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SFC
證監會

Consultation Conclusions Concerning the Regulatory Oversight of Credit Rating Agencies

29 October 2010

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Consultation conclusions concerning the regulatory oversight of credit rating agencies

Introduction

1. On 19 July 2010, the Securities and Futures Commission ("**SFC**") issued a consultation paper ("**Consultation Paper**") concerning the regulatory oversight of credit rating agencies ("**CRAs**") in Hong Kong. It discussed the objective of regulating CRAs and introduced a series of reform proposals designed to achieve this, including:-

   (a) Proposed legislative amendments to Schedule 5 of the Securities and Futures Ordinance ("**SFO**") by which a new type of regulated activity (Type 10: providing credit rating services) would be introduced;

   (b) A draft Code of Conduct for Persons Providing Credit Rating Services ("**CRA Code**"); and

   (c) A draft list of Recognized Industry Qualifications and Local Regulatory Framework Papers for Type 10 regulated activity to be incorporated into the Guidelines on Competence ("**Competence Guidelines**").

2. The public consultation ended on 20 August 2010. The SFC received a total of 21 written submissions, including five that reached the SFC after the end of the consultation period. These written submissions were received from CRAs, industry associations, professional bodies, a listed company and market practitioners. The submissions are available on the SFC's website at www.sfc.hk. A list of respondents is set out in **Appendix A**. Of the 21 respondents who made submissions to the SFC, one requested that its name and comments not be published and another requested that its submission be published without disclosing its name. We thank all respondents for their feedback and comments.

Summary of major issues raised by the respondents

3. Respondents overwhelmingly welcomed and supported the proposal to establish a regulatory regime for CRAs operating in Hong Kong. Of the reform proposals set out in the Consultation Paper, respondents mainly focused their comments on the following areas:-

   (a) Although there was general support of the proposal to extend the existing SFO regime to include the regulation of CRAs conducting business in Hong Kong, some respondents, principally the CRAs, would prefer to see exemptions from the licensing requirements for individual rating analysts.

   (b) In general, respondents supported the new regulatory regime excluding activities relating to:-

      - Internal credit rating systems;
      - Private credit ratings prepared pursuant to an individual order; and

- Sharing or analyzing consumer or commercial credit data.

However, some respondents commented that the regulatory scope should also cover private credit rating services due to the potential impact of the provision of these services on investment decisions.

(c) Regarding the possibility of restricting Type 10 licensed or registered persons from carrying on business activities other than credit rating services, respondents generally recognized the need to prevent conflicts of interest which would compromise the objectivity and independence of a credit rating. Some respondents supported the imposition of a sole business restriction under the SFO. More respondents preferred the alternative approach of requiring Type 10 licensed or registered persons to maintain an effective Chinese wall policy to manage potential conflicts of interest.

(d) Some respondents provided drafting comments concerning the CRA Code.

International regulatory developments

4. In formulating its proposals concerning the future regulation of CRAs in Hong Kong, the SFC looked closely at international developments in this area and, in particular, at initiatives in the US and the EU. The SFC considered this to be important in the interest of ensuring that the regime under which CRAs will be regulated in Hong Kong is generally consistent with the relatively uniform approach to regulation that appears to be developing internationally in this area. An additional factor influencing the SFC, has been its wish to create proposals for regulatory reform that can be expected to result in credit ratings prepared by CRAs in Hong Kong continuing to be serviceable in the EU. This issue has become relevant because the EU has taken the position that credit ratings which are issued by CRAs outside the EU are unlikely to be serviceable in the EU from 7 June 2011 onwards unless the regimes under which these CRAs are regulated are "equivalent to" or "as stringent as" that which exists in the EU. Accordingly, the SFC sought clarifications from representatives of Committee of European Securities Regulators ("CESR") concerning aspects of the EU regulatory model that could usefully be replicated in Hong Kong.

5. After carefully considering the explanations given by representatives of CESR and the submissions received from the 21 respondents to the SFC's Consultation Paper, the SFC has made some amendments to the CRA Code, a marked-up version of which is at **Appendix B** to this paper. Subject to possible minor amendment following further clarifications from representatives of CESR, the CRA Code and the proposed amendments to the Competence Guidelines will become effective when the new regulatory regime governing CRAs in Hong Kong comes into force.

Comments received and the SFC's responses

Question 1: Is it appropriate for Hong Kong to subject CRAs to a regulatory oversight regime consistent with international developments?

Compatibility with international standards

Public comments

6. Respondents generally welcomed and supported the proposal that CRAs in Hong Kong be subjected to a regulatory oversight regime consistent with international developments. While welcoming the regulatory proposals, some respondents emphasized the importance of establishing the new CRA regime on a globally consistent basis.

SFC's response

7. In line with the general support received from respondents, the SFC intends to proceed with its proposal to establish a regulatory regime for CRAs in Hong Kong. In finalizing the regulatory model for Hong Kong, the SFC is mindful of maintaining regulatory consistency with international developments, including consistency with the revised Code of Conduct Fundamentals for Credit Rating Agencies ("**IOSCO Code**") issued by the International Organization of Securities Commissions ("**IOSCO**") and Regulation (EC) No. 1060/2009 of the European Parliament and of the Council of 16 September 2009 ("**EU Regulation"**), to the extent that this is reasonable and consistent with the regulatory model that exists in Hong Kong. Since the proposed regime is an extension of the existing regulatory model created under the SFO, there is limited scope for departure from aspects of the existing Hong Kong regulatory model in relation to areas such as the licensing of individuals and minimum financial resources requirements.

Licensing procedures

Public comment

8. One respondent suggested that the SFC should introduce a "fast-track" licensing procedure for CRAs that adhere to the IOSCO Code and are registered with the Securities and Exchange Commission as Nationally Recognized Statistical Rating Organizations ("**NRSROs**").

SFC's response

9. As the principal regulator of the securities and futures markets in Hong Kong, the SFC considers it important to maintain consistency in the manner in which it licenses the intermediaries who fall under the provisions of the SFO. The "fast-tracking" of licensees by virtue of their being licensed in another jurisdiction is not a practice which the SFC is able to adopt in relation to its existing population of licensees, and it sees no justification for departing from its current approach in the case of CRAs. The SFC's proposals include one to "grandfather" the existing rating analysts employed by Hong Kong CRAs, thereby

exempting them from passing the Local Regulatory Framework Papers. Similar measures were in place at the time when the SFO came into force in 2003 and the SFC considers this to be an appropriate and consistent approach in the case of the rating analysts of CRAs who are already conducting business in Hong Kong. This approach should facilitate a relatively uncomplicated transition from a situation in which such CRAs and their rating analysts are not licensed in Hong Kong to one in which they are. The SFC intends to further assist in this process by deploying sufficient resources to provide guidance to CRAs and their rating analysts in relation to the licensing process.

Communication with Mainland regulators

Public comment

10. Another respondent suggested that apart from CESR, it is equally important for the SFC to initiate dialogue with the China Securities Regulatory Commission ("**CSRC**") concerning the regulation of CRAs.

SFC's response

11. The SFC agrees that it is important to maintain dialogue with the CSRC in relation to a wide range of matters and is cognizant of the fact that CRAs have been regulated in Mainland China since August 2007. Accordingly, within the context of its regular and ongoing contact with the CSRC, the SFC will welcome the opportunity to exchange views with the CSRC concerning the regulation of CRAs.

Question 2: Should regulatory oversight of CRAs be achieved by extending the existing licensing regime under the SFO to CRAs and those of their staff who perform regulated functions?

Licensing requirements for individual analysts

Public comments

12. All respondents who responded to this question supported the proposal to extend the existing licensing regime under the SFO to CRAs. However, some respondents, principally the CRAs with existing businesses in Hong Kong, raised concerns regarding the imposition of licensing obligations on individual rating analysts. They pointed out that individual licensing is not required in other major jurisdictions such as the US, the EU, Japan and Australia. Their concerns included possible consequences arising from individual licensing obligations, such as:-

    (a) Creating a disincentive for senior rating analysts to relocate to Hong Kong;

    (b) Discouraging visiting rating analysts from overseas offices from working in Hong Kong; and

    (c) Making it more difficult for CRAs to recruit new rating analysts.

SFC's response

13. The SFC accepts that, currently, there is no individual licensing requirement under regulatory systems governing CRAs in the US, the EU, Japan and Australia. However, Hong Kong is not the only jurisdiction that imposes individual licensing requirements. For example, senior management and rating staff of CRAs in Mainland China, who provide credit rating services in relation to the securities market, are also required to be registered with the CSRC[1] or the Securities Association of China. In addition, the recently enacted Dodd-Frank Act also illustrates that US legislators have taken steps to ensure the competency of rating analysts of the NRSROs.

14. The licensing of individuals is a fundamental and integral part of the existing licensing system in Hong Kong. The SFC considers consistency in regulation to be very important and can see no justification for treating rating analysts differently from other individuals performing regulated functions in relation to the regulated activities conducted by the licensed corporations to which they are accredited.

15. The SFC has discussed this issue with CRAs and believes that the concerns expressed in relation to the licensing of rating analysts has arisen, in part, out of a misunderstanding concerning the qualification criteria that the SFC would apply in relation to the licensing of individuals, and also out of a lack of familiarity with the licensing requirements imposed by the SFO. In fact, the SFC considers that the licensing obligations that will be imposed on rating analysts will be considerably less onerous than the CRAs and their rating analysts initially believed and that recognition of this will to some extent allay the concerns expressed by some respondents in their responses to the Consultation Paper.

Regulatory scope

Public comments

16. Most of the respondents supported the scope of the proposed Type 10 regulated activity. However, two respondents proposed extensions to the scope of "credit ratings" or "providing credit rating services". One of them suggested that the definition of "credit ratings" should be refined to cover all types of risk ratings because the risks of Islamic bonds and structured finance products involve more than simply default risk, and that the risk rating process of other risk dimensions relating to financial assets should be captured by the proposed regime. Another respondent suggested that the individual licensing requirements should be extended to the staff of CRAs who are involved in the marketing of rating services.

