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Credit Rating Agencies' Liabilities

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Abstract

Credit ratings assess the creditworthiness of an issuer or financial instrument. They help overcome information asymmetries and facilitate the functioning of financial markets. Credit ratings also serve a regulatory function, as they are used, inter alia, to determine the regulatory capital requirements of banks. Credit rating agencies thus act as private gatekeepers in financial markets. The global financial crisis of 2008 revealed serious shortcomings in the credit rating industry and led to a significant tightening of regulation and oversight. This paper focuses on the civil liability of credit rating agencies. The central issue concerns the liability of credit rating agencies towards investors who suffer losses as a result of excessively optimistic ratings. Credit rating agencies have traditionally been considered largely immune from civil liability. While this remains true to some extent, the paper demonstrates that the legal landscape is evolving. Some jurisdictions have adopted specific liability rules (China, the EU). Courts have tested concepts of quasi-contractual liability, as known in civil law jurisdictions (e.g., Austria, Germany, Portugal, and Türkiye), and in mixed legal systems (e.g., Israel). Similarly, courts have adjudicated cases on the basis of the common law tort of negligent misrepresentation (e.g., Australia, Singapore, the United Kingdom, and the United States). As a general finding, the emerging public regulation of credit rating agencies appears to trigger corresponding civil duties and, in turn, to enhance liability risks. Credit ratings are increasingly treated as professional assessments. It is therefore less likely today that a court will deny liability on the ground that the rating constitutes protected speech. The paper presents the key findings of a cross-country study conducted under the auspices of the International Academy of Comparative Law. It examines the relevant law and policy in 18 jurisdictions, including the European Union.

JEL Classification: D53, G15, G20, G24, G30, K12, K13, K15, K20, K22

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The central issue concerns the liability of credit rating agencies towards investors who suffer losses as a result of excessively optimistic ratings. Credit rating agencies have traditionally been considered largely immune from civil liability. While this remains true to some extent, the paper demonstrates that the legal landscape is evolving. Some jurisdictions have adopted specific liability rules (China, the EU). Courts have tested concepts of quasi-contractual liability, as known in civil law jurisdictions (e.g., Austria, Germany, Portugal, and Türkiye), and in mixed legal systems (e.g., Israel). Similarly, courts have adjudicated cases on the basis of the common law tort of negligent misrepresentation (e.g., Australia, Singapore, the United Kingdom, and the United States).

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General Report: Liability of Credit Rating Agencies

Patrick C. Leyens

1 Introduction

Credit ratings are a global phenomenon. The assessments of the default risks by Credit Rating Agencies (CRAs) serve an important function for capital markets. They enable investments, especially cross-country, by helping to overcome information asymmetries between investors and issuers, especially in the bond market. Credit ratings hence contribute to an efficient use of resources. Today, the gatekeeper role and accountability of information intermediaries of capital markets, including their liability, form an independent field of research.[1] CRAs' liabilities have attracted the attention of a number of comparative studies.[2]

Financial Markets significantly depend on the information services of CRAs. Sudden corporate breakdowns, which were allegedly not anticipated by CRAs, and, on a larger scale, the role of CRAs in financial market crises have raised the question of how to hold CRAs accountable. There has been increasing awareness that the dependence of financial markets on information intermediaries involves severe risks. The systemic dimension is not limited to CRAs but extends to statutory auditors and possibly a small number of other information providers. CRAs and statutory auditors stand out because their private services have been embedded into regulatory contexts and consequences.[3] As a reaction to the global financial market crises which culminated with the collapse of Lehman Bros. in autumn 2008, the focus of the discussion shifted towards possible legal options to strengthen the accountability of CRAs

1 Accounts of the fundamental issues are provided by Coffee, „Gatekeepers: The Role of the Professions and Corporate Governance“, 2005; Leyens, Informationsintermediäre des Kapitalmarkts: Private Marktzugangskontrolle durch Abschlussprüfung, Bonitätsrating und Finanzanalyse, 2015.

2 Comparing Australia, European Union, United Kingdom, United States of America: Miglionico, „The Governance of Credit Rating Agencies: Regulatory Regimes and Liability Issues“, 2019; on EU, Dutch, French, German, English law: Verheij, Credit rating agency liability in Europe: Rating the combination of EU and national law in rights of redress, Den Haag 2021, p. 224; on EU, German and US law Schroeter, Ratings – Bonitätsbeurteilungen durch Dritte im System des Finanzmarkt-, Gesellschafts- und Vertragsrechts, Tübingen 2014.

3 Partnoy, "How and Why Credit Rating Agencies Are Not Like Other Gatekeepers", in: Yasuyuki Fuchita, Robert E. Litan (eds), Financial Gatekeepers: Can they protect investors?, 2006.

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through a regulatory set of duties flanked by public sanctions, and, in some countries, also by civil liability for misconduct.

Commentators have observed that CRAs are largely immune to civil liability.[4] This is still true to some extent but, as this study will show, it appears that times are changing. Most remarkable are the US billion-dollar settlements with Standard & Poor's and Moody's for their roles in facilitating the financial crisis of 2008. Similarly noteworthy are civil law suits in some countries, the outcome of which, a few years ago, would have been a clear absence of liability. In some, albeit only a few cases, CRAs have been held liable for damages to injured investors. A prominent example is the Australian ABN AMRO (Bathurst) case.[5]

Liabilities of information intermediaries are seen as an indispensable component of a functioning system of the division of labor.[6] Constitutional defences to civil liability such as the freedom of speech are increasingly interpreted in a way that takes the professional character of the credit rating into account. The introduction of specialized liability rules into financial regulation in some countries, especially the EU, has removed remaining doubts as to the adequacy of civil liability. Still, civil liabilities of CRAs touch upon a set of fundamental questions in law and in economics which strongly influence the application of specialized rules as well as liability under general rules such as the law of torts. The most important ones involve non contractual negligence liability for pure economic loss, the specific forms of professional liabilities, and, more generally, the trade-offs between private and public enforcement. Comparatists frequently cite the land mark cases of *Ultramares* (United States of America),[7] *Caparo* (United Kingdom),[8] or *Hedley Byrne* (United Kingdom)[9] when explaining their own courts' approaches to the named issues. Dogmatic differences aside, the overarching challenge for courts, today also for the regulators, lies in navigating the difficult path between holding CRAs accountable and avoiding over-deterrence and chilling effects.

The present study explores the policy issues and experiences with civil liability of CRAs. The study was conducted under the auspices of the International

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4 Coffee (n 1); Partnoy, "Barbarians at the Gatekeepers? A Proposal for a Modified Strict Liability Regime", 79 Wash. Univ. L. Q. 491, 540 et seqq (2001).

5 ABN AMRO Bank NV v Bathurst Regional Council [2014] FCAFC 65; (2014) 224 FCR 1.

6 Kraakman, Gatekeepers: The Anatomy of a Third-Party Enforcement Strategy, 2 J.L. Econ. & Org. 53 (1986).

7 Ultramares Corp. v. Touche 174 NE 441 (NY 1931).

8 Caparo Industries plc v Dickman [1990] 2 AC 605 (HL). Cf. United Kingdom, p. 596.

9 Hedley Byrne & Co Ltd v Heller & Partners Ltd [1963] 3 WLR 101 (HL). Cf. United Kingdom, p. 599.

Academy of Comparative Law. Preliminary results were presented at the XXIth General Congress in Asunción in 2022. The study builds on 20 special reports. Two reports cover private international law aspects and provide an assessment of where we stand and what might be the future of CRAs' liabilities.[10] The heart of the research is formed by country reports that cover 18 jurisdictions, including an assessment of European Union law.[11] The special report on European Union law explains the law and economics of CRAs' liabilities, the opportunities offered by harmonization, followed by a discussion of legals aspects treated in all country reports. The country reports follow the structure of the questionnaire which is attached to this volume as an Appendix.

The present report closely follows the structure developed in the questionnaire: 1. Introduction, 2. Foundations, 3. Case Law Overview, 4. Legal Basis of Liabilities, 5. Eligible Claimants, Duty Standard, and Behavior with High Liability Risk, 6. Causality and Recoverable Loss, 7. Fault Standard, 8. Comparative Negligence, 9. Burden of Proof, 10. Liability Limitations (Disclaimers), 11. Time Limitations. The study concludes with 12. Main Findings.

2 Foundations

2.1 Credit Ratings

2.1.1 The Nature of Credit Ratings

Credit ratings are forward looking statements that serve as a global language to compare the relative creditworthiness of issuers and issues.[12] Credit ratings are neither a measure of asset value (fundamental value) nor an indication

10 EU law (Wagner); Cross-border disputes (Rielaender); current and future issues (Cash). In the following, the indication of a short title refers to the contributions within this volume.

11 Australia (Hanrahan), Austria (Kalss/Ebner/Jaritz), Brazil (Borges), China (Huang/Liu), France (François), Germany (Rielaender); India (Varottil), Israel (Shapira), Italy (Miranda/Rigazio), Japan (Yamanaka), Netherlands (Keijzer), Portugal (Ferreira Gomes), Singapore (Witting), Spain (Gomez Ligüerre), Türkiye (Akçura Karaman), United Kingdom (Ferran), United States of America (Manns). In the following, the indication of a country name refers to the contributions within this volume.

12 Leyens, "Credit Rating Agency", in: Cottier, Nadakavukaren, eds., Elgar Encyclopedia of International Economic Law, Cheltenham, 2nd ed., 2027, forthcoming. For details cf. Miglionico (n 2), at 1.04., 2.01.

of the appropriateness of an investment. Credit ratings take default risk into account, meaning they always factor in the possibility of default. It is important to understand that, consequently, the mere fact that a failure occurs does not in itself constitute an error in valuation or a cause of damage.

The rating categories of leading CRAs use symbols, such as a letter or numerical symbol, which might be accompanied by appending identifying characters. The rating scales are usually divided into investment (e.g., from AAA to BBB-) and non-investment or junk (e.g., below BBB- to D).

A credit rating can be assigned to securities, especially bonds (issue rating), but also to the issuers of debt or securities, including sovereigns (issuer rating, sovereign rating). Both types, issue and issuer ratings, can be assigned when an issuer enters the market, as well as on an ongoing basis.

Professional investors and financial institutions such as banks use rating triggers as covenants in bond servicing or loan agreements. Typical clauses require the borrower to provide additional collateral or pay a higher interest rate to account for an increase in the risk of default. It is often stipulated that if the borrower's rating falls below a certain level, the lender has the right to call the bond. However, setting off the first rating trigger often leads to a loss of liquidity, which then sets off further triggers (cascade effect). This can increase the probability of default (downward spiral).

2.1.2 Market for Credit Ratings (Oligopoly)

Credit ratings emerged as a by-product of industrialization.[13] In the middle of the 19th century, Henry Varnum Poor started to compile factual information on major infrastructure projects in the United States of America, such as canals and railways.[14] The beginnings of modern rating date back to 1909 when John Moody started to offer assessments of the bonds of US railway corporations. The use of rating codes can be traced back to John Knowles Fitch, who first used a rating scale from AAA to D after Fitch Ratings was founded in 1913.

In the beginnings, credit ratings were financed by investors, often on the basis of a subscription (investor pays). In the 1970s, increased pressure on issuers and advancements in copy technology led to a transition to a new business model. Today, the vast majority of credit ratings is solicited by issuers (issuer

13 Cantor/Packer, The Credit Rating Industry, 19 FRBNY Q. Rev. 1, 2 (Summer/Fall 1994); Sylla, A Historical Primer on the Business of Credit Ratings, in: Levich/Majnoni/Reinhart (eds), Ratings, Rating Agencies and the Global Financial System, Boston MA 2002, pp. 19 et seq.

14 Chandler, Henry Varnum Poor, Cambridge 1956, pp. 31 et seq.

pays). As far as is known, only a few important countries do not have to pay for their country ratings.

In most countries, the market for credit ratings is dominated by three big credit rating agencies. The rating oligopoly is formed by Moody's, Standard & Poor's, and Fitch Ratings. An exception is India where the rating market, though oligopolistic, is not as heavily concentrated.[15] The Indian regulator SEBI set up a prohibition for CRAs to hold directly or indirectly 10% or more of the shares in another CRA. This might further complicate concentration. It is uncertain whether concentration can be countered in the long run. The rating oligopoly is seen as a global phenomenon. In developed countries, especially the US, consolidation processes started early and are continuing.[16] The so-called 'Big Three' mainly work at the request of the issuer. It seems that smaller CRAs operate regionally and/or focus on particular industries. For the EU, the European Securities and Markets Authority annually publishes information on the market share of the individual CRAs.[17]

Over the years, there have been many pleas to break up the CRA oligopoly. Plans to establish a European CRA as a counterbalance to the big three have not been pursued further, though. In 2013, the Universal Credit Rating Group (China) was founded in Hongkong as a partnership of Dagong Global Credit, Egan-Jones Ratings, and RusRating. This is of importance since Egan Jones (USA), founded in 1995, is known for offering its credit ratings to investors, i.e. it works on the basis of the investor pays model. However, the Universal Credit Rating Group has apparently ceased operations.

Newly established rating agencies are often bought up by the established agencies. For example, after a country rating downgrade, Türkiye encouraged the establishment of domestic credit rating agencies.[18] The CRA DCR Turkey was founded in 1998, but only two years later merged with Fitch. In Israel, Maalot, one of the two domestic CRAs, started in the early 1990s following an initiative of the state, but became part of S&P in 2008.[19] The other Israeli CRA Midroog started operating in the early 2000s. Today it is controlled by Moody's through a majority shareholding. In China, restrictions were removed in 2017 that previously required foreign CRAs to partner with local firms.[20] This

15 India, p. 364.
16 Coffee (n 1), pp. 283 et seq.
17 ESMA, CRA Market Share Report, ESMA84-2037069784-2228, 19.12.2024.
18 Türkiye, p. 557.
19 Israel, p. 395.
20 China, p. 280.

reform enabled Standard & Poor's and Fitch to enter the Chinese market as wholly foreign-owned CRAs in 2019 and 2020.

2.1.3 CRAs as Private Gatekeepers

Initially, credit ratings were intended solely for informational purposes. In a second step, rating grades and rating triggers became an essential component of the transaction practice.[21] These developments took place on a purely private level. Nevertheless, they established CRAs as private gatekeepers of financial markets. Gatekeepers are private parties that provide positive, qualified, or negative assessments. The market reacts to their assessments by lowering or raising the prices of capital, which is usually reflected in interest rates, coupons, or bond prices. In this manner, CRAs facilitate, complicate, or even prevent an issuer's access to the capital market.

Finally, credit ratings assumed a regulatory function, mainly through banking regulation (rating-based regulation). It is this regulatory function that has significantly fostered the gatekeeper role of CRAs. Already in the 1930s, US banks were required to hold only bonds with an investment grade provided by at least two CRAs (double rating). In 2005, the Basel Committee on Banking Supervision issued its Accord II, which introduced risk sensitive measurements of the regulatory capital that must be held by a bank. Only credit ratings of recognized CRAs can be used to determine the amount of regulatory capital needed. The integration of credit ratings into financial regulation might take different forms. The use of credit ratings to determine the regulatory capital of financial institutions is a global phenomenon.[22]

Once regulation began to attach legal consequences to private credit ratings, the character of CRAs changed. CRAs no longer simply commercialized opinions, but started to sell regulatory licenses to their clients. Their function evolved towards a quasi-public service provider. Professor Frank Partnoy describes what had happened as a delegation of monitoring by the state.[23]

In 2010, the US legislator concluded that CRAs "play a critical 'gatekeeper' role in the debt market that is functionally similar to that of securities analysts, who evaluate the quality of securities in the equity market, and auditors, who review the financial statements of firms. Such role justifies a similar level

21 Supra 2.1.1. on rating triggers.
22 ESG, p. 173 on the origins.
23 Partnoy (n 3), p. 82.

of public oversight and accountability" (s 931(2) Dodd-Frank Act 2010, United States of America).[24]

2.2 Regulation of CRAs

2.2.1 Failures of CRAs

The experiences with failures of CRAs vary across countries, as do regulatory responses.[25] It seems that the credit ratings relating to bonds have generally been reliable. However, CRAs have a history of failures similar to other gatekeepers such as auditors.[26] Rating errors have been observed in a number of unexpected corporate breakdowns, such as the major collapse of ENRON in the United States of America in 2001, or of Parmalat in Italy in 2003.[27] In both cases the issuers' securities enjoyed extremely positive ratings until the day before their respective defaults.

The global financial market crisis of 2008 marked the turning point in the discussion about the need for regulation of credit ratings. The crisis had already become apparent in 2007. However, it is usually dated back to the collapse of the investment bank Lehman Bros. in the fall of 2008, which led to the escalation of the crisis. Unlike the corporate collapses of Enron and others at the beginning of the new millennium, the global financial crisis was caused by systematic weaknesses in banking and financial market regulation. These weaknesses included overreliance on ratings, the synchronization of ratings-based decisions and the downward spirals caused by this.[28]

The main failure of CRAs was seen in the late adjustment of ratings. In connection with the global financial market crisis of 2008, serious errors were made in credit ratings relating to structured financial products, namely of residential mortgage-backed securities (RMBS). The CRAs assigned highest rating grades to the (multiple) securitizations (collateralized debt obligations, CDO, CDO2, CDO3, etc.). They did not adequately consider the fact that securitization only diversifies the individual default risks of the mortgage debtors, but not the risks arising from dependence on real estate prices and interest rate

24 Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111–203, 124 Stat. 1376 (2010).

25 United States of America, p. 625, for a detailed report.

26 Coffee (n 1), pp. 15 et seq.

27 Healy/Palepu, 17 J. Econ. Persp. 3 (2004/2) on Enron; Carrara, RabelsZ 70 (2006), 538 on Parmalat.

28 Supra section 2.1.1 on downward spirals (cascade effects).

developments, which affect all receivables equally. The ratings were not corrected even when the impending market collapse became apparent.[29]

In the sovereign debt crisis of 2009, in contrast to previous developments, sovereign credit ratings were downgraded despite measures initiated by the European Union, which deprived these measures of some of their effect. The CRAs were heavily criticized, although, on a closer look, the only thing they did was to give their professional views on changes in the creditworthiness.

2.2.2 Over-Reliance on Credit Ratings

Today, there is general agreement that over-reliance on credit ratings contributed to the global financial crisis that escalated in 2008. The US Dodd-Frank Act of 2010 reacted, i.a., by prescribing a removal of statutory references to credit ratings. Similarly, the CRAR (EU) as amended in 2013 strengthened the internal risk assessment of institutional investors and banks. According to art 5a CRAR (EU), the relevant entitites shall make their own credit risk assessment and shall not solely or mechanistically rely on credit ratings for assessing the creditworthiness of an entity or financial instrument. The main goal was to avoid automatisms and downward spirals.[30] The amendment of 2013 also introduced the liability rule in art 35a CRAR (EU).

A decade later, it seems that the credit ratings provided by CRAs have not decreased in importance. Arguably, financial system stability still depends on credit ratings to a considerable extent and over-reliance hence remains a problem.

However, credit ratings became a regulated activity in many parts of the world. Today, it is accepted that credit ratings must be drafted on the basis of diligence standards. The IOSCO Code of Conduct Fundamentals, first published in 2004 and last updated in 2015, reflects internationally accepted rating practices. In many countries, CRAs must be registered. This means rating services may only be offered to the public if certain regulatory requirements are fulfilled.

2.2.3 Regulatory Framework for CRAs

In the United States of America, since 1973, a credit rating may only be used for regulatory purposes if it has been prepared by a Nationally Recognized

29 SEC, Summary Report of Issues Identified in the Commission Staff's Examinations of Select Credit Rating Agencies, July 2008, p. 12; Recital 10 CRAR (EU).

30 Recital 9 Reg (EU) No 462/2013 of the European Parliament and of the Council of 21 May 2013 amending Reg (EC) No 1060/2009 on credit rating agencies, OJ L 146, 31.5.2013.

Statistical Rating Organization (NRSRO requirement).[31] To receive recognition as NRSRO, a CRA must prove acceptance in the market, but market acceptance largely depends on recognition. It is reported that only four recognition procedures were successful between 1980 and 2000.[32] Arguably, the NRSRO requirement contributed to the present market concentration because it builds on the test of a whether the CRA is established in the market. It is obvious that non-recognized CRAs face difficulties in demonstrating that their credit ratings are relied upon by the market participants. Similar observations can be made in many other countries, e.g., in Singapore.[33]

In the United States of America, the Dodd-Frank Act imposed tighter conflicts of interest restrictions, due diligence requirements, and a duty to blow the whistle on lawbreaking. Last but not least, it subjected rating agencies to private liability exposure.[34] As a result of such measures, which may also be observed in other countries, rating agencies now appear to have a sort of hybrid status. They are private service providers, but at the same time they are involved in performing tasks in the public interest.

In the EU, the failures of CRAs prior and during the global financial market crisis of 2008 led to the Credit Rating Agencies Regulation of 2009; in short: CRAR (EU).[35] As a regulation, the CRAR (EU) is directly applicable in the European Member States[36] since regulations, unlike directives, do not need to be transposed into national law to become binding. The CRAR (EU) is a reaction to the observation that most credit rating agencies are headquartered outside the EU. Under art 4 para 1 subpara 1 CRAR (EU), a rating may only be used for regulatory purposes if it is issued or endorsed by a CRA that is registered within the EU in accordance with this regulation. According to art 15 para 1 and Annex II Nr. 1 CRAR (EU), registration requires that the CRA maintains an office within the EU.

