



Legal Framework for Credit Ratings in Japan

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Background

- Establishment of Credit Rating Agencies (CRAs) in Japan (late 1970's-)
- Use of Credit Rating in Regulation
 - Designated Rating Agencies System (1992-2010)
 - The FSA Commissioner designated certain CRAs as Designated Rating Agencies (DRAs) whose credit ratings may be used in disclosure of corporate affairs under the Financial Instruments and Exchange Act, etc.
 - DRAs system was integrated into the credit rating service provider system in 2010.
 - External Credit Assessment Institutions (2006-present)
 - The FSA Commissioner designates certain CRAs as External Credit Assessment Institutions whose credit ratings may be used in the calculation of bank' capital adequacy ratios.

Introduction of Regulation for CRAs

- Amendment of the Financial Instruments and Exchange Act (June 2009)
 - Consistency with IOSCO Code of Conduct
 - Introduction of the Registration System
 - For the most part in effect on April 1, 2010
- Amendment of the Cabinet Office Ordinance (December 2009)
 - Requirements for establishment of control system (quality control of the rating process, ensuring of independence and fairness, prevention of conflicts of interest), etc.
- Promulgation of the Guidelines for Supervision of CRAs (April 2010)

Overview of Regulation for CRAs

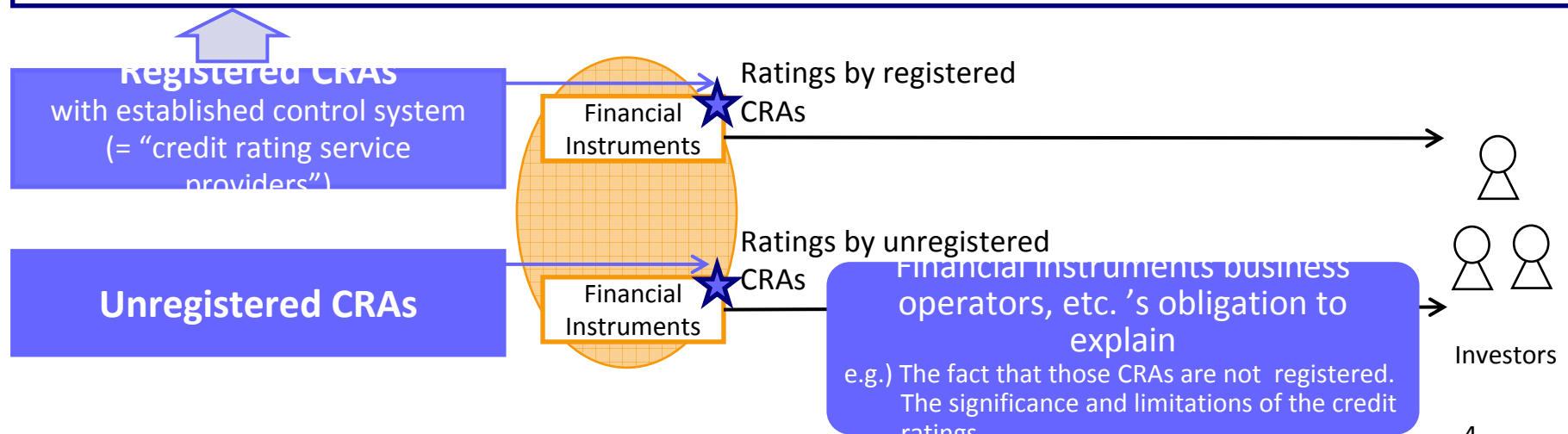
■ Purposes

1. Independence of CRAs from issuers, etc. of the financial instruments that they rate, and prevention of conflicts of interest
2. Quality and fairness in the rating process
3. Transparency for the market participants such as investors

■ Four Major Pillars of Regulation

1. Duty of good faith
2. Information disclosure (Timely disclosure, periodic disclosure)
3. Establishment of control systems (Quality control and fairness of the rating process, prevention of conflicts of interest, etc.)
4. Prohibited Acts (Close relationship with the issuers of the financial instruments to be rated, etc.)

■ Inspection/Supervision, etc



CRAs in Japan

Name of CRAs	Year of establishment
Japan Credit Rating Agency, Ltd.	1985
Rating and Investment Information, Inc. (R&I)	1998 - established by merger of Japan Bond Research Institute(established in 1979) and Nippon Investors Service, Inc. (established in 1985)
Moody's Japan K.K.	1985
Moody's SF Japan K.K.	2010
Standard & Poor's Ratings Japan K.K.	2010 - established Tokyo office in 1985
Fitch Ratings Japan Limited	2010 - established Tokyo office in 1989

(Source) Websites of Japan's FSA, Japan Credit Rating Agency, Ltd., Rating and Investment Information, Inc. , Moody's Japan K.K., Moody's SF Japan K.K., Standard & Poor's Ratings Japan K.K.

Applicability of Regulation to Credit Ratings Determined by Foreign CRAs

- The regulation does not apply to credit rating activities relating to a “non-Japan-related rating,” determined at an overseas location by a foreign CRA which satisfies all of the following conditions:
 - 1) The rating is not a credit rating of a financial instrument that is premised on solicitation by financial instruments business operators, etc. in Japan
 - 2) The rating stakeholders are not domiciled within Japan; and
 - 3) In the case of asset securitization products, the main underlying assets are not located in Japan
- The Designated CRA-Group Supervisory System regarding Explanation
 - If there are registered CRA and unregistered CRAs in the same group, and the FSA Commissioner designates the unregistered CRAs as fulfilling the following conditions, Financial Instrument Business Operators, etc. ‘s obligation to explain is to be reduced.
 - 1) Level of publishing information is the same as that of the registered CRA
 - 2) Rating policy common to the group is adopted
 - 3) Rating policy common to the group is published via the registered CRA

Treatment of Sovereign Debt Ratings in Regulation

- There are no special regulations for sovereign debt ratings in Financial Instruments and Exchange Act in Japan.
- Any legal measures to be taken regarding sovereign debt ratings?
 - Japan's current situation
 - Avoidance of sovereign debt crisis / Purpose of regulation for CRAs (Independence of CRAs and prevention of conflicts of interest, etc.)
 - For enhancement of transparency of credit ratings