Sustainable Finance Strategy

ABA Submission to the Australian Treasury Consultation

1 December 2023

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Australian Banking Association

Key Recommendations

1. **Prioritise the uplift of Australian climate data (Priority 7):**
    a. Continue to develop publicly available climate data in the following categories:
        i. Data to support downscaled climate scenarios, including both transition and physical risk, in line with the Australian Prudential Regulation Authority's (**APRA**) comments on the release of the results of the climate vulnerability assessment (**CVA**).
        ii. Damage functions, to provide a less resource intensive approach for calculating economic loss in scenario analysis.
        iii. Emissions factors and data relevant to support calculation of Scope 3 emissions, with priority on residential housing, agriculture and commercial real estate.
        iv. Natural perils information, including flood, bushfire, coastal inundation and erosion, hail, cyclone frequency and building resilience characteristics.
    b. Create and publish a holistic view of the data and information that should be generated through initiatives underway at both the State and Commonwealth level.
    c. Create and publish downscaled climate scenarios.
    d. Stand up a forum for ongoing uplift and development of Australian climate data.
2. **Undertake further consultation on the issues raised in the Sustainable Finance Strategy:**
    a. Noting the broad range of emerging and complex issues canvassed in the consultation, and the timeframe for response, we strongly recommend further consultation occur on any proposals before the Australian Government moves to formalise policy outcomes to allow additional time for industry consideration.
3. **Support other sustainability reporting on an opt-in or voluntary basis (Priority 1):**
    a. Allow the market time to develop maturity with voluntary or opt-in Taskforce for Nature-based Financial Disclosures (**TNFD**) disclosures before considering further expansion of mandatory sustainability reporting.
    b. In the interim, Government should continue to build out Australia's nature and biodiversity data, including long and short-term scenario narratives, to support voluntary or opt-in disclosures.

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About the ABA

The Australian Banking Association advocates for a strong, competitive and innovative banking industry that delivers excellent and equitable outcomes for customers. We promote and encourage policies that improve banking services for all Australians, through advocacy, research, policy expertise and thought leadership.

Overview

The Australian Banking Association (**ABA**) welcomes the opportunity to provide a submission to the Treasury consultation on the *Sustainable Finance Strategy*. Demonstrating the banking industry's commitment, the ABA has progressed a range of industry initiatives this year, including:

- Develop guidance documents for financed emissions calculations and recommendations for improved datasets at a sector level. In September 2023, the ABA published the first iteration of the *Financed Emissions Guidance for Residential Mortgages*,[1] with work underway on similar guidance for commercial real estate and agriculture.
- Facilitated a joint session on capability uplift with Deloitte and Chartered Accountants Australia and New Zealand (**CAANZ**) aimed at preparing the banking sector for climate disclosures.
- Developing a position paper on *Climate Risks and Capital*,[2] and progressed development of an industry position on climate scenario analysis.
- Developed industry thinking on datasets needed to underpin climate disclosures, which we have drawn upon in this submission.

The ABA notes that the timeframe for response to this consultation has not allowed the industry to provide detailed comments on all areas raised. Where possible, we have made some high-level comments. However, we strongly emphasise these areas will require further consultation if the Australian Government chooses to proceed.

The ABA response to the *Sustainable Finance Strategy* draws upon and reiterates key points from our earlier submissions, including:

- Department of Climate Change, Energy, the Environment and Water (**DCCEEW**), *Nature Repair Market Bill – Exposure Draft*[3]
- International Sustainability Standards Board (**ISSB**), *Consultation on Agenda Priorities*[4]
- Climate Change Authority (**CCA**), *Setting, Tracking and Achieving Australia's Emissions Reduction Targets*[5]
- Treasury, *Climate-related Financial Disclosures* (first and second-round consultations)[6]
- Treasury, *Housing Legislation Package*[7]
- Senate Standing Committee on Economics, *National Reconstruction Fund Bill 2022*[8]

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[1] ABA (September 2023) *Financed Emissions Estimation Guidance for Residential Mortgages* (link)
[2] ABA (March 2023) *Climate Risk and Capital* (link)
[3] ABA (March 2023) *Submission – Nature Market Repair Bill – Exposure Draft* (link)
[4] ABA (August 2023) *Submission – ISSB Consultation on Agenda Priorities* (link)
[5] ABA (July 2023) *Submission – Setting, Tracking and Achieving Australia's Emissions Reduction Targets* (link)
[6] ABA (February 2023) *Submission – Climate-related Financial Disclosures* (link), ABA (July 2023) *Submission – Climate-related Financial Disclosures, Second-Round Consultation* (link)
[7] ABA (January 2023) *Submission – Housing Legislation Package* (link)
[8] ABA (February 2023) *Submission – National Reconstruction Fund Bill 2022* (link)

Australian Banking Association

Pillar 1: Improve transparency on climate and sustainability

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

What are the opportunities for Government, regulators and industry to support companies to develop the required skills, resources and capabilities to make climate disclosures under the proposed new obligations?

