

REPUBLIC OF SOUTH AFRICA

CREDIT RATING SERVICES BILL

Draft for public comment  
As approved by Cabinet on 26 July 2011

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*(As introduced in the National Assembly (proposed section 75); explanatory  
summary of Bill published in Government Gazette No.     of     )*  
*(The English text is the official text of the Bill)*  
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(MINISTER OF FINANCE)

## **CREDIT RATING SERVICES BILL**

**To provide for the registration of credit rating agencies; for the control of certain activities of credit rating agencies; conditions for the issuance of credit ratings and rules on the organisation and conduct of credit rating agencies, and for matters connected therewith.**

**BE IT ENACTED** by the Parliament of the Republic of South Africa as follows:—

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## CHAPTER I DEFINITIONS, PURPOSE AND APPLICATION

### Definitions and interpretation

1. (1) In this Act, unless the context indicates otherwise -

“**Board**” means the Financial Services Board, established by section 2 of the Financial Services Board Act;

“**Companies Act**” means the Companies Act, 2008 (Act No. 71 of 2008);

“**credit rating**” means an opinion regarding the creditworthiness of –

- (a) an entity;
- (b) securities or a financial instrument;
- (c) an issuer of securities or a financial instrument;

issued using an established and defined ranking system of rating categories excluding any recommendation to purchase, sell, or hold any security or financial instrument;

“**credit rating agency**” means a person incorporated under the Companies Act, and who is registered to provide credit rating services in terms of this Act;

“**credit rating services**” means data and information analysis, evaluation, approval, issuance and review of credit ratings;

“**FSB official web site**” means the web site of the Board;

“**Financial Services Board Act**” means the Financial Services Board Act, 1990 (Act No. 97 of 1990);

“**Minister**” means the Minister of Finance;

“**outsource**” means the contracting out of a function to an external provider in a manner that may impair materially the quality of the credit rating agency's internal control and the ability of the registrar to supervise the credit rating agency's compliance with obligations under this Act;

**“person”** means any natural person, partnership or trust, and includes -

- (a) any organ of state as defined in section 239 of the Constitution of the Republic of South Africa, 1996;
- (b) any company incorporated or registered as such under any law;
- (c) any body of persons corporate or unincorporate;

**“prescribed”** means prescribed by the registrar by notice in the *Gazette*;

**“publish”** means any direct or indirect communication transmitted by any medium, or any representation or reference written, inscribed, recorded, encoded upon or embedded within any medium, by means of which a person seeks to bring any information to the attention of a person, or all or part of the public, and “published”, “publishes” or “made public” has the same meaning;

**“public regulation”** means any legislation, including subordinate legislation, or any registration, licence, directive or similar authorisation issued by a regulatory authority or pursuant to any statutory authority;

**“rating category”** means a rating symbol, such as a letter symbol or a numerical symbol which might be accompanied by appending identifying characters, used in a credit rating to provide a relative measure of risk to distinguish the different risk characteristics of the type of rated entity, issuer, or financial instrument or other asset;

**“registrar”** means the registrar or deputy registrar of credit rating agencies referred to in section 22;

**“regulated person”** means a person that has been granted authority to conduct business or activities by a regulatory authority;

**“regulatory authority”** means any organ of state as defined in section 239 of the Constitution of the Republic of South Africa, 1996 responsible for the supervision or enforcement of legislation or a similar body designated in the laws of a country other than the Republic to supervise or enforce legislation of that country;

**“regulatory purposes”** means the use of credit ratings for the specific purpose of complying with national legislation or the listings requirements made by an exchange under section 12 of the Securities Services Act, 2004 (Act No. 36 of 2004);

**“regulation”** means a regulation under section 35;

**“rule”** means a rule prescribed by the registrar under section 25;

**“structured finance instrument”** means a financial instrument or other assets resulting from a securitisation transaction or scheme;

**“this Act”** includes the regulations, any prescribed rule, and any notice or directive given, approval or exemption granted, determination made, requirement or condition determined or imposed, or any other decision of the registrar; and

**“web site”** has the meaning set out in section 1 of the Electronic Communications and Transactions Act, 2002 (Act No. 25 of 2002).

(2) For purposes of this Act, any reference to “company”, “holding company” or “subsidiary” means a reference to a company, holding company or subsidiary, as the case may be, as defined in the Companies Act, or a similar entity incorporated under the laws of a country other than the Republic.

(3) The definition of “this Act” is included for drafting simplicity purposes only and does not afford administrative actions referred to in the Act legislative status.

(4) Any decision or other action of an administrative nature taken by the registrar that affects the rights of another person, including a regulated person, must comply with the Promotion of Administrative Justice Act, 2000 (Act No. 3 of 2000), unless another fair administrative procedure has been provided for in this Act.

(5) (a) A credit rating agency that publishes any information or any credit rating in the performance of credit rating services or is required to publish, disclose, produce or provide a policy, code, document or information under this

Act, must publish, disclose, produce or provide that credit rating, information, policy, code or document -

- (i) in the prescribed form, if any; or
- (ii) in plain language, if no form has been prescribed.

(b) For the purposes of this Act, a credit rating, policy, code, document or information is in plain language if it is reasonable to conclude that a person of the class of persons for whom the credit rating, policy, code, document or information is intended, with average literacy skills and minimal experience in dealing with credit ratings, credit rating services and credit rating agencies, could be expected to understand the content, significance and import of the credit rating, information, policy, code, document or information without undue effort, having regard to -

- (i) the context, comprehensiveness and consistency of the credit rating, information, policy, code, document or information;
- (ii) the organisation, form and style of the credit rating, policy, code, document or information;
- (iii) the vocabulary, usage and sentence structure of the credit rating, policy, code, document or information; and
- (iv) the use of any illustrations, examples, headings or other aids to reading and understanding the credit rating, policy, code, document or information.