Upon the enactment of this provision, the major CRAs decided to register within the EU and hence opened offices within the EU. The major CRAs, or more precisely, their European offshoots are hence subject to the liability rule of art 35a CRAR (EU).[37] Being directly applicable in 27 EU Member States, the CRAR is the biggest regulatory framework in the world. For this reason, its

31 United States of America, p. 628.

32 Hill, „Regulating the Rating Agencies", 82 Wash. U. L.Q. 43, 55 Fn. 61 (2004) on the developments.

33 Singapore, p. 489.

34 United States of America, p. 653.

35 Reg (EC) No 1060/2009 of 16. September 2009 on credit rating agencies.

36 Art 288 para 2 Treaty on the Functioning of the European Union (TFEU).

37 European Union, p. 91.

details are set out, not only in the following country reports, but also in a report exclusively devoted to the regulation of CRAs in EU law.[38]

The regulation of CRAs is country-specific. In Australia, ratings are seen as investment advice.[39] Advisers need a different type of license depending on whether they advise retail investors. The major CRAs have chosen to be licensed only for providing advice to wholesale clients. The regulatory distinction is due to the unique architecture of the Australian wealth management sector. In Australia, financial products are often distributed through financial advisers that are not affiliated with issuing institutions.[40] As a result, the credit ratings of the major CRAs are not directed at the investor public. This has major consequences for the structure of duties and the eligibility of claimants which is seen to be restricted to the addressees of the ratings, i.e. to wholesale clients.

India was one of the first jurisdictions to establish a comprehensive regulatory framework for CRAs in the form of the SEBI (Credit Rating Agencies) Regulations.[41] This happened well before CRAs became subject to close regulatory scrutiny in markets such as the United States and the European Union. In many countries, the regulation of CRAs was strengthened only after the global financial market crisis of the years 2008 et seq. To give examples, the EU passed its CRAR (EU) in 2009[42] and the US introduced more stringent regulation with the Dodd-Frank Act of 2010.[43] Brazil, enacted regulation in 2012.[44]

While it appears to be commonly accepted that reliance on soft law and self-commitments falls short of achieving a meaningful regulation of CRAs, the manner and mode of regulation vary between jurisdictions. While the EU chose to open a new line of regulation, some countries tied the regulation of CRAs to existing regimes. For example, in Australia, credit ratings are regulated under the regime applicable to the provision of financial product advice.[45] In Türkiye, a dual regulatory system was adopted that subjects credit ratings of financial products and of financial institutions such as banks to the supervision of different supervisory authorities.[46] The regulation of credit rating services alone, it seems, is not a guarantee for the integrity of credit ratings. For example, in China, the development of a robust credit rating system is

38 European Union, p. 91.
39 Australia, p. 211.
40 Australia, p. 206.
41 India, p. 366.
42 European Union, p. 89.
43 United States of America, p. 625.
44 Brazil, p. 264.
45 Australia, p. 211.
46 Türkiye, p. 557.

generally considered a key component in advancing China's economy. Nevertheless, CRAs in China have been criticized for being susceptible to political bias and lack of independence[47] – a criticism that has already been voiced in other countries, however.

2.3 Civil Liability of CRAs

2.3.1 Negligence Liability for Pure Economic Loss

It is widely agreed that civil liability (private enforcement) can and should complement regulation and public law sanctions (public enforcement) to safeguard the integrity of credit ratings.[48] In the beginnings, commentators believed that reputational concerns would sufficiently discipline information intermediaries like external auditors and CRAs.[49] Only later did it become clear that the reputation mechanism is significantly more complex than initially assumed.[50] It is true that credit ratings strongly build on their reputation as a reliable source for determining the default risk. Reputation is built over time, it is a long-term asset. Long-term assets are not risked for short-term gains, the logic goes. However, this logic already changes when we factor in differences in the time horizons and risk willingness between private institutions such as CRAs and their individual employees such as rating analysts. While risking reputation might not make sense for the institution, it might be a fully rational choice for the individual, even more so if the short-term profit is needed to gain a bonus payment or safeguard the position. Experiences with the failures of information intermediaries in corporate scandals like ENRON or in the global financial market crises have shown that reputation alone does not sufficiently deter wrongdoing.

The role of civil liabilities of CRAs differs (strongly) between countries although it appears to be commonly agreed that civil liability can have a supplementary function to public regulation, oversight and sanctioning power. The majority of jurisdictions, however, relies on public enforcement by a financial authority instead of private enforcement be injured investors.

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47 China, p. 280.

48 Cross-border Disputes, p. 133. Cf. further Picciau, "The Evolution of the Liability of Credit Rating Agencies in the United States and in the European Union: Regulation after the Crisis" (2018) 15 *European Company and Financial Law Review* 339, 356–401.

49 Goldberg, "Accountable Accountants: Is Third-Party Liability Necessary?", 17 J. Legal Stud. 295, 303 (1988) arguing that the reputational costs that accountants may face from failing to detect wrongdoing provide them with adequate incentives to monitor their clients.

50 Shapira, Law and Reputation, 2020, pp. 19 et seq.

Civil liabilities (as well as public sanctions) must strike a balance between under-deterrence and over-deterrence of CRAs. Under-deterrence could increase the number of imprudent ratings and lead to a loss of confidence in financial markets. Conversely, over-deterrence could lead to over-cautious credit ratings (defensive ratings) or to a decrease of publicly available credit ratings (chilling effect). This would result in an increase in information costs and possibly reduce the number of private transactions, and ultimately cause a loss of private welfare.

There is no doubt that CRAs, like any other party to an agreement, should be liable for a breach of contract. However, contractual liability to the issuer that solicited the rating only helps to align the interests of the CRA with those of the issuer. This does not necessarily ensure the integrity of the rating. The duty to safeguard the issuer's interests rather creates a misplaced tendency to provide overly positive evaluations. In sum, contractual liabilities to the issuer fall short of protecting the interests of the investor public and induce overoptimism and one-sided ratings in the interest of the issuer.

It is also clear that a CRA will be liable to third parties for intentional misconduct, but this will only apply to the most flagrant cases of misconduct. The pressing policy question is whether CRAs should be liable for (gross) negligence in cases of pure economic loss. The legislator is free to set up a liability rule in such cases. In fact, many countries have adopted negligence liability for pure economic loss by auditors.[51] Regarding CRAs, France pioneered with a specific liability rule in 2010.[52] The EU followed with art 35a CRAR (EU) in an amendment to the existing regulation of 2013.[53]

Absent a specific liability rule, pure economic loss is only compensable within a contractual relationship in most jurisdictions. Some jurisdictions recognize a category of a comparable special legal relationship (quasi-contractual liability).[54] The relevant legal concepts that deal with this issue, i.a., ask whether there was a duty of care towards the plaintiff (proximity; interest in the inclusion of a third party into the contract), or whether it was reasonable for the plaintiff to rely on the credit rating (reasonable reliance).

51 E.g., Netherlands, p. 445; Spain, p. 533 Cf. also s 323 para 1 sentence 3 Handelsgesetzbuch (German Commercial Code).

52 France, p. 315.

53 Reg (EU) No 462/2013 of the European Parliament and of the Council of 21 May 2013 amending Reg (EC) No 1060/2009 on credit rating agencies, OJ L 146, 31.5.2013, p. 1.

54 E.g., Austria, p. 238.; Spain 3.14.–6.4.

The dogmatic concepts differ in civil law and common law. Attempts to formulate specialized liability rules, as far as is known, take a rather pragmatic starting point. Each of these concepts serves to filter out cases in which holding CRAs liable would be disproportionate. Perceptions as to the reasonable extent of liability, be it civil or public, have changed over the past one or two decades. The turning point appears to be the shift in perception of what a credit rating is. Earlier, credit ratings were seen as an expression of free opinion, like statements in a newspaper, or free speech, like a political view in a TV show. Emerging regulation transformed this perception into a view of credit ratings as professional statements that must be formed according to professional standards.

The duty standards of professionals are higher than those of non-professionals.[55] Professional negligence concerns a failure to comply with the diligence standards of the relevant profession or with sector standards. There is a vast body of case law concerning liabilities of auditors, attorneys, financial advisers and other professional service providers. The view that CRAs should be subject to similarly high professional duty standards is relatively new.[56] In the jurisdictions considered in this volume, there is no clearly defined concept of professional liabilities. Rather, the term refers to courts adopting techniques to account for the clients' trust in professional advisers. As far as known, professional liabilities are fault-based. The highest standards apply to professionals that perform a statutory function, e.g., statutory auditors.

Some have argued in favor of subjecting CRAs to strict liability to account for their gatekeeper role.[57] In France, strict liability was considered but ultimately rejected.[58] Strict liability would expose CRAs to even higher liability risks than statutory auditors. As far as is known, no jurisdiction has adopted this approach.

2.3.2 Limits of Civil Liability (Private vs. Public Enforcement)

The degree to that civil liability (private enforcement) serves to complement regulation and public law sanctions (public enforcement) essentially depends on the chances to succeed in the courtroom from the ex-ante view of the

55 E.g., Austria, p. 238.; Italy, p. 419; Netherlands, p. 446.

56 E.g., Netherlands, p. 446.

57 Pacces/Romano, "A Strict Liability Regime for Rating Agencies", 52 Am. Bus. L.J. 673 (2015); Partnoy (n 4), p. 540 ff.; Kraakman (n 6) on the foundations.

58 France, p. 315.

injuree. The very small body of case law suggests that the motivation of injurees to act as plaintiffs is rather low. The remainder of this report (sections 3 et seq) is devoted to show in which cases there are, at least, some chances to succeed in court, or, conversely, which legal filters serve to prevent CRAs from liabilities.

Generally, the view prevails that civil liability could not replace regulation and public sanctions. This is because private plaintiffs will mostly lack the necessary information to plead and prove the relevant misconduct. So far, the available experience is mainly with public sanctions. As opposed to private plaintiffs, supervisory authorities make use of investigation powers. Naturally, the question arises whether private plaintiffs could rely on the findings of supervisory authorities to back up a private law suit (infra section 7.3.).

The most prominent example that involved a remarkable sanction is of a hybrid nature as it combined litigation with authoritative investigation powers. In 2013, the US-American Federal Department of Justice filed a law suit against Standard & Poor's, later also against Moody's.[59] These suits led to billion-dollar settlements. The suits were based on the rather infrequently applied anti-fraud provision of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). The FIRREA legislation grants the US Department of Justice extraordinary pre-suit civil discovery powers, to directly subpoena documents, and to take depositions for a civil investigation of fraud. Clearly, the threat of potentially large liabilities helps to induce defendants to settlements.

The US experience in the FIRREA cases reveals a notorious problem of CRAs' civil liabilities: In many countries, sanctions have been imposed (in some instances) for breaches of regulatory duties of CRAs. In contrast, only a few courts have tested what potentially constitutes a misconduct that leads to civil liability.[60]

From the viewpoint of the CRAs, cases with a certain probability of liability, be it public or private, are preferably settled out of court. Court decisions pose a long-term threat. Precedents increase liability exposure while settlements appear in law reports only in few jurisdictions, e.g., in Australia.[61] For most jurisdictions, it is part of the logic of a settlement to be confidential, i.e. to avoid any clarification of the duty standard. It seems that the rating industry has managed for long to uphold the impression that CRAs are judgement-proof defendants. The purpose of the present study accordingly includes identifying

59 United States of America, p. 644.
60 United States of America, p. 644.
61 Australia, p. 208.

liability dangers which a CRA might consider sufficiently severe to agree to a settlement (infra section 5.3.).

It should be clear, however, that some problems cannot be solved as effectively by civil liability. To give one often cited example: In the aftermath of the Residential Mortgage-Backed Securities (RMBS) crisis, the New York Attorney General Andrew Cuomo reached an agreement with the three leading CRAs in 2008. Under the Cuomo Settlement, the CRAs agreed to fostered independence standards and enhanced transparency for a term of three years. The settlement included, i.a., a fee-for-service structure that required compensation regardless of whether the investment bank ultimately selected the CRA to rate a RMBS, as well as the disclosure of due diligence information by investment banks. These measures were intended to prevent a race to the bottom in rating quality. There had been signs of overoptimistic preliminary assessments and rating shopping by investment banks. While the Cuomo Settlement was also criticized, in particular its fee-for-service structure is considered an innovative measure whose effect could not have been achieved to a comparable extent through civil liability.

In most countries, the emphasis has been on public enforcement. Only few countries collected experience with civil law actions against CRAs. There is no clear division between common law and civil law as is shown by the case law examples from the US and Australia on the one hand and from Germany on the other hand (infra section 3.2.). India is an example for a more or less exclusive reliance on public enforcement which, however, is not rating-specific but rather resembles a general approach to capital market regulation.[62] This approach targets issuers and their gatekeepers, including CRAs. It is aimed much less, if at all, at compensating investors for losses.

One of the most important differences between public and private sanctions relates to damage causation.[63] To illustrate, art 36, 36a CRAR (EU) provide for sanctions and penalties in case of a breach of regulatory duties while a compensation claim based on art 35a CRAR (EU) would require proof of damage causation. In some countries, including Australia, the penalties for a breach of the statutory standards have recently been increased significantly.[64] A similar trend can be observed in Brazil.[65]

62 India, p. 379.
63 Spain, p. 526.
64 Australia, p. 210.
65 Brazil, p. 270.

2.3.3 Overview of CRA's Liabilities to Issuers and to Investors

The following overview shows the possible parties to and claims of civil liability.

CRA defendant	**Issuer** plaintiff	**Investor** plaintiff
Solicited issue/issuer credit rating (rating contract with issuer or investor subscription) **Unsolicited issue/issuer credit rating** (CRA provides credit rating at own cost)	Injunction/withdrawal[a] or damages for loss, e.g., due to higher capital costs	Reversal of transaction,[b] or damages for excessive purchase price

a Injunction not to publish a rating or withdrawal of an existing rating.

b 'Reversal of the transaction' describes a claim in which a plaintiff seeks to be put back into the position s/he would have been in had s/he not invested into the securities. The defendant would pay the plaintiff the original purchase price. Tlaintiff would hand-over the securities to the defendant in turn. This is rathher theoretical though as the securities will often be worthless due to the default of the issuer.

2.4 Cross-Border Litigation, Jurisdiction and Applicable Law

2.4.1 Localization of Pure Economic Loss

Capital market related information is often produced abroad and it crosses borders. A faulty rating produced in state 1 might be considered by investors in states 2, 3, 4 etc.[66] To hold a credit rating agency liable for a faulty rating, the claimant must file suit at a court that has jurisdiction and that applies a law which provides a basis for the claim. Jurisdiction and applicable law are determined according to laws that differ between countries. There are some commonalities but there is no universally applicable set of rules or principles.

It is apparent that the most difficult problem concerns a claim of a third-party investor, i.e. of an investor who has not solicited the rating. A third-party investor will have to base the claim on non-contractual liability, including, in some countries, quasi-contractual liability. The claim will be for compensation of pure economic loss, and, hence, raise the notoriously difficult problem of

66 Cross-border Disputes, p. 134 et seqq, on the following.

the localization of pure economic loss. The specific challenges of capital market information liabilities are part of a larger debate that goes beyond what is discussed in this volume on credit rating agencies' liabilities. The current state of the debate will be explained in more detail in report 2.2. For the purpose of the present general report, the following short notes on jurisdiction and applicable law must suffice (sections 2.4.2 et seq).

One preliminary remark appears justified, however: The era of judgment-proof CRAs might be over. It appears that the major underpinnings for court abstention are much weaker today than they were before. It is not entirely clear how a court hearing a case will address issues of jurisdiction and applicable law. For a court in an EU Member State, the adoption of a rating-specific liability provision in the European Union in art 35a CRAR, however, clearly shows that legislature expects the courts to deal with liability cases.

2.4.2 Jurisdiction

It is generally recognized that courts at the seat of the CRA have jurisdiction. For example, according to art 4(1) Brussels Ia Regulation[67] a EU-based CRA can be sued in the courts of the Member State where it has its 'domicile' within the meaning of art 63 Brussels Ia Regulation. This concerns actions against the EU-based subsidiaries of the big three and against the (smaller) European agencies, such as ARC Ratings (Portugal), Euler Hermes Rating (Germany), Scope Ratings (Germany), Spread Research (France).[68]

According to art 7(2) Brussels Ia, the place of damage determines international jurisdiction. This leads to the notoriously difficult question of how to determine the place of damage in situations where the damage is purely financial. Some have advocated a market-based approach which locates the loss at the place of the transaction or where the financial instrument is admitted to trading. The discussion is ongoing.[69]

In light of the reluctance of US-American courts to hold CRAs liable towards third-party investors, the major question is whether an investor can sue one of the big three CRAs in a foreign court. The Brussels Ia Regulation does not provide for international jurisdiction since the defendant is not domiciled in an EU Member State. Within and outside the EU, international jurisdiction is

67 Reg (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (recast), OJ L 351, 20.12.2012, p. 1.

68 Cross-border Disputes, p. 137.

69 Cross-border Disputes, p. 146.

hence decided by national law. However, even if a foreign court would assume competence to hear the dispute it appears doubtful whether a US court would recognize and enforce a foreign judgment which orders a US-based CRA to pay damages to a foreign investor.

2.4.3 Applicable Law

Once the court has assumed jurisdiction it must decide which substantive law to apply. In a case involving third-party investor claims, a court will probably begin by stating that a choice-of-law agreement contained in the rating contract between the CRA and the issuer or another party does not have effect on the rights of third-party investors who are not privy to that agreement. In the EU, this follows from art 3(2) second sentence Rome I Regulation and art 14(1) second sentence Rome II Regulation.[70] The determination of the law governing non-contractual claims of investors against CRAs for faulty credit ratings is an unsettled issue, very much like the question of international jurisdiction.[71] The discussion revolves around the localization of purely financial damage under art 4(1) Rome II-Regulation. Based on the already mentioned market-based approach, the loss might be located at the place of the transaction or where the financial instrument is admitted to trading.[72] However, it has been argued that the law of the (registered) seat of the rating agency has the closer connection and therefore takes priority under art 4(3) Rome II-Regulation. This would lead to the application of US law which, at least in the past, has tended to be favorable to CRAs. The discussion is ongoing.

3 Case Law Overview

3.1 Overview: Scarce Case Law

The frequency of legal action, especially private damage suits, against CRAs varies greatly between countries. Generally, case law on civil liability is rare. If a case finds its way into the courtroom, it is often settled privately. For many common law and civil law countries, no case law has been reported, e.g., in Singapore, the United Kingdom, Portugal, and Türkiye. In some countries, credit ratings have been subject to civil liability litigation, however, without

70 Reg (EC) No 864/2007 of the European Parliament and of the Council of 11 July 2007 on the law applicable to non-contractual obligations (Rome II), OJ L 199, 31.7.2007, p. 40.

71 Cross-border Disputes, p. 154.

72 Cross-border Disputes, p. 164.

ultimately leading to liability, e.g., in Brazil, Japan, Italy, Israel. Only in few countries, CRAs have been held liable to investors or issuers, e.g., in Australia, China, Germany, and the United States of America.

This brief sketch already shows that the differences cannot be easily explained by macro factors such as the state of development of a capital market, or a divide between legal families, and, in particular, not by a divide between common law and civil law. The motivation of possible claimants to file a law suit was understandably low in the past. CRAs have literally been immune to civil liability.[73] This is true especially for the United States of America due to the widespread perception that ratings are merely an expression of opinion. Opinions are protected by constitutions, in the United States of America, under the so called first amendment defense. The first amendment defense is still accepted by courts of some Federal States in the United States of America but following the global financial crisis, courts of other Federal States have rejected this defense.[74] Today, the position is far less clear than it was two decades ago. The trend appears to be to see credit ratings as professional statements which benefit from protection under the constitutional freedom of opinion to a much lower extent. Nowadays, it would be short-sighted by a CRA to believe that it is fully protected against liabilities.

3.2 Credit Ratings as Professional Statements (Limits to Freedom of Opinion)

Judicial support for the view that credit ratings are free speech can also be found outside the United States of America.[75] However, in many countries, this does not mean that the action is dismissed, but it affects the duty standard. A court in Japan emphasized the investor's own duties with regard to informed decision-making and also mentioned the nature of a credit rating as a statement of the CRA's opinion. Nevertheless, it found that the CRA was under a good faith duty to make credit ratings sincerely and fairly.[76]

An Italian court denied liability of the CRA but made clear that standards of professional negligence apply, i.e., CRAs must comply with the principles of professional diligence and sector standards as set out in financial regulation.[77]

73 Supra section 1.

74 United States of America, p. 644 on Abu Dhabi Commercial Bank v. Morgan Stanley & Co., 651 F. Supp. 2d 155, 176 (S.D.N.Y. 2009): First Amendment defense for ratings of structured finance products denied, because the product was only targeted to a small pool of investors.

75 Japan, p. 435.

76 Japan, p. 435, on Nagoya High Court, 2005WLJPCA06299005, 29 June 2005.

77 Italy, p. 419, on The Tribunal of Catanzaro (Tribunale di Catanzaro, 2/03/2012 n. 685).

Already in 2006, a German court held that the tort law duties of CRAs follow a standard that has been developed in a series of decisions on the publication of (comparative) commodity and/or performance tests and rankings.[78] Such tests relate to household appliances. From the viewpoint of a consumer a high ranking of the tested appliance is a recommended purchase, a ranking as average can be compensated by a lower price, but a low ranking will often mean that consumers do not buy the product. The parallels to credit ratings are apparent. The application of the duty standard for performance tests and rankings to credit ratings means that the rating must be neutral, diligent and be made in an effort to be objectively correct.

Similarly, courts in the Netherlands have argued that providers of credit scores must adhere to professional standards, i.e., they have the obligation to act with due care, expertise and competence.[79]

3.3 Liability for Negligence in the Primary Market

Court holdings that assume liability for negligent misrepresentation are clearly an exception. In China, many cases were dismissed prior to 2022 due to the requirement of administrative or criminal penalties which was eliminated only in 2022.[80] In one case decided in 2020, the CRA Dagong was held liable for a faulty credit rating of a bond issue on the basis of the Chinese specialized CRAs' liability regime but it is unclear whether the court assumed intent or recklessness.[81]

The Australian ABN AMRO (Bathurst) case of 2014,[82] so far, is the most prominent example for liability based on negligent misrepresentation, in that case by Standard & Poor's. Similar to the US-American Abu Dhabi case against Standard & Poor's and Moody's of 2009,[83] however, the case concerned a bond issue that was targeted at a defined (small) group or class of investors. It is

78 Germany, p. 343; KG Berlin 12.5.2006, VuR 2006, 484 – Scope Rating. See also Leyens (n 1), pp 364, 451, 478.

79 Netherlands, p. 442; cf. also Verheij (n 2), p. 224. District Court Rotterdam 29 December 2010, ECLI:NL:RBROT:2010:BP5369 (*Vitesse*); District Court Amsterdam 14 January 2015, ECLI:NL:RBAMS:2015:6 (*Graydon*).

