Australian Chamber of Commerce and Industry

Sustainable Finance Strategy

ACCI Submission

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1. Introduction

The Australian Chamber of Commerce and Industry (ACCI) appreciates the opportunity to provide comment to the Treasury on the *Sustainable Finance Strategy* and the implementation of standardised, internationally aligned requirements for disclosure of sustainability and climate-related financial risk and opportunities in Australia.

In recent years, investors have increasingly taken action to integrate climate change and broader sustainability concerns into their investment decisions and portfolio allocations. However, there is a widely perceived need for greater certainty on the environmental sustainability of different types of investments and economic activities. Research by PwC Australia showed that in FY22, 49 per cent of the ASX200 disclosed a net-zero target, a 13 per cent increase on FY21, and significant work is underway on transitional planning and Board upskilling[1]. Many corporates and other organisations are undertaking efforts to increase their sustainability disclosures, which extends beyond net zero to include broader environmental impacts intrinsic to a holistic sustainability program.

A number of countries have been implementing more advanced regulations concerning sustainability-related disclosure. The United Kingdom's Green Finance Strategy and the EU's newly formed Corporate Sustainability Reporting Directive require investment firms and fund companies to disclose sustainability risks more fully. In part, New Zealand has instituted an International Climate Finance strategy, complemented by ongoing efforts to create a sustainable finance taxonomy specific to New Zealand.

Acknowledging that this space is relatively new, there are some gaps in disclosure, participation and credibility of sustainability and climate-related financial disclosure. ACCI had recommended in its submission for the Climate-related Financial disclosure that the ISSB-S2 standard should be used as a base for developing the Australian standard. The Australian climate disclosure standard must be aligned with the new ISSB-S2 standards to ensure consistency at the international level and avoid duplication. This alignment is equally pertinent in the development of sustainability-related financial disclosures, including those associated with the Taskforce on Nature-related Financial Disclosures (TNFD) in the Australian context. Ensuring conformity with the international framework is essential to minimise the compliance burden on businesses and to guarantee consistency in reporting requirements across states and territories.

Businesses in Australia are already heavily regulated. The introduction of sustainability-related financial disclosure requirements adds to the administrative burden and compliance costs entities must undergo. Australia needs a tax and regulatory environment that enables our industries to compete in the international market and make Australia a more attractive destination for foreign businesses to engage and invest. As such, the processes of sustainability-related financial disclosures need to be streamlined to minimise regulatory burden and avoid disrupting business as usual. A threshold on the size of the business involved should also be set, acknowledging the relevance of reporting to certain businesses and their ability to resource disclosure processes.

However, we caution that the benefits of standardised reporting frameworks need to be appropriately weighed against the deterrence and barriers placed upon stakeholders engaging in the Australian marketplace and the regulatory burden placed on business.

[1] PwC, *ESG tends in 2023*, April 2023

2. Sustainable finance taxonomy

The global momentum behind the development of sustainable finance taxonomies has surged in recent years. However, this surge is not without its challenges, as there exists no settled consensus on the definition of a 'sustainable' entity or a universally accepted metric for measuring sustainability in the context of general corporate purpose lending — an integral component of our comprehensive corporate financing portfolio. ACCI recommends that the criteria for defining the sustainable activities should align with the ISSB standard to ensure international consistency. The criteria set should allow flexibility to businesses to determine which sustainability-related risks and opportunities are material to the organisation's goals and can have a financial consequence on the company's reports.

Moreover, the actions of a business working to create a positive impact on one goal may result in other impacts. For example, should we expect public transport that supports social inclusiveness by connecting communities in remote areas to also align with our environmental objectives to be recognised as 'sustainable'?

Even though EU Sustainable Finance Taxonomy has taken steps to address this complexity through overarching principle to incorporate minimum safeguards and the requirement to 'Do No Significant Harm' to any of the other EU Taxonomy objectives. However, the practical application of this principle is challenging, requiring a degree of subjective interpretation and estimation.

