Submission: Climate-related financial disclosure

17 February 2023

Overview

The Responsible Investment Association Australasia (RIAA) thanks Treasury for the opportunity to comment on the *Climate-related financial disclosure Consultation paper* (consultation paper).

RIAA strongly supports the introduction of a robust, fit-for-purpose mandatory climate-related financial disclosure regime in Australia. This will constitute another important step towards a much-needed broader sustainability reporting regime.

Many of Australia's global partners are mandating sustainability disclosures. Without equivalent mandatory standards, Australian markets will increasingly lag behind the rest of the world. This is because investors will continue to struggle to obtain high-quality, consistent corporate disclosures in the Australia market, resulting in a loss of confidence detrimental to investment attraction and retention.

Mandatory local sustainability disclosure standards, provided they are harmonised with leading global developments, and cover an appropriate range of entities, will play a key part in revitalising Australian markets. They will send a strong signal that Australia is one of a growing number of countries that acknowledge the significance of accurate and useable sustainability information in markets. They will also provide deeper understanding and certainty to investors, in turn attracting domestic and international capital. Clear mandatory disclosure and overarching regulation are critical for the competitiveness of key Australian industries into the future.

In RIAA's view, the key priorities for the new disclosures regime should be:

- alignment with the International Sustainability Standards Board (ISSB), and adapting to Australia with a building-block approach,
- a fit-for purpose regulatory framework that can be expanded to incorporate broader sustainability disclosures,
- Government support for companies under the mandatory regime, including:
    - prompt introduction, with targeted, time-bound transitional arrangements to address key challenges for preparers and audit/assurance providers,
    - support from government including free, fit-for-purpose data access, and climate scenarios, and
    - practical regulatory guidance on aspects of disclosures that present challenges.

RIAA's responses to Treasury's consultation questions are detailed below. RIAA's position broadly aligns with other recent submissions on sustainability standards:

- Empowering the AASB to deliver sustainability standards (December 2022),
- Submissions to ISSB draft standards: ISSB [Draft] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information, ISSB [Draft] IFRS S2 Climate-related Disclosures (July 2022), and
- AASB consultation on ISSB standards: AASB ED 321: ISSB Draft Standards – S1 General Requirements for Disclosure of Sustainability-related and Financial Information and S2 Climate-related Disclosures (July 2022).

RIAA was also an active contributor to the detailed cross-industry submission on the ISSB's draft standards: Joint Australian bodies submission on the International Sustainability Standards Board's draft standards (July 2022).

Recommendations

Reform principles

1. Specify the intended outcomes of the mandatory disclosures regime, and set performance indicators to track and measure the impact of the regime.

Process

2. Promptly adopt an internationally-aligned mandatory disclosures framework, to deliver benefits to companies, investors, consumers and government, and avoid the costs of delayed action.

Covered entities and timing

3. All reporting entities required to prepare financial reports under the Corporations Act, and equivalent Commonwealth reporting entities required to prepare annual financial statements, should be covered by the climate reporting regime.
4. Phase 1 of the mandatory climate disclosures regime should commence in 2024-25.
5. Phase 1 should cover S&P/ASX300 companies, financial institutions with consolidated annual revenue of over $100 million or $5 billion or more in AUM, and any other companies covered by the Safeguard Mechanism and/or NGER Scheme, as well as equivalent Government entities.
6. Phase-in should recognise the need for investors and other financial institutions to have investee company disclosures, in order to prepare their own high-quality disclosures.
7. Large proprietary companies and any Government entities not covered in phase 1 should be a priority in subsequent phases.
8. Government should support SMEs indirectly covered by the mandatory reporting regime, at minimum, through Regulatory Guidance on scope 3 reporting.

International alignment of disclosures

9. Align Australia's mandatory climate reporting regime with the ISSB standards, with a view to how this will evolve into the global minimum baseline for a broader sustainability reporting regime.
10. Apply Australia-specific considerations including our significant physical risks of climate change, the urgent need to embed leading standards and keep pace with international developments, and the global challenge of incorporating other prominent reporting frameworks.

Regulatory framework for required disclosures

11. The regulatory framework should be mandatory, flexible, consistent, appropriately resourced, and supported by guidance.

Periodic reporting requirements

12. Ensure location requirements for disclosures align with ISSB requirements for connectivity, and enable investors to easily understand and navigate sustainability disclosures.

Materiality of climate risks

13. Australia should adopt the ISSB materiality definition and guidance.
14. Australia should embed a broad definition of materiality which includes the external impacts of the company.
15. Robust Regulatory Guidance should ensure that materiality assessments are consistent and appropriate to the Australian market.

Assurance of climate risks

16. Assurance of sustainability disclosures should be equivalent to audit requirements for financial statements, subject to targeted transitional arrangements.

Reporting of metrics (including emissions), offsets and transition plans

17. Transition plan and offset requirements should align with ISSB requirements and include:

    - interim targets, to set out and track the trajectory towards long term goals,
    - the governance structures and lines of responsibility to achieve the transition plan,
    - the levels of offsets used, or planned to be used, and
    - application of the Oxford Offsetting Principles.

18. Mandate disclosure of scope 1, 2 and 3 emissions.
19. Take a leading role in the ISSB's work to shape and influence the global industry-specific standards and ensure adopted standards are fit-for-purpose.
20. Transitional arrangements should provide a genuine benefit for both companies and investors, be specific and time-bound and suitable for a range of companies.

Data and capability to support climate reporting

21. Establish a free, fit-for-purpose repository of Government climate-related data for company use.
22. Set internationally-aligned scenarios for Australia.

Governance of supporting information for disclosures

23. Provide consistent climate scenarios and Regulatory Guidance on challenging areas, including materiality, 'reasonable basis' for forward-looking statements, emissions reporting and for asset owners and managers.