In our submission to the Treasury consultation, *Climate-related financial disclosures: Second-round consultation*, the ABA nominated several factors that will determine whether reporting entities are able to meet the proposed timeframe, including:

> *Assurers will need to rapidly meet the requirements to provide reasonable assurance for all climate disclosures (carbon accounting, scenario analysis, net zero transition planning, etc.) and the assurance industry will need to be sufficiently mature to provide these services consistently and at reasonable costs.*
>
> *Supporting data, scenarios and methodologies will need to come online rapidly to support Australian businesses in undertaking the analysis required for the mandatory disclosures, and to minimise additional cost.*

Absent a national strategy, capacity constraints will emerge that impact the ability of Australian businesses to make those disclosures with confidence and credibility and supported by assurance. The phased implementation approach proposed by the Treasury will be useful in allowing smaller reporting entities to develop skills and capabilities ahead of mandatory implementation dates. This could be complemented by focus on matters such as:

- Data, which we discuss in more detail under **Priority 7**.
- Labour and/or skillset shortages, which are relevant in preparing organisations assurance/audit providers and regulators.
- Recognition from regulators of the challenges in making these disclosures, given data availability, and the adoption of an educative rather than punitive posture in the first instance.
- Enabling greater literacy on climate and sustainability risks and opportunities across the business community, potentially through centralised education and/or toolkits.
- Additional consideration of how to build capacity across industry, not only demonstrating the interconnectedness of the impact areas but also the reliance on the full value chain to deliver the expected impact.

How should the Government, regulators and industry prepare for global developments in sustainability-related financial disclosure frameworks and standards, including the TNFD?

The key priority of the Australian Government should be the successful domestic implementation of IFRS S1 and S2. This is consistent with the ISSB's strategic direction of "climate first, not climate only". Beyond that, we view that the appropriate stance for Government is two-fold:

1. Allow the market time to develop maturity with voluntary or opt-in TNFD disclosures before considering further expansion of mandatory sustainability reporting.
2. In the interim, Government should continue to build out Australia's nature and biodiversity data, including long and short-term scenario narratives, to support voluntary or opt-in disclosures.

While our submission does not comment in detail, we also note that social reporting and disclosure – for example as contained in the *Modern Slavery Act* – will need to be considered in tandem. There are specific issues for banks with, for example, respect to tipping off provisions. The ISSB is considering social reporting as a future priority.

With respect to the first of our recommendations, ***allow market maturity for nature-related reporting to develop***, we reiterate our earlier position outlined in our submission to the ISSB:

> *Biodiversity is a rapidly emerging new area of reporting and a growing focus for both investors and government. There is also interconnectivity with climate reporting and existing frameworks (such as the TNFD and GRI) that could be drawn upon.*
>
> *However, biodiversity reporting remains at a nascent state, and much more experimentation and development is needed before it becomes suitable for formal incorporation into reporting standards.*

We note the lead-time for climate-related financial disclosures. The Taskforce for Climate-related Financial Disclosures (**TCFD**) recommendations were released in 2017, with the International Sustainability Standards Board (**ISSB**) creating the reporting standards IFRS S1 and S2 earlier this year. Domestic implementation is currently under consultation by the Australian Accounting Standards Board (**AASB**), and the Australian Government has proposed that mandatory ISSB-aligned climate disclosures commence from FY2024-25, with final cohort proposed to be subject to mandatory reporting by 2030-31. Even given this lead-time, challenges remain.

By contrast, the TNFD recommendations were published in September 2023 and some companies will begin reporting on a voluntary basis from next financial year. It is likely that biodiversity standards will rapidly evolve as reporting begins. Given the length of time taken for climate-related financial reporting to develop, we recommend the Australian Government allow TNFD reporting to evolve, and that reporting remain on a voluntary basis as market maturity develops.

In the interim, the Australian Government would play a constructive role by continuing to ***build out Australia's nature and biodiversity data***. Our submission to the ISSB stated:

> *Much more work is needed on the supporting infrastructure for biodiversity reporting. This includes more detailed metrics, methodologies and measurement tools downscaled to appropriate national contexts. This supporting infrastructure will be required for preparer organisations to make meaningful disclosures that are useful for investors.*

The need for uplift in Australia's environmental data and information was a key theme of the *Independent Review of the Environment Protection and Biodiversity Conservation Act 1999*, which found that "there is no clear, authoritative source of environmental data and information".

The Australian Government may also wish to consider developing a centralised repository of learning, education, and resources to support stakeholders – potentially within a public-private partnership model. This could include matters such as: examples of best practice guidance and reporting, nationally consistent definitions and metrics and potentially agreed status of regional natural capital and ecosystems flows, and main risks identified in those regions. Climate and nature outcomes are deeply interconnected, both in terms of risk and opportunities. Additional work could be undertaken to understand how and where these dependencies exist.

Priority 2: Develop a sustainable finance taxonomy

What are the most important policy priorities and use cases for an Australian sustainable finance taxonomy? What are the key insights from international experience to date?

What are priorities for expanding taxonomy coverage after the initial focus on climate mitigation objectives in key sectors?

What are appropriate long-term governance arrangements to ensure that the taxonomy is effectively embedded in Australia's financial and regulatory architecture?

The ABA supports the Australian Government playing a leading role in the creation of a sustainable finance taxonomy.[9] Effective government participation and leadership can have positive benefits of providing market clarity and fostering investor confidence.[10] Compared to a purely private sector approach, governments are better positioned to ensure uniformity of approach across different sectors of the economy and to ensure that taxonomies are aligned with broader policy goals.

Additional areas for consideration in taxonomy coverage could include: physical resilience in the built environment, evolving language and protected terms,[11] and/or costs associated with adherence and how implementation may impact institutions of different sizes.

