1976, AFTE (French Association of Corporate Treasurers) AFTE represents around 1 000 corporate treasurers or financial managers of approximately 800 industrial and commercial companies or groups.

AFTE will respond to the following questions:

- 2 to 18 (except 7)
- 22 to 27

Q2: Please explain whether you issue instruments requiring credit ratings at local, national, EU and/or global level. If your organisation issues financial instruments at EU or global level, please provide a list of the jurisdictions in question.

Most of our members are rated as companies and also ask for the rating of their debt instruments of different natures:

- Issuance of bonds within an EMTN Program or not. Issuance of bonds on "foreign markets" such as the US market, the GBP market, the Chinese RMB market, and potentially any other specific currency markets where a bond market is developed or developing ...
- Issuance of French Billets de Trésorerie / more rarely US Commercial papers
- upon specific request from an investor, for a private placement
- for hybrid bond issuances

Q3: What criteria to do you use to select a CRA? Do you use different CRAs to rate different instruments and/or in different jurisdictions? If so, please explain whether, and if so how, your criteria vary.

Criteria used to select a CRA are :

- recognition of the CRA among investors (mentioned as the most important criteria by our members)
- understanding of the industry and business model
- coverage in terms of business and geographies
- pricing

Q4: How many ratings do you solicit for each type of instrument you want to market in each jurisdiction? If more than one, please explain why.

Unless mandatory for legal reasons, some companies only ask for 1 rating.

It could be the investor's interest to rely on two independent credit opinions rather than only one.

In fact, a number of our rated members are rated by two different rating agencies (on a solicited basis). The major reason is to be in line with what people feel are a normal "market standard" i.e. give two credit opinions rather than one. It is also seen as a guarantee of a "balanced" treatment in case one rating agency would have a very different approach of the industry or the company from another one.

Q5: When you seek multiple ratings for certain types of instrument, please explain:**(1) The criteria you use to choose which CRA(s) to engage to rate different types of instruments.**

See Q3

(2) How many CRAs can currently meet these criteria in your view, and why other CRAs cannot meet these criteria.

Only few CRAs have been identified to meet criterias for French companies needs. Because recognition is the major criteria, so far, most of our members are rated by S&P and Moody's and, to a lesser extent, Fitch.

They are currently the only CRAs with a strong brand awareness among investors, thanks to their track record and long history in credit rating.

However AFTE is following very carefully through its "Rating Working Group" the offer which is currently being developed by newly ESMA registered rating agencies

(3) Whether you apply the same criteria to select all of the CRAs engaged or whether you select a main CRA and then one or more secondary CRAs using different criteria. In particular, please explain whether the market share of the primary and/or secondary CRAs plays a part in this decision.

Same criteria are applied by our members in the selection of any of their CRA. The market share is indeed seen as one of the market recognition element of the CRAs as well as the way investor make reference to the major rating agencies in their communications with our companies.

Q6: Under which circumstances would you consider seeking ratings from a CRA which has not previously rated a particular asset class? Please give reasons for your answer.

Our members would not consider a CRA without any experience in a particular asset class.

Q8: Please explain how the prices of credit ratings and the other products and services provided by CRAs have changed since 2010.

CRAs have significantly increased their prices overtime and especially since 2010. This increase does not reflect neither any additional work performed by CRAs nor additional information (provided to rated companies or investors).

Their "pricing" practice is being challenged by a number of our rated members which, as much as practicable, try to negotiate their own rating costs in a rather constrained context ("yearly price list sent by rating agencies to their customers).

CRA's have been claiming in the recent past that increased regulatory pressures were impacting their costs. While rated companies can understand the point, they have not access to enough information on the CRA's P&L structure to judge it.

Q9: Please explain how you would respond if your preferred CRA(s) increased the costs of providing credit ratings for different asset classes by 5-10%. If your answer would differ depending on the jurisdiction or asset class in question, please explain why.

AFTE would first recommend companies to investigate the rationale behind the price increase and then to negotiate prices. It is worth noting that "AFTE Rating Commission" has already called on a CRA which "fee schedule" was unilaterally very significantly increased to communicate the companies' reaction to such a practice. However, companies are aware that it cannot easily withdraw a rating without having to face market reactions and feel they have at the end to come to an agreement with their CRA. This is the reason why we were mentioning earlier that companies were in a "constrained" environment: (1) CRA's issue updated fee schedule on a yearly basis and send them to the rated companies as the new "standard fee" and (2) rating withdrawal is a major decision for a company and is indeed very rare.

Q10: Please explain the impact on your business of the following obligations and provide an estimate of your costs of complying with each of these obligations from 2013 to present where possible:

(1) to appoint at least two CRAs to provide ratings of structured finance instruments; and

AFTE members do not feel really concerned by this requirement as, indeed, they rarely issue structured instruments.

