15 December 2023

Sustainable Finance Unit
Climate and Energy Division
Treasury
Langton Cres
Parkes ACT 2600

Dear Sustainable Finance Unit

**Sustainable Finance Strategy Consultation Paper**

The Australian Financial Markets Association (**AFMA**) is pleased to respond to Treasury's Sustainable Finance Strategy Consultation Paper (**the strategy**).

AFMA is the leading financial markets industry association promoting efficiency, integrity and professionalism in Australia's financial markets, including the capital, credit, derivatives, foreign exchange, energy, and other specialist markets, including environmental products, carbon and sustainability related and linked products. Our membership base is comprised of over 125 of Australia's leading financial market participants, from Australian and international banks, leading brokers, securities companies and state government treasury corporations to fund managers, energy companies and industry service providers. AFMA members are some of the major issuers and intermediaries of sustainability products, as well as some of the key investors in sustainable activity and products.

AFMA and our members support and welcome the publication of the Government's Sustainable Finance Strategy Consultation Paper and we look forward to working with government on implementation across our sector, and economy-wide. We believe that working collaboratively with industry on the strategy's implementation and ensuring international allignment, will be vital to its success. We also assess that ensuring this strategy flows through all of government and government bodies, will aid the transition to a more sustainable economy as a whole. We also view the pressing need to address data and analytical challenges as central to the entire strategy, and likewise its success, as well as the wider sustainability ecosystem.

AFMA views this consultation paper as a first scoping exercise, with further consultation and detailed implementation proposals on each priority, to come. As such, AFMA's submission focuses on the priorities, pillars and vision of this paper at a high level during this development phase rather than granular detail, which will follow in subsequent consultation. AFMA has provided a table of key points & recommendations and made detailed comments on each priorities as follows.

Thank you for considering the points and suggestions raised in this submission. AFMA would welcome the opportunity to discuss this submission further and would be pleased to provide further information or clarity as required. Please contact myoung@afma.com.au or 02 9776 7917.

Yours sincerely

David Love

**David Love**
**General Counsel**

## Table of Key Points & Recommendations

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| **Pillar 1** | AFMA supports Pillar 1 and agree that enhancing transparency and sustainability is imperative. |
| Priority 1 | AFMA supports Priority 1 but cautions government that core elements of the framework (resourcing, assurance, and data needs) require investment, enhancement, and immediate attention to facilitate reporting. |
| Priority 2 | AFMA supports Priority 2, and that international alignment is particularly important. AFMA believes that government should establish an industry advisory body to work with government on designing the appropriate regulatory and governance architecture. |
| Priority 3 | AFMA supports Priority 3 and believes plans should be fully consulted on with the respective sectors. |
| Priority 4 | The ICMA Principles are the current Australian industry standard which have worked efficiently. AFMA recommends recognition and support of these Principles from ASIC, as it similarly provided for TCFD as the standard for reporting and disclosures. |
| **Pillar 2** | AFMA supports Pillar 2 and believes it to be the most vital Pillar, but it is AFMA's view that Pillar 2 should be Pillar 1, given that we will need to achieve Pillar 2 to be able to achieve Pillars 1 and 3. |
| Priority 5 | AFMA supports the intention of Priority 5 with further planning and consultation and agrees there is a case for regulating ESG ratings providers, in line with other similar providers, such as credit rating providers. AFMA also recommends implementing a regulatory grid. |
| Priority 6 | Whilst supportive of Priority 6, AFMA maintains that financial institutions are well aware of climate- and sustainability-related financial risks and have been planning and responding appropriately. |
| Priority 7 | AFMA strongly agrees with Priority 7 and views it as of paramount importance. AFMA has identified specific data and analytical challenges requiring immediate attention. |
| Priority 8 | AFMA supports Priority 8 but urges government to ensure any governance and decision-making requirements are not overly prescriptive. |
| **Pillar 3** | AFMA supports Pillar 3 and agrees that strong leadership from government and extensive engagement will be vital to the strategy's success. |
| Priority 9 | AFMA supports Priority 9 and welcomed the recently published framework but believes that greater alignment with the ICMA GBP would be beneficial. AFMA also believes that once developed, the taxonomy should seek to align with the program. |
| Priority 10 | AFMA supports Priority 10 and would encourage the CEFC to establish a formalised working relationship with the private sector to collaborate on these mutual efforts. Whilst co-benefits are supported, AFMA believes that investment in the transition should remain CEFC's focus. |
| Priority 11 | Priority 11 is strongly supported and should be a central theme throughout the strategy. The focus should remain on maximising transitional activity that is Paris Agreement aligned. |
| Priority 12 | AFMA supports Priority 12, and has provided some first step recommendations below. |

