



Securities and Exchange Commission of Pakistan

Securities Market Division

Market Supervision and Registration Department

Islamabad, the 13th January, 2014

SUBJECT: Directive under the Credit Rating Companies Rules, 1995

For establishing a procedural framework for credit rating companies and in the interest of public and the capital market, the Commission, in exercise of the powers conferred by rule 7 of the Credit Rating Companies Rules, 1995 is pleased to direct that the Credit Rating Companies shall follow and comply with the following **Code of Conduct for Credit Rating Companies/Agencies** with immediate effect.

1. PREAMBLE:

- 1.1 Credit Rating Companies/Agencies (CRAs) play important role in the development of capital market. CRAs typically opine on the creditworthiness and ability of the borrowing entities and the issuers of debt securities to honor their financial obligations. CRAs provide credit ratings for different types of debts and financial obligations, for example, private loans, publicly and privately traded debt securities, preferred shares and other securities that offer a fixed or floating rate of return.
- 1.2 Investors and other stakeholders give immense importance to the assessment conducted and opinions expressed by CRAs. The growing importance placed on CRAs assessments and opinions, requires CRAs to conduct their credit rating activities in accordance with the principles of integrity, transparency, quality and good governance. This will help assuring that investors and issuers are treated fairly and the confidential material information provided to them by the issuers is safeguarded and not misused.
- 1.3 The regulatory landscape on CRAs has recently experienced a shift on the global scale. Pursuant to the International Organization of Securities Commissions' (IOSCO) Code of Conduct Fundamentals for CRAs of May 2008, a number of jurisdictions have undertaken various regulatory measures to strengthen oversight on CRAs and to raise the standards for CRAs. Considering this development, it is important for the Securities and Exchange Commission of Pakistan (the Commission) to ensure that our CRAs continuously adhere to the international standards and best practices.
- 1.4 In order to enhance credibility to the processes and procedures associated with the credit rating, it has been decided, in consultation with the CRAs, to review the existing regulatory frame work for CRAs and prescribe a revised Code of Conduct. Currently, CRAs are regulated under Section 32B of the Securities and Exchange Ordinance, 1969 (the Ordinance); the Credit Rating Companies Rules, 1995 (the Rules); Circular No.06 of 2002 dated April 01, 2002 – Dissemination of Ratings by CRAs; Circular No. 20 of 2004 dated April 14, 2004 – Rating Contract/Agreement Between the CRAs and Their Clients; the Code of Conduct for CRAs dated February 17, 2005 and Circular No.2/2007 dated 26 February 2007 – Dissemination of Credit

Rating. Purpose of the review is to strive to improve quality and credibility of the processes and procedures associated with credit ratings, investors' protection and the fairness, efficiency and transparency in the securities markets and reduce systemic risk.

- 1.5 The Code of Conduct for the Credit Rating Companies/Agencies (hereinafter referred to as the Code) is issued, in supersession of the Code of Conduct for CRAs dated February 17, 2005, Circular No.06 of 2002 dated April 01, 2002 – (Dissemination of Ratings by CRAs); Circular No. 20 of 2004, 14 April 2004 – (Rating Contract/Agreement Between the CRAs and Their Clients) and Circular No.2/2007 dated 26 February 2007 – (Dissemination of Credit Rating), by the Commission in exercise of the powers conferred by rule 7 of the Credit Rating Companies Rules, 1995 and the Commission hereby directs that all the Credit Rating Agencies shall comply with this Code from the date of its issue.

2. QUALITY AND INTEGRITY OF THE RATING PROCESS:

2.1 Quality of the rating process:

CRA shall:

- (a) develop well-defined rating criteria, methodologies and procedures for solicited and unsolicited credit ratings, each class of entity, instrument and issue and such rating criteria, methodologies and procedures will act as guiding principles for analysts to enable them to analyze and interpret the information appropriately. The criteria, methodologies and procedures shall be updated proactively, taking into account changes in the market environment;
- (b) ensure that analysts follow the defined rating criteria, methodologies and procedures carefully, uniformly and in a consistent manner as consistent application of rating criteria, methodologies and procedures is essential for comparing;
- (c) establish a rating committee who shall assign and decide on each credit rating and all rating decision, including decisions regarding changes in rating shall be taken to the rating committee. Members of the rating committee must have adequate qualification, knowledge and experience of the financial markets and the credit ratings and at least one-third or two members of the rating committee, whichever is higher, including the Chairman of the committee shall be external members which will ensure objectivity and effectiveness of the rating committee;
- (d) keep the following records in support of each credit rating and review thereof:
 - (i) summary of discussions with the issuer, its management, auditors and creditors which have a bearing on the credit rating;
 - (ii) decisions of the rating committee, including voting details and notes of dissent, if any, by any member of the rating committee; and
 - (iii) where a quantitative model is a substantial component of the credit rating process, the rationale for any material difference between the credit rating implied by the model and the credit rating actually assigned.
- (e) ensure that for all ratings whether active, withdrawn or matured, records shall be maintained for a period of not less than five years and in case of instrument rating/grading, the time period of five years shall be reckoned from the date of maturity of such instrument.;