(2) to document the CRAs appointed.

Documentation is adding to the administrative tasks that companies have to fulfil. AFTE is concerned by the increasing administrative burden that companies are subject to. AFTE would therefore ask ESMA to really take this factor into consideration when issuing instructions to the market authorities.

Q11: Do you provide information to CRAs who issue ratings by subscription which are paid for by investors as well as for the ratings that you pay for? What are the advantages and disadvantages of these different business models from your perspective?

AFTE has not access to detailed information on detailed CRA'S P&L. AFTE understands however that investors need to subscribe and pay for CRA's services as soon as it needs to access not only the ratings themselves (which can be considered as public information overtime) but to rating analysis and rating analysts.

AFTE considers that while the issuer pay model is not ideal the investors only pay model may not unfortunately be a better solution because AFTE fears that it may lead to a reduction of coverage, especially for medium size companies.

AFTE recalls that its members can also be seen as "users" of rating services especially when it comes to measure their potential counterparty risks either with banks and Financial Institutions or with their various suppliers. Group treasurers are indeed especially interested in following their banks status in terms of ratings.

The methodology of the CRA is the key factor. AFTE considers it useful that the regulator performs periodical controls to guarantee the compliance with the methodology and guarantee that there is no conflict of interest in ratings.

Q12: Please explain whether there are other models which would allow CRAs to seek payment for the credit ratings they issue, giving reasons for your answer.

A better split of CRA's revenues between issuers and investors could be an interesting route to pursue should it be really unbalanced currently: AFTE indeed believes that ratings serves equally the need of issuers and investors on the financial markets.

Q13: What are the average durations of your agreements with CRAs for credit ratings and your agreements with CRAs for ancillary services? Please explain whether this differs by asset class and/or jurisdiction and how this has changed since 2010.

Our members mentioned contracts from 1 to 3 years.

Q14: Please describe the process you would typically follow when seeking a credit rating for a new financial instrument you wished to market, explaining how this process has changed since 2010, if at all. In particular:

(1) how many CRAs you would contact or hold preliminary discussions with:

AFTE members would contact their CRA(s) exclusively. For structured instruments AFTE members rarely issue them. They understand that they would need to have two ratings in such case and

therefore may need to appoint a new CRA if they had only one. AFTE members are therefore concerned by the additional cost incurred.

(2) how you would compare the ratings and ancillary services being offered by different CRAs.

AFTE members see in fact few "ancillary services" except:

- 1) Shadow ratings which AFTE members see as potentially useful and interesting . AFTE sees it as a potentially interesting information for a company. AFTE recalls that it considers that the publication of a rating by a Company is a financial strategic decision which must be left at the Company's initiative exclusively.
- 2) "Rating Assessment Services" which are named differently by the CRA's but consist into offering access to the rating potential consequences of company's strategical decisions. These services are solicited usually in a very short time frame. CRA's capacity of mobilisation in such contexts is required and is real. This comes with a cost. The publicity of such appraisal is left at the initiative of the company having requested it.

Under normal circumstances, the on going CRA service is less time constrained.

Q15: Once you have chosen your preferred CRA, please explain your involvement in the process of preparing, issuing and subsequently reviewing the rating of your instrument.

CRA's are on the mailing lists and get immediately all public information. In addition, a number of direct contacts either by phone, mail or face to face are organised all along the years to address any CRA's questions. CRA's also very often (but not always) get forecasts from companies which may not publicly released. These forecast can vary from one to two years usually

Q16: Do you give CRAs more detailed information about how the instruments for which you are seeking ratings are developed and how they subsequently perform in practice now than you did before 2010? If so, please explain what kinds of additional information you now provide.

From our discussion with our members, companies are not providing the CRAs with more detailed or new type of information since 2010.

Q17: Do CRAs currently give you more information about how their credit ratings are developed, issued and revised and how their credit ratings compare to the market performance of the rated instruments than they did before 2010? If so, please explain what additional information you receive and whether this makes it easier for you to compare the ratings products and other services being offered by different CRAs.

AFTE confirms that CRAs are transparent on the methodology. On the contrary AFTE members does not seem to have ever seen analysis of CRA's on relative performance of their rated financing instruments but they recognize that they have not really been claiming to get such analysis.

AFTE recalls that Standard & Poor's issued a new corporate methodology last year and confirm that S&P communicated a lot with AFTE Rating Commission and rated companies on the changes to be implemented and their immediate impacts on the individual company's ratings. AFTE also noted that this consultation process has seriously been treated by S&P which has even changed certain of its initial intentions on its methodological approaches. This process has ben very well conducted in the opinion of AFTE members

CRA's methodology is indeed a key rating factor that the market, at large, must have access to and understand. Any methodology change must continue to be publicised widely before implementation

AFTE is aware that periodical controls from the Market authorities are now performed on methodology implementation and believes that this is a positive move to guarantee compliance with methodology and the lack of conflict of interests in the rating process.

