

Securities and Markets Stakeholder Group

Advice to ESMA

SMSG advice to ESMA on its consultation paper on draft technical standards under the Regulation on the transparency and integrity of Environmental, Social and Governance (ESG) rating activities

Executive Summary

The SMSG welcomes the opportunity to comment on to ESMA's Consultation Paper (CP) on the draft technical standards (the RTS) under the Regulation on the transparency and integrity of Environmental, Social and Governance (ESG) rating activities (the Regulation).

The SMSG welcomes the simplification approach taken by ESMA, but notes that there may be room for even more simplification. The SMSG would like to see further analysis done to determine if the right information is requested, for whom such information would be useful, and how information once provided would have to be updated.

The SMSG in this advice gives some examples of where information requirements relating to ESG analysts and methodology may be reconsidered, modified or taken out. The SMSG also asks for further clarity about the applicability and rules relating to SMEs and start-ups as well as to outsourcing.

The SMSG questions the reference to "scientific methodology" and notes the risks with including such reference. The SMSG would further like to see more clarity around certain definitions used, as well as on what applies in areas where there is (not yet) an established scientific methodology, but where there may be "standards" or similar.

The SMSG notes that users of ESG ratings may be interested in learning what weight an ESG rating provider gives to certain factors or data. The SMSG also raise the concern amongst rated companies that ESG rating providers do not communicate with them and that providers fail to correct information that is not correct. The SMSG therefor ask ESMA to consider if more can be done to improve data-verification within timeframes to be determined by ESMA and methodological transparency for ESG rating providers, so as to bolster the reliability and impartiality of their published ratings.

The SMSG notes that reviews are presently ongoing of several other ESG related regulatory frameworks incl. the CSRD and would like some further clarity on what the implications of such reviews may have on the Regulation and the forthcoming RTS.

Introductory remarks

1. The SMSG welcomes the opportunity to comment on to ESMA's Consultation Paper (CP) on the draft technical standards (the RTS) under the Regulation on the transparency and integrity of Environmental, Social and Governance (ESG) rating activities (the Regulation).
2. The SMSG welcomes the simplification approach taken by ESMA, in that one RTS covers several areas and that ESMA takes a "building blocks" approach on the information side.
3. This said the SMSG notes that there may be room for even more simplification as it can be questioned if all information requested is needed. Further analysis is also required to determine if the right information is requested, for whom such information would be useful, and how information once provided would have to be updated.

Information requirements

4. As regards the information that is proposed to be provided by ESG rating providers, the SMSG questions the usefulness of all details regarding ESG analysts employed by the ESG rating provider. While it is useful for a user or ratings to learn e.g. if the provider is a small "boutique" or a global firm, we wonder why details of all analysts etc. is needed and if so for what purpose.
5. The SMSG finds that if details of all analysts are provided, it may put undue pressure on the individual analysts. A question in this regard is here to what extent such information would be made public and if/how often this information would have to be updated.

SMEs and start-ups in the rating sector

6. The SMSG notes that further clarity could be provided if and if so to what extent the rules set out in the draft RTS will apply to SMEs and start-ups. As the rules are drafted they seem to imply that the ESG rating provider already has an operation up and running, as details seem to have to be provided about existing operations and does not leave room for presenting such information in the form of business plans etc.

Methodology

7. As regards the requirements to provide information about methodology, the SMSG considers that a balance must be struck between such proprietary information as a provider has a legitimate interest in keeping inhouse, and transparency towards the users of ESG ratings.
8. The SMSG also questions the reference to “scientific methodology” and would like to see further clarity on what applies in areas where there is (not yet) an established scientific methodology, but where there may be “standards” or similar.
9. In connection with the above, the SMSG sees a risk that ESG rating providers may be tempted to refer to a “scientific methodology” where no such methodology exists, creating an illusion.
10. The draft RTS also refers to “updates” or “changes” of methodologies, but it is not clear when (within what timeframe) and to what extent ESG rating providers must provide information about updates.
11. It could e.g. be questioned how significant a change must be to require an “update” or “change” and it is unclear who takes the decision on when an “update” is needed, and what the consequences are if no “update” is provided.
 - Example: Would a change (or not) of an approach/a view from a human rights perspective on a country be an “update” or “change” of methodology by an ESG rating provider - this may be a very important matter for some users.
12. The SMSG also notes that users of ESG ratings may be interested in learning what weight an ESG rating provider gives to certain factors or data, so that they can consider this in their own use of the rating.

Relationship with rated companies

13. The SMSG notes that there is a concern amongst rated companies that ESG rating providers do not communicate with them and that providers fail to correct information that is not correct. Against this background, the SMSG would like to ask ESMA to consider if more can be done to improve data-verification within timeframes to be determined by ESMA and methodological transparency for ESG rating providers, so as to bolster the reliability and impartiality of their published ratings.

Outsourcing

14. The SMSG notes that it is unclear if and to what extent rules apply in the case of outsourcing requirements and would like to see further clarity on this matter..

Interaction with other regulatory frameworks

15. The SMSG notes that reviews are presently ongoing of several other ESG related regulatory frameworks incl. the CSRD and would like some further clarity on what the implications of such reviews may have on the Regulation and the forthcoming RTS.

This advice will be published on the Securities and Markets Stakeholder Group section of ESMA's website.

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[Signed]

Giovanni Petrella
Chair
Securities and Markets
Stakeholder Group

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Urban Funered
Rapporteur