

Grade A rating? Reviewing the EU ESG Ratings Regulation

Top 10 things about the new EU rules

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The EU's ESG Ratings Regulation was published in the Official Journal on 12 December 2024. This starts the clock running on the implementation timetable: the Regulation applies from 2 July 2026.

In this briefing note, we summarise the Top 10 things that providers of ESG ratings need to know about these important new rules. This is relevant both to firms which provide ESG ratings as a standalone business and also to those which provide ESG ratings as part of other products or services, including investment firms and asset managers.

The view from 10,000 feet:

The ESG Ratings Regulation is another significant development in the EU's already complex landscape for ESG regulation.

The primary focus of the ESG Ratings Regulation is on **rating providers which issue and publish/distribute ESG ratings** to their clients. The Regulation creates a new authorisation regime for EU-based rating providers (requiring firms to seek authorisation from ESMA), along with detailed new organisational, conduct of business and transparency rules. Firms which produce and distribute ESG ratings as a core business line will be directly in-scope, and will need to focus on the authorisation requirements.

However, beyond the primary ratings providers, the regime also catches other business models. In particular, both (a) ESG ratings issued by **regulated financial undertakings** in the EU, in respect of regulated products and services, and (b) **mandatory SFDR disclosures**, are exempt from the authorisation requirements of the Regulation. However, they are both subject to new **mandatory transparency** requirements.

Firms will need to prioritise **scoping** whether and how the Regulation applies to them. To help with this, much of the focus of this briefing note is on explaining core concepts, including application provisions and exemptions.

1. What is the EU ESG Ratings Regulation?

The EU has published in the Official Journal the new *Regulation on the transparency and integrity of Environmental, Social and Governance (ESG) rating activities* ([Regulation \(EU\) 2024/3005](#)) (the **ESG Ratings Regulation**).

The EU recognises that ESG ratings play an important role in global capital markets. In particular, investors, borrowers and issuers increasingly use ESG ratings as part of investment or financing decisions, or as a reference point for the sustainability risks and opportunities of an investment.

The broad policy purpose of the ESG Ratings Regulation is to ensure that ESG ratings are independent, comparable, impartial, systematic and of adequate quality and that rating activities are conducted in accordance with the principles of integrity, transparency, responsibility, and good governance.

The core focus of the ESG Ratings Regulation is to create a **new regulatory regime** for ESG rating providers **operating in the EU**. This involves both a new authorisations regime (to be operated centrally via ESMA) and also detailed new governance and conduct of business requirements.

It's important, though, to emphasise that there are **extensive exemptions** from the authorisation requirement. Firms which provide ESG ratings will need to scrutinise the exemptions carefully, to determine whether and, if so, how they apply.

There is also a separate set of rules which permit **non-EU firms** to provide ESG ratings in the EU, under equivalence, endorsement or recognition regimes.

2. What's the new regulatory framework for ESG ratings?

In overview, the ESG Ratings Regulation applies to **ESG ratings** issued by **ESG rating providers** which are **operating in the EU**. A firm which meets this definition will need to obtain authorisation from ESMA (or have a permitted status for a non-EU firm) and comply with the governance and conduct rules.

That summary statement involves several layers of complexity:

- *What is an ESG rating?* There is a formal definition of an ESG rating, which we summarise below in section 4 of this note.
- *Which rating providers are in-scope?* The Regulation applies where an ESG rating provider **issues** and **distributes/publishes** ESG ratings.
- *Which rating providers are exempt?* There is a lengthy list of exempt ratings and providers, which we summarise below in section 5 of this note. There is also an

important territoriality modifier, which we summarise below in section 6 of this note.

- *How do the authorisation requirements apply?* There are significantly different authorisation requirements for in-scope ratings providers, depending on whether the provider is established (a) in the EU or (b) outside the EU. These provisions are summarised below in sections 7 and 8 of this note, respectively.
- *What requirements apply to exempt ratings?* Finally, there are certain transparency obligations, which will apply to regulated financial services which otherwise fall out-of-scope of the regulation. These are summarised below in section 9 of this note.

3. When does the regulation first apply?

The ESG Ratings Regulation was published in the Official Journal on 12 December 2024, and it enters into force on 2 January 2025.

The more important **practical deadline**, however, is the application date, which is **2 July 2026** – i.e. **18 months** after entry into force. This is the date on which the provisions of the regulation come into effect (subject to certain transitional provisions not covered in this note).

The ESG Ratings Regulation will be directly applicable in each EU member state and does not need to be implemented into national law.