## Pillar 1: Improve transparency on climate and sustainability

### Priority 1: Establish a framework for sustainability-related financial disclosures

AFMA has long supported the Taskforce on Climate-related Financial Disclosures (TCFD) recommendations and International Financial Reporting Standards (IFRS) S2 Standards. We therefore welcome the Government's commitment to legislate climate-related financial disclosures and agree with the need to establish an appropriate framework to enable this. In line with these globally aligned initiatives, we would also request government to adopt IFRS S1 as soon as practically possible.

However, as AFMA highlighted in its submission responses to both rounds of consultation on the proposed disclosure requirements, we believe that Scope 3 reporting by financial institutions should remain voluntary during the transition period, which we have recommended to be five years to allow companies time to adjust, be appropriately resourced and for the outstanding data and information systems issues, which the disclosures rely on, to be worked through.

As well understood by government, resourcing, assurance, and data require investment, enhancement, and immediate attention to facilitate the forthcoming disclosure requirements. These tools are central pillars to the framework but remain in an underdeveloped state, the capabilities and resources are not yet consistent with the requirements. Appropriate evidencing and data democracy is crucial to enabling the disclosures, particularly as it relates to human rights. Therefore, whilst supportive of the disclosure requirements, AFMA would caution the Government to allow time to appropriately build and equip the framework. AFMA has outlined specific data and analytical challenges requiring immediate attention in Priority 7, but raises the concern here, given that data is what the disclosure will rely upon. AFMA believes that the data and analytical challenges require greater consideration and allowance in the forthcoming exposure draft legislation. Similarly, government support for the development of building out assurance providers and centralised data systems will be critical. AFMA believes that the Council of Financial Regulators should play a key role in working collaboratively with industry in its assessment of the options being considered to address the current data challenges.

AFMA notes the intent to extend the disclosure requirements beyond climate to broader sustainability areas, such as nature, over time. AFMA believes that an appropriate voluntary compliance period should be provided ahead of any legislative requirement, to enable firms to adequately prepare whilst also managing the new incoming TCFD requirements. AFMA has expanded on this issue in response to Priority 3, but we caution government over-loading a system still in an infancy state that will be working through climate policies and achieving economies of scale by prematurely directing those resources away to broader sustainability and nature goals. We also therefore risk failing to achieve our primary objective — climate change response.

AFMA does however agree that to support voluntary Taskforce on Nature-related Financial Disclosures (TNFD), the Australian Securities and Investments Commission (ASIC), should update their guidance in relation to voluntary nature-disclosures, as it did for climate disclosures in 2019. AFMA would encourage ASIC to work directly with industry on this. Similarly, AFMA would also encourage ASIC to work collaboratively with industry on the forthcoming regulation and regulatory guidance on climate-related financial disclosures to support transparent, manageable, and standardised practices.

AFMA would also take the opportunity to highlight to government that the 'Do No Significant Harm' provision will be technically and practically challenging to apply. AFMA would urge government to ensure that there is no room for miss-application or discrepancies in understanding of its meaning and subsequent requirements. To mitigate this, we believe it would be most appropriate to legislate the 'Do No Significant Provision' contained within the primary legislation, with accompanying legislative definitions and enforcement principles — rather than delegated legislation. The provision will require substantial consultation with industry to ensure that it provides the intended protections with integrity but does not become overly prescriptive to where it limits investment into transitional activities or emerging technologies.

### Priority 2: Develop a Sustainable Finance Taxonomy

AFMA has also long supported and advocated for the development of a sustainable finance taxonomy. We believe that a taxonomy will be central to supporting investment and providing investor confidence. AFMA supports the ongoing work of the Australian Sustainable Finance Institute (ASFI) in developing an Australian taxonomy.

