# Interactions between regulatory realms: new administrative law and credit rating agencies in a globalized society

## *Interacciones entre ámbitos regulatorios: el nuevo derecho administrativo y las agencias de calificación crediticia en una sociedad globalizada*

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**Abstract:** This article examines European legislation and academic literature concerning the regulation of Credit Rating Agencies (CRAs) during times of crisis, focusing on the perspective of administrative law in global governance. To this end, it proposes a perspective that considers a communicative process to minimise negative consequences for society within the context of CRA regulatory activity. Existing regulations, reports from European, American, and international authorities, as well as relevant literature, are reviewed to understand how regulatory challenges are addressed in the era of globalization.

A significant shift in regulatory focus is identified, with a move towards new governance models that recognise the private sector as a partner in a relationship of shared responsibilities following crises. The importance of considering new regulatory strategies to organise public and policy responsibilities more effectively is emphasised. While an analysis of deficiencies in CRA regulation during crises is provided, the aim is not to offer a comprehensive analysis of regulatory evolution to date. Subsequent research will analyse this evolution, assessing the effectiveness to date of regulatory policies proposed during crises.

This work contributes to the debate on CRA regulation by proposing a novel regulatory perspective from administrative law in global governance. It provides a comprehensive view of regulatory challenges in a context of increasing global interconnectedness. It is concluded that responsibility for promoting the public interest should be shared between the state and society, recognising the crucial role of the private sector as a partner in risk management and the promotion of economic stability globally.

**Keywords:** legal pluralism; credit rating agencies; administrative law; global governance; regulation.

**Resumen:** Este artículo analiza la legislación europea y la literatura académica sobre la regulación de las Agencias de Calificación Crediticia en momentos de crisis, centrándose en la perspectiva del derecho administrativo de la gobernanza global. Para ello, se propone una perspectiva que considera un proceso comunicativo para minimizar las consecuencias negativas para la sociedad en el contexto de la actividad regulatoria de las Agencias de Calificación Crediticia. Se examinan las regulaciones existentes, informes de autoridades europeas, estadounidenses e internacionales así como la literatura relevante para comprender cómo se abordan los desafíos regulatorios en la era de la globalización.

Se identifica un cambio significativo en el enfoque regulatorio, con un movimiento hacia nuevos modelos de gobernanza que reconocen al actor privado como un socio en una relación de responsabilidades compartidas tras momentos de crisis. Se resalta la importancia de considerar nuevas estrategias regulatoria para organizar las responsabilidades públicas y políticas de manera más efectiva. Aunque se ofrece un análisis de las deficiencias en la regulación de las Agencias de Calificación Crediticia en tiempos de crisis, no se pretende ofrecer un análisis exhaustivo de la evolución de la regulación hasta nuestros días. En otros trabajos de investigación sucesivos se analizaría esa evolución donde se evaluaría la efectividad hasta nuestros días de las políticas regulatorias propuestas en tiempos de crisis.

Este trabajo contribuye al debate sobre la regulación de las Agencias de Calificación Crediticia al proponer una perspectiva regulatoria novedosa desde el derecho administrativo de la gobernanza global. Ofrece una visión integral de los desafíos regulatorios en un contexto de creciente interconexión global. Se concluye que la responsabilidad en la promoción del interés público debe ser compartida entre el Estado y la sociedad, reconociendo el papel crucial del sector privado como socio en la gestión de riesgos y la promoción de la estabilidad económica a nivel global.
**Palabras clave:** pluralismo jurídico; agencias de calificación crediticia; derecho administrativo; gobernanza global; regulación.



## I. Introduction

In the last century 'globalization' has been reflected in a wave of legal pluralism where states are giving up sovereignty to supranational structures as well as diminishing its traditional functions through engaging in collaborative regulatory activities with private forces. Between national and global spheres complex systems are involved in decision-making processes. A globalized in-

terdependence that is inevitable –and desired. In such a scenario, administrative law of global governance is called to manage the communicative process that takes place, in order to minimise negative consequences.

In the context of economic crisis, e.g., 2008, this work is divided into four main sections. The first section is devoted to briefly expose the main literature regarding the phenomenon of legal pluralism in connection to globalization. This section introduces the core idea of this work: the shift from a hierarchical model of laws and organization of society to a heterarchical one, -specially, in regulatory activities.

In the second section, it is demonstrated that such a shift is happening in what has been called 'new administrative law'. In this section the blurring of territorial frontiers is explained as well as the blurring of the traditional public/private divide. The consequences of such new tendencies for society and law are also laid out. The last subsection of the second part of this work concludes introducing the case of credit rating agencies (CRAs), namely, it addresses the role played by private entities in public governance.

The third section illustrates the theory. It does it by providing the historical example of CRAs' contribution to the 2008 financial crisis. Their weaknesses as well as the regulatory measures taken globally (especially in the European Union) to fight against them are analysed.

Before concluding, the last section suggests how the transition might be facilitated. Thus, it is suggested to avoid the classical understanding of division of powers that classify lawmaking and implementation as differentiated phases of the regulatory process. New governance models have to be designed to empower agencies to participate in the design, development, implementation and monitoring of public policies.

## II. A new wave of regulation in a globalized world: from a theoretical focus on legal pluralism to a pragmatic focus on collaboration

Legal Pluralism is a fact, it is undeniable. So, why is it such a controversial issue? Scholars' main concerns over this phenomenon reside on finding the theoretical explanation that could make sense of it. Making sense of the


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phenomenon is their aspiration, but the way of achieving it varies depending on the line of thought. Current theoretical efforts to formulate legal pluralism find difficulties in defining 'law'. On the one hand, legal philosophers wonder whether a concept of law is necessary or not for the explanation of the phenomenon. Some of them are convinced that a concept of law is necessary in order to filling the loopholes in the explanation of legal pluralism. On the other hand, some legal sociologists' purpose seems to be limited to describe social phenomena as mere observers just trying to look for what the problems are, not looking for the solutions (Niklas Luhmann, 1997, p. 11). Sociologists' work is not a prescriptive, is a descriptive one.[1] Brian Z Tamanaha (2007) claims that the conceptual problem of legal pluralism cannot be resolved (p. 376). Thus, instead of facing the conceptual problem, he adopts a cross-disciplinary focus of legal pluralism. Emmanuel Melissaris (2009) on the contrary, advocates for the search of a concept of law for the purposes of making sense of legal pluralism.[2]

Despite the diverging views on framing the same issue, I would like to point out that it is precisely in the multidisciplinary approach, in an exercise of collaboration, where knowledge can be generated adequately to find solutions (when it is the aim) or to try to arrive to a better understanding of the problem in the first place. Following Tamanaha distant position from trying to solve conceptual problems, but not abandoning the issue of co-existing legal systems interacting in our networked society, I will deal with this issue in the context of the so-called traditional dichotomy of public/private regulatory realms. However, I will do so in an attempt to show how the dichotomy is disappearing and becoming instead a conglomerate of efficient collaborative practices. Thus, this work will not come back to the debate on the existence or necessity of a certain concept of law. My enterprise from here on will be describing what the new administrative law is and its relations,

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[1] Iris Jean-Klein and Annelise Riles (2005) examine the exceedances that anthropologists or sociologists perform when they try to engage more than they should in what they observe, hence, denaturalizing its commitment: the 'anthropological engagement'.