80 China, p. 299 (Misrepresentation Provisions 2022).

81 China, p. 299, on Wang Fang v. Wuyang Construction Group and Chen Zhizhang & Debang Securities Company (2020) Zhe 01 Minchu No. 1691.

82 Australia, p. 208 ABN AMRO Bank NV v Bathurst Regional Council [2014] FCAFC 65; (2014) 224 FCR 1.

83 United States of America, p. 644. Abu Dhabi Commercial Bank v. Morgan Stanley & Co., 651 F. Supp. 2d 155, 176 (S.D.N.Y. 2009).

characteristic for those cases that they concern the purchase of a new issue (primary market) by a group of investors that could, at least theoretically, be identified (identifiable group of investors).

Remarkably, a German district court even found simple negligence to be sufficient (MS Deutschland).[84] Unsurprisingly, the parties settled privately and the Court of Appeal did not have a chance to affirm. The district court based its judgement on quasi-contractual liability concepts which are known in a number of civil law jurisdictions, namely special trust into presentations of a third party and the concept of a contract which unfolds protective effect towards a third party.

The case concerned the German CRA Scope Ratings, one of the biggest CRAs in Europe, though considerably smaller than the big three. The CRA had rated a bond issue secured solely by one (used) cruise ship. The CRA had initially provided the issue with a positive rating which helped to sell the bonds but then, rather quickly, published downgrades. The CRA rating report clearly stated that the rating analysis and grade were based on the auditor's report. This means the CRA openly explained that its assessment was based on a limited source of information. The said auditor report, however, contained rather unrealistic assumptions of the value of the cruise ship which it measured against book value leaving out of consideration that the market value at the time of a possible default would be presumably much lower. It should be noted that a diligent CRA could not have overlooked this.

In Israel, there are two cases which both were decided on the basis of general civil law, not on the Israeli CRA Act which came into force later.[85] The first case is Lavi v. Midroog which was decided by the Israeli Supreme Court in 2018 following a judgment of the specialized business court. The CRA Midroog, controlled by Moody's, was sued for not sufficiently differentiating between different types of bonds and their backing by distinct types of securities and collaterals in an initial credit rating that the CRA later corrected. The class-action was based on the allegation of negligence, breach of contract (toward third parties) and of statutory duty, and a violation of securities laws (misleading item). The claim was dismissed. Still, it brought forth two informative holdings. Firstly, a CRA owes a duty of care to investors and bondholders who rely on the CRAs' ratings. Secondly, however, liability will be imposed on CRAs

84 Germany, p. 354 on LG Berlin, Urteil vom 5.5.2020 – 11 O 5/19 (MS Deutschland), WM 2021, 444. For details cf. Leyens, in BeckOK Wertpapierhandelsrecht, 17th ed, Munich 2022, art 35a VO (EU) 1060/2009 para 101, 115, 123.

85 Israel, p. 396.

only under extreme circumstances (equivalent to gross negligence) in order to avoid a chilling effect.

The second case in Israel is Monrov v. Midroog which was also decided in 2019 by Israel's specialized business court.[86] The case concerned a favorable credit rating issued by Midroog that was included into a prospectus, i.e., a primary market constellation. Shortly after the issuer had to publish a financial restatement the bonds dropped by 53% and the issuer went bankrupt. The claim was dismissed. The court found that the relevant information was either new, or not accessible to the CRA at the time of its original rating. It also found that a CRA may, generally, rely on the audited financial reporting of the issuer. The judgements hence clarified the role of a CRA against the background of its interaction with other intermediaries: CRAs do not need to independently investigate and extract additional inside information on the rated entity. A diligent rating assessment can be based upon the report of the statutory auditor.

There was one case in Brazil but the plaintiff failed to prove causality or that the defendants acted with intent or fault by not detecting, in a timely manner, the issuer's mismanagement.[87] Similarly, in Italy an obiter dictum shows a certain liability danger but also highlights the high hurdles to prove causality.[88] In sum, the case law is not very developed.

3.4 Issuers' Rights to Injunctive Relief

The issuers' rights to injunctive relief against faulty ratings have not formed a major discussion focus. In China, a court granted injunctive relief (and a compensation payment) to an issuer that had been falsely accused by the CRA Dagong of poor disclosure and risk control capabilities, suspected related-party transactions, and inability of debtors' repayment.[89]

An Indian court had to decide whether an issuer has a right of permanent injunction restraining the CRA from making any alteration in the credit rating of the applicant, hence to to prevent a downgrading.[90] The claim was dismissed as a CRA is bound by existing regulations, including the code of conduct issued by the financial market SEBI, but an injunction of the claimed kind

86 Israel, p. 396.

87 Brazil, p. 275 on TJSP, Appeal (*Apelação*) No. 0103970-75.2007.8.26.0000, Des. R. Lino Machado, Câmara Reservada à Falência e Recuperação, ruled on 12.13.2011.

88 Italy, p. 421 on Tribunale di Roma, 27/03/2015 n. 6827.

89 China, p. 284 on Dagong Global Credit Rating Group v. Beijing Dolphin Network Company (2016) Jing 02 minxia zhong No. 354.

90 India, p. 380, on First Leasing Company of India Ltd. v. ICRA Ltd, 2000 SCC OnLine Mad 1051.

would cause irreparable harm to the CRA and be unfair as long as the CRA has acted in good faith and reasonably.

4 Legal Basis of Liabilities

4.1 Overview

The legal basis of a damage claim of an injuree who has solicited the rating is the rating contract. A claim based on contract provides the claimant with certain advantages in many countries. Inter alia there might be a rebuttable presumption of fault, e.g., in Germany.[91]

The laws of the countries considered differ with regard to the legal basis of CRAs' liabilities towards an injuree who has not solicited the rating. Broadly, four categories can be distinguished: Firstly, a specialized liability regime may exist. The adoption of such specialized liability regimes, usually as a part of securities regulation, is a relatively new phenomenon, e.g., art 35a CRAR (EU) as amended 2013. Arguably, the existence of a specialized liability regime can have indirect implications on the scope of general contract or tort law claims and de facto lower liability dangers, e.g., in the United Kingdom.[92]

Secondly, in some countries the liability rules under securities regulation might provide for several pathways of liability claims, e.g., in Australia, and in the United States of America.[93] In some countries, general corporate law contains remedies that supplement those of securities regulation and that are relevant for CRAs' liabilities, e.g., in Australia.[94] Interestingly, art 63 CML No. 6362 of the Turkish Capital Market Law applies to both auditors and CRAs.[95] In other countries, where no such specialized liability provision exists, courts have not yet seriously considered drawing an analogy to the specialized rules applicable to the liability of statutory auditors.

Thirdly, in all countries considered, contract law and tort law provide a liability basis. Contractual claims in a strict sense, of course, are only available to an injured party who has contractually solicited the rating. Investors who have not solicited the rating might be entitled to damages on a quasi-contractual basis that will be treated below. In all countries considered, the existence of

91 S 280 para 1 sentence 2 German Civil Code.
92 United Kingdom, p. 596.
93 Australia, p. 216.; United States of America, p. 647.
94 Australia, p. 216, especially p. 218, p. 220.
95 Türkiye, p. 516.

specialized liability regimes, either for CRAs in particular or more generally for securities regulation, does not preclude claims based on general contract law and tort law. Further, there are no reports of an exclusion of general tort law liability by liability for misleading information or unfair commercial practices and in some countries, it appears advisable to use general tort law instead as such a claim offers the most leeway in bringing forward the relevant arguments, e.g., in the Netherlands.[96]

It appears that most countries allow claimants to plead all possible contractual, quasi-contractual, or tortious liabilities, e.g., in Australia, Brazil, the Netherlands, and Singapore.[97] In some countries, a non-cumul principle precludes the claimant from combining contractual (or quasi-contractual) remedies with a claim on a non-contractual basis, e.g., in France, and Spain.[98] With regard to compensation claims by injured investors, courts have heard cases based on negligent misrepresentation, which according to the law of some countries may provide a tort law claim for pure economic loss, e.g., in Australia, Singapore, the United Kingdom, and the United States of America.[99]

Fourthly, some countries recognize an intermediate basis between contract and tort. The so-called quasi-contractual liabilities generally serve to fill gaps that result from the fact that tort law does not adequately protect against pure economic loss. Despite all differences, it appears that the factors to be considered are similar to those factors that would, in other countries, constitute a claim based on negligent misrepresentation (supra). One possible basis of quasi-contractual liability is a protective effect of the rating contract for third parties, e.g., Germany, and Portugal.[100] Another basis would be that the expert has evoked special trust in her opinion, e.g., in Austria, Germany, Israel, Portugal, Türkiye.[101] Courts do not necessarily draw a clear line between these bases, e.g., in Germany.[102]

Lastly, remedies are only as good as their operation in practice. In India, e.g., there is apparently a tort law deficit, which is attributed, i.a., to steep litigation costs, including high attorney fees, long duration of first instance proceedings

96 Netherlands, p. 445.

97 Australia, p. 316; Brazil, p. 267; Netherlands, p. 445.; Singapore, p. 494.

98 France, p. 315.; Spain, p. 522.

99 Australia, p. 216; Singapore, p. 498.; United Kingdom, p. 596 and 601.; United States of America, p. 652.

100 Germany, p. 334; Portugal, p. 467. For further details regarding Germany cf. Leyens (n 84), para 123 et seqq.

101 Austria, p. 238.; Germany, p. 334; Israel, 398; Portugal, p. 467.; Türkiye, p. 564.

102 Cf. already supra 3.3.

and appeals, low awards of damages, and poor enforcement of judgments, together with a culture of wariness of lower civil courts.[103]

4.2 Specialised Liability Rules for CRAs

Specialized rules for the liability of CRAs can be found in EU law, in China, and in Türkiye. The EU introduced its specialized liability regime in 2013 with a new art 35a CRAR, i.e., as an amendment to the regulation that had already existed since 2009.[104] The United Kingdom maintains a corresponding regime as so-called assimilated law with The Credit Rating Agency (Civil Liability) Regulations 2013.[105] Issuers and investors are equally entitled to base a claim on art 35a CRAR. The CRA incurs liability if it can be proven that it committed, intentionally or with gross negligence, any of the infringements listed in Annex III of the CRAR. In EU law, a regulation unfolds a binding effect in all Member States.

However, art 35a CRAR (EU) abstains from full harmonization in that it leaves central elements of liability to the national law applicable according to private international law (hybrid basis of liability). These elements concern 'damage', 'intention', 'gross negligence', 'reasonably relied', 'due care', 'impact', 'reasonable' and 'proportionate'. The approaches of national law to these elements will be discussed in the remainder of this report.

Moreover, the provision does not provide for any real facilitation of evidence. Rather, it is left to the national court to take "into consideration that the investor or issuer may not have access to information which is purely within the sphere of the credit rating agency." So far, the provision has not resulted in any liability and it seems that it did not increase liability risks for CRAs.[106]

The Chinese Securities Law 2019 is another example of a specialized liability rule.[107] The approach taken by Chinese law is more comprehensive than that of the EU because it includes CRAs and other information intermediaries such as auditors. These experts, including CRAs, shall act with due care and diligence, and, in particular, examine and verify the truthfulness, accuracy and completeness of the contents of the documents and the information the credit rating will be based on. In case of inaccuracy and loss caused to other persons, the agency shall bear several and joint liabilities together with the entrusting

103 India, p. 378.
104 European Union, p. 89; cf. also supra 2.3.1.
105 United Kingdom, p. 589.
106 European Union, p. 91.
107 China, p. 289.

party, unless the institution could prove that it is not at fault (art 163 Securities Law).

4.3 Capital Market Law and Corporate Law (Liabilities for False or Misleading Capital Market Information)

4.3.1 Prospectus Liabilities (Primary Markets)

Generally, specialized regimes of liabilities for capital market information distinguish between information that accompanies an issue of securities (primary market prospectus liability) and information that concerns matters which are relevant for subsequent trading (secondary market liabilities for breaches of continuing disclosure duties). Prospectus liability appears to be attractive for claimants because it might come with the benefit of a judicial assumption of individual reliance on the prospectus and/or other relaxations of the liability elements otherwise required under general tort law. Clearly, the issuer is responsible for the accurateness of the information provided in a prospectus. Experts such as statutory auditors, and perhaps also CRAs, may assume legal responsibility for the accurateness of their assessments, if included into a prospectus, e.g., according to the EU prospectus regulation.[108]

The approaches taken differ strongly. In Australia, the ratings of the big three cannot be included in a prospectus or a product disclosure statement for a retail offer because those CRAs have a wholesale-clients-only license.[109]

Only in a few countries, prospectus liability appears to be a real liability risk for CRAs. For example, in the Israeli Monrov v. Midroog case, a CRA was sued on the basis of prospectus liability and the claim was only dismissed because the court was not convinced that the CRA had acted negligently.[110]

In the United States of America, the Dodd-Frank Act 2010 tried to increase responsibility of CRAs for registration documents.[111] It repealed Rule 436(g) Securities Act 1933, which had exempted the credit ratings of recognized CRAs (NRSROs) from being considered part of a registration statement. Before Dodd-Frank, a credit rating could be included into the registration documents without creating an increase of liability risks for CRAs. After the repeal of the

108 Art 11 para 2 Reg (EU) 2017/1129 of the European Parliament and of the Council of 14 June 2017 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Directive 2003/71/EC, OJ L 168, 30.6.2017, p. 12.

109 Australia, p. 206, 214; infra 2.2.3 for details.

110 Israel, p. 396.

111 United States of America, p. 648.

exemption, a CRA faces liability for material misstatements or omissions relating to its rating pursuant to Section 11 Securities Act 1933. CRAs have since refused to give their consent to the inclusion of ratings in issuer registration documents. The SEC suspended this part of the legislation, first for six months and then for the indefinite future. The reform is said to have missed its goal.

In India, like in some other countries, a CRA can be classified as expert for the purposes of prospectus liability, but it is not very likely that a rating will be regarded as a statement of fact.[112] In Germany, the prospectus liability of experts depends on whether they have (explicitly) accepted responsibility for the prospectus.[113] In many countries, experts may be liable according to general civil law.

4.3.2 Other Capital Market Information Liabilities (Secondary Markets)

Specialized liability rules for secondary market information can only be found in few countries. The best-known example is the US-American liability under "rule 10b-5". A CRA could, in principle, be held liable under this rule but it is difficult to prove intent to commit fraud, knowledge, or recklessness with particularity.[114]

Historically, the provision was toothless in practice due to its high pleading standard. The lowering of the pleading standard by the Dodd-Frank Act 2010 unburdened plaintiffs who then needed only to allege particular facts that create a strong inference that the CRA knowingly or recklessly failed to conduct reasonable investigation of the factual elements underpinning the portfolios. Several shortcomings of the pleading changes have been reported. As a side effect, the changes created a safe harbor from antifraud liability if rating agencies engage in due diligence, such as by obtaining reasonable verification of the information from independent third parties. Other shortcomings relate to the narrow focus on due diligence only. However, private parties will rarely uncover facts from which one can strongly infer the absence of a reasonable investigation.

In most of the other countries considered in this study, there is no specialized liability rule for misrepresentations on secondary markets. In Germany, however, liability dangers arise in case of false or misleading ad hoc disclosure by issuers as a complement to the insider trading prohibition.[115]

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112 India, p. 375.

113 S 9 para 1 sentence 1 no. 1 Securities Prospectus Act (Wertpapierprospektgesetz). Cf. Schwark/Zimmer/Heidelbach, Wertpapierprospektgesetz, 5. Aufl. 2020, WpPG § 8 Rn. 11.

114 United States of America, p. 649.

115 SS 97, 98 German Securities Trading Act (Wertpapierhandelsgesetz).

4.4 Contractual and Quasi-Contractual Negligence Liability (Civil Law)

4.4.1 Concepts of Quasi-Contractual Liabilities

Contractual liabilities concern the relationship between the CRA and its client. Accordingly, contractual liabilities will normally occur towards the issuer that solicited the rating. In a smaller amount of cases, this might involve an investor who has solicited the rating and the liability might be towards the investor. The legal basis for liabilities towards third parties, i.e., to investors or issuers that did not solicit the rating will generally be tort law.[116] Some jurisdictions, however, recognize a category of liabilities that stands between contract and tort. Due to its hybrid nature, this category has been termed quasi-contractual liability. Liabilities of this kind are recognized in Austria, Germany, Portugal, Türkiye.[117] Quasi-contractual liability is judge-made law. Its emergence is a reaction to overly rigid tort law, including a too restrictive approach to compensation of pure economic loss. In common law jurisdictions like the United Kingdom or the United States of America, third party liabilities for pure economic loss are mainly based on the tort of negligent misrepresentation.

Quasi-contractual liability is particularly attractive to the plaintiff. Like contractual liability, quasi-contractual liability also lowers the pleading standard and alleviates the burden of proof. The plaintiff must plead and, if necessary, prove a breach of duty, but the defendant must rebut the assumption of her negligence.

Essentially, two legal institutions fall into the category of quasi-contractual expert liability: Firstly, liability might be based on a breach of pre-contractual duties (culpa in contrahendo). The requirements and consequences are similar to those under the Misrepresentation Act 1967 (UK). Third parties, such as experts, are liable, especially, if they have invoked special reliance in the accurateness of the representations.[118] One possible constellation concerns a third party that acted to further the goals of the other party, without necessarily being an agent of that party in a legal sense ('Sachwalter'). Another scenario concerns professional liabilities of experts for the accuracy of their information service, whereby the concept of the expert determines the scope of liabilities.

Secondly, the contract concluded upon the solicitation of the rating might unfold a protective effect towards a third party. Under this concept, the plaintiff

116 Supra 4.1.

117 Austria, p. 238.; Germany, p. 333.; Portugal, p. 467; Türkiye, p. 564.

118 For details, e.g. Portugal, p. 467.

is the third party (not the CRA). Compared to concepts of pre-contractual liability (which consider the CRA as a third party) the plaintiff might be slightly worse off. The reason is that the claim is derivative, i.e. it is rooted in the contract between the issuer and the CRA and accordingly the CRA may invoke defenses under that contract.[119] For example in Germany, courts argued that the right to invoke defenses has been implicitly waived if the expert statement might be more authoritative for the purchasers than the information provided by the seller himself.[120]

Courts in different countries will treat the rather loose requirements under these two liability concepts differently. German case law served as a source of inspiration for courts in some jurisdictions, e.g., Portugal, Spain, Turkey.[121] In those countries judges might continue to look to German law for interpretation guidance. Under German law, an expert might be subject to pre-contractual liability if s/he has invoked special reliance, i.e. a degree of reliance that goes beyond reliance on the general sincerity of a person involved in legal transactions. For a contract to unfold protective effect, a German court will look at (i) whether the injured third party is equally affected by the effects of performance as the CRA's client, (ii) whether the CRA was willing to take responsibility for this effect and, lastly, (iii) whether there is a need to protect the third party, i.e. the investor.

Both liability concepts, pre-contractual liability of a third party and contracts with protective effect towards third parties, have been used by courts to accommodate new liability constellations, including prospectus liability and also the liability of experts such as statutory auditors. Despite differences in theory and actual application, courts appear to consider similar factors when applying the one or the other liability concept. In the MS Deutschland decision of 2021, a German county court openly refused to distinguish between the two concepts, arguing that the relevant factors for either, third party liability or liability towards a third party, are essentially the same.[122]

4.4.2 Reasonable Reliance

The most critical limb of the legal test concerns whether it was reasonable to expect that the injured would rely on the assessment. This filter has an

119 E.g., s 334 German Civil Code.

120 Germany, p. 334.

121 E.g. Portugal, p. 468; Türkiye, p. 564.

122 Germany, p. 334 on LG Berlin, Urteil vom 5.5.2020 – 11 O 5/19 (MS Deutschland), WM 2021, 444. For details cf. Leyens (n 84), para 123 et seqq.

effect comparable to 'reasonable reliance' under the common law concept of negligent misrepresentation and its precise scope and limits are equally ambiguous.

To start with, credit ratings that are solicited by the issuer and are made publicly available will, naturally, be included into a decision to invest. It is exactly this effect which is the historical reason for the emergence of credit ratings and it also explains why customers are willing to pay for credit ratings.[123] Initially, investors paid for credit ratings, the issuer-pays model emerged only later when duplication techniques made it unprofitable to sell ratings to investors. The economics of credit ratings are unchanged since then: The credit rating helps to overcome an information asymmetry which otherwise would preclude the transaction or make it considerably more costly. In the absence of a credit rating an issuer would have difficulties attracting finance from anonymous investors. This is why an issuer pays for the rating.

However, it has been argued that CRAs only provide an opinion that should not be used for the purpose of making investment decisions.[124] In light of what we know about real-world investment decisions this sounds unrealistic. However, concepts of quasi-contractual (professional) expert liability assume duties towards a person with whom the expert does not have a contract. The line of argument employed to underpin such liability is similar to that used with regard to the protection of CRAs against liability under the US-American 1st amendment defense: While someone who simply provides an additional opinion will not assume liability, a professional expert is subject to tighter duties and might be held liable for an incautious statement. In some civil law countries, we also find statutory liability rules for negligent professional advice.[125] Austrian law, e.g., stipulates the liability of a person who holds herself out to be an expert and provides services for remuneration.[126]

In some countries, new theories develop that might be used to widen the criterion of special reliance. In Portugal, e.g., the idea of a pre-contractual network has been discussed.[127] According to this line of argument, in case of a solicited rating the CRA should not be regarded as a third party because its rating forms part of a pre-contractual plan. As opposed to that, in case of an unsolicited rating, the CRA would not form part of the pre-contractual plan and hence be treated as a third party.