ACCI agrees strong international alignment is important to minimise compliance costs for Australian based multinational corporations. In developing the Australian standard taxonomy, taxonomies in other countries like EU taxonomy, Southeast Asian Nations Taxonomy, Climate Bonds Initiative Taxonomy, should be used as a benchmark to ensure consistency and comparability for businesses operating and investing internationally.

The introduction of government-sponsored taxonomies could lead to a substantial increase in demand for data from issuers and investors to verify the eligibility of activities and/or investments. The availability of data emerges as a central issue in the widespread adoption of taxonomies. Successful implementation requires a certain standardization of the provided data, facilitating aggregation and assessment of compliance in a consistent and comparable manner.

An additional crucial consideration is the "ease of use" of a taxonomy. In Australia, where businesses already face pressures due to high inflation and interest rates, the introduction of a mandatory taxonomy framework could strain financial and human resources. This underscores the importance of making taxonomy compliance achievable for smaller businesses and financial market participants. ACCI recommends adopting a proportionality approach when designing compliance and verification criteria.

Recommendation 1: Ensure close alignment of the Australian taxonomy with those of other countries to guarantee consistency and comparability for businesses engaged in international operations and investments.
Recommendation 2: Adopt a proportionality approach in designing compliance and verification criteria for the Australian taxonomy to ensure ease of use.

3. Transitional Planning

The reporting requirements against ISSB-S1 standards are high. The ISSB-S1 requires all businesses to disclose significant sustainability-related risks and opportunities that can reasonably be expected to affect a business's value. These include write-downs to fixed asset values, availability and cost of labour and materials, or the impact of carbon prices on a business's bottom line if introduced to drive decarbonisation. Businesses must quantify and disclose the current and anticipated future effects of significant sustainability and climate-related risks and opportunities on their business model and value chain over the short, medium and long term.

There continues to be a gradual improvement in voluntary reporting of these disclosures around the risk of climate change to Australian businesses, just over half (55 per cent) of ASX200 identify climate change as a current or emerging risk that is being considered by the board and management. More companies are reporting net zero targets, with 49 per cent of ASX200 committing to net zero[2]. Of these, half (55 per cent) of ASX200 include a reasonable level of detail on a transition plan to achieve their target.[3]

With the current reporting regime being voluntary, the volume of reporting in measuring climate and sustainability performance has increased. And, if the government goes beyond the ISSB-S1 disclosure requirements in prescribing the regulations, it risks imposing a huge regulatory burden on businesses as smaller businesses lack the appropriate resources and time to compile the information necessary to disclose their climate and sustainability-related risks.

Recommendation 3: The sustainability-related financial disclosure framework should remain flexible for voluntary participation.
Recommendation 4: The government must exercise caution in expanding regulations beyond ISSB-S1 disclosure requirements to avoid imposing a significant regulatory burden, especially on smaller businesses lacking adequate resources and time for compiling necessary information.

4. Transparency in Climate Risks and Sustainability

A significant barrier to the appropriate valuation of business investment in climate-related practices is a lack of transparency and the potential for false or misleading claims. Greenwashing is prevalent in the market and can significantly derail the effectiveness of the proposed climate and sustainability disclosures. If claims are not verified by independent sources or accompanied by assurances, then the trust stakeholders and investors place on climate and sustainability-related disclosure is jeopardised. This would undermine and undervalue honest climate and sustainability-related governance, strategy and risk management investments made by business.

ASIC is appropriately resourced in this area to regulate sustainability rating providers. An example is the current backlash which sustainability investing is facing in the United States. A few years back investors were embracing sustainable investing. In 2021, when Hartford Funds inserted sustainable into the name of its core brand product, it subsequently saw investors pour in $100 million. However, after missing its performance targets last year, and with tightened regulatory oversight on greenwashing, it rebranded the

[2]PwC, *ESG Reporting in Australia-Change afoot, but are companies ready?*
[3] ibid

fund back to its conventional name.[4] Similarly, Deutsche Bank's investment arm, DWS Investment Management Americas, agreed to pay $19 million to settle an investigation into alleged greenwashing by the firm for overstating how the company factored sustainability data into investment decisions.[5]

The absence of a common definition for sustainability ratings leads to confusion and misunderstandings by investors and issuers. While the existence of different methodologies and approaches reflects the diversity of client needs, varying degrees of methodology and data transparency further limit the comparability of these ratings and the ability to understand what the main drivers and limitations are.