AFMA's overarching recommendation is to ensure, to the extent possible, international alignment on the taxonomy to ease discrepancy, safeguard international investment, and reduce compliance burden. To achieve this, the taxonomy should be subject to thorough consultation with industry, once available. In light of some of the challenges currently arising in the EU with the operation of their taxonomy, AFMA would encourage government to seek to study the reasons for the problems and avoid them with the assistance of industry-wide consultation.

With regard to taxonomy expansion beyond its initial climate focus, AFMA believes that this should be considered at a later stage, once industry, regulators and government have the ability to access the successes and pitfalls of the taxonomy. Appropriate time to implement and assess the taxonomy should be provided ahead of any plans for expansion. Doing so will also enable government the opportunity to expand based on emerging areas of urgency rather than a second lengthy development.

AFMA notes that the consultation paper also requests feedback on what are appropriate long-term governance arrangements to ensure that the taxonomy is effectively embedded in Australia's financial and regulatory architecture. Ensuring appropriate regulatory and governance architecture will be key to the taxonomy's success. It is AFMA's view that it would be most appropriate for government to establish an industry advisory group to work with government on designing the necessary architecture. We believe that captured entities, are the most appropriate to work with government on its regulatory development.

### Priority 3: Support credible net zero transition planning

As recently identified by the Climate Change Authority, markets are an enabler of a prosperous, resilient net zero Australia. AFMA supports credible net zero transition planning, not only to support our net zero transition but because clarity and forward planning sends positive market signals, helps boost investment and enables effected entities to appropriately plan for the future. To do this will require government investment in the management and dissemination of environmental data as well as collaborative policy planning with effected entities.

AFMA would therefore urge government to ensure that effected entities, such as energy firms, are involved in all transition plans. Managing the transition is an important challenge currently facing both industry and government, including consideration of transition fuels such as gas. AFMA supports the collaborative and industry inclusive approach taken by the UK in establishing the Transition Plan Taskforce and would request government to consider establishing a joint industry and government body to carry this work forward. To this end, AFMA welcomes the inclusion of the sectoral decarbonisation plans. We ask government to work with each sector closely whilst developing these plans.

As AFMA previously stated to the Climate Change Authority during their consultation on setting, tracking and achieving Australia's emissions reduction targets in our submission, we believe it vital to provide the market and effected entities with:

1. An emissions policy based on long-term targets
2. Coherent and achievable goals and objectives for the energy transition
3. Legislate disclosure frameworks and standards

For sake of consistency, as part of government's work on developing transition plans, AFMA would also ask government to review and ensure that the National Greenhouse and Energy Reporting (NGER) framework is appropriately aligned with the forthcoming corporate disclosures.

AFMA notes the final question posed as to enhancing the target setting and transition planning for nature and other sustainability issues. Given that climate remains the priority, AFMA would propose government prioritise the climate policies, with broader sustainability and nature goals to follow on. As expressed throughout this submission, upscaling, data, and adequate resourcing is a sizeable hurdle for both government and industry to overcome. We therefore caution against over-loading a system still in an infancy state, that will be working through new climate policies and achieving economies of scale whilst also directing those resources away to broader sustainability and nature goals.

## Priority 4: Develop a labelling system for investment products marketed as sustainable

AFMA is supportive of the use of a labelling system for investment products marketed as sustainable. AFMA believes such systems boosts confidence, transparency, and cohesion in methodology for all parties and helps to mitigate risks of greenwashing. As expressed throughout this consultation, AFMA views international alignment and cohesion as critical to accelerating sustainable finance and sustainable markets in Australia. The International Capital Market Association (ICMA) currently maintain and administer the industry led and developed de facto global set of ESG-based issuance standards, the ICMA Principles. The ICMA Principles are comprised of the Green Bond Principles (GBP), Social Bond Principles (SBP), Sustainability Bond Guidelines (SBG) and the Sustainability-Linked Bond Principles (SLBP). The GBP and SBP provide thorough guidelines and standards for issuance covering, definitions, use of proceeds, process for project evaluation and selection, management of proceeds, reporting, frameworks for transparency and external reviews. The SLBP provides clear definitions, selection of Key Performance Indicators, calibration of Sustainability Performance Targets, bond characteristics, reporting and verification. While the SBG has been developed to provide transparency and standards for the market that has developed for bonds aligned to both the GBP and the SPB.