4. What is an ESG rating?

The regulation applies to ESG ratings, as defined.

Defined term	Meaning
ESG rating	<p>an opinion or a score (or a combination of both) regarding a rated item's:</p> <ul style="list-style-type: none">• profile or characteristics with regard to ESG or human rights factors, or• exposure to risks or impact on ESG or human rights factors, <p>and that is based on both an established methodology and a defined ranking system of rating categories.</p> <p>This applies irrespective of whether such ESG rating is labelled as 'ESG rating', 'ESG opinion' or 'ESG score' (defined below)</p>

Defined term	Meaning
ESG opinion	an ESG assessment that is based on a rule-based methodology and defined ranking system of rating categories, directly involving a rating analyst in the rating process
ESG score	an ESG measure derived from data, using a rule-based methodology, and based only on a pre-established statistical or algorithmic system or model, without any additional substantial analytical input from a rating analyst
rated item	<p>a legal person, a financial instrument, a financial product, a public authority or a body governed by public law which is explicitly or implicitly rated in the ESG rating.</p> <p>This is irrespective of:</p> <ul style="list-style-type: none"> • whether such rating has been requested • whether the legal person, public authority or body governed by public law has provided information for that ESG rating

Note that the definition of an ESG rating is deliberately **narrow and specific**. Amongst other things, it will require that the rating is **either an ESG opinion and/or ESG score**, and requires the rating to be based on an established methodology and a defined ranking criteria. However, the label or title applied to the rating will not be relevant.

It is also important to note that the definition of ESG rating will be triggered, whether or not the subject of the rating (the “**rated item**”) requested the rating or cooperated with the provision of information for the rating.

5. What is exempt from the definition of an in-scope ESG rating?

The ESG Ratings Regulation contains an extremely **lengthy list of exemptions**. These are summarised in the table below.

For the most part, the **impact** of falling within the exemption is that the **ESG Ratings Regulation does not apply at all** to the relevant product or service.

However, please see **exemptions (c), (d) and (m)** in the list below, for which **additional requirements** will expressly apply, in order to benefit from the exemption. These additional requirements are summarised below, following this table.

<u>Exemption</u>	<u>Scope of exemption</u>
(a) Private ratings	private ESG ratings that are not intended for public disclosure or for distribution
(b) In-house or intra-group financial services	ESG ratings issued by regulated financial undertakings in the EU that are used exclusively for internal purposes or for providing in-house or intragroup financial services or products
(c) Regulated products and services *	ESG ratings issued by regulated financial undertakings in the EU, in respect of regulated products and services. * Please see below for the additional requirements which apply.
(d) Non-EU providers – reverse solicitation *	ESG ratings issued by ESG rating providers established outside the EU, which are distributed in response to the own exclusive initiative of the user of the ESG rating. * Please see below for the additional requirements which apply.
(e) Data	publication or distribution of data on ESG or human rights factors
(f) Credit ratings	credit ratings issued pursuant to the EU Credit Rating Agencies Regulation, and any ESG-related scores or assessments that are produced or published as part of the methodologies for credit ratings or as an input or output of the creditworthiness assessment
(g) Investment research	products or services that incorporate an element of an ESG rating, including investment research
(h) Reviews of green bonds	external reviews of European Green Bonds
(i) Reviews and opinions on debt instruments	external reviews or second-party opinions on bonds marketed as environmentally sustainable, sustainability-linked bonds, and bonds, loans and other types of debt instruments marketed as sustainable, to the extent that such external reviews and second-party opinions do not contain ESG ratings issued by the external reviewer or the second-party opinion provider
(j) EU institutions and member states	ESG ratings issued by EU institutions, bodies, offices and agencies or Member State public authorities where such ratings are not published or distributed for commercial purposes
(k) Third party distribution of ratings from authorised provider	ESG ratings issued by an authorised ESG rating provider where such ratings are published or distributed by a third party
(l) Central Banks	ESG ratings issued by members of the European System of Central Banks where such ratings are not published or distributed for commercial purposes

<u>Exemption</u>	<u>Scope of exemption</u>
(m) SFDR *	mandatory disclosures pursuant to Articles 6, 8, 9, 10, 11 and 13 of SFDR * Please see below for the additional requirements which apply.
(n) Taxonomy	disclosures pursuant to Articles 5, 6 and 8 of the Taxonomy Regulation
(o) Accreditation or certification	ESG ratings developed exclusively for accreditation or certification processes, which do not target investment analysis, financial analysis, investment decision-making or financial decision-making
(p) Labelling	labelling activities provided that the labels granted to the relevant entities, financial instruments or financial products do not involve the disclosure of an ESG rating
(q) Non-profit activities	ESG ratings published or distributed by non-profit organisations for non-commercial purposes

We note that **exemption (k)** may prove to be very important in practice. This effectively exempts the mere **distribution or publication** of ratings which are separately issued by a third party EU-authorized ESG rating provider. For example, if a firm includes a rating from a third party EU-authorized ratings provider in its documentation, that will be exempt from the scope of the ESG Ratings Regulation.