(6) If, in terms of this Act, a credit rating, policy, code, document, information, record or statement is required -

- (a) to be retained, it is sufficient if an electronic original or reproduction of that credit rating, policy, code, document, information, record or statement is retained as provided for in section 15 of the Electronic Communications and Transactions Act, 2002; or
- (b) to be published, disclosed, produced or provided, it is sufficient if—

- (i) an electronic original or reproduction of that credit rating, policy, code, document, information, record or statement is published, disclosed, produced or provided by electronic communication in a manner and form such that the credit rating, policy, code, document, information, record or statement can conveniently be printed by the recipient within a reasonable time and at a reasonable cost; or
- (ii) a notice of the availability of that credit rating, policy, code, document, information, record or statement, summarising its content and satisfying any prescribed, is delivered to each intended recipient of the policy, code, document, information, record or statement, together with instructions for receiving the complete document, record or statement.

### **Purpose of Act**

2. The purpose of this Act is to –
- (a) ensure responsible and accountable credit rating agencies;
  - (b) protect the integrity, transparency and reliability of the credit rating process and credit ratings;
  - (c) improve investor protection;
  - (d) improve the fairness, efficiency and transparency of financial markets;  
and
  - (e) reduce systemic risk.

### **Application of Act**

3. (1) This Act applies to -
- (a) credit rating services performed in the Republic;

- (b) credit ratings that are published in the Republic; and
- (c) any person that performs credit rating services or issues credit ratings that are published in the Republic.

(2) With effect from a date determined by the Minister by notice in the *Gazette*, a person may not perform credit rating services or issue a credit rating that is published in the Republic unless that person is registered as a credit rating agency under this Act.

(3) This Act does not create a general obligation for –

- (a) all securities or financial instruments to be credit rated;
- (b) financial institutions or investors to invest only in entities, securities or financial instruments that are credit rated.

### **Use of credit ratings**

4. A regulated person must for regulatory purposes use credit ratings that are issued by credit rating agencies that are registered in accordance with this Act.

## **CHAPTER II REGISTRATION AS CREDIT RATING AGENCY**

### **Application for registration**

5. (1) An application for registration as a credit rating agency, must be made in the prescribed form and manner, and be accompanied by -

- (a) the applicant's certificate of incorporation under the Companies Act;
- (b) details of its –
  - (i) registration, authorisation or approval in countries other than the Republic to undertake credit rating services;

- (ii) ownership structure, organisational structure and corporate governance;
  - (iii) subsidiaries, if any;
  - (iv) resources and expertise to perform credit rating services;
  - (v) programme of operations, including indications of where the main business activities are expected to be carried out, branches to be established, and the type of business that will be undertaken;
  - (vi) expected outsourcing arrangements, including details of the persons that will be assuming outsourcing functions;
  - (vii) policies and procedures to identify, manage and disclose any conflicts of interests;
  - (viii) compensation and performance evaluation arrangements; and
  - (ix) compliance with or adherence to the Code of Conduct Fundamentals for Credit Rating Agencies issued by the International Organisation of Securities Commissions;
- (c) a description of the procedures and methodologies to be used to issue and review credit ratings;
- (d) information to satisfy the registrar that the applicant, its directors and employees comply with the fit and proper requirements prescribed , in respect of –
- (i) personal character qualities of honesty and integrity;
  - (ii) competence;
  - (iii) operational ability; and
  - (iv) financial soundness;
- (e) any other information prescribed; and
- (f) the prescribed application fee.

(2) An applicant must promptly amend its application for registration if, during the application process, the applicant becomes aware that any information referred to in subsection (1) had changed.

(3) The registrar may exempt an applicant who is or whose holding company is registered, authorised or approved by a foreign regulatory authority as a credit rating agency from providing some or all of the information required under subsection (1), if the applicant –

- (a) requests an exemption;
- (b) provides proof of such registration, authorisation or approval; and
- (c) the registrar is satisfied that such registration, authorisation or approval was granted in accordance with public regulation that is equivalent to this Act.

(4) The registrar must make known the receipt of an application on the FSB official web site. The notice must state-

- (a) the name of the applicant; and
- (b) the period within which objections to the application may be lodged with the registrar.

(5) The registrar may -

- (a) require an applicant to furnish additional information and require that information or any information that accompanied the application to be verified; and
- (b) take into consideration any other information regarding the applicant, derived from whatever source, including another regulatory authority.

(6) (a) The registrar, after consideration of an application and after consultation with any local regulatory authority that relies on, refers to or uses credit ratings in its supervision and regulation activities, must -

- (i) if satisfied that an applicant complies with the requirements of this Act, grant the application; or

(ii) if not so satisfied, refuse the application.

(b) Where an application is refused, the registrar must notify the applicant of the refusal.

(7) The registrar may grant an application for registration subject to any condition he or she may determine.

(8) The registrar must, on granting an application, issue a certificate of registration to a credit rating agency and publish a notice of the registration on the FSB official web site.

(9) A credit rating agency must ensure that -

- (a) a reference to the fact that such a certificate of registration held is contained in all business documentation, advertisements and other promotional material; and
- (b) its certificate of registration is at all times available to any person requesting proof of its registration status under authority of a law or for the purpose of entering into a business relationship with the credit rating agency.

### **Suspension of registration or de-registration**

6. (1) The registrar, after consultation with any local regulatory authority that relies on, refers to or uses credit ratings in its supervision and regulation activities, may at any time suspend the registration of or deregister a credit rating agency if satisfied, on the basis of available facts and information, that the credit rating agency -

- (a) expressly renounces the registration or has provided no credit ratings for the preceding six months;
- (b) has obtained the registration by making false statements or by any other irregular means;
- (c) no longer meets the conditions under which it was registered;

- (d) has failed to comply with any condition imposed under this Act;
- (e) has failed to comply with any directive issued under this Act; or
- (f) has been liquidated.

(2) (a) Where the registrar suspends the registration of a credit rating agency under subsection (1), the registrar may do so subject to any condition that the registrar may determine.

(b) The registrar may revoke any suspension under subsection (1) if the registrar is satisfied that the credit rating agency has complied with all of the conditions to which the suspension was made subject.

(3) (a) The registrar must publish a notice of any suspension or de-registration, the reasons therefore and any terms attached thereto on the FSB official web site and any other appropriate media.

(b) The suspension or de-registration of a credit rating agency takes effect on the date specified in the notice referred to in paragraph (a).

(c) Where a credit rating agency has appealed against a decision of the registrar referred to in subsection (1), the registrar must not publish the notice referred to in paragraph (a) until the appeal has been finalised.