The ICMA Principles have long been voluntarily adopted by the in the Australian Debt Capital Market.. These principles  have worked efficiently and boosted transparency in the Australian market, when applied. Not only has Australia's adoption of these principles enhanced transparency and clarity in the domestic economy but has also smoothed international investment as a result of global alignment. AFMA believes that the whole of market adoption of the Principles in the Australian market can be achieved by recognition of these global leading Principles.. In its Information Sheet 271 'How to avoid greenwashing when offering or promoting sustainability-related products', ASIC states: *"To help improve the quality of disclosure, ASIC recognises the recommendations by the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) and encourages voluntary disclosure that is in accordance with the TCFD framework. If you report climate-related information under the TCFD framework, we expect that you will be well placed to transition to any future standard."*

AFMA believes that a similar statement of recognition and support from ASIC for the ICMA Principles would achieve the aims of this Priority. AFMA would encourage ASIC to work with industry on their support in formally recognising these global principles in the Australian market.

## Pillar 2: Financial system capabilities

AFMA supports Pillar 2 and its aims, but we assess that, as previously highlighted above, without significant upscaling of financial system capabilities, we risk not achieving many of the aims under Pillar 1. We therefore believe it would be more appropriate to make financial system capabilities Pillar 1 rather than Pillar 2.

### Priority 5: Enhancing market supervision and enforcement

AFMA supports the aim of Priority 5 in that the transparency-related measures across the strategy will aid the enhancement of market supervision and enforcement. AFMA believes it is important for government to clearly identify and outline their expectations of ASIC and any other body external to government, as part of this strategy. The role of regulators across the strategy's aims should be clearly articulated to regulated entities, to enable them to work constructively with regulators in these enhancement efforts. It is also our view that regulatory direction should be consistent with the legislation, having been thoroughly consulted on with industry and other stakeholders.

AFMA is however concerned that the architecture of Australia's existing corporations and financial services laws could hinder efforts to combat greenwashing and slow down institutional investor activity. AFMA maintains that much of Australia's governing financial services laws, particularly elements of Chapter 7 of the Corporations Act 2001, do not appropriately differentiate between institutional investors and retail investors. Given the infancy, variance, nuances, and complexities associated with the variety of ESG related products and funds currently available on the market, we believe ensuring legal and regulatory separation between institutional and retail investors—is of high importance. AFMA understands that ASIC's recent enforcement action on greenwashing has been against firms for misleading retail investors, which we believe highlights this issue. AFMA believes that different requirements, particularly as it relates to how a products/ fund is marketed and accompanying information, may need to be different for institutional versus retail investors.

With regard to the question posed on regulating ESG ratings providers, AFMA understands that other jurisdictions are currently considering proposals to regulate ESG ratings providers. Given the cross-border nature of ratings providers, AFMA welcomes the inclusion of this consideration in the strategy. AFMA agrees that regulating ESG ratings providers in line with other similar services, such as credit rating providers, would aid transparency, particularly as it relates to varying methodologies. AFMA would encourage government to explore common cross-border regulatory approaches.

Whilst AFMA reserves detailed comment and recommendation until proposal specific consultation, we do think it's important for government to thoroughly consider that an issuer requires clear lines of site, understand the process, and have the ability to comment on data sources or provide data. Therefore, there is a clear market need to ensure that methodologies and actual data applications, are more transparent. A move toward standardisation, as appears a key aim throughout the consultation paper and a limited number of credible providers, would be an appropriate direction to consider.

With much forthcoming regulation expected in 2024 and beyond we believe that implementing a regulatory grid, which sets out the pipeline and timing of incoming regulation, would also be beneficial for government, regulators, and the regulatory community to prepare for incoming regulation. The UK Government has already implemented a Financial Services Regulatory Initiatives Gird which has provided enhanced regulatory efficiency and resource allocation.