- (f) establish a set of transparent policies, controls and procedures in order to ensure consistency of its rating operations as well as to maintain a fair and robust relationship with its external stakeholders and as a minimum standard, a CRA shall develop the policies as specified in **Annexure-I** of this Code;
- (g) assess whether the existing rating criteria, methodologies and procedures for credit ratings of structured products are appropriate when the risk characteristics of the assets backing a structured product change materially and where the complexity or structure of any structured product or the lack of information about the assets backing the structured product raise the questions as to whether the CRA has the capability to determine a credible credit rating for the security, CRA should refrain from assigning a credit rating;
- (h) establish a Criteria Group, comprising atleast two senior analysts , which shall be responsible for formulating and reviewing such criteria, methodologies and procedures as specified in **Annexure-II** and such Criteria Group will ensure that all new rating criteria, methodologies and procedures and subsequent amendments therein have been made after careful and thorough analysis from both analytical and market perspective.

2.2 Monitoring and review of the rating:

CRA shall:

- (a) monitor all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc, is disseminated to the market, in a timely and effective manner, after appropriate consultation with the entity/issuer;
- (b) review all the outstanding ratings on annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so;
- (c) initiate immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating;
- (d) engage with the issuer and the Debt Securities Trustee, to remain updated on all information pertaining to the rating of the entity/instrument.

2.3 Integrity of the rating process:

2.3.1 Appointment of the Compliance Officer:

- (a) CRA shall:
 - (i) designate one of its officers as a compliance officer possessing relevant qualification and experience and certification as may be specified by the Commission and appointment of such compliance officer shall be reported to the Commission;
 - (ii) ensure that compliance officer shall be responsible for:
 - (A) monitoring compliance by the CRA with the Rules;
 - (B) monitoring compliance by the CRA with all the provisions of this Code particularly compliance relating to dissemination, reporting and filing, implementation of the policies relating to rating processes and employees;

- (C) reporting of any non-compliance with any provision of the Rules or the Code to the Board of Directors and to the Commission;
 - (D) redressal of creditors', investors' and other stakeholders grievances and complaints; and
 - (E) reporting to the Commission immediately if the CRA ceases to maintain any of the requirements referred to in rule 3 of the Rules.
- (b) In order to enable the compliance officer to discharge his duties properly and independently, the CRA shall ensure that:
- (i) the compliance officer has the necessary authority, resources and access to all the relevant information; and
 - (ii) the compliance officer has direct line of reporting, relating to his duties as compliance officer, to the CRA's Board of Directors in addition to his regular reporting on carrying out of his routine duties to the senior management.
- (c) In case the compliance officer is replaced, the same shall be intimated to the Commission within seven days of such replacement.

2.3.2 Whistle- Blower Policy:

CRA shall:

- (a) frame and implement whistle-blower policy encouraging all employees to intimate the compliance officer any unethical practice or misconduct relating to the credit rating, by another employee of the CRA that came to his knowledge;
- (b) ensure that all reported events shall be investigated promptly by the compliance officer in accordance with the provisions provided in the whistle-blower policy;
- (c) ensure that investigation shall be completed within the time period specified in the whistle-blower policy;
- (d) ensure that whistle-blower policy must contain the clauses (i) requiring the compliance officer to keep name of the person secret who report the above-mentioned unethical practice or misconduct and (ii) preventing discrimination, retaliation or harassment against any whistle-blower, the compliance officer or any member of the investigation process.

