

European Association of Corporate Treasurers Summit – Brussels

Verena Ross

ESMA Chair

Thank you very much for the invitation to come and speak here today. I always find it enriching and interesting when I get the opportunity to interact with representatives of the “real economy”. After all, as financial supervisors, our role is to ensure the orderly functioning of capital markets which should ultimately contribute to the financing of our economy.

When speaking here today, we are all still saddened by the devastating situation in Ukraine. The most important thing right now is of course to get peace back to the continent and to address the acute humanitarian situation. From ESMA’s side, our focus is on supporting the implementation of the restrictive measures put in place in the financial services industry against Russian and Belarussian individuals and entities while closely monitoring market developments in relation to energy and commodity markets and the overall economic outlook.

One of ESMA’s main strengths, which is particularly important in this situation, is its close co-operation with the national competent authorities in the EU’s member states. Indeed, as ESMA Chair, a position I took over in November last year, I chair ESMA’s governing body which is composed of the heads of the 27 national authorities. The coordination with national supervisors is an important reason why we can ensure the broad support of ESMA’s activities across the EU.

ESMA’s mission is to enhance investor protection across the EU and promote stable and orderly financial markets. We achieve that mission through four activities in a broad range of areas by (1) assessing the risks to investors, markets and financial stability, (2) completing the EU Single Rulebook for EU financial markets, (3) promoting supervisory convergence and (4) supervising specific financial entities. Indeed, ESMA develops the Technical Standards needed for the implementation of EU law for example in relation to the Prospectus Regulation.

By promoting supervisory convergence, we ensure that the single rulebook is applied consistently across the EU for example by conducting peer reviews on how national authorities conduct supervision.

Today, I would like to focus on two topics that are of importance for companies getting the financing they need to grow. Firstly, the role and future of corporate reporting and how we promote sustainable finance. Secondly, our work as the supervisors of credit rating agencies.

1 Corporate Reporting

Let me start with the important topic of corporate reporting and the future of disclosures. I will share with you two perspectives which both link to ESMA-wide strategic priorities namely the promotion of sustainable finance and digitalisation.

1.1 Improving corporate sustainability disclosure:

The first topic I want to touch upon is the ongoing evolution of requirements for corporates to disclose information about the sustainability profile of their activities.

ESG factors have been growing in importance in financial markets for some time. There is a general momentum building, and not just in Europe, to reorient private finance towards sustainable investing. This movement towards green finance is not just driven by politicians and regulators like me, but to a large degree by the private sector itself. We are seeing investor preferences shifting and we are seeing issuers looking for ways to finance their transition into more sustainable activities. For ESMA, it is important that we are able to seize this opportunity and deliver the necessary regulatory building blocks to make this transition possible. Without reliable, comparable, and standardised information about the sustainability of economic activity, investors will not be able to make informed decisions. And without the institutional framework to ensure the credibility of that information and of sustainability commitments made by issuers, we will not foster the necessary trust to make this new market flourish.

In the following, I want to highlight two ongoing legislative initiatives which contribute in different ways to the green transition:

- the Green Bonds Standard (GBS) and
- the corporate sustainability reporting directive (CSRD).

The forthcoming Green Bonds Standard is an important pillar in the sustainable finance framework.

Over the past few years, we've seen a boom in the issuance of green bonds aligned with the ICMA green bond principles which is the main label currently used in Europe. Whilst this is certainly positive, this market growth has also generated new potential risks. The diversity of issuers and projects being financed and the limitations relating to the availability and comparability of the data describing the projects makes the market difficult to navigate for investors. A lack of trust could eventually slow the flow of capital, while a lack comparability creates a risk of misallocation of this capital.

To address this risk, the European Commission published last summer a proposal for a European green bond standard. The GBS will, once adopted, be a voluntary label which issuers can choose to adhere to. Where an issuer wants to market a bond as green, however, the obligations set out in the standard will be binding on the issuer. The most important obligation concerns the allocation of proceeds of the issuance to assets or activities aligned with the EU Taxonomy Regulation. In addition, the issuer will be required to make a range of information available to the investor about the use of the proceeds.

Two separate mechanisms of compliance monitoring are foreseen in the proposal. First the national supervisor of the issuer will be competent to check overall compliance of the issuer with the requirements in the standard. Second, the issuer will be required to solicit the services of an independent verifier that will perform verification of the issuer's disclosures pre- and post-issuance.

ESMA's role in this respect will consist in authorising and supervising the independent verifier and supporting coordination among national supervisors. At ESMA, we are very excited about this proposal which we consider to be robust and to have the potential to make real improvements for both issuers and investors.

Another important and ongoing initiative is the Corporate Sustainability Reporting Directive. For some years now, large EU companies have been required to provide so-called non-financial information as part of their annual disclosures for investors and other stakeholders.