Proportionate application of liability

24. Liability risks for certain types of disclosures should be addressed through regulatory guidance, disclosure of assumption and methodologies, and collaborative development of best practice guidance and tools.

Interaction with other reporting obligations

25. The Government should develop a mandatory disclosures regime that will allow for the incorporation of other sustainability disclosure requirements into the reporting mechanism.

Other implementation issues

26. Design the climate disclosures framework to accommodate broader sustainability disclosure requirements in future, in line with the direction of the ISSB, international markets and investor and community expectations.
27. Follow international direction and mandate digital reporting, to improve efficiencies and insights.

Ensuring the financial reporting framework is fit for purpose to support climate risk disclosures

28. Establish a regulatory structure in line with Treasury's Option 2, for international alignment, or Option 3 (with additional consultation), to better integrate reporting standards, stakeholder input, international developments and advice to Government.
29. The regulatory structure should be appropriately resourced, independent and required and capable of incorporating industry, including investor, views into standards development; and have sufficient expertise in climate change and broader sustainability issues. .

About RIAA and our members

RIAA champions responsible investing and a sustainable financial system in Australia and Aotearoa New Zealand, and is dedicated to ensuring capital is aligned with achieving a healthy society, environment, and economy.

With more than 500 members managing more than USD29 trillion in assets globally, RIAA is the largest and most active network of people and organisations engaged in responsible, ethical and impact investing across Australia and Aotearoa New Zealand. RIAA's membership includes superannuation funds, KiwiSaver default providers, fund managers, banks, consultants, researchers, brokers, property managers, community trusts, foundations, faith-based groups, financial advisers, financial advisory groups, and others involved in the finance industry, across the full value chain of institutional to retail investors. RIAA represents 58% of all managed funds in Australia.

Representing over 80 Aotearoa New Zealand members, and having engaged with the Aotearoa New Zealand Government in the development of its mandatory climate reporting regime, RIAA is in a unique position to provide informed comment on the Australian Government's proposal.

Response to consultation questions

Reform principles

RIAA strongly supports Treasury's six 'reform principles' guiding the establishment of a mandatory climate disclosures regime (consultation paper, page 6).

In our view, this reform could and should deliver the following outcomes:

1. **Support climate goals**
    a. Capital shifts towards investments which support the Paris Agreement and achieving or exceeding Australia's commitments to emissions reduction and net zero.
    b. Companies are prompted to accelerate their climate change mitigation and adaptation measures.
2. **Improve information flows**
    a. Investors, fund managers, advisers and others can more accurately evaluate and compare risks and opportunities.
    b. Climate risk is efficiently priced, and companies with strong strategies and performance are advantaged in the market.
    c. Consumers and clients benefit from better-informed and more efficient decision-making by institutional investors, through potential improvements to investment performance and fees.
    d. Disclosure processes and governance reduce the risks of greenwashing.
    e. Increased investor confidence in risks and opportunities, and valuation.
    f. Company and investor efforts towards improving real-world sustainability outcomes are highlighted.
    g. Governments and investors gain insights on systemic risks in markets or sectors, and the macroeconomic implications of those risks.
3. **Well-understood**
    a. Regulatory guidance provides practical support for reporting entities on the key priorities and challenges in sustainability reporting, and is refined to target areas for improvement.
    b. Over time, companies better understand, measure, manage and communicate their sustainability-related risks, opportunities and impacts.
4. **Internationally aligned**
    a. Australia's reporting framework aligns with the ISSB as a minimum baseline.
    b. Australia's reporting framework is enhanced using a 'building blocks' approach, to meet leading international practice.
    c. Australian regulatory guidance is closely aligned with international guidance, ideally through IOSCO-aligned guidance.

5. **Scalable and flexible**
    a. The climate disclosures regime is the first stage in establishing a fit-for-purpose sustainability disclosures framework which incorporates broader sustainability issues over time.
6. **Proportional to risk**
    a. Investors have climate risk information on key companies and sectors.
    b. Companies which present higher risks and/or significance in Australia's climate commitments have a higher level of transparency.
    c. Companies are incentivised to place appropriate governance around their climate-related risks and opportunities, including board oversight and executive responsibilities and/or accountabilities.
    d. Large institutional investors, as universal owners, are better placed in the economy-wide climate transition.

These reforms will make Australian markets immediately more transparent, making them attractive and viable for both local and international investors.

To ensure the impacts of the mandatory disclosures regime reflect the reform principles, the Government should set performance indicators and measure progress in the market. This could include setting a baseline prior to the introduction of the mandatory disclosures regime and tracking progress through data analysis and qualitative research. Key baseline information could include:

- The proportion of investments in Australia aligned with Australian and global emission reduction targets and net zero goals,
- Qualitative assessment of current voluntary disclosures by companies:
    - targeted at companies of a significant size, sector, emissions intensity etc,
    - focused on key elements or metrics of disclosures, for example, scenario analyses and scope 3 emissions disclosures,
    - to map types of governance and processes for climate and broader sustainability disclosures.
- Qualitative assessment of how investors use climate and sustainability disclosures in decision-making.
- How effectively existing regulatory guidance is used by companies in Australia and overseas.

Recommendation 1: Specify the intended outcomes of the mandatory disclosures regime, and set performance indicators to track and measure the impact of the regime.

Process

Question 1: *What are the costs and benefits of Australia aligning with international practice on climate-related financial risk disclosure (including mandatory reporting for certain entities)? In particular:*

1.1 What are the costs and benefits of meeting existing climate reporting expectations?

1.2 What are the costs and benefits of Australia not aligning with international practice and in particular global baseline standards for climate reporting?

RIAA strongly supports international alignment of the Australian climate disclosures regime.