## Priority 6: Identifying and responding to potential systemic financial risks

AFMA supports the aim of Priority 6 but maintains that industry is well aware of climate- and sustainability-related financial risks and both recognise and respond to the fact that climate change is a distinct financial risk consideration. For many, this understanding and action is embedded across risk modelling, company ethics, investment strategies, renumeration, and KPI; with many firms also continuing to invest, upscale and upskill their climate vulnerabilities and mitigation assessments and modelling. Should the Government choose to proceed, we believe establishing a specialist sustainability standards board may be the most appropriate body to be responsible for this priority.

AFMA believes that any climate assessment efforts should be coordinated across government and agencies, particularly around aims, methodologies and definitions. To the extent possible, noting Australia's unique climate and ecosystem, we view that assessments and the underlying methodologies should be internationally aligned. We believe it would also aid transparency and standardisation to produce Australian specific climate scenarios for industry for use in their scenario analysis. This could also be beneficial in helping industry meet disclosure requirements.

More broadly, it is AFMA's view that we all have a part to play in addressing climate risks. Therefore, AFMA would recommend expanding the Australian Prudential Regulation Authority's (APRA) Climate Vulnerability Assessments to other financial entities whose impact is important, such as superannuation funds and appropriate small to medium firms.

AFMA also would encourage government authorities to work more closely with state level governments to ensure that the scope of work being undertaken on a state level is supporting best practice and aligned with the national ambition. As government will be aware, many state governments are developing their own climate change adaptation and resilience frameworks which involve close work with scientific institutes and emerging technologies. It is our view that a cohesive approach will aid the goal of better understanding risks and vulnerability that provides evidence base for climate adaption initiatives. A stronger climate change focus, beyond energy, from the Energy and Climate Change Ministerial Council, could also be of benefit.

## Priority 7: Addressing data and analytical challenges

As highlighted above under Priority 1, AFMA views the need to address data and analytical challenges as paramount. Specifically, AFMA has identified the following challenges as key and requiring immediate attention which should be earmarked for prioritisation, as part of this strategy.

- Consolidated, machine readable and democratised data accessible to all;
- Support and resources to enable later in-scope SMEs to provide the data that reporting entities will rely upon;
- Consistency in baseline assumptions and scenario analysis, including standard language and definitions;
- Defining and provide commonality for minimum reporting requirements for different scenarios;
- Upscale assurance providers to service reporting entities at the scale required;
- Facilitate streamlined information sharing from NGER entities to reporting entities;
- NGER requirements should be expanded to other sectors and relevant SMEs whose data reporting entities will rely upon.

### Priority 8: Ensuring fit for purpose regulatory frameworks

AFMA supports Priority 8 and agrees that mainstreaming sustainability considerations and decision-making process can help boost investor confidence and transparency. However, AFMA would ask the Government to ensure that any such requirements are guiding and not overly prescriptive.

As highlighted above, for many firms, this is already deeply embedded across the business and is often unique. Whilst commonality will boost confidence in achieving shared objectives, any requirements should not limit a firms' unique approaches, rather it should be complementary. AFMA would also caution that overly prescriptive requirements could have negative consequences by being burdensome and restrict a firms' appetite to explore emerging risks, specific investor demands and company cultural objectives that may not be explicitly covered in APRA's guidance; or do not meet the prescribed balance required. AFMA believes that any amendments to regulatory frameworks should be made with the goal to maximise climate consideration and response, inclusive of all efforts, rather than a prescriptive list of actions or investment and issuance products. Any forthcoming requirements should be consulted on thoroughly with industry to support this.

## Pillar 3: Australian Government leadership and engagement

### Priority 9: Issuing Australian sovereign green bonds

AFMA warmly welcomed the 2022/23 Federal Budget announcement of Australia's Sovereign Green Bond Program, to be issued by the Australian Office of Financial Management (AOFM) and in consultation with institutional investors.

AFMA understands that Treasury will take responsibility for project evaluation, selection, and management. With issuance scheduled to begin in mid-2024, AFMA believes that the framework should be aligned with current market practices and existing frameworks, in both the domestic and international markets. AFMA would therefore encourage greater alignment of  the ICMA GBP, given its status as both the Australian and de facto international standard for Green Bond issuance. The ICMA Principles have proven effective in the Australian Debt Capital Market in providing the necessary transparency and enhanced methodological standardisation whilst not being overly prescriptive that it limits inclusion.