(4) (a) Credit ratings issued by a credit rating agency whose registration has been suspended or who has been deregistered may continue to be used for regulatory purposes for:

- (i) 14 days after the publication of the notice referred to in subsection (3), if credit ratings of the same entity, securities, financial instrument or issuer were issued by other credit rating agencies registered under this Act; or
- (ii) three months after the publication of the notice referred to in subsection (3), if no credit ratings of the same entity, securities, financial instrument or issuer were issued by other credit rating agencies registered under this Act.

(b) The registrar may extend the period referred to in paragraph (a)(ii) to mitigate any potential market disruption or ensure financial stability.

### **CHAPTER III DUTIES OF CREDIT RATING AGENCY**

#### **General duties**

7. (1) A credit rating agency must -

- (a) comply with this Act;
- (b) provide the registrar with any information required;
- (c) subject to section 8, immediately inform the registrar if any information submitted in respect of its application under section 5 changes;
- (d) be organised in a way that ensures that its business interest does not impair the independence and accuracy of its credit ratings or credit rating services;
- (e) have sound administrative and accounting procedures, internal control mechanisms, effective procedures for risk assessment, and effective control and safeguard arrangements for information processing systems;
- (f) establish appropriate and effective organisational and administrative arrangements to –
  - (i) prevent, identify, eliminate or and manage and disclose any conflicts of interest of the credit rating agency, its analysts and employees; and
  - (ii) protect confidential information made available to it by issuers, including prohibiting its analysts and employees from using such information to enter into transactions;

- (g) employ appropriate systems, resources and procedures to ensure continuity and regularity in the performance of its credit rating services;
- (h) regularly monitor and evaluate the adequacy and effectiveness of its systems, internal control mechanisms and arrangements and take appropriate measures to address any deficiencies;
- (i) ensure that it at all times has the necessary knowledge and experience to issue credit ratings and perform its credit rating services; and
- (j) establish a function within its organisation to communicate with investors, potential investors and the public about any questions, concerns or complaints that it may receive.

### **Appointment of directors**

8. (a) A credit rating agency must, within 14 days of the appointment of a director, inform the registrar of the appointment and furnish the registrar with such information on the appointment as the registrar may reasonably require.

(b) The provisions of paragraph (a) may not be construed as rendering the appointment of a director of a credit rating agency subject to the approval of the registrar.

(c) If the registrar reasonably believes that a director of a credit rating agency is not, or is no longer, a fit and proper person to hold that office, or if it is not in the public interest that the director holds or continues to hold such office, the registrar may object to the appointment, or continued appointment, of a director, stating the grounds for the objection, and provide such to the credit rating agency concerned.

(d) If the registrar objects to an appointment in terms of paragraph (c), the credit rating agency must terminate the appointment within 30 days of the registrar informing the credit rating agency of the finalisation of the processes and procedures provided for in the Promotion of Administrative Justice Act, 2000 (Act No.3 of 2000).

## **Methodologies, models and key rating assumptions**

- 9.** A credit rating agency must -
- (a) adopt, implement and enforce adequate measures to ensure that the credit ratings it issues are based on a thorough analysis of all the information that is available to it and that is relevant to its analysis according to its rating methodologies;
  - (b) use rating methodologies that are rigorous, systematic, continuous and subject to validation based on historical experience, including back-testing;
  - (c) regularly review its methodologies, models and key rating assumptions such as mathematical or correlation assumptions, any significant changes or modifications to them and the appropriateness of those methodologies, models and key rating assumptions where they are used or intended to be used for the assessment of new financial instruments; and
  - (d) establish internal arrangements to monitor the impact of changes in macroeconomic or financial market conditions on credit ratings.

## **Credit ratings**

- 10.** (1) A credit rating agency must –
- (a) publish any credit rating or any decision to discontinue a credit rating on a non-selective basis and in a timely manner;
  - (b) when publishing a credit rating –
    - (i) state clearly and prominently any attributes and limitations of the credit rating; and

(ii) provide an explanation of the key elements underlying the credit rating that an investor, potential investor or a member of the public, as the case may be, are able to understand how a rating was arrived; and

(c) monitor credit ratings and regularly review its credit ratings.

(2) A credit rating agency must when issuing a credit rating for a structured finance instrument ensure that the rating categories that are attributed to structured finance instruments are clearly differentiated using an additional symbol which distinguishes them from rating categories used for any other entities, securities, financial instruments or issuers.

(3) A credit rating agency must disclose its policies and procedures regarding unsolicited credit ratings.

(4) A credit rating agency must refrain from issuing a credit rating or withdraw an existing rating if the lack of reliable data, the complexity of a financial instrument or the quality of information available cannot result in a credible credit rating.

### **Code of conduct**

**11.** (1) A credit rating agency must adopt, publish and adhere to a code of conduct that –

- (a) contains practical measures for implementing and giving effect to its duties and other requirements provided for under this Act;
- (b) describes how the measures referred to in paragraph (a) fully implement and give effect to its duties and other requirements provided for under this Act; and
- (c) describes how the code of conduct will be enforced.

(2) A credit rating agency must publish any changes to its code of conduct.

### **Outsourcing and other services**

**12.** (1) A credit rating agency may not, without the prior written approval of the registrar, outsource any of its operational functions.

(2) (a) A credit rating agency, subject to paragraph (b), may not, without the prior written approval of the registrar, provide services other than credit rating services to a third party.

(b) A credit rating agency may provide services ancillary to its credit rating services, which services comprise of market forecasts, estimates of economic trends, pricing analysis, other general data analysis and related distribution services and any other services as prescribed.

### **Disclosures**

**13.** (1) A credit rating agency must disclose to the public and its subscribers—

- (a) the practices, procedures, processes, methodologies, models and key rating assumptions it uses in its credit ratings and credit rating services and any material modification thereto;
- (b) its code of conduct;
- (c) the general nature of its compensation arrangements; and
- (d) its policy on publishing credit ratings and other related communication.

(2) A credit rating agency must, every six months, disclose to the public and its subscribers data about the historical default rates of its rating categories.