Priority 3: Support credible net zero transition planning

What are key gaps in Australian capability and practice, including relative to 'gold standard' approaches to transition planning developed through the TPT and other frameworks?

The ABA and its members will continue to consider this policy priority and will make more detailed comments during formal consultations.

As an overarching comment, a clear and effective transition planning framework will support ongoing funding during the transition. Globally, we are seeing funding availability in some jurisdictions impacted by lack of clarity, and many Australian industries will need funding support to align to net zero. While measures of transition plan effectiveness may be sector-specific, they should use comparable metrics.

The ABA provides the following high-level observations to inform the Government's work:

- **Australia's position in the world.** In other areas of sustainable finance policy, other jurisdictions, most notably the UK and EU, have provided experience and lessons, enabling Australia to take the position of fast follower. This is not necessarily the case for transition planning, which is is relatively new in most jurisdictions.

- **Global best practice.** There are several transition planning frameworks developed by organisations which all differ slightly.[12] While international approaches have set the gold standard, that does not necessarily reflect the stage where most companies (particularly smaller ones) currently are at. Further, while transition frameworks are welcome additions to the disclosure framework, they do not themselves address questions around alignment. Additional frameworks or reference points, such as sectoral pathways, may be needed to address this gap.

- **Sectoral Approach.** While other jurisdictions have approached transition from a whole-of-economy perspective, Australia will likely need to take a sector-by-sector approach. In considering transition planning, it may be worthwhile for the Australian Government to identify and sequence different sectors based on their material contribution.

- **Capability and capacity development.** There is opportunity to consider from the outset how to develop the capabilities, skillsets, tools, and capacities that will be required for transition planning that is appropriate for organisations of various sizes and loan book compositions.

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[9] ABA (December 2022) *Media Release – ABA welcomes decisive action on climate change* (link)
[10] OECD (October 2020) *Developing Sustainable Finance Definitions and Taxonomies – A Brief for Policy Makers* (link)
[11] For example, the emerging terminology "blue" (as opposed to "green") is intended to signify social rather than environmental focus. As other terminology may emerge in future, guidance may be useful to prevent overly complex terminologies developing.
[12] Including GFANZ, the UK Transition Plan Taskforce, the Transition Pathway Initiative, etc

To what extent will ISSB-aligned corporate disclosure requirements improve the transparency and credibility of corporate transition planning? What additional transition disclosure requirements or guidance would be most useful in the medium-term?

Are there related priorities and opportunities for supporting enhanced target setting and transition planning for nature and other sustainability issues?

While ISSB-aligned corporate disclosure requirements will improve the transparency and consistency of transition planning, they are not proposed to fully apply to all Groups until FY 2030-31. An important element will be the speed of implementation for non-listed entities.

Australia will likely be an early mover with transition plan expectations requiring investment and facilitating the development of capability. Further engagement is recommended across a broad range of stakeholders to support the developing this capability with a role for Government in facilitating the governance if a taskforce type initiative is established.

Finally, consideration will need to be given for large organisations that are subject to disclosure obligations but whose customer base is not. There is a need to consider how such entities would meet guidance expectations if the guidance were written principally to account for financers of higher-emission entities.

Priority 4: Develop a labelling system for investment products

What should be the key considerations for the design of a sustainable investment product labelling regime?

How can an Australian model build off existing domestic approaches and reflect key developments in other markets?

The ABA and its members will consider and make more detailed comments on this policy priority during formal consultations.

This priority appears to be targeted at sustainable investment products and labelling for funds, and it is unclear whether it would extend to labelled sustainable financial instruments such as bonds, deposits and loans. The labelling of certain financial instruments (e.g. green bonds) is important as they are key investment products for sustainable funds. Consistent application of the taxonomy criteria across sustainable finance instruments can promote product integrity and manage greenwashing.

Where possible, international labelling approaches should be leveraged rather than duplicated – noting the myriad of labelling schemes already published or under consultation in jurisdictions as diverse as the US, UK, EU, ASEAN, and so on. As capital is global and mobile, harmonisation will aid liquidity and mobilisation.

Pillar 2: Financial System Capabilities

Priority 5: Enhancing market supervision and enforcement

Are Australia's existing corporations and financial services laws sufficiently flexible to address greenwashing? What are the priorities for addressing greenwashing?

We will consider and make more detailed comments on this policy priority should the Government proceed to formal consultation.

While existing laws are sufficiently flexible, there is a need for additional clarity and guidance, particularly respect to compliance and enforcement. For example:

- Disclosures in this space are frequently statements about the future, and there are known limitations that disclosing entities face in making forward-looking statements about ESG (this includes science, data, methodologies and other). There is insufficient guidance as regards what constitutes "reasonable grounds" for such forward-looking statements.
- There are inconsistencies in existing regulatory guidance. As climate disclosures and statements can fall into the remit of more than one regulator, this can create challenges for disclosing entities. One example of where ASIC and ACCC guidance appears to differ is regarding "aspirational statements". ASIC guidance is permissive of aspirational statements. It encourages companies to make clear where statements are aspirational. Conversely, ACCC guidance discourages companies from making aspirational statements. There is need for greater guidance on expectations and approach to compliance and enforcement.

Is there a case for regulating ESG ratings as financial services?

