



European Securities and  
Markets Authority

# Consultation Paper

**Guidelines on Disclosure Requirements Applicable to Credit Ratings**





## Table of Contents

Responding to this paper.....	3
Legislative references, abbreviations and definitions .....	4
1. Executive Summary .....	5
2. Introduction .....	6
3. Disclosure Requirements for Credit Rating Press Releases .....	8
4. Environmental, Social and Governance Factors under the CRA Regulation.....	17
Annex I Cost Benefit Analysis.....	22
Annex II Guidelines .....	25
Annex III List of Questions.....	30

## **Responding to this paper**

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex III. Comments are most helpful if they:

- respond to the question stated;
- indicate the specific question to which the comment relates;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

ESMA will consider all comments received by 19 March 2019.

All contributions should be submitted online at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading 'Your input - Consultations'.

### **Publication of responses**

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publically disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

The collection of confidential responses is without prejudice to the scope of Regulation (EC) No 1049/2001. Possible requests for access to documents will be dealt in compliance with the requirements and obligations laid down in Regulation (EC) No 1049/2001.

### **Data protection**

Information on data protection can be found at <https://www.esma.europa.eu/data-protection> under the heading Data Protection.

### **Who should read this paper**

This paper may be of interest to users of credit ratings, credit rating agencies and entities interested in applying to be a registered CRA.

## Legislative references, abbreviations and definitions

Action Plan	European Commission’s Action Plan for Sustainable Finance
CP	Consultation paper
CRA	Credit Rating Agency
CRA Regulation or CRAR	Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit ratings agencies as amended by Regulation (EU) No 513/2011 of the European Parliament and of the Council of 11 May 2011, Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011, Regulation (EU) No 462/2013 of the European Parliament and of the Council of 21 May 2013, and Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014
EU CRA	A credit rating agency registered with ESMA
ESG	Environmental, Social or Governance
ESMA	European Securities and Markets Authority

# 1. Executive Summary

## Reasons for publication

1. The CRA Regulation includes a number of disclosure requirements relating to the issuance of credit ratings. The purpose of these requirements is to ensure a sufficient level of transparency around the characteristics of the credit ratings themselves. This transparency enables the user of the credit rating to understand the main reasons for the credit rating, any limits or uncertainties underpinning the credit rating as well as where further information can be found to facilitate their own due diligence.
2. In this regard, ESMA has noted an inconsistent level between CRAs regarding the information that is disclosed in accordance to these requirements. As a result, ESMA believes that it would be beneficial to collate a set of good practices in a single guidance document covering the disclosure requirements that are applicable to credit ratings' press releases. In doing so, this will contribute to ESMA's core tasks of contributing to investor protection within the EU.
3. It is with a view to increasing the quality of these general disclosures that Chapter three of these Guidelines is provided. In addition, Chapter four of these Guidelines has the objective of improving the quality of CRA's disclosures in a manner that provides the users of credit ratings with greater transparency as to whether Environmental, Social or Governance factors were considered a key underlying element of a credit rating issuance. This Chapter is provided specifically with a view to supporting the European Commission's Action Plan on Sustainable Finance<sup>1</sup>.

## Contents

4. This Consultation Paper proposes measures in the following areas:
  - Guidance to improve the quality and consistency of the information that is disclosed alongside the issuance of a credit rating in a publicly available press release.
  - Guidance to improve the transparency of credit rating press releases concerning the extent to which sustainability factors have been considered as part of a credit rating.
  - A cost-benefit analysis of the Guidelines is included in Annex I of this CP.

## Next Steps

5. ESMA will consider the responses it receives to this CP in Q2 2019 and expects to publish a final report by 30 July 2019.

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<sup>1</sup> [Communication for the Commission: Action Plan for Financing Sustainable Growth](#)

## 2. Introduction

6. The CRA Regulation includes a number of disclosure requirements for CRA's relating to the issuance of credit ratings or credit rating outlooks ('credit ratings'). The purpose of these requirements is to ensure a sufficient level of transparency around CRA's credit ratings. With this transparency, the user of the credit rating is better placed to understand the reasoning behind the credit rating, any limitations in the judgements or assumptions underlying the applicable methodology as well as where further information can be found to allow them to conduct their own due diligence.
7. This information is typically disclosed through the issuing of a publicly disclosed press release. In this regard, ESMA has noted that there is an inconsistent level between CRAs in the manner in which these requirements are being complied with. This inconsistency leads to problems of transparency and reduces the value of the press releases which accompany the issuance of a credit rating. The purpose of these proposed Guidelines is therefore to improve the quality and consistency of the information that is disclosed as part of a credit rating's publicly available press release. In this regard, the Guidelines are composed of two chapters.
8. Chapter three provides guidance as to how ESMA expects CRAs may best meet their disclosure obligations with regards to the press release that accompanies the issuance of a credit rating. ESMA has noticed that the approaches adopted by different CRAs with regards to these disclosure requirements can vary significantly. These differences can make it difficult for the users of ratings to critically evaluate credit ratings issued by different CRAs. As a result, ESMA considers that there should be certain minimum standard in terms of the quality of information presented in the credit rating press release in order to prevent a situation whereby the presentation of critical aspects of a credit rating are not consistent across CRAs.
9. Chapter four focuses on improving how CRAs disclose the consideration of ESG factors when they are a key underlying element behind the issuance of a credit rating. Although this is not a subject which is addressed explicitly under the CRA Regulation, ESMA recognises that in light of the European Commission's Action Plan for sustainable finance it is desirable to provide some guidance to the industry in order to ensure that the quality of their disclosures can support investors needs in light of the greater focus that is now being placed on sustainability factors in investment decisions.
10. It is with a view to supporting Action 6 of the Commission's Action Plan, which invited ESMA to include environmental and social sustainability information in its guidelines on disclosure for CRAs, that Chapter four of these Guidelines is provided. In this regard, Chapter four has the objective of improving investor's understanding as to whether and how any Environmental, Social or Governance factors were considered as part of a credit rating.