Furthermore, with issuance due to commence sometime ahead of the taxonomy completion, AFMA believes that the taxonomy should be aligned and follow suit of the AOFM and Treasury's framework and guidelines. Noting that some state governments have already introduced their own green or social bond programs, AFMA would also encourage government to work with the states to ensure alignment across the domestic market. For the market to function well, transparency, depth of market and liquidity is what is required, and the frameworks and guidelines put into place should facilitate this.

### Priority 10: Catalysing sustainable finance flows and markets

To further accelerate the work of the Clean Energy Finance Corporation (CEFC) efforts, AFMA would encourage the CEFC to establish a formalised working relationship with the private sector to collaborate on catalysing sustainable finance flows and developing markets and products. We think such a working group would aid progress in achieving these mutual goals. Particularly with the CEFC expected to help develop standards and frameworks to boost growth and integrity of sustainable finance products and markets.

We know that the energy transition will require sizeable investment, particularly from the private sector, but also the public sector. With a focus on climate and as echoed throughout AFMA's submission response, AFMA believes that the focus of the CEFC in relation to this strategy should remain on clean and renewable energy technologies and assets to aid decarbonisation efforts, further the energy transition and meet the net zero emissions targets. Whilst investments with climate co-benefits such as nature and biodiversity are an added bonus, AFMA affirms its position that climate should remain the initial priority.

### Priority 11: Promoting international alignment

As echoed throughout our submission, AFMA fully supports this priority and would urge government to pursue international alignment across all sustainable finance policy. International alignment is important for all parties involved, issuers, intermediaries, government, regulators, and investors. We believe that promoting international alignment across all sustainability policy is of paramount importance and should be central to the strategy. Climate is a global solution requiring global response.

When considering international alignment in sustainable finance, AFMA believes that aligning with leading jurisdictions, would be advantageous. However, in some instances, 'Australianisation' may be required. AFMA would therefore encourage strong consultation with industry on issues which may require localisation, ahead of any formalised agreement.

We note that this priority, like much of the consultation paper, has a particular focus on transition. AFMA believes its important to focus on ensuring that transition in relation to climate change mitigation in Australian financial markets architecture and frameworks can physically support maximising transition activity. AFMA sees risk in being both overly ambitious and setting qualification timeframes too early. Once frameworks are established, they could quickly become unusable and not support the intention for which they are established. A clear example of this is sunset dates for 'transition' activities by sector aligning to a 1.5-degree pathway. With many sunset dates approaching in 2025, we could end up in a situation where we have sunsetting dates without a finalised taxonomy. Even once we have a taxonomy and its regulatory architecture in place, we note that other jurisdictions such as the EU, have still faced challenges. Therefore, practicality of application and maximisation of application should be a key criterion, such as being Paris Agreement aligned, coupled with broader international alignment.

AFMA would also note that a delay to alignment on various activity transition dates does not represent a lack of international alignment in the medium term, instead it would likely mean more chance of achieving our goals in the longer term if we can maximise financial market support.

### Priority 12: Position Australia as a global sustainability leader

AFMA shares the Government's ambition to position Australia as a global sustainable leader. AFMA would like to see Australia as a leader in sustainable markets, the go to location in the region for ESG linked and related products. With many other regions likewise aiming to be a leader in this space, AFMA believes that Australia should position itself accordingly. To grow local markets, Australia will need to ensure international alignment, efficient regulation and a competitive operating environment. We can achieve these through collaborative engagement with industry, government, and regulators.

To begin this effort, AFMA would first specifically recommend:

1. Creating a class exemption sustainability related collaboration, in line with developments in the UK, EU, and New Zealand.
2. To boost the much-needed capability, at the next federal budget, government should invest in training across government in financial markets, investment, and the role of private capital as well as the power of sustainable finance more broadly.
3. As industry also works to capacity build, support for industry led initiatives, such as the ICMA Principles and reputable educational training, would aid the implementation of the priorities within the strategy.