Aligning Australia with prevailing international practices and frameworks will be a strong signal that Australia is a stable, transparent and mature market. This means alignment with the International Sustainability Standards Board's (ISSB) standards as a baseline, which draw on and align with the Taskforce on Nature-related Financial Disclosures (TCFD). This is imperative for Australian companies, investors and the broader economy.

Many international partners, competitors and significant economies have either introduced, or are in the process of developing, mandatory climate reporting regimes. Australian regulation is now playing 'catch up' with many of global trade partners and key markets. The adoption of an internationally-aligned disclosure regime is time-critical.

The significant benefits of Australia aligning with international practice would include:

For reporting companies, reduced time, cost and complexities in preparing disclosures under misaligned frameworks and standards.

- **For investors**, reduced time, cost and complexities in assessing and comparing disclosures, and being better-informed when they make decisions to allocate capital.
- **For clients and consumers**, such as superannuation fund members, benefits from the flow-on effects of improved efficiencies, including:
  - institutional investors making better-informed decisions, which positively impact long-term returns, and
  - fees which reflect the efficiency gains for the asset owners and managers servicing them.
- **For regulators and other users of disclosures**, easier interpretation of disclosures due to consistency and greater transparency.
- **For companies seeking capital**, more opportunities to attract Australian and international investors due to stronger transparency and attractiveness to banks committed to climate action.
- **For Australian exporters,** streamlining the preparation and assurance of disclosures that are required to participate in international markets.[1]
- **For Australian investors in international markets**, ease and efficiencies in navigating company disclosures which are more easily comparable.

We also highlights other benefits identified in the Investor Group on Climate Change (IGCC) submission to this consultation, such as levelling the playing field for companies, and positioning Australia as a global leader in physical risk disclosure.

If Australia does not promptly align our disclosures requirements with international practice, we risk missing opportunities with real consequence. For example:

- a lack of international alignment could cause duplication of work for companies and investors, and provide the market with conflicting information that is not easily comparable,
- the costs of duplicative work are likely to increase sharply over time, as more markets move towards alignment of climate disclosure requirements, and
- other markets may gain comparative advantages over Australia due to Australia being – and being seen to be – a laggard on the provision of climate-related information.

The transition away from high-emitting industries inevitably poses social challenges in communities currently relying on high-emitting industries for jobs, and will require strong economic and social planning. The social and economic challenges and the community level have been well-documented. This cost or risk of economic transition needs to be closely managed, to provide a just transition for affected communities. Some investors recognise their role in a just transition, as illustrated in RIAA's *Human Rights and Climate Change – a guide for institutional investors*. This can be done effectively, with enough Government investment and appropriate planning, and support for the workers and broader communities affected, as has been the case in Germany's phase out of coal.[2]
If the Australian Government acts promptly, it can still equip Australian investors and companies with the efficiencies, capabilities and understanding of climate risks and opportunities for Australian industry – and communities – to thrive. If done well, the broader impacts on markets, consumers and the Australian economy could be profound.

Recommendation 2: Promptly adopt an internationally-aligned mandatory disclosures framework, to deliver benefits to companies, investors, consumers and government, and avoid the costs of delayed action.

[1] For example, the European Union will soon introduce its Carbon Border Adjustment Mechanism, to apply tariffs on imports of some carbon-intensive products such as iron, aluminium and electricity. This means Australians exporting to the EU must clearly state the greenhouse gases embodied in their products. This will be simpler if robust assurance is in place from appropriately skilled and accredited auditors.
[2] See Andrea Furnaro, Philipp Herpich, Hanna Brauers, Pao-Yu Oei, Claudia Kemfert, and Wesley Look, *German Just Transition: A Review of Public Policies to Assist German Coal Communities in Transition*, Report 21-13, November 2021.

Covered entities and timing

Question 2: *Should Australia adopt a phased approach to climate disclosure, with the first report for initially covered entities being financial year 2024-25?*

2.1 What considerations should apply to determining the cohorts covered in subsequent phases of mandatory disclosure, and the timing of future phases?

Question 3: *To which entities should mandatory climate disclosures apply initially?*
3.1 What size thresholds would be appropriate to determine a large, listed entity and a large financial institution, respectively?
3.2 Are there any other types of entities (that is, apart from large, listed entities and financial institutions) that should be included in the initial phase?

RIAA strongly supports Treasury's proposals to:

- phase entities into the mandatory disclosures regime, and
- commence phase 1 in the 2024-25 financial year.

Timing

Commencement of the regime in 2024-25 strikes the appropriate balance between the need to keep pace with international markets, and the readiness of companies and sectors to prepare climate disclosures. It is clear the Australian market is ready for the introduction of mandatory climate disclosures, given many companies are already reporting voluntarily against climate reporting frameworks (see further our responses to questions 9 and 12) and the TCFD in particular has been a workable framework for many years.

Phase 1

From its introduction in FY 2024-25, the mandatory disclosures regime should cover:

- **Large listed companies:** companies in the S&P/ASX 300,
- **Large financial institutions:** banks, insurers, superannuation funds and managed funds with annual consolidated revenue of more than $100 million or total AUM of $5 billion or more,[3]
- **Heavy emitters:** Companies which, due to the emissions intensity of their activities, are covered by the Safeguard Mechanism and/or reporting requirements under the *National Greenhouse and Energy Reporting Act 2007* (NGER) scheme, including Government, public and proprietary entities, and
- **Equivalent federal, state and territory Government entities**: State, territory and federal Governments should enter into the requisite agreements to ensure that all Government entities equivalent to large proprietary companies and large financial institutions are covered by the regime. This will be important to meet wider policy objectives of this policy, in particular, national alignment with the Paris Agreement.

These types of entities are currently best-placed to report under the new disclosures regime, and their climate-related risks and opportunities represent a significant share of the market.