2.3.3 Rating Shopping:

CRA shall:

- (a) maintain principle of integrity in seeking rating business;
- (b) not accept a rating assignment where a client has prematurely terminated a rating contract with its existing CRA, unless such client obtains No Objection Certificate (NOC) from its existing CRA or ensure in writing that it shall continue credit rating with its existing CRA till the period as agreed in the rating agreement. A clause to this effect shall be included by the CRA in each rating agreement; and

- (c) observe a silent period of minimum two-years between the notification of the unsolicited rating and acceptance of the assignment for the solicited rating, where an unsolicited rating becomes a solicited rating.

3. INDEPENDENCE AND AVOIDANCE OF THE CONFLICT OF INTEREST:

3.1 Independence and Conflict of Interest:

(a) CRA shall ensure that:

- (i) at least one third or two members, whichever is higher, of its Board of Directors are independent;

Explanation: For the purpose of this clause, the expression "independent director" means the same as provided in clause (i) (b) of the Code of Corporate Governance.

- (ii) members of its Board of Directors shall not involve in the rating process and shall provide an undertaking to this effect at the time of appointment as member of the Board of Directors;

- (iii) its rating committees are able to perform their duties free of undue intervention or influence from its shareholders, its management and its Board of Directors;

- (iv) the external members inducted on its rating committee are not less than as mentioned in para 2.1(c) above ;

[Explanation: For the purpose of this clause the term "external member" means any person who has no direct or indirect association with the CRA or any of its Directors and shareholders.

- (v) it has not appointed any individual as a member of a rating committee who has or is perceived to have a business development function of the CRA; or who initiates or participates in discussion regarding fee or payment with any client of the CRA;

- (vi) the criterion for constitution of the rating committees is capable to promote continuity and to discourage biasedness in the rating process. Considering the adequacy of its staffing strength, the CRA shall use its best endeavor to subject its rating analysts to an appropriate rotation mechanism that provides for gradual change in rating teams;

- (vii) it shall not provide consultancy/advisory services or other services to any of its clients or to any of its clients' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities;

- (viii) it has included a statement in each rating report that the CRA, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating done by them. In case there is any conflict of interest, CRA shall disclose

in the respective rating report, nature of such conflict of interest and its impact on the rating grade assigned;

- (ix) it has made the reporting lines and compensation arrangements for its employees in a way to eliminate or effectively manage actual and potential conflicts of interest. An analyst must not be compensated on the basis of revenue generated from the entities rated by him;
- (x) it shall conduct periodic reviews of compensation policies for analysts and other employees who participate in or who might otherwise have an effect on the rating process to ensure that these policies do not compromise the objectivity of the CRA's rating process;
- (xi) the credit rating assigned to an entity or instrument should not be affected by the existence of a business relationship between the CRA and the entity or any other party, or the non-existence of such a relationship;
- (xii) an analyst having any interest in a credit rating or any of his family members has any such interest, shall not be involved in such rating process;
- (xiii) it has established appropriate policies governing investments and trading in securities by its employees.;
- (xiv) the analysts and members of the rating committees including the external members have disclosed all the conflict of interest, including those of their family members, if any, to the officer designated by the CRA for the purpose; and
- (xv) the analysts or any of its family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes.

[Explanation: For the purpose of this clause, the term "family" means such person who falls within any one of the following categories:

- (A) spouse;
- (B) parent; and
- (C) children including an adopted child and step-child.

3.2 Default Studies:

CRA shall, upon the occurrence of default, conduct default studies in each case of default by any entity rated by it and disseminate the same on its website for public information. The default studies must describe the definition of default, the reasons of default and the factors overlooked, if any, by the CRA.

3.3 Contents of the Rating Agreement:

CRA shall not accept any rating assignment except through a rating agreement in writing and the rating agreement must contain all the necessary provisions including but not limited to the following:

- (a) a clause requiring the client to provide the CRA true, accurate, complete, and updated information to enable it to arrive at and maintain a fair and true rating of the client and/or the instrument, as the case may be;
- (b) a clause empowering the CRA to call and obtain, any time during the validity period of the agreement or during the tenure of the instrument, all such information as deem necessary by it for conducting effective and timely review of the rating assigned;
- (c) a clause regarding consent of the client authorizing the CRA to conduct review of the rating any time during the validity period of the agreement or during the tenure of the instrument;
- (d) a clause requiring the client to continue credit rating through the CRA till the validity of the agreement. In case the client switchover to any other CRA, it shall continue rating with the existing CRA as well unless it obtains NOC from the existing CRA;
- (e) rights and obligations of each party to the agreement;
- (f) nature of the rating/grading i.e. entity rating, instrument rating or both; equity issues grading;
- (g) tenure of the rating;
- (h) validity period of the agreement; and
- (i) fee to be charged by the CRA and payment schedule thereof.

