

CIRCULAR

SEBI/HO/MIRSD/MIRSD4/CIR/P/2016/119

November 1, 2016

To
All Credit Rating Agencies Registered with SEBI

Dear Sir/ Madam,

Sub: Enhanced Standards for Credit Rating Agencies (CRAs)

1. SEBI constituted a committee on “Strengthening the Guidelines and Raising Industry Standards for Credit Rating Agencies (CRAs)”, which included representatives from all the CRAs. The objective of the Committee was to deliberate upon measures and guidelines to bring about greater transparency in the policies of the CRAs, enhance the standards followed by the industry and, thereby, facilitate ease of understanding of the ratings by the investors.
2. With a view to implementing the recommendations of the said Committee, the guidelines as [annexed](#) to this Circular are being issued. These guidelines cover the following broad areas:
 - I. Formulation of Rating Criteria and rating processes and public disclosure of the same.
 - II. Accountability of Rating Analysts
 - III. Standardisation of Press Release for rating actions.
 - IV. Functioning and evaluation of Rating Committees/Sub-Committees.
 - V. Disclosure of ratings in case of non-acceptance by an issuer
 - VI. Disclosure in case of delay in periodic review of ratings.
 - VII. Policy in respect of non-co-operation by the issuer.
 - VIII. Strengthening and enhancing the relevance of Internal Audit of CRAs, viz. appointment and rotation of auditors and scope of the audit.
3. The CRAs shall effectively implement these guidelines within 60 days from the date of issue of this circular.

4. The CRAs shall at all times observe high standards and fairness in conduct of the business and any act of omission or commission in contravention of the provisions of clauses 12 and/or 23 of Code of Conduct , as specified under Third Schedule of the SEBI (Credit Rating Agencies) Regulations, 1999, in letter or spirit, may result in violation of the provisions of section 12A of the Securities and Exchange Board of India Act,1992 and SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003.

5. This circular is issued in exercise of the powers conferred by Section 11 (1) of Securities and Exchange Board of India Act, 1992 read with the provisions of Regulation 20 of SEBI (Credit Rating Agencies) Regulations, 1999 to protect the interest of investors in securities and to promote the development of, and to regulate, the securities market.

Yours faithfully,

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[Encl: Annexure](#)

Annexure A

1. Operations Manual/ Internal governing document:

- A. The Operations Manual/ Internal governing document, formulated by the CRA, shall, inter-alia, cover operating guidelines, criteria, policies and procedures related to the rating process.
- B. The contents of the Operations Manual/ Internal governing document, as well as any changes to the same, shall be communicated to employees promptly, and training of employees on the same shall be conducted at regular intervals.

2. Rating Criteria, Rating Process and their Disclosure:

A. Rating 'Criteria'

- I. Each CRA shall frame detailed rating criteria, include the same in its Operations Manual/ Internal governing document and disclose the same on its website. At the least, the following rating criteria shall be formulated by each CRA:

Criteria on:

- a) Default recognition and post-default curing period (Instrument-wise definition of default to be followed by all CRAs is provided in **Annexure-A1**.)
 - b) Financial ratios (Explaining how a CRA analyses various financial ratios including adjustments made to financial statements for the interpretation of financial ratios)
 - c) Consolidation of companies
 - d) Parent support/group/government support
 - e) Manufacturing, trading companies, and services sector
 - f) Banks and financial institutions
 - g) Securitization transactions
 - h) Public finance
 - i) Infrastructure ratings
- II. Each criteria shall be reviewed periodically by the CRA and the periodicity for such review shall be disclosed on the CRA's website. While disclosing the revised criteria on their website, CRAs shall also provide a reference/ hyperlink to the original criteria (before revision), so as to enable investors to discern the changes made to the same.
 - III. The criteria shall be placed on the CRA's website in a user-friendly manner in order to facilitate easy and ready access of the same by investors.
 - IV. Press Release, related to rating action, shall provide a reference/ hyperlink to the specific criteria applied for the rating.