It is particularly important to include unlisted entities because:

- for some investors, smaller, unlisted entities form a sizable part of their portfolios and constitute a significant portion of the investors' own emissions,

[3] These definitions of 'large listed company' and 'large financial institution' reflect recommendations 11 and 12 of the Australian Sustainable Finance Roadmap in relation to the first phase of voluntary industry reporting against the Taskforce on Climate-related Financial Disclosures (TCFD) framework.

- if unlisted entities do not have to report under the regime, there may be a risk of regulatory arbitrage or a 'loophole' where companies fall outside the reporting requirements, despite being significant in their size, sector and/or level of emissions, and
- it will be important for investors, Government and others to get an understanding of economy-wide emissions, and Australia's national progress – or lack thereof – towards emissions targets.

Reporting by investors

Some investors, including many RIAA members, are both users and preparers of corporate disclosures. Asset owners and asset managers rely on the information disclosed by investee companies to prepare significant parts of their own disclosures. The implications of this include:

- if a significant portion of investee companies are covered by the mandatory climate disclosures regime, investors will be better placed to prepare high-quality, comprehensive climate disclosures, and
- investors will need time to incorporate investee company information into their own disclosures, particularly in the initial reporting period, which includes their global holdings.

Subsequent phases

At the end of any transitional arrangements, all reporting entities required to prepare financial reports under the *Corporations Act 2001*, and equivalent Commonwealth reporting entities required to prepare annual financial statements, should be covered by the climate reporting regime.

The phase-in of entities into the mandatory reporting regime should follow a clear pathway to the end point.

There are several considerations in the phase-in of entities to the climate reporting regime.

Government entities

Government entities which are not covered in phase 1 should be a priority in subsequent phases.

Large proprietary companies

Any company which is a 'large proprietary company' according to the revenue, assets and/or employees thresholds under section 45A of the Corporations Act, and is not covered by phase 1, should also be a priority in subsequent phases.

Sector prioritisation

The materiality of climate change to a particular sector should be a factor in prioritising how companies are phased into the regime (for example, the energy and resources sector is an obvious priority due to the high emissions intensity of these sectors).

Unintended coverage of smaller companies

It is likely that a significant number of smaller companies which are not required to report under the mandatory regime will nonetheless need to prepare some climate information to provide to larger entities. For example, an entity may need to provide data on their emissions to a large financial institution for that large entity to report on its scope 3 emissions.

There will be a particular need for Government support for SMEs indirectly brought under the regime. This should include at minimum, clear Regulatory Guidance for SMEs required to provide information to investors or other financial institutions for the purpose of scope 3 emissions reporting.

Importance of Government signals and guidance

RIAA supports IGCC's recommendations, as contained in its submission to this consultation, that Government should send clear and early signals to the market about which entities will be covered under and under which phases, and that guidance and capability building will be important in subsequent phases, which will cover more entities that are not currently reporting on a voluntary basis.

Recommendation 3: All reporting entities required to prepare financial reports under the Corporations Act, and equivalent Commonwealth reporting entities required to prepare annual financial statements, should be covered by the climate reporting regime.

Recommendation 4: Phase 1 of the mandatory climate disclosures regime should commence in 2024-25.

Recommendation 5: Phase 1 should cover S&P/ASX300 companies, financial institutions with consolidated annual revenue of over $100 million or $5 billion or more in AUM, and any other companies covered by the Safeguard Mechanism and/or NGER Scheme, as well as equivalent Government entities.

Recommendation 6: Phase-in should recognise the need for investors and other financial institutions to have investee company disclosures, in order to prepare their own high-quality disclosures.

Recommendation 7: Large proprietary companies and any Government entities not covered in phase 1 should be a priority in subsequent phases.

Recommendation 8: Government should support SMEs indirectly covered by the mandatory reporting regime, at minimum, through Regulatory Guidance on scope 3 reporting.

International alignment of disclosures

Question 4: *Should Australia seek to align our climate reporting requirements with the global baseline envisaged by the International Sustainability Boards?*

4.1 Are there particular considerations that should apply in the Australian context regarding the ISSB implementation of disclosures relating to: governance, strategy, risk management and/or metrics and targets?

4.2 Are the climate disclosure standards being issued by the ISSB the most appropriate for entities in Australia, or should alternative standards be considered?

RIAA supports the alignment of Australia's climate disclosures standard with the ISSB standards, as the emerging minimum global baseline.

The additional considerations for Australia are:

- **Physical risks:** The significant physical risks of climate change in Australia should be a consideration in the provision of Government support, for example, in data provision and regulatory guidance.
- **Embed international best practice:** Given Australia lags behind parts of the world in climate disclosures, we should urgently establish standards which reflect international best practice in leading markets such as the European Union and United Kingdom. This could be achieved through a 'building blocks' approach, using the ISSB standards as a baseline, which Australia's regulatory framework must support.
- **Keep pace with leading practice:** Australian sustainability standard setters should factor in leading international trends in the ongoing development, consultation and formulation of sustainability standards in Australia.
- **Align with other leading frameworks:** The ISSB consolidates the Climate Disclosure Standards Board (Climate Disclosure Project) and Value Reporting Foundation (Sustainability Accounting Standards Board and International Integrated Reporting Council) and is influenced by the TCFD framework. However, it does not yet formally align with the Global Reporting Initiative framework and the emerging Taskforce on Nature-related Financial Disclosures framework. Alignment and interoperability with these is a significant global challenge but one that standard setters, including in Australia, must get right.

Alignment is important to support companies and investors through the adoption of a mandatory disclosure regime, and to maximise our opportunities with international markets and investors.

For Australia's sustainability disclosure standards to succeed, they must be interoperable with key markets, now and in future.

Recommendation 9: Align Australia's mandatory climate reporting regime with the ISSB standards, with a view to how this will evolve into the global minimum baseline for a broader sustainability reporting regime.