3.4 Operational Requirements:

- (a) A CRA shall have adequate infrastructure and information systems to provide reliable rating services and maintain its credit rating operations and facilities with adequate security, system capacity and contingency arrangements; and
- (b) A CRA shall ensure that all its dealings and transactions, commercial or otherwise, with its shareholders, including the holding company, if any, are periodically reviewed by its Board of Directors to ensure that such dealings and transactions are undertaken in a fair and justifiable manner without having any adverse impact on the rating process and its quality.

3.5 Adoption of the International Standards:

- (a) Unless provided otherwise in this Code, CRAs are encouraged to adopt all the requirements of the Code of conduct for CRAs issued by IOSCO.
- (b) CRA shall acquire and maintain membership of the Association of Credit Rating Agencies in Asia (ACRAA); and

- (c) Unless provided otherwise in this Code, CRAs shall follow the best practices guidelines and principles issued by ACRAA from time to time.

3.6 Adoption of the Code of Corporate Governance:

CRAs are encouraged to adopt the Code of Corporate Governance issued by the Commission for listed companies.

3.7 Reporting and Filing:

CRA shall report to and file with the Commission the following information/documents:

- (a) Copy of the rating criteria, methodologies and policies and any subsequent modification therein as and when takes place;
- (b) A report containing clause-wise compliance status of this Code and the Rules on yearly basis within three months of the close of its financial year. The report must be certified by the Board of Directors;
- (c) Its audited annual accounts within the time period as mentioned in the Companies Ordinance, 1984;
- (d) Intimation regarding appointment of the compliance officer within seven working days of the date of such appointment;
- (e) Cessation of the employment of the compliance officer within seven working days of the date of such cessation; and
- (f) Certified true copy of the minutes of the meetings of its Board of Directors and that of the general meetings within seven days of the confirmation of the same.

4. RESPONSIBILITIES:

4.1 Transparency and Timeliness:

- (a) Where feasible and appropriate, prior to issuing or revising a rating, the CRA shall inform the issuer of the critical information and principal considerations upon which a rating will be based and provide the issuer an opportunity to clarify any likely factual misperception or other matter that the CRA would wish to be made aware of in order to produce a fair rating. A CRA will duly evaluate the response. Where in a particular circumstance the CRA has not informed the issuer prior to issuing or revising a rating, the CRA should inform the issuer as soon as practical thereafter;
- (b) Every CRA shall indicate with each of its ratings when the rating was last updated and each rating announcement should also indicate the principal methodology or methodology version that was used in determining the rating and where a description of that methodology can be found. Where the rating is based on more than one methodology, or where a review of only the principal methodology might cause investors to overlook other important aspects of the rating, the CRA should explain this fact in the rating announcement, and indicate where a discussion of how the different methodologies and other important aspects factored into the rating decision can be found; and
- (c) A CRA should conduct industry specific studies and disseminate findings of such studies on its website.

4.2 Private Rating:

- (a) A CRA may be approached either by the entity or any third party for assigning private rating and the CRA shall not publicly disclose the private ratings. The CRAs policy for private rating must clearly articulate non-publication and non-dissemination of the private ratings and confidentiality of the related information; and
- (b) Whenever a private rating is made public, it shall be dissemination in the manner as provided in para 4.3.

4.3 Disclosure:

4.3.1 Disclosure through Newspapers:

A CRA shall disseminate all ratings assigned by it, whether solicited or unsolicited, except the private ratings, by way of press release through a news agency and ensure that these are disseminated through at least one English and one Urdu language daily newspaper having nationwide circulation, within two working days of the notification of such ratings.

4.3.2 Disclosure through Website:

A CRA shall maintain an official website and disseminate on it, atleast the following:

4.3.2.1 Rating Procedure:

- (a) All criteria, methodologies and procedures regarding the credit rating including both solicited and unsolicited credit ratings and subsequent modification, if any, therein. This will help that rating criteria, methodologies and procedures are followed uniformly because any deviation can be subject to market scrutiny. Dissemination of rating criteria and methodologies will enhance the acceptance of ratings among users;
- (b) The rating definition and the symbol related thereto;
- (c) Latest credit rating report and rating press releases, except the reports and press releases relating to private rating, for atleast the last five years, where applicable. A CRA shall ensure that each credit rating report contains:
 - (i) names and contact detail of the rating analysts;
 - (ii) purpose of the rating;
 - (iii) latest assets and liabilities position and financial ratios of the entity/issuer;
 - (iv) in case of secured instrument, quantum and nature of security, nature and book value of the assets backing the instrument;
 - (v) in case of structured finance products, information about the originator like its name, its principle business, its brief financial and operating position for the last five years, nature of defaults and delay, if any, in repayment of any financial obligation during the last five years, nature and value of

assets backing the instrument, detail of guarantee, if any, or any other additional security arrangement, transaction structure, collection mechanism etc;

[Explanation: Structured Finance Products are the instruments resulting from the securitization transactions.]

- (vi) in case of unsolicited ratings, the fact that it is unsolicited, the extent of participation by the entity/issuer, its management, its creditors and its auditors in the credit rating process. The information used and its source in arriving at the credit rating;
 - (vii) assumptions and rationale for the rating assigned and the risk factors considered in the assessment;
 - (viii) the probability of default;
 - (ix) where relevant, the benchmarks used, any sensitivity analyses performed and its results, comparative analyses made with other industries or companies and credit enhancements;
 - (x) history of the credit rating for at least five years in case of entity rating and for the full tenure in case of instrument rating; and
 - (xi) a statement by the analysts that rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be;
- (d) All policies as mentioned in **Annexure-I**;
 - (e) All rating review reports of the outstanding issues within five days of the notification of the review; and
 - (f) All the information as mentioned in **Annexure-III**.

4.3.2.2 List of Fee/Charges:

A CRA shall prepare list of charges relating to rating services and disseminate the same on its website. The list of charges must contain all the rating services render and functions perform by it and the rate of fee for each such service and function. The fee may be provided in terms of percentage, in the form of range (i.e. minimum and maximum) or in the form of fixed amount for each service/function.

4.3.2.3 Shareholding:

- (a) A CRA shall disclose its latest pattern of shareholding, showing atleast names of the shareholders, number and percentage of shares held by each shareholder or group of shareholders, names of shareholders holding 10% or more share in the CRA; and

- (b) Changes in the pattern of shareholding of a CRA since its inception. The changes shall reflect names of the previous and subsequent shareholders along with number and percentage of shares held.

4.3.3 Disclosure in Financial Reports:

A CRA shall disclose in its audited annual financial reports, the following information:

- (a) its total revenue from rating services and non-rating services separately;
- (b) client-wise non-rating revenue of the CRA or its holding or subsidiary companies, if any, in case where non-rating revenue of the CRA or its holding or subsidiary companies, if any, from any single client or group is ten percent (10%) or more of its or its holding or subsidiary companies' total revenue; and
- (c) names of the clients who along with their associates contribute ten percent (10%) or more of the total revenue of the CRA or its holding or subsidiary companies.

4.4 Treatment of the Confidential Information:

- (a) Except as required under this Code, a CRA shall not, without obtaining prior written approval of its client, share with or disclose to press or any other party including its other clients, any confidential information about its client, which has come to its knowledge in the course of the rating process, except in case where sharing and disclosure of such confidential information is required under any law;
- (b) A CRA shall frame its own policy to prevent; abuse of the non-public information by its employees and other persons involved in the rating process, sharing and dissemination of the non-public information by such persons to outside parties; and
- (c) In cases where a CRA is a parent, subsidiary, joint venture partner or affiliate of any organization that might benefit from the non-public information available with CRA, the CRA shall ensure strong firewalls to prevent disclosure or use of the said non-public information by these related parties or their personnel.

4.5 Shareholding Structure:

An institution involved in the financial and capital market businesses may hold shares in a CRA provided that direct and indirect shareholding of such institution is not more than 26%. An individual should not directly and indirectly hold more than 10% shares in a CRA. Individuals' aggregate shareholding shall not exceed 40% at any time. The existing CRAs shall change their shareholding structure accordingly by December 31, 2014.