(3) A credit rating agency must provide prominent links to the disclosures referred to in subsections (1) and (2) on its web site.

## Records

14. A credit rating agency must arrange for adequate records and, where appropriate, audit trails of its credit rating services to be kept for a minimum period of 5 years or in accordance with applicable law.

## Annual report

15. (1) A credit rating agency must annually publish a report to the public, which report must include at least -

- (a) detailed information on its legal structure and ownership;
- (b) a description of its internal control mechanism ensuring quality of the credit rating services;
- (c) a description of its record-keeping policy;
- (d) the outcome of the annual internal review undertaken by its independent compliance function;
- (e) financial information on its revenue sources, divided into fees from credit rating services, ancillary services and other services;
- (f) a list of 20 clients who alone or together with affiliates contribute more than 10% to the total annual revenue of the CRA; and
- (g) any other prescribed information.

(2) The annual report referred to in subsection (1) must be –

- (a) submitted to the registrar together with the credit rating agency's audited financial statements; and
- (b) published within three months after the end of each financial year and must remain available on the web site of the credit rating agency for at least five years.

### **Independent compliance function**

**16.** (1) A credit rating agency must establish and maintain a permanent, independent and effective compliance function.

(2) A credit rating agency must –

- (a) ensure that the compliance function has the necessary authority, resources, expertise and access to all relevant information; and
- (b) appoint a compliance officer that is responsible for the compliance function and for any compliance reporting and inform the registrar of such appointment and the details of that person.

(3) A compliance officer must -

- (a) monitor and report on compliance of the credit rating agency and its employees with the credit rating agency's obligations under this Act and any codes, policies, procedures or systems required to be established under this Act;
- (b) advise and assist the credit rating agency in complying with its obligations under this Act;
- (c) report directly to the board of the credit rating agency;
- (d) review compliance with policies and procedures to manage conflicts of interest and assess the risk of non-compliance for the integrity of the credit rating process;
- (e) review compliance with internal controls with respect to the procedures and methodologies for determining credit ratings, including quantitative and qualitative models used in the rating process, and assess the risk of non-compliance for the integrity and quality of the credit rating process; and
- (f) in consultation with the board of the credit rating agency, resolve any conflicts of interest that may arise.

(4) A compliance officer may not -

- (a) perform credit ratings;
- (b) participate in the development of rating methodologies or models;
- (c) perform marketing or sales functions; or
- (d) participate in establishing compensation levels, other than for employees working for the compliance officer.

(5) The compensation of a compliance officer may not be linked to the business performance of the credit rating agency and shall be structured in a manner that ensures independence of judgment.

(6) (a) A compliance officer must annually prepare a report on the compliance of the credit rating agency with this Act and any codes, policies, procedures or systems required to be established under this Act.

(b) The compliance report must be submitted to the registrar, together with the credit rating agency's audited financial statements.

(7) A compliance officer must submit such reports, other than the report referred to in subsection (6), to the registrar in the manner and regarding the matters, as may be prescribed.

(8) Despite anything to the contrary contained in any law, a compliance officer must report to and inform the registrar in writing of any irregularity or suspected irregularity in the conduct or the affairs of the credit rating agency that, in the opinion of the compliance officer, is material.

(9) If the appointment of a compliance officer is terminated, the compliance officer must –

- (a) submit to the registrar a statement of what the compliance officer believes to be the reasons for that termination; and
- (b) if the compliance officer would, but for that termination, have had reason to submit to the registrar a report contemplated in subsection (8), the compliance officer must submit such a report to the registrar.

(10) The registrar may direct a credit rating agency to terminate the appointment of a compliance officer, if the compliance officer fails to comply with any provision of this section in a material manner.

### **Accounting and auditing requirements**

17. (1) Except to the extent exempted by the registrar, a credit rating agency must annually prepare, in respect of the relevant financial year of the credit rating agency, financial statements reflecting -

- (a) the financial position of the entity at its financial year-end;
- (b) the results of operations, the receipt and payment of cash and cash equivalent balances;
- (c) all changes in equity for the period then ended, and any additional components required in terms of South African Generally Accepted Accounting Practices issued by the Accounting Practices Board or International Financial Reporting Standards issued by the International Accounting Standards Board or a successor body; and
- (d) a summary of significant accounting policies and explanatory notes on the matters referred to in paragraphs (i) to (iii).

(2) A credit rating agency must cause the statements referred to in subsection (1) to be audited and reported on in accordance with auditing pronouncements as defined in section 1 of the Auditing Professions Act, 2005 (Act No. 26 of 2005) by an external auditor.

(3) The credit rating agency's audited financial statements must be submitted to the registrar within six months after its financial year-end.

(4) The provisions of sections 16(8), (9) and (10) apply, with the necessary changes, to the external auditor of a credit rating agency.

## CHAPTER IV

### ENDORSEMENT OF EXTERNAL CREDIT RATINGS

#### Definitions and interpretation

18. (1) In this Chapter, unless the context indicates otherwise –

“**associate**” means, in relation to -

(a) a juristic person -

(i) which is a company, means its subsidiary and its holding company and any other subsidiary or holding company thereof as defined in section 1 of the Companies Act;

(ii) which is a close corporation registered under the Close Corporations Act, 1984 (Act No. 69 of 1984), means any member thereof as defined in section 1 of that Act;

(iii) which is not a company or close corporation means another juristic person which would have been its subsidiary or holding company—

(aa) had it been a company; or

(bb) in the case where that other juristic person is not a company either, had both it and that other juristic person been a company;

(iv) means any person in accordance with whose directions or instructions its board of directors or, in the case where such juristic person is not a company, the governing body of such juristic person, acts;

(b) any person -

(i) means any juristic person whose board of directors or, in the case where such juristic person is not a company, the governing body of

such juristic person, acts in accordance with its directions or instructions;

(ii) means a trust controlled or administered by it.

**“external credit rating”** means a credit rating issued by an external credit rating agency;

**“external credit rating agency”** means a person authorised or registered by a regulatory authority to perform credit rating services similar to that regulated under this Act and is subject to the laws of a country other than the Republic, which laws –

- (a) establish a regulatory framework equivalent to that established by this Act; and
- (b) are supervised by a regulatory authority; and

**“group”** means a group consisting of two or more juristic persons, irrespective of whether any of those persons is domiciled in the same country as any of the others, and one or more of which is a credit rating agency and -

- (a) each of those persons is an associate of any one of the others; or
- (b) which persons are so inter-connected that should one of them experience financial difficulties, another one or all of them would likely be adversely affected.