ESG ratings and products play an instrumental role in the sustainable financial market.[13] ESG ratings can provide a valuable service as a starting point for data aggregation, benchmarking performance within sectors, assisting investors with their research and decision-making and supporting issuers in understanding and improving their own performance. However, ESG ratings providers often provide divergent ratings of the same companies – with confusion as the basis for the divergence is often not apparent. Given the influence of these ratings, it is important that their methodologies, including reliance on external data, are transparent and credible and that companies are provided with the opportunity for meaningful engagement on their ratings.

Priority 6: Identifying and responding to potential systemic financial risks

Are there specific areas where the Government or regulators could further contribute to market-wide understanding of systemic sustainability related risks, including climate-related financial risks?

In early 2023, the ABA developed a position paper on *Climate Risk and Capital*. The ABA and member banks are developing a detailed position paper on climate scenario analysis, aiming for finalisation in early 2024. We look forward to sharing the results with Treasury and the CFR at that time.

The paper made recommendations in several areas – for banks, supervisory regulators, and government more broadly. Key recommendations for Government and supervisors include:

> *Lead and/or assist in the development of new short-term (e.g., five year) climate scenarios and data inputs (including insurance coverage data) for the Australian economy, which will enable banks to run more targeted scenario analysis that is relevant for capital adequacy purposes.*

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[13] International Organization of Securities Commissions (IOSCO), Environmental, Social and Governance Ratings and Data Product Providers Final Report (November 2021).

Support facilitation with the CSIRO and Bureau of Meteorology for the provision of scenario data for community and government agencies, and industry planning.

Government may wish to consider establishing a forum for deeper cross-industry collaboration. Australia has an opportunity to learn from other regions where well-established groups, driven by central banks and/or prudential supervisors, bring together a variety of stakeholders, including regulators, policymakers, banks, insurers, consultants, climate scientists, superannuation funds, data vendors, climate analytics providers, and so on. Two key examples include the United Kingdom Climate Financial Risk Forum[14] and the United States Commodity Futures Trading Commission Climate-related Market Risk Subcommittee.[15]

Priority 7: Addressing data and analytical challenges

What are the priorities for ensuring that data-related initiatives already underway are tailored to meet the needs of firms and investors?

What key sustainability data gaps or uncertainties faced by financial institutions in Australia should be prioritised by the CFR?

Addressing these challenges is a key input to delivering on the Australian Government's regulatory requirements. A harmonised and coordinated approach, including greater alignment on data sources, will be critical for ensuring comparability across different sectors of the Australian economy.

This section commences by outlining the nature and scope of the problem. Specific examples are provided in three distinct areas: ***financed emissions***, ***climate scenario analysis*** and ***natural perils***. For each of these areas, we outline the role and significance of data, challenges in data availability, and opportunities for improvement. This section then finishes with a proposed path forward.

A detailed and more granular breakdown of opportunities to improve Australia's climate-related data in included in the **Appendix**.

Nature and scope of the problem

There is global recognition that accurate, public, and easily accessible data will be foundational to the net zero transition.[16] Equally, there is recognition that much remains to be done to improve the quality and accessibility of climate data, both in Australian and globally. The ABA therefore welcomes the Government's commitment that:

*…the Treasurer will request that the [Council of Financial Regulators (**CFR**)] assess key sustainability data gaps and priorities from a financial system perspective and provide key recommendations to Government on how these could be addressed [and] ask that the CFR publish its recommendations to Government by the end of 2024.*

Over time, an increasing number of businesses will need to make disclosures and undertake complex tasks such as scenario analysis.[17] By way of illustration, the Australian Sustainability Reporting Standards (**ASRS**) Exposure Draft[18] includes requirements to make disclosures on, among other matters:

- ***14 - Strategy and decision making -*** "how the entity has responded to, and plans to respond to, climate-related risks and opportunities in its strategy and decision-making, including how the entity plans to achieve any climate-related targets it has set and any targets it is required to meet by law or regulation."

[14] Bank of England (accessed November 2023) *Climate Financial Risk Forum* (link)
[15] Commodity Futures Trading Commission (accessed November 2023) *Market Risk Advisory Committee* (link)
[16] For example, see: PCAF, CDP (June 2023) *The importance of data quality in the journey toward decarbonization* (link)
[17] Treasury (July 2023) *Climate-related financial disclosures: Second consultation paper* (link) 8-9
[18] AASB (October 2023) *Exposure Draft ED SR1 Australian Sustainability Reporting Standards – Disclosure of Climate-related Financial Information* (link)

- ***22 – Climate Resilience -*** "the resilience of the entity's strategy and business model to climate-related changes, developments and uncertainties, taking into consideration the entity's identified climate-related risks and opportunities" including "climate-related scenario analysis to assess its climate resilience using an approach that is commensurate with the entity's circumstances."
- ***29—32 - Climate-related metrics*** - including "absolute gross greenhouse gas emissions generated during the reporting period" for Scopes 1 through 3.

Comparability across entities will require a degree of alignment in data. Reporting entities will need ready access to high-quality data and metrics to meet each of these reporting requirements. For example:

- In calculating its Scope 3 emissions, a reporting entity will need robust data on emissions in its customers value chain. Where a reporting entity has retail or small-to-medium enterprises in its value chain, that data is unlikely to be directly available from customers or could be resource-intensive for smaller entities to gather. We expand on this challenge under the sub-section ***Area One: Scope 3 Financed Emissions***.
- In undertaking climate scenario analysis, a reporting entity will need robust data on the likely impacts of transition risk (such as economic impacts, policy settings, and so on) and physical risk (changes to Australia's natural environment). The resource burden on smaller entities will scale with frequency. Again, we expand on this challenge under the sections ***Area Two: Downscaled Climate Scenarios*** and ***Area Three: Natural Perils***.