4.6 Human Resources and Expertise:

- (a) A CRA shall have analysts who are competent and qualified to carry out rating assignments and subsequent monitoring of the ratings. In assessing the competence of its analysts, a CRA shall consider, among other things, their level of education; experience within the sector, industry and geographic location; experience with particular transactions and asset classes; and other areas of expertise;
- (b) A CRA shall ensure that its analysts maintain sufficiently high level of analytical and monitoring standards. In this regard, the CRA shall consider the number of

entities/instrument/issues that can be effectively covered by a particular analyst, taking into account a broad spectrum of variables, including the size and complexity of the particular issue and the experience and expertise of the analyst;

- (c) A CRA shall ensure that all its officers involved in the rating and monitoring process are qualified and possess the requisite skill and expertise;
- (d) A CRA shall arrange trainings for the capacity building and skill development of its analysts and other employees involved in the rating process; and
- (e) A CRA's analysts should be held to high standards of integrity and a CRA shall not employ individuals who are known to it as dishonest or the persons with compromised integrity.

4.7 Appointment of Directors:

CRA shall make sure that the persons nominated for the position of chairman, chief executive and director meet the fit and proper criteria provided at **Annexure-IV** to this Code. The chief executive of a CRA should be independent and must not have any direct or indirect shareholding in the CRA;

4.8 Other Obligations of CRAs:

A CRA shall abide by the following:

- (a) It shall not rate its own instruments.
- (b) It shall not rate its associated companies and undertaking and the instruments issued by such associates;
- (c) It shall not get involved in unfair competitive practices nor shall solicit the clients of any other rating company on implicit or explicit assurance of higher rating or any other undue benefit;
- (d) It shall not make unsubstantiated claims, in order to induce clients, about qualifications of its professional staff or its capabilities to render certain services or its achievements concerning services rendered to other clients;
- (e) It shall not be party to creation of false market;
- (f) It shall not disclose price sensitive information to any person or take any other action which is unethical, unfair and against the interest of investors and the market;
- (g) A CRA shall establish a cell within its organization responsible to communicate with market participants and the public about any questions, concerns or complaints that the CRA may receive;
- (h) A CRA shall participate in the public awareness programs with other market participants for the development of the capital market;
- (i) A CRA shall arrange and conduct training programs from time to time for the capacity building and skill development of the officers of other institutions;

- (j) A CRA shall formulate necessary code of conduct for its employees regarding handling of the non-public information. The code of conduct must contain at least such information as mentioned in **Annexure-V** attached to this Code; and
- (k) CRAs shall engage independent and separate foreign experts to conduct comprehensive review of their rating policies, procedures and methodologies with a view to revamp their existing practices, if found necessary. The CRAs shall engage the foreign experts once in each three years period. For the first time, the foreign experts must be engaged by June 30, 2014. Terms of reference of the foreign experts shall be finalized with the prior written approval of the Commission.

(Imran Inayat Butt)
Director/HOD (MSRD)

[No. SMD/CIW/CR/03/2012]

**LIST OF POLICIES TO BE DEVELOPED AND DISCLOSED BY A CREDIT RATING
COMPANY/AGENCY**

The Policies to be developed and disclosed by a CRA shall include at least the following:

- (i) Policy for solicited credit rating, un-solicited credit rating and private credit rating.
- (ii) Policy for announcement of rating.
- (iii) Policy for withdrawal and suspension of rating.
- (iv) Policy for charging fee relating to the credit rating services.
- (v) Policy for review of credit ratings. The policy must cover all the reviews including annual review, review upon occurrence of any event where CRA deems appropriate that the rating be reviewed and review on the basis of request by an investor, creditor or the Issuer.
- (vi) Whistle blower policy.
- (vii) Policy for rotation of analyst.
- (viii) Policy for treatment of the confidential information by the CRA and its employees.
- (ix) Policy for investment and trading in securities by employees of a CRA.

**CRITERIA AND METHODOLOGIES TO BE DEVELOPED AND DISCLOSED BY
A CREDIT RATING COMPANY/AGENCY**

The criteria, methodologies and procedures to be developed and disclosed by a CRA shall include at least the following:

- (i) Entity rating criteria for each class of entity.
- (ii) Instrument rating criteria for various types of instruments like Corporate Bonds, Govt. Bonds, Sukuk, Preference Shares etc.
- (iii) Rating criteria for structured financial products.
- (iv) Criteria for rating watch and its timeline.
- (v) Criteria for rating outlook and its meaning.
- (vi) Methodology governing linkages between parent and subsidiary companies.
- (vii) Criteria on subordinated loans and preferred debt by corporate and financial institutions.
- (viii) Correlation between short and long term rating scale.
- (ix) Definition of default and calculation of the default rates.