B. Rating Process and Policies

- I. CRAs are mandated to have in place a proper rating process and disclose the same on their website.
- II. The following shall also be specified in the Operations Manual/ Internal governing document of CRAs:
 - a. Basic Minimum information required for conducting the Rating Exercise
 - b. External entities (bankers, auditors etc.) that need to be contacted
 - c. Mode of seeking information from external entities. CRAs should endeavor to obtain such information/confirmation in writing.
 - d. Policy regarding internal approvals and timelines at each step of the Rating Exercise
 - e. Policy regarding monitoring and review of ratings, including the timelines within which such review is to be completed
- III. Each CRA shall frame detailed guidelines on the following, include them in its Operations Manual/ Internal governing document and disclose the same on its website:
 - a. General nature of compensation arrangements with rated entities
Policy for appeal by Issuers against the Rating being assigned to its instruments
 - b. Policy for placing ratings on credit watch
 - c. Guidelines on what constitutes non-cooperation.
 - d. Gift policy
 - e. Confidentiality policy
 - f. Policy on outsourcing of activities
 - g. Policy on provisional ratings
 - h. FAQs on ratings
 - i. Disclosure on managing conflict of interest
- IV. Any change in the rating process or policies shall be disclosed on the CRA's website, while also providing a reference/ hyperlink to the original provision/ process/ policy, to enable the investors to discern the changes made to the same.

C. Accountability of Rating Analysts of CRAs:

- I. Roles and responsibilities of the rating analysts of CRAs shall be clearly laid out in the CRA's Operations Manual/ Internal governing document.
- II. Analysts shall be responsible for undertaking the rating process and adhering to the timelines as specified in the Operations Manual/ Internal governing document.

D. Standardization of Press Release for Rating Actions

- I. CRAs are mandated to issue a Press Release after assigning a rating. With a view to harmonizing the format of the Press Release, it has been decided that all CRAs shall follow a standardized template, which is attached as **Annexure-A2**. It may be noted that this template specifies the minimum

information that must be covered in the Press Release. CRAs can include additional information, while maintaining the basic format of the Press Release.

- II. While the Press release for the initial rating of bonds, debentures, etc. shall disclose information about the rated amount of the instrument, the subsequent Press Releases shall also disclose additional details of the rated instrument, viz. coupon, maturity date, etc.
- III. Each CRA shall assign a rating Outlook and disclose the same in the Press Release.
- IV. Press Release related to review of rating shall also carry the rating transition/ history of all instruments of that issuer, rated by the CRA in the past 3 years, irrespective of whether the instrument is currently outstanding or not.
- V. The rating history, Press Releases and Rating Reports, including those ratings which have been withdrawn, shall be available on the CRA's website.

3. Functioning and Evaluation of Rating Committees/Sub-Committees

- A. Each CRA shall define the obligations, responsibilities, areas of conflict of interest, etc. of rating committee members in its Operations Manual/ Internal governing document. The following shall be specifically set out in the Operations Manual/ Internal governing document of each CRA and disclosed on its website
 - I. Eligibility for becoming committee/sub-committee members
 - II. Composition of committee/sub-committee
 - III. Minimum quorum required
 - IV. Duties of committee members
 - V. System of voting and recording of dissent.
 - VI. Managing conflict of interest in the rating committee/sub-committee.
- B. Persons who have business responsibility shall not be part of the Rating Committee. However, the MD/ CEO may be a member of the Rating Committee if the majority of the Rating Committee members are independent. ("*Independent*" would mean people not having any pecuniary relationship with the CRA or any of its employees).
- C. Minutes of each case discussed at the committee shall be maintained and signed (digitally or manually) by the Chairperson. Standard format for the Minutes of Rating Committee Meeting is placed at **Annexure-A3**.
- D. The process of discussion of case by circulation must be avoided, unless there is urgency in taking a rating action.
- E. Chairperson(s) of each rating committee/sub-committee of the CRA shall, on an annual basis, undertake a review of the decisions taken by the Committees in that year, which would, inter alia, include:

- I. Ratings assigned by the rating committees/ sub-committees including ratings assigned based on best available information in cases of non-cooperation by the issuer.
- II. Sharp changes in ratings.

The review report thereof shall be placed before the Board of the CRA.

4. Disclosures:

A. In case of rating notaccepted by an issuer

- I. Each CRA shall disclose on its website details of all ratings assigned by them, irrespective of whether the rating is accepted by the issuer or not, even in case of non-public issues. Details disclosed shall include the name of the issuer, name/ type of instrument, size of the issue, rating and outlook assigned, etc.

B. In case of delay in periodic review

- II. Each CRA shall promptly disclose on its website details of all such ratings where the review became due but was not completed by the due date, as per the timelines specified in the CRA's Operations Manual/ Internal governing document. Details disclosed shall include the name of the issuer, name/ type of instrument, size of the issue, date of last review, reasons for delay in periodic review, hyperlink to the last Press Release, etc.

5. Policy in respect of non-co-operation by the issuer

- A.** In case of non-cooperation by the issuer (such as not providing information required for rating, non-payment of fees for conducting surveillance), inline with the existing Regulations, the CRA shall continue to review the instrument, on an ongoing basis throughout the instrument's lifetime, on the basis of best available information, in accordance with the rating process and policies set forth in its Operations Manual/ Internal governing document.
- B.** In such cases the credit rating symbol shall be accompanied by "Issuer did not co-operate; Based on best available information" in the same font size.
- C.** The rating action(s) in such cases shall be promptly disclosed through press release(s), which shall mention, atleast, the following:
 - I. Date of Press Release
 - II. Details of Instrument
 - III. Rating Action and Indicative/updated rating based on best available information
 - IV. A brief write-up on the non-co-operation by the Issuer/ Borrower and the consistent follow-up done by the CRA for getting the information.
 - V. Hyperlink/ reference to the applicable "Criteria"

- VI. Limitations regarding information availability (shall have a suitable caveat cautioning the investors/lenders /public)
- VII. Rating History for last three years
- VIII. Name and contact details of the Rating Analyst(s)

- D. In case an issuer, having not co-operated with a CRA in the past, approaches another CRA for rating, the new CRA shall, in its Press Release, disclose the aspect of non-co-operation.
- E. The Rating Agreement, signed between the CRA and its client (issuer/ borrower), shall have an additional clause stating that -

"The client (issuer/ borrower) agrees to disclose the history and status (non-cooperation, non-payment of fees etc.) of previous rating relation with the earlier CRA(s) to the new CRA along with reasons for non-cooperation,, etc. if applicable."

6. Internal Audit of CRAs:

For strengthening and improving the relevance of the internal audit of CRAs, as envisaged under Regulation 22 of the SEBI (Credit Rating Agencies) Regulations, 1999 and Circular SEBI/ MIRSD/CRA/Cir-01/ 2010 dated January 06, 2010, it has been decided to implement the below mentioned additional norms for the Internal Audit:

A. Eligibility of Auditors for conducting the Internal Audit of the CRA

- I. The audit firm shall have a minimum experience of three years in the financial sector.
- II. The internal auditor of a CRA shall declare that
 - a) The firm has not been employed by other CRAs for any other services (such as statutory audit, taxation, consultancy/ retainership etc.) in the past two years, and
 - b) The partners/ firm do not have any association with any other CRA.
- III. The audit team must be composed of, at least, a Chartered Accountant (ACA/FCA) and a Certified Information Systems Auditor (CISA).

B. Rotation of Internal Auditors

- I. An auditor shall be appointed for a maximum term of five years, with a cooling-off period of two years.

C. Scope of the Internal Audit

The scope of the internal audit shall be expanded to include the following additional checks:

- I. CRA and its employees, who are associated directly or indirectly with the rating business, have complied with the regulations and code of conduct.
- II. CRA has defined processes for operations that have been followed during the rating exercise.
- III. Rating analysts have adhered to their roles and responsibilities laid down in the Operations Manual/Internal governing document and processes disclosed on the CRA's website, during the rating
- IV. Policy in respect of non-cooperation by the issuer, including procedures to be followed for the same, have been complied with.
- V. CRA has framed a policy for default recognition, consistent with regulatory guidelines, and is adhering to the same. At a minimum, it shall be checked if any irregularities/ delays/ defaults in debt servicing had been indicated by any of the below mentioned entities and suitable action with regard to the same was taken by the CRA:
 - a) The issuer/ borrower
 - b) The Company's statutory auditor
 - c) The borrower's bankers, during interactions with the CRA
 - d) Debenture Trustees

Cases where there are deviations to the checklist shall be documented by the auditor as part of the audit report submitted to the board.

- VI. Review of ratings has been carried out as per the review policy of the CRA.
- VII. Dissents, if any, have been recorded for each committee meeting, as stated in the Operations Manual/ Internal governing document.
- VIII. CRA has complied with the timelines for publication of press release/ rating rationale for the ratings assigned, as set out in its Operations Manual/ Internal governing document.
- IX. The Press Releases issued are broadly in line with the standard template as placed at **Annexure-A2**.
- X. Verify the rating disclosures made by the CRAs on their website.
- XI. Comment on the conflict of interest, if any, arising due to composition of the rating committee and participation in the rating committee meetings.

D. Action on the Internal Audit Report:

- I. Upon receipt of the internal audit report, the Compliance Officer of the CRA shall provide detailed comments on each of the observations therein and place the same before the Board of the CRA.

- II. The final action taken report, including the comments/ recommendations made by Compliance Officer and the Board of the CRAAs well as the corrective steps taken by the CRA, shall be submitted to SEBI within 2 months from the date of receipt of the internal audit report or 1 month from the date of Board Meeting of the CRA, whichever is later, in the following format:

| Sr. No. | Observations of the auditor | Remarks by the Compliance Officer | Comments of the Board of the CRA | Corrective actions taken |
|---------|-----------------------------|-----------------------------------|----------------------------------|--------------------------|
| | | | | |
| | | | | |

7. Modification in format of Annexure IV under Clause 6.2.2 of SEBI Circular CIR/MIRSD/CRA/6/2010 dated May 3, 2010:

The format of Annexure IV under Clause 6.2.2 of SEBI Circular CIR/MIRSD/CRA/6/2010 dated May 3, 2010, providing the format for disclosure of “Movement of each credit rating that has moved by more than one notch over last six months” is modified. The revised format is placed at **Annexure-A4**. All other provisions of the aforesaid Circular remain unchanged.

Annexure-A1: Instrument-wise definition of default

| Facilities | Rating Scale | Proposed Definition of Default |
|--|-----------------------|---|
| <i>Fund-based facilities & Facilities with pre-defined repayment schedule</i> | | |
| Term Loan | Long Term | A delay of 1 day even of 1 rupee (of principal or interest) from the scheduled repayment date. |
| Working Capital Term Loan | | |
| Working Capital Demand Loan (WC DL) | | |
| Debentures/Bonds | | |
| Certificate of Deposits (CD)/ Fixed Deposits (FD) | Short Term/ Long term | |
| Commercial Paper | Short term | |
| Packing Credit (pre-shipment credit) | Short Term | Overdue/unpaid for more than 30 days. |
| Buyer's Credit | Short Term | Continuously overdrawn for more than 30 days. |
| Bill Purchase/Bill discounting/Foreign bill discounting /Negotiation (BP/BD/FBP/FBDN) | Short Term | Overdue/unpaid for more than 30 days. |
| <i>Fund-based facilities & No Pre Defined Repayment Schedule</i> | | |
| | | |
| Cash Credit | Long Term | Continuously overdrawn for more than 30 days. |
| Overdraft | Short Term | Continuously overdrawn for more than 30 days. |
| <i>Non fund-based facilities</i> | | |
| Letter of credit (LC) | Short Term | Overdue for more than 30 days from the day of devolvement. |
| Bank Guarantee (BG)(Performance/ Financial) | Short Term | Amount remaining unpaid from 30 days from invocation of the facility. |
| <i>Other Scenarios</i> | | |
| When rated instrument is rescheduled: | | Non-servicing of the debt (principal as well as interest) as per the existing repayment terms in anticipation of a favourable response from the banks of accepting their restructuring application/ proposal shall be considered as a default. Rescheduling of the debt instrument by the lenders prior to the due date of payment will not be treated as default, unless the same is done to avoid default or bankruptcy. |
| Curing Period | | 90 Days – for Default to Speculative Grade and generally 365 Days for Default to Investment Grade |