11. In providing this Guidance, ESMA is mindful of the restrictions that are imposed by Article 23 of the CRA Regulation that prevents ESMA, the European Commission or any public EU or Member State authority from interfering with the content of credit ratings or methodologies.
12. As such, this guidance is focused on improving how the consideration of ESG factors are disclosed when they are a key underlying element of a credit rating, it does not mandate or recommend that these factors be considered by CRAs in their creditworthiness assessments. Likewise these Guidelines should not be understood as suggesting that the consideration of ESG factors are more relevant than the consideration of non-ESG factors to the creditworthiness assessment of an entity or issuer.
13. Beyond ensuring that these rating actions are accompanied by the various disclosure requirements, it is also necessary to highlight Article 13 of the CRA Regulation which requires that CRAs do not charge a fee for any information provided in accordance with Articles 8 to 12 of the CRA Regulation. In practice, this means that these press releases should be located on a section of a CRA's website that can be accessed without any barrier to entry or registration requirement.
14. Finally, this CP should be seen as a first step in a broader approach to improve the quality of CRA's credit rating related disclosures. It leaves open the possibility of providing guidance in other areas of the regulation such as sovereign research reports, access to methodologies and preliminary ratings.



### 3. Disclosure Requirements for Credit Rating Press Releases

#### Introduction

15. When issuing a credit rating, the CRA regulation requires a CRA to comply with a number of disclosure requirements. These requirements are typically addressed through a press release which serves the purpose of providing investors and the users of the credit ratings with transparency around the reasons for the credit rating, as well as relevant information on the credit rating to allow them to conduct their own due diligence. This has the benefit of improving the transparency of credit ratings as well as assisting the users of ratings to mitigate any mechanistic reliance on credit ratings<sup>2</sup> by enabling the assessment of any risks, uncertainties and limitations inherent in a credit rating.
16. Given the relevance of this information to ensuring investor protection, it is desirable to ensure that all the elements that are required to be disclosed with the issuance of a credit rating are disclosed and that this is done so according to an appropriate standard. This will ensure that not only are CRA's consistent in terms of what they are disclosing, but they will also be consistent in terms of how they are disclosing it.
17. Although Guidance has already been provided on some aspects of these disclosure requirements in the form of Q&A's (on the solicitation status of credit ratings<sup>3</sup>) and ESMA Guidelines (on the applicability of these disclosure requirements to credit ratings that are endorsed into the European Union<sup>4</sup>), ESMA has noticed that the approaches adopted by different CRAs with regards to these disclosure requirements can vary significantly.
18. These differences can make it difficult for the users of ratings to critically evaluate credit ratings issued by different CRAs. For this reason, ESMA considers it desirable to introduce guidance that will increase the level of harmonisation regarding the presentation of certain key pieces of information within the press release.

#### Overview of Credit Rating Press Releases

19. The CRA Regulation, Article 10(1), requires that a CRA discloses any credit rating on a non-selective basis and in a timely manner, and when they do so that they adhere to the requirements for presentation that are set out in Annex I, Section D, I, 2.

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<sup>2</sup> CRA Regulation Article 5a: The entities referred to in the first sub-paragraph of Article 4(1) shall make their own credit risk assessment and shall not solely or mechanistically rely on credit ratings for assessing the creditworthiness of an entity or financial instrument.

<sup>3</sup> [ESMA Questions and Answers on the CRA Regulation. Part IV Unsolicited Credit Ratings, Question 9.](#)

<sup>4</sup> [ESMA Guidelines on the application of the endorsement regime under Article 4\(3\) of the CRA Regulation. Section 2.6 Disclosure.](#)

20. The typical market practice is for CRA's to comply with these requirements through the publication of a press release when issuing a credit rating. As a result, this press release has become the vehicle through which a CRA meets the majority of its disclosure obligations with respect to credit rating issuances.
21. In this regard, the disclosure requirements contained in the CRA Regulation that are required to accompany a press release are wide-ranging, including information regarding the reasons for the rating issuance, whether the rating was solicited or unsolicited, and whether the rating has been endorsed into the EU to be used for regulatory purposes. As a result, the content and format of these disclosures is important to ensure the users can conduct their own due diligence and understand the principal characteristics of the credit rating.

### **CRA Regulations' requirements for Press Releases**

22. When announcing a credit rating, a CRA must disclose in a press release or report a number of pieces of information concerning that credit rating. These requirements arise in a number of different articles throughout the main body of the CRA regulation, as well as in its Annex which concerns rules on the presentation of credit ratings. In this regard, the CRA Regulation sets out that these key elements should include:
- An indicator of whether the credit rating has been endorsed [Article 4 (2)];
  - In the case of an unsolicited credit rating, a statement to this effect and a prominent statement using a clearly distinguishable colour code [Article 10 (5)];
  - In the case of an unsolicited credit rating a statement as to whether the credit rating agency had access to the accounts, management and other relevant internal documents for the rated entity of related third party [Article 10 (5)];
  - Name and job title of persons primarily responsible for approving the credit rating or rating outlook [Annex I Section D, I, 1];
  - Indication of all substantially material sources used to prepare the report are indicated [Annex I Section D, I, 2(a)];
  - The principal methodology(s) used in determining the rating including and a hyperlink to a comprehensive description of that methodology on the CRA's website [Annex I Section D, I, 2(b)];
  - The sensitivity of the credit rating to future developments that could lead to a subsequent upgrade or downgrade [Annex I, Section D, I, 2(c)];
  - The meaning of each rating category, including definitions of default, risk warnings, sensitivity analyses, key rating assumptions etc. [Annex I Section D, I, 2(c)];
  - The date at which the credit rating was first released for distribution and when it was last updated [Annex I Section D, I, 2(d)];
  - Information as to whether the credit rating concerns a newly issued instrument and whether the CRA is rating the financial instrument for the first time [Annex I, Section D, I, 2(e)];

- In the case of a rating outlook, a time horizon during which a change in the credit rating is expected [Annex I, Section D, I, 2(f)];
  - An indication whether the rating was disclosed to the rated entity and amended following that disclosure [Annex I Section, D, I, 2a];
  - A clear and prominent statement of any attributes and limitations in the credit rating or rating outlook [Annex I Section D, I, 4];
  - The key elements underlying the credit rating [Annex I, Section D, I, 5].
23. Finally, while Annex I Section D, I, 5 of the CRA Regulation allows for some of these requirements to be omitted from the press release where it would be disproportionate to the length, this provision still requires that the report include references and links to where this information can be found on the CRAs website. However, excluding certain information from the press release or report should not negatively affect the readability of the document for investors, nor should this information be placed behind a registration barrier or pay-wall.