OTHER INFORMATION TO BE DISSEMINATED ON THE WEBSITE OF A CREDIT RATING COMPANY/AGENCY

In addition to the information mentioned in para 4.3.2 of the Code, CRAs shall disseminate on its website the following information:

- (1) Detail of all credit ratings conducted during the last five years, both solicited and unsolicited. The detail must contain atleast the following:
 - (i) In case of entity ratings:
 - (a) Name of the entity rated;
 - (b) Name of sector belonged to; and
 - (c) Rating grade assigned.
 - (ii) In case of instrument ratings:
 - (a) Nature of the instrument;
 - (b) Tenure of the instrument;
 - (c) Size of the issue;
 - (d) Redemption schedule;
 - (e) Nature of security, in case of secured instrument;
 - (f) Rating grade assigned; and
 - (g) Name of the Trustee.
- (2) List of entities and issues switched over from one CRA to other CRAs during the last five years.
- (3) Detail of transitions/changes in the credit ratings reviewed during the last five years. The detail should contain the ratings upgraded, downgraded and those remained unchanged. For ease of comparison both the rating i.e. before and after the review and the number of notches upgraded or downgraded should be disclosed.
- (4) History of the credit rating of all the outstanding issues. The history should contain name of the issuer, nature of the instrument, initial credit rating and its date, first revised credit rating and its date, second revised credit rating and its date, third revised credit rating and its date and so on.
- (5) Rating scales both long term and short term and their definitions.
- (6) Definition of the term, “default”.
- (7) Entity-wise list of defaults for all the outstanding issues and for all the issues redeemed during the last five years.
- (8) Rating scale-wise list of default for all the outstanding issues and for all the issues redeemed during the last five years separately for structured instruments and non-structured instruments.
- (9) Number of private ratings conducting during the last five years and number of private ratings made public during the last five years.

FIT & PROPER CRITERIA FOR APPOINTMENT OF THE CHAIRMAN, CHIEF EXECUTIVES AND DIRECTORS OF A CREDIT RATING COMPANY

To determine whether a person is fit and proper to hold the position of the Chairman, Chief Executive and director in a CRA, the CRA would consider the following:

- i) Reputation of the nominee in the industry.
- ii) Length of service and relevancy of his past experience to the nature of the job.
- iii) Educational qualification and its relevancy to the nature of the job.
- iv) Likely impact of his holding that position in the CRA on any client of the CRA, the investors and the market.
- v) Any other fact and information as may deem appropriate by the CRA.
- vi) CRA shall ensure that the person nominated for the position of chairman, chief executive or director has not been:
 - (a) convicted in any criminal offence or directly involved in any settlement in civil/ criminal proceedings in any court, particularly with regard to investments, business misconduct, fraud/ forgery, breach of trust and financial crime etc;
 - (b) declared associated with any unauthorized financial activity by any regulatory authority;
 - (c) disqualified/removed from the post of chairman, chief executive and director or from any other senior management position* of a company by the Commission or any other regulatory authority;
 - (d) convicted by a court of competent jurisdiction as a defaulter in payment of any loan to a financial institution;
 - (e) in default of payment of dues owed to any investor/creditor; and
 - (f) restrained, prohibited or debarred from dealing in securities in the capital market or from accessing the capital market by the Commission; or penalty of Rs.500,000/- or more has not been imposed on him by the Commission in the last three years, under any law administered by the Commission.

Provided that a person may be considered eligible in case a period of at least three years from the date of expiry of the period specified in the order for which such person has been restrained/ prohibited/ debarred has elapsed.
- vii) CRA shall ensure that:
 - (a) membership of the person nominated for the position of chairman, chief executive or director has not been suspended or cancelled by any association, professional body or entity;
 - (b) registration/license of any company in which the person nominated for the position of chairman, chief executive or director remained director during the last three years has not been suspended or cancelled by the Commission or any other regulatory;

- (c) no investigation or enquiry is under process in the Commission or in any other regulatory authority against the person nominated for the position of chairman, chief executive or director;
 - (d) no investigation or enquiry is under process in the Commission or in any other regulatory authority against any company in which the person nominated for the position of chairman, chief executive or director remained director during the last three years; and
 - (e) the person nominated for the position of chairman, chief executive or director has signed and submitted a declaration on the format provided at **Annexure-VI** to this Code.
- (viii) The person nominated for the position of chairman, chief executive or director should:
- (a) hold at least bachelor degree in business administration, accounting, finance, commerce, economics, statistics or mathematics from any university duly recognized by the Higher Education Commission of Pakistan; and
 - (b) have experience of at least three years at senior management position* in the field of financial audit and analysis, investment advisory services relating to investment in securities particularly the corporate bonds, corporate finance, investment in corporate bonds or any other related activity.