### **Requirements for the endorsement of external credit ratings**

**19.** (1) A credit rating agency may endorse a credit rating issued in a country other than the Republic, if -

- (a) the credit rating services resulting in the issuance of the credit rating to be endorsed are undertaken partly or entirely by the credit rating agency or by an external credit rating agency belonging to the same group as that credit rating agency;
- (b) the credit rating agency has verified and is able to demonstrate on an ongoing basis to the registrar that the external credit rating agency is

authorised or registered by a regulatory authority to perform credit rating services similar to that regulated under this Act and is subject to the laws of a country other than the Republic, which laws –

- (i) establish a regulatory framework equivalent to that established by this Act; and
  - (ii) are supervised by a regulatory authority;
- (c) the ability of the registrar to assess and monitor the compliance of the external credit rating agency with the regulatory framework referred to in paragraph (b) is not limited;
- (d) the credit rating agency provides the registrar, on the registrar's request, with all information necessary to enable the registrar to supervise, on an ongoing basis, compliance with this Act;
- (e) there is an objective reason for the credit rating to be issued in a country other than the Republic; and
- (f) an agreement referred to in section 31 has been entered into between the registrar and the relevant regulatory authority of the external credit rating agency, which agreement, at least, provides for –
- (i) mechanisms for the exchange of information; and
  - (ii) procedures for the coordination of regulatory activities to facilitate the monitoring of credit rating activities resulting in the issuance of the endorsed credit rating on an ongoing basis.

(2) A credit rating endorsed under this section is deemed –

- (a) a credit rating issued by a credit rating agency registered under this Act; and
- (b) to have been issued when the credit rating is published on the credit rating agency's web site or by other means, or distributed by subscription and presented and disclosed in accordance with the requirements of this Act.

(3) A credit rating agency that endorsed a credit rating under this section remains fully responsible for that credit rating and for compliance with this section and the Act.

(4) (a) A credit rating agency must inform the registrar of any credit rating it intends to endorse under this section prior to endorsing that credit rating.

(b) The registrar, if the registrar is of the opinion that a credit rating will not be endorsed in accordance with this section or the requirements of this Act, may instruct the credit rating agency not to endorse the credit rating.

(5) A credit rating agency may not use endorsement with the intention of avoiding the requirements of this Act.

## **CHAPTER V**

### **LIABILITY AND INDEPENDENCE OF CREDIT RATING AGENCY**

#### **Limitation of liability**

**20.** (1) A credit rating agency does not incur any liability to an investor or a member of the public in respect of a credit rating issued or credit rating services performed in the ordinary course of business, unless it is proved that the credit rating was expressed or the credit rating services were performed maliciously, fraudulently or pursuant to the negligent non-compliance with the obligations of the credit rating agency under this Act.

(2) Despite subsection (1), a credit rating agency incurs liability to an investor or a member of the public who has relied on a credit rating, for financial loss suffered as a result of having relied thereon, only if it is proved that –

(a) the credit rating was issued pursuant to a negligent non-compliance with the obligations of the credit rating agency under this Act; and

(b) the credit rating agency knew, or could in the particular circumstances reasonably have been expected to know, at the time when the negligence occurred, that the credit rating would be used to induce that investor or member of the public to act or refrain from acting in some way or entering into a transaction.

(3) Nothing in subsections (1) or (2) affects any additional or other liability of a credit rating agency arising from a contractual relationship.

(4) A credit rating agency may not through a contract, agreement or in any other way limit or reduce the liability that such credit rating agency may incur in terms of this section.

### **Independence**

**21.** No person, including the registrar, may hinder, interfere, obstruct or improperly attempt to influence a credit rating, the content of a credit rating or any methodology, model and key assumption used by a credit rating agency to derive a credit rating.

## **CHAPTER VI ADMINISTRATION OF ACT**

### **Registrar and deputy registrar of credit ratings and credit rating agencies**

**22.** The executive officer and deputy executive officer referred to in section 1 of the Financial Services Board Act are the registrar and deputy registrar of credit rating agencies, respectively and have the powers and functions provided for by or under this Act or any other law.

### **Delegation and assignment**

**23.** (1) The registrar may, in writing, delegate any of the powers entrusted to the registrar under this Act and assign any of the duties or functions imposed on the registrar under this Act to a deputy registrar or any other person.

(2) A delegation or assignment in terms of subsection (1)—

- (a) is subject to any limitations or conditions that the registrar may impose;
- (b) may authorise sub-delegation; and
- (c) does not divest the registrar of the responsibility concerning the exercise of the delegated power or the performance of the assigned duty.

(3) The registrar may confirm, vary or revoke any decision taken by a deputy registrar or any other person, subject to any rights that may have vested as a consequence of the delegation or assignment.

### **General powers and functions of registrar**

**24.** (1) The registrar, in addition to other powers or functions conferred on the registrar by or in terms of any other provision of this Act, -

- (a) must supervise and enforce compliance with this Act;
- (b) must take steps that the registrar considers necessary to protect investors in their dealings with credit ratings, credit rating services and credit rating agencies;
- (c) may by notice require any person, including a credit rating agency, to furnish the registrar, within a specified period, with specified information or documents;
- (d) may impose conditions that are consistent with this Act in respect of any registration or approval granted or requirement imposed by the registrar and may amend or withdraw such conditions;

- (e) may, on the written request of a credit rating agency, extend any period within which any documentation, information or report must be submitted to him or her;
- (f) must determine the form, manner and period, if a period is not specified in this Act, within which any documentation, information or report that a credit rating agency is required to publish, disclose, provide or submit under this Act must be published, disclosed, provided or submitted;
- (g) may, despite the provisions of any law, furnish information acquired by him or her under this Act to any person charged with the performance of a function under any law, including a regulatory authority;
- (h) may issue guidelines on the application and interpretation of this Act; and
- (i) may take any measures that the registrar considers necessary for the proper performance and exercise of his or her functions or duties or for implementation of this Act.