[2] On the tension between the sociological and philosophical conceptions of legal pluralism see Roger Cotterrell (2009) review on Melissaris work. Cotterrell disagrees with Melissaris' argument on that 'sociology of law depends ultimately on legal philosophy's conceptual inquiries'.

as public law, with private actors which also participate in regulatory activities as is the case of credit rating agencies (CRAs). A mélange of regulations that I consider are part of the legal pluralism phenomenon. And I will do it with the lens of an administrative law researcher who describes how the measures taken are improving (or maybe not) CRAs deficiencies that contributed to the economic crisis.

For the late twentieth century, the manifestations of 'globalization' have given rise to a wave of legal pluralism where states are losing power (giving up sovereignty to supranational structures like EU) as well as diminishing its traditional functions as a result of the control of private forces (Brian Z Tamanaha, 2008, p. 386). Consequently, 'unofficial' legal orders are created. In this line, Gunther Teubner (1997) does not talk about officiality/unofficiality but about the idea of functionally differentiated systems with transactional reach. As an example of such idea, he analyses *lex mercatoria*. He claims that *lex mercatoria* is a law that grows and changes according to what global economy transactions and organizations command so that it is vulnerable to pressures from the political system. Nevertheless, he also acknowledges that *lex mercatoria* flexibility not necessarily means weakness, since a global unification of law will be helped by flexible and adaptive laws (Gunther Teubner, 1997, p. 15). Flexibility is one of the key characteristics in contributing to public-private *corresponsibility*.[3] Gunther Teubner's conception of global legal pluralism is based on two assumptions: on self-organized processes ('contracting' itself could be said to be the primary source of law of global contracts) and on the no necessity to produce 'rules of recognition' because what we face is a 'self-legitimating' situation.[4] For Gunther Teubner, global law can only be explained by theories of legal pluralism, but once these theories reformulate their core concepts. His proposal is shifting their focus from groups and communities to discourses and communicative networks. Here is the connection with what I will explain later: the new wave of communicative efforts in decentralising the decision-making process in public law, specifically in adminis-

[3] In relation to administrative law this concept is used by Javier Barnés. See: Javier Barnés (2019, p. 79).

[4] Although Gunther Teubner acknowledges that *lex mercatoria* needs recognition by other legal orders, he also emphasizes the secondary character of such recognition since it is 'not constitutive' of the existence of a legal order (Gunther Teubner, 1997, p. 14).


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trative law. Legal pluralism is no longer a set of conflicting social norms, but a multiplicity of diverse communicative processes in a given social field. Likewise, administrative laws are no longer a set of norms alienated from private norms or agencies regulations. There are not any more different regulations, but a realm of regulation were communicative processes take place to deliver outcomes in the most efficient way from which the whole society should benefit (not only a handful of privileged social groups).

So, the first step to this new understanding of what law is becoming entails considering the traditional hierarchical frames broken (Gunther Teubner, 2002). The new wave of regulation demands collaborative networked processes in a heterarchical dimension. The traditional nation state model of law is different to the new proposals of global law. The main difference is that territorial boundaries disappear. These are replaced by invisible communicative networks.

Despite what has been said so far, some authors agree that the search for legal unity is no more than a utopia or at least, if it would be attainable, not the way to bring efficiency and better outcomes to society. Gunther Teubner and Fischer-Lescano (2004) acknowledge 'the vain search for legal unity in the fragmentation of global law' (p. 1017). A fragmentation of global law that does not come from territorial lines (since there is a shift from hierarchy to heterarchy) but it does come from sectorial lines (Luhmann in Gunther Teubner and Fischer-Lescano, 2004, p. 1000). In such a helpless situation of fragmentation the endeavours should be focused not on achieving unity but on achieving 'structural couplings' between global social sectors and thus selective networking of colliding realms such as public/private law realms. Here it would be interesting to introduce Hugh Collins (2015) contribution on the connection between transnational norms created by private actors and those fundamental rights, principles and concerns of public policy that should prevail in both national and international law democratic systems. Can a transnational law be created and successfully work ignoring these public values? Collins (2015) claims that the private norm creation has the defect of ignoring externalities, the general interest, social justice, human rights, and principles generally (p. 22). I agree that the private sector regulations cannot escape public values. Moreover, they should not since these private bodies' decisions (e.g. CRAs') in certain issues (e.g. sovereign debt) indirect-

ly but deeply affect citizens' lives.[5] Therefore, although ensuring to increase networking between them and public regulators a 'limit' should be established on their actions (avoiding that an excessive entry of private interests[6] breaks the democratic balance). If certain inalienable external public principles did not canalize the networking, the resulting system would tend to grow so hugely that it will destroy itself. As Luhmann states, 'the occurrence of catastrophe is contingent. It depends on whether countervailing structures will emerge [for me those countervailing structures could be administrative law or public law principles which are external to private agencies] which prevent the positive feedback catastrophe [that of the private individual interest invasion of the public sphere conditioning –even forcing to, public policy decision-making to the detriment of society interest]' (in Gunther Teubner, 2012, p. 77).

Thus, society, through the legal instrument of public law –specifically administrative law, is represented in the above-mentioned principles of control such as transparency, accountability, giving reasons, conflict of interests principles, expertise, and the like,[7] that would legitimize private actors regulatory power that have an impact in society.

## III. New administrative law. From hierarchy to heterarchy: decentralising the decision-making process

Traditional administrative law studies on administrative bodies are descriptive in nature. Administrative organization used to be seen as a competence system (who may do what). In the last two decades, the approach of administrative guidance for governance, as Annelise Riles (2011) remarks, has been mostly portrayed by academic observers as 'flawed and outdated' (p. 127).

[5] E.g., when governments modify their public policies depending on what CRAs report about their sovereign debt, what if those agencies' calculations, whose main principle is secrecy about methodology, make a mistake? A whole country's policy is modified according to their evaluation, an evaluation that cannot be scientifically challenged by a third party because nobody knows the procedures carried out for the calculation. In the end, those affected by such unprincipled practice are the ordinary citizens, since governments' reaction to those evaluations is implementing austerity policies, reducing access to social services, etc.

[6] It leads to 'regulatory capture', a concept that will be explained later.

[7] Principles that will be analyzed later in relation to CRAs.


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However, nowadays administrative law studies are discovering, in dialogue with other sciences, new dimensions. In Annelise Riles' (2011) words, 'recently, the fashion in policy, journalistic, and academic circles has swung the other way, toward thinking about new forms of public-private regulatory cooperation' (p. 127). On the one hand, administrative organization is a system of knowledge management where administrative bodies must manage the best information and knowledge available in order to make good decisions. It involves activities such as gathering, processing, transferring or sharing information. On the other hand, administrative intervention and, more broadly, governance and regulation are frequently 'organizational intervention' or 'organizational regulation'. Legal design of organization is a very important regulatory function. For example, when legislators want to improve the regulation of financial markets, they establish new and better regulators (like organizations aiming to get better outcomes) (Annelise Riles, 2013).