123 Supra 2.1.2.
124 Supra 2.3.1.
125 E.g., s 323 para 1 sentence 2 German Commercial Code on statutory auditors' liabilities.
126 S 1300 Austrian Civil Code.
127 Portugal, p. 470.

4.4.3 Registered CRAs as State-Approved Experts?

Within the EU, a credit rating can be used for regulatory purposes if it has been prepared by a registered CRA (in the US: by a NRSRO).[128] So far, there is only one (appealed) decision by a German court that argued that a CRA might assume liability due to its position as an expert recognized by the state.[129] A similar line of argument has been used with regard to statutory auditors, e.g., in Austria.[130]

Hence, regulation and especially registration requirements of CRAs might foster their exposure to quasi-contractual liability as they bring a CRA closer to the role of a state-approved expert. This does, however, not eliminate the need to determine the scope of duties. It has been argued, that even if a credit rating aims to protect the investor public by providing the information necessary to make investment decisions, an individual investor is still protected only indirectly.[131]

The views differ as to whether, on this basis, one might assume that a CRA has claimed a special degree of trust and thereby significantly influenced the contractual negotiations or the conclusion of the contract within the meaning of the relevant concept of quasi-contractual liability, e.g. Germany.[132] Arguably, the concepts of quasi-contractual liability, which were inspired by German law, are less narrowly interpreted by foreign courts. For example, it is reported for Türkiye, that a CRA might be held liable if a bank reasonably relied on the accuracy of a publicly disclosed credit rating and approved a loan for a customer that thereafter defaulted.[133]

4.5 Negligence Liability in Tort (Common Law)

4.5.1 Breach of Statutory Duties that are Intended to Protect Another Person

In countries that do not recognize non-contractual negligence liabilities in cases of pure economic loss, the legislator may, of course, adopt provisions that specifically protect against such losses. Where provisions have been adopted

128 Art 4 para 1 CRAR.
129 OLG Düsseldorf, Urteil vom 8.2.2018 – I-6 U 50/17, BKR 2018, 210, BeckRS 2018, 2321. Cf Leyens (n 84) para 138–141.
130 Austria, p. 249 and p. 244.
131 Portugal, p. 512.
132 Germany p. 334, 342.
133 Türkiye, p. 564.

that specifically protect against pure economic loss, a liability concept is established that is close to what is known in common law jurisdictions as statutory breach. Similar concepts exist in civil law. For example, the law of torts in Germany provides for liability in case of a breach of a statute that is intended to protect another person against pecuniary loss (s 823 para 2 German Civil Code). Congruent provisions can be found, e.g., in Portugal and Türkiye.[134]

For EU Member States, the existence of a specialized liability rule in art 35a CRAR in 2013 has calmed the debate as to whether the CRAR unfolds protective effect in the aforementioned sense. Discussions might continue in some countries, e.g., in Portugal.[135] It is difficult to see though how national law could base liability on a provision of the CRAR although that same regulation has set the terms of liability itself in art 35a CRAR.

The Turkish art 63 CML No. 6362 could become a driver of the comparative debate. According to this provision, CRAs are subject to the same liability rule as statutory auditors. It reads: "Independent audit firms shall be responsible, with the auditors that have signed the report, within the limited scope of their duties, for damages that may result from the fact that financial statements and reports they have audited have not been audited in accordance with legislation. Independent audit firms, credit rating agencies, and appraisal firms shall be liable for damages they have caused due to false, misleading, and incomplete information included in reports they have prepared as a result of their activities."[136] The alignment of CRAs' liabilities with those of auditors is convincing against the background of the gatekeeper function that is specific to each of the two information intermediaries. In many countries, there is a large and continuously growing body of case law on auditors' liabilities. According to the Turkish liability standard, courts may reasonably draw on decisions regarding auditors when assessing CRAs' liabilities. It can be assumed that courts are able to deal appropriately with the differences between the two intermediation services, e.g., with regard to information access and differences between backward-looking and forward-looking assessments.

4.5.2 The Concept of Negligent Misrepresentation

In common law, the tort of negligent misrepresentation has some similarities with civil law quasi-contractual liabilities which have been discussed in the previous section. Especially, pure economic loss of a third party is compensable

134 Portugal, p. 572; Türkiye, p. 563.
135 Portugal, p. 468,
136 Cf. Türkiye, p. 561 for this translation.

and the burden of disproving negligence lies on the defendant, provided the plaintiff can overcome the (potentially high) hurdles of establishing a duty of care of the defendant.[137] Further, as shown by the English landmark case Hedley Byrne v. Heller of 1964, even an opinion may be a misleading statement that leads to liability provided a 'special relationship' existed between the parties.[138] A closely related route of liability derives from various misrepresentation acts, which have been adopted in common law countries all over the globe. For example, under s 2(1) of the Misrepresentation Act 1967 (UK), civil redress is available to a party that has been induced to enter into a contract by a misrepresentation.

The assessments differ with regard to the practical relevance of the common law tort of negligent misrepresentation. The best-known example of its application against a CRA is the Australian ABN AMRO judgement of 2014, in which Standard & Poor's was held liable to investors who had not solicited the rating. It should be noted, however, that the group of injured investors was limited and known to the CRA who was also aware that its rating would be used to inform those investors.[139] The case hence concerned a primary market constellation.[140] The role of the CRA was similar to that of an expert whose opinion is included into a prospectus.[141]

From the Australian perspective, the impact of the decision appears to be much more limited than one might believe from the outside. Observers from other common law countries have noted that it is far from clear that courts in their countries would evaluate the relevant factors in the same way, e.g. Singapore.[142] In the United Kingdom, the existence of a specialized liability rule based on art 35a CRAR will probably reinforce the courts' reluctance to interfere with legislative decisions.[143] Since Australia did not have a dedicated statutory remedy like art 35a CRAR, the ABN AMRO case is distinguishable.

The definitions and elements of negligent misrepresentation (and a negligent misstatement) differ between countries and, in the case of the United

137 Singapore, p. 498 on Animal Concerns Research & Education Society v Tan Boon Kwee [2011] 2 SLR 146, [77].
138 Hedley Byrne & Co Ltd v Heller & Partners Ltd [1963] 3 WLR 101 (HL). Cf. United Kingdom, p. 599.
139 ABN AMRO Bank NV v Bathurst Regional Council [2014] FCAFC 65; (2014) 224 FCR 1 (ABN AMRO).
140 Cf. further infra 5.1.1. on the distinction between primary and secondary market constellations.
141 Cf. supra 4.3.1. on prospectus liability.
142 Singapore, p. 494 and p. 498.
143 United Kingdom, p. 596.

States of America, even between the Federal States.[144] It appears to be an overarching goal of all legal tests considered, however, to prevent indeterminate liabilities towards third parties, to keep liability risks calculable, and to avoid a chilling effect in the market for credit ratings.

4.5.3 The Legal Test, Especially Proximity

In principle, there must be a duty towards the injured person, or, in other words, it must have been reasonable to rely upon the statement. In the United Kingdom, the '*Caparo*' test provides a certain, albeit not definitive orientation.[145] The test is based on foreseeability, proximity, and it being fair, just and reasonable to impose a duty of care in tort. A three-pronged test of foreseeability, proximity, and policy is also used in other countries, including Israel.[146] In Singapore, the so-called 'Spandeck' framework is used to further delineate the elements.[147] The framework involves considering (i) the factual foreseeability of harm to (a class of) persons, (ii) the presence of legal proximity as between the actual parties, and, again, (iii) whether policy considerations negate any prima facie duty of care.

In another judgement, a court in Singapore explained that to prove proximity the plaintiff must show that "the [claimant] was so closely and directly affected by the defendant's actions that the latter ought to have had the former in contemplation in acting."[148] Proximity is thus a highly fact-specific inquiry. The relevant factors include whether the defendant had control over the circumstances in which harm is caused, the defendant holding herself out as possessing special skill or expertise, knowledge of likely reliance, vulnerability and/or risk of harm to the claimant, and causal proximity, in the sense of the shortness of the causal chain between failure to take care and harm to the claimant.[149] Overall, it appears that, in most cases of CRAs' liabilities, claimants will fail to prove proximity and reasonable reliance. US courts found that a negligent misrepresentation is only (potentially) actionable if it was disseminated to a person or limited category of people.[150] Hence, a US court might

144 United States of America, p. 651.

145 United Kingdom, p. 596. on Caparo Industries plc v Dickman [1990] 2 AC 605 (HL).

146 Israel, p. 398.

147 Singapore p. 498 on Spandeck Engineering (S) Pte Ltd v Defence Science & Technology Agency [2007] 4 SLR(R) 100, [73], [77] and [83].

148 Singapore, p. 498: NTUC Foodfare Co-Operative Ltd v SIA Engineering Co Ltd [2018] 2 SLR 588, [39].

149 Singapore, p. 498 on the relevant case law.

150 United States of America, p. 651. on In re Nat'l Century Fin. Enters., Inc., Inv. Litig., 580 F.Supp.2d 630, 647 (S.D. Ohio 2008).

find negligent misrepresentation not to be actionable at all if the faulty credit rating was disseminated to the public.[151]

In particular English courts are said to be resistant to the imposition of a duty of care in an unprecedented constellation.[152] The Australian ABN AMRO case, which resulted in liability, concerned a credit rating that was targeted at a small group of people. The court holding shows that proximity may be established by the plaintiff. Arguably, also courts in other common law countries would generally be open to consider liability in such a constellation.[153]

Any duty of care owed under a liability concept based on negligent misrepresentation, however, will be limited in scope. For example, courts in Singapore are likely to find that a credit rating does not constitute advice. As an opinion on creditworthiness, it is merely one piece of information. Courts in Singapore would limit liability based on the degree to which misleading information was causal for the harm (so-called 'SAAMCO cap').[154]

Further, it is argued that courts in Singapore would be less inclined toward the finding that the investing local councils were 'vulnerable' parties.[155] A local council might have adequate means of verifying the information themselves, even if those were less effective than the means available to the defendant.[156] Courts in Singapore decided that a private bank customer who is 'commercially savvy [with] sufficient knowledge of investment principles to understand the types of risk involved' is not in need of protection by his or her bank.[157]

4.6 Liability for Intentional Behaviour

4.6.1 Deceit

In a number of jurisdictions, including Austria, Germany, Portugal, Spain, Türkiye, the law of torts, with few exceptions,[158] does not provide for compensation in cases of negligently caused economic loss.[159] As explained above, this

151 United States of America, p. 651.
152 United Kingdom, p. 596.
153 Singapore, p. 498.
154 Singapore, p. 498 on South Australia Asset Management Corp. v. York Montague Ltd. [1997] 1 AC 191, 214.
155 Singapore, p. 498.
156 Singapore, p. 498.
157 Go Dante Yap v Bank Austria Creditanstalt AG [2011] 4 SLR 559, [48].
158 E.g., liability for harm caused by negligent misrepresentation of facts (not a prognosis like a rating) under s 824 German Civil Code.
159 Austria, p. 238; Germany, p. 332.; Portugal, p. 572.; Spain, p. 542; Türkiye, p. 563.

is one of the reasons for the emergence of quasi-contractual liabilities in some of those countries.[160] The protection under the general law of torts is restricted to cases of intentional behavior. The most obvious reason for liability is deceit, i.e. fraudulent behavior.

In English law, deceit was first established through the case Pasley v. Freeman of 1789 that concerned the liability of an intermediary for providing a false credit reference concerning a purchaser of goods.[161] The US Restatement (Third) of Torts characterizes a fraud claim as follows: 'One who fraudulently makes a material misrepresentation of fact, opinion, intention, or law, for the purpose of inducing another to act or refrain from acting, is subject to liability for economic loss caused by the other's justifiable reliance on the misrepresentation.'[162] The legal tests in other common law countries such as Singapore, but also in civil law jurisdictions such as Germany or Italy, are alike.[163] In sum, the definition and elements of a deceit claim are very similar in the jurisdictions considered.

The view prevails, however, that the tort of deceit is unlikely to be of great use in holding CRAs liable.[164] This is due to the high pleading standard and the onus probandi. Under the US Federal Rules of Civil Procedure, a plaintiff must at least allege the fraudulent scheme and/or the fraudulent intent.[165] Similarly, English courts assume an inherent improbability of fraud and hence require a substantial amount of initial evidence.[166] The burden to prove knowledge or recklessness is on the plaintiff. It is less likely that third-party plaintiffs, such as injured investors, will be able to prove intention in relation to a CRA.[167] Courts in Singapore have shown a willingness to accept a proof of intention if the misrepresentation was circulated to the general public with a view to being acted upon.[168] In cases where fraudulent behavior can be proven, courts in England and Singapore will draw a strong inference or evidential presumption of

160 Supra 4.4.1.

161 Pasley v Freeman [1789] 3 TR 51. The old English case still serves as a basis in common law countries like Singapore 3.13.–2.1.5.

162 Restatement (Third) of Torts: Liability for Econonic Harm, 2020, § 9. Cf. United States of America 3.17.–3.2.4.

163 Germany, p. 339; Italy, p. 425; Singapore, p. 494.

164 M. Hemraj, Credit Rating Agencies, 2015, p. 183.

165 United States of America, p. 652.

166 United Kingdom, p. 595.

167 Singapore, p. 496.

168 Singapore, p. 496 with reference to JTRust Asia Pte Ltd v Group Lease Holdings Pte Ltd [2020] SGCA 95, [192]–[193].

reliance from the fact that the claimant entered into the contract after receiving a false statement.[169]

4.6.2 Intentional Misconduct (Professional Liability)

In some countries, including Germany, Austria and Portugal, courts have assessed expert liabilities under the tort of intentional damage inflicted in a manner offending common decency.[170] Under s 826 of the German Civil Code, a person is liable who, in a manner contrary to good morals (bonos mores), intentionally inflicts damage on another person. 'Good morals' is an indeterminate legal term. It relates to the standards of social morals generally accepted and required within a civil society. The relevant liability provisions in the law of torts serve to protect an ethical-legal minimum (not maximum) standard. For experts, the relevant duties are often specified in professional codes of conduct (deontologia professional).[171] The risk of an expert to be held liable in tort, in essence, depend on how precisely such specifications are drafted and on public expectations regarding the integrity of the expert. Within the EU, the detailed provisions of the CRAR, its registration requirement and the public oversight by ESMA are clearly an expression of greatly increased public expectations regarding the integrity of the previously unregulated CRAs.

The infringement requires intentional behavior which is generally seen as a high liability hurdle. Intention, however, includes all forms of dolus and, hence, dolus eventualis suffices. Thus, knowledge of a high probability of the occurrence of damage is sufficient for intent to cause damage. German courts have affirmed intent where the expert can be assumed to have had doubts about the correctness of the statement.[172] A notorious case concerns statements made "out of the blue" without sufficient examination of the facts. German courts have been subject to criticism for blurring the line between intent and gross negligence. In fact, the Supreme Court for Civil Matters held that unconscionable (reckless) conduct in the aforementioned sense may already be present if

169 United Kingdom, p. 602 with reference to Hayward v Zurich Co Ltd [2016] UKSC 48; similar Singapore. p. 507.

170 Austria, p. 242 (s 1295 para 2 Austrian Civil Code); Germany, p. 339 (s 826 German Civil Code); Portugal, p. 472 (either the claim is based on an abuse of right under art 334 Portuguese Civil Code or on an unwritten rule aimed at protecting a basic ethical-legal value).

171 Portugal, p. 472.

172 Germany, p. 339, on the case law, e.g., BGH, Urteil vom 6. 5. 2008 – XI ZR 56/07.

the expert is grossly negligent in refusing to recognize the incorrectness of his or her judgment.[173]

Many of the cases on professional tort liabilities concern chartered auditors and chartered tax advisers, i.e. professions that stand for high standards and are tightly regulated. The situation is similar with regard to the so-called deontologia professional, e.g., in Portugal.[174] Against the background oftightened duty standards under the CRAR, it does not seem unreasonable to assume that a German court might hold a CRA liable to an investor for intentional misconduct against bonos mores (s 826 BGB).[175] So far, German courts have rejected the liability of rating agencies.[176] Not every (serious) misconduct may be classified as unconscionable, also because the determination of intentional conduct will result in the denial of insurance coverage.[177]

5 Eligible Claimants, Duty Standard and Behavior with High Liability Risk

5.1 Duties of a CRA to Issuers and to the Investor Public

5.1.1 Overview: the Basic Distinction between Primary and Secondary Markets

Courts appear to generally distinguish between cases that concern credit ratings of initial issues of securities (primary markets) and credit ratings of continuing trades (secondary markets). A primary market transaction is a sale from the issuer to the investor, often through an intermediary like a bond dealer. Professional experts such as CRAs pledge their reputation for this specific transaction. Depending on the circumstances, the audience of the credit rating might be an identified group (participants in an exclusive sales event) or non-identified group (non-exclusive public sale event). In the latter case,

173 BGH, Urteil vom 26.9.2000 – X ZR 94/98, BGHZ 145, 187 = NJW 2001, 360 marginal no. 55 (juris) (chartered auditor). For details cf. Leyens (n 1), pp 375, 426, 447, 508.

174 Portugal, p. 472.

175 Germany, p. 339.; Leyens (n 1), p. 507 ff.

176 OLG Düsseldorf, Urt. v. 8.2.2018 – I-6 U 50/17, BKR 2018, 210 para 34 ff. For details cf. Leyens (n 84), para 138 et seqq.

177 S 103 German Insurance Contract Act (Versicherungsvertragsgesetz) precludes insurance coverage in cases of intentional behavior of the insured person.

the individual investors are not identifiable. However, the number of the securities, and, accordingly, the maximum number of investors are known to the CRA.

A secondary market transaction concerns a sale between investors, again regularly conducted by an intermediary such as a bond dealer. Professional experts also play a role on secondary markets because they can also pledge their reputation to facilitate or ensure continuing sale transactions. For example, a CRA can provide a credit rating on a regular basis, as a rating of the issuer (issuer rating), or as a rating of the existing issue (issue rating). The audience of the credit rating consists of investors that are not known to the CRA and not identifiable because the sale transactions are executed via the market, i.e. between anonymous parties.

In some jurisdictions, the distinction between primary and secondary markets is well established through landmark cases on the liability of statutory auditors. For example, in the United Kingdom (Caparo),[178] the United States of America (Ultramares),[179] and in Germany,[180] auditors may be liable for a negligent breach of their duty of care to an identified or identifiable audience, while they do not owe duties of care to the investor public. As far as is known, only in a few countries, including Austria, a statutory auditor has been held liable for a negligent breach of the duty of care to the investor public.[181]

In Australia, the major CRAs are not licensed to provide their credit ratings to the investor public but only to wholesale investors.[182] The major CRAs have opted for a license that allows them to service wholesale clients only, not retail investors. In Australia, retail investors are currently non-eligible as plaintiffs of a damage suit against the major CRAs.

From a legal comparative perspective, it would be of interest to explore the factors that courts take into consideration to determine to whom a CRA (or a professional expert) owes its duties. For the purpose of an overview, factors that may give rise to liability include privity, proximity, and knowingly influencing investors. Where liability is denied, arguments relate to incalculable liabilities, unlimited litigation (floodgates argument), and/or to the rejection of a role of the information intermediary as insurer of the investor public.

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178 United Kingdom, p. 596 on Caparo Industries plc v Dickman [1990] 2 AC 605 (HL).

179 Ultramares Corp. v. Touche 174 NE 441 (NY 1931).

180 BGH, Urteil vom 2.4.1998 – III ZR 245–96, BGHZ 138, 257 = NJW 1998, 1948 (statutory auditor). Cf. Leyens (n 1), pp 390, 426, 466, 487 et seqq, 508, 527.

181 OGH 27.11.2001, 5Ob262/01t, ÖBA 2002, 820 (statutory auditor).

182 Australia, p. 221. Cf. supra 2.2.3.

To conclude this overview, a note of caution appears appropriate: The distinction between primary and secondary markets is a rather rough tool, and, more importantly, views might be changing. One possible driver of change is seen in the climate change litigation in the Netherlands.[183] In the landmark case of Shell/Friends of the Earth of 2021, the District Court of The Hague ordered the oil and gas company Shell to reduce its scope 1, 2 and 3 greenhouse emissions by 45% by 2030.[184] More than 17,000 individual plaintiffs joined Friends of the Earth in this litigation. The first instance judgment was overruled in 2024.[185] However, the case impressively demonstrates that the mere fact that the plaintiffs form a broad and diverse group may not prevent liability. Hence, it cannot be completely ruled out that liability may arise in the future and that a CRA will be held liable to the investor public.

5.1.2 Primary Markets

Art 35a CRAR (EU) covers transactions on the primary as well as on the secondary market.[186] There is no trading requirement, i.e. investors may claim damages for losses deriving from a decision to buy, sell, or hold a particular security. Investors who decide not to buy a particular security on the basis of a defective credit rating cannot base a claim on art 35a CRAR (EU).

The German High Court of Düsseldorf held, however, that issuer ratings are not covered by art 35a CRAR.[187] Commentators have criticized this narrow interpretation because it would lead to an imbalance in incentives that the CRAR was designed to mitigate.[188] The CRA would face a threat of being held liable by an issuer in case of an unduly pessimistic rating, while it remained protected against liability towards investors in case of an overly optimistic rating. The court based its view on the wording of art 35a para 1 vis-à-vis para 2. The interpretation is thus a matter of EU law that may eventually reach the ECJ.

Quasi-contractual liabilities and liability for negligent misrepresentation require to establish a duty of care towards the investor. The probability that a court will assume such a duty differs between countries. Arguably, a court in the United Kingdom will not be easily be convinced of the necessity to assume

183 Netherlands, p. 445, see also 4.3. (ESG ratings).
184 Rechtbank Den Haag, 26 May 2021, ECLI:NL:RBDHA:2021:5337 (Milieudefensie v. Shell).
185 Gerechtshof Den Haag, 12.11.2024, ECLI:NL:GHDHA:2024:2099 (Milieudefensie v. Shell).
186 European Union, p. 94.
187 OLG Düsseldorf, Urteil vom 8.2.2018 – I-6 U 50/17, BKR 2018, 210. For details cf. Leyens (n 84) para 25 et seqq.
188 European Union, p. 94; Germany, p. 329.

such a duty because there is an alternative statutory civil law claim available under art 35a CRAR (UK).[189]

Remarkably, in the Australian ABN AMRO case, the court held that 'Knowledge of the identity of the person or persons to whom a duty is owed is not necessary, or generally of significance, in determining the existence of a duty of care'.[190] Similarly, in the German case MS Deutschland 2019, the courts found that a CRA may have a duty towards a class of investors who acquire a specific bond issue.[191] Already, the US-American decision in the Abu Dhabi case of 2009 pointed into that direction. The court denied the CRA the 1st Amendment defense based on the fact that the product was only targeted at a small pool of investors.[192]

5.1.3 Secondary Markets

The list of claimants eligible under art 35a CRAR (EU, UK), quasi-contractual liability and under tort law is not generally limited. However, the liability threat appears to be considerably lower with regard to secondary market transactions. It appears that courts in all jurisdictions considered will ask whether the expert knew or must have known that the opinion would be used in making a specific purchase decision.[193] Further proximity factors (salient features) might play a role, especially the inability of the purchasers to second-guess the correctness of the expert opinion.[194] Generally, investors have a significantly greater need for information in primary markets which in turn justifies a stronger liability threat. This rationale also underlies specialized regimes of prospectus liability which restrict the eligible claimants to those who purchased a newly issued security, thus excluding purchasers who bought an already existing security on the market.

Courts in China appear to be more inclined to assume (some) duties to the investor public[195] whereas in India, there is insufficient proximity even if

189 United Kingdom, p. 596.

190 Australia, p. 221.

191 Germany, p. 334 on LG Berlin, Urteil vom 5.5.2020 – 11 O 5/19 (MS Deutschland), WM 2021, 444 on an issue rating but see OLG Düsseldorf, Urteil vom 8.2.2018 – I-6 U 50/17, BKR 2018, 210 on an issuer rating. For details cf. Leyens (n 84), para 115.

192 United States of America, p. 644 on Abu Dhabi Commercial Bank v. Morgan Stanley & Co., 651 F. Supp. 2d 155, 176 (S.D.N.Y. 2009) (financial product targeted to a small pool of investors).

193 Australia, p. 221. on ABN Amro Bank NV v Bathurst Regional Council (2014]) 224 FCR 1, [578]; Singapore, p. 498.

194 Australia, p. 221.

195 China, p. 288 with reference to Wang Fang v. Wuyang Construction Group and Chen Zhizhang & Debang Securities Company (2020) Zhe 01 Minchu No. 1691.

a misstatement contained in the prospectus influenced a secondary market purchaser.[196] Similarly, in Austria, most scholars argue that liability – as a general principle – only arises if the liability risk can be estimated and limited.[197] Hence, CRAs only owe duties to identifiable groups of investors and are only liable towards third parties if the rating relates to a specific 'project'. This limits liability risks to the issuance of ratings and probably excludes issuer ratings.[198] It should be remembered though that Austria is one of the very few countries where a statutory auditor has been held liable for a negligent breach of the duty of care to the investor public.[199]

In the United States of America, there is "no affirmative duty to verify the quality of the underlying portfolios."[200] It will therefore be difficult to convince a court that a duty of care existed or that a CRA had a duty to look deeper into the portfolios and disclose what it found.[201] Similarly, a case from Singapore explains that, in the absence of an explicit duty, the crux of proximity is 'whether the [claimant] was so closely and directly affected by the defendant's actions that the latter ought to have had the former in contemplation in acting'.[202]

5.2 Duty Standard for Professional CRAs

5.2.1 Overview: Procedural Duty Standard

The term 'duty standard' is used here with a view to functional comparison. A specialized liability rule might define specific duty breaches. In the absence of such specifications, courts apply different liability rules or legal concepts to cases that appear to be very similar. This is true even for different courts of the same jurisdiction. For example, German case law on the liabilities of professional experts swings back and forth between (quasi-)contractual liability and tortious liabilities to third parties for infringements of bonos mores.

As the discussion stands, there is no definite global duty standard in the sense of a positive description of good conduct requirements. Still, a large part of the discussion revolves around the question of whether a rating is merely an opinion and, if so, what consequences this entails. It appears that, in the past,

196 India, p. 383.
197 Austria, p. 244.
198 Austria, p. 244.
199 OGH 27.11.2001, 5Ob262/01t, ÖBA 2002, 820 (statutory auditor).
200 United States of America, p. 653.
201 Manns, "Downgrading Rating Agency Reform", [2013] 81 Geo. Wash. U. L. Rev. 749, 756.
202 Singapore, p. 498.

courts and commentators overemphasized or perhaps even misunderstood the freedom of opinion.

The progress that has been made in the discussion in the years after the global financial market crisis of 2008 might be summarized as follows:[203] A credit rating is an opinion about the probability of a future contingency. It would be wrong to judge the accuracy of a forecast based on whether it turned out to be true in retrospect. Only a procedural standard appears appropriate. Since the credit rating is made by a professional service provider, the procedures that must be followed form a professional duty standard. To conclude, the duty standard will mainly serve to determine a breach in cases where a credit rating is excessively high or low.

The next sections will explore how specialized liability rules further differentiate the duty standard, which approach is taken under quasi-contractual liabilities and general tort law, and, finally, how spill-overs from regulatory duties and codes of conduct could inform courts on the application of general liability rules in contract or tort.

5.2.2 Specialized Liability Rules

The specialized liability regimes of the CRAR (EU) and the corresponding regime in the United Kingdom build on a procedural approach to mitigate the freedom of opinion issues and to account for the problem that a prognosis as such cannot be right or wrong. Liability under art 35a CRAR (EU) is triggered by the infringements listed in Annex III of the CRAR, provided the infringement has had an impact on the credit rating. The infringements relate to the organizational obligations and duties of conduct set out in the CRAR (EU). Accordingly, no finding is required as to the correctness of the rating.

Instead, it is the crux of the procedural approach to prove the impact on the rating, i.e. the causality between the infringement and the outcome of the rating process. Out of the approximately 90 violations listed in Annex III of the CRAR (EU), only a few may have any impact on the rating process.[204] The reason for this is that the list of violations was set up originally for the purpose of public enforcement. Regarding civil liabilities, for example, it appears unlikely, if not impossible, that a claimant will establish that ignorance of the corporate governance requirements, such as the number of independent directors, office periods, or director remuneration has had an impact on the outcome of a particular rating process.

203 Cf. also supra 2.2.1 et seq. on CRAs failures and regulatory reactions.

204 European Union, p. 98. Cf. infra section 5.3 on types of behavior with high liability risk.

It should be noted that the competent supervisory authorities, ESMA (EU) or FCA (UK), can establish a statutory offence independently of whether the infringement has had an impact on the credit rating.[205] This shows once again that private law enforcement has, at best, a complementary function to the existing tools of public enforcement.[206]

5.2.3 Quasi-Contractual Liabilities and General Tort Law

Professional liability for negligence, whether quasi-contractual or based on misrepresentation in tort law, in essence, builds on a test that asks whether one could reasonably expect an expert to assume a duty to the claimant. If this is the case, it appears commonly agreed that professional experts must adhere to higher standards of behavior than laymen. It is therefore essential for an expert to assure that her statements do not mislead.

Accounts from most of the countries considered show that today, a CRA is commonly seen as a professional expert in the context of professional liability under quasi-contractual or general tort law standards.[207] Registration requirements e.g. under the CRAR (EU) or a recognition as NRSRO (USA) appear to be drivers of a classification as state-approved agent, which might impose an even higher duty standard. A state-approved expert is different from other experts as she must assume that her expert judgment will influence or induce the decisions of non-experts. German courts, e.g., therefore generally argue that state-approved experts must act independently, conscientiously, and impartially.[208] German courts explicitly held that a registered CRA counts as a state-approved expert.[209] However, while the District Court of Berlin found that a CRA has a duty of care towards investors who did not solicit the rating, the High Court Düsseldorf came to the opposite conclusion in an unrelated proceeding.[210]

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205 E.g., Scope Ratings GmbH v The European Securities and Markets Authority (Decision Ref.: 2020–D–03) (Board of Appeal of the European Supervisory Authorities against a decision by ESMA to impose a fine on a CRA for infringements relating to its methodologies).

206 Cf. generally supra 2.3.2 on public vs. private enforcement.

207 Austria, p. 247; Germany, p. 334; Italy, p. 419; Singapore, p. 498; Spain, p. 533. Cf. also supra sections 2.1.3 and 3.2.

208 Germany, p. 343. BGH, Urteil vom 9.12.1975 – VI ZR 157/73, NJW 1976, 620, 622 (Warentest II). Cf. Leyens (n 84), para 119. Leyens (n 1), p 363 et seqq.

209 OLG Düsseldorf, Urteil vom 8.2.2018 – I-6 U 50/17, BKR 2018, 210; LG Berlin 5.5.2020, BeckRS 2020, 23328 (MS Deutschland). Cf. Leyens (n 84), para 115, 123.

210 Germany: OLG Düsseldorf 8.2.2018, BKR 2018, 210 para 27; LG Berlin 5.5.2020, BeckRS 2020, 23328 (MS Deutschland). Cf. Leyens (n 84), para 119.

A German court already gave a positive description of the procedural duty standard in 2006 before the need for regulation of CRAs became apparent. It made use of the set of procedural criteria that were initially developed by the BGH for (comparative) product and service tests provided by consumer organizations. According to these criteria the testimony should be "neutral, diligent and made in an effort to be objectively correct".[211] The standard appears to properly reflect the fact that a credit rating includes elements of a prognosis. Under this standard, judicial review is limited to examining whether the methodologies used and the conclusions reached are plausible and legally acceptable. It is an implicit requirement that the rating must be based on a sufficient factual basis, measured in terms of the assessment made, comprehensible and transparent. To fulfil these requirements, the rating methodologies must be used consistently and in accordance with the principle of equal treatment.

In Israel, courts appear to agree that a procedural standard applies which in turn limits the judicial review of a credit rating.[212] The standard is embodied in the specialized legislation on CRAs. It requires CRAs to conduct the rating in an appropriate manner.[213] In turn, the general securities law framework exempts experts from liability provided they have taken 'all appropriate measures' to ensure that the opinion 'did not contain any misleading items'.[214] Courts and perhaps also the supervisory authority might contribute to fleshing out details further.

In the United States of America, there is no specific duty standard for professional credit ratings.[215] Traditionally, US courts have tended to emphasize the freedom of opinion which shielded CRAs from liabilities and courts remain divided on whether credit ratings enjoy constitutional protection.[216] In the Abu Dhabi case of 2009, a three-factor-test was used to judge whether constitutional protection applies. The court considered the (limited) number of recipients, the agency's intentions and level of information, and possible conflicts of interest.[217] The test shows that it can be difficult for courts to separate

211 KG Berlin, Urteil vom 12.5.2006–9 U 127/05, WM 2006, 1432 (Scope Ratings). See also Leyens (n 1), pp 364, 451, 478.

212 Israel, p. 401.

213 Translation according to Israel, p. 401.

214 Translation according to Israel, p. 401.

215 United States of America, p. 654.

216 United States of America, p. 644.

217 Abu Dhabi Commercial Bank v. Morgan Stanley & Co. 651 F. Supp. 2d 155, 166 f., 179 f. (SDNY 2009).

the question of the duty standard and the question of who is protected by the duties.[218]

In Australia, CRAs are regulated as a subcategory of financial services providers. Their assessments count as 'general advice', with a different connotation with regard to the protection of free speech.[219] Outside the regulatory context, however, Australian law considers credit ratings as opinions as does the majority of the countries.

The opinion of an expert may be a misleading statement, i.e. a breach of duty. From a US-American perspective, the duty standard requires that the CRA does not choose a rating grade contrary to the information it has at hand.[220] Australian courts generally use an objective test but the type of audience at which the statement is directed must be included in the assessment whether the statement is misleading.[221] For the United Kingdom, the landmark case Hedley Byrne v. Heller of 1963 forms the starting point:[222] The case concerns a misleading statement, i.e. a breach of duty, where the statement is issued by a party with special skills and knowledge without having reasonable grounds for the view that it expresses, and/or without having exercised due care and skill in forming the view. This assessment appears to be generally in line with the approaches towards professional experts' liabilities in civil law jurisdictions.

With a view to collect some (perhaps) universally agreed insights: The standard of care includes a certain amount of due diligence with regard to information gathering and processing,[223] and also a minimum level of qualification and competence.[224] CRAs are not generally expected to conduct due diligence of information they receive from the issuer or to verify the findings of the (statutory) auditor.[225] Due to the nature of the credit rating as prognosis, beyond regulatory prescription, CRAs have discretion regarding how exactly to conduct their ratings.[226] It also appears agreed that CRAs are not expected to generally conduct due diligence of the information they receive from the

218 Cf. supra section 5.1 et seq. on eligible claimants.
219 Australia, p. 211.
220 United States of America, p. 654.
221 Australia, p. 223.
222 United Kingdom, p. 599 on Hedley Byrne & Co Ltd v Heller & Partners Ltd [1963] 3 WLR 101, HL.
223 India, p. 385.
224 Singapore, p. 498.
225 Israel, p. 401.
226 Israel, p. 401.

issuer or the statutory auditor.[227] These points will be elaborated further with a view to behavior that carries a particular risk of civil liability.[228]

5.2.4 Spill-Overs from Regulatory Duties and Codes of Conduct

Existing case law does not indicate that or how courts consider regulatory duties and codes of conduct to determine the duty standard. It does not seem too far-fetched that spill-overs will materialise in some countries, e.g., in India.[229]

Another source could be a code of conduct. Even if such a code is issued by a supervisory authority, a failure to comply with it might not in itself render the person liable. In Singapore, the duty standard set out in such a code is an important factor and can be relied upon by any party to the proceedings to establish or negate liability.[230] Arguably, the IOSCO Code of Conduct[231] would count as a code in this sense in Singapore.

It is less clear how private codes of conduct affect the duty standard. The leading CRAs maintain individual codes of conduct. For example, courts in Spain might be prepared to look at codes of conduct.[232] In Singapore, the content of the reasonableness standard will be determined upon consideration of an amalgam of factors, including a code of practice.[233] However, the codes of conduct of leading CRAs contain a disclaimer for liability which might lower the possible significance of such a code.

5.3 Types of Behaviour with High Liability Risk

5.3.1 Overview: Regulatory Infringements vs. Civil Duty Breach

Certain types of misbehavior are more likely to trigger liability than others. Despite their high relevance in practice, several issues have not yet been tested in court and the precise scope of liability risks remains unclear. For example, the multifaceted field of conflicts of interest, the conflict deriving from the contractual relationship to the issuer (issuer pays) and parallel offers of

227 Israel, p. 401; United States of America, p. 654.
228 Infra section 5.3.
229 India, p. 385.
230 Singapore, p. 490.
231 Cf. supra 2.2.2.
232 Spain, p. 536.
233 Singapore, p. 502.

non-rating services (consulting or advisory) have not yet been considered in their entirety by the courts.[234]

In the absence of precedents, courts will probably consider case law on other information providers. In countries where CRAs are regulated and where the regulatory use of credit ratings is limited to registered CRAs, it appears reasonable to assess the comparability with (statutory) auditors.

Credit ratings are different from certain other forms of standardized creditworthiness assessments and especially from credit scoring services. A credit rating involves an element of human discretion by a rating analyst. This difference is the reason why, e.g., art 2 para 2 (b) CRAR (EU) excludes credit scores and credit scoring systems or similar assessments from its scope. The discretion of rating analysts is also the reason why the regulation of CRAs places great weight on the prevention of conflicts of interest, e.g., as shown by art 6 et seq CRAR (EU). Nevertheless, a court might consider the case law on standardized creditworthiness assessments and especially on credit scoring as persuasive with regard to failures that do not relate to the discretionary part of the assessment.

5.3.2 Specialized Liability Rules

The list of infringements in Annex III of the CRAR (EU) appears to be the most comprehensive catalogue available at present. So far, there is no case law, neither on the original catalogue of the CRAR, nor on the corresponding catalogue in the United Kingdom.[235] Some of the of the approximately 90 infringements relate to severe misbehavior but the liability risks appear to be more theoretical in nature as it would be difficult to establish in court that the infringement had an impact of the outcome of the rating process.[236] This is particularly true for the area of conflicts of interest. It might be proven by a claimant that the CRA itself, or a member of the group of companies that the CRA belongs to, holds equity in the rated issuer, but despite the severity of this type of conflict of interest, it will be difficult to prove that it had an effect on the credit rating.

Commentators believe that, if at all, infringements of duties relating to the process of rating might gain practical significance.[237] This concerns the duties regarding methodology, informational basis, and also the duties regarding the review of the rating result (No. 42–51). The CRAR was not yet applicable

234 Baghai/Becker, “Non-rating revenue and conflicts of interest” (2018) 127 J. Fin. Econ 94.

235 European Union, p. 91; United Kingdom, p. 595.

236 On this requirement see 4.2.

237 European Union, p. 98.

in the few available German cases, but observers have noted that plaintiffs based their claims on conduct of the CRA that would fulfil the requirements of infringements No. 42 and 51.[238] No. 42 reads: "The credit rating agency infringes Article 8(2) by not adopting, implementing or enforcing adequate measures to ensure that the credit ratings and rating outlooks it issues are based on a thorough analysis of all the information that is available to it and that is relevant to its analysis according to the applicable rating methodology." No. 51 stipulates: "The credit rating agency infringes Article 10(2), in conjunction with the second paragraph of point 4 of Part I of Section D of Annex I, by issuing a credit rating or not withdrawing an existing rating in a case where the lack of reliable data or the complexity of the structure of a new type of financial instrument or the quality of information available is not satisfactory or raises serious questions as to whether the credit rating agency can provide a credible credit rating."

In other countries with regulatory standards and/or specialized liability regimes for CRAs, e.g., China and Türkiye, comparatively shorter lists can be found that inform directly or indirectly about types of behavior with a high probability of liability.[239]

The following failures will probably also count as breaches of duty under the specialized art 35a CRAR (EU), or lists of standards or principles in other parts of the world.

5.3.3 Insufficient Information

Although a CRA is not generally obliged to verify information provided by the issuer, by the statutory auditor, or publicly available information, failure to do so may result in a liability risk. In the judgement of a German court, which held a CRA liable, the CRA relied on an auditor report that was clearly inaccurate and insufficient as an information basis.[240] Similarly, in the Australian ABN AMRO case, reliance on false information provided by the issuer led to liability. The case concerned a structured financial product. The CRA had been involved in customizing the product and failed to independently verify whether the information was accurate.[241] An Indian court granted an injunction against

238 European Union, p. 98.

239 China, p. 292; Türkiye, p. 567.

240 Germany, p. 334, on LG Berlin, Urteil vom 5.5.2020 – 11 O 5/19 (MS Deutschland), WM 2021, 444.

241 Australia, p. 208 on ABN AMRO Bank v. Bathurst Regional Council [2014] FCAFC 65, 6.6.2014; cf. already the first instance judgement Bathurst Regional Council v Local Government Financial Services Pty Ltd (no 5) [2012] FCA 1200.

a downgrade based on the finding that the factual basis was improper.[242] In many countries, including Austria, Germany, and Portugal, a CRA will incur liability if the rating was issued 'out of the blue', without even a rudimentary evaluation of the factual situation.[243]

5.3.4 Flawed Method

So far, courts have been reluctant to criticise the methodology of a credit rating. As an Indian court put it, the rating methods vary from industry to industry and the court will not interfere if an opinion is plausible on the facts, and neither perverse nor arbitrary nor mala fide.[244] It follows that, conversely, a breach of the fundamental principles of professional conduct may lead to liability: e.g., arbitrariness, failure to treat the same the same, ignorance of available information, the issuing of a rating with knowledge of the issuer's inaccurate information, i.e., a creditworthiness assessment against better knowledge. An Australian court found that the publication of a rating comes with the implied representation that the CRA has formed its opinion based on reasonable grounds and as the result of an exercise of reasonable care and skill.[245] This is very much in line with the German judicature on the publication of (comparative) commodity and/or performance tests and rankings.[246] By publishing the rating the CRA makes a misleading representation. The most likely reason for liability is that the CRA has failed to collect and consider relevant information in arriving at the rating or that it used an inherently flawed methodology. Similarly, it is likely that a court in the United States of America will be able to hold a CRA liable if the CRA had solid, verifiable information suggesting a low rating and instead awarded a high grade.[247] From an Austrian perspective, a lack of relevant industry knowledge, sufficient qualification of the rating analyst or verification of the correctness of the data basis may also be considered a breach of the duty of care.[248]

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242 India, p. 386, on Oren Hydrocarbons Pvt. Limited v. India Ratings and Research Pvt. Limited (2017) 6 CTC 870.

243 Germany, p. 351.; Portugal, p. 472 (claims on general tort law).

244 India, p. 380 on Jindal Power Limited v. ICRA Limited (2020) 273 DLT 80, at [52].

245 Australia, p. 208 on ABN AMRO Bank NV v Bathurst Regional Council [2014] FCAFC 65; (2014) 224 FCR 1 (*ABN AMRO*) [12].

246 Supra 5.2.3 for details.

247 United States of America, p. 654.

248 Austria, p. 249.

5.3.5 Misleading Conduct

In Australia, misleading or deceptive conduct is routinely invoked in civil litigation also between sophisticated parties.[249] The claim appears to be particularly attractive under Australian law, inter alia, because there is no requirement of intent or of a finding that the defendant ought to have known that the statement or even silence was misleading, there is no due diligence defense and disclaimers do not provide a basis for denying liability.

Generally, an Australian court will ask whether a significant proportion of the target audience, or a not insignificant number of reasonable or ordinary persons in the class, would be misled or deceived.[250]

In Germany, the creation of an impression that there has been a comprehensive evaluation of a wide range of variables that has not actually taken place has led to liability of a credit assessment office (not a CRA).[251]

5.3.6 Conflicts of Interest

The notorious problem with regard to conflicts of interest, including aiding and abetting the issuer, relates to the difficulties in establishing causality between the infringement and the incorrectness of the rating. In Israel, the CRA legislation does contain a (rebuttable) presumption, according to which a CRA has operated in bad faith if it violated one of the numerous provisions of its chapter 5, which deals with conflicts of interest.[252] In contrast, the CRAR (EU) does not contain a similar presumption.

An Indian court issued an injunction against a CRA that downgraded the securities of an issuer after the contract with that issuer had been ended based on the finding that the CRA was biased.[253] A German court held that it would constitute intentional harm to investors under tort law if a CRA allows itself to be abused and acts in the service of the issuer in a reckless manner.[254] To be liable, however, the CRA must at least accept that its credit ratings will primarily serve to harm potential investors and induce interested parties to subscribe

249 Australia, p. 218.

250 Australia, p. 314.

251 OLG Frankfurt a. M., Urt. v. 7.4.2015 – 24 U 82/14, BeckRS 2015, 6846 (Scoring).

252 Israel, p. 403.

253 India, p. 386 on Magma Leasing Limited v. Credit Rating Information Services of India Limited 2001 SCC OnLine Cal 356.

254 Germany, p. 351 on s 826 German Civil Code.

to a bond that does not correspond to the perceptions evoked by the issuer.[255] In practice, the problem will be to prove that the CRA served the issuer in such a manner.

5.3.7 Failure to Downgrade

One of the main failures of CRAs during the global financial crisis is seen in the delayed adjustments. In India, the supervisory authority sanctioned a CRA for failure to downgrade, or delay in downgrading.[256] The Delhi High Court recognized that, since banks offer credit facilities based on the rating assigned, it is a duty of the CRA to "fairly continue to assess the credit rating of the party which is called "surveillance rating" during the life time of the credit facility."[257]

6 Causality and Recoverable Loss

6.1 Causal Chain for Investor Claims (Unsolicited Rating)

6.1.1 Overview: the Link between Causality and Recoverable Loss

The causality requirement is important to filter out extensive claims, especially by the investor public. In all jurisdictions considered in this report, the causation chain comprises one or more factual elements and, in addition, one or more normative elements.[258] The relevant tests for factual causation are known as 'but for' or 'conditio sine qua non'. Factual causation serves to filter out non-causal occasions for the loss.[259]

The relevant normative tests are known as 'legal causation', 'scope of liability', or 'scope of protection nexus' (Schutzzweckzusammenhang). Normative elements serve to include and implement policy considerations and value

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255 OLG Düsseldorf, Urteil vom 8.2.2018 – I-6 U 50/17, BKR 2018, 210. Cf. Leyens (n 84), para 140.

256 India p. 386 on Securities and Exchange Board of India, Order in the Matter of Care Ratings Limited (22 September 2020), at [33].

257 India, p. 380 on Jindal Power Limited v. ICRA Limited (2020) 273 DLT 80, at [21].

258 See, e.g., Australia, p. 218 on section 5D(1) of the Civil Liability Act 2002 (New South Wales): A determination that negligence caused particular harm comprises the following elements: (a) that the negligence was a necessary condition of the occurrence of the harm (factual causation), and (b) that it is appropriate for the scope of the negligent person's liability to extend to the harm so caused (scope of liability).

259 See, e.g., Singapore, p. 507.

judgments. Often, such considerations and judgments influence the interpretation of criteria such as 'reasonable reliance' on the side of the plaintiff or 'foreseeability' on the side of the defendant. Many jurisdictions qualify these issues as causality matters. This qualification is not compulsive as shown by a recent decision of the United Kingdom Supreme Court on common law negligence liability, in which the court clarified that scope of duty questions are distinct from causation matters.[260]

In the majority of jurisdictions considered in this report, reasonable reliance is a necessary element of the causation chain: The defendant's conduct must have given the claimant adequate reasons for acting in reliance upon the misstatement.[261] This leads to the essential interdependency between causality and recoverable loss. In essence, one might distinguish between two alternative causality chains. The first requires causality between the rating and the investment decision, also known as inducement and reliance (type 1: transaction causality). The second requires causality of the rating for an excessively high purchase price (type 2: price causality).

Logic suggests that the proof of transaction causality, i.e. reliance on the rating (type 1), should only be required if the investor claims damages in an amount equivalent to the reversal of the transaction, i.e. reimbursement of the purchase price by the CRA in exchange for a transfer of the acquired financial instruments. In contrast, it would make sense to ask whether the rating was causal for an excessively high purchase price (type 2), not for the decision of the investor, if the investor claims the difference between the purchase price paid and the price that the investor would have paid had the information been accurate.

In some jurisdictions, the investor is free to choose between the two options and has to prove causality accordingly, i.e. transaction causality for a transaction reversal and price causality for a recovery of the price difference (types 1 and 2), while in other jurisdictions, damages might be limited to the price difference and still require the proof of transaction causality. It is important to understand the practical differences of these approaches to reevaluate the notorious argument against liability, which is that CRAs should not serve as insurers against market risks. In fact, a transaction reversal could lead to this result because the claim is based on the false information and the resulting erroneous assumption at the time of the transaction. At the time of the reversal, the bond price might have been influenced by many additional factors. To clarify, the impact of a defective rating on the price might be very significant,

260 United Kingdom, p. 602 on Hughes-Holland v BPE Solicitors [2017] UKSC 21.
261 See, e.g., Singapore, p. 507.

let us say 25% while other relevant factors such as geopolitical crisis or a currency decline may have a much stronger influence of up to 75%.

The most prominent doctrinal approach to these problems has been developed in US case law on rule 10b-5, which requires pleading intent to commit fraud, knowledge, or recklessness with particularity and which limits the recoverable loss to the price difference. However, the claim requires proof of reliance which causes major difficulties in practice as it is often not possible to prove whether and how a specific information influenced the investment decision. To overcome insurmountable hurdles of the reliance requirement, the US court of Basic v. Levinson developed the fraud-on-the-market theory.[262] The theory is based on the assumption that, in an efficient securities market, prices are a function of all material information about the issuer and the issue. A material misstatement thus defrauds the entire market and equally affects the reliance of (many) individual investors due to its impact on the price.

For example, Spanish courts have applied an approach that might overcome weaknesses of the traditional understanding of reliance in civil law and common law.[263] Regarding auditor liability, Spanish courts interpreted the causation requirement in terms of probability. This means the courts determined the degree of probability to which the audit report had influenced the investor's decision, in other words, the courts asked how likely it is that the investor would have behaved otherwise if the audit report had been correct.

6.1.2 Specialized Liability Rule

The causation element of art 35a CRAR (EU) consists of three limbs:[264] Firstly, the infringement must have had an impact on the rating result. Secondly, there must be a causal link between the infringement and the claimant's loss. Thirdly the investor must have 'reasonably relied (…) on a credit rating for a decision to invest into, hold onto, or divest from a financial instrument covered by that credit rating.'

The first two limbs concern factual causality. Already, the first limb can be an insurmountable hurdle because the relevant infringements concern work processes or matters of internal organization of the CRA that are not known to the investor.

262 Basic v. Levinson 485 US 224, 243 (1988); Erica P. John Fund v. Halliburton 563 US 1 ff. (S. Ct. 2011); Halliburton v. Erica P. John Fund (Halliburton II) 134 S. Ct. 2398 (2014).

263 Spain, p. 534.

264 European Union, p. 100 et seq.

The third limb 'reasonable reliance' is factual in that it requires reliance and, at the same time, it is normative in that it requires reasonability. The explicit reliance criterion indicates that the EU chose a liability rule of the type transaction causality (type 1).[265] If the investor cannot prove that s/he knew the rating and relied upon its accurateness, a claim for a reversal (rescission) of the transaction or money damages will not succeed.

The normative criterion requires that the investor has 'reasonably relied, in accordance with art 5a (1) CRAR (EU) or otherwise with due care, on a credit rating'. Art 5a CRAR (EU) has been introduced into the CRAR to mitigate the so-called overreliance problem by requiring that, institutional investors in particular 'shall make their own credit risk assessment and shall not solely or mechanically rely on credit ratings for assessing the creditworthiness of an entity or financial instrument'.

The two criteria seem to be incompatible to some part or even mutually exclusive: It is hard to imagine how an investor might be able to prove on the one hand that s/he relied on the defective rating and on the other hand that s/he fulfilled the obligation to make an own credit risk assessment. Observers expect that courts will have (major) difficulties to balance out the two criteria.[266]

According to art 35a para 4 CRAR (EU), the term reasonable reliance shall be interpreted and applied in accordance with the applicable national law.[267] For example, in German case law on general capital market information liability, reliance has been interpreted rather restrictively.[268] An investor will have to prove that s/he exclusively relied on the credit rating when making the investment decision. In most cases, the CRA defendant will counter that the investor based her/his decision also on other sources of information, which will lead to a dismissal of the claim. If, exceptionally, the investor is successful in proving reliance, the claim might still be dismissed because the investor failed to establish that the reliance was reasonable.

The approach of the Chinese specialized liability regime is similar in that it requires a type 1 transaction casualty.[269] As a defense, the defendant may prove that the false statement lacks materiality.[270] It is a special feature of the Chinese liablity regime that the law sets up a presumption under the following

265 See supra section 6.1.1.

266 European Union, p. 100.

267 European Union, p. 89 and p. 91., see also p. 100.

268 Germany, p. 345.

269 China, p. 295.

270 The Misrepresentation Provisions 2022, art 10.

circumstances: (1) the service provider has made a false statement; (2) the plaintiff traded securities directly related to the false statement; (3) the plaintiff acted in this way after the date of implementation of the false statement, the date of disclosure or the date of correction.

On the side of the defendant, five possible circumstances can be applied to rebut the presumption: (1) the plaintiff's dealings occurred before the misrepresentation, or after a correction; (2) the plaintiff knew or should have known that there was a false statement at the time of the transaction, or the false statement had been widely known on the securities market; (3) the plaintiff's trading behavior was affected by other major events such as the acquisition of a listed company, major asset reorganization, etc. that occurred after the implementation of the false statement; (4) the plaintiff's trading behavior constitutes insider trading, securities market manipulation or another securities violation; and (5) other circumstances in which the plaintiff's trading behavior and false statements do not have a causal relationship with the transaction.

6.1.3 Quasi-Contractual Liabilities and General Tort Law

For an investor claim that is based on quasi-contractual liabilities or general tort law to succeed, it is necessary, firstly, to establish that the CRA's negligent or misleading conduct was a material cause of the claimant's loss. Secondly, the additional elements of the causation chain, which are of a normative nature, must be established. It is not surprising that jurisdictions differ with regard to the normative elements.

To start with, in a number of countries the recoverable loss will generally not extend to a reversal of the transaction but be focused on money damages. Reversal of the transaction might require additional pleadings, e.g., in the Netherlands.[271] In other countries, there is no comparable experience. A reversal of the transaction does not appear likely, e.g. in Israel.[272]

To succeed with a common law claim for negligent misrepresentation, it must be shown that the defendant induced (or caused) the representee's decision. Inducement means that the representee relied on the misrepresentation. In most cases, it will be difficult to prove reliance because the plaintiff must present evidence that s/he took notice of the rating and that s/he acted on the basis of that rating. As described, in the United States of America this problem might be overcome by the fraud on the market doctrine.[273]

271 Netherlands, p. 454.
272 Israel, p. 401.
273 Cf. supra 6.1.1.

Courts outside the United States of America do not appear fully convinced of the merits of the doctrine. For example, the Israeli Supreme Court has discussed the doctrine in a context unrelated to CRAs liabilities but neither explicitly accepted nor rejected it.[274] The German Supreme Court in Civil Matters has explicitly rejected it. It also refused to mitigate the difficulties of a plaintiff regarding the burden of proof requirement. For example, the court refused to apply a concept that builds on a generally positive perception of the investment in the market ('Anlagestimmung'). This concept, developed for prospectus liabilities, i.e., for primary market transactions, allows a court to assume a causal effect of the prospectus in cases where the plaintiff cannot prove that s/he read the prospectus. With regard to secondary market transactions, the court also rejected other alleviations of causality such as prima facie evidence.[275] The Austrian Supreme Court in Civil Matters follows this line but it has granted relief if the investor obtained knowledge of prospectus information via a financial services provider.[276]

All jurisdictions considered in this report require an additional normative element, e.g., justifiable reliance on the side of the plaintiff (USA), or foreseeability on the side of the defendant (Israel).[277] Courts in Israel appear to be divided: In an obiter dictum to the Monrov case, it was argued that plaintiffs would not be able to show that, out of a set of information, the rating was the 'but-for' cause of the harm. Accordingly, the plaintiff would fail to prove factual causation. In contrast, the Lavi court found that a CRA should expect that investors will rely on its opinion. Based on this finding, a claim might meet the foreseeability test. A court in the United Kingdom will possibly argue that the (usual) disclaimers impede reliance.[278]

Regarding a claim based on fraud or deceit, a court in the United Kingdom might assume a strong inference or evidential presumption of reliance.[279] However, the claimant must plead an intentionally deceptive statement and provide sufficient evidence. In the United States of America, a rule 10b-5 claim requires pleading intent to commit fraud, knowledge, or recklessness with particularity.[280] Arguably, a claimant will only be successful in proving that a CRA had the required mental state to commit fraud if s/he can point at evidence of red flags, such as an internal memo or e-mail correspondence or evidence of

274 Israel, p. 402.
275 Germany, p. 358.
276 Austria, p. 250.
277 Israel, p. 402.; United States of America, p. 652.
278 United Kingdom, p. 602.
279 United Kingdom, p. 602..
280 United States of America, p. 655.

significant deviations from the ratings process.[281] Such evidence will normally not be available to the plaintiff. It might become available through an investigation by a supervisory authority provided the plaintiff or court is granted access to the findings (infra section 9.4).

Comparable problems concern a claim based on intentional infliction of damage to another person in a manner contrary to good morals (bonos mores), a civil law tort known, e.g., in Germany.[282] However, it is unclear whether a plaintiff must prove transaction causality only for a transaction reversal or also for a recovery of the price difference.[283]

The problem that CRAs should not be treated as insurers against market risk must be tackled independently of the legal basis of the claim. In many of the countries considered, courts will use the normative element of causation to prevent CRAs from being insurers. In Spain, and other civil law countries, the doctrine of 'compensatio lucri cum damno' (compensation for gain with loss) may be used to prevent an undue extension of liability to the insurance of market risks.[284] In Portugal, legislation has enshrined a version of this approach for prospectus liability.[285] In Austria, the outcome will probably be functionally equivalent, but founded on the 'scope of protection nexus' or the lack of an unlawful connection ('Rechtswidrigkeitszusammenhang').[286]

In the United Kingdom and similarly in Singapore, courts are keen to exclude causal factors through the SAAMCO rule.[287] According to this rule, a loss pleaded by the plaintiff will be recoverable only if it falls within the 'scope of the duty' that has been held to apply. Hence, the defendant will be responsible only for the consequences of the particular information being incorrect. The recoverable loss may thus be limited to the difference between the price that the claimant would have offered for the securities in question if he or she had been given the proper credit rating and the price that the claimant actually paid for them.

The situation in Germany appears unclear.[288] As outlined for claims based on art 35a CRAR (EU), German courts tend to require transaction causality, i.e., the plaintiff must prove that s/he relied on the rating when making the

281 United States of America, p. 655 ("smoking guns").
282 S 826 German Civil Code.
283 Germany, p. 347.
284 Spain, p. 539.
285 Portugal, p. 479.
286 Austria, p. 256.
287 Singapore, p. 507 on South Australia Asset Management Corp. v. York Montague Ltd. [1997] 1 AC 191 (English case).
288 Germany, p. 347.

purchase decision.[289] As described, this is not convincing when the plaintiff claims that s/he purchased the securities? for an excessively high price and only asks for compensation of that difference in price. More recent case law shows a growing awareness of the appropriateness of lower hurdles of price causality in insider trading cases (ad-hoc disclosure), but there is doubt whether the insights will be used in cases of expert liabilities such as CRAs' liabilities.

6.2 Causal Chain for Issuer Claims (Solicited Rating)

Since issuers do not invest in securities, the question of reasonable reliance is remote.[290] A claim based on art 35a CRAR (EU/UK) would therefore simply require a causal link between the infringement and the loss.[291]

7 Fault Standard

7.1 Overview: Fault Standard as a Trigger of One-Sided Credit Ratings

In some countries, liability for capital market information may be strict. However, the availability of due diligence defenses blurs the line between a strict liability rule and fault-based liability, especially if fault-based liability is coupled with a fault presumption. Based on the countries considered in the present report, the most common approach appears to be fault-based liability.[292]

In a contract, the fault standard for parties is negligence. The majority of credit ratings is solicited by the issuer (issuer pays model). It follows that under the contract with the issuer, the CRA may face a considerable risk of liability to its contractual partner, depending on possible liability limitations (disclaimers). In contrast, liability risks are comparably low with a view to losses of the investor public if, absent a contractual relationship, the fault standard is intention. It follows that a CRA will focus its efforts on care to avoid losses by issuers rather than losses by the investor public. As agreed in a number of countries, e.g., Germany,[293] this difference in the fault standard causes adverse

289 Supra section 6.1.2.
290 Cf., e.g., Germany, p. 348.
291 European Union, p. 102.
292 E.g. Spain, p. 525.
293 Germany, p. 351.

incentives: CRAs receive significant incentive to unilaterally serve the interests of issuers and to issue overly generous ratings.[294]

For a comparative account, it appears important to understand whether and to what extent the law of a country contributes to the one-sidedness of the incentives of the CRA by employing different fault standards for issuer and investor claims.

7.2 Negligence Liability

In all jurisdictions considered in this report, the liability of CRAs is (widely) framed as fault-based liability. The divide between high risks of liability vis-à-vis the issuer who solicits the rating and low risks vis-à-vis the investor public appears to exist in all countries considered.[295] It is true that the specialized liability rule of art 35a CRAR (EU) and also the Israeli CRA Act[296] set the fault standard at gross negligence as does Chinese law.[297] It is also true that art 35a CRAR (EU) equally applies to solicited and unsolicited ratings, and also equally to issuers and investors, including the investor public. However, firstly, an issuer who has solicited the rating will not sue on the basis of art 35a CRAR (EU/UK) but for breach of contract. Secondly, as shown throughout this report, it is unlikely that an investor will ever succeed with a claim based on art 35a CRAR (EU/UK). This returns the cases to national law.

In the national laws considered in this report, simple negligence serves as the fault standard for quasi-contractual liabilities as known in a number of civil law countries, especially in continental Europe, and also for the common law tort of negligent misrepresentation. Dutch law is perhaps an outlier, as due to the broad discretion of courts it is not clear which fault standard will apply.[298]

7.3 Intent

In all countries considered, the hurdles to liability for intentional acts are high, both in terms of mens rea and the nature of the wrongdoing. This is true for the tort of deceit (fraud) and also for specialised liability rules. The best-known specialised liability rule is the US-American rule 10b-5.[299] It requires that the

294 European Union, p. 111 on the foundations.
295 E.g., Singapore, p. 511.
296 Israel, p. 405.
297 Cf. China, p. 299.
298 Netherlands, p. 453.
299 United States of America, p. 658.

plaintiff proves that the defendant had the requisite scienter, i.e. the intent to deceive, manipulate, or defraud. In addition, the pleading standard for a rule 10b-5 claim is high in accordance with the Private Securities Litigation Reform Act (USA):[300] the complaint must (1) specify each statement alleged to have been misleading, and the reason or reasons why the statement is misleading; and (2) state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind.

Liability for misleading statements under the Australian Corporations Act does not formally require an element of fault, but the plaintiff must show that the CRA knew or ought to have known that the implied representation was false, which brings the fault requirement close to simple negligence.[301]

In some countries, including Germany, non-contractual liability for pure economic loss under general tort law is limited to intentional behavior (with few exceptions).[302] However, professional experts might de facto be liable to third parties for gross negligence. Courts have based expert liabilities on the tort of willful infliction of damages against good morals (s 826 German Civil Code), however, only in cases of recklessness. For example, in 2013, the Federal Court of Justice ruled that an auditor who, against her/his better knowledge, advertises the issuer to salespeople at seminar events breaches his duty of care towards third parties in a particularly serious manner, which leads to tort liability under s 826 German Civil Code.[303]

In comparison, the approach taken in the United Kingdom appears to be more restrictive. The Credit Rating Agencies (Civil Liability) Regulations 2013 (UK) define gross negligence for the purpose of art 35a CRAR as behaviour that exists '(1) […] if the senior management of the credit rating agency were reckless as to whether the infringement occurred. (2) For the purposes of this regulation, the senior management of a credit rating agency are reckless if they act without caring whether an infringement occurs.' A German court would probably categorize such behavior as eventual intention (dolus eventualis). Further, it is surprising that the definition narrows possible misconduct to recklessness of senior management. It has been argued that the statutory regime in effect precludes liability.[304]

300 Section 21D (b) Private Securities Litigation Reform Act (USA): The complaint must '(1) […] specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading […]' and '(2) […] state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind.'.

301 Australia, p. 218.

302 Supra section 4.6.1.

303 BGH, Urteil vom 19.11.2013 – VI ZR 336/12, WM 2014, 17, Juris-para 10.

304 United Kingdom, p. 609.

The FCA as the United Kingdom competent supervisory authority has issued a portfolio letter to the CEOs of UK-registered CRAs in February 2022 that lists serious organizational failings extending to the top levels of CRAs.[305] There is a certain probability of supervisory action which in turn might provide private plaintiffs with information on which they might successfully base their liability claims.[306] This expectation again underlines that the chances of an investor to succeed with a liability claim are small under normal circumstances.