(2) The registrar must, in performing the powers and functions provided for by or under this Act or any other law -

- (a) act in a manner which—
  - (i) is compatible with the purpose of this Act; and
  - (ii) is most appropriate for meeting the purpose of this Act; and
- (b) have regard to—
  - (i) international supervisory standards;
  - (ii) the principle that a restriction which is placed on a credit rating agency, the issuing of credit ratings or the performance of credit rating services, should be proportionate to the purpose for which it is intended;
  - (iii) the international nature of credit rating agencies, credit ratings and credit rating services;

- (iv) the principle that competition between regulated persons should not be impeded or distorted; and
- (v) the need to use resources in the most effective and cost-efficient way.

### **Power to make rules**

- 25.** (1) The registrar may prescribe rules with regard to -
- (a) any matter that is required or permitted to be prescribed in terms of this Act;
  - (b) organisational requirements for credit rating agencies;
  - (c) the independence of credit rating agencies and the avoidance of conflicts of interest by credit rating agencies;
  - (d) the quality and integrity of credit ratings;
  - (e) the presentation of credit ratings;
  - (f) additional obligations in relation to credit ratings of structured finance instruments;
  - (g) the design of methodologies and models;
  - (h) rating assumptions;
  - (i) additional disclosures;
  - (j) adequate and appropriate record-keeping;
  - (k) fraudulent and misleading advertising, canvassing and marketing;
  - (l) suitable guarantees, professional indemnity or fidelity insurance cover, and mechanisms for adjustments of such guarantees or cover by the registrar;
  - (m) the control or prohibition of incentives given or accepted by a credit rating agency;

(n) the responsibilities of credit rating agencies to investors and the public;  
and

(o) any other matter for the better implementation of this Act or a function or power provided for in this Act.

(2) Rules referred to in subsection (1) may -

(a) apply to credit rating agencies, credit ratings or credit rating services generally; or

(b) be limited in application to a particular kind or type of credit rating agency, credit rating or credit rating services.

(3) (a) Before the registrar prescribes any rule under this section, he or she must publish a draft of the proposed rule in the *Gazette*, together with a notice calling for public comment in writing within a period stated in the notice, which period may not be less than 30 days from the date of publication of the notice.

(b) If the registrar alters a draft rule because of any comment, he or she need not publish the alteration before prescribing the rule.

(4) The registrar may, if circumstances necessitate the immediate publication of a rule, publish that rule without complying with subsection (3)(a).

### **On-site visits and inspections**

**26.** (1) The registrar may –

(a) authorise any suitable person to conduct an on-site visit of the business and affairs of a credit rating agency or associate as contemplated in section 18 of this Act to determine compliance with this Act; or

(b) instruct an inspector under section 3 of the Inspection of Financial Institutions Act, 1998 (Act No. 80 of 1998).

(2) A person conducting an on-site visit in terms of paragraph (a) may -

(a) at any time during business hours -

- (i) enter the premises of the credit rating agency or associate and the credit rating agency or associate must, upon request, provide any document;
  - (ii) search the premises of the credit rating agency or associate for any document;
  - (iii) examine, make extracts from and copy any document or, against the issue of a receipt, temporarily remove the document;
  - (iv) seize any document against the issue of a receipt, which may furnish proof of any failure to comply with the provisions of this Act;
- (b) require the credit rating agency or associate to produce at a specified time and place any specified documents or documents of a specified description in the possession or under the control of the credit rating agency;
- (c) require any person that is holding or is accountable for any document, to provide information and an explanation of that information.

(3) After an on-site visit or inspection has been carried out in terms of subsection (1), the registrar may direct the credit rating agency or associate concerned to take any steps, or to refrain from performing or continuing to perform any act, to terminate or remedy any contravention of or failure to comply with any provision of this Act.

(4) The registrar, by notice on the FSB official web site, or by means of any other appropriate public media, may make known-

- (a) the status and outcome of an inspection;
- (b) the details of an inspection, if disclosure is in the public interest;
- (c) the outcome and details of an on-site visit, if disclosure is in the public interest.

## Directives

27. (1) The registrar may, in order to ensure the implementation and administration of this Act, or to protect investors and the public in general, issue a directive to a credit rating agency -

- (a) to implement specific practices, procedures or processes;
- (b) to take specific actions or measures;
- (c) to desist from undertaking specific practices, procedures, processes, actions or measures; or
- (d) prohibiting certain practices, procedures, processes, actions or measures.

(2) A directive referred to in subsection (1) may—

- (a) apply to credit rating agencies, credit ratings or credit rating services generally;
- (b) apply to a specific credit rating agency credit rating or credit rating service; or
- (c) be limited in its application to a particular kind or type of credit rating agency, whether external or internal, credit rating service published or performed in the Republic, or credit rating, whether relating to an opinion regarding –
  - (i) an entity;
  - (ii) securities or a financial instrument; or
  - (iii) an issuer of securities or a financial instrument..

(3) A directive issued in terms of subsection (1) takes effect on the date determined by the registrar in the directive, and may take effect immediately.

(4) The registrar may cancel or revoke any previously issued directives.

(5) The registrar must, where a directive is issued to ensure the protection of investors, potential investors or the public in general, publish the directive in the *Gazette* and any other media that the registrar deems appropriate.

### ***Exemptions***

**28.** (1) The registrar may exempt any credit rating agency from, or in respect of, any provision of the Act if the registrar is satisfied that –

- (a) practicalities impede the strict application of a specific provision of the Act; and
- (b) the granting of the exemption will not –
  - (i) conflict with the public interest;
  - (ii) prejudice the interests of -
    - (aa) the clients of credit rating agencies;
    - (bb) the users of credit ratings or credit rating services; or
    - (cc) regulatory authorities that rely on, refer to, or use credit ratings in their supervision and regulation activities; and
  - (iii) frustrate the achievement of the objects of this Act.

(2) Any exemption in terms of subsection (1)) may apply to credit rating agencies generally, a specific credit rating agency or be limited in its application to a particular kind or type of credit rating agency.