The first premise is that, on the one hand public administrations can be seen as 'systems' that process information; on the other hand, that administrative procedures can be seen as 'processes' that gather and process information (Eberhard Schmidt-Assmann, 1993). The second is that organizational legal design can become a strategic tool for accomplishing regulatory tasks (Javier Barnés, 2011, p. 471). Thirdly, the rigid (theoretical) divide between state/society, between public administration/private sector (rather public organization/private organization) according to a classical administrative law perspective is blurred and transformed into a new collaborative paradigm. The final premise is that the traditional hierarchical administrative bodies in most nation-states, once 'omniscient' (that seemed to know everything they needed), with top-down organizations and processes, corresponded to an autarchic one. But these premises need to be replaced by new structures, since knowledge only can be generated by collaboration (interagency collaboration, public-private cooperation). Thus, a new administrative organization law must be developed, considering that administrative bodies alone are not those suitable to gather and process information in other hands, nor to generate knowledge under a new cooperative and networked environment.

## 1. *New administrative law. Breaking frames*

The history of administrative law has always been a history of change and reform. However, today, more intense changes are taking place: from state-centred administrative law to a global administrative law; from an imperative, autarchic hierarchical administration to a heterarchical collaborative administrative action; from a regulatory process focused on the formal division between the stages of lawmaking and implementation to an administrative process that promotes a dynamic interaction between these stages. The traditional domains of administrative law have been widened to include unexplored 'domains' in constant evolution (global and private spheres). These domains are to be 'colonized' by an emerging new administrative law. In this context of change, administrative procedure is a key protagonist, given its central role in administrative law, a prominent position that is best understood when seen in the light of the disappearance of two traditional frontiers, addressed as follows.

### A. *National and supranational borders*

Between global and national spheres there is a wide area of mixed bodies and procedures, joint decisions, and complex systems (Sabino Cassese, 2005, pp. 676-681 and 683-689). In making and implementing public policies, administration has become a more-than-national entity.[8] Administrative law of global governance is designed to address the consequences of globalized interdependence in all relevant fields.

A response to the disappearance of national borders has been put forward with 'composite' procedures between domestic and European regula-

[8] Regulation has been internationalized in an informal way; the primary impetus for its development has been domestic bureaucracies themselves. See David Zaring, 2005, p. 547. This phenomenon is intense at the European level. The European Union is a union of domestic and European non-hierarchical administrations based on the collaboration principle. Procedures, information gathering, and exchange, control and regulations are not divided according to a separation principle between national and European spheres. Conversely, all administrations and agencies are involved in sophisticated governance models. See Eberhard Schmidt-Assmann in Javier Barnes (ed.), 2006, pp. 103-111. See also its complementary expanded 2012 edition.


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tory bodies that grow, both horizontally and vertically, proportionally to the increase in transnational administrative activities of the member states.

But there are more consequences derived from the phenomenon, namely, national, and international domains are no longer autonomous. Globalization has a 'domestic face' (Alfred C. Aman, 2005, p. 520): the international cooperation of domestic regulatory organizations must be subject to democratic internal legitimacy mechanisms and cannot be excluded from national accountability. New globally oriented domestic administrative law should carefully observe the internal rulemaking process of private and public actors. It requires subsequent adjustments to meet domestic accountability, transparency, participation, and legitimacy standards, not only in the internal ascending phase (preparing rules or standards, policies developments, etc.) before domestic organizations go abroad, but also in the descending phase (domestic implementation) once those organizations have participated in a supranational regulatory system and 'return home'.[9] Therefore, the evolution of domestic administrative law must also contemplate the procedural aspects of policy making and implementation existing in those new scenarios.[10]

### B. *Public-private divide*

Traditional administrative law upheld a liberal belief in the public/private divide, so it has focused on administrators primarily as decision makers and concerned itself with their impact on regulated private actors as well as the dangerous influence of private participation (Jody Freeman, 2000, pp. 557-558 and pp. 563-564).[11] However, the shift from traditional regulation to new governance models (Orly Obel, 2004, p. 342) implies that the new administrative law considers the private actor differently, as a partner of a relationship mutually beneficial, in a system of shared responsibilities. Privatization should not be considered as a zero-sum game between public norms

[9] On the impact of global governance on the rules of domestic procedure see Richard Stewart, 2006, p. 695.

[10] On International regulation and global administrative law see, Richard Stewart, 2003, at 445.

[11] 557-558 (private actors are considered in terms of danger), pp. 563-564 (administrative law reacts to the 'private' defensively).

and private power (Jody Freeman, 2000, p.547). It is not a surrender of powers on behalf of the state, nor does it mean the creation of a minimalist state. The public-private construct constitutes 'a new way of organizing public responsibilities and politics' (Jody Freeman, 2003, p. 1289), a new regulatory strategy that shifts the weight of the transaction costs to the private sector. Therefore, the responsibility should be shared between state and society in the promotion of the public interest, remaining the ultimate control of the final result in the hands of the administration. Public agencies, the private and non-profit sectors, and members of the public should be enrolled in the collaboration project specially through open discussions of regulatory problems within new institutions designed to facilitate problem-solving. A project that would lead to more effective and efficient solutions than those attained through only traditional administrative decision-making.

A much greater field related to public-private cooperation[12] relates to the issues of private procedure, namely: how, public values are to be extended to privatized sectors by means of procedural arrangements, —e.g. imposing due process and fairness requirements to the interested parties (Jody Freeman, 2000, p. 587, 589); or, in standard-setting organizations, requiring balanced representations on their technical committees to avoid the disproportionate influence of the more powerful interests involved (Jody Freeman, 2000, p. 641), or designing internal procedural rules to promote information disclosure, reasoned decision making, (Jody Freeman, 2000, p. 643) etc.

### 2. *Private actors main role in regulatory activities*

Private actors (associations, foundations, corporations, individuals) play a main role in regulatory activities at national, supranational (EU), and international level. They share responsibilities with the public sector, with administrative bodies. Public and private actors participate in policy making,

[12] New changes give rise to new regulatory and procedural questions that require new solutions: 'how best can non-state actors be involved in decision-making processes; how can we maximize the flow of information involving these decisions; and how can we mitigate conflict of interest concerns that arise from the fusion of public and private that typify many markets and market approaches to policy issues--issues ranging from private prisons to welfare eligibility.' (Aman, 2005, p. 516).


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implementation, and enforcement, thereby decentralizing the decision-making process through overseeing, monitoring, controlling activities, self-regulation, co-regulation, and the like. It is the case of the Advertising Standards Authority[13] (ASA), the International Organization for Standardization[14] (ISO), public standards agencies, CRAs that assess the sovereign debt of member states, or Global GAP.[15] Therefore, the need for a transfer of public values from public law to private law arises, from a public law point of view, because private actors actually regulate. Using Gunther Teubner (1997) phrasing, what we would be dealing with here is not with a set of conflicting social norms, but with a multiplicity of diverse communicative processes in a given social field.

These private actors should be subject to criteria or principles of public law, especially when they are transnational organizations. If a Central Bank is required to comply with public law principles, a CRA should also be required to follow public law principles such as transparency, accountability, giving reasons, conflict of interests' principles, and the like. However, it should be noted that what has been addressed does not mean to claim that private law loses its autonomy and flexibility in order to adopt the organizational and procedural principles of administrative law.

In fact, (administrative) procedures and (administrative) organizations play a major role as a regulatory strategy of the parliament to steer agencies and public bodies. While procedural rules establish how to decide, organizational rules establish how it works.[16] From this point of view, the use of procedural and organizational components and principles of administrative law as a way to regulate 'private regulators' must be further researched. The purpose of such further research in this point is to find out how this transfer of values to private organizations ought to be developed and under which conditions, depending on the actors, sectors, and levels.

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13 http://www.asa.org.uk/

14 http://www.iso.org/iso/home.html

15 http://www.globalgap.org/uk_en/

16 From USA, see Mathew McCubbins, Roger G. Noll, Barry R. Weingast, 1987. From Europe, see Eberhard Schmidt-Assmann, 2004 and the Spanish version, Eberhard Schmidt-Assmann, 2003.

Private actors collaborate with the public sector in delivering services of general interest and in regulatory activities too; therefore, they may also become regulatory resources for administrative law capable of producing accountability. In such scenario, private actors are expected to adopt principles and guarantees similar to those followed in public law by public actors but adjusted to the logic of private law. Both, public and private actors, form a complex network of actors where everyone's contribution matters. Thus, non-governmental actors perform not only 'normative' or 'adjudicative' roles but also regulatory tasks setting standards, providing services, and delivering benefits. They also help to implement, monitor, and enforce compliance with regulations. To illustrate this idea, a clear example is set as follows. Private-sector professional associations ruled by private law, civil law, such as lawyers', economists' or architects' ones, establish quality standards for the delivery of their services. As professionals, they are experts in determining the best conditions to develop their activity. Therefore, they draw up codes of conduct embodying generally agreed canons of best practice at EU level.[17] Hence, national governments implement those quality standards in their national regulations. This means that private actors develop regulatory activities in collaboration with public authorities (administrative authorities, legislators, courts). Thus, it becomes a 'co-production process'. Due to this relationship, the decision-making process of these associations as well as their composition should be governed by principles derived from administrative law. Which those principles should be? How should this collaboration-cooperation process take place and under which conditions? An attempt to answer these questions has been done in this work and in forthcoming work.

[17] See the Model Code of Conduct for European Lawyers adopted in 2021 by the Council of Bars and Law Societies of Europe here: https://www.ccbe.eu/fileadmin/speciality_distribution/public/documents/DEONTOLOGY/DEON_CoC/EN_DEONTO_2021_Model_Code.pdf


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## IV. From theory to practice: credit rating agencies

### 1. *The public interest and independent agencies. A Comparative approach*

The shadow of private interests in administrative decision making –allegedly based exclusively on the public interest, is not a new issue. How to define 'public interest' has never been easy. On the one hand, it can be configured by the parliament through general laws. On the other hand, it can be defined through no political intermediaries so that the only way of delivering 'public services' is directly by the administration. There is a clear tension on defining public interest.[18] The relation between Public Administration and the 'Public interest' varies from one country to another. In the US the traditional role of the Administration has never followed the European one of understanding itself as the 'legitimate interpreter of the public interest' (Karl-Heinz Ladeur, 2002, p. 2, 5).

Some European administrations developed a remarkable degree of knowledge in all technical fields by accumulating common knowledge which they used to elaborate technical regulations. Thus, they got to play a very active role in distributing knowledge to private firms and as a result, a public logic was internalised by private actors through 'general technical standards' coming from the state. Nevertheless, this situation changed when the economy started to impose its own rules to the state. The tables were turned and due to the technical complexities, it was the state which became more and more dependent on private expertise, –as it seems to be the case until today.

Such technical complexity in the US, without the European strong tradition of administrative expertise, was managed through independent administrative agencies.[19] Special interests (of the agencies) were intertwined with

[18] More in what has come to be called 'public interest law', and different conceptions of public interest see: Edwin Rekosh, 2004. A published and revised version of a public lecture delivered at Central European University in Budapest on 22 November 2000.

[19] Such as the 'Inter-State Commerce Commission' (ICC), the first agency with regulatory

general interests (since the conception of the agencies implied legislative, administrative, and adjudicative competencies). Expertise that was increasingly adapted to political considerations as a means to fill the lack of what should be a specific administrative law devoted to balancing the weight of private interests in decision making processes (Karl-Heinz Ladeur, 2002, pp. 7-9). But more than a century after the creation of the first American agency, it remains a questioned milestone.

Whereas in the European conceptions the law is derived from an original source, the legislative power, emanating directly from the sovereign (whether the king, the nation, or a People's Assembly); in the American conception, the legislator is not the original source of power, rather he is conceived as a 'subdelegated power'. Hence, the agencies act by subdelegation of the Congress (Jesús Avezuela Cárcel, 2008, p. 5). Rule-making and adjudication functions are necessarily borrowed by the agencies. According to the American professor, Peter L. Strauss (1996), the phenomenon of subdelegation 'is an inevitable by-product of a complex society and the limits of time and resources available to a generalist legislature.'( p. 747) However, a different line of thought suggests that agencies have also contributed to the deterioration of the constitutional system –designed as a response to the crisis of the duality of powers: administrative branch v. executive branch. Thus, implying a clear misuse of powers in favour of the President through what has been termed, the 'unitary executive power' theory (Jesús Avezuela Cárcel, 2008, p. 8). The case of CRAs illustrates the debate. But how to balance effectiveness with democratic control?

## 2. *The case of credit rating agencies (CRAs): origins and deficiencies*

The European Commission (EC) defines 'Credit rating' as 'an opinion issued by a specialised firm on the creditworthiness of an entity (e.g., an issuer of bonds) or a debt instrument (e.g., bonds or asset-backed securities)'. This opinion is based on research activity and presented according to a ranking system issued by a CRA. In other words, it is 'a service provider specialised

powers, created by the Interstate Commerce Act 1887. After ICC others such as the 'Food and Drug Agency' (FDA) were created.


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in the provision of credit ratings on a professional basis'. Standard & Poor's, Moody's and Fitch are the three main rating entities covering approximately 95 % of the world market; the rest is covered by smaller rating agencies.[20] CRAs were created as a response to the need of investors to accumulate information on increasing investment options (Raquel García Alcubilla and Javier Ruiz del Pozo, 2012, p. 2). These are private companies which provide assessments of the ability of users to meet their debt obligations; thus, playing a crucial role in the financial markets as informative intermediaries between investors and issuers (Andrea Miglionico, 2012, p. 9). But independently of whether the rated entity is a private enterprise or a sovereign borrower, credit ratings highly influence the cost of funding.

Although the debate about the role and functioning of the CRAs existed before 2008,[21] the global crisis and the euro crisis since 2010 reignited the debate about the information content of (especially sovereign) ratings and the market impact of CRAs (Joshua Aizenman, Mahir Binici and Michael M. Hutchison, 2013) ultimately affecting citizens' well-being. This situation revealed serious weaknesses on credit ratings as well as in the then existing EU rules on them. As a reaction to CRAs power and loopholes in its regime, in 2010, the ECON Committee of the European Parliament, in March 2011, adopted the 'Report on Credit Rating Agencies: Future Perspectives'.[22] Important matters were included such as the over-reliance on ratings in regulation, the increased capacity for supervisors, etc. External credit ratings have played and continue to play an important role in financial markets, but recent years have shown that they can 'contribute to and exacerbate a financial

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[20] European Commission, *New rules on credit rating agencies (CRAs) enter into force – frequently asked questions* MEMO/13/571 Event Date: 18/06/2013 They continue to be called 'the big three': e.g.: ESMA *Market Report on the EU Credit Ratings market 2023*, ESMA50-165-2477, 25 April 2023.

[21] As García Alcubilla and Ruiz del Pozo put it (2012): 'CRAs jumped into the international debate during the summer 1997 when they were unable to anticipate the difficulties of the Asian economies and were again in the spotlight at the beginning of this century when they failed to predict the collapses of huge companies in the USA and the EU (Enron, Worldcom, Parmalat)' (p. 27).

[22] Committee on Economic and Monetary Affairs, *Report On Credit Rating Agencies: Future Perspectives* (2010/2302(INI)). A7-0081/2011. Rapporteur: Wolf Klinz. 23.3.2011.

or sovereign debt crisis'.[23] Sovereign ratings play a crucial role for the rated country, while an upgrade means easier financing, a downgrade means that a country's borrowing is more expensive or difficult. As more governments borrow on the international bond markets, CRAs have 'stolen the show' (Ahmed Naciri, 2015, pp. 2-3), increasing their influence.

'Regulation' and 'agencies' are two concepts that have always been closely related. The US included CRAs in the regulatory framework in the 1930s, coinciding with the spread of the use of the expressions 'credit rating agency' and 'rating agency' in banking and academic circles, same time of 'the height of the New Deal and the birth of the modern administrative state. It may have reflected the contemporaneous opinion that CRAs had become de facto regulators' (Norbert Gaillard, and Michael Waibel, 2018, p. 1086). The outcomes of such relationship have not always been the desired ones by both, public and private sectors. In this line, it is worth mentioning the 'theory of the capture of the agency'. Posner defines 'regulatory capture' as the 'subversion of regulatory agencies by the firms they regulate'. He distinguishes it from the regulation intended by the legislative body that enacts it to serve the private interests of the regulated firms, for example by shielding them from new entry. Therefore, capture implies conflict, and 'regulatory capture implies that the regulated firms have, as it were, made war on the regulatory agency and won the war, turning the agency into their vassal' (Richard A. Posner, 2013, p. 2). Moreover, some authors like Bernstein (in Avezuela Cárcel, 2008, p. 17), claim that the regulatory *capture* of the agency occurs as a result of the negotiated procedure of regulation, whereby what should be considered 'public interest' is not exclusively defined by the executive power democratically legitimated but also by private interests. It means that such participation of private interests in the definition of 'public interest' may be eroding the democratic principle.

Thus, it seems to be the risk that a democratic society has to run in a context of a more and more globalized networked society whose complexity demands more flexibility. Preventive measures, as regulatory interven-

[23] European Commission, Directorate-General for Financial Stability, Financial Services and Capital Markets Union, *Study on the Feasibility of Alternatives to Credit Rating. Executive Summary.* EV-02-15-689-EN-N, (December, 2015).


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tion, are proposed by some authors like Riles, who claims: 'in certain cases and situations, at least *ex ante*, informal and coordinated public private regulation can indeed be efficient and innovative' (e.g., to avoid the financial crisis). In my view, as the public/private divide blurs, concessions should be granted by both parties. Nevertheless, the aim of a completely pacific coexistence in a harmonious combination is always under (regulated) negotiation. To achieve a viable negotiation that considers democratic principles, the European Parliament[24] considers of outmost importance that all CRAs abide by the highest standards of transparency, integrity and disclosure included in Regulation (EC) No 1060/2009, ensuring the quality of ratings, and avoiding 'rating shopping'.

But before focusing on the analysis of current regulation and proposals, closer attention should be paid to the weaknesses in CRAs' practices.

### A. *Transparency*

The adequate information about the characteristics and limitations of the ratings is crucial for investors to be able to correctly understand the real meaning and value of the ratings. Moreover, the methodology that CRAs use differs considerably between CRAs, making it more difficult for a third party to compare their performance (García Raquel Alcubilla and Javier Ruiz del Pozo, 2012, p. 30). Thus, the lack of transparency in CRAs methods is the main obstacle that policymakers are trying to remove.

It should be noted that transparency ought not to be achieved by forcing issuers to grant open and free access to all relevant data. Instead, policymakers should determine which information is necessary to be revealed to the investing public;[25] then establishing a more complete format for the information to be disseminated by CRAs. It is not a matter of quantity of information

[24] Committee on Economic and Monetary Affairs, *Report on Credit Rating Agencies: Future Perspectives* (2010/2302(INI)). A7-0081/2011. Rapporteur: Wolf Klinz. 23.3.2011. at 6.

[25] This is the policy suggested by the Committee on the Global Financial System, *Ratings in structured finance: what went wrong and what can be done to address shortcomings?*, CGFS Papers, No 32, at 28 (2008). Report submitted by a Study Group established by the Committee on the Global Financial System. This Study Group was chaired by Nigel Jenkinson of the Bank of England. July 2008, p. 28.

to be revealed but of quality. How the selection is to be done (which criteria should be used) is something policymakers are trying to determine in a way that public and private interests are balanced.[26]

Pagano and Volpin explain that disclosure requirements are imposed on the issuers instead of being imposed on the rating agencies themselves. For CRAs to become more accountable to the public, they would have to disclose all information used to determine ratings. But when a higher degree of transparency in rating methods is achieved, new problems arise; Marco Pagano and Paolo Volpin (2009) warn of a potential danger: 'transparency about rating models could lead to greater collusion with issuers [...]; S&P was so transparent about its CDO Evaluator Manual that issuers could predict perfectly the rating they would get, and thus structure deals so as to just get an AAA rating!' (p. 19).

### B. *Reliability*

The reliability of the ratings has also been a matter of debate due to the methodology followed by CRAs. This issue becomes even more relevant given the background of the sovereign credit ratings. And still today these agencies are rating the creditworthiness of more than a hundred of nations. Iyengar in an attempt to check such reliability points out that some studies show that the unreliability of CRAs is mostly derived from grounding their ratings on qualitative judgments rather than on quantitative analysis (Shreekant Iyengar, 2012, p. 70).[27] Therefore, consistency of rating decisions is called into question. He states further that, even in terms of communication of facts, the reliability of these ratings is questionable (Shreekant Iyengar, 2012, p. 81). Not only a lack of diligence has been observed when using inadequate information or data to ground their ratings on, but also irresponsibility even in some cases fraud, on the side of other market participants. Moreover, its methodologies were concentrated more in the issuance of new

[26] Although, as Marco Pagano and Paolo Volpin (2009), remark 'the degree of ratings transparency that is optimal for society usually exceeds that chosen by issuers of structured bonds' (p.16).

[27] Note here the contrast with the transparency aim, where the purpose was establishing criteria on the quality of the information revealed rather than on the quantity.


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ratings not devoting sufficient attention to surveillance (Raquel García Alcubilla and Javier Ruiz del Pozo, 2012, p. 29).

### C. *Conflicts of interest*

Conflicts of interest in the rating activity reflect CRAs' lack of integrity. A CRA has a clear incentive to provide favourable ratings to the issuer in order not to risk the revenues it receives from it for ancillary services. As Raquel García Alcubilla and Javier Ruiz del Pozo (2012) clearly explain there is a conflict of interests between, on the one hand, a CRA's interest in providing ratings that accurately reflect the probability of default of an issuer, and on the other hand, its interest in satisfying the issuer from whom it receives its revenue, who at the same time wishes to reduce its borrowing costs (as a consequence of the highest rating (p. 28).[28]

What makes things worse is that it remains a persistent problem despite the measures taken by several governments. As an example of the fact that the fight against conflicts of interest in CRAs is still a 'work in progress', I would like to mention US Securities and Exchange Commission 2012 annual staff report. It shows the findings of examinations of CRA registered with the SEC as Nationally Recognized Statistical Rating Organizations (NRSROs) in a moment of financial crisis. The staff identified the following findings:[29]

- One of the smaller NRSROs had *insufficient policies and procedures* for a committee responsible for managing certain conflicts of interest.
- Two of the larger NRSROs and three of the smaller NRSROs did *not fully disclose* certain conflicts of interest or their related policies and procedures and *may not have adequately managed* certain conflicts of interest.

