

COUNTRY UPDATE-Croatia: ESG reporting

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Environmental, social and governance (ESG) reporting is a major and evolving regulatory area in Europe. Disclosures play a vital role in helping the financial sector address climate change and sustainability. They are also being used to address issues such as poor workplace diversity and gender pay gaps. Several jurisdictions have introduced or plan to introduce measures dealing with ESG risks in supply chains.

After an outline of EU legislative developments, this article provides an overview of ESG law in Croatia by [Marija Gregorić](#) (partner) and [Lovro Klepac](#) (senior associate) of [Babic & Partners Law Firm LLC](#), Zagreb.

Principal EU ESG reporting legislation

Implementation of the EU's Sustainable Finance Action Plan is now well advanced. The plan contains three legislative measures:

- The [Sustainable Financial Disclosure Regulation 2019/2088](#) (SFDR) imposes disclosure requirements on financial market participants. SFDR came into effect for 'level 1' disclosures in March 2021 and it is planned that more onerous 'level 2' disclosures will be required from January 2023.
- [Taxonomy Regulation 2020/852](#) standardises definitions and processes to be used when determining whether an activity is environmentally sustainable or meets other ESG criteria for disclosures under SFDR. The Taxonomy Regulation came into force in July 2020 and has applied in practice since January 2022.
- A proposed Corporate Sustainability Reporting Directive COM(2021)189 (CSRD), in effect replacing the [Non-Financial Reporting Directive 2014/95](#) (NFRD). This will apply to many more companies than the NFRD, greatly extend the ESG information they must disclose and be aligned with the SFDR and Taxonomy Regulation.

Trilogue negotiations on CSRD started in March 2022 between the EU Parliament, Council and Commission. The EU Parliament and the Council reached political agreement on the proposal for a CSRD in their trilogue meeting on June 21, 2022. Its implementation has been postponed to 2024, with first companies' CSRD compliant

reports to be published in 2025. Consultation on draft European Sustainability Reporting Standards (ESRS) for the CSRD started on April 29, 2022.

Proposed EU due diligence directive

In February 2022, the European Commission published a proposal- COM(2022) 71- for a Corporate Sustainability Due Diligence Directive (CSDDD).

CSDDD would impose a duty of due diligence on large companies and medium sized ones in high-impact sectors. They would have to identify actual or potential adverse environmental and human rights impacts of their activities, their subsidiaries' and in their value chain.

ESG in Croatia

1. Which national authority or authorities oversee ESG reporting?

ESG reporting requirements imposed with the transposition of NFRD into Croatian Accounting Act are overseen by the Croatian Ministry of Finance. According to Article 39 of the Croatian Accounting Act, Croatian Ministry of Finance is authorized to monitor compliance with non-financial reporting requirements either via direct or indirect supervision.

Based on Article 14(1) of the SFDR and Article 21 of the Taxonomy Regulation, Croatia is required to ensure that competent authorities designated in accordance with the sectoral legislation referred to in Article 6(3) SFDR and in accordance with Directive 2013/36/EU, transposed into Croatian Credit Institutions Act (Official gazette no. 159/13, 19/15, 102/15, 15/18, 70/19, 47/20, 146/20), monitor compliance of financial market participants and financial advisers with the requirements of SFDR.

According to Article 11 of the Croatian Act on enforcement of SFDR and Taxonomy regulation adopted on July 3, 2021 ("Enforcement Act"), the Croatian Financial Services Supervisory Agency (HANFA) is authorized to monitor compliance with SFDR and Articles 5, 6 and 7 of the Taxonomy Regulation. HANFA is authorized to monitor compliance with the above rules, as well as the Enforcement Act by (i) financial market participants (as defined under Article 2(1) of the SFDR), (ii) pension insurance company with respect payments of pensions within voluntary pension insurance scheme and (iii) financial advisers from Article 2(1) of the SFDR.