SFC's response

17. The SFC is of the view that the adoption of these two suggestions would substantially extend the proposed scope of the regulatory regime proposed for CRAs in Hong Kong, thereby introducing inconsistency with other important jurisdictions and being out of line with international trends in relation to the regulation of CRAs. In particular, the adoption of these suggestions would constitute a substantial departure from the provisions of the

[1] http://www.csrc.gov.cn/pub/zjhpublic/zjh/200804/t20080418_14513.htm?keywords=

IOSCO Code and the model under which CRAs are regulated in the EU. The SFC considers such departures to be inappropriate and to potentially create difficulties in relation to the equivalence assessment that the EU is currently conducting in relation to the regime that the SFC is proposing for the regulation of CRAs operating in Hong Kong. Moreover, the SFC is aware that the business practices adopted internationally by CRAs are relatively uniform and it believes that the creation of requirements that are so far out of step with the regulatory models in other important jurisdictions, might call into question the continuing viability of the Hong Kong operations of these larger CRAs. Requiring the marketing staff of CRAs to be licensed as representatives would be inconsistent with section 114(3) of the SFO. That provision requires only those individuals performing regulated functions in relation to the regulated activity conducted by the licensed corporations to which they accredited to be licensed. In light of these circumstances, the SFC does not support these suggestions.

Competition within the CRA industry

Public comment

18. One respondent suggested that the SFC should prevent the formation of a monopoly on credit rating business and maintain effective competition in the industry.

SFC's response

19. The regulatory regime created under the SFO has been designed to create and maintain a level playing field for market practitioners by ensuring that all those seeking to be licensed under the SFO are free to do so provided they comply with requirements that are universally and consistently applied. This means that any firm complying with the regulatory obligations that are intended to be imposed under the SFO in relation to CRAs will be able to establish itself in Hong Kong as a CRA. The SFC sees nothing anticompetitive in its proposed regulatory reforms in this area. Indeed, the opposite would appear to be the case. Furthermore, the SFC is not able to take action designed to actively promote competition amongst its licensees, with the objective of actively discouraging monopolies, because it is not empowered to do so.

Question 3: Do our draft amendments to the SFO effectively distinguish "providing credit rating services" from "advising on securities"?

Definitions of Type 4 and Type 10 regulated activities

Public comments

20. Each of the sixteen respondents who responded to this question recognized the need to distinguish Type 10 regulated activity (providing credit rating services) from Type 4 regulated activity (advising on securities) under the SFO. Thirteen of them agreed that the draft amendments effectively distinguish the two types of regulated activities.

21. Two respondents commented that the draft amendments do not effectively distinguish

Type 4 and Type 10 regulated activities. One of them took the view that credit rating is a form of financial advice and further suggested that the SFC should distinguish between credit ratings used by institutional investors and the ratings assigned to retail financial products. Another respondent was of the opinion that it is not clear whether an adviser licensed to advise on securities, who comments on the creditworthiness of a financial instrument when advising clients on securities, is also required to hold a Type 10 licence.

SFC's response

22. The SFC has reviewed these matters carefully and concurs with the views expressed by the majority of respondents that the draft amendments to Schedule 5 of the SFO effectively distinguish between Type 4 and Type 10 regulated activities. The SFC considers that paragraph 16 of the Consultation Paper correctly explains why "providing credit rating services" cannot properly be regarded as falling within the SFO definition of "advising on securities". In response to the suggestion that it is necessary to differentiate between ratings used by institutional and retail investors, the SFC does not consider this to be appropriate. Furthermore, it would not be consistent with the approach adopted by IOSCO. The proposed definition of "providing credit rating services" is concerned with preparing credit ratings which will be seen by the public, which includes both institutional and retail investors. The SFC considers this to be appropriate and sees no sound policy reason to distinguish between institutional and retail investors in the manner proposed, and no resulting benefit from doing so.

23. A person licensed to carry on business in Type 4 regulated activity, who during the course of advising a client concerning the acquisition or disposal of securities comments on the creditworthiness of a financial instrument, is very unlikely to be required to hold a Type 10 licence. There are two principal reasons for this. First, the person would not be *carrying on a business* of providing credit rating services. He would be carrying on the business of advising on securities and his reference to the creditworthiness of a particular financial instrument would merely be incidental to that particular business. Secondly, his comments concerning the creditworthiness of the financial instrument would be unlikely to be expressed "using a defined ranking system".

24. Having carefully considered these comments, the SFC does not see a need to alter its reform proposals to further distinguish between Type 4 and Type 10 regulated activities.

Applicability of licensing requirements

Public comment

25. One respondent suggested that the definition of "providing credit rating services" be modified so that it would capture only those activities constituting the preparation of credit ratings for securities where the lead analyst responsible for analyzing the issuer or securities is permanently based in Hong Kong. It was contended by this respondent that a consensus is forming that the location of the lead analyst should dictate which regulatory regime takes precedence.

SFC's response

26. The SFC disagrees with these views. Under the SFO, licensing requirements arise if regulated activities are performed in Hong Kong. The SFC sees no sound basis upon which to change this position. Effective regulation involves the regulator responsible for regulation in a particular jurisdiction supervising persons performing activities in that jurisdiction. It follows that where the lead analyst is conducting his work in one jurisdiction and doing so in conjunction with team members who conduct their functions in other jurisdictions, the team and/or the CRA are likely to find themselves having to be licensed and/or being supervised in multiple jurisdictions. The SFC considers this to be appropriate and disagrees that there is any consensus forming, certainly amongst regulators, that only the lead analyst need be licensed and only then in the jurisdiction where he is based.

Question 4: Should the proposed new licensing requirement apply to the rating of sukuk?

Public comments

27. All respondents who commented on this question were supportive of the application of the proposed new licensing obligation to those preparing ratings of sukuk. One respondent further suggested that the proposed CRA regime should be applicable only to sukuk which provide fixed and predictable income to their holders. Another respondent indicated that sukuk also have risk elements other than default risk, such as legal risk.

SFC's response

28. In line with the views expressed by the respondents who commented on this question, the SFC agrees that the proposed licensing requirements should apply to the preparation of sukuk generally and is satisfied that the proposed definitions, as set out in Appendix A to the Consultation Paper, will have this effect. If appropriate, the SFC will consider clarifying this by means of FAQs published on its website.

Question 5: Should the following activities be excluded from the proposed new licensing requirement:

(a) preparing credit ratings for an organization's internal purposes;

(b) preparing private credit ratings; and

(c) sharing or analyzing consumer or commercial credit data (such as through consumer or commercial credit reference agencies)?

Activities excluded from the CRA regime

Public comments

29. Nearly all of the respondents who replied to this question supported the exclusion of all or some of the activities referred to in paragraphs (a) to (c) from the activities that give rise to licensing obligations on the part of CRAs and their rating analysts. One respondent, who supported excluding all three types of activities, suggested that CRAs should disclose their

exemption status to their clients.

30. One respondent commented that there might be a need to define "internal purposes" with greater precision for activity (a), and to clarify whether the licensing requirements should apply if the internal information is released to the public.

31. Another respondent, while agreeing that the exclusion should apply to the initial commissioning of a private rating, suggested putting some limits on the definition of "private credit ratings" which would take certain business activities outside the ambit of the proposed licensing and regulatory requirements.

32. While some of the respondents commented that either one or two of these activities should not be excluded from the activities which are captured within the definition of "providing credit rating services", there were differing views as to which of the activities these should be. These views can be summarised as follows:

    (a) One respondent commented that activities (a) and (b) should not be excluded because internal credit rating systems should still be subject to the licensing requirements in order to avoid misuse and misinterpretation of these credit ratings and to bolster the databases maintained by CRAs that may provide further evidence concerning the rating basis. This respondent also raised concerns about the leakage of private ratings and agreed to the proposed measures set out in paragraph 19 of the CRA Code (i.e. the pre-requisite of compliance with the provisions of the CRA Code before the subsequent dissemination of "private ratings" to the public, or distribution by subscription whether in Hong Kong or elsewhere).

    (b) One respondent supported excluding activity (a), but not activities (b) and (c). This view was advanced on the basis that private credit ratings can play a significant role in the market and the proposed exclusion would deprive clients of their rights and remedies. This respondent also commented that given that the synthesis and analysis of credit data was an integral part of the credit worthiness assessment process, it would be contradictory for the SFC to exempt activity (c) when CRAs would probably analyze the relevant credit data or history when assessing the creditworthiness of a company.

    (c) One respondent objected to the exclusion of activity (b) because while many jurisdictions choose to focus on monitoring the rating process in the regulation of credit ratings, private rating is the same as public rating in terms of analytical methods and procedures and the generation of research reports, with the main difference being that private rating is not subject to public disclosure.

SFC's response

33. With reference to the suggestions made by respondents concerning the scope of "private credit ratings", the disclosure by CRAs to their clients of their exemption status, defining "internal purposes", and the proposed inclusion of private credit ratings and internal credit rating systems, the SFC considers that the implementation of these proposals would create practical difficulties, both from a legislative drafting perspective and from the perspective of CRAs being able to comply with them. The SFC considers that these difficulties would outweigh any possible benefits. The SFC is also of the view that it is not

appropriate to impose a Type 10 licensing obligation which arises out of the possibility that private ratings might be leaked to the public. In any event, such disclosure would be likely to fall within the definition of "providing credit rating services", which might well trigger an obligation to secure a Type 10 licence. This, in turn, would give rise to an obligation to comply with the provisions of paragraph 19 of the CRA Code prior to public dissemination.

34. It is also noteworthy that the exclusion of the activities (a) to (c) would be consistent with the position prevailing in other jurisdictions, including the EU. The SFC considers this to be the preferred approach.