[28] See also: Chunping Bush, 2022.

[29] Summary Report of Commission Staff's Examinations of Each Nationally Recognized Statistical Rating Organization. As Required by Section 15E (p) (3) (C) of the Securities Exchange Act of 1934, at 15-18 (November 2012) .

- One of the larger NRSROs and one of the smaller NRSROs appeared to *have weaknesses* with respect to their *policies and procedures for managing and monitoring* the potential conflict of interest posed by employee securities ownership.
- Two others, smaller NRSROs, appeared to have some weaknesses with respect to their *securities ownership policies and procedures*.
- The Staff identified other areas where some NRSROs *lacked* certain conflict of interest policies and procedures or where such policies should be strengthened.

This summary of findings is the evidence of how much still needed to be done in 2012, four years after the burst of the 2008 financial crisis[30]. Moreover, it does give us food for thought on whether regulation is a sensible course of action, or different means should be used.

### D. *Oligopoly*

The limited scope of competition among CRAs has been identified by many studies as another failure of the CRAs' industry that has contributed to aggravate the rest of deficiencies. The OECD treated this issue through its competition committee on a hearing on 'Competition and Credit Rating Agencies' held in June 2010[31]. There was a consensus on that credit rating market is a natural oligopoly and therefore increased competition is challenging (p. 20).

This issue of insufficient competition was the subject of an EC public consultation in November 2011. Section 3 of this document entitled 'Enhancing Competition in the Credit Rating Industry' does not go far enough in the issue as to propose any solution or measure to, as EC claims, 'enhance competition'. It merely describes the situation and suggests possible

[30] However, conflicts of interest have not been resolved, as e.g.Chunping Bush (2022) claims when he refers to the US legal reforms as 'partially successful', since the SEC failed to improve the 'issuer-pay' model and other existing provisions are weak. In the same vein, he adds that the US law is ineffective and has a detrimental effect on the international rating industry because the most influential CRAs are subject to US law (p. 362).

[31] with contributions from Prof. John C. Coffee, Columbia University Law School (United States) and Prof. Karel Lannoo, Center for European Policy Studies (CEPS).


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related areas to be explored (such as national central banks, establishment of European network of small and medium CRAs, etc.).[32] With the 2013 EU amendment regulation more concrete measures were established, as it will be analysed later.

Nevertheless, while the conflict can be seen as triggered by a context of oligopoly, some scholars claim that the solution of introducing more competition is likely to aggravate the conflict even more, leading to increase ratings inflation (a general increase in ratings levels that lessens the quality of ratings) (Bo Becker and Todd Milbourne, 2011, p. 496). The explanation for this position is that increasing the number of CRAs in order to increase competition reduces an individual CRA's reward from maintaining reputation (Pragyan Deb and Gareth Murphy, 2009).

## 3. *Responses to the deficiencies*

### A. *EU Regulation*

In the US, a regulatory framework for CRAs' activity has existed since 1975, reinforced by the 'Credit Rating Agency Reform Act of 2006'[33] which aims to foster more transparency, accountability, and competition in the CRAs industry. Despite the fact that this regulatory framework did not prevent the catastrophic consequences of the agencies' performance, the European Union followed suit adopting the U.S. model with the 2009 regulation on CRAs[34]. The EU regulation focuses on ensuring that CRAs avoid the above examined weaknesses. Mr Barnier[35] pointed out that the EU has been working

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32 European Commission, Directorate General Internal Market and Services, *Public consultation on credit rating agencies*,19-23 (5/11/2010).

33 The Credit Rating Agency Reform Act of 2006 amended the Securities Exchange Act of 1934.

34 Regulation (EC) No 1060/2009 of the European Parliament and of the Council, of 16 September 2009, on credit rating agencies. Amended in 2011 by Regulation (EU) No 513/2011 of the European Parliament and of the Council, of 11 May 2011. And amended a second time in 2013 by Regulation (EU) No 462/2013 of the European Parliament and of the Council of 21 May 2013 (amending Regulation (EC) No 1060/2009 on credit rating agencies).

35 European Commissioner for Internal Market and Services.

for several years to build a strong legal framework for CRAs with the help of the supervisory powers of the European Securities and Markets Authorities (ESMA)[36] from 2011. In March 2012, ESMA issued its first report on the supervision of CRAs.[37] Nevertheless, he admits that important concerns remain because the weaknesses have not entirely disappeared yet.[38]

ESMA's 2012 annual report[39] on the application of the Regulation (EC) No 1060/2009 on CRAs, as amended according to Article 21(5) in the EU, identified the aforementioned deficiencies as a result of its investigations. The shortcomings revealed were in relation to CRAs' rating processes, governance, and internal control mechanisms. Remedial action plans were implemented in order to establish 'appropriate record-keeping and documentation procedures, improve data quality and confidentiality, strengthen resources dedicated to internal control functions, increase transparency in the disclosure and presentation of ratings and enhance the involvement of senior management in their activities' (ESMA, 2012, p. 4).[40] Indeed, ESMA is playing an active role in order to achieve preventative supervision. In 2013 ESMA identified progress by CRAs in their activities to meet the regulatory requirements on integrity, transparency, and improved disclosure of methodologies. However, ESMA believed that improvements were still necessary in the areas of conflict of interest, consistent application and comprehensive presentation of rating methodologies, the monitoring of ratings, and the reliability of IT infrastructures (Rasha Alsakkaa, Owain ap Gwilym, and Tuyet Nhung Vu, 2014, p. 240). In fact, ESMA examined the bank rating methodologies of S&P, Moody's and Fitch, due to the strong linkages between bank and sovereign ratings; shortcomings were found in the processes of disclosure

36 European Securities and Markets Authority (ESMA) is the single authority with exclusive supervisory responsibility for CRAs in the EU.

37 ESMA, *Credit Rating Agencies Annual Report 2012*, 18 March 2013 | ESMA/2013/308 https://www.esma.europa.eu/sites/default/files/library/2015/11/2013-308.pdf

38 Answer given by Mr Barnier on behalf of the Commission when asked by the press on CRAs issue. 29/02/2012. Parliamentary questions - E-000566/2012(ASW).

39 ESMA, CRAs Annual Report 2012, No. ESMA/2013/308 (2013).

40 Furthermore, ESMA reports on the work on policy and cooperation, including the adoption of the draft Regulatory Technical Standards (RTS), guidelines and recommendations on the scope of the Regulation, cooperation with third countries and ESMA's supervisory competences in view of the CRA3 Regulation.


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and implementation of changes in bank rating methodologies as well as in the systematic application and review process of methodologies.