*[Explanation – “senior management position” shall include the followings:

- A. Any executive, including the chief executive or any officer acting as second to chief executive officer including chief operating officer/chief rating officer or by whatever name called;
- B. chief financial officer, head of accounts or head of finance;
- C. head of operations;
- D. head of treasury or chief investment officer;
- E. head of law, company secretary or compliance officer; and
- F. any other position, by whatsoever name called, which may be construed as a senior management position.]

MINIMUM CONTENTS OF THE CODE OF CONDUCT FOR EMPLOYEES OF A CRA

- (1) The CRA must have a Code of Conduct for its employees, hereinafter referred to as the Employees' Code of Conduct.
- (2) The Employees' Code of Conduct must require the employees to sign a Non-Disclosure Agreement (NDA).
- (3) The NDA must contain at least the following:
 - (i) A clause requiring all the employees:
 - (a) not to share the non-public information known to them due to their position in the CRA with outsiders and irrelevant employees;
 - (b) not to use such non-public information for their personal benefits or for the benefits of any of their relatives, friends and associates or for any other purpose except the conduct of the CRA's business;
 - (c) not to disclose any non-public information about rating opinions or possible future rating actions by the CRA, except to the rating entity/issuer or its designated agents;
 - (d) not to disclose any confidential information about its clients, which has come to their knowledge in the course of the rating process, to any person including other clients and press without prior written approval of such client, except when such disclosure is required under any law;
 - (e) not to use or share confidential information for the purpose of trading in securities or for any other purpose except the conduct of the CRA's business; and
 - (f) to fully adhere to the CRA's policy for trading in securities by its employees.
 - (ii) A clause prohibiting all the employees from participation or otherwise influence the determination of the CRA's rating of any particular entity or instrument, if the employee;
 - (a) owns securities of such entity, other than holdings in diversified collective investment schemes;
 - (b) owns securities of any entity related to such rated entity, the ownership of which may cause or may be perceived as causing a conflict of interest, other than holdings in diversified collective investment schemes;
 - (c) has had a recent employment or other significant business relationship with such rated entity that may cause or may be perceived as causing a conflict of interest;
 - (d) has an immediate relation (i.e., a spouse, partner, parent, child, or sibling) who currently works for such rated entity; or
 - (e) has, or had, any other relationship with such rated entity directly or indirectly that may cause or may be perceived as causing a conflict of interest.

- (iii) A clause requiring the rating analyst to disclose, before commencement of the rating process, relationship, if any, with the rating entity or any of its major shareholder and director or any other interest in the entity to the officer designated by the CRA for this purpose.
- (iv) A clause prohibiting the rating analysts to join, within one year of the relieving from CRA, any entity rated by such CRA.

Date:

To:

The ...[Name of the respective Credit Rating Company].....;

Dear Sir;

DECLARATION FOR NOMINATION AS [] OF [NAME OF THE CRA] PURSUANT TO THE CODE OF CONDUCT FOR THE CREDIT RATING AGENCIES

- (1) I declare to the best of my knowledge and belief that:
- a) I have not been convicted or charged with any offence under the securities laws or other laws involving fraud or dishonesty in a court of law within or outside Pakistan, during the last ten (10) ten years from the date of this undertaking;
 - b) neither I have received any notice nor subject to any inquiry or investigation by any regulatory authority within and outside Pakistan;
 - c) I am not defaulter of any financial institution nor declared as defaulter during the last ten (10) years;
 - d) there is no omission of any material fact from this Undertaking and the documents provided to the CRA with respect to my appointment as chairman/chief executive officer/director of the CRA; and
 - e) there is no false or misleading statement in this Undertaking and the documents provided to the CRA with respect to my appointment as chairman/chief executive officer/director of the CRA.
- (2) I hereby undertake that:
- a) I will continuously exercise integrity, diligence, competence and soundness of judgment in fulfilling my responsibilities for this position under the applicable laws;
 - b) I will not interfere in the fair implementation of the rating policies, criteria, methodologies and procedures and will not influence any of the rating process.
- (3) The above declaration has been signed by me pursuant to my nomination as(Name of the position nominated for) of ...(Name of CRA)...

Yours faithfully,

.....

Name:

Date:
