Revoking the License of Brickwork Ratings

Why in news?

Securities Exchange Board of India (SEBI) has revoked the licence held by Brickwork Ratings and asked it to wind down its credit rating operations within six months.

What are credit rating agencies?

- Credit Rating Agencies (CRA) are agencies that assess the creditworthiness of organisation, individual or entity and assign ratings to it.
- They take into consideration several factors like the financial statements, level and type of debt, lending and borrowing history, ability to repay the debt, and the past debts of the entity.
- The entities that are rated by credit rating agencies comprise companies, state governments, non-profit organisations, countries, securities, special purpose entities, and local governmental bodies.
- In India, CRAs are regulated by SEBI (Credit Rating Agencies) Regulations, 1999 of the Securities and Exchange Board of India Act, 1992.
- **Brickwork ratings**- Brickwork is one of the SEBI-registered credit rating agencies in India.
- It is also a Reserve Bank of India (RBI) accredited credit rating agency.

The SEBI registered credit rating agencies in India are

1. *ICRA Limited*
2. *Credit Rating Information Services of India Limited (CRISIL)*
3. *Acute Ratings & Research Limited*
4. *Credit Analysis and Research Limited (CARE)*
5. *Infomerics Valuation and Rating Private Limited*
6. *Fitch India*

What is the significance of the rating?

- **Informed decisions-** It provides additional inputs to the investor following which the investor analyses and takes a sound investment decision.
- **Serves as benchmark**- The credit ratings that are given to the entities serve as a benchmark for financial market regulations.

- **Determination of borrowing rate of companies**- A higher rating means that the company is deemed worthy of credit.
- So, investors will be willing to lend money at a lower interest rate.
- **Approval of loans**- It helps banks and investors decide about approving loan applications and the rate of interest offered.

How is credit rating different from credit score?

- **Credit rating**- A credit rating is used to determine the creditworthiness of a business or a company rather than individuals.
- The rating is usually shown as a series of alphabetical symbols.
- It is calculated using corporate financial instruments.
- **Credit score**- A credit score is a number, usually between 300 and 900, that is given to individuals to rate their creditworthiness.
- It is calculated by credit bureaus based on the person's credit information report.
- It plays a role in determining whether or not they are approved for loans and credit cards.

What is the SEBI's recent order about?

- The SEBI issued a winding-up order against Brickwork Ratings on because of major lapses in the credit rating agencies' operations.
- SEBI issued the order to shut down the agency in 6 months.

Reasons

- The Brickwork Ratings did not exercise proper skill, care, and diligence, while discharging its duties as a credit rating agency.
- The Brickwork Ratings lacked a surveillance mechanism for tracking the interest/ principle repayment schedule of issuers
- This in turn led to inaccurate ratings.
- Brickwork also failed to review the rating of non-convertible debentures (NCDs) of Great Eastern Energy Corporation after another credit rating agency downgraded the NCDs in 2017.
- Brickwork has been delaying or not recognising the default of NCDs of several companies.
- Other reasons include the agency's
    - Failure to independently assess issuer projections
    - Not taking banker feedback
    - Incomplete rating releases
    - A rating committee member having a business development role

What are the implications of the SEBI's move?

- The move shrinks the choice of rating agencies available to issuers from seven to six.
- It also casts doubt on the reliability of credit ratings for over 8,699 instruments which were under Brickwork's coverage at the time of the order.

- This order has implications not just for Brickwork but also for other rating agencies, bond issuers and investors at large.

References

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