Further, the above relates to only ***one*** regulatory requirement. Different sectors of the economy will have other requirements, although there is likely to be overlap. Additionally, global methodologies – including for facilitated emissions – will continue to develop. As we outline in the sections below, there are key gaps in much of the data that reporting entities will need to undertake these disclosures.

Area One: Scope 3 financed emissions

A bank's "financed emissions" represents the level of greenhouse gas (**GHG**) emissions that it finances across the economy and is a critical component of its Scope 3 emissions and the most material component of banks Scope 1, 2 and 3 emissions.[19] Measuring and reporting financed emissions is a key requirement of the global sustainability reporting standards, the International Financial Reporting Standards (**IFRS**) S1 and S2.

International standards set out methodological guidance for measuring and reporting GHG emissions associated with a range of financial activities and asset classes.[20] Further, accurately measuring financed emissions is critical for target setting activities such as those undertaken under commitments made through the Net-Zero Banking Alliance (**NZBA**) or the Science-Based Target Initiative (**SBTi**).

Data is the key input in financed emissions calculations. The comparability of calculations ultimately requires high-quality public datasets for common use by all reporting entities.

Australian bank lending activities cover the breadth of the economy. To accurately calculate their financed emissions, banks need to identify data sources across the breadth of their lending activities.[21] In practical terms, this requires assessment of economic sectors on an individual basis to locate existing datasets that could act as the basis for financed emissions calculations.

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[19] This section draws heavily on lessons learnt from the ABA's work with member banks to develop guidance documents for financed emissions. For more information on this work, see "Overview".
[20] For example, see PCAF (Accessed November 2023) *Global GHG Accounting and Reporting Standard for the Financial Industry* (link)
[21] The PCAF Guidance provides a "hierarchy" of different data types that can be used. Broad industry averages are allowable as a baseline, with the highest quality score attributed to customer-provided actual energy consumption.

This poses several challenges, which are illustrated below by case studies on ***residential mortgages*** and ***agricultural emissions***:

- Locating and identifying data sources across different economic sectors is a relatively resource intensive process.
- High quality and publicly accessible emissions data does not exist for every sector.
- Where data does exist:
  - It was often created for a non-related purpose and therefore requires interpretation before it can be used in financed emissions calculations.
  - It is at a sectoral level – meaning that financed emissions calculations rely on averages or proxies rather than actual emissions data.
- While the introduction of climate-related financial disclosures will improve data quality, gaps will remain. Many key sources of emissions will not immediately be captured (or will never be captured) by the proposed framework.
- There is a risk that different areas of the economy may align on different data sources, which would complicate comparability.

Case Study: Residential Emissions	
Significance	Making up around 62% of all banking lending in Australia, a bank's residential mortgage portfolio is one of its most significant sources of bank financed emissions.[22]
How is it calculated	The ABA ***Financed Emissions Guidance for Residential Mortgages*** provides guidance for Australian banks in calculating and reporting emissions in the residential mortgage portfolio. A summary is below. In the absence of actual household energy consumption data, the bank will first create a "proxy" that estimates household energy use. This will be based on factors such as its physical location, household size, and so on. The bank will typically refer to the *Australian Energy Regulator Survey* (**AERS**) or the *Australian Energy Statistics* (**AES**), which provide estimates of retail energy usage aligned to state (AES) or climate region (AERS). Once the bank has created a household proxy, it can use national emissions factors to estimate an emission for that house. Banks typically use the National Greenhouse Gas and Energy Reporting Scheme (**NGERS**).
Opportunities	Shorter-term: • Additional granularity in surveys of residential energy usage would allow for more accurate and precise calculations. This could include, for example, the AES providing breakdowns below state-level or the AER undertaking survey on a more regular basis. • Commitment to continued and regularised survey data on household energy at the level of climate region or below.[23]

[22] As at October 2023, Australian banks had written $2.14 trillion in loans to residential mortgages, including $1.45 trillion to owner occupiers and around $691 billion to investors.
[23] The ABA notes that the Australian Energy Regulator has indicated that it may not proceed with surveys, which would mean the discontinuation of an important source of data supporting financed emissions calculations.

	• Continued expansion of the National Household Energy Rating Scheme (**NatHERS**) to support more accurate and granular proxies. • Embodied emissions. Longer-term: • While the actual energy usage of a household is known by both the occupant and their energy company, this information is unavailable to the bank. Further exploration of best practice use of customer-provided energy usage data. • Continued consideration of how existing platforms, such as the open energy implementation of the consumer data right, could be leveraged – including improved adoption rates and data available through the system.