Consequently, sustainability ratings do not serve their purpose and do not sufficiently enable investors consumers and other stakeholders to make informed decisions as regards to sustainability-related risks, impacts and opportunities. To ensure transparency sustainability rating providers should be encouraged to publish information on the source of the data and the methodology used in determining sustainability ratings. Greater transparency also supports the more appropriate use of such scores by companies, financial institutions, and central banks for a range of sustainability objectives.

Recommendation 5: To address greenwashing and enhance the credibility of climate and sustainability disclosures, sustainability rating providers must publish information on data sources and methodologies

5. Data and Analytical Challenges

A significant gap in the reporting of sustainability data arises from the inherent challenges associated with the potential forward-looking nature of reporting, particularly when aligning with the International Sustainability Standards Board (ISSB) standards. Estimating the potential future financial impact on a specific asset or liability balance or revenue or cost line under evolving scenarios carries risk. Adopting disclosures while maintaining commercial/competitive advantage also presents a challenge.

An example is the significant amount of data required to measure and report on Scope 3 emissions as required for Climate-related Financial Disclosure. The disclosure of Scope 3 emissions is very complex and challenging, including data availability, calculation methodologies, scoping and organisational barriers. In addition, there are inherent limitations of the methodology for Scope 3 emissions accounting and reporting, which can result in double counting the emissions. Further, the cost associated with verifying the data reported that underpin the disclosure across essential topics is high. While initially only larger companies are responsible for reporting their scope 3 emissions, much of this data is sourced from smaller businesses further down their supply chain. If these smaller businesses cannot provide the necessary information, they risk losing contracts with larger businesses. Furthermore, requiring small businesses to provide data on their scope 3 emissions, is a substantial administrative burden and challenging without a standardised framework.

The sustainability performance and reporting by the businesses is currently in the early stages of development. While some consultants do provide assurance services, often this work is highly subjective, due to the lack of experience and the absence of an established consistent framework for undertaking these audits and making the certification. Finding people with the right skills in the existing labour market shortage is a challenge. In recent years, the consulting firms have been actively recruiting staff and building teams to undertake sustainability-related assurance work, but these young recruits often have a

[4] Financial News, *Wall Street's ESG craze is fading.*
[5] ibid

background in tax and not carbon accounting and other sustainability measures. Further, companies still need to improve sustainability competencies at the board and executive levels. Recent research shows that of companies disclosing climate change performance, only 25 per cent have of at least one board member and 7 per cent have an executive, with the skills and training to be competent in reporting this information.[6]

Recommendation 6: Scope 3 emissions should not be included in the climate-related financial, due to the reliability of the data and the increased administrative burden.

6. Design of Regulatory framework (Fit for purpose)

The development of the regulatory framework for sustainability-related financial disclosure should adopt a least-burdened approach. Businesses in Australia are already weighed down by overbearing regulation and adding to this would cause significant unrest and uncertainty in the business community. It is important that operations are not impacted or hindered dramatically from their current state, and correspondingly the design of the regulatory framework should build upon existing requirements to disclose any material risk. Reinventing the wheel enforces significant changes to the flow of business operations, disrupting productivity, output and confidence. Comparatively, using existing disclosure requirements and developing them to incorporate sustainability-related finances, whilst still adding to administrative burden, is a least-burdensome approach and avoids major disruptions to business.

Recommendation 7: The design of the regulatory framework must take a least-burdensome approach and build upon the existing disclosure requirements.