This requirement was a milestone introduced with the Non-Financial Reporting Directive and it has set the EU on a path towards company transparency on ESG matters.

It has, however, been widely recognised that the current rules do not go far enough. To address this problem, the European Commission last April published a legislative proposal for a Corporate Sustainability Reporting Directive (CSRD). The proposal expands the requirement to publish sustainability information to a much larger group of companies. It also lays the foundation for the adoption of detailed, mandatory reporting standards and strengthens the role of auditors to ensure the disclosures are dependable.

ESMA is following this work closely and once the new requirements are in place, we will work with national securities regulators to ensure they are applied and enforced in a harmonised way.

At the same time as these legislative changes are ongoing in Europe, similar developments are taking place internationally. A very important such development is the establishment of the new International Sustainability Standards Board, ISSB, under the IFRS Foundation. The ISSB will exist in parallel to the International Accounting Standards Board and will establish sustainability-related disclosure standards constituting a comprehensive global baseline which will apply in those jurisdictions that sign up to them.

Many companies who operate both within and outside the EU are likely to apply both the European reporting standards and the ISSB standards. It is therefore important to ensure that the European and the ISSB standards are inter-operable, to ensure helpful disclosure to investors and also to limit unnecessary burden on companies.

I am aware that the achievement of full transparency and comparability on companies' sustainability profile will take some time and that it will require a significant effort from your side. However, these are necessary steps to be able to redirect capital towards more sustainable long-term investments. Therefore, these topics are for ESMA an area of absolute priority.

1.2 Digitalisation: ESAP

With this I will now turn to another point of priority for ESMA while staying in the realm of corporate reporting: namely data and digitalisation.

In recent years, data has become a central element to financial regulation and supervision. Detailed reporting requirements now constitute a key component of financial sector legislation. ESMA undertakes very wide range of activities to improve the quality, consistency, coherence and availability of data.

I would like to highlight one very important legislative proposal in this space: The European Single Access Point – or ESAP for short. Nowadays corporates are required to generate large amounts of text and data to fulfil various obligations for disclosure and transparency. Some of this information is being collected by national registers and regulators whereas other information is reported directly to European authorities like ESMA.

The fragmentation is not just limited to the location of the data but also to the format and the language in which the data is provided. This situation is not only inefficient for the companies providing the data, it also constitutes an important barrier for investors and other users of the data and as such could be detrimental to cross-border investment and thus to companies' ability to raise capital across the EU.

The objective of the new ESAP legislative project is to create a common source of public and freely available financial and sustainability-related information of EU companies and investment products, regardless of where in the EU they are located or originated while enabling a better use and reuse of this information. In doing so, the European Commission hopes to be able to provide more visibility and make funding more accessible for EU companies and save time and resources to investors in finding information, so that investors will be able to make sound and well-informed investment decisions.

In concrete terms, if adopted, ESAP will be a data platform through which an investor will be able to draw information reported to several national and EU registers. ESAP is not foreseen to create new reporting obligations or new checks or audits on the data and information reported. Instead, the idea is to gather all the information into a simple user-friendly web portal available in all EU official languages. The portal should include automated translation services and search tools and is planned to support an API and notification services enabling easy access and monitoring.

The aim of ESAP is to over time include all relevant information relating to debt issuers as well as financial products. However, the implementation will be in done in phases, foreseen to start

as soon as 1 January 2024 with a gradual expansion which will continue until 2026 and potentially beyond. The first data which will be available will be that which is reported under the Transparency Directive, the Prospective Regulation, the Short Selling Regulation, the Securities Financing Transactions Regulation, and the Taxonomy Regulation.

If adopted, ESMA will play a central role in the development of this portal, both in terms of delivering, maintaining, and managing the IT necessary infrastructure as well as in terms of developing the technical and legal standards.

2 CRA Supervision

The last topic I want to cover today is our work supervising CRAs, a responsibility that was entrusted to ESMA from its set-up in 2011 in a response to the financial crisis. In fact, this was the first supervisory powers entrusted to an EU body ever.

Given the role of the CRAs in the 2007-8 and given the common reliance across the Union of a handful of large CRAs, it was in many ways the obvious candidate for EU level supervision. The institutional innovation aside, I would contend that this was also a significant step in practical terms for the quality and reliability of credit ratings in the EU.

If we take a look at the market structure today, we will see that there are 24 CRAs in the EU registered with ESMA, located in 13 different Member States. The 3-4 companies which people generally associate with this sector, account for approximately 92% of the overall market share. The remaining CRAs can be grouped into two categories: (i) the medium-sized CRAs which offer the same suite of rating offerings as the large CRAs but don't have the same market share and (ii) the smaller CRAs who are either specialised in certain industries or certain markets.

The supervisory experience which ESMA has acquired since 2011 has proved essential to enable ESMA to take on supervisory responsibilities in an increasing number of areas since then including Trade Repositories, Securitisation Repositories, third-country CCPs and Benchmarks providers.