The Enforcement Act has implemented rules on HANFA's supervisory and investigatory powers in monitoring compliance of the obliged entities in accordance Article 14 of the SFDR and Article 21 of the Taxonomy Regulation. Specifically, Enforcement Act provides that HANFA has the powers set forth under the laws governing the conduct of business by supervised entities, i.e., the laws governing insurance undertakings, investment firms, alternative investment fund managers, voluntary pension funds, UCITS funds, capital markets, as well as the powers set under Regulation (EU) 2019/1238 on a pan-European Personal Pension Product. Furthermore, Enforcement Act authorizes HANFA to request access to any and all documents required for purpose of supervising compliance with SFDR, Taxonomy Regulation and the Enforcement Act from the supervised entities.

HANFA is also authorized to oversee compliance with ESG reporting requirements that apply to issuers of financial instruments traded on the regulated market (such as Zagreb Stock Exchange).

2. What ESG reporting or ESG due diligence regulatory developments have there been in Croatia since May 1, 2021?

Since May 1, 2021, the Croatian Parliament adopted the Enforcement Act, which entered into force on July 3, 2021. The Enforcement Act defines entities that are subject to the rules set forth in the SFDR, as well as entities which are required to apply Articles 5 – 7 of the Taxonomy Regulation, sets forth detailed rules on transparency of integration of sustainability risks (Article 6 of the SFDR), transparency of adverse sustainability impacts at financial product level (Article 7 of the SFDR), transparency of the promotion of environmental or social characteristics in pre-contractual disclosures (Article 8 of the SFDR), as well as on transparency of sustainable investments in pre-contractual disclosures (Article 9 of the SFDR).

Furthermore, as of July 29, 2021, the Croatian Capital Markets Act has introduced additional rules on gender pay gap analysis, as described in more detail below in response to question no.7.

3. Briefly, how great a change to existing Croatian legislation would be required to implement the CSRD, as currently drafted?

The existing Croatian legislation (specifically, the Croatian Accounting Act) has implemented NFRD. In this regard, the existing legislation will need to be changed to the extent that CSRD amends NFRD.

4. Does any national law require firms to disclose the environmental/ sustainability impact of their activities, or of companies in which they invest?

Yes. The Enforcement Act, which sets forth detailed rules on implementation of SFDR and Taxonomy Regulation, provides that financial market participants and financial advisers must include in their remuneration policies the information on how those policies are consistent with the integration of sustainability risks. Specifically, the relevant information should be included (i) by an insurance undertaking in its remuneration policy from Article 275 of the Commission Delegated Regulation 2015/35; (ii) by an insurance intermediary in its remuneration policy as specified under the Croatian Insurance Act; (iii) by an investment firm in its remuneration policy which needs to be implemented for all categories of employees, for the management board, supervisory board, and other relevant persons in accordance with the Croatian Capital Markets Act; (iv) by a credit institution which provides investment services in its remuneration policy adopted in accordance with the Croatian Credit Institutions Act; (v) by an alternative investment fund (AIF) manager (AIFM) in its remuneration policy which applies to senior management, risk takers, control functions, and all employees receiving total remuneration that takes them into the same remuneration bracket as senior management and risk takers if professional activities have a material impact on the risk profiles of the AIFMs or of the AIFs they manage (as set forth in the Alternative Investment Funds Act); (vi) by a UCITS management company in its remuneration policy which applies to senior management, risk takers, control functions, and all employees receiving total remuneration that takes them into the same remuneration bracket as

senior management and risk takers if professional activities have a material impact on the risk profiles of the management company or of the funds they manage (as specified in the Croatian UCITS Act); (vii) by a management company of a voluntary pension fund in its remuneration policy adopted in accordance with the Croatian Voluntary Pension Funds Act; and (viii) by a pension insurance company in its remuneration policy adopted in accordance with the Croatian Pension Insurance Companies Act. The Enforcement Act also sets out detailed rules about the disclosure of the information in pre-contractual documents, as well as of the information on promotion of environmental or social characteristics and of sustainable investments in periodic reports.