(3) The registrar may at any time by notice on the FSB official web site withdraw, wholly or in part and on any ground which he or she deems sufficient, any exemption granted under subsection (1).

## **Fees and penalties**

**29.** (1) (a) The registrar may by notice on the FSB official web site determine the fees payable to the registrar by any person, or category of persons seeking a decision, applying for registration or the performance of any other act by the registrar under this Act, and may in a similar manner amend, substitute or withdraw any such notice.

(b) The fees are payable in the manner, and are subject to the requirements, determined by the registrar by notice on the FSB official web site.

(2) (a) A person who is liable to pay the fees contemplated in subsection (1)(a) and who fails to pay the amount due on the date or within the period specified, must pay interest on the amount outstanding at the prescribed rate.

(b) The fees, and interest owed in respect thereof, are regarded as debts due to the registrar and may be recovered by the registrar by way of a judicial process in a competent court.

(3) The registrar may impose a fine in the case of any failure by a credit rating agency to submit to the registrar within any period specified by or under this Act any statement, report, return or other document or information required by or under this Act to be so submitted, not exceeding R1 000 or such other amount prescribed for every day during which the failure continues.

(4) The registrar must, before imposing a fine, by written notice to the credit rating agency—

(a) inform the credit rating agency of the registrar's intention to impose a fine;

(b) specify the particulars of the alleged failure;

(c) set out the reasons for the intended imposition of a fine;

(d) specify the amount of the fine intended to be imposed; and

(e) call upon the credit rating agency to show cause within a period specified by the registrar why the fine should not be imposed.

(5) If the registrar, after consideration of representations made by the credit rating agency, decides to impose a fine, the registrar must by written notice inform it that, not later than 30 days after the date of the notice, the credit rating agency may—

(a) pay the fine; or

(b) appeal in terms of section 34 against the imposition of the fine to the appeal board.

(6) If a credit rating agency fails to pay the fine or note an appeal in terms of subsection (5), the registrar may file with the clerk or registrar of any competent court a statement certified by the registrar as correct, stating the amount of the fine imposed on the credit rating agency, and such statement thereupon has all the effects of a civil judgment lawfully given in that court in favour of the board for a liquid debt in the amount specified in the statement.

### **Relationship with other regulatory authorities**

**30.** (1) The registrar may—

(a) liaise with any regulatory authority on matters of common interest;

(b) negotiate agreements with any regulatory authority to –

(i) co-ordinate and harmonise the reporting and other obligations of credit rating agencies, and external credit rating agencies and groups as defined in section 18;

(ii) provide mechanisms for the exchange of information; and

(iii) provide procedures for the coordination of regulatory activities to facilitate the monitoring of credit rating activities resulting in the issuance of the endorsed credit rating on an ongoing basis.

(c) participate in the proceedings of any regulatory authority; and

(d) advise or receive advice from any regulatory authority.

(2) The registrar, without detracting from the generality of subsection (1), may enter into a written agreement, including a memorandum of understanding, with a foreign regulatory authority in whose country a subsidiary or holding company of a credit regulating agency is incorporated, which cooperation agreement may include -

- (a) a provision that the registrar or foreign regulatory authority may conduct an on-site examination or an inspection of a credit rating agency, or external credit rating agency or any member of a group as defined in section 18;
- (b) a provision that the registrar and foreign regulatory authority may share information relating to the financial condition and performance of the institutions referred to under paragraph (a);
- (c) a provision that the registrar or foreign regulatory authority -
  - (i) be informed of adverse assessments of qualitative aspects of the operations of a credit rating agency, the institutions referred to under paragraph (a); or
  - (ii) may provide information regarding significant problems that are being experienced within a credit rating agency, the institutions referred to under paragraph (a);
- (d) such other matters as the Registrar may deem relevant.

## **CHAPTER VII**

### **ENFORCEMENT ACTIONS AND REMEDIES**

#### **Enforcement committee**

**31.** The registrar may, despite and in addition to taking any step he or she may take under this Act, refer any contravention of this Act to the enforcement committee established under section 10A of the Financial Services Board Act.

### **Civil action**

**32.** The registrar may, when satisfied on the basis of available facts and information that a person has contravened or not complied with any provision of this Act, or is likely so to contravene or not to comply, apply to a Court for an order restraining such person from continuing to commit any such act or omission or from committing it in future, and requiring the person to take such remedial steps as the Court deems necessary to rectify the consequences of the act or omission, including consequences which prejudiced or may prejudice any client.

### **Offences and penalties**

**33.** Any person who -

- (a) contravenes or fails to comply with a provision of section 3(2) or 4; or
- (b) deliberately makes a misleading, false or deceptive statement, or conceals any material fact;
- (c) in the execution of duties imposed by this Act gives an auditor or compliance officer information which is false, misleading or conceals any material fact;

is guilty of an offence and is on conviction liable to a fine not exceeding R1 000 000 or to imprisonment for a period not exceeding 10 years, or to both such fine and such imprisonment.

### **Right of appeal**

**34.** Any person who feels aggrieved by any decision by the registrar under this Act which affects that person, may appeal to the board of appeal established by section 26A of the Financial Services Board Act.

## CHAPTER VIII MISCELLANEOUS AND GENERAL PROVISIONS

### **Ministerial Policy**

**35.** (1) The Minister may, after consultation with the registrar, make policy to further –

- (a) enhance the objects of this Act; and
- (b) promote the national government's objective to encourage participation in and effective regulation of the financial services industry.

(2) Any policy made under subsection (1) must be published in the *Gazette*.

### **Saving of rights**

**36.** No provision of this Act, and no act performed under or in terms of any such provision, may be construed as affecting any right of a person to seek appropriate legal redress in terms of common law or any other statutory law, and whether relating to civil or criminal matters, in respect of a credit rating or credit rating agency.