Specific use of internal ratings

Public comment

35. One respondent pointed out that insurance companies or banks may rely on their internal ratings (a) to make significant investments for their proprietary accounts that would ultimately affect the financial health of those institutions, or (b) to assemble the underlying financial products of a bond fund for sale to the public. This respondent, which is an industry association, also indicated that some of its members reflect the internal ratings of certain bonds, without official ratings from CRAs, in their marketing materials for authorized funds (e.g. fund fact sheets and fund reports), which may be distributed to the retail public in Hong Kong.

SFC response

36. The SFC takes the view that if internal ratings, which fall within the definition of "credit ratings" set out in the Consultation Paper, are prepared for dissemination to the public or distribution by subscription, persons who prepare these ratings are likely to come under an obligation to be licensed or registered for Type 10 regulated activity. The SFC considers this to be appropriate.

Question 6: Further to question 5, do our draft amendments to the SFO effectively exclude these activities from the proposed new licensing requirement?

Effectiveness of the draft amendments

Public comments

37. With reference to the draft amendments, eight out of twelve respondents to this question supported the view that the draft amendments to the SFO would effectively exclude from the definition of "providing credit rating services" the activities referred to in paragraphs (a) to (c) of Question 5 above.

38. Two respondents provided some specific drafting comments on the draft definitions set out in the Consultation Paper. One respondent commented that the drafting is not clear enough to differentiate internal credit rating systems from private ratings. One respondent suggested distinguishing between the mere transmission of raw data from the synthesis

and analysis of such data in the drafting of sub-paragraph (ii) of the definition of "providing credit rating services". Another respondent raised its concern that the definition of "credit ratings" could be construed to unintentionally cover those aspects of its business such as the provision of scores that predict future trade delinquency or business failure.

SFC's response

39. The SFC concurs with the view predominantly expressed by respondents that the activities referred to in paragraphs (a) to (c) in Question 5 are excluded from falling within the proposed definition of "providing credit rating services". Accordingly, the SFC sees no basis upon which the proposed amendments to Schedule 5 of the SFO need to be revised.

Exemption under sub-paragraph (iii) of the definition of "providing credit rating services"

Public comment

40. One respondent commented that the criteria upon which the SFC or the Financial Secretary might grant an exemption under sub-paragraph (iii) of the definition of "providing credit rating services" are not stipulated in this exemption provision. This power of exemption would permit the SFC or the Financial Secretary to declare the conduct of a person, or class of persons, as falling outside the meaning "providing credit rating services".

SFC's response

41. As explained in paragraph 21 in the Consultation Paper, the power of the SFC or the Financial Secretary to grant an exemption under sub-paragraph (iii) would only rarely be used. Its purpose is to create a mechanism by which those who might unintentionally fall within the meaning of the words "providing credit rating services" could, in exceptional circumstances, be excused from the obligation to secure a Type 10 licence. The SFC does not consider it appropriate to stipulate in sub-paragraph (iii) the situations in which this power may be exercised because the exemption power is, in fact, designed to cater for unanticipated circumstances. However, were this power to be conferred on the SFC, it would, by way of FAQs published on its website, provide the market with guidance as to the types of issues it would take into account in deciding whether to exercise the power in favour of a person or class of persons.

Question 7: Are the proposed paid-up share capital and liquid capital requirements for Type 10 regulated activity appropriate?

Public comments

42. Eleven out of fourteen respondents were supportive of the proposed paid-up share capital and liquid capital requirements for corporations conducting Type 10 regulated activity. Three of these respondents suggested that CRAs might purchase professional indemnity insurance in addition to complying with the proposed capital requirements.

43. Three respondents did not support this proposal. One respondent suggested that the SFC

should raise the minimum capital requirements for CRAs in order to ensure their financial soundness. Another argued that the proposal would introduce a cumbersome and inflexible approach that would require constant monitoring and oversight. This respondent therefore suggested that the capital requirements for CRAs should not be variable and subject to change on a daily basis. The other argued against the imposition of capital requirements on CRAs because there is no similar requirement under Hong Kong corporate laws and because CRAs neither process transactions nor hold client funds.

SFC's response

44. The SFC sees no reason why CRAs should not be subject to capital requirements in the same manner as all other corporations licensed under the SFO are. Other licensed corporations, which do not handle client assets, are required to meet the minimum capital requirements prescribed in the Securities and Futures (Financial Resources) Rules ("**Financial Resources Rules**") and, in the interest of consistency, the SFC considers that CRAs should also be required to meet similar obligations. Section 129(1)(a) of the SFO requires the SFC to have regard to financial status or solvency when reaching a determination as to fitness and properness. The SFC is also obliged, by section 116(3)(b) of the SFO, to refuse to grant a licence to an applicant if it fails to satisfy the SFC that it will be able, if licensed, to comply with the Financial Resources Rules, and it sees no basis upon which CRAs should be allowed to avoid the capital obligations which are fundamental to the Financial Resources Rules.

45. The SFC does not share the view that Type 10 licensed corporations should be subjected to mandatory insurance obligations. There is no similar requirement for other types of licensed corporations, with the exception of licensed corporations which are also exchange participants, and the SFC sees no sound justification for singling CRAs out for different treatment in this connection.

46. In line with the views expressed by the majority of the respondents, the SFC intends to maintain the position stated in the Consultation Paper concerning the capital requirements that CRAs will be expected to meet after they secure Type 10 licences.

Question 8: Does the CRA Code of Conduct satisfactorily set out the factors that should guide CRAs in the conduct of their business and which should be relied upon by the SFC in considering whether a person is, or remains, fit and proper to be licensed or registered for Type 10 regulated activity?

Applicability of the CRA Code

Public comments

47. Fifteen out of the seventeen respondents who answered this question generally expressed the same view that the CRA Code satisfactorily achieves the specified purposes set out in this question. Two respondents suggested that the CRA Code should be subject to regular review after implementation.

48. Two respondents commented as follows that some provisions of the CRA Code were more

prescriptive and detailed than the IOSCO Code:

(a) One of them raised its concern over the requirement proposed under paragraph 30 of the CRA Code which obliges licensed CRAs to be legal entities that are separate from all other businesses. It urged the SFC to implement the licensing framework in a flexible and proportionate manner and recognize that legal separation is not necessary to effectively manage potential conflicts of interests, and to adopt rules that only impact Hong Kong-based ratings businesses and staff, regardless of whether the local operations are conducted through a legal entity, branch office or other structure.

(b) The other respondent argued the importance of the CRA Code making clear the respective responsibilities of CRAs and their licensed representatives. In addition, the respondent expressed the view that CRAs should only be required to comply with the CRA Code because many paragraphs of the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission ("**SFC General Code**") are not relevant to the business activities of CRAs. It was argued that this approach would ensure a level regulatory playing field for CRAs with international operations. The same respondent raised another concern in relation to the definition of "structured investment product". This definition, it was contended, departed from the approaches adopted in other jurisdictions and may include derivative products publicly distributed in Hong Kong and may unintentionally capture instruments which are not traditionally considered to be structured finance instruments, such as certain types of corporate bonds.

SFC's response

49. The purpose of the requirement under paragraph 30 of the CRA Code is to prevent any potential conflict of interest that might arise if a CRA were to conduct any business other than the provision of credit rating services. The CRA is expected to operationally and legally separate its credit rating business from any other business where the potential for conflict of interest exists. The SFC sees no compelling reason to relax these requirements, particularly when the independence of the rating process is one of the fundamental principles that a CRA should observe.

50. The SFC accepts that some provisions of the CRA Code may be more prescriptive than those contained in the IOSCO Code. As explained in paragraphs 9 and 10 of the Consultation Paper, the creation of a regulatory regime governing CRAs conducting business in Hong Kong is, in part, intended to ensure that ratings prepared in Hong Kong continue to be serviceable in other jurisdictions, including the EU. Accordingly, the SFC considers it appropriate to incorporate into the CRA Code, requirements that are in line with those that apply in the EU. After careful consideration of these comments and the clarifications from representatives of CESR, the SFC has decided to revise the CRA Code (see Appendix B). By way of brief summary, the amendments that have been made to the CRA Code include:

(a) Drawing a clearer distinction between the responsibilities of CRAs and their licensed representatives;

(b) Adopting a new definition of "structured finance products", which is generally

consistent with the approach adopted in other jurisdictions, including the EU, and dispensing with the concept of "structured investment products"; and

(c) Introducing some changes to provisions which we anticipated may not be in line with CESR's published technical advices and which now more closely coincide with similar provisions contained in the EU Regulation.

51. The SFC does not agree that CRAs should be exempted from the obligation to comply with the SFC General Code. The SFC General Code provides guidance to the market as to the manner in which the SFC views conduct going to the fitness and properness of corporations and persons licensed by it. The provisions of the SFC General Code have general application to all licensees and, in the interest of consistency, the SFC sees no reason why they should not apply to licensed CRAs and their licensed representatives.

Enforceability of the CRA Code

Public comment

52. One respondent questioned the legal standing or enforceability of the CRA Code.

SFC's response

53. The SFC has the power under section 169 of the SFO to make codes of conduct for the purpose of giving guidance relating to the practices and standards with which intermediaries and their representatives are expected to comply. Failure to comply with such practices and standards may influence the SFC's view concerning the fitness and properness of an intermediary or representative to be or to remain licensed.

Operational requirements

Public comment

54. One respondent suggested certain fine-tuning of the CRA Code in relation to operational requirements:-

(a) Requiring a CRA to establish and maintain an effective compliance function in line with the EU Regulation;

(b) Tightening up paragraph 34(b) of the CRA Code in line with the EU Regulation, by requiring a CRA to disclose if it or its group receives 5% (as distinct from the proposed 10%) or more of its annual revenue from a single party; and

(c) Requiring rating analysts to disclose their existing investment holdings upon joining a CRA, and on a regular basis thereafter, in line with the requirement stipulated in paragraph 2.1.1 of the Fund Manager Code of Conduct ("**FMCC**").