In addition, under the Croatian Companies Act, a supervisory or management board of a company whose stocks are traded on a regulated market is required to ensure that the management or the executive directors provide at least the following information in a separate section of the company's annual report: (a) the information about the code of corporate governance to which the company is subject and/or which the company voluntarily applies, and/or corporate governance practices which the company applies in addition to those strictly necessary under the law, as well as the information on where such corporate governance codes and practices are published; and (b) the information on whether the company departs from the above codes or practices of corporate governance, the extent to which it does, as well as the reasons thereof. The Code of Corporate Governance adopted by HANFA and Zagreb Stock Exchange requires from a company listed on Zagreb Stock Exchange to comply with certain rules on ESG reporting. In particular, the supervisory board and the company's management must align and adopt policies on (i) assessment of environmental and social impact of company's activities, as well as on management of related risks; (ii) protection of human and employees' rights; and (iii) prevention and sanctioning of bribery and corruption. The above policies must be published on the company's website and must be made available free of charge. Furthermore, when the company's management is requesting a prior approval of a resolution by the supervisory board, the documents accompanying the proposal for the relevant resolution must explain how the proposed measure/resolution aligns with the above company's ESG policies.

Under the Rules of Zagreb Stock Exchange, issuers of financial instruments whose stocks are traded on Zagreb Stock Exchange are subject to the Code of Corporate Governance, and each issuer company is required to provide the completed compliance questionnaire to the stock exchange by June 30 and to publish the questionnaire on its website. The above provisions of the Rules of Zagreb Stock Exchange are also based on the Croatian Capital Markets Act, which expressly requires from the issuers to provide information, documents and statements related to corporate governance as well as to the application of the code of corporate governance based on HANFA's requests. Failure to comply with such HANFA's request constitutes a violation of the Croatian Capital Markets Act and is subject to fines set in the range between HRK 50,000 – 100,000 (about EUR 6,700 – 13,400) for the company and between HRK 5,000 – 10,000 (about EUR 670 – 1,340) for the responsible individuals (e.g., directors).

There are no additional national laws (other than SFDR and Croatian Accounting Act transposing NFRD) that require firms to disclose the environmental / sustainability impact of their activities, or of companies in which they invest. Croatian law transposing

Directive 2016/2341 (EU) on the activities and supervision of institutions for occupational retirement provision mandates that an institution for occupational retirement provision invests in accordance with the "prudent person" rule. The institution for occupational retirement provision may consider the potential long-term impact of investment decisions on environmental, social and governance factors when applying "prudent person" rule to its investments. However, there are no requirements for disclosure of environmental / sustainability impacts of firms' activities or investments.

5. Does any national law regulate whether an activity or investment can be classified or promoted as sustainable/ environmentally friendly?

No, other than the Taxonomy Regulation, Croatian national legislation does not regulate whether an activity or investment can be classified as sustainable / environmentally friendly.

6. Does any national law or regulatory guidance cover workplace diversity, for example, the representation of women on a firm's management or supervisory body?

The Croatian Gender Equality Act (Official gazette no. 82/08, 69/17), transposing Directive 2006/54/EC, sets out general rules covering workplace diversity and anti-discrimination, including in the area of employment. Under Article 11 of the Croatian Gender Equality Act, state-owned legal entities and public authorities are required to apply specific measures and adopt action plans aimed at promoting and establishing gender equality, which should be approved by the Croatian Government's Gender Equality Office.

The Croatian Gender Equality Act requires that any job advertisements clearly provide that persons of both genders may apply for the advertised posting. Under Article 15 of the Croatian Gender Equality Act, political parties are required to respect the principle of gender equality and to account for balanced participation of women and men within candidacy lists when proposing candidates for election to the European Parliament, Croatian Parliament, and local or regional representative bodies. Specifically, political parties are required to ensure that there is no significant imbalance between women and men in their candidacy lists, i.e., that participation of persons of each gender amounts to at least 40%. Infringement of rules on balanced participation of women and men within candidacy lists of political parties is subject to fines set in the range between HRK 20,000 – 50,000 (about EUR 2,650 – 6,610) for a political party.

