

# Sebi moves against 3 rating agencies over IL&FS fiasco

Action against agencies comes as they failed to warn investors about firm's credit profile

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**A** Securities and Exchange Board of India (Sebi) investigation of the role of ratings agencies in the Infrastructure Leasing and Financial Services Ltd (IL&FS) crisis found them lacking, chairman Ajay Tyagi said, adding the regulator has now begun adjudicating proceedings against the agencies.

Tyagi, who spoke to journalists after a meeting of the Sebi board, did not name the rating agencies.

"This (Sebi proceedings) comes after the agencies failed to warn investors in time about the deteriorating credit profile of IL&FS," said a Sebi official, seeking anonymity.

However, India Ratings & Research, ICRA, and Credit Analysis and Research Ltd (CARE), had given IL&FS the highest rating of AAA, even when its subsidiary, IL&FS Transport Networks, defaulted in June. There was also an abrupt downgrade in the ratings of bonds sold by IL&FS and related entities, after they defaulted on payment obligations in September. Credit rating agencies (CRAs) had downgraded the bonds from high investment grade (AA+ in some cases) to default or junk.

To stem systemic risk due to bond papers, the regulator on Wednesday allowed mutual fund houses the facility of a so-called "side-pocket", wherein liquid schemes can separate their risky securities from the rest. Mint had first reported the proposal earlier this month.

This will be based on major credit events at the issuer level such as



## Capital market regulator looks to close loopholes

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impeding defaults. The enabling provision was optional for mutual funds and needs to be approved by the trustees and regularly monitored for recovery of affected assets. "There will be additional safeguards so that this provision is not misused," said Tyagi, adding that the decision will protect retail investors.

Sebi will also issue a framework for valuation of debt papers when debt schemes invest in them. "We are looking at papers with 60-day maturities and how to value papers when they fall below default or investment grade,"

said Madhabi Puri Buch, a whole-time member of Sebi.

The regulator is also in consultation with the Association of Mutual Funds in India and the industry on

ensuring better information flow from issuers. "We are in consultation with the Reserve Bank of India (RBI), issuers of debt papers, credit rating agencies and mutual funds to have more disclosures about the basic characteristic of the paper and trading history. The discussion is right now on 'how and when'. But it will be calibrated and not a knee-jerk reaction," said Buch.

**Sebi is also in consultation with the AMFI and the industry on ensuring better information flow from issuers**

"The bond market is largely an opaque market due to the institutional nature with transactions being done between counter parties. So, the price discovery is not exactly optimal," said Kaustubh Belapurkar, director of fund research at Morningstar Investment Adviser India Pvt. Ltd.

Fund houses largely rely on ratings given by rating agencies for investing in bonds. Other decisions taken by the regulator include relaxing the offer-for-sale framework to companies with more than ₹1,000 crore of market capitalisation, relaxing norms for clubbing of FPI limits and relaunching the start-up platform with a new name, "innovators growth platform".