Simmons & Simmons comment: We have noted a potential ambiguity associated with exemption (k). There is a risk that a firm distributing or publishing an ESG rating issued by a third party provider that is *not* EU authorised could not make use of this exemption. Therefore, checking the status of the ESG rating provider should form part of the due diligence before a firm publishes or distributes a third-party ESG rating. The terms of exemption (k) suggest that there is a risk that publishing or distributing an ESG rating from a non-EU authorised provider could bring a firm in scope of the ESG Ratings Regulation (unless it can rely on a different exemption). Firms will need to keep abreast of developing regulatory policy in respect of this exemption.

As noted above, **exemptions (c), (d) and (m)** are subject to **additional requirements** under the ESG Ratings Regulation in order for the exemption to apply. We now summarise each of these in turn.

Exemption (c), Regulated products and services – additional requirements:

This exemption applies where ESG ratings are issued by **regulated financial undertakings** in the EU and disclosed to a third party. The exemption applies only where:

- The rating is incorporated into a product or service which is already **separately regulated** under EU law. This includes (amongst others) products and services

provided by credit institutions, insurance and reinsurance, fund managers under UCITS and AIFMD, crypto assets under MICA, benchmarks, and IORPs.

- In addition, the regulated firm will be required to include on its website the same **disclosures** as are required for website disclosure by authorised EU ESG ratings providers. *Please see section 9 of this memo, below, which summarises those disclosures in more detail.*

Exemption (d), Non-EU reverse enquiry – additional requirements:

In summary, this effectively provides a **reverse enquiry exemption** for **non-EU ratings providers**. The conditions are:

- The rating provider must be established outside of the EU.
- The rating provider must not be authorised or recognised under the ESG Ratings Regulation.
- The rating must be distributed only at the “**own exclusive initiative**” of the EU user of the rating. This means that there cannot be any prior contact, solicitation, promotion, advertisement or any other initiative by the ESG rating provider (or a third party on its behalf).
- This exemption will not be available if the provider has a “substantial” market share in the EU.
- This exemption will not be available if the provider has a website in any of the official languages of the EU, other than English.

The availability of this exemption does not entitle the provider to distribute ratings to the relevant user on a recurrent basis, nor to any other user.

Exemption (m), SFDR disclosures – additional requirements:

In summary, this exemption applies to **mandatory disclosures** which are published under the EU Sustainable Finance Disclosures Regulation (**SFDR**). This includes the mandatory **pre-contractual, periodic and website** disclosures under SFDR.

The ESG Ratings Regulation amends SFDR, to require new website **disclosures** under the SFDR website disclosure regime. These new mandatory disclosures are the same disclosures as are required for website disclosure by authorised EU ESG ratings providers. *Please see section 9 of this memo, below, which summarises those disclosures in more detail.*

This is the same set of additional disclosures as will apply to the providers of regulated products and services.

6. What is the territorial scope of the new regime?

The ESG Ratings Regulation applies to ESG rating providers which are **operating in the EU**. The meaning of the term “operating in the EU” varies, depending on whether the provider is **established in the EU**, or **established outside of the EU**. Another key variable is **how** the provider provides ESG ratings in practice.

We summarise the territorial scope below.

How are the ESG ratings provided?	EU ESG rating provider	Non-EU ESG rating provider
<p>→ issue and distribute ESG ratings by subscription or other contractual relationships to:</p> <ul style="list-style-type: none"> • regulated financial undertakings in the EU • undertakings within scope of the EU Accounting Directive • undertakings within scope of the EU Transparency Directive • EU institutions or EU member state public authorities 	→ in-scope	→ in-scope
→ issue and publish ESG ratings on the firm’s website or through other means	→ in-scope	→ not in-scope

We note, therefore, that both EU and non-EU rating providers are in-scope of the regulation, where they issue and distribute ESG ratings through subscription or other contractual means to one or more of the specified types of user. However, non-EU firms are not in scope merely by publishing ESG ratings on the firm’s website (but EU firms will be).