In addition, the Croatian Employment Act (Official gazette no. 93/14, 127/17, 98/19) and Croatian Anti-Discrimination Act (Official gazette no. 85/08, 112/12) provide for general rules prohibiting discrimination based on gender (including provisions on equal pay for women and men) and other grounds, for example, religion, belief, disability, age, sexual orientation, gender identity etc. However, Croatian laws do not contain general rules implementing specific workplace diversity measures in private sector companies, such as a rule requiring representation of all genders on a firm's management or supervisory body.

This said, the Code of Corporate Governance which applies to companies whose stocks are traded on Zagreb Stock Exchange expressly provides that the company's supervisory board must include members of different genders, age, profiles, and experience in order to ensure diversity when adopting resolutions. This requirement is

also reflected in the questionnaire which must be provided by each company listed on a regulated market (i.e., Zagreb Stock Exchange) to HANFA by June 30 each year. Furthermore, the information which must be provided to HANFA annually within the above questionnaire, necessarily includes diversity related data such as the number of female members on the company's management board, supervisory board, as well as the number of female employees within the company, etc.

Croatian sector-specific legislation contains very few provisions governing workplace diversity. For example, the Croatian Credit Institutions Act provides that the Croatian National Bank (HNB) collects information about the diversity policy with regard to selection of members of the management bodies of credit institutions, its objectives and any relevant targets set out in that policy, and the extent to which these objectives and targets have been achieved, which must be published by a credit institution in accordance with Article 435(2)(c) of the Regulation 575/2013 (EU).

7. Does any national legislation require firms to report on gender or other diversity pay gaps?

The law does not expressly require a firm to report on gender or other diversity pay gap; however, recent amendments to the Croatian Capital Markets Act (implementing Directive (EU) 2019/2034 on the prudential supervision of investment firms) have introduced new rules governing the reporting and collection of information on gender pay gaps for investment firms. Specifically, under the Croatian Capital Markets Act, HANFA is authorized to collect the information published in accordance with Article 51(1)(c) and (d) of the Regulation (EU) 2019/2033, as well as the information on gender pay gaps provided by investment firms and used to benchmark remuneration trends and practices. Although the law does not explicitly mandate that an investment firm reports gender pay gap information to HANFA (e.g., by way of a periodical report), the law does require from an investment firm to have a gender neutral remuneration policy and to internally supervise the implementation of such policy, while HANFA is authorized to request from the investment firm the provision of various information, including on total remuneration for all members of the company's managing body / senior management.

8. Are firms under any national legal duty to identify or mitigate environmental, human rights or other ESG risks at subsidiaries or in their supply chain?

No, other than the duties set forth in the Croatian Accounting Act implementing NFRD, firms are under no specific national legal duty to identify or mitigate environmental, human rights or other ESG risks at subsidiaries or in their supply chain.

Specifically, the Croatian Accounting Act provides that large undertakings which are public-interest entities exceeding on their balance sheet dates the criterion of the average number of 500 employees during the financial year, shall include in the management report a non-financial statement containing information necessary for an understanding of the undertaking's development, performance, position and impact of its activity, relating to, as a minimum, environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters, including: (a) a brief description of the undertaking's business model; (b) a description of the policies pursued by the undertaking in relation to those matters, including due diligence processes implemented; (c) the outcome of those policies; (d) the principal risks related to those matters linked to

the undertaking's operations including, where relevant and proportionate, its business relationships, products or services which are likely to cause adverse impacts in those areas, and how the undertaking manages those risks; (e) non-financial key performance indicators relevant to the particular business. The undertaking's subsidiary is exempted from the above obligation if the subsidiary and its subsidiary undertakings are included in the consolidated management report or the separate report of another undertaking.

Furthermore, public-interest entities which are parent undertakings of a large group exceeding on its balance sheet dates, on a consolidated basis, the criterion of the average number of 500 employees during the financial year, shall include in the consolidated management report a consolidated non-financial statement containing information necessary for an understanding of the group's development, performance, position and impact of its activity, relating to, as a minimum, environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters specified above under items (a) – (e) which relate to the group.