### **Approach of the Guidelines**

24. ESMA understands the challenges CRAs face in ensuring that each of these requirements are fulfilled in every press release that accompanies a credit rating issuance, and that the CRA Regulation itself allows a certain degree of flexibility in terms of how and where this information is included in the press release. ESMA also recognises that CRAs may take different approaches as to how these requirements are met, and may also choose to go further by providing a greater level of detail and information than is strictly required by the Regulation.
25. However, ESMA also considers that there should be a minimum standard in terms of the quality of information in the rating issuance press release in order to prevent a situation whereby the presentation of critical aspects of a credit rating is not consistent across CRAs. In this regard and following a review of existing market practice by CRAs in the EU, ESMA has identified a number of areas where inconsistencies in the approaches of different CRAs could pose difficulties for the users of these ratings.
26. It is with a view to addressing some of these deficiencies to ensure that the overall transparency and usability of credit rating press releases is improved, ESMA is proposing the following draft guidance for **the following elements** of CRA's press releases which have been identified as the most in need of guidelines.

*An indicator of whether the credit rating has been endorsed.*

27. An indicator or statement as to whether the credit rating has been endorsed by an EU registered CRA is an important piece of information as it allows the user to understand whether that credit rating can be used for regulatory purposes in the EU. Unfortunately, the inconsistent application of this provision by CRAs (whereby some press releases include

it and others do not) has significantly hampered its effectiveness, as from a readers perspective it is unclear whether the statements' absence from a press release is an indicator that the credit rating has not been endorsed, or, that the CRA has decided to disclose the information elsewhere.

28. Therefore, ESMA considers that CRAs should include a statement or identifier in the press release outlining whether or not a rating has been endorsed for use in the EU. This will ensure that there can be no confusion on the part of the user as to whether the lack of an indicator is deliberate or otherwise.

*In the case of an unsolicited credit rating a prominent statement using a clearly distinguishable colour code explaining the involvement of the rated entity.*

29. Knowledge as to whether a particular credit rating is unsolicited is important information for the user of a rating, as it provides relevant context to the rated entities' level of participation in the rating process. However, this indicator is not consistently included in the press releases of CRAs. As a result, it can be difficult for the user of the rating to understand the solicitation status of a credit rating without recourse to the CRA's website. Therefore, CRAs should include a clear statement in the press release accompanying the credit rating as to whether it is an unsolicited credit rating according to the CRA Regulation<sup>5</sup>.
30. With regards to clearly explaining the involvement of the rated entity, this is a provision that is also implemented on a highly inconsistent basis by CRAs. However, a clear explanation as to whether the CRA had access to the accounts of the rated entity, or a related third party when producing the credit rating is highly relevant information for the user of the rating. Therefore, to improve the application of this provision and to assist CRAs in delivering a consistent application of this provision, ESMA is proposing a schematic that CRAs can use to indicate the involvement of the rated entity or related third party in the credit rating process.

*Name and Job Title of Persons Responsible*

31. The CRA Regulation requires that the name and job title of the persons responsible for a credit rating are disclosed. While the job titles can vary depending on the CRA, this typically involves providing the contact details for the lead analyst, secondary analyst and the chair of the rating committee. This serves the purpose of providing the user of the rating with a specific point of contact within that CRA should they have questions or wish to raise any issues. The inclusion of this information in the press release accompanying the credit rating is generally applied in a consistent manner by CRAs with most CRAs including at least two contacts, one for the lead analyst and another for the person approving the credit rating. However, ESMA did notice that some CRAs took a more comprehensive approach to the

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<sup>5</sup> [ESMA Questions and Answers on the CRA Regulation. Part IV Unsolicited Credit Ratings. Question 9.](#)

inclusion of the information, providing the contact details for each of the individuals as well as the name and address of the legal entity which issued the rating.

32. ESMA considers that the inclusion of this additional information is a more effective way of achieving the objectives of the Regulation. As such when CRAs are including the name and job title of the lead analyst and the chair of the rating committee (where they are the persons responsible for approving the credit rating), it is beneficial that CRAs also provide contact details (ideally an e-mail address and telephone number for each) where each person can be contacted, in addition to the name and address of the legal entity responsible for issuing the credit rating. This final element will also enable the user of the rating to assess whether they are reliant on credit ratings issued by a particular legal entity of a CRA or credit ratings from legal entities based in a particular jurisdiction.

*Indication of all substantially material sources used to prepare the credit rating*

33. One of the key pillars of the CRA Regulation was the requirement for financial institutions to mitigate against a mechanistic reliance on credit ratings. While there are a number of ways for a financial institution to mitigate their reliance on credit ratings, an important contributory element is the ability of the user of the rating to conduct their own due diligence on the rating, for which they will need to have full knowledge of the material sources the CRA relied upon when conducting its analysis.
34. The purpose this element of the guidance is not to define what a “substantially material source” is, as this could impact issues that this paper is not seeking to address, but rather to ensure that from an editorial perspective, the facts and figures cited within the press release are supported with appropriate referencing. For example, where a CRA bases an element of its analysis on a recently published report or statistical data, the sources of this information should be provided and referenced within the press release itself.

