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QUESTIONNAIRE REGARDING THE RATING OF STRUCTURED FINANCE INSTRUMENTS¹

As previously announced in its public statement (CESR 07-304), CESR is in the process of preparing its second annual report on the credit rating agencies' (CRAs) compliance with the IOSCO Code of Conduct.

To this respect, CESR sent a letter to the 4 CRAs that have chosen to adhere to the voluntary framework requesting them to provide information on the changes introduced in their codes since the publication of CESR's first annual report. In their responses to CESR (attached to the public statement), the CRAs informed that for the time being no changes have been made in their internal codes. However, some CRAs informed that they do intend to revisit their codes in the next several months taking into account not only CESR's December 2006 report but also the new SEC NRSRO rules and the outcome of IOSCO's consultation report on CRAs (that discusses potential areas for clarification of the IOSCO code).

Considering this information, the European Commission has agreed to CESR's suggestion to set April 30th 2008 (instead of 31st December 2007) as new deadline for the preparation of CESR's second annual report on CRAs, to allow CESR to assess the changes in the CRAs codes when they take place.

In the meantime CESR will work on other relevant sections of the report and specially on the analysis of rating process as regards structured finance instruments (e.g. quality of the rating process, conflicts of interests) as specifically requested by the European Commission in its letter to CESR (attached to the public statement).

To this effect, CESR is publishing today a questionnaire regarding the rating of structured finance instruments. The purpose of this questionnaire is to enable CESR to gather information from interested parties on the functioning of this specific segment of the rating business.

To facilitate the participation in this consultation, CESR has divided the questionnaire in two sections; the first one is addressed to the credit rating agencies and the second one to all market participants. Nevertheless, CESR would welcome comments from anyone on the first section as well. **The deadline for comments has been extended to 10 September 2007 and if specifically requested, respondents may submit their responses on a confidential basis.**

¹ According to the Committee on the Global Financial System of the Bank for International Settlements, structured finance involves the pooling of assets and the subsequent sale to investors of claims on the cash flows backed by these pools. Typically, several classes (or "tranches") of securities are issued, each with distinct risk-return profiles. In addition, the underlying collateral asset pool is usually legally separated from the balance sheet of the transaction's originator.



A) QUESTIONS ADDRESSED TO THE CREDIT RATING AGENCIES

Organisation

1. What proportion of your total rating revenue comes from structured finance related activity?²
2. Do you offer non rating “ex post” services related to structured finance products (i.e. pricing or valuation models,)? If yes, what proportion of your total structured finance derived revenue comes from those ancillary/advisory services?
3. Please describe any specificities of the way you determine your fees for the rating of structured finance products as compared to the fees charged in corporate ratings.
4. How are the fees you charge for any “ex post” ancillary/advisory activities determined – are they determined separately from fees relating to the actual rating?
5. How is staff remuneration determined for structured finance ratings analysts? Is this different staff from staff that work on related ancillary/advisory services?

Rating process

6. Is the organisation of the rating process similar for corporate and for structured products? If not, please explain the differences.
7. Which parties does your firm liaise with directly as part of the rating process? Are there clear policies governing how this relationship is conducted?
8. What information about the remuneration for providing the rating is provided to the various parties to the deal?
9. Please describe any specificity regarding your policy of publication of ratings in the structured finance segment.

Rating methodologies

10. How do you adapt your methodologies to market developments? Have you changed them recently? How do you apply the changes to the surveillance of rated transactions?
11. Do you consider that the track record of your ratings of structured finance products supports the appropriateness of your models?
12. To what extent can another rating agency’s underlying ratings be incorporated into a structured finance rating by your firm? Are they treated in the same way as your own underlying ratings? Are there any risks emerging from the use of another agency’s ratings?

On-going surveillance of the transactions

13. How do you monitor rated structured products? What are the main inputs into your review process?
14. Is there any difference between corporate credit ratings and structured finance ratings in terms of the frequency (ie. happen more often) and magnitude (ie. are larger) of rating amendments?
15. Is the internal process for amending a structured finance rating similar to the one for amending a corporate rating?

² The individual percentages will be kept confidential although CESR’s report might provide aggregated data.



Potential conflicts of interest

16. Do you think that the iterative process inherent in rating structured finance transactions may involve additional conflicts of interest compared to those arising in corporate ratings? If yes, how your firm is organised and what additional measures do you have in place to manage those potential conflicts?
17. Do you perceive any potential conflicts of interest between the structured rating activity and any ancillary/advisory services mentioned in question 2?

B) QUESTIONS ADDRESSED TO THE USERS OF RATINGS AND OTHER INTERESTED PARTIES

Please indicate what your role (interest, involvement and experience) is in the structured finance market.

Rating process

1. Do you consider that access to and availability of structured finance ratings (and any subsequent changes) is satisfactory?
2. Are you satisfied with the CRAs disclosures on their fees policy?

Rating methodologies

3. What are your views on the fact that the agencies use different analytical models to assess the portfolio credit risk? Are you satisfied with the way the rating agencies assess such risk?
4. Are you satisfied with the way the rating agencies assess the structural risks of the deals (i.e. legal risks, cash flow analysis, third parties' involvement in the transaction)?
5. Are you satisfied with the way the CRAs disclose their methodologies?

On-going surveillance of the transactions

6. Are you satisfied with the frequency and quality of the information provided by the rating agencies to the market in connection with the monitoring of rated structured products (e.g. monitoring reports, special comments, etc.)? Are you satisfied with the frequency and quality of the information provided by the issuers/arrangers of structured transactions in order to monitor rated structured products?
7. Are you satisfied with the CRAs disclosures on the reasons for a change in a structured finance rating?

Potential risks (conflicts, resourcing)

8. Are there any risks unique to rating structured finance compared to corporate credit rating?
9. Are you aware of any CRAs which provide ex post ancillary/advisory services? If so, do you perceive any potential conflicts of interest between the structured rating activity and any ex post ancillary/advisory services those CRAs may provide (i.e. pricing or valuation models)?
10. Is there a risk of conflicts of interest when a rating agency provides the rating of the provider of credit enhancement to structured finance products it has also rated?
11. Are you satisfied with the way the agencies' communicate the measures they have adopted to manage those potential conflicts of interests?



12. Do you think those measures are effective?
13. Is there sufficient resource and experience at the rating agencies to deal effectively with the demand for structured finance ratings?

IOSCO Code on Structured Finance

14. Does the current IOSCO Code of Conduct for CRAs deal appropriately with the risks in the rating of structured finance?

Additional comments

15. Are there any additional points you would like to raise, on the basis of your experience in the structured finance business?