2.1 Supervisory powers

To ensure that we carry out our mandate in an efficient and effective manner, ESMA has adopted a risk-based approach to the supervision. This allows us to prioritise our supervisory activities according to the level of risk identified and the outcomes we need to achieve. To address the risks we identify, we have a number of different supervisory tools available to us, ranging from engagement with CRAs to conducting investigations and requesting the implementation of remedial action plans. Where breaches of the regulation are identified, ESMA has the power to adopt enforcement actions. These actions can range from the issuance of public notices to the imposition of fines and the withdrawal of the CRA's registration. Most recently, in March last year, ESMA for example imposed a fine on a large CRA for breaches of the regarding independence and the avoidance of shareholder conflicts of interest.

Where needed, ESMA supplements these supervisory activities with the development of public guidance. For example, ESMA, recently published guidance on disclosure obligations relating to preliminary ratings and initial reviews which aim at avoiding rating shopping by issuers.

Where we identify regulatory gaps which we do not have the power to address through supervisory actions or guidance, we inform the European Commission and recommend ways this can be tackled through adjustments to the legal framework. A recent example of this relates to the access and use of credit ratings. Credit ratings are published on CRAs' websites as well as on ESMA's European Rating Platform. However, the usability of these credit ratings is severely limited as they cannot be accessed in a machine-readable format or downloaded in sufficient numbers to be used for regulatory purposes. Over the years, users of credit ratings such as yourselves have reported to ESMA concerns about the licence agreements they must enter into to be able to use credit ratings in their systems and the lack of transparency in price increases. Last September, ESMA published an opinion in which we recommended ways to address these problems through legislative changes to the CRA Regulation or to other legislation such as for example ESAP which I mentioned earlier.

2.2 Supervisory priorities for 2022

As regards ESMA's supervisory priorities for CRA supervision in 2022, the primary driver is as mentioned ESMA's risk assessments of the supervised CRAs. This year, for example, ESMA identified several aspects of CRAs' internal controls as a focus areas including the role of the compliance function, the review function and the independent non-executive directors.

However, the broader economic environment increasingly also impacts on ESMA's work priorities:

Last year, the focus on the fallout of the COVID-crisis including the development in high-yield bond markets played an important role and remains an area which we closely monitor.

The war in Ukraine also introduced new uncertainty and risks which ESMA needs to take into account. In this regard, ESMA is monitoring the impact of sanctions on CRAs' operations in close cooperation with other regulators and engages with CRAs to ensure sufficient transparency around ratings.

IT and information security controls including cybersecurity and cloud outsourcing are topics which has been on ESMA's radar for a while now and not just for CRAs. In 2020, ESMA published a transversal set of guidelines to help supervised firms identify, address and monitor the risks arising from cloud outsourcing arrangements. In 2022 ESMA intends to assess the implementation of these Guidelines by CRAs.

2.3 ESG factors in credit ratings and ESG ratings

To round off, I would like to say a few words about two CRA-related topics which like cybersecurity are linked to the ESMA-wide strategic priorities:

- The integration of ESG factors in credit ratings; and
- the emerging market of ESG ratings.

ESMA's supervisory mandate covers credit ratings which are defined in the CRA Regulation as an opinion regarding creditworthiness of an entity or a debt instrument. There's been some discussion over whether ESG factors ought to be taken into account in credit ratings. ESMA published guidance addressing this question back in 2020, where we clarified that CRAs must disclose how ESG factors are taken into account whenever they are a key driver behind a credit rating action. We recently reviewed the disclosure practice of CRAs regarding ESG factors and observed an overall improvement since the introduction of the Guidelines with some room for further improvement remaining.

This is one of the reasons that ESG factors will remain one of the focus areas for ESMA supervision of CRAs in 2022, where we are reviewing the incorporation of ESG factors into CRA methodologies.

Beyond credit ratings, we are aware that CRAs are increasingly active in the market for pure ESG ratings and related information. The relevance of ESG ratings has co-evolved with investor appetite for ESG products. We see that ESG ratings are becoming an important area for CRAs as a stand-alone business line separate from credit rating activities.

To support the Commission's work on ESG ratings, ESMA recently conducted a call for evidence regarding the market structure for ESG rating providers in the EU as well as costs of possible supervision.

At ESMA, we believe there are many important lessons from CRA supervision which we can draw upon in a potential future framework for supervision of ESG rating providers. Specifically, like credit rating methodologies we believe these should be independent and free from external interference. We are not in favour of standardising or harmonising methodologies. Indeed, different ESG ratings can have different measurement objectives. This variety can support the different purposes and needs users may have. Instead, a potential future supervision should focus on safeguarding the independence and quality of the assessment.

With this I will close off by saying many thanks for the attention. I hope you found the information useful and look forward to answering any questions you might have.