Recommendation 10: Apply Australia-specific considerations including our significant physical risks of climate change, the urgent need to embed leading standards and keep pace with international developments, and the global challenge of incorporating other prominent reporting frameworks.

Regulatory framework for required climate disclosures

Question 5: *What are the key considerations that should inform the design of a new regulatory framework, in particular when setting overarching climate disclosure obligations (strategy, governance, risk management and targets?*

The regulatory framework should be:

- **Mandatory**, to level the playing field for companies and encourage them to provide investors with high-quality and consistent information,
- **Flexible**, so that over time it can continue to meet leading international practice, incorporate additional sustainability standards and reporting approaches, such as integrated reporting,
- **Consistent**, enabling investors to rely on and compare information between companies and sectors,
- **Appropriately resourced**, to support high-quality reporting and empower standard setters to keep pace with international developments, and
- **Supported by guidance**, to enhance compliance with the regime and the effectiveness of disclosures in the market.

Recommendation 11: The regulatory framework should be mandatory, flexible, consistent, appropriately resourced, and supported by guidance.

Periodic reporting requirements

Question 6: *Where should new climate reporting requirements be situated in relation to other periodic reporting requirements? For instance, should they continue to be included in an operating and financial review, or in an alternative separate report included as part of the annual report?*

The goal of location requirements should be to ensure that sustainability information is presented in a way that is relevant to investor needs, easily navigated and understood and of equivalent status to financial data.

Requirements for where sustainability disclosures fit in companies' reporting ecosystem should be aligned with the relevant ISSB standard/s as a baseline. RIAA broadly agrees with the connectivity requirements proposed in [Draft] IFRS S1, which reflect the close relationship between various elements of general purpose financial reports and sustainability reports. This approach will encourage more fit-for-purpose reporting, enabling investors to understand how sustainability risks and opportunities are being managed and how these feed into a company's financial outlook. We note that the ISSB has prioritised work on connectivity of sustainability and financial reports.

Recommendation 12: Ensure location requirements for disclosures align with ISSB requirements for connectivity, and enable investors to easily understand and navigate sustainability disclosures.

Materiality of climate risks

Question 7: *What considerations should apply to materiality judgements when undertaking climate reporting, and what should be the reference point for materiality (for instance, should it align with ISSB guidance on materiality and is enterprise value a useful consideration)?*

RIAA supports Australian alignment with the current proposed ISSB definition plus guidance, as the global baseline.

We note that the ISSB draft standards proposed an 'enterprise value' concept of materiality, which the ISSB has subsequently moved away from. The ISSB materiality definition will align with the IASB definition, that is: 'information material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general-purpose financial reporting make on the basis of' that reporting. The 'enterprise value' definition is unlikely to be useful, given the prevailing international standard has now shifted away from that approach.

In our view:

- Australia should align with the ISSB definition and guidance,
- Australia should embed in our market a broad definition of materiality which includes the external impacts *of* the company, which over time become impacts *on* the company,
- Robust Regulatory Guidance will be needed to ensure that this core element of the disclosures regime is applied consistently and is appropriate to Australian companies and markets.

Recommendation 13: Australia should adopt the ISSB materiality definition and guidance.

Recommendation 14: Australia should embed a broad definition of materiality which includes the external impacts of the company.

Recommendation 15: Robust Regulatory Guidance should ensure that materiality assessments are consistent and appropriate to the Australian market.

Assurance of climate risks

Question 8: *What level of assurance should be required for climate disclosures, who should provide assurance (for instance, auditor of the financial report or other expert), and should assurance providers be subject to independence and quality management standards?*

As an end goal, assurance of sustainability disclosures should be equivalent to audit requirements for financial statements. This aligns with the likely direction of the ISSB standards.

Given current capacities of the audit and assurance sector, and preparer experience, this is one area where targeted transitional arrangements may be appropriate. For example, there may be a transition from limited to reasonable assurance, and assurance which is fit-for-purpose for climate-related disclosures.

Recommendation 16: Assurance of sustainability disclosures should be equivalent to audit requirements for financial statements, subject to targeted transitional arrangements.

Reporting of metrics (including emissions), offsets and transition plans

Question 9: *What considerations should apply to requirements to report emissions (Scope 1, 2 and 3) including use of any relevant Australian emissions reporting frameworks?*

RIAA has long supported international progress towards mandatory scope 1, 2 and 3 emissions disclosure. Transparency across the value chain is critical for investors to effectively gauge the climate risks and impacts of companies.

The significance of scope 1, 2 and 3 emissions varies significantly depending on sector. For example, while steel and transport sector emissions are predominantly scope 1, across all sectors globally, scope 3 emissions on average account for around 75% of companies' total GHG emissions.[4] ACSI research also found that 93 companies in the ASX200 were already reporting their scope 3 emissions data in 2022.[5]

In this context, it is both practical and necessary for scope 3 emissions reporting to be mandated.

Question 10: *Should a common baseline of metrics be defined so that there is a degree of consistency between disclosures, including industry-specific metrics?*

Common baselines, including at the industry level, are important for consistency and comparability across disclosures, which is in turn important for good investment decision-making.

We note that the ISSB intends to develop industry-specific sustainability standards and metrics based on the internationally established SASB standards. Australia should take a leading role in shaping and influencing the global industry-specific standards, and in ensuring industry-specific metrics and standards adopted in Australia are fit-for-purpose.

Question 11: *What considerations should apply to ensure covered entities provide transparent information about how they are managing climate related risks, including what transition plans they have in place and any use of greenhouse gas emissions offsets to meet their published targets?*

Company transition plans enable investors to understand not just the climate risks and opportunities of a business, but also what the company is doing to align its business model to national and global goals for emissions reduction and global warming limits. This is important information for investors to assess the likely medium to long term value of an entity, and can significantly differentiate companies in the same sector.