In November 2011 the Commission put forward proposals to reinforce the regulatory framework on CRAs and deal with persistent weaknesses. The new rules entered into force on 20 June 2013.[41] I would like to briefly comment on what these rules added with respect to the 2009 UE regulation and 2011 amendments. The main measure introduced is that the 2013 Amendment Regulation imposed new obligations not only on CRAs but also on issuers, originators, and sponsors in connection with structured finance instruments. The aims of the 2013 regulation focused on:

1) *Reducing overreliance on credit ratings*. For that purpose:
- the articles 5a, b and c were introduced in Title I entitled 'Over-reliance on credit ratings by financial institutions', 'Reliance on credit ratings by the European Supervisory Authorities and the European Systemic Risk Board' and 'Over-reliance on credit ratings in Union law' respectively.
- In this respect article 39 were also amended adding paragraph 5.g which introduced the obligation for the Commission, after having reviewed the situation in the credit rating market, to submit a report by 1 January 2016 to the European Parliament and to the Council, accompanied by a legislative proposal if appropriate, assessing, in particular: (g) whether there is a need to propose measures to address contractual over-reliance on credit ratings.

2) *Improving the quality of ratings of sovereign debt of EU Member States*. In this respect article 39b was inserted entitled 'Reporting obligations'; it establishes the obligation of the Commission, by 31 December 2014, of submit a report to the European Parliament and to the Council on the appropriateness of the development of a European creditworthiness assessment for sovereign debt.

3) *CRAs will be more accountable for their actions*. In this respect article 8 (a) paragraph 2 was replaced by the obligation of a CRA of adopting, im-

[41] Regulation (EU) No 462/2013 of the European Parliament and of the Council of 21 May 2013 amending Regulation (EC) No 1060/2009 on CRAs.

plementing and enforcing adequate measures to ensure that the credit ratings [...] are based on a thorough analysis of all the information that is available to it and that is relevant [...] as well as of adopting all necessary measures so that the information it uses in assigning credit ratings and rating outlooks is of sufficient quality and from reliable sources.

4) *Reduced conflicts of interests due to the issuer pays remuneration model*. In this respect:

- Paragraph (4) is added to article 6 in Title 1: CRAs shall establish, maintain, enforce, and document an effective internal control structure governing the implementation of policies and procedures to prevent and mitigate possible conflicts of interest and to ensure the independence [...] shall establish standard operating procedures (SOPs) with regard to [...] the management of conflicts of interest [...].
- Article 6a is inserted: 'Conflicts of interest concerning investments in CRAs'.
- An obligation for the Commission to review that CRAs are complying with what has been established before (added in paragraph 5 (b) in Title IIIA)

5) *Publication of ratings on a European Rating Platform*. This obligation is established in the new Article 11a inserted in title I entitled 'European rating platform'.

The new legislation not only aimed at making CRAs more transparent and accountable when rating sovereign states, but at increasing competition too, —since the ratings industry was and is still, dominated by a few market players. Reducing the over-reliance on ratings by financial market participants was also another aim.[42]

The point here is that behind CRAs lurks the service that they provide to the investing public as well as a service to the general public, –since the general well-being is in large part a function of the well-being of the economy generally. Although the *raison d'être* of private sector, in general, or of for-profit CRAs, in particular, is not directly public service (Timothy E. Lynch,

[42] This idea was also expressed by Mr. Barnier http://ec.europa.eu/commission_2010-2014/barnier/


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2009, p. 292), in fact they regulate. Therefore, some control should be established to these private entities which develop functions beyond their private spheres. The necessity of regulating CRAs is justified by their de facto participation in regulation with, a not always positive, impact on the general public. Think of mistakes made in risk appreciations during the crisis. Mistakes that not only impact investors, borrowers, issuers but also governments when they do sovereign ratings,[43] —a downgrading can have the immediate effect of making a country's borrowing more expensive, which at the same time may require changes in public policies that conditions citizens' living standards.

In order to comply with those reporting obligations, ESMA was required to provide technical advice on those matters. In September 2014, 'Technical Advice in accordance with Article 39(b) 2 of CRAR 3 regarding the appropriateness of the development of a European creditworthiness assessment for sovereign debt' was provided. In the annex 'Credit Rating Agencies Sovereign Ratings Investigation, ESMA's assessment of governance, conflicts of interest, resourcing adequacy and confidentiality controls', ESMA concluded: 'all registered CRAs have established policies and procedures to ensure ongoing compliance with the Regulation.' However, ESMA also warned CRAs about the need 'to operate with no discrepancies between these formal procedures and the way they are put into practice by their staff. ESMA perceives a risk that these discrepancies impair the integrity of the rating process and the CRAs' compliance with the Regulation'. Thus, despite this warning, ESMA reports positive findings, that is, that required processes of adaption of CRAs working methods to comply with the principles enshrined in EU Regulation had been taking place; that is to say, CRAs seemed to have internalised EU regulations. 2015 ESMA annual report also concluded in the same token.

Following ESMA's technical advice, two reports from the Commission completed the CRA Regulation call: the first report, published in October 2015 addressed the appropriateness of the development of a European cred-

[43] European Commission, *New rules on CRAs enter into force – faqs.* MEMO/13/571 Event Date: 18/06/2013.

itworthiness assessment for sovereign debt.[44] In this report the main conclusion was the inappropriateness of the creation of a European credit rating agency because 'it would have only limited impact on the efforts to reduce reliance on sovereign debt ratings as it would, most likely, duplicate existing information' at the same time as 'if not managed correctly, it could entail the risk of creating over-reliance on a new alternative if relied upon by investors in an exclusive way' (p. 18). A second report, answering to article Article 39b(1), Article 39b(2), Article 39(4)(5) reporting obligations, came to light in October 2016, addressing: alternative tools to external credit ratings, the state of the credit rating market, competition and governance in the credit rating industry, the state of the structured finance instruments rating market and the feasibility of a European Credit Rating Agency.[45] In this report the Commission reached the same conclusions as in the 2015 report on that no feasible alternatives to CRA that could replace them would be implemented given the important role they play in some parts of the EU's regulatory framework for the financial sector.

### B. *Academic Proposal to address deficiencies*

Despite the high investment costs for building its reputation, Sylvester C. W. Eijffinger (2012, p. 920) claims, the creation of a European rating agency will improve rating quality and transparency. A public agency would not aim at profit maximization but a total control over the financial regulatory framework. However, some authors are against this idea, in line with the Commission reports. For instance, Panayotis Gavras (2012) claims that even if this solution would resolve conflicts of interest, this possibility is beyond the ability of individual countries and other problems could arise, namely 'regulatory protectionism' (p. 36). Moreover, in relation to sovereign rating, countries

[44] Report from the Commission to the European Parliament and the Council on the Appropriateness of the Development of a European Creditworthiness Assessment for Sovereign Debt. COM (2015) 515 final. Brussels, 23.10.2015.

[45] Report from the Commission to the European Parliament and the Council on alternative tools to external credit ratings, the state of the credit rating market, competition and governance in the credit rating industry, the state of the structured finance instruments rating market and on the feasibility of a European Credit Rating Agency COM (2016) 664 final.


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would be rating themselves or be rated by an entity they own, as a result, issues to do with political influence would arise (p. 37).

For Andrea Miglionico (2012, p. 95) CRAs regulatory regime is too weak to enhance the accuracy of ratings. He advocates for an independent internal body that checks the accuracy of CRAs opinions, since one of the main problems of these agencies is incomplete information of ratings. It is a proposal that with the creation of ESMA has become a reality in Europe.