*Principal methodology(s) used in the credit rating*

35. The CRA Regulation requires that when a CRA issues a credit rating it discloses the principal methodology(s) used in determining the rating, including a link to them on the CRA’s website. The purpose of this is to ensure that the user of the rating understands which of the CRA’s methodologies and criteria were used to prepare the credit rating and can access a description of that methodology in order to assess for themselves the factors that were considered by that CRA in the determination of the credit rating. This requirement can therefore be broken down into two main elements, the principal methodology itself, any related criteria or models that were used in determining the credit rating listed and a direct link provided to where they can be accessed on the CRAs website.
36. With regards to the first of these requirements, ESMA has noticed that while the majority of CRAs are good at disclosing the principal methodology that was used as part of the

credit rating, other CRAs go further by providing additional relevant information such as the date or version of the methodology used.

37. For the second of these requirements regarding a direct web-link, ESMA has noticed that some CRAs provide only a general link to the “methodologies” section of that CRAs website, and do not provide a direct hyperlink to the principal methodology underlying the credit rating. This has the effect of increasing difficulties of access and frustrating the efforts of the user to accessing the methodology itself.
38. As a result, ESMA is recommending that within the press release the CRA includes a section which lists the principal methodology(s) while any underlying criteria applied to determine the credit rating are also listed. For these items, ESMA would expect the CRA to include the applicable “as at” date for the document in the press release. For each of the documents listed, the CRA should provide a direct web-link that takes the user to that methodology on the CRAs website.
39. Where the credit rating is based on more than one methodology, or where reference to the principal methodology alone might be insufficient to understand the important aspects of the credit rating an explanation or direct web-link to a document which explains how the different methodologies or other aspects are taken into account in the rating should also be provided in the press release.

*Sensitivity of the rating to future developments*

40. The CRA Regulation requires that when issuing a credit rating, CRAs provide a sensitivity analysis of that credit rating, including on the key rating assumptions such as mathematical or correlation assumptions, accompanied by best and worst-case scenario credit ratings. CRAs should provide the sensitivity of the credit rating to future developments, specifically, those actions or events that could lead to a rating upgrade or a rating downgrade. The purpose of this information is to provide the user of that credit rating with the ability to assess the uncertainties, risks and limitations inherent in that credit rating.
41. In its assessment of current practice ESMA has identified that some CRAs are presenting this information in a manner that is clearer and more comprehensible than others. Specifically, ESMA has noted that some CRAs have a dedicated and clearly labelled section within the credit rating press release that describes the actions that would lead to a rating upgrade and a dedicated paragraph describing the actions that would lead to a rating downgrade. ESMA is of the opinion this is an effective way of presenting this information in the press release in a way that is clear and comprehensible for the user.

*The meaning of each rating category, including definitions of default, risk warnings, sensitivity analyses, key rating assumptions etc.*

42. As part of a credit rating, the CRA Regulation also requires CRAs to disclose the meaning of each rating category, definitions of default and risk warnings amongst others. The inclusion of this information in the credit rating is needed to enable the user of the rating to understand the credit rating that has been assigned. However, ESMA has noticed that information of this kind is not systematically included by CRAs in the press releases, either in the body of the text or through a hyperlink accompanying the press release.
43. While it is not necessary to include this information directly in the press release itself it is still necessary for the CRA to include a link to where this information can be found on its website. As a result, for this element of the press release ESMA would expect CRAs to include an explanatory paragraph outlining where the user of the rating can find information on the definition of each credit rating category, including definitions of default, risk warnings, etc. Should this be on a section of the CRA's website, then a dedicated link should be provided to that section or document(s) in that section. If this is in a section of the principal methodology, then a reference to the section of the methodology should be included. Given the importance of this information to understanding the methodology and the credit rating itself, it is not appropriate that the information under this point be located on a section of that CRA's web-site that is restricted by a pay or registration barrier.

*An indication whether the rating was disclosed to the rated entity and amended following that disclosure*

44. The CRA Regulation includes a requirement that the rated entity be provided with an opportunity to review the credit rating for any factual errors prior to its publication. The requirement for a CRA to include a disclosure on the outcome of this process in the press release accompanying a rating issuance is therefore important to provide the end user with clarity and transparency on this element of the credit rating. ESMA has noticed that this element of disclosure is not consistently being included by all CRAs. For example, in some cases a CRA will outline that the rated entity participated in the rating process without specifying whether that participation included the rating being disclosed to the rated entity prior to publication and being amended.
45. CRAs should include a statement explaining whether or not the rating was disclosed to the rated entity and amended following that disclosure paragraph that outlines whether the rating was changed following this process.

*The key elements underlying the credit rating*

46. ESMA does not intend to provide guidance in this area at this juncture. However, with a view to facilitating the European Commission's Action Plan on Sustainable Finance, ESMA

is providing guidance as to how CRAs can better meet their requirements of explaining whether and how ESG factors were considered as part of a specific credit rating issuance. For this guidance please see Chapter 4. In this regard it is important to highlight that in providing this guidance ESMA is not indicating that the consideration of ESG factors is more important than the consideration of other factors relevant to a creditworthiness assessment.

Text of proposed guidelines			
ESMA considers that a credit rating or rating outlook, published within the meaning of Articles 10(1), 10(2),10(5) and Annex I, Section D, I, 1,2,2a and 4 should at least include:			
i. A statement as to whether or not the credit rating has been endorsed for use for regulatory purposes in the EU in accordance with the CRA Regulation.			
ii. A clear statement as to whether the credit rating is an unsolicited credit rating.			
iii. In the case of an unsolicited credit rating the use of the following scheme to clarify the level of the rated entities participation:			
<b>Unsolicited Credit Rating</b>			
[YES]		[YES] / [NO]	
<b>With Participation</b>		<b>No Participation</b>	
[NO]	[YES]	[YES] / [NO]	[YES] / [NO]
<b>Of Issuer</b>	<b>Of Related Third Party</b>	<b>Of Issuer</b>	<b>Of Related Third Party</b>
<b>Access to Accounts</b>		<b>Access to Accounts</b>	
[YES]	[YES]	[YES] / [NO]	[YES] / [NO]
<b>Of Issuer</b>	<b>Of Related Third Party</b>	<b>Of Issuer</b>	<b>Of Related Third Party</b>
iv. The names, job titles and contact details for the persons responsible for the credit rating together with the name and address of the legal entity responsible for the credit rating.			
v. A reference to all substantially material sources used for the report should be listed at the end of the report. Where a fact or figure is cited in the press release this should be referenced via footnote to the sources listed at the end of the press release.			
vi. The name of the principal methodology and associated models or criteria used in determining the credit rating are listed alongside dates of applicability or version number. For each methodology or associated model a direct web-link should be provided to that document on the CRA’s website.			



- vii. A section clearly identified as addressing actions or events that could lead to an upgrade or downgrade of the credit rating accompanied by best and worst-case scenario credit ratings, with dedicated paragraphs addressing factors that could lead to an upgrade, and actions or events that could lead to a downgrade.
- viii. An explanatory paragraph outlining where the user of the rating can find information on the definition of each rating category, including definitions of default, risk warnings, etc. If this is on a section of the CRA's website then a dedicated link to that section or document(s) in that section. If this is in a section of the principal methodology, then a reference to the section of the methodology.
- ix. A statement explaining whether or not the rating was disclosed to the rated entity and amended following that disclosure.

#### **Questions**

**Q1. Do you agree with the proposed Guidelines for press releases that accompany credit ratings or rating outlooks? If not, please explain.**

**Q2. Do you agree that a standardised scheme indicating the rated entities level of participation would be beneficial? Do you have any comments on the proposed standardised scheme?**

**Q4. Do you have any comments on specific items under this section? If yes, please explain with reference to the proposed item's number.**

## 4. Environmental, Social and Governance Factors under the CRA Regulation

### Introduction

47. On 8 March 2018 the European Commission's Action Plan for Sustainable Finance (Action Plan) was published. The purpose of the Action Plan is to better connect finance with the specific needs of the European and Global economy by reorienting capital flows towards sustainable investment in order to achieve sustainable and inclusive growth, managing financial risks stemming from climate change, resource depletion, environmental degradation and social issues, and fostering transparency and long termism in financial and economic activity.
48. To achieve these goals the Action Plan includes ten specific Actions, one of which, Action Six, is concerned with "Better integrating sustainability in ratings and market research". As part of this specific Action, the European Commission requested ESMA to include ESG information in its guidelines on disclosure for credit rating agencies by Q2 2019.
49. With a view to meeting this objective ESMA engaged throughout 2018 with CRAs to gather information on the current practices within the industry as to the integration of ESG factors within credit ratings, and consequently the ability of CRAs to disclose more information in this regard.
50. As part of this effort ESMA issued a questionnaire to a number of CRAs during the third quarter of 2018 requesting more formal views as to how ESG factors are currently considered and disclosed as part of their credit rating issuances, in order to identify good practices.
51. In response to this questionnaire, CRAs highlighted a number of challenges. However, the responses also provided ESMA with an insight as to what actions CRAs could take that would be beneficial to improving the transparency around whether and how a credit rating issuance or outlook has considered ESG factors.
52. It is the purpose of these Guidelines to propose measures to improve the quality and consistency of ESG related disclosures in credit ratings and rating outlooks in a way that balances the scope and legal basis of the CRA Regulation with the increasing need for the users of ratings to have greater clarity and information regarding whether and how ESG criteria have been considered as part of a credit rating or outlook. This increased level of visibility and transparency will assist the users of ratings to take greater account of ESG considerations within their own business decisions and decision making processes.