SFC's response

55. In response to the suggestion referred to in paragraph (a), Part V of the Management, Supervision and Internal Control Guidelines for Persons Licensed By or Registered with the Securities and Futures Commission ("**Internal Control Guidelines**") sets out detailed guidance concerning the policies and procedures that need to be established and maintained in order to ensure that an appropriate level of compliance is achieved. Paragraph 24 of the CRA Code will be read alongside Part V of the Internal Control Guidelines and CRAs will be obliged to comply with the requirements of both. Paragraph 132 of the Technical Advice to the European Commission on the Equivalence between the US Regulatory and Supervisory Framework and the EU Regulatory Regime for Credit Rating Agencies issued by CESR in May 2010[2] ("**CESR Technical Advice**"), recognizes that the obligation to have a permanent and effective compliance function, which operates independently, need not necessarily either be identical to that imposed under the EU Regulation or incorporated into law. However, it seems clear that CESR expects that, by some means, this obligation should be put in place. The SFC concurs and believes that imposing compliance obligations by means of paragraph 24 of the CRA Code, which will be read in conjunction with Part V of the Internal Control Guidelines, is appropriate within the Hong Kong context. However, in recognition of the importance of CRAs establishing an independent compliance function, the SFC has concluded that it is desirable to amend paragraph 24 of the CRA Code to give greater emphasis to this.

56. In response to the suggestion referred to in paragraph (b), paragraph 34(b) of the CRA Code is based on paragraph 2.8.b of the IOSCO Code. However, the SFC recognizes the importance of effective conflict of interest management and the importance that CESR also attaches to this. Accordingly, the SFC agrees that the threshold stipulated in paragraph 34(b) of the CRA Code should be reduced from 10% to 5%, thus bringing it into line with the same requirement under the EU Regulation.

57. In response to the suggestion referred to in paragraph (c), the SFC is not aware of any regulatory requirement set out in the IOSCO Code or the EU Regulation that resembles paragraph 2.1.1 of the FMCC. This is perhaps not unexpected bearing in mind the significant differences that exist between the business conducted by CRAs and that conducted by fund managers. The SFC sees no compelling reason to incorporate a provision resembling paragraph 2.1.1 into the CRA Code and, in this respect, prefers to maintain consistency with the approach that has been adopted internationally.

Special requirements for structured finance products

Public comments

58. A respondent, which is a CRA, recommended that the SFC should not adopt paragraphs 38 to 40[3] of the CRA Code because these paragraphs would create incentives for arrangers, investors and CRAs to act in a manner that is inconsistent with the goals of a more transparent, fair and efficient market. Another respondent also expressed the view

[2] http://www.cesr-eu.org/popup2.php?id=6642

[3] Paragraphs 38 to 40 of the CRA Code were based on the Rule 17g-5 of the Securities and Exchange Act in the United States and Articles 8(a) and (b) of the Proposal for a Regulation of the European Parliament and of the Council on amending Regulation (EC) No 1060/2009 on credit rating agencies (i.e. the EU Regulation).

that the drafting of paragraphs 38 to 40 of the CRA Code is unnecessarily strict.

SFC's response

59. These paragraphs, which contain provisions designed to attract unsolicited ratings of structured finance products, are primarily modeled on Rule 17g-5, which was promulgated under the US Securities Exchange Act of 1934. The EU subsequently proposed the possible imposition of similar requirements in relation to CRAs conducting business in the EU. In the US, the Securities Exchange Commission has postponed the full implementation these requirements. In the EU, it is still undecided whether it is appropriate to impose these requirements at all. In view of the uncertainty in this area, the SFC prefers to adopt a "wait and see" approach until the regulatory landscape in both the US and the EU becomes clearer. Accordingly, it has been decided to delete paragraphs 38 to 40 from the CRA Code at this time and, in due course, to reconsider the introduction of these or other provisions.

Additional disclosure requirements set out in the EU Regulation

60. It seems clear that CESR regards the following disclosure obligations as being of importance, the implication of which is that the manner in which they are addressed in the CRA Code might well be of significance when CESR assesses whether or not the regime under which CRAs are regulated in Hong Kong is as stringent as the EU regime:-

    (a) Statements disclosing the name and job title of the lead rating analyst, as well as the name and the position of the person primarily responsible for approving the rating (Paragraphs 178 and 179 of the CESR Technical Advice).

    (b) Disclosure of all material sources, including the rated entity or, where appropriate, a related third party, that are used to prepare the credit rating, together with an indication as to whether the credit rating has been disclosed to that rated entity or its related third party and amended following such disclosure and before being issued (Paragraphs 178 and 179 of the CESR Technical Advice).

    (c) Disclosure of the level of assessment a CRA has performed concerning the due diligence processes carried out at the level of underlying finance products or other assets of structured finance products. The CRA should disclose whether it has undertaken any assessment of such due diligence processes or whether it has relied on a third-party assessment, and indicate how the outcome of such assessment impacts on its credit rating (Paragraphs 184 and 186 of the CESR Technical Advice).

    (d) General disclosure of a list of ancillary services rendered by a CRA (Paragraphs 191 and 192 of the CESR Technical Advice).

    (e) A description of the following information on an annual basis:-
        - Internal control mechanisms ensuring the quality of its credit rating activities;
        - Record-keeping policy;
        - Quality control system;
        - Management and rating analysts rotational policy; and

- Outcome of the annual internal review of its independent compliance function (Paragraphs 197 and 198 of the CESR Technical Advice).

SFC's response

61. The SFC has decided to introduce these additional disclosure requirements into the CRA Code because:-

    (a) It anticipates CESR taking these disclosure requirements into account when assessing whether or not the regime is as stringent as that existing in the EU; and

    (b) The disclosure of this additional information is beneficial to the market, without creating an unreasonable additional operational burden for CRAs.

Question 9: Should persons licensed or registered for Type 10 regulated activity be permitted to be licensed or registered for other types of regulated activity?

Question 10: Should persons licensed or registered for Type 10 regulated activity be subject to a sole business restriction?

Public comments

62. Respondents generally recognized the need to prevent conflicts of interest in order to avoid compromising the objectivity and independence of credit ratings. However, there were two different views on how a CRA can effectively address this concern. While one group of respondents supported the position that a Type 10 licensed or registered person should not carry out other regulated activities (or even any business activity other than provision of credit rating services), most of the respondents favoured not imposing any statutory restriction under the SFO. Their view was that a Type 10 licensed or registered person could effectively segregate other forms of business from their credit rating business by maintaining effective Chinese Walls. One respondent further elaborated that the imposition of sole business restriction would limit the opportunity for CRAs to carry out other innovative business activities, such as research, publishing, etc., which would not give rise to any conflict of interest concerns.

SFC's response

63. In line with the majority view, the SFC does not favour the imposition of sole regulated activity and/or sole business restrictions on Type 10 licensed or registered persons. IOSCO does not support such restrictions and they do not exist in other jurisdictions, including the EU, provided the carrying on of other ancillary activities by a CRA does not give rise to any potential conflict of interest. The SFC agrees with this position and will insist upon Type 10 licensed or registered persons not conducting any business which might potentially create conflicts of interest with their credit rating business.

Question 11: Is the draft list of Recognized Industry Qualifications and Local Regulatory Framework Papers for Type 10 regulated activity appropriate?

Appropriateness of the draft list

Public comments

64. Amongst the eleven respondents who commented on this question, six of them supported the draft list, including the proposed development of new examination papers in Local Regulatory Framework and Recognized Industry Qualifications. Two of them further proposed that exemptions from the obligation to sit the relevant examination papers could be granted by reference to the Competence Guidelines and the qualifications of the rating analysts who might otherwise have to pass such examinations. One of these two respondents was also concerned as to whether the Hong Kong Securities Institute (**"HKSI"**) could provide the training courses and examinations on a breakeven basis due to the expected smaller number of Type 10 licensees.

65. Two other respondents, both being CRAs, indicated that the examination requirements are not necessary. Instead, in order to preserve the independence of analysts and the analytical process, one respondent suggested that it would be better for the SFC to give guidance to CRAs and allow them to determine the competence and continuous professional training ("**CPT**") for their rating analysts in accordance with their own codes of conduct and internal requirements.

SFC's response

66. After carefully considering these responses, the SFC has decided that the proposed draft list of Recognized Industry Qualifications and Local Regulatory Framework Papers is appropriate and that its adoption would be consistent with the requirements that apply in the case of other persons seeking to be licensed under the SFO. The impression gained by the SFC from the feedback it has received concerning this matter suggests that there might be some misunderstanding that the draft list dictates the manner in which all rating analysts will be required to establish their competence prior to being licensed. However, the draft list must be read in conjunction with other parts of the Competence Guidelines. For example, Type 10 licence applicants might well be able to rely on Appendix B of the Competence Guidelines which sets out different options for them to meet the test of competence. In addition, various exemptions from the Recognized Industry Qualification and Local Regulatory Framework Paper requirements set out in Appendices D and E of the Competence Guidelines are also likely to be applicable to Type 10 licence applicants.

67. Currently, the SFC is working with the HKSI in connection with the creation of new examination papers for Type 10 responsible officers and the revision of the existing general examination papers to reflect the creation of this new type of regulated activity.

Relevance of the examinations

Public comments

68. One respondent queried whether the content of existing local regulatory framework papers would be relevant to rating analysts. Another respondent took the opposite view that Type 10 regulated activity has similarities to Type 4 regulated activity. It was therefore suggested that the SFC should categorize Type 10 regulated activity under the same group of competence requirements as apply to Type 1, Type 4 and Type 8 regulated activities[4] for the purposes of the local regulatory framework paper requirement and the CPT requirement.

SFC's response

69. The SFC considers that the credit rating industry is specialized in terms of industry knowledge and experience. Accordingly, it feels that parts of the existing examination papers are not directly relevant to CRA industry. The SFC has therefore concluded that it is more appropriate to regard Type 10 regulated activity as a separate category in terms of competence and CPT requirements.