7. How do the authorisation requirements apply to an EU firm?

We turn now to consider the **authorisation requirements** for an ESG rating provider which is established in the EU. We assume for these purposes that the firm is issuing ESG ratings (as defined), that it does not benefit from any of the exemptions, and that it is territorially in-scope as a result of being established in the EU.

Application for authorisation:

EU ESG rating providers will need to **apply to ESMA** for authorisation. This will involve submitting a formal application to ESMA, which includes detailed information on the firm, its ownership structure, its senior management and staff, and its operations. ESMA will conduct a formal review of the application.

Governance and conduct rules:

Firms which obtain authorisation by ESMA under the ESG Ratings Regulation will be subject to a detailed range of **governance and conduct of business** obligations. The specification of those rules takes up the bulk of the ES Ratings Regulation, and the full detail is beyond the scope of this note. In overview, the areas of regulation include:

- General governance and systems and controls requirements
- Requirements around separation of business and activities
- Requirements applicable to ratings analysts and other employees involved in the provision of ESG ratings
- Record-keeping requirements
- Complaints-handling procedures
- Outsourcing rules
- Transparency requirements – both on public websites, and more specified disclosures to users of ESG ratings and to issuers of rated items.

(Please see below at section 9 of this note, for more detail on the public website transparency requirements. As noted, those transparency requirements will also be relevant under exemption (c) for regulated products and services, and exemption (m) for SFDR disclosures)

- Independence and conflict of interest requirements
- Fair, reasonable, transparent and non-discriminatory treatment of ESG users

The ESG Ratings Regulation also specifies in detail the **powers of ESMA**, and how ESMA interacts with national regulators. This includes enforcement powers, including the imposition of fines and other penalties for non-compliance.

Temporary regime for smaller providers:

We note finally that there is a concessionary regime which applies to certain **smaller EU ESG rating providers**. This allows such firms to comply with only a sub-set of the rules, for a **temporary period of 3 years**. That regime is not covered further in this note, but please let us know if you'd like to discuss it further.

8. How does the regulation apply to a Non-EU firm?

In parallel with the regime for providers established in the EU, there is a separate regime under the ESG Ratings Regulation for providers established **outside of the EU**. We summarise those requirements in this section of the note.

We assume for these purposes that the firm is issuing ESG ratings (as defined), that it does not benefit from any of the exemptions, and that it is territorially in-scope as a result of operating in the EU.

The ESG Ratings Regulation provides **three alternative routes** to market for non-EU firms.

Route	Summary
Equivalence decision	<p>The regulation anticipates that the European Commission will recognise third country authorisation regimes for non-EU firms as being equivalent. This regime requires both a formal equivalence decision for the third country regime, and cooperation agreements with the regulators in the third country.</p> <p>If and when any such equivalence regime is available, the Non-EU provider will need to submit a formal notification to ESMA of its intent to use the equivalence regime.</p> <p>We note that it's too early to determine whether or when the EU may decide to treat any third country regime as equivalent.</p>
Endorsement	<p>The regulation allows an authorised EU ratings provider to formally "endorse" ratings that are provided by a Non-EU ratings provider in its group. In effect, this regime is designed to allow international groups which have an authorised EU ratings provider to use that EU firm to give a "stamp of approval" to ESG ratings issued by its international affiliates.</p> <p>The regulation sets out formal substance requirements and additional conduct rules for the EU firm, as well as certain conditions around the use and operation of the endorsement process.</p>

Route	Summary
Recognition	The final option for third country firms is to apply to ESMA to be “recognised”. This regime is available to smaller third country firms, and only in the period of time before the Commission adopts an equivalence decision.

We note that none of these options offers a solution which is straightforward or automatic. Each route is subject to prior approval by the EU, and subject to detailed pre-conditions. Any Non-EU firm seeking to rely on any of these routes to operate in the EU will need to take specialist advice, which we are happy to provide as needed.

9. What are the public transparency requirements for ESG ratings?

As noted above, the ESG Ratings regulation includes **detailed public transparency requirements** for in-scope ESG rating providers, to be published on the firm’s website. This applies both to **authorised EU rating providers**, and also to firms which are **exempt** under either or both of:

- Exemption (c) for regulated products and services; or
- Exemption (m) for mandatory SFDR disclosures.