CRA's have also made progresses on the way they explain their restatements made on the Company's published figures. However AFTE is still rather uncomfortable on the subject:

- AFTE believes that restatements have become excessively complex given their purpose. Interesting to note that these restatements seem to be mechanically made by specialists which supply them to the analysts. Some analysts can sometime be unable to precisely explain some of the restatements that they use and which directly impact released figures/ratios: this seems to confirm the currently excessive complexity of these technical restatements
- AFTE believes that the reconciliation table between the Company's published figures and the figures included in the CRA's public releases should always be supplied with the release itself to allow, at all times, issuers and investors to understand the reconciliation and the nature of the changes made to the company's public figures.

Q18: Please explain what, if any, further measures could be taken to increase the quality and independence of ratings, giving reasons for your answer.

The methodology of the CRA is a key factor for the quality of the rating. Therefore AFTE is in favour of audit performed by the regulator to check consistency of the analysis performed with the methodology and respect of the rules to prevent conflicts of interests. Those audits are also important to ensure the independence of the ratings.

Lastly, AFTE as indicated above would really like restatements on figures to be systematically released as soon as figures publicly used by CRA's differ from the Company's publications. In an ideal world (!), AFTE would also like restatements to be simplified whenever possible and tends to believe this is feasible without impacting the quality of the rating analysis and results...

Q22: Please explain whether a 4-year contract term is appropriate for this rotation provision, and if not, what would be an appropriate length?

As a general comment on rotation, AFTE is not in favour of mandatory rotation because a CRA needs time to know the company, understand its financial management and risk management, and understand its business sector and competitors. Company's also need to provide the CRA with confidential information and it take time to trust the CRA.

AFTE has, at this stage no comment, on rotation related to ratings of re-securitisations

Q23: Please explain whether mandatory rotation should be extended to other asset classes. If so, please:

(1) list the asset classes to be covered and state the appropriate contract length for each;

No mandatory rotation should be extended to other asset classes

(2) estimate the cost to your business of complying with the extension to each additional asset covered in your response to question 23(1) above;

(3) explain whether, and if so why an obligation should be introduced for CRAs to provide a handover file to the incoming CRA at the end of the maximum contract term.7

AFTE is not in favour of a handover of files between CRA's. It indeed believes that rating service is not a "commodity" and must not be treated as a commodity. In particular, it is not comparable to an audit of financial statements. Each CRA should be capable of making its own opinion based on its public methodology and on any information it has or receives from a Company. This leads back to the

quality of the methodology, the skill level of analysts, the lack of conflict of interests... commented upon above.

In addition, some information of interest at a given time can no longer be of any interest later on.

Q24: Please explain, giving reasons for your answer, whether, and if so how, the exemption from the mandatory rotation provision should be maintained where at least four CRAs each rate more than 10% of the total number of outstanding re-securitisations.

AFTE is not in favour of mandatory rotation but in favour of competition among CRAs, and control of the CRAs by the regulator.

AFTE also asks the regulator to recognize the CRA responsibility when there is negligence (which is currently the case under the CRA regulation).

Q25: Please explain whether, and if so how CRAs compete to win your business.

As mentioned above, most of French companies are rated, on a solicited basis, by the first two major CRAs. AFTE doesn't really see competition between those two which have had their own franchise for a very long time.

What has changed in the past years is the quality of the interactions with CRA's and transparency on their methodologies. There are real progresses made.

On the more negative side AFTE members express concerns on the level of fee increases year after year both in absolute terms but also when compared to standard indexes of price inflation

Q26: If you have been aware of competition between CRAs, please explain whether, and if so how, the nature of competition has changed between 2010 and present.

Since the new ESMA regulation, small CRAs have emerged. Some of them have actively started to contact issuers or treasurer associations. In the short term, it is fair to say that the lack of name recognition and track records of these CRAs does not allow creating a real competition.

AFTE has therefore entered into contact with some of these new CRA's which are trying to develop their presence on the market. AFTE is organising meetings for its members with some of these "new rating agencies" to allow them to present their rating offer and allow its members to judge their merits on an educated basis.

Q27: Have you seen other changes to the behaviour of CRAs since 2010? If so, please explain what these changes have been and to which products or services these changes related.

Yes . please refer to comments above

Q28: Should further measures be taken to stimulate competition between CRAs overall and/ or in respect of the rating of particular types of asset class such as structured finance instruments? If so, please explain what measures should be taken and what impact you think these would have on the quality of credit ratings.

This is not our priority: strength and transparency of the rating methodology must be the priority.