Case Study: Agricultural Emissions	
Significance	Agribusiness accounts for around $117 billion of bank lending. The agricultural sector accounts for around 13% of Australia's GHG emissions, of which around 42% comes from methane emissions (primarily driven from livestock).
How is it calculated	As noted above, the ABA is currently working with members to develop financed emissions guidance for the agricultural sector, with the aim to finalise and publish in H1 2024. In the absence of widespread uptake of farm-level activity calculators, banks can estimate agricultural emissions based on either: • ***Production intensity***, which estimates emissions using on-farm production activity (eg. head of cattle), or • ***Economic intensity***, which estimates emissions using economic indicators such as revenue or loan amount. Irrespective of which method is adopted, a key challenge lies in the limitations of publicly available emissions factors. For example, the National Inventory Economic Sector results provide emissions for the Agricultural sector and is not broken down to key commodities (dairy, beef, cropping, etc). While the National Inventory data does provide Scope 1 emissions data broken down by key commodities, significant manual construction is required. This adds additional steps, and further requires combination with other data sources (such as the ABS) to derive an emissions metric by production or value.
Opportunities	Shorter-term: • Nationally provided emissions and emissions factors, both production and economic based, at the level of agricultural sub-sectors to allow for consistent calculation • Agreed methodology for calculating emissions from mixed-used agriculture. Longer-term: • In conjunction with key stakeholders in the agricultural sector, explore opportunities to move to farm-level calculators.

Area Two: Downscaled climate scenarios

Scenarios are narratives of possible future states, constructed using science-based data and possible policy settings. Climate scenarios typically look at two types of climate risk: transition risk and physical risk.[24]

As many of the climate scenarios currently in use are global, they need to be "downscaled" to be made more directly applicable to Australia. This requires using Australian-specific data to understand how they could translate into domestic physical and economic impacts such as changes to Australia's physical environment (including the frequency and intensity of natural perils), economic impacts such as interest rates, GDP and employment levels, how those impacts would evolve over the course of the scenario and the impacts on insurability and land-use planning.

APRA has highlighted opportunities for data uplift across both transition risk and physical risk:

> *…climate-related data quality and accessibility remain a challenge. From a transition risk perspective, inputs and estimates essential to modelling a transition to a lower emissions economy scenario remain a significant challenge. As for data relating to physical risk, business lending asset location and future climatic data modelling remains an area for improvement.*[25]

The industry also recognises that uplift in data, models and methods will be required. For example, the development of accepted damage functions[26] to apply towards the assessment of physical climate risk in lending portfolios. Other challenges to be overcome include insufficient data on emissions, limited reconstruction of historical data to inform future physical risk assessments, and lack of Australia-specific climate projections.

Opportunities for improvement		
Nationally consistent downscaled scenarios	Insurance coverage, including change over time	Planned mitigation and adaptation measures
Damage functions	Land use planning and zoning	

Area Three: Natural Perils

The ***Royal Commission into Natural Disaster Arrangements*** recognised the impact of climate change on the frequency and intensity of natural hazards.[27] This will be a key driver of risks across the economy. A harmonised national approach to collecting, disseminating, and regularly updating data on natural perils would allow stakeholders, including business and the Australian community, to have a consistent view of Australia's changing natural environment.

Beyond data on the natural perils themselves, a further additional input is Government policy and plans regarding mitigation, adaptation, resilience, and other related measures.

This could potentially be integrated with the coordinated national approach to mitigation and adaptation (and related measures) recommended by the Joint Select Committee Inquiry into the Cyclone Reinsurance Pool in March 2023, namely that the *"Australian Government facilitate a coordinated approach to land use planning, building codes, mitigation and disaster resilience that includes the National Emergency Management Agency and other levels of government."* (Recommendation 5)

[24] The ASRS Exposure Draft also applies to these two risk categories.
[25] APRA (Nov 2022) *Information Paper – Climate Vulnerability Assessment Results* (link) 9-10
[26] Climate damage functions are an approach to estimating economic damage resulting from climate change. They provide a less resource intensive method for calculating economic loss in scenario analysis. There are currently no agreed damage functions for the Australian context.
[27] Royal Commission into Natural Disaster Arrangements (October 2020) *Final Report* (link) 22

Opportunities for improvement		
Flood information	Coastal inundation and erosion	Tropical cyclone frequency
Bushfire information	Hail	Building characteristics

Role of Government in solving the problem

Below, we highlight three areas in particular that could be the focus of Government work. The ABA would be happy to work with Government in driving this strategy:

- ***Gap analysis.*** Our response to **Priority 7** has highlighted some of the key climate data sources and their limitations. An initial role for Government would be to coordinate a whole-of-economy gap analysis, aiming to identify existing climate data sources, and assess their adequacy to meet incoming regulatory requirements. Industry could work with Government to provide views, and the gap analysis could also consider the various climate-related initiatives underway at both the State and Commonwealth level.[28]

- ***Prioritisation.*** The above exercise will provide a view of data sources, potential opportunities for uplift and identification of areas of high impact and low resource cost (low-hanging fruit). Given the diversity of climate data sources across the economy, there may be a range of uplift opportunities – some data-producing organisations may drive uplift opportunities themselves, in other areas there may be opportunities for collaboration, and so on. Where there are clear gaps, and no obvious pathway to filling them, these could act as priority areas for joint Government and industry work.

- ***Ongoing Uplift.*** Uplift in climate data is likely to be an ongoing process. First, the regulatory and policy environment will continue to evolve, particularly as global methodologies develop and mature. Second, many areas will have both "low-hanging fruit" and longer-term opportunities. The Government may therefore wish to consider options for ongoing coordination. This could be through regular, standing forums that bring together a range of key data providers and users.

