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March 31, 2011

To: ESMA
Via e-mail to: www.esma.europa.eu

Re: DBRS' response to Consultation Paper - ESMA Guidelines on the application of the endorsement regime under Article 4 (3) of the Credit Rating Regulation 1060/2009 (Consultation Paper)

DBRS[1] appreciates the opportunity to provide its comments on the Consultation Paper.

DBRS understands that the Credit Rating Regulation 1060/2009 is in process of being modified to reflect the European Securities and Markets Authority (ESMA) as fully responsible for the supervision of credit rating agencies (CRAs) in Europe (revised CRA Regulation). In line with the revised CRA Regulation, the guidance on the endorsement regime initially issued by the former Committee of European Securities Regulators (CESR) must be updated and issued by ESMA by June 7, 2011.

The Consultation Paper seeks to clarify the endorsement regime and update the endorsement guidelines. ESMA currently interprets that "as stringent as" CRA requirements must be established by law or regulation in a third country by June 7, 2011 in order for the use of endorsement. It does not currently support the interpretation that a third country CRA would be permitted to follow "as stringent as" standards through its own policies and procedures. The Consultation Paper states that the CRA Regulation does not envisage a dual system of compliance or some combination of a third country legal/regulatory regime topped up by policies and procedures adopted by the third country CRA.

By way of background, endorsement allows the use in the EU of ratings issued outside the EU under certain conditions. Among other conditions, an EU-registered (or seeking registration) CRA must verify and demonstrate on an ongoing basis that the conduct of credit rating activities by the third-country CRA resulting in the issuing of the credit rating to be endorsed fulfills requirements which are at least "as stringent as" the requirements set out in Articles 6 to 12 of the CRA Regulation.

In DBRS' view, the concept of "as stringent as" means whether the mechanisms and internal controls established by a third country CRA are functionally equivalent to those under the CRA Regulation. It does not mean that there are official regulatory requirements established by law in the third country. The latter was meant for the certification mechanism which refers to CRAs which are not systemically important to the financial stability or integrity of the financial markets of one or more EU Member States.

DBRS does not support ESMA's current interpretation that it cannot supervise EU-registered CRAs who use endorsement without an equivalent third country regulatory regime in place. The key test

[1] DBRS operates its rating business through DBRS Limited, DBRS, Inc. and DBRS Ratings Limited.

should be whether a third country CRA adheres to standards as stringent as those required by the CRA Regulation, whether or not a third country regime has been enacted into law. Article 4.6 of the CRA Regulation provides that an equivalence decision is sufficient to fulfill Article 4.3, but it is not necessary. Where the (EU) Commission has recognized the third country regime to be equivalent under Article 5, it will no longer be necessary for the endorsing CRA to verify or demonstrate that they follow policies and procedures "as stringent as" the CRA Regulation.

Apart from the interpretation of "as stringent as", the June 7, 2011 deadline is problematic. Of the twenty countries listed in the Consultation Paper, at present, only Japan is considered to have a technically equivalent regulatory regime. A requirement that "as stringent as" third country regulatory regimes must be in place by June 7, 2011 will have a significant impact on the EU capital markets due to the high number of non-endorsed ratings based on data outlined in the Consultation Paper. At the time of writing, the U.S. NRSRO regime is considered broadly equivalent, and it is uncertain when the applicable new CRA requirements under the Dodd-Frank Act[2] will be in place to enable the EU to update its decision. Canada has recently published a revised regulatory proposal for CRAs that it acknowledges will not be implemented in time to meet the June 7, 2011 deadline[3].

The Consultation Paper outlines the substantive negative economic impact in the form of the additional cost of capital incurred by financial institutions from the inability to endorse ratings. The capital cost would mainly derive from securitization positions, in particular from ratings in the U.S. and Canada, but also in South America and Australia. Intermediaries have also flagged non-endorsable risks for corporate and sovereign exposures in Asia. DBRS suggests that the cost-benefit to financial institutions and other market participants needs to be more heavily considered.

In terms of the impact on CRAs, apart from the operational cost of restructuring parts of their business (relocation of analysts, systems etc.), there is an impractical element that the Consultation Paper has not considered. Analytical expertise of issuers with heavy exposure to non-EU regions may not be readily available in the EU and where relocation of analysts is not possible, this leaves a gap in affected ratings coverage where investors request such ratings. Morever, the European Central Bank and other EU regulators espouse the benefits of additional CRA competition and a two ratings market.

There is an additional unstated impact on EU regulators regarding ESMA's interpretation. For endorsed ratings, the third country regime would be subject to two sets of supervision, direct supervision by its home regulator and indirect supervision through the endorsing CRA registrant by EU supervisors. DBRS does not believe the CRA Regulation and EU regulators envisaged additional regulatory responsibilities. Rather, Article 4.3 stipulates that the third country CRA must be subject to domestic regulatory supervision, and also requires that cooperation agreements be in place between EU and third country regulators.

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[2] Dodd-Frank Wall Street Reform and Consumer Protection Act

[3] Proposed National Instrument 25-101 Designated Rating Organizations, Related Policies and Consequential Amendments

If ESMA takes the position that "as stringent as" requirements must be enforceable in law, then one possible way to mitigate the market impact of the June 7 deadline is to permit third country CRAs the flexibility or choice to demonstrate that they have implemented equivalent requirements on a voluntary basis awaiting implementation of equivalent domestic regulatory regimes. This approach would address the situations in the U.S. and Canada, at a minimum.

As part of its EU registration application, DBRS has implemented an endorsement policy which is disclosed on its public website under http://www.dbrs.com/eudisclosures and a standard credit rating process that includes requirements which are as stringent as the requirements set out in Articles 6 to 12 of the EU CRA Regulation. Once it is permitted to endorse, DBRS rating announcements for endorsed ratings will clearly indicate that the rating is an "endorsed rating". Endorsed Ratings will be publicly available on www.dbrs.com.

DBRS would be pleased to further discuss any of the matters raised herein and/or provide additional information. Please do not hesitate to contact me.

Very truly yours,

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