SQUIRE PATTON BOGGS

New EU Legislative Proposal on ESG Ratings

EU – July 2023

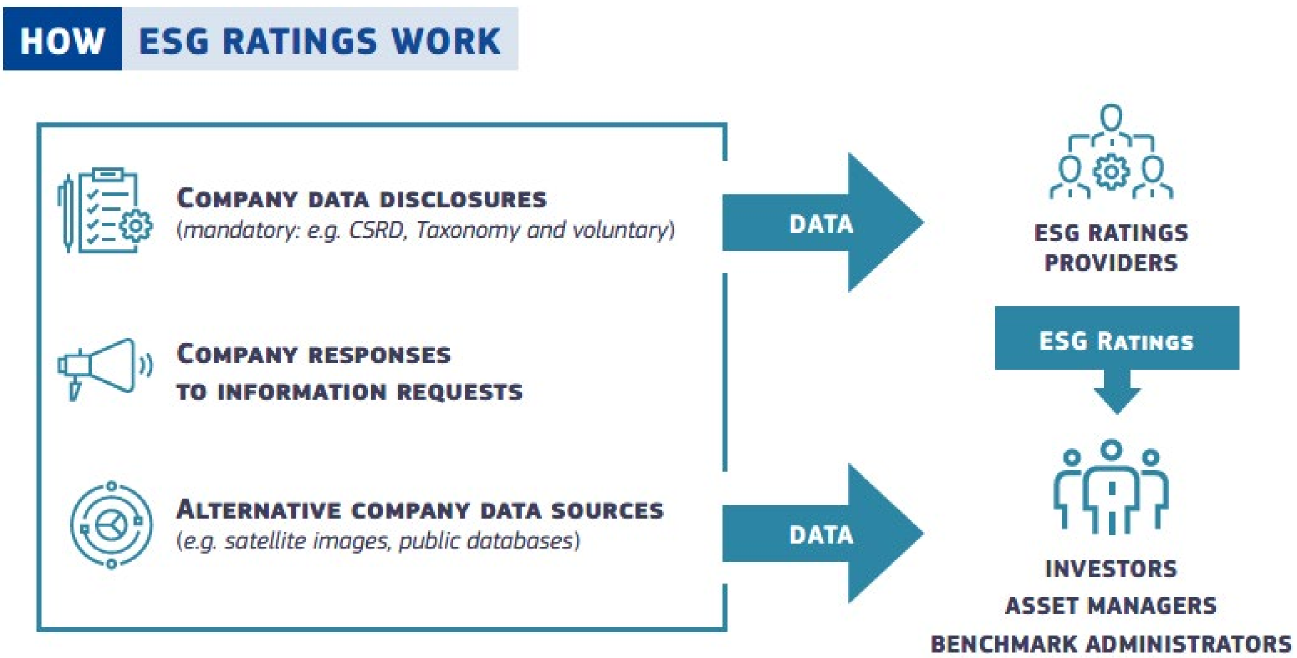
On June 13, 2023, the EU Commission (EC) proposed a new [regulation to regulate environmental, social and governance (ESG) rating providers] that operate in the EU.
The EC seeks to address a lack of transparency and consistency in the ESG rating market, which is expected to grow substantially in the coming years. The inefficiencies include a lack of transparency regarding the characteristics of ESG ratings, their methodologies, data sources and how ESG rating providers operate more generally. Currently, the EC thinks that ESG ratings do not sufficiently enable users, investors and rated entities to take informed decisions. The EC wants companies to get better clarity on the way they are rated.

All ESG rating providers will, in future, need an authorization from the European Securities and Markets Authority (ESMA), which is based in Paris. The authorization shall also increase the quality and reliability of their services, to protect investors and ensure market integrity.

The EC proposal will, however, not harmonize the methodologies used for the creation of ESG ratings, in order to ensure a variety of approaches and choices in the ESG ratings market (i.e., ESG ratings may differ among themselves and cover different areas).