Industry qualifications

Public comment

70. One respondent commented that the proposed industry qualification in Appendix C to the Consultation Paper may not be sufficient for modern credit ratings, and made certain suggestions such as requiring specific postgraduate qualifications for rating analysts who will rate structured finance products.

SFC's response

71. The Competence Guidelines are designed to provide the minimum competence requirements that licensed individuals are expected to meet, and to give objective guidance to the industry concerning the manner in which the SFC assesses the competence of an individual seeking a licence under the SFO. On this basis, the SFC does not consider it necessary or appropriate to substantially raise the industry qualifications as set out in the Competence Guidelines. Apart from the fact that postgraduate qualifications are not necessarily indicative of competence, it would be very difficult from an administrative perspective to maintain a comprehensive list of all such qualifications which the SFC would recognize for this purpose.

Recognition of Mainland qualifications

Public comment

72. One respondent suggested that the SFC should make arrangements for the mutual

[4] Under the Guidelines on Continuous Professional Training, Type 1, Type 4 and Type 8 regulated activities have the same competence requirements.

recognition of the qualifications of the credit rating practitioners in Mainland China and in Hong Kong.

SFC's response

73. Mutual recognition of this sort would require cooperation between regulatory bodies in Mainland China and Hong Kong. Accordingly, the making of such arrangements would not rest solely in the hands of the SFC. However, this matter is probably of little consequence because the SFC will recognize academic qualifications and relevant industry experience obtained in Mainland China when assessing the competence of applicants for Type 10 licences, in the same way as it will recognize academic qualifications and relevant industry experience obtained in other jurisdictions. The SFC regards consistency in this area as being of importance.

Question 12: Are the proposed transitional arrangements appropriate?

Implementation details of transitional arrangements

Public comments

74. All respondents who commented on this question generally supported the proposed transitional arrangement including the "grandfathering" approach for the rating analysts of CRAs which are well established in Hong Kong. However, some respondents made the following suggestions in connection with the implementation details of this proposal:-

(a) The SFC should clearly indicate the length of the transitional period.

(b) The SFC should consider extending the grandfathering provision to the rating analysts of CSRC-regulated CRAs.

(c) The SFC should publish the licensing procedures for Type 10 activities.

SFC's response

75. On balance, the SFC is satisfied that its proposal in this connection is fair and reasonable. This appears to be borne out by the general support which it has received from respondents. The SFC is of the view that these transitional arrangements should only be extended to rating analysts who are working in Hong Kong with CRAs which are well established in Hong Kong. To extend the transitional arrangements to rating analysts in Mainland China (the majority of whom would presumably have no Hong Kong experience) would require a detailed assessment as to whether this would be appropriate and, in fairness, would require an additional assessment as to whether rating analysts in other jurisdictions should also have the same option extended to them. This would give rise to administrative and assessment complications which the SFC believes would be inappropriate and would impose an unacceptable burden on the SFC. The creation of a regulatory regime for CRAs and their rating analysts in Hong Kong requires amendments to the SFO. In the event of these amendments being made to the SFO, the SFC will be in a position to provide the market with additional information concerning operation of the

transitional arrangements.

Tight implementation timeframe

Public comments

76. One respondent expressed the view that the proposed timetable for the creation of a regulatory regime governing CRAs in Hong Kong is sufficient. However, another respondent expressed its concern in relation to the tight implementation timetable bearing in mind the substantial effort that will initially be required in completing the licensing processes.

SFC's response

77. In order that credit ratings prepared by CRAs in Hong Kong can continue to be serviceable in EU, Hong Kong must have in place by 7 June 2011 a regulatory regime governing CRAs conducting business in Hong Kong. The SFC accepts that the timeframe within which it is seeking to achieve this is very tight. However, the SFC believes that it is achievable, provided the necessary legislative amendments are implemented in a timely manner. Once this is achieved, the SFC believes that the necessary licences can be granted by 7 June 2011. In order to expedite the licensing process, the SFC intends to give priority to the licensing of CRAs and their rating analysts and to assist them as much as reasonably possible with their licence applications.

Way forward

78. Following the publication of these consultation conclusions, the SFC will work closely with the Government in an effort to secure the passage of the necessary legislative amendments. Once this process is completed, the SFC will be in a position to announce details concerning matters such as application procedures and timing.

79. The SFC anticipates ongoing dialogue with the CRAs that are conducting business in Hong Kong. The SFC will endeavour to work closely with them in order to address their concerns, answer their questions and assist them to prepare themselves and their rating analysts for the licensing process, which we currently anticipate occurring in the period leading up to June 2011.

80. Developments internationally concerning the regulation of CRAs are ongoing and dynamic. Accordingly, the SFC will closely monitor any regulatory changes that occur in this area in other jurisdictions with a view to making such adjustments as would seem necessary to ensure that CRAs are regulated in Hong Kong in a manner which is comparable with regulation in this area internationally, and which is likely to result in ratings prepared by Hong Kong CRAs continuing to be serviceable in the EU after 7 June 2011.

Appendix A

List of respondents

(in alphabetical order)

1. **Australasian Compliance Institute**
2. **Business Information Industry Association**
3. **CFA Institute and The Hong Kong Society of Financial Analysts (joint submission)**
4. **CLP Holdings Limited**
5. **Coface Greater China Services Limited**
6. **CompliancePlus Consulting Limited**
7. **Dun & Bradstreet (HK) Ltd.**
8. **Hong Kong Investment Funds Association**
9. **Hong Kong Securities Association**
10. **Hong Kong Securities & Futures Professionals Association**
11. **LIEM Kevin**
12. **Moody's Investors Service Hong Kong Limited**
13. **Pengyuan Credit Rating Co., Ltd.**
14. **Standard & Poor's International LLC, Hong Kong Branch**
15. **The Chamber of Hong Kong Listed Companies**
16. **The Hong Kong Institute of Chartered Secretaries**
17. **The Law Society of Hong Kong**
18. **WONG Michael**
19. **ZHANG Zhijun**
20. **One respondent has requested that its submission be published without disclosing its name**
21. **One respondent has requested that its name and comments not be published**

Appendix B

SECURITIES AND FUTURES COMMISSION
證券及期貨事務監察委員會

SFC
證監會

Code of Conduct for Persons Providing Credit Rating Services

[Date]

Table of Contents

Introduction

1. This Code applies to persons licensed by, or registered with, the Securities and Futures Commission ("**SFC**") for Type 10 regulated activity (providing credit rating services), including, ~~except where the context otherwise requires, their~~as appropriate, representatives (as defined in section 167 of the Securities and Futures Ordinance~~,~~ (Cap. 571) ("**SFO**")). The SFC recognizes that some aspects of compliance with this Code might not be within the control of a particular representative. In considering the conduct of representatives under this Code, the SFC will take into account their levels of responsibility within their firms, any supervisory duties they may perform, and the levels of control or knowledge they may have concerning any failure by their firms, or by individuals under their supervision, to ~~follow~~observe this Code.

2. The SFC will be guided by this Code in considering whether a licensed or registered person satisfies the requirement that it/he is fit and proper to be or to remain licensed or registered. This Code, which is based on the revised Code of Conduct Fundamentals for Credit Rating Agencies issued by the International Organization of Securities Commissions in May 2008 ("**IOSCO Code**")[1], does not have the force of law and does not replace any legislative provisions, ~~nor~~or any other codes or guidelines issued by the SFC. In particular, it supplements, and should be read in conjunction with, the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission ("General Code of Conduct").

3. For the purposes of this Code:

   (a) "**CRA**" means a "licensed corporation" or "registered institution" (as defined in Part 1 of Schedule 1 of the SFO), which is licensed or registered to carry on business in Type 10 regulated activity;

   ~~(a)~~(b) "**ratings**" has the same meaning as "credit ratings" (as defined in Schedule 5 of the SFO);

   ~~(b)~~(c) "**rating target**" means the subject of a credit rating and may be a person, debt securities or an agreement to provide credit;

   ~~(c)~~(d) "**rated entity**" means the rating target or, in the case of a rating target that is debt securities or an agreement to provide credit, the issuer of the debt securities or the person agreeing to provide credit; and

   ~~(d) "**structured investment product**" includes a structured investment product (regardless of the legal form that it may take):-~~

      ~~(i) which, or the issue of any advertisement, invitation or document in respect of which, requires the Commission's authorization pursuant to Part IV of the SFO; and~~

      ~~(ii) which involves derivative arrangements and is commonly regarded in the market as an equity, index, commodity or credit-linked investment product.~~

   (e) "**structured finance products**" means securities or a money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction.

[1] http://www.iosco.org/library/pubdocs/pdf/IOSCOPD271.pdf

Part 1 – Quality And Integrity Of The Rating Process

Quality of the Rating Process

4. A ~~licensed or registered person~~ CRA should adopt, implement and enforce written procedures to (a) document reporting lines and allocate functions and responsibilities, and (b) ensure that the credit ratings it prepares are based on a thorough analysis of all information known to the ~~licensed or registered person~~CRA that is relevant to its analysis according to the ~~licensed or registered person's~~CRA's published rating methodology.

5. A ~~licensed or registered person~~CRA should use rating methodologies that are rigorous, systematic, and, where possible, which result in ratings that can be subjected to some form of objective validation based on historical experience, including back-testing.

6. A ~~licensed or registered person~~ CRA should keep records properly and in line with all applicable statutory requirements, including the provisions of the Securities and Futures (Keeping of Records) Rules (Cap. 571O). Proper record keeping includes maintaining records to support credit ratings prepared by ~~the licensed or registered person~~ a CRA. A ~~licensed or registered person~~CRA should keep such records for not less than seven years, in writing in the Chinese or English language, or in such a manner as to enable the records to be readily accessible and readily convertible into written form in the Chinese or English language.

7. A ~~licensed or registered person~~ CRA should use representatives who, individually or collectively (particularly where rating committees are used), have appropriate knowledge and experience in developing a rating for the type of credit being applied. Representatives should apply a given methodology in a consistent manner, as determined by the ~~licensed or registered person~~CRA.

