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ESG and Human Rights – What's in it for doing business in Portugal?

ESG topics have risen to the forefront of public policy discussions, and companies have been pressured by European regulations to comply with ESG standards and procedures.

Since the Sustainable Development Goals of the UN 2030 Agenda for Sustainable Development and the affirmation and commitment to these goals in the European Commission's Communication of November 22, 2016, the EU has been working on a legislative package aimed at corporate sustainability and the safeguarding and promotion of human rights.

Here is the status of the main legislative frameworks and proposals.

European Ecological Pact

The European Commission presented on December 11, 2019, the European Ecological Pact (Green Deal), which comprises a set of measures to enable European businesses and citizens to benefit from a sustainable transition, aiming to achieve climate neutrality by 2050, making Europe the first climate-neutral continent, which ultimate aim is to slow global warming, and mitigate its effects.

The European Climate Law (Regulation (EU) 2021/1119), entered into force on 29 July 2021, setting into legislation the aim of a climate-neutral EU by 2050. This law also establishes an intermediate goal of reducing net greenhouse gas emissions by at least 55% by 2030, in relation to 1990 levels.

Furthermore, the Low Carbon Benchmark Regulations (Regulations (EU) 2020/1816 and (EU) 2020/1817) provide new benchmark classifications and require administrators of benchmarks to publish and disclose certain documents and information.

Non-Financial Reporting Directive (Directive 2014/95/EU)

The 2014 Directive sets the rules on disclosure of non-financial information relating to ESG areas (environmental protection, social responsibility and treatment of employees, respect for human rights, anti-corruption and bribery, and diversity on company boards) by certain EU public-interest companies. Decree-law no. 89/2017 transposed this Directive into Portuguese law. These obligations are addressed essentially to big companies and listed ones.

A Proposal for a Corporate Sustainability Reporting Directive was adopted by the Commission on 21 April 2021, which will adjust the current reporting requirements of the Non-Financial Reporting Directive. This new Directive will substantially increase the number of companies covered by the disclosure obligation (from a few dozen to more than 1000 companies).

The Second Shareholders Rights Directive (Directive 2017/828/EU)

Adopted by the European Council in June 2017, the Second Shareholder Rights Directive (SRD II) enhances the shareholders' rights by establishing requirements concerning to the exercise of certain shareholder rights attached to voting shares in relation to general meetings of companies which have their registered office in a Member State and the shares of which are admitted to trading on a regulated market situated or operating within a Member State. The Shareholders Rights Directive II was transposed into Portuguese law by Law no. 50/2020, issued on August 25, 2020.

Sustainable Finance Disclosure Regulation (Regulation (EU) 2019/2088)

The Sustainable Finance Disclosure Regulation entered into force on 29 December 2019 (but effective disclosure duties began in March 2021) and refers to the disclosure of information related to ESG criteria in the financial sector, with respect to financial products, including the impact of ESG risks on their investment decision-making or advisory activities. Broadly speaking, the SFDR aims to ensure that financial market participants consider sustainability and ESG factors in their investment decisions.

Taxonomy Regulation (Regulation (EU) 2020/852)

The Taxonomy Regulation entered into force on 12 July 2020 (but effective consequences are now just starting) and introduces an EU-wide taxonomy of environmentally sustainable activities, therefore establishing a classification system or framework to facilitate financial market participants to invest sustainably – from an *E*(nvironmental) perspective. This Regulation sets sustainability objectives and conditions that need to be met by a business in order to be considered environmentally sustainable.

The Corporate Due Diligence and Corporate Accountability Directive

On 10 March 2021, a proposal for a Directive on Corporate Due Diligence and Corporate Accountability was adopted by the EU Parliament. The Resolution adopted called for mandatory human rights, environmental and governance due diligence requirements across the value chain for companies operating in the EU internal market (companies that are headquartered or do business in the European Union, regardless of their size, shape, nature, sector, and corporate structure), accompanied by reporting and communication obligations regarding the risks identified and the mitigation and prevention measures adopted, with potential sanctions for non-compliance.

Some Member States have already approved legislation (e.g. France, Germany and The Netherlands) and the European Parliament is pushing forward but now it is up to the European Commission to make the next move and start the legislative procedure for this new framework.

What now?

The market is changing, the financial market operators are seeking to achieve a better ESG score and the increase in the European legislation on ESG has been contributing to the adoption of ESG ideals in their investment processes, leading to an inevitable connection between profitable and sustainable investment. These tendencies have warned the Portuguese market operators, who are already starting to address these topics publicly. The ESG regulation will naturally progress in Portugal and the national regulators will be increasingly pressured and encouraged to adapt (and even go beyond) the existing European Regulation to the needs and characteristics of the Portuguese market. Issues such as contracting with companies from countries where freedom of speech is not accepted, contracting with companies who do not comply with environmental standards in their global activities may well be at stake in the near future.

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