Priority 8: Ensuring fit for purpose regulatory frameworks

Do you agree that existing regulatory and governance frameworks and practices have adapted well to support better integration of sustainability-related issues in financial decision making? Are there barriers or challenges that require further consideration? This may include:

- **Corporate governance obligations, including directors' duties**
- **Prudential frameworks and oversight, including in relation to banks and insurers**
- **Regulation of the superannuation system and managed investment schemes**

What steps could the Government or regulators take to support effective investor stewardship?

We will consider and make more detailed comments on this policy priority should the Government proceed to formal consultation.

Our submissions to consultations on *Mandatory Climate-related Financial Disclosures* have highlighted that Australian laws are already stringent when compared to peer jurisdictions. Notably, Australia does not possess safe harbour defences for forward-looking statements – while both the UK and US apply some form of safe harbour.

[28] For example: the Hazards Insurance Partnership, National Climate Risk Assessment, the ongoing expansion of NatHERS, the development of sector transition pathways, modelling to support Australia's next round of nationally determined contributions and the insurance sector CVA.

As we have outlined in our previous answers, Government can best "support better integration of sustainability-related issues in financial decision-making" by working with industry on practical issues relating to existing or incoming regulatory requirements. Ongoing policy work, including the implementation of ISSB-aligned mandatory disclosures and the development of a sustainable finance taxonomy, will assist.

ASIC may wish to provide further guidance on how it will approach its regulatory responsibilities, including during the proposed regulator-only enforcement period for climate disclosures. This could include guidance on what would constitute a "reasonable basis" – taking into account current limitations of Australian climate data. Additionally, Regulators should take an "improvement" posture for early climate disclosures, while also recognising that enforcement will remain appropriate in clear examples of wrongdoing.

Further barriers and challenges have been discussed in **Priority 5**.

Australian Banking Association

Pillar 3: Australian Government leadership and engagement

Priority 9: Issuing Australian sovereign green bonds

What are the key expectations of the market around issuance of, and reporting against, sovereign green bonds? What lessons can be learned from comparable schemes in other jurisdictions?

What other measures can the Government take to support the continued development of green capital markets in Australia?

The ABA and its members will consider and make more detailed comments on this policy priority during formal consultations. At this time, we note that issuance of green sovereign bonds will largely set the expectations for bank and corporate green issuance. Sustainable capital markets are subject to risk given the lack of clear direction in eligible assets and the associated "green washing" risks. A clear framework will support the development of green capital markets in Australia.

The market expects sovereign green bond issuers to address climate actions holistically and is increasingly requiring additional data points beyond the assets financed through the bond. Alignment of Government policy to Paris Agreement objectives is key.

Allocation and impact reports are becoming the most important documents post issuance for investors. As market and sustainable finance principles change rapidly, a review and regular update of the green bond framework (and/or external reviews) would be positively received by investors. To support market integrity and reduce hurdles of issuance, the Monetary Authority of Singapore is offering a Sustainable Loan/Bond Grant Scheme to borrowers covering the cost of their external reviews (assurance or SPO) reducing the risk of greenwashing and cost to transact. All issuers of sustainable bonds in the Australian market are advised/already seek external reviews pre-issuance but agree this is not the case offshore. A grant scheme would help the market develop whilst ensuring integrity – reduce greenwashing perception.

Other expectations for the market may include:

- A sovereign green bond framework should be credible, reflect market best practice and endure through time.
- Articulating the rationale for the framework and how it integrates Australia's strategic sustainability priorities and climate change objectives. An emphasis on new and additional eligible expenditures, not those considered as BAU or funded through other hypothecated revenue sources.
- The framework should demonstrate alignment with the *Sustainable Finance Strategy* including frameworks for sustainability and climate reporting, while highlighting the desire to drive the development of Australian sustainable debt markets and attract additional investor capital.
- Collaboration with the RBA to understand how they will incorporate Green Bonds into their own mandates and otherwise support the Green Bond market.

Other areas for consideration in the development of a green bonds program could be:

- Whether the Australian Government plans to align to an existing framework (for example, the ICMA Green Bond Principles, the CBI standards, European Bond Standard etc.) or develop their own framework.
- Alignment between the framework and the Australian Sustainable Finance Taxonomy (noting that the framework and first issuance will likely be released ahead of the taxonomy).
- The need for a registration and/or supervisory framework for external reviewers of Australian green bonds.

- Bank balance sheets are important participants to the domestic capital markets, whilst operating under strict capital requirements rules. Any capital requirement incentive for asset owners to invest in green and sustainable products might provide an incentive to increase funds and portfolio supporting green issuance.

Priority 10: Catalysing sustainable finance flows and markets

What role can the CEFC play to support scaling up of sustainable investment in Australia, as part of a more comprehensive and ambitious sustainable finance agenda?

What are the key barriers and opportunities for the CEFC to support financing and market development in areas with significant climate co-benefits, including nature and biodiversity?