7. International Alignment

The Australian market is increasingly attracting global investors and many Australian businesses operate and invest internationally. International alignment of sustainability-related reporting is essential in providing consistency and comparability for businesses operating and investing internationally. To avoid fragmentation and overburdening business with administrative and compliance costs, Australia must align with international baselines.

Furthermore, the information disclosed cannot be compared when the data is misaligned. This undermines and undervalues the sustainability-related investments and practices that a business engages, ultimately disincentivising needed progress. For these reasons, ensuring that the reporting requirements in Australia are aligned to international standards is important as well as these requirements need to cater effectively to the issues that are most relevant for Australia's economy.

Given these concerns, a number of countries have started to legislate to create official definitions of sustainable finance products. For instance, In United States banks and borrowers have collaborated to create new financial instruments, such as sustainability-linked loans and sustainability-linked bonds which require businesses to report their long-term energy transition plans and ESG objectives voluntarily. The Sustainable Finance Action Plan introduce by EU require businesses to mandatory report whether – and

[6] PwC, *ESG Reporting in Australia-Change afoot, but are companies ready?*

to what extent they or their investee companies' activities make a substantial contribution to any of the environmental objectives listed under the taxonomy regulation. These regulations imposed are quite broad in their scope and stringent in their requirements. And would have far reaching impacts on Australian businesses, who are operating in or seeking investment from EU entities as they will need to adhere to taxonomy and regulatory requirements.

Moreover, as these new frameworks like ISSB standards and sustainable finance taxonomies mature, interoperability across different markets and countries will be vital to promote cross-border sustainable finance flows. It is also important that the reporting requirements are consistent across taxonomies so that the investors can easily assess whether activities in international markets align with their own strategies and with regulatory requirements in Australia.

Recommendation 8: Reporting requirements, whilst closely aligned to international standards, should be fit to the Australian context and unified across states and territories.

8. Australia as a global sustainability leader

Australia proactively contributes to international efforts to mitigate, ameliorate and adapt to the economic, social, and environmental impacts of climate change in the most effective, efficient and equitable way.

Australia's sustainable finance objectives and framework should be consistent with global taxonomies, taking account of Australia's circumstances, including international relationships, and be set at the national level covering all sectors of the economy. This is essential so that Australian businesses are not placed at a competitive disadvantage relative to businesses in other countries with less ambitious emissions reduction targets.

Sustainable finance policy should prioritise competitive, market-based solutions that provide economy-wide benefits, while delivering sustainable long-term emissions reductions at lower costs. Australia should adopt a no regrets policy approach, with the focus on developing productivity enhancing new technologies that strengthen the economy and at the same time deliver sustainable outcomes. Any policies and measures should aim to minimise regulation and government subsidies. They should also be consistent with the principles of equity (sharing the mitigation effort fairly across industries and states/territories), risk management, least cost abatement, and policy stability.

Australian business and their skilled workforce have the potential to play a major role in improving sustainable outcomes across the economy. The government should review and realign research and development incentives and other supportive policies, particularly in blended finance, to enable Australian business to become a world leader in innovative sustainability practices.

About ACCI

The Australian Chamber of Commerce and Industry represents hundreds of thousands of businesses in every state and territory and across all industries. Ranging from small and medium enterprises to the largest companies, our network employs millions of people.

ACCI strives to make Australia the best place in the world to do business – so that Australians have the jobs, living standards and opportunities to which they aspire.

We seek to create an environment in which businesspeople, employees and independent contractors can achieve their potential as part of a dynamic private sector. We encourage entrepreneurship and innovation to achieve prosperity, economic growth, and jobs.

We focus on issues that impact on business, including economics, trade, workplace relations, work health and safety, and employment, education, and training.

We advocate for Australian business in public debate and to policy decision-makers, including ministers, shadow ministers, other members of parliament, ministerial policy advisors, public servants, regulators and other national agencies. We represent Australian business in international forums.

We represent the broad interests of the private sector rather than individual clients or a narrow sectional interest.

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