8. A ~~licensed or registered person~~CRA should ensure that the credit ratings it prepares are assigned by the ~~licensed corporation or registered institution~~CRA (or its affiliate~~sd corporation~~) and not by any individual representative.

9. A ~~licensed or registered person~~ CRA and its representatives should take steps to avoid issuing any credit ratings that contain misrepresentations or are otherwise misleading as to the general creditworthiness of the rating target.

10. A ~~licensed or registered person~~CRA should ensure that it has, and devotes, sufficient resources to carry out high-quality credit assessments of all its rating targets. When deciding whether to rate or continue rating a rating target, it should assess whether it is able to devote sufficient personnel with sufficient skill sets to make a proper rating assessment, and whether its personnel likely will have access to sufficient information needed in order to make such an assessment. A ~~licensed or registered person~~ CRA should adopt reasonable measures so that the information it uses in assigning a rating is of sufficient quality to support a credible rating. A ~~licensed or registered person~~ CRA should refrain from assigning a rating, and should ensure that any existing rating is withdrawn, if the ~~licensed or registered person~~CRA does not have sufficient quality information to support a credible rating. If the rating involves a type of financial product presenting limited historical data (such as an innovative financial vehicle), the ~~licensed or registered~~

personCRA should make clear, in a prominent place within the rating report, the limitations of the rating.

11. A licensed or registered person CRA should establish a formal review function made up of one or more senior staff members with appropriate experience to review the feasibility of providing a credit rating for a financial product that is materially different from the financial products the licensed or registered personCRA currently rates.

12. A licensed or registered personCRA should establish and implement a rigorous and formal review functions responsible for periodically (and at least annually) reviewing (a) the methodologies and models, and significant changes to the methodologies and models, it uses, and (b) the adequacy and effectiveness of its systems and internal control mechanisms. Where feasible and appropriate for the size and scope of its credit rating services, tThis function should be independent of the business lines that are principally responsible for rating various classes of rating targets. The findings of any such review should be comprehensively recorded in a written report, a copy of which should be provided to the SFC forthwith upon its completion. A licensed or registered personCRA should take appropriate measures to address any deficiencies identified during the course of any such review.

13. A licensed or registered person CRA should assess whether existing methodologies and models for determining credit ratings of structured investmentfinance products are appropriate when the risk characteristics of the assets underlying a structured investmentfinance product change materially. In cases where the complexity or structure of a new type of structured investmentfinance product or the lack of robust data about the assets underlying the structured investmentfinance product raise serious questions as to whether the licensed or registered persona CRA can determine a credible credit rating for it, the licensed or registered personCRA should refrain from issuing a credit rating.

14. A licensed or registered person CRA should structure its rating teams to promote continuity and avoid bias in the rating process. Where practicable, in view of a licensed or registered person'sCRA's staffing resources, representatives who are involved in the rating process should be subject to an appropriate rotation mechanism which should provide for gradual change in rating teams.

Monitoring and Updating

15. A licensed or registered person CRA should ensure that adequate personnel and financial resources are allocated to monitoring and updating its ratings. Except for ratings that clearly indicate they do not entail ongoing surveillance, once a rating is published the licensed or registered personCRA should monitor, on an ongoing basis, and update the rating by:

    (a) regularly rReviewing, at least annually, the rating target's creditworthiness;

    (b) iInitiating a review of the status of the rating, which is consistent with the applicable rating methodology, upon becoming aware of any information that might reasonably be expected to result in includingthe rating requiring revision or termination of the rating, consistent with the applicable rating methodology; and

(c) ~~u~~Updating the rating on a timely basis, as appropriate, based on the results of such review.

16. Subsequent monitoring should incorporate all cumulative experience obtained. Changes in methodologies, models or key assumptions used in preparing credit ratings should be applied where appropriate to both initial ratings and subsequent ratings. A ~~licensed or registered person~~CRA should review affected credit ratings as soon as possible and not later than ~~within~~ six months after the change, and should in the meantime place those ratings under observation.

17. If a ~~licensed or registered person~~CRA uses separate analytical teams for determining initial ratings and for subsequent monitoring of ratings, each team should have the requisite level of expertise and resources to perform their respective functions in a timely manner.

18. Where a rating is made available to the public, the ~~licensed or registered person~~CRA should in a timely manner publicly announce (or ensure that its affiliate publicly announces) if the rating is discontinued. Where a rating is provided only to subscribers, the ~~licensed or registered person~~CRA should in a timely manner announce (or ensure that its affiliate announces) to the subscribers if the rating is discontinued. In both cases, the ~~licensed or registered person~~CRA should ensure that continuing publications of the discontinued rating indicate the date the rating was last updated and the fact that the rating is no longer being updated.

19. A ~~licensed or registered person~~ CRA should ensure that its "private ratings" (prepared pursuant to an individual order, and which are provided exclusively to the person who placed the order without being intended for dissemination to the public or distribution by subscription, whether in Hong Kong or elsewhere), are only subsequently disseminated to the public or distributed by subscription, whether in Hong Kong or elsewhere, if such ratings have been prepared in compliance with the provisions of this Code.

Integrity of the Rating Process

20. A ~~licensed or registered person~~ CRA and its representatives should deal fairly and honestly with issuers, investors, other market participants, and the public.

21. Representatives of a ~~licensed or registered person~~CRA should maintain high standards of integrity, and a ~~licensed or registered person~~CRA should not employ individuals with demonstrably compromised integrity.

22. A ~~licensed or registered person~~ CRA and its representatives and employees should not, either implicitly or explicitly, give any assurance or guarantee of a particular rating prior to the ~~issue of a~~ rating assessment. This does not preclude a ~~licensed or registered person~~CRA from developing prospective assessments used in structured ~~investment~~finance products and similar transactions.

23. A ~~licensed or registered person~~ CRA should prohibit its representatives who are involved in the rating process from making proposals or recommendations regarding the design of structured ~~investment~~finance products that the ~~licensed or registered person~~CRA rates.

24. A ~~licensed or registered person~~ CRA should institute policies and procedures that clearly specify a person responsible for compliance by the ~~licensed or registered person~~CRA and

its employees with the provisions of its code of conduct (as further described under paragraph ~~71~~68 of this Code) and with any law, rules, regulations, ~~and~~ codes or other requirements which apply to the CRA and are issued, administered or ~~issued~~enforced by the SFC ~~and the requirements of~~ or any other regulatory authority ~~which apply to the licensed or registered persons~~or agency. This person's reporting lines and compensation should be independent of the ~~licensed or registered person's~~CRA's rating operations.

25. A ~~licensed or registered person~~ CRA should institute policies and procedures requiring its representatives and employees, upon becoming aware that another representative, employee or entity under common control with the ~~licensed or registered person~~CRA is engaging, or has engaged, in conduct that is illegal, unethical or contrary to the ~~licensed or registered person's~~CRA's code of conduct (as further described under paragraph 68 of this Code), to report such information immediately to the individual in charge of compliance ("**compliance officer**") or a responsible officer of the ~~licensed or registered person~~CRA, as appropriate, so that proper and appropriate action may be taken. A ~~licensed or registered person's~~CRA's representatives and employees are not necessarily expected to be experts in the law. Nonetheless, they are expected to report ~~the~~ such activities ~~that~~ as a reasonable person in their position would question or be concerned over. ~~A licensed or registered person~~ A CRA should ensure that its compliance officer or responsible officer, who receives such a report from a representative or employee, is obligated to take appropriate action, ~~as determined~~including such action as is required by any law, rules, regulations ~~and~~, codes or other requirements which apply to the CRA and are issued, administered or ~~issued~~enforced by the SFC, ~~the requirements of~~ or any other regulatory authority ~~which apply to the licensed or registered persons~~or agency, and by the CRA's own rules, guidelines ~~and~~ or codes ~~set forth by the licensed or registered person~~. A ~~licensed or registered person~~CRA should not retaliate, and should prohibit retaliation by its other representatives or employees, ~~or by the licensed corporation or registered institution itself,~~ against any representative~~s~~ or employee~~s~~ who, in good faith, make~~s~~ such a report~~s~~.

Part 2 – Independence And Avoidance Of Conflicts Of Interest

General

26. A ~~licensed or registered person~~CRA should ~~not~~neither forbear ~~or~~nor refrain from preparing or revising any rating based on the potential effect (economic, political, or otherwise) on the ~~licensed or registered person~~CRA, an issuer, an investor, or other market participant.

27. A~~ licensed or registered person~~ CRA and its representatives should use care and professional judgment to maintain both the substance and appearance of independence and objectivity.

28. The determination of a credit rating should be influenced only by factors relevant to the credit assessment.

29. The credit rating a ~~licensed or registered person~~CRA assigns to a rating target should not be affected by the existence of, or potential for, a business relationship between the ~~licensed or registered person~~CRA (or its affiliates) and the issuer (or its affiliates), or any other party, or by the non-existence of such a relationship.

30. A ~~licensed or registered person~~CRA should ~~separate, operationally and legally, its credit rating~~ not carry on any business ~~and representatives who are involved in the rating process from any other businesses of the licensed or registered person, including consulting businesses,~~ which ~~may present a~~ can reasonably be considered to have the potential to give rise to any conflict of interest in relation to its business of providing credit rating services. A ~~licensed or registered person~~CRA should ~~ensure that ancillary business operations which do not necessarily present conflicts of interest with the licensed or registered person's rating business~~ have in place procedures and mechanisms designed to minimize the likelihood ~~that~~of conflicts of interest ~~will~~ arising, and to identify any conflict of interest should it arise, in relation to the conduct by it of any ancillary business. A ~~licensed or registered person~~CRA should also define what it considers~~, and does not consider,~~ to be an ancillary business and why it cannot reasonably be considered to have the potential to give rise to any conflict of interest with the CRA's credit rating business. For the avoidance of doubt, a CRA should not provide consultancy or advisory services to a rated entity, or a related party of a rated entity, regarding the corporate or legal structure, assets, liabilities or activities of that rated entity or related party.