In summary, the additional website disclosures are:

List of information to be included on website
Overview of the rating methodologies used (and changes), including whether analysis is backward-looking or forward-looking and the time horizon covered.
The industry classification used.
Overview of data sources, including whether data is sourced from sustainability statements required under the EU Accounting Directive or from information disclosed under SFDR, and whether sources are public or non-public and an overview of data processes, estimation of input data in case of unavailability and frequency of data updates.
The ownership structure of the ESG rating provider.
Information on whether and how the methodologies are based on scientific evidence.
Information on the ratings’ clearly defined objective and marking whether the rating is assessing risks, impacts, or both, according to the double materiality principle, or any other dimensions, and in the case of double materiality the proportion of the risk and impact materiality.

List of information to be included on website

The rating's scope – i.e., whether it covers an individual factor (E, S, or G) or whether it is an aggregated rating (aggregating E and S and G factor), or whether it covers specific issues (e.g., transition risks).

In the case of an aggregated ESG rating, weighting of the three overarching ESG factors categories (e.g., 33% Environment, 33% Social, 33% Governance), and the explanation of the weighting method, including weight per individual E, S and G factors.

Within the E, S or G factors, specification of the topics covered by the ESG rating/score, and whether they correspond to the topics from the sustainability reporting standards developed pursuant to the EU Accounting Directive.

Information on whether the rating is expressed in absolute or relative values.

Where applicable, reference to the use of Artificial Intelligence (AI) in the data collection or rating/scoring process including information about current limitations or risks of using AI.

General information on criteria used for establishing fees to clients, specifying the various elements taken into consideration, and general information on the business/payment model.

Any limitation in data sources and methodologies used for the construction of ESG ratings.

The main risks of conflicts of interest and the steps taken to mitigate them

if an ESG rating of a rated item covers the E factor, information on whether that rating take into account the targets and objectives of the Paris Agreement or any other relevant international agreements.

if an ESG rating of a rated item covers the E factor, information on whether that rating take into account the targets and objectives of the Paris Agreement or any other relevant international agreements.

Any limitation on the information available to ESG rating providers.

ESMA is mandated to develop **regulatory technical standards (RTS)**, which specify further detail on the presentation of these disclosures.

10. What should firms do now?

Firms have a year and a half from December 2024, before the regulation applies in July 2026.

A key initial task will be **scoping**. Does the firm produce any materials which meet the definition of an ESG rating? If yes, will any one or more of the exemptions apply? (If either the regulated products or services exemption, or the SFDR disclosures exemption applies, then firms should note the additional disclosure requirements).

If a firm is producing ratings, but does not fall within any exemption, then the next step will be to consider the approach either to authorisation (for EU firms) or market access options (for non-EU firms).

Simmons & Simmons stands by to assist with your compliance. Please do contact any of the experts listed below, and we would be pleased to assist.

Key Contacts



Nick Colston
Partner, FS Regulatory
T +44 20 7825 4147
E nicholas.colston



Lucian Firth
Partner, FS Funds
T +44 20 7825 4155
E lucian.firth



Louise Tudor Edwards
Partner, Financial Markets
T +65 6831 5546
E louise.tudor-edwards



Daniel Faundez
Partner, FS Funds
T +44 20 7825 3649
E daniel.faundez



Craig Bisson
Partner, FS Funds
T +44 20 7825 4691
E craig.bisson



James Wallace
Partner, FS Regulatory
T +44 20 7825 4249
E james.wallace



Catherine Weeks
Partner, FS Regulatory
T +44 20 7825 3940
E catherine.weeks



Harald Glander
Partner, Financial Markets
T +49 69 506 072 037
E harald.glander



Daniel Lühmann
Partner, Financial Markets
T +49 69 506 072 023
E daniel.luehmann



Benedikt Weiser
Partner, Financial Markets
T +49 69 506 072 041
E benedikt.weiser



Iris Dingemans
Partner, Financial Markets
T +3120 722 2335
E iris.dingemans



Pieter Leguit
Partner, Financial Markets
T +352 26 21 16
E pieter.leguit



Derek Lawlor
Partner, Financial Markets
T +353 1266 1158
E derek.lawlor



Tristram Lawton
Of Counsel, FS Regulatory
T +44 20 7825 3488
E tristram.lawton



Patricia Schneider

Supervising Associate,
Financial Markets

T +49 69 506 072 036

E patricia.schneider



Katherine Tracey

Of Counsel, FS Funds

T +44 20 7825 4820

E katherine.tracey



William Clarke

Supervising Associate, FS
Regulatory

T +44 20 7825 3782

E william.clarke