### **CRA Regulations' requirements for ESG related disclosures**

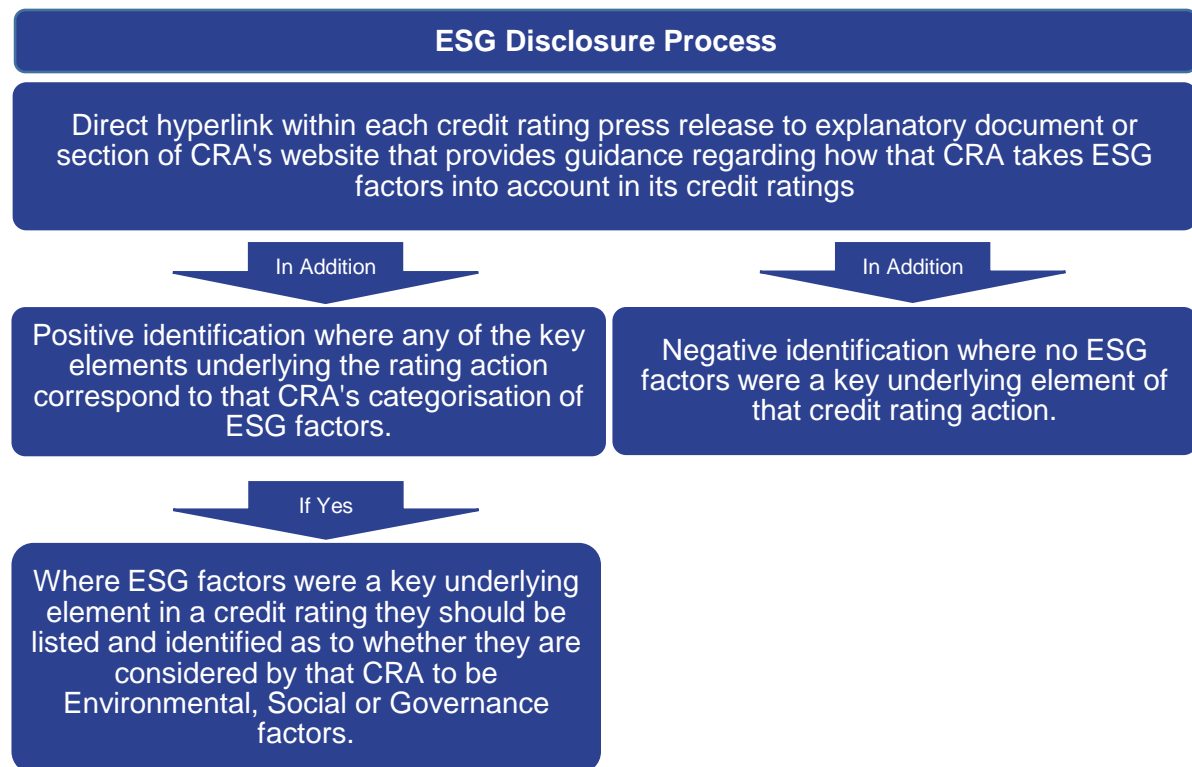
53. The CRA Regulation does not refer to or recognise ESG factors or sustainability considerations on a standalone basis. As a result, there is no provision in the CRA Regulation which explicitly sets out whether or how a CRA should disclose whether they were considered as part of the issuance of a credit rating.
54. However, it is also recognised that information as to whether ESG factors were considered as part of a credit rating is becoming increasingly important for investors in the EU, and that this situation may develop further if other elements of the Action Plan are enacted. With this in mind, it is necessary to provide some guidance as to how CRAs can adapt their processes to meet the challenges of this new environment while staying within the boundaries of the CRA Regulation.
55. One possible way to improve the current level of disclosures in this area, while staying within the creditworthiness boundaries of the CRA Regulation, is to focus on improving **how** CRAs disclose the consideration of ESG factors **when** they are a key underlying element behind the issuance of a credit rating.
56. As a result, the following provisions within the regulation could be referred to when referring to the disclosure of ESG factors when they are considered as part of the issuance of a credit rating:
- *The key elements underlying the rating issuance [Annex I, Section D, I, 5]*
  - *A credit rating agency shall accompany the disclosure of rating methodologies, models and key rating assumptions with guidance which explains assumptions, parameters, limits and uncertainties surrounding the models and rating methodologies used in credit ratings... [Annex I, Section D, I, 2a]*
57. In doing so it is worthwhile to remind readers that in no way does this guidance recommend or mandate **what** factors a CRA should be considering as part of their creditworthiness assessments nor does it suggest that the consideration of ESG factors are more important than other factors to the creditworthiness assessment of an entity or issuer.
58. The CRA Regulation requires CRAs to ensure that their credit ratings and rating outlooks are based on an analysis of **all the information** that is available to it and that is relevant to its analysis according to the applicable methodologies. As such, ESMA recognises that ESG factors **may not** be a key underlying element of a credit rating action if the CRA does not consider them relevant according to the applicable methodology.

### **Observed Market Practices**

59. Given that to date CRAs have not been treating the consideration of ESG factors any differently from other key elements underlying the issuance of a credit rating, the identification of specific best practice regarding their disclosure is difficult. However, ESMA has noticed that as the awareness of ESG factors among investors has increased over the last number of years, CRAs have become more transparent as to how they integrate the consideration of ESG factors into their credit rating.
60. In this regard, ESMA notes that some CRAs have developed standalone sections of their websites to collate all ESG related guidance and research published by that CRA while other CRAs have published dedicated guidance explaining how ESG factors are considered within their methodologies. Both types of action should be seen as positive steps forward.
61. The goal of this chapter of the draft Guidelines is to propose measures which improve the link between these actions, that some CRAs are already taking, and the CRAs individual credit rating press releases.

### **Approach of the proposed Guidelines**

62. The proposed approach of these Guidelines is therefore to propose a set of incremental yet complimentary measures for CRAs to implement. Any one of this measures will improve the users' understanding of whether ESG factors were considered. Taken altogether they will amount to a significant improvement in the current level of ESG related disclosures that accompany the issuance of a credit rating. In short, these measures aim to improve transparency as to whether ESG factors were considered, and when they were considered, which ones.
63. By proposing incremental measures, ESMA is also ensuring that there is some degree of proportionality available for all CRAs. Under this approach, all CRAs should implement at least one element of the guidance, but those CRAs with the ability to do more, should do more. Figure 1 below provides an illustration as to how these incremental measures would work in practice.



64. At the top, is the most basic element, a requirement for CRAs to include a reference and link to either the section of their website where their ESG related material can be found, or a document that explains how ESG factors are considered within their credit rating methodologies.
65. The next two steps are mutually exclusive, either a positive statement in the press release by the CRA that ESG factors **were** a key underlying element behind that credit rating, or a negative statement in the press release explaining that ESG factors **were not** a key underlying element behind that credit rating.
66. In the case of a positive statement, the CRA should then identify which of the key underlying elements behind the credit rating relate to ESG factors. This should be accompanied by an indicator as to whether, in the absence of an agreed taxonomy for sustainable finance, that key underlying element is considered to be either an Environmental or Social or Governance factor by that CRA.
67. So, in the example where the effectiveness or otherwise of a rated entities' Board of Directors is a key element underlying a credit rating upgrade or downgrade, a CRA would include in the press release:
  - A positive statement confirming that ESG factors were considered as part of that credit rating; and,

- A separate statement explaining that the effectiveness of a rated entities' Board of Directors is considered by that CRA to be a Governance factor.

68. It would therefore be clear to the user of the rating that an ESG factor was considered as a key underlying element of the credit rating, that the ESG factor considered was the effectiveness of the rated entities' Board of Directors, and that that CRA considers this to be a Governance factor.
69. Should this approach be adopted by all CRAs, it will over time become clear which CRAs consider ESG factors as part of their credit ratings, and of the CRAs that do consider ESG factors, what factors they are considering on the most regular basis.

