

ESG RATING vs CREDIT RATING

Education Series #4



Assessment types

ESG RATING

CREDIT RATING

Definitions

‘ESG rating’ means an **opinion, a score or a combination of both, regarding a rated item’s profile or characteristics with regard to environmental, social and human rights, or governance factors or exposure to risks or the impact** on environmental, social and human rights, or governance factors, that are based on both an established methodology and a defined ranking system of rating categories, irrespective of whether such ESG rating is explicitly labelled as ‘ESG rating’, ‘ESG opinion’ or ‘ESG score’

ESG rating providers regulation - Article 3 (1)

‘Credit rating’ means an **opinion regarding the creditworthiness of an entity**, a debt or financial obligation, debt security, preferred share or other financial instrument, or of an issuer of such a debt or financial obligation, debt security, preferred share or other financial instrument, issued using an established and defined ranking system of rating categories.

CRA regulation - Article 3 (1)(a)

Assessments covered

ESG ratings can assess both the financial materiality and/or the impact materiality of Environmental, Social and Governance factors. They are either expressed as “an opinion, a score or a combination of both”, i.e. a human intervention is not required by the upcoming regulation.

While credit rating agencies shall disclose whether ESG considerations played a material role in the determination of credit ratings, **they focus only on creditworthiness (i.e. financial materiality).** Credit ratings are opinions, i.e. they require a “rating-specific analytical input from a rating analyst”

Dominant business model

Investor-pays
Distribution via subscriptions

Issuer-pays
The rated entity requests the credit rating from the rating agency.

Requirements on methodologies

ESG rating providers shall use rating methodologies for the ESG ratings they provide that are rigorous, systematic, independent and **capable of justification** and shall apply those rating methodologies continuously and in a transparent manner.

ESG rating providers regulation - Article 15 (7)

A credit rating agency shall use rating methodologies that are rigorous, systematic, continuous and **subject to validation based on historical experience, including back-testing**

CRA regulation - Article 8 (3)

Organisational requirements

Highly comparable organizational requirements on both ESG rating providers and credit rating agencies in terms of avoidance of conflict of interests, requirements on rating analysts, pre-disclosure of the rating to the rated entities, disclosures and transparency, registration with and supervision by ESMA.

About EACRA:

The European Association of Credit Rating Agencies (EACRA) is a platform for cooperation among EU-based Credit Rating Agencies (CRAs). Our mission is to support CRAs in meeting regulatory requirements through effective communication, cross-border knowledge sharing, and the promotion of best practices. EACRA also seeks to advance the understanding and value of Credit Ratings within the financial community and among the general public, while advocating for the interests of CRAs across Europe. Established in November 2009 and registered in Paris, EACRA is listed in the French Association Directory (N° W751202513) and the EU Transparency Register (ID 24205924101-57).