It is also important that transition plans enable investors to assess an entity's real progress on reducing its impact on climate change, as well as its performance against its transition plan and other aspects of its disclosures.

In our submission on ISSB draft S2 Climate-related disclosures, RIAA supported the ISSB's proposals for transition plans and recommended that transition plan requirements include:

- interim targets, to set out and track the trajectory towards long term goals, and
- the governance structures and lines of responsibility to achieve the transition plan.

We also note IGCC's five principles for credible transition plans, which provide valuable direction for companies.[6]

---

[4] CDP Technical Note: Relevance of Scope 3 Categories by Sector, 2022-23, pp 5-6.
[5] ACSI, Promises, pathways and performance. Climate change disclosure in the ASX200, 2022, p 17.
[6] IGCC, *Corporate transition plans: A guide to investor expectations*, March 2022.

Offsets

The ultimate objective of action on climate change is to keep global temperature rises below the goal of the Paris Agreement. The use of offsets to meet climate targets at the national or company level can obscure true progress towards that goal.

Regarding the use of offsets:

- the level of offsets used, or planned to be used, is important information for investors to assess the contribution of offsets to transition plans, and to compare companies within the same sector, and
- we agree with the Australian Council of Superannuation Investors (ACSI) submission to this consultation that the Oxford Offsetting Principles should apply, including cutting emissions first, using high-quality offsets, and revising offsetting strategy as best practice evolves.[7]

RIAA supported the ISSB's proposed detail on carbon offsets in its draft S2. Adopting these requirements should enable investors to better understand how an entity is reducing emissions, and the credibility and integrity of the offset component.

Recommendation 17: Transition plan and offset requirements should align with ISSB requirements and include:

- interim targets, to set out and track the trajectory towards long term goals,
- the governance structures and lines of responsibility to achieve the transition plan,
- the levels of offsets used, or planned to be used, and
- application of the Oxford Offsetting Principles.

Question 12: *Should particular disclosure requirements and/or assurance of those requirements commence in different phases, and why?*

Specific and finite transitional arrangements could be useful to ensure that a robust mandatory disclosures regime is introduced in a way that is both timely and practical. This can address the challenge of meeting the needs of investors for timely information, while also ensuring accuracy in data, methods, assumptions and the resulting disclosures.

We note that many Australian companies are already committed to global and national climate goals, and are voluntarily disclosing climate information to the market. For example:

- in mid-2022, 103 ASX 200 companies were fully or partially aligning their disclosures to the TCFD framework, and TCFD disclosure was more prevalent in higher-risk sectors such as energy and utilities.[8]
- in December 2022, 45% of ASX companies had net zero commitments for scope 1 and 2 GHG emissions targets, and 96% of ASX Scope 1 and 2 emissions were covered by net zero targets (68% of these were covered by 1.5 degree-aligned targets), and
- also in December 2022, one-third of ASX companies fully disclosed Scope 3 emissions, and 9% of ASX companies had net zero targets for Scope 3 emissions in line with a 1.5-degree pathway.[9]

In this context, any transitional arrangements should be:

- **Specific** and targeted only to the part/s of disclosures where transitional arrangements are needed (for example, due to the preparedness of audit/assurance providers), and will provide a genuine benefit for

---

[7] See Principle 1 of *The Oxford Principles for Net Zero Aligned Carbon Offsetting*, Smith School of Enterprise and the Environment, University of Oxford, September 2020.
[8] ACSI, *Promises, pathways & performance: Clima/te change disclosure in the ASX200*, July 2022, p 6.
[9] FTSE Russell, *COP27 Net Zero Atlas*, November 2022; Climateworks Centre, *Net Zero momentum tracker*, November 2022.

companies and investors. An obvious example is reporting of scope 3 emissions of certain types of entities, which may present challenges in early reporting periods.
- **Time-bound,** specifying for example that relief only applies to the first reporting period under which a company is required to report under the mandatory regime.
- **Suitable for a range of companies**, including those that are already providing disclosures, for example, by specifying that the disclosure of scope 3 emissions is voluntary in the first reporting period, as has been the case for mandatory climate-related disclosures in Aotearoa New Zealand.

Recommendation 18: Mandate disclosure of scope 1, 2 and 3 emissions.

Recommendation 19: Take a leading role in the ISSB's work to shape and influence the global industry-specific standards and ensure adopted standards are fit-for-purpose.

Recommendation 20: Transitional arrangements should provide a genuine benefit for both companies and investors, be specific and time-bound and suitable for a range of companies.

Data and capability to support climate reporting

Question 13: *Are there any specific capability or data challenges in the Australian context that should be considered when implementing new requirements?*
13.1 How and by whom might any data gaps be addressed?
13.2 Are there any specific initiatives in comparable jurisdictions that may assist users and preparers of this information in addressing these challenges?

Companies which are leading in climate disclosures practice are already providing useful information to markets based on available data. A lack of perfect data, or gaps in data, should not prevent companies from providing disclosures. Disclosures which are qualified and incomplete are likely in the early periods of reporting.

Government support for data and capability could significantly boost the quality and usefulness of disclosures for a broad array of companies, and level the playing field for companies under the mandatory regime.

Key areas where Government could add significant value include:
- a free and fit-for-purpose single repository of Government climate-related data (for example, on physical risk) for companies to use to prepare strategies, plans and disclosures, and
- setting internationally-aligned, Australian-specific scenarios for scenario analysis, which would address a significant challenge for preparers and improve the credibility, consistency and comparability of disclosures for investors.

Recommendation 21: Establish a free, fit-for-purpose repository of Government climate-related data for company use.

Recommendation 22: Set internationally-aligned scenarios for Australia.