**For bank loan ratings, default recognition will need to be in line with the RBI guidance*

Annexure-A2: Standard Template for Press Release (Minimum Information be disclosed)

Name of the Company

Date of Press Release

Details of Instrument

| Name of the instrument | Date of issuance | Coupon rate | Maturity Date | Size of the issue | Rating assigned, along with Rating Outlook |
|------------------------|------------------|-------------|---------------|-------------------|--|
| | | | | | |

Rating action (assigned/upgraded/downgraded) for the instrument.

Detailed Rationale justifying the Rating Action/ rating assigned.

List of key rating drivers for the Rating Action i.e. factors justifying favourable assessment (strengths) and factors constituting risk (weakness).

Detailed description of key rating drivers highlighted above.

Analytical approach (wherever applicable) taken by the CRA to assign the rating.

Hyperlink/ reference to the applicable "Criteria" for rating the instrument.

About the Company: Factual details of the company along with the major financial information for the last and current financial year.

Status of non-cooperation with previous CRA (if applicable): Reason and comments on status of non-co-operation with the previous CRA (if applicable).

Any other information:

Rating History for last three years:

| S.No | Name of Instrument (NCD/ Bank Loan/ Non-Fund based facilities/ Commercial Paper etc.) | Current Rating (Year T) | | | Chronology of Rating History for the past 3 years (Rating Assigned and Press Release Date) along with Outlook/ Watch, if applicable | | |
|------|---|------------------------------|---------------------------------|--------|---|--|--|
| | | Type (long term/ Short term) | Amount Outstanding (Rs. Crores) | Rating | Date(s) & Rating(s) assigned in Year T-1 | Date(s) & Rating(s) assigned in Year T-2 | Date(s) & Rating(s) assigned in Year T-3 |
| 1 | | | | | | | |
| 2 | | | | | | | |

Note on complexity levels of the rated instrument:

Name and Contact Details of the Rating Analyst(s):

About CRA:

CRA Disclaimer:

Annexure-A3: Summary Record of the Rating Committee Meeting (RCM)

A. Preliminary Information

- Date of the RCM
- Names of all the persons attending the RCM
- Name of rating committee members present (only rating committee members will have voting rights)
- Name of the Chairperson of the meeting
- Any other special invitees (if any)

B. Information Relating to Rating Decision

Following information/details of each rating decision shall be captured:

- Name of the rated issuer/entity
- Rating exercise i.e. whether it's a fresh rating or review/surveillance case
- Rating outcome i.e. rating assigned, along with rating outlook and special rating symbol, if any.
- Summary of key issues discussed during the rating committee.
- Dissent (if any) by any RCM member

C. Authentication and Maintenance of Rating Committee Summary

- The summary of the RCM shall be approved/signed by the Chairperson either manually or digitally.
- The approved/ signed summary shall be maintained either manually or electronically.

Annexure-A4: Movement of each credit rating that has moved by more than one notch

| Rating Movement by more than one-notch between Apr-Sep / Oct -Mar | | | | |
|--|---------------------------|-----------------------------|-------------------------|------------------------------|
| S.No | Name of the Issuer | Rating post revision | Notch Difference | Date of Rating Change |
| Rating prior to revision- AAA category | | | | |
| 1. | | | | |
| 2. | | | | |
| Rating prior to revision- AA category | | | | |
| 1. | | | | |
| 2. | | | | |
| Rating prior to revision- A category | | | | |
| 1. | | | | |
| 2. | | | | |
| Rating prior to revision- BBB category | | | | |
| 1. | | | | |
| 2. | | | | |
| Rating prior to revision- BB category | | | | |
| 1. | | | | |
| 2. | | | | |
| Rating prior to revision- B category | | | | |
| 1. | | | | |
| 2. | | | | |
| Rating prior to revision- C category | | | | |
| 1. | | | | |
| 2. | | | | |