

# How should ESG ratings be designed to reflect the sustainability performance of companies?

ESG ratings have become established on the capital market, which make it their business to evaluate the sustainability performance of companies. The ratings often form the basis for investment decisions by sustainability-oriented investors to select suitable securities. In addition, the ESG ratings are used as a basis for compiling company values for sustainability indices. In this context, ratings are of vital importance in assessing performance against the backdrop of the increasing importance of the sustainable capital market.

In principle, the German Chemical Industry Association (VCI) supports the EU Commission's plan to make ESG ratings more transparent with the help of minimum requirements and to make them easier to use for important stakeholders. We would like to support the development of high-quality standards by contributing the practical knowledge of the chemical and pharmaceutical industry. To this end, we have outlined below what we consider to be the key aspects for future regulation:

- 1. Only the uniform definition of ESG ratings for different application purposes enables transparent and comparable performance assessments.**
- 2. The regulation of ESG ratings must include the handling of controversies (e.g. red flags) to establish transparency regarding the approach and scope.**
- 3. To ensure the comprehensibility and comparability of ESG ratings, it is necessary that the same data basis is used, and that recourse is made to established sustainability standards (ESRS).**
- 4. The materiality analyses of companies (and not the rating agencies) must be used to determine the relevant areas for ESG ratings.**
- 5. To ensure that competition-relevant information remains protected, ESG ratings should work exclusively with publicly available data.**
- 6. The inclusion of affected companies in the rating process is indispensable to ensure the completeness and validity of a rating. For this purpose, the rating process should be clearly defined while adhering to appropriate feedback periods.**
- 7. To ensure the objectivity and validity of ESG ratings, an independent arbitration body should be established.**
- 8. Established sector-specific standards and certifications must be recognised and used in performance ratings. In addition, cultural differences must be sufficiently addressed.**

## Summary

ESG ratings are of decisive importance on the capital market in steering investments towards sustainability. It can currently be observed that rating providers have established different approaches to assessing performance. **For investors to be able to make informed investment decisions based on ESG ratings, a standardisation of the requirements on the part of the EU is to be welcomed.** The focus should be on a **practicable design and orientation towards established standards**, and a dialogue process between rating agencies and rated companies should be defined. In this way, the transparency, comparability, and validity of ESG ratings can be increased.