Governance of supporting information for disclosures

Question 14: *Regarding any supporting information necessary to meet required disclosures (for instance, climate scenarios), is there a case for a particular entity or entities to provide that information and the governance of such information?*

The key supporting information from Government that is required to ensure companies can prepare robust disclosures includes:

- Consistent climate scenarios for use in scenario analysis (see above)
- Regulatory Guidance on areas which are challenging, including:
  - determining materiality,
  - deeper guidance on what is a ‘reasonable basis’ for forward-looking statements in the context of climate disclosures,
  - emissions reporting, particularly scope 3, and
  - specific guidance for asset owners and assets managers who are required to report under the regime.

Recommendation 23: Provide consistent climate scenarios and Regulatory Guidance on challenging areas, including materiality, ‘reasonable basis’ for forward-looking statements, emissions reporting and for asset owners and managers.

Proportionate application of liability

Question 15: *How suitable are the ‘reasonable grounds’ requirements and disclosures of uncertainties or assumptions in the context of climate reporting? Are there other tests or measures that could be considered to ensure liability is proportionate to inherent uncertainty within some required climate disclosures?*

The current ‘reasonable basis’ requirements for corporate disclosures under the Corporations Act are an important and appropriate framework for climate risk reporting.

RIAA refers to the legal opinion of Sebastian Hartford-Davis and Kelly Dyon of Counsel, attached to this submission. This opinion was sought by ACSI, IGCC and RIAA in response to earlier discussions about the risks to entities and directors in complying with the draft ISSB standards, specifically in relation to forward-looking statements.

Counsel’s opinion states:

- **The draft ISSB requirements are consistent with existing directors duties:** The ISSB draft standards require disclosures which are more numerous and specific than, but broadly consistent with, existing requirements for listed companies. Company directors should already be considering these things in the proper discharge of their directors duties. It follows that ‘for diligent company directors properly supported by competent management, the ISSB Draft Standards should not increase directors’ exposure’ (para 6).
- **The 'reasonable basis’ requirements acknowledge uncertainty:** The requirement to have a ‘reasonable grounds’ for making forward-looking statements is ‘capable of being sensitive to the inherent uncertainties in the scope, distribution, impacts and timing of the impacts of climate change’. The Corporations Act requires genuine assessment of the appropriateness of forward-looking statements when they are made, but directors will not be liable solely because an assessment is later found to be incorrect (para 6).
- **A safe harbour is not required:** A safe harbour for climate and/or sustainability-related disclosures is not necessary or desirable (Section D.2). ‘Investors and courts do not expect companies to predict the unpredictable, but instead to make sensible disclosures on a reasonable basis, and to update earlier disclosures if they become misleading by reason of later events’ (para 59). For example, for scope 3

emissions disclosures, using a supplier's scope 1 and 2 emissions data would likely form a 'reasonable basis', provided there was not a reason to mistrust that data, and that it included disclaimers about the reliability of the data (para 60).

- **ISSB standards may assist directors and companies to manage liability:** The draft ISSB standards have a 'significant capacity to *assist* company directors' by clarifying the things that may already be required under existing directors duties and company reporting requirements. The draft ISSB standards may also help directors to ensure management is doing what is required to minimise liability risks (para 33).

As this submission previously noted (see questions 9 and 12 above), the proposed mandatory requirements are emerging from disclosure frameworks which many companies are already reporting against voluntarily. These companies are already managing the liability risks of forward-looking statements in climate disclosures within the existing legal framework.

Mandating specific climate-related disclosures recognises the increasing prominence of climate related information in investor decision-making. Investors rely on climate disclosures, including forward looking statements, to inform significant decision-making, and must be able to have confidence in the information on which they are basing decisions.

Institutional investors make decisions which affect the wealth and retirements incomes of millions of Australians. There are significant real-life impacts of investor decision-making, and climate risk and opportunities are highly relevant to company valuation and performance. In this context, companies and directors should be legally required to make forward-looking statements about climate risks and opportunities on a reasonable basis.

Investors recognise that uncertainty and assumptions are inherent in some types of disclosures. However, reduced liability for disclosures risks diluting the value of the regime.

The challenges faced by companies preparing climate disclosures, particularly in the early reporting periods, should be addressed through:

- Regulatory Guidance on what constitutes a 'reasonable basis' for forward-looking statements in climate and broader sustainability disclosures,
- disclosure of data sources, assumptions, methodologies and use of disclaimers which will assist investors to understand the 'reasonable basis' for forward-looking statements, and
- collaborative development of best practice guidance and tools for climate disclosures by companies, investors and regulators.

We strongly recommend Counsel's view on the principles that should be followed by directors to minimise liability risks as a valuable starting point for Regulatory Guidance and best practice guidance and tools. These include (para 61 of the opinion):

- governance, process and monitoring,
- expert input and independent assurance,
- description of specific assumptions, methodologies and time periods for forward-looking climate information and scenario analysis of physical and transition risk,
- warnings and cautionary language, and
- consideration of requirements under ASIC's RG 170 Prospective financial information.

Recommendation 24: Liability risks for certain types of disclosures should be addressed through regulatory guidance, disclosure of assumption and methodologies, and collaborative development of best practice guidance and tools.

Interaction with other reporting obligations

Question 16: *Are there particular considerations for how other reporting obligations (including continuous disclosure and fundraising documents) would interact with new climate reporting requirements, and how should these interactions be addressed?*

The Government should consider how other disclosure obligations interact with sustainability reporting obligations in the preliminary design of the climate disclosures regulatory framework. Companies and investors will benefit from aligned reporting structures, which will ensure efficiency in reporting activities.