#### Text of proposed guidelines

With regard to the disclosure as to whether and how ESG factors were considered as key underlying elements of a credit rating issuance in accordance with Article 10(1), 10(2) and Section D, Annex I, I, points 2a and 5, CRAs should:

- i. Include a direct web-link at the bottom of each credit rating press release to the section of that CRA's website that includes guidance explaining how ESG factors are considered as part of that CRA's credit ratings. [Annex I Section D, I, 2a]
- ii. Outline in the press release whether any of the key underlying elements of the credit rating issuance correspond to that CRA's categorisation of ESG factors.[Annex I, Section D, I, 5]
  - a. Where ESG factors were not a key underlying element of the credit rating, the CRA should include a statement in this regard.
  - b. Where ESG factors were a key underlying element of a credit rating, the CRA should clearly identified whether the factor or factors refers to either an Environmental, Social or Governance factors. [Annex I, Section D, I, 5]

#### Questions

**Q5. Do you have any comments on the proposed Guidelines under this section?**

**Q6. Are there any additional actions that CRAs could take to improve the disclosure of the consideration of ESG factors?**

## Annex I Cost Benefit Analysis

### *Background*

1. In the years following the publication of the CRA Regulation, ESMA has noted that different CRAs have interpreted the disclosure requirements of the provisions in different ways. This lack of consistency has weakened the purpose of these provisions the purpose of which was to improve transparency and enhance the ability of the users of ratings to perform their own due diligence.
2. With publication of the European Commission's Action Plan on Sustainable Finance which has the objective of better integrating the consideration of Environmental, Social and Governance factors into the actions of financial market participants, it has become even more necessary that the disclosure provisions under the CRA Regulation are fully adhered to.

### *Reasons for Publication*

3. The purpose of this consultation paper is to propose a set of Guidelines that increases the standard and consistency of these credit rating related disclosure practices in a manner that gives full effect to the objectives of the Regulation's provisions. In so doing it is noted that this guidance seeks to harmonise the application of existing Level 1 provisions, rather than imposing any new requirements for CRAs.
4. As a result, it is difficult to argue that they impose any new or material costs on CRAs. In addition, as the philosophy behind these Guidelines, has been to recommend the widespread adoption of practices that have already been observed in the market ESMA believes that the measures proposed are proportionate and achievable.
5. In this regard the approach of the guidelines is to improve the content of the most common rating related publication, the credit rating press release. As part of this approach ESMA would like to support the European Commission's Action Plan for sustainable finance by improving how CRAs disclose how ESG factors have been considered as part of a credit rating action within these press releases.

### *CBA*

6. The following table summarises the potential costs and benefits resulting from the implementation of these Guidelines.

<b>Policy objective</b>	To harmonise the presentation and content of CRAs' most common credit rating related disclosures, in order to increase investors' protection and further assist the users of credit ratings to perform their own due diligence.
<b>Technical proposal</b>	<p>To provide guidance to EU registered CRAs regarding how they can comply with CRAR requirements regarding the presentation of credit ratings and credit outlooks.</p> <p>This is done by proposing good practices and encouraging their uptake.</p>
<i>Benefits</i>	<p>For ESMA, a higher uptake of these guidelines will mean that CRAR requirements on the presentation of credit ratings and ratings outlooks will be more consistently applied which will contribute to its mandate to promote investor protection and orderly financial markets.</p> <p>ESMA expects that these guidelines will benefit EU CRAs by:</p> <ul style="list-style-type: none"> <li>- Providing clarity and guidance on the expected rating related disclosures, in terms of their scope and degree of precision.</li> <li>- ESMA also expects that these guidelines will benefit the users of credit ratings by and contributing to consumer and investor protection within the EU by: <ul style="list-style-type: none"> <li>- Facilitating a consistent implementation of the rules on the presentation of credit ratings and credit outlooks, through encouraging the adoption of similar standards.</li> <li>- Increasing the transparency of CRAs credit rating actions.</li> <li>- Improving the ability of the users of credit ratings to perform their own due diligence.</li> <li>- Improving the transparency around whether and how ESG factors were considered as part of a credit rating.</li> </ul> </li> </ul>
<i>Costs for CRAs</i>	For those CRAs who are already implementing some or all of the practices in these Guidelines, it is expected that these Guidelines will have limited additional initial, ongoing or ad-hoc costs.



<p><i>Initial Costs</i></p>	<p>For those CRAs who do not currently apply the practices outlined in this paper, the Guidelines will have an initial cost related to the adaptation of their procedures related to disclosures. However, this cost should be scaled to the current level of a CRAs compliance with their requirements under CRAR.</p> <p>For example if a CRA is already implementing the provisions of the regulation in a manner similar to the Guidelines then adapting its processes to the practices in these guidelines should be relatively less costly than for a CRA that is implementing the provisions of the Regulation in a manner very different from the Guidelines, as it will have a further distance to travel in order to but in place the measures proposed by these guidelines.</p> <p>For newer CRAs, the effect of these Guidelines should be to lower costs, by reducing the need for them to dedicate time and resources to the development of their own internal policies and procedures. Indeed, these Guidelines should save them from having to develop their own systems and procedures to define the appropriate disclosures. They could outright implement the disclosures set out in the Guidelines.</p>
<p><i>Ongoing Costs</i></p>	<p>There may be a slight increase in ongoing costs, as some CRAs will have to increase their efforts in order to meet the guidelines.</p>
<p><i>Ad-Hoc</i></p>	<p>Ad-hoc costs may decrease, as the need for corrections and enforcement by ESMA should be reduced, since clear standards are set in the Guidelines.</p>
<p><b>Costs for ESMA</b></p>	<p>For ESMA the costs entailed with these guidelines are limited given that they do not propose a significant shift in its supervisory practices.</p>

## Annex II Guidelines

### Scope

#### Who?

1. These guidelines apply to credit rating agencies established in the Union and registered with ESMA (hereinafter “EU CRAs”) in accordance with Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies<sup>6</sup> (hereinafter “CRAR”) which are endorsing or which intend to endorse credit ratings issued by a third-country CRA in accordance with Article 4(3) of the same Regulation.