8 Comparative Negligence

8.1 Overview: the Concept of Comparative Negligence

The jurisdictions considered in this report use the legal concept of comparative negligence to take account of the victim's failures with regard to a defective rating. According to this concept, the amount of compensation to be paid by the CRA is reduced by a function that uses the fault of the injurer as a variable relative to the fault of the injured party. In this context, the fault of the injured party lies in a failure to mitigate the loss. A more rigorous concept, not used in the countries considered, is contributory negligence which completely exempts the injurer from liability in case of imprudent behavior of the victim.[307]

Comparative negligence is a general legal concept which is applicable to all sorts of damage claims. The defence of comparative negligence is rooted in notions of equity, corrective justice and fairness. An inherent limitation, e.g., known in Germany[308] and Singapore,[309] relates to claims based on intentional and unscrupulous damage causation. It would be inconsistent and unjust to allow an intentional tortfeasor to make use of the defence. Accordingly, in cases of intentional and unscrupulous damage causation the defendant cannot use the defense.

305 FCA, Portfolio Letter for Credit Rating Agencies, 23 February 2022, https://www.fca.org.uk/publication/correspondence/portfolio-letter-credit-rating-agencies.pdf.

306 United Kingdom, p. 609.

307 For details of the legal concepts, e.g., Germany, p. 354, Israel, p. 406, and United States of America, p. 660 (most Federal States in the United States of America abolished contributory negligence and instead adhere to comparative negligence).

308 Germany, p. 354 on s 826 German Civil Code.

309 Singapore, p. 513.

8.2 Practical Isssues

The concept of comparative negligence has not yet been tested in cases of CRAs' liabilities in the considered jurisdictions.[310] Accordingly, the outcomes are uncertain. It appears generally accepted, however, that the vulnerability of the injured person should be taken into account.[311] Accordingly, the duties of retail investors are less far reaching than those of professional investors.[312] In most countries, e.g., in Austria, a court is likely to assume contributory negligence of a professional investor if the investor could reasonably be expected to recognize that the rating was faulty.[313] With regard to retail investors, arguably, the CRA's misconduct will usually outweigh the other party's failure.[314] This assumption appears particularly convincing in light of the fact that the fault standard for a probabilistic estimate such as a credit rating de facto appears to be gross negligence as a minimum. For example, art 35a CRAR (EU) explicitly limits liabilities to gross negligence. Cases will therefore concern gross negligence on the side of the CRA and often mere negligence on the side of the investor.

Comparative negligence of the victim, if significant, might in principle cause an exemption of liability, e.g., in Türkiye.[315] In particular, the approach taken by art 35a CRAR (EU) reduces the chances of victims of a defective rating achieving a damage award.[316] This is due to a complex interplay of rules of the CRAR (EU): To start with, art 35a CRAA (EU) leaves it to national law to determine the consequences of comparative negligence.[317] In addition, an investor may claim damages under this Article only "where it establishes that it has reasonably relied, in accordance with Article 5a(1) or otherwise with due care" on the credit rating. art 5a(1) obliges financial entities to make their own risk assessments. The rule was introduced to reduce the risks of mechanical reliance on credit ratings, which is seen as one of the causes of the global financial market crisis of 2008.[318] Other investors, in particular retail investors, are

310 E.g., United States of America, p. 660.

311 Singapore, p. 498.

312 Austria, p. 257.; Singapore, p. 498 on the Australian ABN Amro case.

313 Austria, p. 257.

314 Germany, p. 354. Cf. also Singapore, p. 513.

315 Türkiye, p. 572.

316 European Union, p. 100.; Germany, p. 345.

317 Cf. art 35a para 4 CRAR: „Terms such as (…) 'reasonably relied' (…) shall be interpreted and applied in accordance with the applicable national law (…)".

318 Recitals 2, 9 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, OJ L 146, 31.5.2013, p. 1.

obliged to exercise "due care". This rule does not imply that non-professional investors must make their own risk assessments but it stands to reason that they should not exclusively rely on credit ratings when making an investment decision.

Arguably, the approach does not reflect the real-world process of decision making by investors: The purchase of a bond essentially depends on two factors, the interest rate and the probability of recovering the investment when the bond matures (default risk). The interest rate is known to the investor, but not the default risk. The credit rating is needed to factor in the default risk. It is difficult to see how an investor, professional or non-professional, could prove that s/he placed greater weight on other estimates than the credit rating.

In some jurisdictions, e.g., in Austria[319] and Spain,[320] overreliance on credit ratings by a professional investor will likely exclude the liability of the CRA. Conversely, to assume "reliance", a German court would require that the plaintiff proves that s/he solely relied on the rating. This, however, would clearly run counter to the idea of the reasonability requirement of art 35a and 5a CRAR (EU). The criterion of "reasonableness" is intended to prevent excessive reliance on credit ratings, especially exclusive reliance.[321]

9 Burden of Proof

9.1 Overview: the Information Gap of Injurees

In civil liability cases, it is a generally accepted rule that the claimant has the burden of pleading and proving, on a balance of probabilities, any averment of fact that needs to be asserted to establish the liability elements of the claim. To start with, intentional behavior will only be established in the most flagrant cases. Conversely, the legal bases for contractual negligence liability often provides for a reversal of the burden of proof regarding fault. This is also true for quasi-contractual liability, e.g., in Germany. A similar reversal of proof for pre-contractual liabilities is known in common law jurisdictions, e.g., in the United Kingdom under the Misrepresentation Act 1967.[322] Specialized capital market

319 Austria, p. 257.
320 Spain, p. 549.
321 (n 319).
322 United Kingdom, p. 608 on section 2 (1) Misrepresentation Act 1967 (UK): "Where a person has entered into a contract after a misrepresentation has been made to him by another party thereto and as a result thereof he has suffered loss, then, if the person making the misrepresentation would be liable to damages in respect thereof had the

law provisions might also provide for a reversal of proof with regard to fault, e.g., in Türkiye.[323]

The main challenge for the plaintiff with regard to CRA's liabilities relates to pleading the breach of duty. As a prognosis, a credit rating is not necessarily inaccurate even if an issuer defaults that has been given a high investment grade. Every rating envisages a probability of default, and, also a low probability may materialize. Hence, to prove a breach, a plaintiff must establish that the CRA failed to comply with the (procedural) duties applicable to a professional prognosis.[324] As shown above, there are several types of behavior with high liability risks.[325] A breach of duty can result, e.g., from insufficient information, the use of a flawed method, misleading conduct, and conflicts of interest of the CRA.

It is apparent that the plaintiff will usually face a lack of information. There are essentially two possible ways in which the law might deal with structural information gaps. The first concerns possible alleviations of the pleading standard and the burden of proof (infra section 9.2). The second focuses on improving the plaintiff's information basis by providing access to the findings of supervisory authorities (infra section 9.3 and 9.4).

9.2 Relaxation of the Pleading Standard and of the Burden of Proof

Alleviations of the pleading standard or the burden of proof might appear appropriate where there is a in structural shortage of information and evidence on the side of the plaintiff. To plead a breach of duty, the plaintiff regularly needs information that is held by the CRA.

The specialized liability regime for CRAs in China addresses this problem by a presumption of fault of the CRA.[326] In contrast, the liability rule of art 35a (2) CRAR (EU/UK) requires that an injured investor or issuer must "present accurate and detailed information indicating that the credit rating agency has committed an infringement of this Regulation, and that that infringement had an impact on the credit rating issued." During the drafting process, a reversal of proof had been discussed. In its finally adopted version, the provision

misrepresentation been made fraudulently, that person shall be so liable notwithstanding that the misrepresentation was not made fraudulently, unless he proves that he had reasonable ground to believe and did believe up to the time the contract was made the facts represented were true."

323 Türkiye, p. 568.

324 Cf. section 5.1.1 et seq for details of the duty standard.

325 Cf. section 5.3.1.

326 China, p. 297.

was considerably watered down: "What constitutes accurate and detailed information shall be assessed by the competent national court, taking into consideration that the investor or issuer may not have access to information which is purely within the sphere of the credit rating agency." Commentators widely agree that the CRAR (EU) does not provide significant relief to plaintiffs.[327] Within the EU, it therefore hinges on the scope and force of the non-harmonized national civil procedure law whether the structural shortage of evidence on the part of the plaintiff is mitigated.

Courts in some countries might be prepared to facilitate the requirements, e.g. in Portugal, Spain, and, to some extent, also in the Netherlands.[328] One possible way is *prima facie* evidence which alleviates the pleading requirements based on the typical course of events and on the rules of experience. Prima facie evidence, however, can be countered by plausible explanation of why the present case does not follow the usual path. A stronger instrument would be a judicial presumption which results in a reversal of the burden of proof. For example, the capital market legislation in Türkiye[329] sets up a presumption of fault and also a presumption of causality if the bond purchase took place shortly after the publication of a credit rating. However, these options have not yet been tested in a case concerning the civil liability of a CRA.

Austrian and German Courts have only granted relief from the burden of proof in cases of prospectus liability (primary market liabilities), but they have refused to do so in cases that concerned continuing disclosure duties or information provided by intermediaries such as auditors (secondary market liabilities). It should be noted that German and Austrian courts have explicitly refused to apply the US fraud-on-the-market theory.[330] According to the US fraud-on-the-market theory, the element of individual reliance under rule 10b-5 liability can be overcome by proving that the market reacted to the faulty information.

UK courts address knowledge-disclosure gaps by taking a generous approach to pleadings but, as in other countries, it remains unclear under what conditions a court would relieve a plaintiff.[331] In Singapore, arguably, a plaintiff might be assisted by the Evidence Act 1893 which reverses the burden of proof if the question as to whether one party acted negligently will presumably be

327 European Union, p. 103; United Kingdom, p. 608 (modest concession).

328 Portugal, p. 476; Spain, p. 544; Netherlands, p. 450.

329 Türkiye, p. 579.

330 Austria, p. 250.; Germany, p. 358.

331 United Kingdom, p. 608 with reference to Boyce v NatWest Markets plc [2020] EWHC 1264 (Ch) [36]; upheld [2021] EWHC 1387 (Ch).

decided on the basis of a document that is expected to be in the hands of the defendant.[332] The operation of the Evidence Act 1893 is similar to relaxations of the burden of proof in other countries and also subject to similar problems: The investor or issuer must make a prima facie case against the CRA.[333] Mere allegations do not suffice. The investor or issuer must show that the CRA regularly obtains or maintains certain kinds of documents. Against the background of heavy documentation and transparency duties under a specific CRA regulation such as the CRAR (EU), it is highly probable that CRAs keep the relevant documentation available.

To make a prima facie case for a negative requirement appears to be more difficult.[334] For example, the reason for the misstatement can lie in the fact that the CRA failed to consider certain detrimental information, or that it was willfully blind to its existence. As in the United Kingdom, courts in Singapore will consider a number of factors, including the relative ease of discharging the burden of proof.[335]

In Israel, a court rejected a shifting of the burden of proof noting that claims against CRAs are unlike claims against issuers, where such burden-shifting may be possible.[336] The reasoning is not free of doubts.

9.3 Access to the CRA's Internal Documentation

The growing regulation of credit rating services has significantly expanded the duties of CRAs to document their internal procedures, the processes relating to single ratings, as well as the relevant data. Access to the CRA's internal documents would thus alleviate or close the information gap. For example, German courts have developed a doctrine allowing the court to order the defendant to disclose information in exceptional cases where the burden of proof would otherwise be insurmountable for the claimant.[337] Similarly, in Türkiye, the

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332 Singapore, p. 509 on Section 108 Evidence Act 1893 (Singapore, 2022 ed.): 'When any fact is especially within the knowledge of any person, the burden of proving that fact is upon that person'. An example of some relevance is given, namely: 'A is charged with travelling on a railway without a ticket. The burden of proving that A had a ticket is on him or her'.

333 Singapore p. 509 with reference to *Bumi Armada Offshore Holdings Ltd and another v Tozzi Srl* (formerly known as Tozzi Industries SpA) [2019] 1 SLR 10, [35].

334 Singapore, p. 409 with reference to *Surender Singh s/o Jagdish Singh and another* (administrators of the estate of Narindar Kaur d/o Sarwan Singh, deceased) *v Li Man Kay and others* [2010] 1 SLR 428, [220].

335 Singapore, p. 509 with reference to *Yap Son On v Ding Pei Zhen* [2017] 1 SLR 219, [80(b)].

336 Israel, p. 403.

337 Germany, p. 348, on the shift of the pleading burden (sekundäre Darlegungslast).

claimant may file a submission request. If the CRA refuses to present that specific document, the claimant's claim will be treated as proven with regard to the document's content.[338] To be sure, such rules provide an exception and they have not yet been tested in a case of CRAs' civil liabilities.

9.4 Access to the Findings of the Supervisory Authority

In the area of CRAs' liabilities, there is no universally accepted approach to the interaction between public and private enforcement.[339] The jurisdictions considered give different answers to the question whether and to what extent a plaintiff is or should be entitled to make use of findings of the supervisory authority or to rely on the authority's legal conclusions in a civil liability case.

The civil liability under art 35a CRAR (EU) is subject to the infringements listed in Annex III of the regulation, which are also the basis for sanctions by the ESMA, the authority entrusted with the supervision of CRAs within the EU. It follows that the findings and legal conclusions of the ESMA would be of great help for a civil claimant. The CRAR (EU), however, does not foresee access to the findings or ways to introduce conclusions into civil proceedings. The ESMA is a supranational supervisory authority, which might make it more difficult to obtain an injunction requiring the provision of information to a national court in the EU Member States. The resolution of this issue and also the question whether legal conclusions of a public authority are binding for a civil court is a matter for the national law of civil procedure.[340]

Some commentators argue that the ESMA is under a duty to provide information access.[341] In Spain, the party interested in filing a claim may file a request, in advance, to obtain documents held by third parties which are necessary for the preparation of the claim.[342] The relevant concepts, it seems though, are based on a case-by-case assessment.

The US Office of Credit Ratings at the SEC, which regulates NRSROs, conducts annual examinations and publishes summary reports of these examinations on its website. The summary reports do not single out individual rating agencies by name but only by size. A plaintiff will therefore not know whether

338 Türkiye, p. 581.

339 Supra section 2.3.2. on the interplay in general.

340 European Union, p. 104.

341 Portugal, p. 477.

342 Spain, p. 544.

the defendant CRA was found to violate rules and regulations or whether it was subjected to fines or other disciplinary measures.[343]

In other countries, we find a pronounced interaction between public and private enforcement. In the United Kingdom, disciplinary notices and reports of the FCA as the competent authority have proved to be an important source of information for potential claimants in other contexts. It should be noted, however, that this may work both ways: While the plaintiff might profit from the factual findings, a United Kingdom court might hold that the notice or report of the supervisory authority triggered a limitation period based on what claimants investigating with reasonable diligence would have discovered.[344]

In Singapore, a false and misleading statement under the Securities and Futures Act 2001 provides for a special procedure.[345] Under this procedure, the court that convicted the CRA or ordered the payment of a civil penalty fixes a date by which claimants shall bring their claims. Claimants need only to prove the dealing in the respective capital market product, reliance, and the loss suffered.

In Australia, private enforcement appears to be considered as a complement to public enforcement. According to the policy of the competent supervisory authority ASIC, supported by legislation, the authority will generally assist litigants by providing information and documents if requested.[346] ASIC takes the view that (intending) plaintiffs and (intending) defendants are entitled to apply for transcripts of the relevant documents.

As an even more pronounced approach, the Israeli CRA Act vests the ISA as the competent supervisory authority with powers to assist private claimants in the funding of their actions against a CRA.[347] There is evidence that the ISA has actively engaged in assistance regarding the financing of two class actions against a CRA. It is clear that such regulatory funding does not only help plaintiffs to file a suit in a particular case. It also sends a signal to the court that the regulator believes in the merits of the case. Given the complexity of a liability claim against a CRA, it stands to reason to believe that the probability of success of the private action has increased.

343 United States of America, p. 657.

344 United Kingdom, p. 609 with reference to Boyce v NatWest Markets plc [2020] EWHC 1264 (Ch) [36]. Decision upheld [2021] EWHC 1387 (Ch).

345 Singapore, p. 510 on the Sections 199, 234, 236 Singaporean Securities and Futures Act 2001.

346 Australia, p. 229, on ASIC Information Sheet 181: Providing documents and information to private litigants (June 2013).

347 Israel, p. 404..

The follow-up question is whether a civil court will be bound by the findings of a supervisory authority. Generally, such findings do to not have binding effect. Examples can be found in the Netherlands, and probably also Brazil.[348] It is true, that any binding effect would harm the constitutional separation of powers. However, the high specialization and superior understanding of financial market authorities appear to have a significant de facto influence on courts.

10 Liability Limitations (Disclaimers)

10.1 Overview

The jurisdictions considered in this report do not provide statutory liability limitations or exclusions, although there might be limitations with regard to certain claims against CRAs. It is generally agreed, however, that parties to a contract can agree to limit, and, to a certain extent, also to exclude their liabilities. Accordingly, in the case of a solicited credit rating, the CRA and the issuer or investor are competent to limit the CRA's liability by adopting a limitation clause in the rating contract or the rating subscription agreement.

It is less clear whether and how a CRA might limit or even exclude its liability to an issuer that did not solicit the credit rating or to the investor public. In practice, CRAs seek to fully exclude their liabilities by inserting clauses into their standard terms (terms of use) such as:

– "Credit ratings are, and will be construed solely as, statements of opinion of the relative future credit risk (…)."
– "Credit ratings should be weighed, if at all, solely as one factor in any investment or credit decision (…) you will with due care, make your own study and evaluation (…)."
– "Credit ratings and (…) materials are not intended for use by retail investors and it would be reckless and inappropriate for retail investors to use (…) credit ratings or (…) materials when making an investment decision."

It is apparent that CRAs have a legitimate interest in making their liability risks calculable. The cited terms do not raise doubts regarding their legitimacy and effectiveness in as far as they explain the nature of credit ratings in line with common expectations. For example, there is no doubt that describing what a credit rating is – a prognosis or a probabilistic statement – is a legitimate

348 Netherlands, p. 452.; Brazil 3.3.–3.3.

statement. However, CRAs would probably not be allowed to shield themselves against liabilities simply by stating that investors should not rely on a credit rating.

The issues to be discussed concern the permissibility in general (infra 10.2), restraints on the use (10.3), lowering duty standard, lowering the duty standard (infra 10.4), caps that limit the recoverable loss to a specified amount (infra 10.5), and liability exclusions or limitations contained in standard terms (infra 10.6).

10.2 Permissibility of (Implicit) Liability Limitations, Especially Restraints on the Use of the Credit Rating

As a rule, liability limitations, and, to some extent, liability exclusions are permissible in all considered jurisdictions, e.g., the Netherlands.[349] The exceptions to this rule, relevant to CRAs, are rooted in different considerations. In Türkiye, e.g., non-liability clauses are considered invalid even if they only exclude liability for slight negligence in cases where the party is engaged in an activity subject to public approval (authorization).[350] Accordingly, in Türkiye, the permissibility of liability limitations for CRAs appears to be restricted.

Under the specialized liability rule of art 35a CRAR (EU), the limitation must be reasonable and proportionate, and allowed by the applicable national law. Art 35a CRAR (EU) applies to solicited and unsolicited credit ratings. According to its wording, the liability rule allows a CRA to limit, but not to exclude its liability to an issuer who has not solicited the rating or to the investor public although there is no contractual basis. Commentators argue that the European legislator failed to establish clear limits of liability and that it did not stipulate statutory caps on damages.[351] This criticism appears fully justified. Liability caps could have mitigated concerns about negligence liability for pure economic loss, not least by safeguarding insurability (infra section 10.5).

An even more pressing reproach concerns the unclear scope of art 35a (3) CRAR (EU). This criticism also applies to The Credit Rating Agencies (Civil Liability) Regulations 2013 (UK) which, otherwise, appear to succeed in clarifying the criteria 'reasonable and proportionate'. The wording does not make clear whether a CRA may also limit its liability to issuers or investors with whom it does not stand in a contractual relationship. The option to include such a limitation into the rating contract with the issuer would be equivalent to a

349 Netherlands, p. 458.
350 Türkiye, p. 585.
351 European Union, p. 108.

contractual provision that aims to deprive a third party of its rights. Under the national laws considered, contracts to the detriment of a third party are invalid. Considering unsolicited ratings against this background, it does not appear sound to allow a CRA as a potential tortfeasor a right to unilaterally limit its liability.[352]

From a United Kingdom perspective, the landmark decision in Hedley Byrne v. Heller[353] establishes the validity of a disclaimer stipulating that the bank as a professional information provider will not take responsibility for the provided information.[354] However, in the Hedley Byrne scenario, the bank provided the information outside of its regulatory duties. As mentioned at the beginning of this section, parties are, at least generally, free to limit (or expand) their liabilities based on a contractual agreement.[355] Conversely, liabilities under art 35a CRAR (EU) are based on the finding of an infringement of regulatory duties and mandatory. A CRA as potential tortfeasor, naturally, cannot evade mandatory liability by a unilateral act.

Interestingly, it appears that a limitation of liability towards third parties does not cause the same doubts in the United Kingdom as in countries such as Germany. The Credit Rating Agencies (Civil Liability) Regulations (UK) list a number of factors to define duties in a reasonable and proportionate way, i.e. the terms used by art 35a CRAR. There is no case law yet. It should suffice to understand that 'a clause in a non-consumer contract has little prospect of being found to be unreasonable unless the balance of the parties' relationship is, in substance, closer to the usual consumer situation'.[356]

The bottom line appears to be that a person (the CRA) cannot unilaterally exclude liability for its conduct. This position is likely to be taken in Australia, and Portugal.[357] Under the French Civil Code, a clause that deprives a debtor's essential obligation of its substance will be deemed void.[358] Arguably, French courts will be reluctant to apply this rule with regard to the liability limitations typically employed by credit rating agencies.

352 European Union, p. 108 on possible exceptions.

353 (n 9).

354 European Union, p. 108.

355 European Union, p. 108 cites the famous lines of Lord Devlin: "A man cannot be said voluntarily to be undertaking a responsibility if at the very moment when he is said to be accepting it he declares that in fact he is not."