31. A~~ licensed or registered person~~ CRA should not enter into any contingent fee arrangement for providing credit rating services. Contingent fees are fees calculated on a predetermined basis relating to the outcome of a transaction or the result of the services performed by the firm. For the purposes of this paragraph, a fee is not regarded as being contingent if established by a court or other public authority.

Procedures and Policies

32. A~~ licensed or registered person~~ CRA should adopt written internal procedures and mechanisms to (a) identify, and (b) eliminate, or manage and disclose, as appropriate, any actual or potential conflicts of interest that may influence (i) the ratings ~~a licensed or registered person~~the CRA makes, or (ii) the judgment and analyses of the representatives

who are involved in the preparation of ratings. A ~~licensed or registered person's~~CRA's code of conduct (as further described under paragraph 68 of this Code) should also state that the ~~licensed or registered person~~CRA will disclose such conflict avoidance and management measures.

33. A ~~licensed or registered person's~~CRA's disclosures of actual ~~and~~or potential conflicts of interest should be complete, ~~timely,~~ clear, concise, specific and prominent, and should be made in a timely manner. A CRA should also make full public disclosure of its ancillary services and update such disclosure in a timely manner.

34. A ~~licensed or registered person~~ CRA should publicly disclose the general nature of its compensation arrangements with rated entities, including:

    (a) Where a ~~licensed or registered person~~ CRA or ~~its related corporation~~any affiliate of the CRA that is a credit rating agency, receives from a rated entity compensation unrelated to its ratings service, ~~a licensed or registered person~~the CRA should disclose the proportion that such ~~non-rating fees~~ compensation constitutes against the fees that the ~~licensed or registered person~~CRA, or its ~~corporate group~~affiliate, receives from ~~the~~such rated entity for the provision of ratings services; and

    (b) A ~~licensed or registered person~~CRA should disclose if it or its ~~corporate group~~any affiliate that carries out credit rating activities, receives ~~10~~5% or more of its annual revenue from a single issuer, originator, arranger, client or subscriber (including any affiliates of that issuer, originator, arranger, client or subscriber).

35. ~~Licensed or registered persons~~CRAs should encourage issuers and originators of structured ~~investment~~finance products to publicly disclose all relevant information regarding these products so that investors and other ~~licensed or registered persons~~CRAs can conduct their own analyses independently of the ~~licensed or registered person~~CRA contracted by the issuers or originators to provide a rating. ~~Licensed or registered persons~~ CRAs should ensure that rating announcements include disclosure as to whether the issuer of a structured ~~investment~~finance product has informed ~~it~~the CRA that it is publicly disclosing all relevant information about the product being rated or ~~if~~whether the information remains non-public.

36. A ~~licensed or registered person~~CRA should ensure that it and its representatives and employees do not engage in any securities or derivatives trading ~~presenting~~giving rise to conflicts of interest with the ~~licensed or registered person's~~CRA's rating activities, or which might reasonably be expected to give rise to such conflicts of interest.

37. In instances where rated entities (e.g. governments) have, or are simultaneously pursuing, oversight functions related to ~~the licensed or registered person~~a CRA, the ~~licensed or registered person~~ CRA should use representatives to prepare and revise its ratings who are not the same individuals involved in its oversight issues.

~~38. Licensed or registered persons issuing or maintaining a credit rating for securities or a money market instrument issued by an asset pool or as part of any asset-backed or mortgage-backed securities transaction that was paid for by the issuer, sponsor, or underwriter of the securities or money market instrument, should maintain on a password-protected website a list of all such securities or money market instruments for which the licensed or registered person maintains or is currently in the process of determining a credit rating. The list should include information identifying the type of securities or money~~

market instrument, the name of the issuer, the date the rating process was initiated, and the internet address where the issuer, sponsor, or underwriter of the securities or money market instrument represents that information (which currently should be relied on to determine or monitor the credit rating) about the characteristics of the assets underlying or referenced by the securities or money market instrument, the legal structure of the securities or money market instrument, and the characteristics and performance of the assets underlying or referenced by the securities or money market instrument can be accessed.

39. Licensed or registered persons maintaining such a website should provide free and unlimited access to such website during each calendar year to any Type 10 licensee, providing such licensee:

(a) Determined and maintained credit ratings for at least 10% of the issued securities and money market instruments for which it accessed information pursuant to this paragraph in the previous calendar year, if it accessed such information for ten or more issued securities or money market instruments; or

(b) Has not accessed information pursuant to this paragraph ten or more times during the previous calendar year.

40. Licensed or registered persons maintaining such a website should obtain from the issuer, sponsor, or underwriter of all such securities or money market instruments, a written representation that can reasonably be relied upon that the issuer, sponsor, or underwriter will:

(a) Maintain on a password-protected website information (which currently should be relied on to determine or monitor the credit rating) about the characteristics of the assets underlying or referenced by such securities or money market instruments, the legal structure of the securities or money market instruments, and the characteristics and performance of the assets underlying or referenced by the securities or money market instruments; and

(b) Provide free and unlimited access to such website during each calendar year to any Type 10 licensee, providing such licensee:

(i) Determined and maintained credit ratings for at least 10% of the issued securities and money market instruments for which it accessed information pursuant to this paragraph in the previous calendar year, if it accessed such information for ten or more issued securities or money market instruments; or

(ii) Has not accessed information pursuant to this paragraph ten or more times during the previous calendar year.

Representatives' Independence

41.38. Reporting lines for representatives, and their compensation arrangements, should be structured to eliminate, or effectively manage, actual andor potential conflicts of interest.

42.39. A licensed or registered person'sCRA's code of conduct (as further described under paragraph 68 of this Code) should state that a representative will not be compensated or

evaluated on the basis of the amount of revenue that the ~~licensed or registered person~~CRA derives from rated entities that the representative rates or with which the representative regularly interacts.

~~43.~~40. A ~~licensed or registered person~~CRA (or its ~~related corporation~~affiliates) should conduct formal and periodic reviews of compensation policies and practices for its representatives and employees who participate in, or who might otherwise have an effect on, the rating process to ensure that these policies and practices do not compromise the objectivity of its rating process.

~~44.~~41. Representatives who are directly involved in the rating process should not initiate, or participate in, discussions regarding fees or payments with any entity they rate.

~~45.~~42. No ~~licensed or registered person (or its~~ representative~~)~~ or employee of a CRA should prepare (or participate in or otherwise influence the determination of) a rating of any particular rating target~~)~~ if the ~~licensed or registered person (or its~~ representative~~, as applicable)~~ or employee of the CRA:

(a) Owns securities or derivatives of the rated entity, other than holdings in collective investment schemes;

(b) Owns securities or derivatives of any entity related to a rated entity, the ownership of which may cause, or may be perceived as causing, a conflict of interest, other than holdings in collective investment schemes;

(c) Has had a recent employment or other significant business relationship with the rated entity that may cause, or may be perceived as causing, a conflict of interest;

(d) Has an immediate relation (i.e. a spouse, partner, parent, child, or sibling) who currently works for the rated entity; or

(e) Has, or had, any other relationship with the rated entity or any related ~~entity~~party thereof, that may cause, or may be perceived as causing, a conflict of interest.

~~46.~~43. A representative involved in the rating process (or his/her spouse, partner, minor children or any account controlled by the representative in which the representative has a beneficial interest) should not buy or sell, or engage in any transaction ~~in~~involving, any securities or derivative based on securities issued, guaranteed, or otherwise supported by any entity within such representative's area of primary analytical responsibility, other than holdings in collective investment schemes.

~~47.~~44. Without prejudice to paragraph 2.4 of the General Code of Conduct ~~for Persons Licensed by or Registered with the Securities and Futures Commission~~, representatives and employees of a ~~licensed or registered person~~CRA should be prohibited from soliciting money, gifts or favours from anyone with whom the ~~licensed or registered person~~CRA does business and should be prohibited from accepting gifts offered in the form of cash or any gifts exceeding a minimal monetary value.

~~48.~~45. Any representative of a CRA, who becomes involved in any personal relationship that creates the potential for any real or ~~apparent~~potential conflict of interest (including, for example, any personal relationship with an employee of a rated entity or agent of such entity within his or her area of analytic responsibility), should be required to disclose such relationship to the compliance officer or responsible officer of the ~~licensed or registered~~

~~person~~CRA who is designated for such purpose by the ~~licensed or registered person's~~CRA's compliance policies.

~~49.~~46. A ~~licensed or registered person~~CRA should establish policies and procedures for reviewing the past work of representatives ~~that~~who leave the employ of the ~~licensed or registered person~~CRA and join an issuer the representative has been involved in rating, or a financial firm with which the representative has had significant dealings as part of his or her duties as a representative or employee of the ~~licensed or registered person~~ CRA.

Part 3 – Responsibilities To The Investing Public and Issuers

Transparency and Timeliness of Ratings Disclosure

50.47. A ~~licensed or registered person~~CRA should ensure that its ratings and updates are distributed in a timely manner.

51.48. A ~~licensed or registered person~~ CRA should ensure that the policies for distributing its ratings and updates are publicly disclosed.

52.49. A ~~licensed or registered person~~ CRA should ensure that each of its ratings includes (a) a clear indication of when ~~the rating was first distributed and when~~ it was last updated, and (b) a clear and prominent statement identifying the name and job title of the lead rating analyst who is responsible for the rating and the name and the position of the person primarily responsible for approving the ratings. Ratings of debt securities should include information on whether the credit rating concerns newly issued debt securities and whether the ~~licensed or registered person~~CRA is rating the debt securities for the first time. Each rating announcement should also indicate the principal methodology or methodology version that was used in determining the rating and where a description of that methodology can be found. Where the rating is based on more than one methodology, or where a review of only the principal methodology might cause investors to overlook other important aspects of the rating, the ~~licensed or registered person~~CRA should ensure that this fact is explained in the ratings announcement. Such explanation should include a discussion of how the different methodologies and other important aspects were factored into the rating decision.