Amadou Nicolas Racine Sy (2009) proposes a three-step method for the regulation of CRAs focusing on macro-prudential matters. Firstly, he calls upon policymakers to be aware of and identify the risks inherent to credit rating. Then, they will have to test systemic institutions' balance sheets and off-balance-sheet positions. And finally, those systemic institutions that are vulnerable to abrupt ratings downgrade may have to hold more capital or liquidity buffers (p. 70). However, he concludes with a caution to policymakers regarding the expenses associated with such an approach. Therefore, it is imperative to conduct a thorough cost-benefit analysis of the program's implications for the proposed change.

Professor John C. Coffee Jr., (2011, p. 271) and Mauro Bussani (2010, p. 4), they both call for CRAs accountability. They argue that the belief in markets self-regulation is far from reality. Therefore, jurists and lawmakers have to design 'planetary solutions' to the actual dimension of the problems. Mauro Bussani claims that the choice of going global cannot be eluded as well as the crucial question affecting the expectations and interests of worldwide investors, market-users and national economies.

Rather than simply proposing a solution, what Mauro Bussani does is pose a question, aiming to inspire anyone willing to fully commit to the accountability mission: 'Is there anyone ready to seriously take up the challenge of making CRAs accountable, or should we await another crisis, and, in the meantime, keep crying our losses in the dark?' (p. 11) That 'anyone' might be the EU whose endeavours contribute to render CRAs more accountable.

Finally, Iyengar (2012, p. 81), in relation to sovereign credit ratings, claims that the problem not only is that CRAs are not reliable enough but that such problem has negative consequences especially for developing countries. These countries have a limited access to the capital markets, so they depend on CRAs assessments. A decrease in rating worsens the terms of the rating

therefore aggravating the economic conditions for the borrowing country. He advocates for a change in the methodology used and the factors or indicators included in the rating process in order to increase the objectivity of the rating decisions as well as rationalization of the criteria.

The rating oligopoly has reacted to the Covid-19 pandemic situation by rushing to mark down bonds and loans: 'as of May 5th [2020], S&P had downgraded, or put on negative watch, a fifth of the corporate and sovereign issuers that it rates' (The Economist, 2020, p. 57). The US SEC reacted to this Covid-19 situation by creating a 'COVID-19 Market Monitoring Group' on the 24th of April 2020. It has primarily focused on the interrelationships between ratings actions, procyclicality and financial stability, that is, the exploration of the effects of CRA downgrades on negative procyclicality and financial stability. Those interrelationships are being examined by other members of the global financial regulatory community with whom SEC shares analysis and observations (2020). Moreover, ESMA established in the 2020-2022 strategy and 2021 Work Programme its intention to actively contribute to the work of international bodies like IOSCO or the FSB regarding CRAs in the COVID-19 scenario.

## V. Conclusion

I would like to conclude this article by reflecting on two realms, that of lawmaking and implementation, on the one hand, and that of governance models as new pathways, on the other.

Firstly, legislation, implementation and enforcement are classified as differentiated phases of the regulatory process, by the classical understanding of division of powers, where administrative procedure takes a secondary position as a tool for applying the law. However, the barriers between those formal phases become more diffuse in the newly formed domains of governance, such as financial markets. The rationale behind it is sound: the legislature cannot anticipate reality and set definitive criteria on subjects that are constantly evolving. An example of this is the authorization of products intended for both human and animal use, which are derived from biotechnology and other advanced technological processes. In such instances, the legis-


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lature can only set values and objectives to be achieved, and just as crucially, outline the procedures, the answer to the 'how' question, for administrators to navigate future decisions on these matters. This indirectly shapes the nature of these decisions. Administrative regulatory bodies establish the relevant standards and implement them by means of legal procedure.

Supervisory powers are an important element in the enforcement phase, ensuring compliance with rules and public principles. Over the years ESMA's mission has been evolving towards more focus on supervision and enforcement actions in order to achieve independence, objectivity and high quality of credit ratings in the EU, thus, reducing the negative lasting impact that ratings can have on the public.[46]

However, it should not be forgotten that such compliance is also a result of cooperation between authorities and private actors. In post-crisis times, an interplay between private regulators and public supervisors within principles-based regulation and meta-regulation has taken place (Olha O. Cherednychenko, 2016). The more the cooperative mindset of the actors involved, private regulators and public supervisors, the higher the chances for compliance with public principles. Thus, as the example of CRAs compliance with EU Regulations has shown, only when private actors adapt to a cooperative landscape as well as when public authorities and administrative law adapt and is responsive to the dynamics of interaction with all sorts of regulatory forms and actors, successful compliance is feasible.

Secondly, on governance as new pathways, I would like to note that the traditional regulatory mechanism of policymaking and implementation, based on regulatory details as pertaining either to outcomes or to methods, differ in many ways from the decentralized, often privatized structures and procedures associated with new governance theory. These latter settings form the natural environment of third generation procedures that creates pathways of interaction across what used to be impassable borders (Javier Barnés, 2015).

According to Professor Barnés (2017):

[46] Regarding ESMA's powers, the discretionary part that is included at the core of its administrative powers has been debated. Marta Simoncini, 2018, p. 4, 6).

> 'First- generation procedures promote outcomes that are consistent with legal mandates and within the limits of authority granted to those exercising power. Second-generation procedures aim to provide simple rules governing executive regulations derived from a hierarchical administration. Third- generation policymaking and implementation procedural arrangements directly facilitate and channel new needs that arise from contemporary governance models. The first and second generations could be drawn in a formal, linear, or staggered structure. A complex intertwined network or web could represent the third'. (p. 343)

Due to the disappearance of boundaries the administration begins to act more and more outside the state, cooperating with private sector, and increasing its discretionary power. Parliamentary enactment of regulatory statutes often now delegates to agencies substantial autonomy to set policy choices. Thus, agencies will be empowered to design the conception, development, implementation, and monitoring of public policies.

Thus, the rationale for the public/private transfer is rooted in the regulatory role played by the private organization (in a broad sense). This entails refraining from merely extending public law requirements to any private entity. Furthermore, this approach is not a classical one that of applying public law values to private organizations acting public functions. Rather, its purpose is dealing with something more specific: private bodies that perform any kind of regulatory activity, within the regulatory process, as far as it impacts the public.

Consider that the required adjustment of values is analogical in nature. This approach necessitates a departure from the notion of an automatic transfer, instead advocating for a fusion of public values and the adaptable nature of private law. Examples of this idea can be found not only in the 2009 EU Regulation on CRAs (and subsequent amendments), as described before but also in the in European law on the award of public service contracts. Regarding the latter, a transfer of values is accomplished, without formalisms, from public procurement contracts to certain companies above certain thresholds, in the realm of regulated sectors.

New governance models and regulatory strategies are needed to deal with the challenges found in these new domains: from a state-centric system


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to a networked multi-party decision-making; from a top-down hierarchical model, to a horizontal and collaborative one; and from the traditional two-step system of implementation and enforcement to a more complex process in which regulatory bodies work actively and continually to make the best possible decision in accordance with the current reality.

In sum, because of the expansion of administrative law both across national borders and into many privatized sectors, it has to construct new spaces where agencies and other actors enjoy more discretionary powers than ever, even if it implies that the administrative procedure, structure and function have to be rethought.

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