356 United Kingdom, p. 614.

357 Australia, p. 233; Portugal, p. 481.

358 France, p. 321, on art 1170 French Code Civile.

10.3 Explicit and Implicit Liability Exclusions, Especially Restraints on the Use of the Rating

Explicit liability exclusions are invalid under art 35a CRAR (EU), as in many other jurisdictions such as, e.g., Australia. However, defining the duties of CRAs can ultimately lead to a liability exclusion, either by the CRA itself or by law. The most intriguing example for the latter is Australia where the rating industry has been divided by legislation into two branches, out of which only one provides credit ratings to retail investors.[359] CRAs which, in the majority, are not licensed to provide credit ratings to retail investors are, in principle, protected by regulation against claims by the investor public.

Regarding the remaining risks of liability of Australian CRAs to wholesale investors, observers have noted that the Australian courts interpreted the liability disclaimers restrictively in the ABN AMRO case.[360] However, in the ABN AMRO case, the CRA knew that the rating would be used by a narrowly defined class of investors. It was therefore reasonable for the court to argue as follows: "The disclaimer was not directed to, and objectively would not be understood to be directed to, the representation necessarily conveyed by the statement of opinion – that S&P had reasonable grounds for the opinion or exercised reasonable care and skill in forming the opinion".[361]

In some jurisdictions, e.g., the Netherlands,[362] a privately stipulated restriction regarding the parties that are legally entitled to make use of the credit rating will generally be respected by a Dutch court, but it might also be challenged on grounds of reasonableness and fairness.

The United Kingdom Unfair Contract Terms Act 1977 contains certain 'anti-avoidance' provisions that in principle could be used to argue that a redefinition of duties aims to achieve a liability exclusion which is not permissible.[363] Nevertheless, courts appear reluctant to interfere. One reason is that the 'anti-avoidance' provisions are generally considered not to apply to terms that merely describe one party's primary obligations to the other. Another reason is that disclaimers tend to pass the test fairly easily if they are well-established in commercial practice and represent the normal basis on which transactions take place. It is not entirely clear, however, whether

359 Australia supra section 2.2.3.
360 Singapore, p. 515 et seq on the licensing approach in Australia see infra 2.2.3.
361 Australia, p. 233, with reference to ABN Amro Bank argued: NV v Bathurst Regional Council (2014) 224 FCR 1, [607, 609].
362 Netherlands, p. 458.
363 United Kingdom, p. 618 on sections 3(b) and 13 Unfair Contract Terms Act 1977.

and how a court would look at the regulatory duties under the assimilated EU CRAR as a yardstick to define acceptable commercial practice under the criterion of reasonableness.

Other countries, such as Israel, appear to take a clearer position against a possible effect of a disclaimer as an 'assumption of risk' defense against investors. Based on the legislative history of the Israeli specialized CRA legislation, a court is unlikely to accept a disclaimer against CRAs' basic duties to conduct ratings in good faith and on an informed basis.[364] The difference only becomes clear on closer examination: In the United Kingdom, a CRA will probably be able to define its credit ratings in a way that excludes reasonable reliance. As a consequence, a court will dismiss a damage claim. In other countries, such as Israel, a court might disregard a disclaimer excluding reliance on a credit rating in an investment decision which states that a credit rating may not be taken into account when forming an investment decision. As a consequence, the scope of possible effects of a disclaimer is considerably reduced.

10.4 Lowering the Duty Standard

A lowering of the duty standard, e.g., with regard to methodology or data reliability, and/or the applicable fault standard, simple or gross negligence, is another form of evading liability for faulty prognoses. In Israel, the specialized rules on CRAs preclude CRAs from lowering the duty standards that apply to credit ratings directed at the investor public.[365] Similarly, in some countries, e.g., Türkiye,[366] and the Netherlands,[367] lowering the duty standard or elevating the applicable fault threshold is unlikely to benefit the CRA because of the regulatory recognition requirements and/or because regulatory standards are considered part of the public order and, as such, cannot be contractually reduced or amended. In the United Kingdom, the reasonableness test under the Unfair Contracts Terms Act 1977, in principle, applies to terms that exclude or substantially modify relevant obligations or duties beyond what can be reasonably expected.[368] It seems, however, that courts give these provisions a quite limited application with a view to not interfering with commercial certainty. From an Australian perspective, the terms on which a rating is provided

364 Israel, p. 406.
365 Israel, p. 406.
366 Türkiye, p. 585.
367 Netherlands, p. 452.
368 United Kingdom, p. 618.

and the explanatory materials that accompany it are significant for determining whether the person receiving it was misled.[369]

Against this background, it is not entirely clear how courts in the United Kingdom or in Australia would treat a case such as the MS Deutschland, Germany 2021, in which a CRA was held liable that included a note into its rating report that the credit rating was based exclusively on one piece of information, the report of an auditor.[370] The German court held the CRA liable for negligence.

10.5 Caps that Limit the Recoverable Loss to a Specified Amount

Specifying maximum amounts of damages contributes to the calculability of liabilities and can make it easier to take out insurance. In the context of art 35a CRAR (EU), the recoverable loss can be limited to a specified amount, provided the cap passes the proportionate and reasonableness tests.[371] In many jurisdictions, e.g., the Netherlands,[372] professional service providers seek to cap their liability at the fee agreed with the client or, alternatively, the amount covered by the insurer. Dutch courts will typically not challenge those clauses.

It appears that liability caps will also withstand a judicial control of standard terms under, e.g., the Unfair Contract Terms Act 1977 (UK).[373] This seems to be the general position amongst the countries considered in this report.

10.6 Liability Exclusions or Limitations Contained in Standard Terms

Liability limitations or exclusions will usually be found in standard terms (terms of use). Jurisdictions take different approaches to the judicial control of standard terms in general. For example, from an Australian perspective, liability limitations and standard terms are considered in the in the factual context of the claim.[374] In essence, the judicial control of standard terms relies on a comparison of the chosen term to what is common with regard to a specific type of contract, service, or transaction.

As far as can be seen, The Credit Rating Agencies (Civil Liability) Regulations 2013 (UK) are the only example for a specific provision on this: 'A limitation of liability is not likely to be reasonable and proportionate if the credit

369 Australia, p. 233.

370 Germany, p. 354, on LG Berlin, Urteil vom 5.5.2020 – 11 O 5/19 (MS Deutschland), WM 2021, 444.

371 United Kingdom, p. 614.

372 Netherlands, p. 452.

373 United Kingdom, p. 614.

374 Australia, p. 233.

rating agency fails to take reasonable steps to bring the limitation to the attention of investors.'[375] It is not entirely clear how this provision further narrows the permissibility of standard terms vis-à-vis the more general judicial control under the Unfair Contract Terms Act 1977 (UK). It appears, however, that a CRA 'would be well advised not to bury exclusions and limitations too deeply in the small print.'[376]

German courts might possibly be more inclined to consider a standard term invalid which denies the duty of the CRA to produce the rating with due care.[377] The position in other EU Member States with regard to standard terms is similar, as far as it concerns consumer contracts. The similarities (not identity) of the applicable provisions is a consequence of the European Directive on Unfair Standard Terms in Consumer Contracts of 1993.[378]

11 Time Limitations

Time limitations play an important role in civil liability. Jurisdictions differ with regard to the details, especially where contractual liabilities are concerned.[379] The pivotal question, however, concerns non-contractual liabilities towards the investor public. Specialized liability regimes operate on the basis of comparatively short statutes of limitation. General statutes of limitation range around 3–6 years.[380]

12 Main Findings

12.1 The State of the Discussion

12.1.1 Public Regulation Triggers CRAs' Civil Duties

Credit ratings are forwardlooking opinions on the relative probability of default of a bond or a bond issuer, including an issuer state. Investors know about the interest rate of a bond. The information asymmetry and information uncertainty

375 United Kingdom, p. 615 on Section 12(3) The Credit Rating Agencies (Civil Liability) Regulations 2013 (UK).
376 United Kingdom, p. 620.
377 Germany, p. 356 (on s 307 German Civil Code).
378 Portugal, p. 481 on Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contract, OJ L 95, 21.4.1993, p. 29.
379 Germany, p. 357 (3 years); Portugal, p. 484 (20 years).
380 Germany, p. 357 (3 years); United States of America, p. 663 (up to 6 years).

concerns the default risk. The default risk explains the probability of the bond being paid upon its maturity. It is one of two pieces of information needed to buy a bond. It is precisely this aspect which can be provided by a CRA.

Without reliable information on the default risk, we must expect a development along the lines of Akerlof's lemon market: information asymmetries will not be overcome (at cheap cost), best guesses serve as an incomplete substitute, prices are drawn in a downward spiral, good issuers disappear, only bad bonds remain on the market. This would mean an obvious loss in the efficiency of finance as a resource.

Credit ratings have also served a regulatory function for a long time. Financial institutions are entitled to use external ratings of CRAs to determine the amount of their regulatory capital, corporations are dependent on positive credit ratings to keep their cost of capital low. Nevertheless, until one or two decades ago, CRAs were largely unregulated. There have been several triggers for regulation, most importantly the global financial market crisis of 2008.

Today, CRAs have become a regulated industry in all countries considered in this report. This means they are supervised by state authorities with far-reaching sanctioning powers. It appears universally accepted that civil liability will (at best) serve as a complement to public enforcement. Very few jurisdictions, e.g., China, and the EU, have set up specialized rules for the civil liability of CRAs.

Conversely, public sanctions are in place and there are many examples of public enforcement. The most prominent concerns the investigations and law suits of the US-American Department of Justice in 2013 against two of the three internationally leading CRAs, Standard & Poor's and Moody's. These suits led to billion-dollar settlements (FIRREA settlements). The size of the compensation payments gives an idea of the dimension. The fact that two of the three leading CRAs were sued indicates that the problems of non-compliance are not limited to individual or insignificant rating agencies. They concern the market for credit ratings as such.

Assessments may differ in detail but there is no doubt that the emergence of regulatory duties has shaped today's understanding: CRAs are subject to a set of civil duties applicable to professional probabilistic statements. Failure to comply with those duties, in principle, can give rise to civil liability.

12.1.2 Civil Courts: Case Law on CRAs' Civil Liabilities Is Emerging

There are very few court decisions on CRAs' liabilities so far.[381] For a long time, CRAs were considered to be shielded against liability under the freedom of

381 Supra 3.1. et seq. for a summary.

speech defense. The elements of the newly introduced special liability provisions in the EU have not yet been tested by courts. CRAs try to avoid creating precedent. Most cases are settled outside the courtroom.

In the United States of America, the Abu Dhabi case of 2009 was one of the first that denied the free speech defense (1st amendment defense). The case concerned a structured financial product that was targeted to a small pool of investors. A few years later, the international debate was intensified by the Australian judgement in ABN AMRO of 2014. The court held that Standard & Poor's was liable to a class of investors who had not solicited the rating on the basis of the common law tort of negligent misrepresentation.

In China, one of the leading Asian CRAs, Dagong Global Credit Rating Group, was held liable in 2020 together with other intermediaries, e.g. auditors, for a violation of securities laws by making false or misleading statements. In Germany, courts are divided. The High Court of Düsseldorf denied liability of a CRA for an issuer rating in 2018 for lack of proximity to investors. In contrast, the district court Berlin held a CRA liable for an issue rating (MS Deutschland) in 2001. The court applied concepts of quasi-contractual liability, which are established in a number of civil law jurisdictions. Similarly, the two leading cases in Israel do not establish a clear line on CRAs' liabilities.

All judgments of liability concern credit ratings that were excessively high or low, made out of the blue, or evidently flawed for other reasons. In many cases in the named countries and elsewhere, courts have explicitly argued that they abstain from judicial control, review or intervention if an opinion is plausible on the facts, and neither arbitrary nor mala fide.

12.1.3 Policy: Securing the Integrity of Credit Ratings by Public Regulation or Civil Liability?

Since their emergence in the 19th century, CRAs have contributed to an increase of people's wealth. Infrastructure projects such as canals and railways in the United States of America would not have been completed in the same time, if at all, without finance by foreign investors from far away. The way in which credit ratings of the project companies have enabled global finance is a sub-function of financial intermediation and hence an essential element of a modern division of labor. Despite all justified criticism, which has been the focus of the present report, there is no evidence that the concept of private credit ratings is per se flawed.

In response to investor expectations, it has become common practice that bonds are rated by at least two rating agencies. In the course of time, CRAs have become an indispensable private gatekeeper. The use of private credit ratings for regulatory purposes, especially in banking regulation, has gone too far (over-reliance problem). There have been attempts to turn back the clock especially in the United States of America and in the European Union, but external credit ratings still serve as the most important yardstick of creditworthiness. The only way forward appears to be to hold CRAs accountable in a way that reflects their importance for financial markets.

There is general agreement that civil liability might contribute to achieving this goal, but, more importantly, powerful oversight and public enforcement by supervisory authorities are needed. A somewhat hidden but very important problem of specialized liability regimes, such as art 35a CRAR (EU), is a possible reversal or weakening of positive effects of regulation. Such adverse effects might occur in particular where liability risks towards the issuer who solicits the rating and who pays for it are high (simple negligence) while the risks of liability to the investor public are low (gross negligence or even intent). Clearly, it is the investor public that will suffer from overoptimistic credit ratings.

Each of the elements of a liability claim that have been discussed throughout this report can alleviate this problem, but they might also deepen it. The main requirement is to strike a balance between the legitimate interests of rating agencies in calculable liability risks on the one hand and the equally legitimate compensation interests of aggrieved investors on the other. The most important prerequisite for this is to prevent one-sided ratings.

12.2 Elements of the Liability Claim

12.2.1 Legal Basis of Liability

An issuer who solicits the credit rating, in theory, may claim damages if the CRA breaches the rating contract.[382] Equally, an investor who solicits the rating or is a subscriber can sue the CRA on a contractual basis. It appears realistic to assume that today, a breach of contract can be proven on the basis of the evolved professional duties if the assessment is excessively pessimistic or optimistic.

However, despite tightened regulation disagreement may still be resolved discursively before the credit rating is published. This option significantly reduces the likelihood of an issuer suing the CRA. Downgrades tend to occur too late rather than too early and are therefore less likely to give rise to major liability issues.

382 Supra 4.1. et seq.

The main issue concerns liabilities of the CRA towards the investor public. Investors who suffered a loss from an excessively optimistic rating can base their claim on a specific liability rule (China, EU), or on general civil law, including quasi-contractual liability, i.e. a form of invoking special trust or a contract which has a protective effect vis-à-vis third parties, as known in civil law jurisdictions (e.g., Austria, Germany, Portugal, Türkiye), and mixed legal systems (e.g., Israel), the common law tort of negligent misrepresentation (e.g., Australia, Singapore, United Kingdom, United States of America), on the universally recognized tort of deceit (fraud), or the tort of intentional infliction of damage on another person in a manner contrary to good morals (bonos mores), which is known in civil law jurisdictions (e.g., Austria, Germany, Portugal), but appears to find a functional equivalent everywhere.

12.2.2 Eligible Claimants

Court decisions that are based on concepts of quasi-contractual duties or negligent misrepresentation, have, up to now, concerned credit ratings of initial issues (primary markets). A CRA might provide a credit rating, either of the issuer (issuer rating), or – more commonly – of the bonds (issue rating), or of both. It is characteristic for a primary market transaction that the group of investors who will be affected by the rating is at least identifiable for the rating agency. Conversely, a secondary market transaction concerns a sale from one investor to another. A CRA might provide its credit rating on a regular basis, again, either as rating of the issuer, or of the (existing) issue, or of both. The rating grade is an important factor for the terms of the transaction and it (heavily) influences the price. In contrast to a primary market transaction, it is characteristic for a secondary market purchase of a bond on the market that the investors who might be affected by the rating are not known or identifiable as a group by the CRA.

In sum, the risks of a CRA to be held liable for negligence concern primary markets while the risks are rather negligible in secondary markets. This is in line with the landmark cases Caparo (UK) and Ultramares (USA) which explained that statutory auditors may be liable for a negligent breach of the duty of care to an identified or identifiable audience, while they do not owe duties to the investor public.

According to these cases and also to their counterparts in other jurisdictions, the essential elements of the liability tests of quasi-contractual liability or negligent misrepresentation relate to proximity and reasonable reliance.

12.2.3 Causality and Recoverable Loss

The causality requirement serves to filter out liability claims by the investor public.[383] The relevant tests for factual causation are known as 'but for' or 'conditio sine qua non'. In addition, causality embraces a normative element. The relevant tests are known as legal causation, scope of liability, or scope of the protection nexus (Schutzzweckzusammenhang). Reasonable reliance appears to be the most widely used criterion.

Out of the elements of causation under art 35a CRAR (EU), 'reasonable reliance' is the most problematic factor. This is due to the CRAR approach, which requires that an investor, to act reasonably, must make an own credit risk assessment. Defendant CRAs will argue that the rating was not the 'but for' reason or the 'conditio sine qua non' of the investment decision. Courts will presumably have difficulties in balancing out reliance against reasonability. It appears that the causality requirement under art 35a CRAR (EU) may systematically prevent an investor claim from being successful.

In Australia, most CRAs operate on a license which allows them to provide their ratings only to wholesale investors, not to retail investors.[384] Accordingly, the regulation of credit ratings in Australia prevents reasonable reliance by retail investors. CRAs around the world state/specify in their standard terms and descriptions of their assessments that their credit ratings may not be used for investment decisions. Whether this (fully) refutes reasonable reliance is a question to be considered in the context of liability limitations (below).

12.2.4 Burden of Proof

The burden of proof is another important filter that shields CRAs from excessive liabilities towards the investor public. Under art 35a CRAR (EU/UK), the national courts shall take "into consideration that the investor or issuer may not have access to information which is purely within the sphere of the credit rating agency." It appears that courts inside and outside of the EU are reluctant to shift the burden of proof. United Kingdom courts mitigate knowledge disclosure gaps by taking a generous approach to pleadings but, as in other countries, it remains unclear under what conditions a court would relieve a plaintiff.

383 Supra 6.1.1. et seq.
384 Infra 2.2.3 for details.

The Singapore Evidence Act 1893 offers an interesting, but so far untested, solution. It reverses the burden of proof if the question as to whether one party acted negligently will presumably be decided on the basis of a document that is expected to be in the hands of the defendant. As a result of the regulation of credit ratings, the documentation obligations of CRAs have been expanded. Arguably, a failure will be apparent from the CRAs documentation.

For civil liability to succeed, it would be a very promising approach to give plaintiffs or courts access to the findings of the supervisory authority. It appears that many jurisdictions are rather reluctant to do so. The tensions regarding data protection, e.g., are palpable.

12.2.5 Fault Standard

The fault standard under art 35a CRAR (EU/UK) is gross negligence. For quasi-contractual liability and negligent misrepresentation, the standard of fault is simple negligence. However, since a rating is a prognosis and the CRA's duties are procedural in nature, the de facto standard of fault appears to be gross negligence in general. As we have seen, in secondary markets, a CRA will usually only be liable for intentional wrongs. The element of fault therefore highlights the adverse divide of incentives: The CRA faces a considerably higher risk to be held liable by the issuer for a breach of its contractual duties than towards the investor public. It appears fully rational for a CRA to tend to overoptimistic ratings.

12.2.6 Liability Limitations

Liability limitations serve the legitimate interest of CRAs to make their liability risks calculable. In practice, CRAs seek to free themselves from any liability by emphasizing that their credit ratings are solely statements of opinion, that they should be weighed, if at all, solely as one factor in any investment or credit decision, that users must make their own study and evaluation, or that it would be reckless and inappropriate for retail investors to base their investment decision on a credit rating.

Liability exclusions appear to be invalid. Limitations are permissible in most countries if they are reasonable and proportionate. It is still unsettled whether art 35a (3) CRAR (EU) permits the limitation of liability towards the investor public unilaterally and/or by means of the rating contract. Under the national laws of many EU Member States, including Germany, contracts to the detriment of a third party are invalid. The Credit Rating Agencies (Civil Liability) Regulations (UK) appear to allow limitations of liability to the investor public provided the CRA takes reasonable steps to bring the limitation to the attention of investors.

The most difficult question concerns the possibility/permissibility of a modification of duties. There is no universal answer. In the United Kingdom, a court might be more prepared to accept that a CRA defines its credit ratings in a way that excludes reasonable reliance. In other countries, such as Israel, a court might disregard the disclaimer with a view to the basic question of whether a credit rating may be taken into account when forming an investment decision. In the Australian ABN AMRO case, the court found that the disclaimer could not be understood to exclude the duty of reasonable care and skill in forming the opinion. It is likely that, for example, a German court would equally deny its effect. Germany and other EU Member States generally provide for a judicial review of general terms and conditions.

12.3 Outlook

The future of civil liability for rating agencies is difficult to predict. Only around two decades ago, credit ratings were mainly considered to be free opinions, a category that is not adequate for professional statements. The expanding regulation of CRAs in reaction to the global financial crisis of 2008 has helped to shape the civil duties of CRAs. In particular, CRAs were forced to professionalize their processes and staff. Civil liability might be a useful supplement to regulation.

In order to make progress, it would be advisable to take a more realistic approach towards investment decisions on bond purchases. The default risk measured by a credit rating concerns the most important (the only?) information asymmetry for which CRAs are required. It follows that a CRAs must accept that the value of their services depends on this insight. To take this one step further, they must accept responsibility for their services, including civil liability. The long-standing debate on negligence liability for pure financial loss might be developed further on this basis. It is an unresolved problem how over-deterrence and chilling effects can be avoided. The options include, e.g., (statutory) liability caps which would be insurable. In the jurisdictions considered, such options have not yet been explored in great detail.

As a final thought, the many differences between the jurisdictions, together with structural weaknesses of civil liabilities might make it advisable to place greater emphasis on regulation and sanctioning by authorities. In the larger context, the challenge consists in developing a liability concept tailored to information intermediaries, and taking into account the special role of gatekeeper intermediaries such as CRAs.

Future discussions might extend to upcoming industries such as ESG ratings.[385] Such new information intermediaries may be expected/are likely to follow a development path similar to CRAs. This is all the more true in a regulatory environment that introduces new rating factors such as sustainability.

The findings of this report show that some progress has already been made, and that there is a certain basis for handling new challenges, but it has also shown the need for further development with regard to CRAs' civil liabilities.

385 On the discussion, see, e.g., Singapore, p. 517; United States of America, p. 667.

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