53.50. A ~~licensed or registered person~~ CRA should ensure that sufficient clear and easily comprehensible information is published about its procedures, methodologies and assumptions (including financial statement adjustments that deviate materially from those contained in the issuer's published financial statements and a description of the rating committee process, if applicable) to enable other parties to understand how a rating was determined. This information should include (but not be limited to) the meaning of each rating category and the definition of default or recovery, and the time horizon the ~~licensed or registered person~~ CRA used when making a rating decision. A CRA should also ensure that all material sources, including the rated entity and, where appropriate, a related party of the rated entity, which were used to prepare the credit rating, are identified. An indication should also be given as to whether the credit rating has been disclosed to the rated entity or to its related party and, following such disclosure, whether the credit rating has been amended before being issued.

54.51. A ~~licensed or registered person~~ CRA should disclose to what extent it has examined the quality of information used in the rating process and whether it is satisfied with the quality of information it bases its rating on.

55.52. Where a ~~licensed or registered person~~CRA rates a structured ~~investment~~finance product, ~~the licensed or registered person~~it should ensure that the public (in the case of a rating which is made available to the public) or subscribers (in the case of a rating which is made ~~provided~~available only to subscribers) are provided with sufficient information about its loss and cash-flow analysis, and an indication of any expected change in the credit rating, so that an investor allowed to invest in the product can understand the basis for the rating. A ~~licensed or registered person~~CRA should also ensure disclosure of the degree to which it

analyzes how sensitive a rating of a structured ~~investment~~ finance product is to changes in the ~~licensed or registered person's~~ CRA's underlying rating assumptions. A CRA should disclose, on a timely and ongoing basis, information concerning all structured finance products submitted to it for its initial review or for a preliminary rating. Such disclosure should be made irrespective of whether the issuer of such a product engages the CRA to provide a final rating. A CRA should state the level of assessment it has performed concerning the due diligence processes conducted in relation to the underlying finance products, or other assets, of structured finance products. The CRA should disclose whether it has undertaken any assessment of such due diligence processes or whether it has relied on a third-party assessment, indicating how the outcome of such assessment influences the credit rating.

~~56.~~53. A ~~licensed or registered person~~CRA should differentiate ratings of structured ~~investment~~finance products from traditional corporate bond ratings, preferably through a different rating symbology or by using an additional symbol which differentiates them from rating categories used for other rating targets. A ~~licensed or registered person~~CRA should also disclose how this differentiation functions. A ~~licensed or registered person~~CRA should clearly define a given rating symbol and apply it in a consistent manner for all types of debt securities to which that symbol is assigned.

~~57.~~54. A ~~licensed or registered person~~ CRA should assist investors in developing a greater understanding of what a credit rating is, and the limits to which credit ratings can be put to use vis-à-vis a particular type of financial product that the ~~licensed or registered person~~CRA rates. A ~~licensed or registered person~~CRA should clearly indicate the attributes and limitations of each credit rating, and the limits to which the ~~licensed or registered person~~CRA verifies information provided to it by the rated entity.

~~58.~~55. When issuing or revising a credit rating, the ~~licensed or registered person~~CRA should explain in its press releases and reports the key elements underlying the rating.

~~59.~~56. Where feasible and appropriate, prior to issuing or revising a rating, the ~~licensed or registered person~~CRA should inform the issuer of the critical information and principal considerations upon which a rating will be based and afford the issuer an opportunity to clarify any likely factual misperceptions or other matters that the ~~licensed or registered person~~CRA would wish to be made aware of in order to produce an accurate rating. A ~~licensed or registered person~~CRA will duly evaluate the response. Where, in particular circumstances, the ~~licensed or registered person~~CRA has not informed the issuer prior to issuing or revising a rating, the ~~licensed or registered person~~CRA should inform the issuer as soon as practical thereafter and, generally, should explain the reason for the delay.

~~60.~~57. In order to promote transparency and to enable the market to best judge the performance of ~~the~~its ratings, a ~~licensed or registered person~~CRA should, where sufficient historical data exists, publish information about the historical default rates of rating categories and about ratings transition frequency. In addition, a ~~licensed or registered person~~CRA should disclose whether the default rates of rating categories have changed over time. ~~–~~ The information should be sufficient to help interested parties understand the historical performance of each category, as well as whether ~~and how~~ rating categories have changed and, if so, how. It should also help interested parties draw quality comparisons among ratings given by different ~~licensed or registered persons~~CRAs. If the nature of ~~the~~a rating, or other circumstances, make ~~a~~an historical default rate inappropriate, statistically invalid, or otherwise likely to mislead the users of the rating, the ~~licensed or registered person~~CRA should explain this. This information should include verifiable~~,~~ and quantifiable historical information about the performance of its rating opinions, organized and

structured, and, where possible, standardized, in such a way as to assist investors in drawing performance comparisons between different providers of credit rating services.

61.58. A licensed or registered personCRA should state prominently in each credit rating whether or not the rated entity, or any related party of the rated entity thereof, participated in the credit rating process, and (for an unsolicited rating) whether the licensed or registered personCRA had access to the accounts and other relevant internal documents of the rated entity or its related third party. A licensed or registered personCRA should also disclose its policies and procedures regarding unsolicited ratings.

62.59. Because users of credit ratings rely on an existing awareness of a licensed or registered person'sCRA's methodologies, practices, procedures and processes, the licensed or registered persona CRA should fully and publicly disclose any material modification to its methodologies and significant practices, procedures, and processes. Where feasible and appropriate, disclosure of such material modifications should be made prior to their going into effect. A licensed or registered person CRA should carefully consider the various uses of credit ratings before modifying its methodologies, practices, procedures and processes. When methodologies, models or key rating assumptions used in preparing any of its credit ratings are changed, a licensed or registered personCRA should immediately disclose the likely scope of credit ratings to be affected by using the same means of communication as was used for the distributions of the affected credit ratings.

The Treatment of Confidential Information

63.60. A licensed or registered person CRA should adopt procedures and mechanisms to protect the confidential nature of information shared with themit by issuers where this occurs under the terms of a confidentiality agreement or otherwise under a mutual understanding that the information is shared confidentially. Unless otherwise permitted by the confidentiality agreement and consistent with applicable laws or regulations, the licensed or registered person (ora CRA and its representatives, as applicable) and employees should not disclose confidential information in press releases, through research conferences, to future employers, or in conversations with investors, other issuers, or other persons, or otherwise.

64.61. A licensed or registered person CRA should use confidential information only for purposes related to its rating activities or in accordance with any confidentiality agreements with the issuer.

65.62. A licensed or registered personCRA should take all reasonable measures to protect all property and records belonging to it, or in its possession, from fraud, theft or misuse.

66.63. Licensed or registered personsA CRA should prohibit theiritsits representatives and employees from engaging in transactions in securities when they possess confidential information concerning the issuer of such securities. A representative (or his/her spouse, partner, minor children or any account controlled by the representative in which the representative has a beneficial interest) should not engage in transactions in securities when the representative possesses confidential information concerning the issuer of such securities.

67.64. In preservation of confidential information, representatives and employees of licensed or registered personsCRAs should familiarize themselves with the internal securities trading

policies maintained by the ~~licensed or registered person~~CRA, and periodically certify their compliance as required by such policies.

~~68.~~65. A ~~licensed or registered person~~CRA should ensure that its representatives and employees do not selectively disclose any non-public information about ratings, or the possible future issue or revision of ratings of the ~~licensed or registered person~~CRA, except to the issuer or its designated agents.

~~69.~~66. A ~~licensed or registered person~~CRA should ensure that it and its representatives and employees do not share confidential information entrusted to it with ~~employees of any affiliated entities~~its affiliates that are not ~~regulated~~ credit rating agencies, or with the employees of such affiliates. A CRA and its ~~R~~representatives and employees should not share confidential information within the CRA, or with ~~other~~its affiliates that are credit rating agencies (including the representatives ~~or~~and employees of ~~the licensed or registered person or of any affiliated entities~~such affiliates), except on an "as needed" basis and as permitted under any relevant confidentiality agreement.

~~70.~~67. A ~~licensed or registered person~~ CRA should ensure that its representatives and employees do not use or share confidential information for the purpose of trading securities, or for any other purpose except carrying on Type 10 regulated activity.

Part 4 – Disclosure Of The Code Of Conduct And Communication With Market Participants

~~71.~~68. A ~~licensed or registered person~~ CRA should have its own code of conduct and should disclose it to the public and describe how its provisions fully implement the provisions of this Code. ~~If a licensed or registered person's code of conduct deviates from this Code, the licensed or registered person should explain where and why these deviations exist, and how any deviations nonetheless achieve the objectives contained in this Code.~~ A ~~licensed or registered person~~CRA should also describe generally how it intends to enforce its code of conduct and should disclose, on a timely basis, any changes to its code of conduct ~~or~~and how it is implemented and enforced.

~~72.~~69. A ~~licensed or registered person~~ CRA should establish a function within its organization (or that of its affiliates) charged with communicating with market participants and the public about any questions, concerns or complaints that the ~~licensed or registered person~~CRA may receive. The objective of this function should be to help ensure that the ~~licensed or registered person's~~ officers and management of the CRA are informed of those issues that they would want to be made aware of when setting the organization's policies.

~~73.~~70. A ~~licensed or registered person~~CRA should publish in a prominent position on its home webpage links to: (a) the ~~licensed or registered person's~~CRA's code of conduct; (b) a description of the methodologies it uses; and (c) information about the ~~licensed or registered person's~~CRA's historic ratings performance data, or that of any of its ~~corporate group~~affiliate that carries out credit rating activities.

71. A CRA should ensure that details of the following information are available to the public on an annual basis:

(a) The internal control mechanisms adopted by it to ensure the quality of its credit rating activities;

(b) Its record-keeping policy;

(c) Its quality control system; and

(d) Its management and rating analyst rotation policy.