### **Amendment of laws**

**37.** The laws referred to in the Schedule are hereby amended to the extent specified in the third column thereof.

### **Short title and Commencement**

**38.** This Act is called the Credit Rating Services Act, 2011.

**SCHEDULE**

## LAWS AMENDED OR REPEALED

<i>Item</i>	<i>No. and year of Act</i>	<i>Short title</i>	<i>Extent of repeal or amendment</i>
I	Act No. 97 of 1990	Financial Services Board Act, 1990	Amends in section 1 the definition of “financial Institution” by inserting in subparagraph (a) as (xiii) the definition of “credit rating agency”

## MEMORANDUM ON THE OBJECTS OF THE CREDIT RATING SERVICES BILL

### 1. BACKGROUND

- 1.1 Credit rating agencies issue opinions on the creditworthiness of a particular issuer or financial instrument, or the likelihood that an issuer will honour its financial obligations on a timely basis. These opinions are referred to as credit ratings. Credit ratings carry considerable weight in financial markets, both in terms of business practice and regulatory requirements.
- 1.2 Credit rating agencies have hitherto been unregulated in South Africa. The only exception is section 85A of the Banks Act, 1990 (Act No. 94 of 1990), which requires the Registrar of Banks to approve an external credit assessment institution or export credit agency before a bank or controlling company may make use of its credit assessment in the calculation of its prescribed minimum amount of required capital and reserve funds.
- 1.3 As stated, credit ratings are applied for *inter alia* regulatory purposes. Apart from such ratings used by banks in the calculation of their prescribed minimum amount of required capital and reserve funds, there are other instances where institutions are legally required to obtain credit ratings. Under the Municipal Finance Management Act, 2003 (Act No. 56 of 2003), a municipality may invest funds only in investments types with an investment grade rating from a nationally or internationally recognised credit rating agency. The JSE Limited's listing requirements refer to credit ratings, as well as the Collective Investment Schemes Control Act, 2002 (Act No. 45 of 2002), to name just a few examples. The investment mandates of most fund managers in South Africa require the use of credit ratings.
- 1.4 There are currently five credit rating agencies operating in South Africa. They are Moody's Investor Services Limited/ Moody's

Investor Services South Africa (Pty) Ltd, Fitch Rating Limited/Fitch Ratings Southern Africa (Pty) Ltd, Standard & Poor's, Global Credit Rating Co. and Ratings Africa.

- 1.5 Following the global financial crisis, credit rating agencies have been criticised for their role in the crisis. The report of the Financial Stability Forum published on 7 April 2008 blamed credit rating agencies for-
  - 1.5.1 failure to detect the worsening of the financial market conditions and to adapt their ratings timeously;
  - 1.5.2 failure to adapt to the new risks of the credit market, e.g. structured credit products (derivatives) and hedge funds;
  - 1.5.3 having given investment-grade (high) ratings to securitisation transactions, i.e. collateralised debt obligations and mortgage backed securities as a result of the close relationship with the issuers of such securities;
  - 1.5.4 lowering some of their ratings due to pressure introduced by competition; and
  - 1.5.5 contributing to the crisis because of the poor quality of some of the ratings of the structured financial instruments.
- 1.6 G20 response to the financial crisis included recommendations on credit rating agencies specifically. It was recommended that credit rating agencies whose ratings are used for regulatory purposes should be subject to a regulatory oversight regime that includes registration.
- 1.7 The International Organisation of Securities Commissions adopted the following principle on the regulation of credit rating agencies in June 2010: Credit rating agencies should be subject to adequate levels of oversight. The regulatory system should ensure that credit rating agencies whose ratings are used for regulatory purposes are subject to registration and ongoing supervision.

## **2. OBJECTS OF THE BILL**

The Bill aims to -

- 2.1 ensure responsible and accountable credit rating agencies;
- 2.2 protect the integrity, transparency and reliability of the credit rating process and credit ratings;
- 2.3 improve investor protection;
- 2.4 improve the fairness, efficiency and transparency of financial markets; and
- 2.5 reduce systemic risk.

## **3. SUMMARY OF THE BILL**

The Bill has eight chapters, which can be summarised as follows:

- 3.1 Chapter I contains the relevant definitions and sets out the purpose and application of the Bill.
- 3.2 Chapter II provides for the registration of credit rating agencies, and details the circumstances under which the registration of a credit rating agency may be suspended or deregistered.
- 3.3 Chapter III deals with the duties of credit rating agencies. It requires credit rating agencies to inform the registrar of the appointment of directors. It deals with the methodologies to be adopted by credit rating agencies when credit ratings are issued and contains general requirements pertaining to credit ratings. It further requires credit rating agencies to adopt a code of conduct, obtain the Registrar's approval before outsourcing, make prescribed disclosures, maintain records, annually publish a report, and to establish and maintain an independent compliance function. Finally, it contains accounting and auditing requirements for credit rating agencies.
- 3.4 Chapter IV contains requirements for the endorsement by credit rating agencies of external credit ratings. It also contains definitions applicable to this Chapter.

- 3.5 Chapter V contains provisions regarding the limitation of liability of credit rating agencies. It further requires credit rating agencies to be independent.
- 3.6 Chapter VI provides for the powers and functions of the registrar and deputy registrar of credit rating agencies. The powers include the power to make rules, authorise on-site visits and inspections, and issue directives. It also prescribes that the registrar may liaise with regulatory authorities.
- 3.7 Chapter VII deals with enforcement actions and remedies. It empowers the Registrar to take civil action in cases of non-compliance or non-adherence to the provisions of the Act. It prescribes offences and penalties.
- 3.8 Chapter VIII contains general and miscellaneous provisions, such as regulation making powers, saving of rights and amendment of laws.

#### **4. DEPARTMENTS OR BODIES CONSULTED**

The National Treasury and the Financial Services Board have consulted extensively during the development of this Bill.

#### **5. FINANCIAL IMPLICATIONS FOR STATE**

None.

#### **6. PARLIAMENTARY PROCEDURE**

- 6.1 The State Law Advisers and the National Treasury are of the opinion that the Bill must be dealt with in accordance with the procedure established by section 75 of the Constitution of the Republic of South Africa, 1996, since it contains no provision to which the procedure set out in section 74 or section 76 of the Constitution applies.

6.2 Furthermore, the State Law Advisers are of the opinion that it is not necessary to refer this Bill to the National House of Traditional Leaders in terms of section 18(1)(a) of the Traditional Leadership and Governance Framework Act, 2003 (Act No.41 of 2003), since it does not contain provisions pertaining to customary law or customs of traditional communities.