#### What?

2. These guidelines concern particular matters relating to the publication of credit ratings, rating outlooks, sovereign research reports and methodologies and models by EU Registered CRAs in accordance with Articles 8(1), 10(1), 10(2), 10(5), 11(1) and Annex I, Section D, I, points 1,2,4 and 5 and Annex I Section D, III, 1,2 and 4.

#### When?

3. These guidelines will apply from XX XXXX 2019.

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<sup>6</sup> OJ L 302, 17.11.2009, p.1.

## Definitions, legislative references and acronyms

The following definitions apply:

CRA	Credit rating agency
CRAR	The Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit ratings agencies as amended by Regulation (EU) No 513/2011 of the European Parliament and of the Council of 11 May 2011, Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011, Regulation (EU) No 462/2013 of the European Parliament and of the Council of 21 May 2013, and Directive 2014/51/EU of the European Parliament and of the Council of 16 April 2014
CRA 2	Regulation (EU) No 513/2011 of the European Parliament and of the Council of 11 May 2011 amending Regulation (EC) No 1060/2009 on credit rating agencies
CRA 3	Regulation (EU) No 462/2013 of the European Parliament and of the Council of 21 May 2013 amending Regulation (EC) No 1060/2009 on credit rating agencies
ESMA	European Securities and Markets Authorities
ESMA Regulation	Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (ESMA Regulation)
EU CRA	A credit rating agency registered with ESMA.

## 1 Purpose

4. The purpose of these Guidelines is to improve the consistency of the information that CRAs are required to disclose as part of certain rating actions. This information is typically included in the rating action press release and sovereign research reports that accompany specific rating actions. As well as issues relating to content, these Guidelines also address issues relating to access, specifically access to CRA's methodologies and models. In assembling these guidelines ESMA's approach has been to look at the current level of compliance across the industry and highlight those practices that ESMA believes would be beneficial if adopted by all CRAs.

## 2 Compliance and reporting obligations

### 2.1 Status of the guidelines

5. This document contains guidelines issued pursuant to Article 16 of the ESMA Regulation. In accordance with Article 16(3) of the ESMA Regulation, CRAs must make every effort to comply with the guidelines.

### 2.2 Reporting requirements

6. ESMA will assess the application of these guidelines by the CRAs through its ongoing supervision and monitoring of CRAs' periodic reporting to ESMA.

## 3 Guidelines

### 3.1 Requirements relating to Press Releases published in accordance with Article 10(1), 10(2) and 10(5).

7. ESMA considers that a credit rating or rating outlook, published within the meaning of Articles 10(1), 10(2),10(5) and Annex I, Section D, I, 1,2,4 should at least include:
  - i. A statement as to whether or not the credit rating has been endorsed for use for regulatory purposes in the EU in accordance with the CRA Regulation.
  - ii. A clear statement as to whether the credit rating is an unsolicited credit rating.
  - iii. In the case of an unsolicited credit rating the use of the following scheme to clarify the level of the rated entities participation:

Unsolicited Credit Rating			
[YES]		[YES] / [NO]	
With Participation		No Participation	
[NO]	[YES]	[YES] / [NO]	[YES] / [NO]
Of Issuer	Of Related Third Party	Of Issuer	Of Related Third Party
Access to Accounts		Access to Accounts	
[YES]	[YES]	[YES] / [NO]	[YES] / [NO]
Of Issuer	Of Related Third Party	Of Issuer	Of Related Third Party

- iv. The names, job titles and contact details for the persons responsible for the credit rating together with the name and address of the legal entity responsible for the credit rating.
  - v. A reference to all substantially material sources used for the report should be listed at the end of the report. Where a fact or figure is cited in the press release this should be referenced via footnote to the sources listed at the end of the press release.
  - vi. The name of the principal methodology and associated models or criteria used in determining the credit rating are listed alongside dates of applicability or version number. For each methodology or associated model a direct web-link should be provided to that document on the CRA's website.
  - vii. A section clearly identified as addressing actions or events that could lead to an upgrade or downgrade of the credit rating accompanied by best- and worst-case scenario credit ratings, with dedicated paragraphs addressing factors that could lead to an upgrade, and actions or events that could lead to a downgrade.
  - viii. An explanatory paragraph outlining where the user of the rating can find information on the definition of each rating category, including definitions of default, risk warnings, etc. If this is on a section of the CRA's website then a dedicated link to that section or document(s) in that section. If this is in a section of the principal methodology, then a reference to the section of the methodology.
  - ix. A statement explaining whether or not the rating was disclosed to the rated entity and amended following that disclosure.
- 3.2 Requirements relating to Article 10(1), 10(2) and Section D, Annex I, I, points 2a and 5.
8. With regard to the disclosure as to whether and how ESG factors were considered as key underlying elements of a credit rating issuance in accordance with Article 10(1), 10(2) and Section D, Annex I, I, points 2a and 5, CRAs should:
    - i. Include a direct web-link at the bottom of each credit rating press release to the section of that CRA's website that includes guidance explaining how ESG factors are considered as part of that CRA's credit ratings.
    - ii. Outline in the press release whether any of the key underlying elements of the credit rating issuance correspond to that CRA's categorisation of ESG factors.
      - a. Where ESG factors were not a key underlying element of the credit rating, the CRA should include a statement in this regard.

- b. Where ESG factors were a key underlying element of a credit rating, the CRA should clearly identified whether the factor or factors refers to either an Environmental, Social or Governance factors.

## Annex III List of Questions

Q1	Do you agree with the proposed Guidelines for press releases that accompany credit ratings or rating outlooks? If not, please explain.
Q2	Do you agree that a standardised scheme indicating the rated entities level of participation would be beneficial? Do you have any comments on the proposed standardised scheme?
Q3	Do you have any comments on specific items under this section? If yes please explain with reference to the proposed item's number
Q4	Do you have any comments on the proposed Guidelines under this section?
Q5	Are there any additional actions that CRAs could take to improve the disclosure of the consideration of ESG factors?