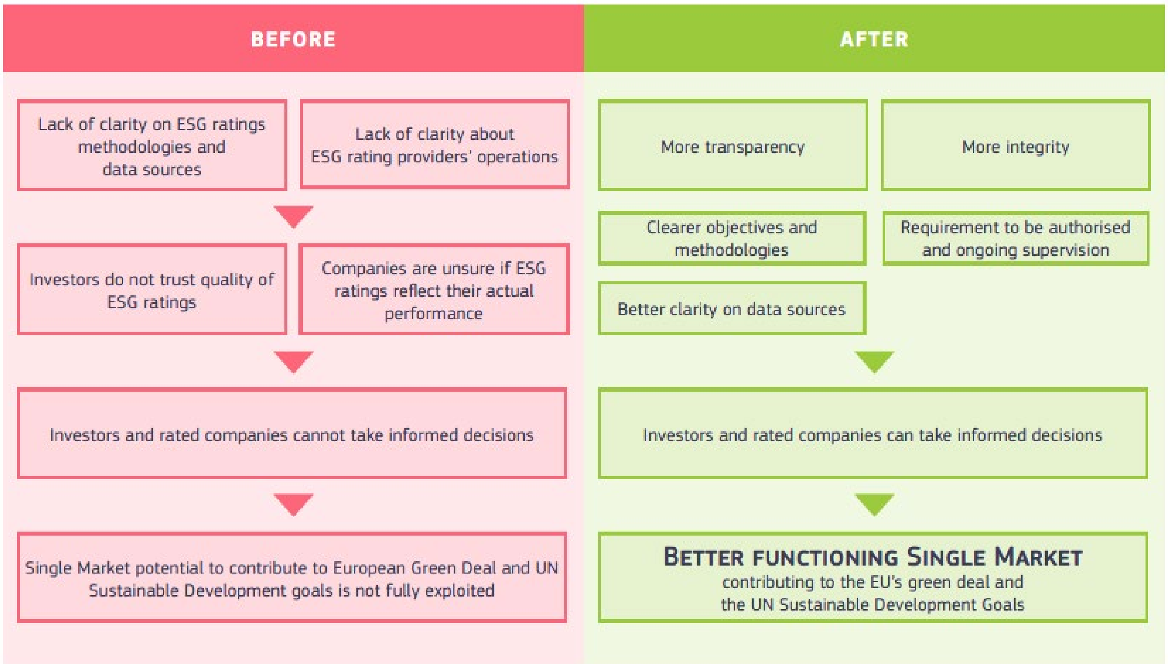
Specific new requirements for ESG rating providers would include:

- The use of rating methodologies that are rigorous, systematic, objective and subject to validation, in order to ensure the quality and reliability of ESG ratings.
- A review of their ESG rating methodologies on an ongoing basis and at least annually.
- The introduction of organizational requirements that ensure the prevention and mitigation of potential conflicts of interest (see Art. 23).
- Ensuring that their ESG ratings are independent, objective and of adequate quality.
- Disclosing information to the public on the methodologies, models and key rating assumptions that those providers use in their ESG ratings activities and in each of their ESG rating products (see Art. 21 and Annex III – minimum disclosures to the public); ESMA will draft regulatory technical standards to define exactly what needs to be disclosed.
- Additional disclosures to the users of ESG ratings and the rates entities related to the methodologies, models and key rating assumptions (see Art. 22 and Annex III/2). Such additional disclosures would include more granular data points, such as the relevant metrics, KPI per E, S and G factor and weighting method.



Source: EU Commission 2023

WHAT IS CHANGING WITH TODAY'S ESG RATINGS PROPOSAL?



© European Union, 2023

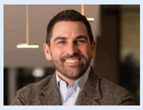
How We Can Help

As a full-service global law firm, we provide insight at the point where law, business and government meet, giving our clients a voice, supporting their ambitions and achieving successful outcomes. Our multidisciplinary team of more than 1,500 lawyers and public policy experts in over 40 offices across four continents provides unrivaled access to expertise and invaluable connections on the ground. It is a seamless service that operates on any scale – locally or globally. It encompasses virtually every matter, jurisdiction and market. And we place our clients at the center.

We combine sound legal counsel with deep knowledge of our clients' businesses to resolve their legal, public policy and political challenges. We care about the quality of our services, the success of our clients and the relationships that are forged through those successes. Our client base spans every type of business, both private and public, worldwide. We advise a diverse mix of clients, from Fortune 100 and FTSE 100 corporations to emerging companies, and from individuals to local and national governments.

Leveraging local connections, while exerting global influence, we are commercial, connected and committed. Our Public Policy Practice Group works with clients to make sure they are heard, at the right time, by the right people, with the right message, in Washington DC, Brussels, London, Canberra and other major capitals around the world. Visit our European Public Policy and International Policy webpages for more information on our team and capabilities.

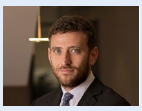
Contacts



Wolfgang Maschek
Partner, Chair of European Public Policy Practice, Brussels
T +32 2 627 1104
E wolfgang.maschek@squirepb.com

Matthew Kirk
International Affairs Advisor, London
T +44 207 655 1389
matthew.kirk@squirepb.com

Nina Kusnierkiewicz
Associate, Public Policy, Brussels
T +32 2 627 1102
E nina.kusnierkiewicz@squirepb.com



Valerio Giovannini
Associate and Public Policy Advisor, Brussels
T +32 2 627 1108
E valerio.giovannini@squirepb.com

Christina Economides
Public Policy Advisor, Brussels
T +32 2 627 1105
E christina.economides@squirepb.com