While Government funding in this area plays a critical role, it should not compete with business lending that can be done on commercial terms. In our response to the *Housing Legislative Package*, we stated:

> *Access to social and affordable housing is an intractable social challenge in Australia. Key to supporting a diverse and thriving community and economy is to unlock affordable housing options for low-income earners and frontline workers near their work.*
>
> *The Government is encouraged to carry out further consultation with industry stakeholders during the implementation of the legislation, once passed, to support the crowding in of financiers who currently operate in this market.*

Our submission to the *National Reconstruction Fund Corporation Bill 2022* provided more detail:

> *Government is encouraged to focus on infant, or prospective infant industries that may grow into strong contributors to the economy that may require up-front government support, rather than some of the identified priority areas that already benefit from traditional private sector investment.*
>
> *The ABA recommends it being a requirement of the investment mandate to consult with traditional private sector participants before making an investment by the Fund, such as via a panel of financiers. Government should assess the commerciality of each prospective investment and refer it to the private sector where it is sensible to do so from the perspective of return and/or risk appetite.*
>
> *This should be coupled with a requirement to 'hand over' funding of investments to traditional investors, such as banks, once the risk profile of the investments has been lowered to a range that can be managed by the private market. Such an approach would support the build out of new and domestic industries that attract a higher risk and possible return, leaving traditional investment to the private market to manage, while freeing up capital to re-invest in the next project.*

The CEFC's ability to specify criteria for green products has been helpful as a 'line in the sand' while a taxonomy has not existed. This may continue once the taxonomy is finalised.

The CEFC may wish to examine programs specifically targeted at low-income households. For example, loan loss guarantees for the Household Energy Upgrades Fund program. Following the completion of the ***Rewiring the Nation*** program, the Government may wish to explore potential roles for the CEFC in clarifying and facilitating best practice among hard-to-abate sectors (for example, agriculture).

Finally, there may be scope for consideration of whether the CEFC's remit could expand into areas of resilience and adaptation, noting the above caveats on its appropriate role.

Priority 11: Promoting international alignment

What are the key priorities for Australia when considering international alignment in sustainable finance?

The ABA supports the development of consistent global standards and interoperability between Australia and other jurisdictions that promote comparability and cross border investments. Alignment is critical for supporting capital flows, given the size of our market and our relatively high global integration. Australia is relatively advanced in the APAC sustainable finance market and it will be important to ensure frameworks don't create barriers to international businesses from less developed markets investing and raising finance in Australia. Broad applicability is also important to allow ease of lender engagement on widely syndicated, global transactions.

Several key priorities should be considered:

- Frameworks and standards that are specific to our economy and region, including the different levels of data availability available in different global jurisdictions.
- Support for practical application and balance between ambition, implementation and costs.
- Consideration of transition periods for sectors of varying maturity regarding sustainable finance, and foundational developments that will support advancement and scale of sustainable finance.

Priority 12: Positioning Australia as a global sustainability leader

What are other key near-term opportunities for Australia to position itself as a global leader in sustainable finance and global climate mitigation and adaptation?

The ABA and its members will consider and make more detailed comments on this policy priority during formal consultations. We are broadly supportive of the ambition to take an international leadership role, and we make the following comments for consideration:

- Australia will benefit from engagement in international sustainable finance frameworks by removing barriers to sustainable capital flows through ensuring the principle of inter-operability can be applied in real-world practice, building markets for green exports in key economies by promoting effective policy that accelerates demand, and enhancing Australia's reputation and influence through role modelling support for decarbonisation and just transition outcomes.
- The structural similarities between Australia's economy and many countries in Southeast Asia that arise from a strong mining industry and historical dependence on fossil fuels, means that our sustainable finance taxonomy will be highly relevant for many key partners. Our approach to defining "transition finance" will be critical in addressing barriers to finance and investment for transition activities, such as the extraction of transition metals and mining.

What are the key market, regulatory and institutional barriers to increasing private sector engagement in blended financing opportunities? How can these barriers be overcome?

The ABA and its members will consider and make more detailed comments on this policy priority during formal consultations. At this point, we make the following comments for consideration:

- **Project pipelines.** In some emerging markets, project preparation for large-scale projects can take 10-15 years, compared to 3-8 years in advanced economies. Preparation costs are also substantial, typically 2.5–5% of total investment. Australia's ability to support increased private sector engagement in blended finance will require dedicated development finance capability and resources. Opportunities for consideration include working early with investors on structuring the funding for projects, design of standardised financing solutions, working more closely with a wider range of partners and financing to offer assistance with project preparation and planning.

- **Procurement Rules.** While banks can advise governments on how to transform their national contribution plans into pipelines of transition projects, this would likely disqualify banks from participating in the financing of the projects themselves. Greater utilisation of Government's development finance capability would allow the greatest financing flexibility and ensure that innovation remains appropriately arm's length from the private sector entities that may later bid for the projects.

- **Research and Development Incentives.** If a bid team submits an innovative financing proposal, the vendor will tend to ask all bidders to implement that strategy at least cost, leaving no return to the R&D investment made by the innovator. This likely accounts for the limited observable R&D in blended finance structures to date. The Australian Government may wish to investigate updating procurement guidance to provide appropriate lanes or status to genuinely innovative bids that further the objective of blended finance innovation and scale.

- **De-risking Investments.** Many transition investments are long term and come with high risk, leading to very high-risk weights that consume large amounts of shareholder capital. These risk weights derive both from regulation and internal risk management. While several international stakeholders have explored the release of capital constraints through unconventional prudential regulation, it is more likely that finance ministries will be left to balance the necessary trade-offs. Blended finance can successfully de-risk projects and may prove a powerful tool since it enables banks to allocate more of their balance sheet to these investments. The use of guarantees – such as from sovereigns, philanthropy, insurers – are appealing to banks for several reasons. It is less clear how bank capital regulation can risk sensitively treat new innovations in risk transfers to ensure benefits are realised. It is important that the financial regulatory community, and those involved in efforts to scale blended finance, understand the capital treatment considerations.

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