For example, companies with revenue of $100 million per annum or more are required to lodge modern slavery statements under the *Modern Slavery Act 2018*. This corporate sustainability reporting requirement is currently administered by the Department of Home Affairs. This should be either brought under a future sustainability reporting regime, or clear alignment drawn with the sustainability reporting regime. Clarifying the coverage of companies under various sustainability reporting requirements is another important consideration.

It is clear that, globally, reporting on biodiversity and nature risks and opportunities under the Task Force on Nature-related Financial Disclosures (TNFD) is also fast gaining ground, particularly as it relates closely to climate related risk.

The Government should hence develop its climate related financial disclosures regime with a view to ensuring the ability to incorporate mandatory reporting on factors such as nature and modern slavery risk in the future.

Recommendation 25: The Government should develop a mandatory disclosures regime that will allow for the incorporation of other sustainability disclosure requirements into the reporting mechanism.

Other implementation issues

Question 17: *While the focus of this reform is on climate reporting, how much should flexibility to incorporate the growth of other sustainability reporting be considered in the practical design of these reforms?*

As noted above, the regulatory framework established for climate disclosures must be able to incorporate other sustainability disclosures standards in future. This would ensure Australia's regulatory framework continues to provide alignment with the likely direction of the ISSB and key overseas markets, and better equip investors to understand companies' broader sustainability risks and commitments, as well as make it easier for companies and investors to comply

Importance of broader sustainability information

The broader sustainability risks of companies, and the extent of their commitment to the SDGs, are increasingly linked to company performance. For example, the TNFD is already starting to lift investors' and companies' understanding of the critical nature of biodiversity risks and opportunities for a range of industries. More stark examples are the Juukan Gorge and Rana Plaza disasters, which demonstrated that a company's impact on communities, and breaches of human rights, are intrinsically linked to the company's value.

International alignment

The ISSB is developing additional standards within its disclosure framework, and likely to focus initially on the incorporation of nature-related risks and opportunities. This appears to be broadly following the direction of the EU, where European Sustainability Reporting Standards are being phased in and will cover an array of sustainability topics beyond climate change. These topics include:

- Cross-cutting: General requirements, General disclosures.
- Environment: Pollution, Water and marine resources, Biodiversity and ecosystems, Resource use and circular economy,
- Social: Own workforce; Workers in the value chain, Affected communities, Consumers and end-users.
- Governance: Business conduct.

Recommendation 26: Design the climate disclosures framework to accommodate broader sustainability disclosure requirements in future, in line with the direction of the ISSB, international markets and investor and community expectations.

Question 18: *Should digital reporting be mandated for sustainability risk reporting? What are the barriers and costs for implementing digital reporting?*

The ISSB is currently consulting on whether digital reporting should be mandated under the ISSB standards. We hereby highlight the IGCC's comments on the growing number of overseas jurisdictions – including key trade partners – that mandate digital reporting, as contained within IGCC's submission to this consultation.

This would provide significant advantages to investors, given the scope to aggregate, compare and analyse sustainability information in digital form. More useable information should bring efficiencies and insights to investors that flow on to more informed decision-making and more competitive costs to clients and consumers. Particularly if this is the international direction, Australia should mandate digital sustainability reporting.

Recommendation 27: Follow international direction and mandate digital reporting, to improve efficiencies and insights.

Ensuring the financial reporting framework is fit for purpose to support climate risk disclosures

Question 19: *Which of the potential structures presented (or any other) would best improve the effectiveness and efficiency of the financial reporting system, including to support introduction of climate related risk reporting? Why?*

Treasury's proposed Options 2 or 3 would be the best structure for a mandatory sustainability reporting regime in Australia.

As noted above (question 5), Australia's regulatory structure should be flexible enough to incorporate broader sustainability standards, and to support integrated reporting practices, which are increasingly common in some overseas markets.

We support the ACSI recommendation that, whichever option the Government choses, the regulatory structure should:

- be appropriately resourced to develop and set climate and sustainability standards,
- be required and capable of incorporating the views of industry, including investors, into standards development,

- have sufficient expertise in climate change and broader sustainability issues, including biodiversity and human rights. We would note in particular the importance of expertise in First Nations Peoples Rights, and
- be independent.

Option 1

RIAA has supported the interim role of the AASB in setting sustainability standards, as proposed in late 2022, to enable prompt introduction of sustainability standards in Australia. However, this is unlikely to be the best long-term governance structure for Australian sustainability standards.

Governance arrangements for standards should be appropriate to the respective standards and reflect prevailing international approaches. Option 1 is unlikely to provide this, and would not give sustainability reporting in general appropriate status in Australia.

Option 2

Option 2 broadly reflects the position of the ISSB under the IFRS Foundation, and it would give the new sustainability standards board equal status to the AASB and AUASB, and a level of independence.

This appears to be a more straightforward approach than Option 3, as it retains the existing structure for the FRC, AASB and AUASB. However, it may not be the best option to future-proof the regulatory structure, or to ensure close alignment between reporting standards.

Option 3

A single entity which would set standards, oversee financial reporting and advise Government could ensure more consistent development and connection between standards, the flexibility to set further sustainability standards and potentially better-enable integrated reporting.

This could ensure flexibility and future-proofing for standards setting. A single, integrated body would also be well-placed to undertake the important work of stakeholder consultation, monitoring of the external environment – including alignment with international developments – and advice to Government, and to build expertise both internally and across other Government agencies.

We note that this option would require significant change to the existing standard-setting structures and warrants further consultation, including on what the implications would be for the FRC, AASB and AUASB.

Recommendation 28: Establish a regulatory structure in line with Treasury's Option 2, for international alignment, or Option 3 (with additional consultation), to better integrate reporting standards, stakeholder input, international developments and advice to Government.

Recommendation 29: The regulatory structure should be appropriately resourced, independent and required and capable of incorporating industry, including investor, views into standards development; and have sufficient expertise in climate change and broader sustainability issues.